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RESEARCH ARTICLE

RE-DEFINING NIGERIA'S TAX SYSTEM AMIDST DIGITALISATION OF THE BUSINESS ENVIRONMENT

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Abstract

Technology, internet and e-commerce have redefined business models and practices such that values are created in environments different from where profits are earned and taxes are subsequently paid. Such practices, which exacerbate base erosion and profit shifting, negatively affect the collectible tax revenues by governments in several jurisdictions including Nigeria, making it difficult for them to meet their social contract obligations to their citizens. Using an ex post facto research design and qualitative research methodology, this exploratory study assessed the capacity of the Nigerian government to address the challenges imposed on its tax system by the emerging digitalized economy. The study observed that the issue of taxation in digitalized economy has not received the desired legislative and governance priority attention largely because of the dearth of knowledge about its complexities as well as the undue dependence on revenue from crude oil. The study therefore recommends that the revenue authorities should set up a think tank comprising chartered accountants, tax practitioners, information technology experts, academics and regulators to develop a comprehensive framework to address the issue from a national perspective while the ECOWAS Commission should be prodded and supported by its member-states to take on the issue at the sub-regional level as OECD is currently doing for its member-states in Europe, USA, Japan and Canada.

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Introduction:-

The taxi cab business in Lagos, Nigeria has been revolutionized by the entry of Uber/Taxify into the commercial transport business in the country. Besides the convenience it brings to human movement, a potential user does not need to leave his home to search for cabs. All that is required is a smartphone with the downloadable applications and you are registered to enjoy the services with the option of paying with a debit card or cash. It is one secured means of transportation as the details of the driver and car are immediately transmitted and stored in the user's phone for reference after the trip. At the end of the trip, an invoice with all details of the trip are automatically generated and sent to the user's phone as his bank account is also charged. The driver receives instant consideration for the service rendered.

The Uber/Taxify example is just one of the many internet-based innovations in the Nigerian e-commerce business space employing many Nigerians and providing them with livelihoods. However, a proportion of their incomes goes

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to Uber/Taxify that cannot readily be determined and taxed by the Nigerian Tax Authorities as such taxable incomes are received abroad. It is instructive to note that Uber, with an asset base of about US\$31.76b as at December, 2019, was incorporated in 2009 in USA and does not own any taxi cab. With an initial public offering at US\$45 a share, Uber's valuation was put at US\$75.5b in 2019 (Reddy, 2019). It earns huge income from intangible asset of franchise or trade name which creates values in many jurisdictions across the globe. To share in this burgeoning revenue, Uber drivers in UK agitated for and were granted employee status, rather than just being drivers, with benefits including minimum wage in the face of economic challenges caused by COVID-19 pandemic (Punch, 2021). To benefit from the huge opportunities in this ride-hailing service market, the Lagos State Government in Nigeria, in conjunction with CIG Motors Company Limited, launched the Lagos Ride brand on March 4, 2021 in Lagos with one thousand (1,000) initial taxis (Pulse, 2021)

Like Uber/Taxify, there are also numerous multinational corporations (MNCs) doing online business across the globe without physical structures in many locations. For instance, there are multi-sided platforms and resellers like Amazon marketplace, Amazon e-commerce, UberEATS, eBay, Blablacars, JB.Com, Alibaba, Facebook, Google and Weibo. There are also pervasive payment portals to facilitate business transactions: VisaCard, Verve, MasterCard and PayPal. These are examples of payment instruments that do not have physical presence in jurisdictions where they create values and earn taxable income. In Nigeria, there are internet portals for online shopping: Konga.com, Jumia.com, OLX Nigeria and Cars45.com. These are byproducts of the advancement in technology and the wind of globalization blowing through the world of business and commerce. This is the era of digitalization and digital economy that is "characterized by an unparalleled reliance on intangibles, massive use of data (notably personal data) and the wild spread adoption of multi-sided business models (OECD, 2018, p. 2)".

Currently, with the rapid advancement in technology, e-commerce has become the vogue rather than exception. Products like Nigeria's Nollywood films, music, video games and e-books are increasingly becoming digital products traded across-borders without the payment of custom tariffs (Rukundo, 2020). To underscore the propensity of what to expect in terms of growth in e-commerce, Statista (2018) reported that in 2014, 2015, 2016 and 2017, the value of retail e-commerce worldwide amounted to US\$1,336b, US\$1,548b, US\$1.845b and US\$2.304b, respectively, representing a growth of 72.5% in 4 years. Yet, e-commerce is still evolving. Here lies the challenge.

While e-commerce innovations will significantly boost businesses and create jobs for young Nigerians, there is a challenge of determining the income earned by digital corporate entities in the process, for purposes of taxation. With digitalization of the economy, intangibles are mostly traded through virtual media which encourages profit shifting thereby making it difficult not only to determine and track taxable income but also, for the government to raise enough tax revenue. This is a critical challenge of a digital economy: its growth is not associated with increased tax revenues in environments where values are created. With digitalization, values are created in environments that are different from where profits are earned raising issues of business ethics, morality and proprietary rights of multinational corporations (MNCs) to draw resources from environments where they do not pay taxes (OECD, 2015). The exploitation of the gaps and mismatches between different countries' tax systems, which manifest as base erosion and profit shifting, is a global problem which only collective actions can address (OECD, 2015). To curb the estimated loss of US\$240b by countries to tax avoidance, over 90 countries have signed on the Multilateral Instrument on BEPS (OECD, 2019). For the tax authorities in Nigeria to be able to appropriately respond to the challenge, they need to understand how digitalization is changing the way the businesses operate and create value.

With its huge population of over 200m people and market, Nigeria is basically a consumer nation and net importer. Its share of world trade is 0.33% (Okonjo-Iweala, 2021). With this size of trade, the Nigerian government cannot significantly influence the direction of global trade, economic activities and the impact of e-commerce at the macro and international levels. Given this situation, how can it continue to earn enough tax revenues to drive its social welfare and economic development agenda? How ready is the nation to brace up to the challenge of digitalization of the economy on taxes? With value creation occurring in different dimensions of the digital economy, how can the government track these values that are precursor to taxable profits? Does the nation have the appropriate technical and legislative framework to track the processes of value creation for the purpose of taxation? The objective of this study therefore is to assess the readiness, in terms of technical and legislative capacity, of the Nigerian nation to address taxation challenges associated with a digitalized economy.

The remainder of this paper is segmented into seven sections. The second section contains the methodology while the third reviews the literature. The fourth section discusses the characteristics and challenges of a digitalized

economy while the fifth considers OECD's initiatives to address the tax challenges of digitalisation. The sixth presents the efforts by the Nigerian government to address the tax challenges of a digitalized economy while the last section contains the conclusions and recommendations.

Methodology:-

As an exploratory work, this study used an ex post facto research design and qualitative research methodology which involved the review of existing literature, secondary data from previous articles, publications and working papers issued by multilateral agencies and the International Chamber of Commerce. This approach was adopted because the framework and pillars of international taxation in a digitalized economy, designed to address the challenge of profit shifting, are still being finalized while many nations are yet to ratify the Multilateral Implementation Instrument to give effect to the BEPS framework. Agreements on the two pillars developed are expected to be reached by the OECD in mid-2021.

Literature Review:-

Conceptual Review

Globalisation

In the literature, there is no unanimity on the definition of globalization because of its diverse perspectives and what the concept entails (Held, McGrew, Goldblatt, Perraton, 1999; Robinson, 2007). In its simplest form, globalization is the process of corporations moving their investible funds, factories and products around the world to maximize the values of their firms. In other words, the concept of globalization refers to the phenomenon in which corporate entities operate in more than one jurisdiction, where there exists organisations with multiple nationalities, where trade is conducted without regards to borders, mobility of people in search of greener pasture is unfettered and people have unlimited access to goods and services which they cannot produce, subject only to their purchasing power limitation (Held, *et al.*, 1999). Driven by information technology, globalisation has altered the nature of business and traditional definition of markets with players now operating in virtual space across jurisdictions without regards to territorial regulations, taxation and local peculiarities. Globally, values are now created more with intangible, than tangible, assets (Bhasin, 2017; Rukundo, 2020). Propelled by technology and modern communication, the myth of international trade between countries with all its uncertainties have now been reduced or eliminated.

Multinational Corporation (MNCs)

Multinational corporations (MNCs) are entities which have subsidiaries in two or more countries that are managed by holding companies located in another country. In addition to their home countries, MNCs operate in different markets and sometimes produce different products for several markets. It is a byproduct of globalization which involves the emergence of a borderless economy driven by MNCs with new systems of production, finance, consumption and worldwide economic integration. It involves the emergence of global cultural patterns, practices and flows as well as the growth of transnational institutions with global governance and authority structures (Eluka, Ndubuisi-Okolo, & Anekwe, 2016; Held, *et al.*, 1999). With these factors have come the issues of transnational migration, identities, communities and increased economic and social inequalities. In the globalized virtual world, MNCs drive transactions in a borderless market.

Taxation

All governments, the world over, depend on taxes to survive and fund their various economic developmental projects. In Public Finance, taxes are the involuntary contributions that citizens are required to make for the running of the government (Musgrave & Musgrave, 1989; Smith, 1776). It is their contributions to support good governance and quality service delivery. Both legal and natural persons are respectively required to pay taxes on their profits and incomes. While it is fairly easy to tax the incomes of persons under the pay-as-you-earn (PAYE) system, most corporate entities often embark on aggressive tax planning to avoid paying taxes. Unlike tax evasion that is illegal, tax avoidance is perfectly legal. However, aggressive tax avoidance practices are beginning to be economically injurious to many nations as they diminish the capacity of affected countries to raise tax revenues.

Base erosion and profit shifting (BEPS)

Profit shifting is one of the corporate tax planning strategies used by MNCs to shift their taxable profits from high-tax jurisdictions to low-tax jurisdictions (Devereux & Vella, 2018; Dharmapala, 2014). The implication of this strategy is that the tax base of the high-tax jurisdiction is reduced making it difficult for it to raise enough taxes to

finance its expenditure. With digitization and the absence of universally accepted framework, this profit shifting practice, which is perfectly legal, is now tending towards tax evasion. As transaction are increasingly done electronically, it has become easier for MNCs to hide their profits and shirk tax payment in environments where taxable income is generated. The implication is that MNCs utilize resources of a given environment to generate profits but they pay taxes in other jurisdictions. In other words, with base erosion and profit shifting (BEPS) practices in international trade, taxes are not paid where values are created (PwC, 2020). Over US\$240billion lost by nations annually to BEPS (OECD, 2015). If unchecked, governments' capacity to provide for the welfare and security of lives and property of their citizens will be vitiated.

Value Creation

Value is created when the usefulness of an asset, whether tangible or intangible, is enhanced. It is about the utility of a product or service to the user or consumer. When the benefits from the use of resources are higher than their acquisition costs, the proprietary interests of shareholders in the business are enhanced through greater profit margins, higher dividend pay-out ratios and appreciation in the value of shares (Asein, 2000). In the context of a digitalized economy, values are created through networks with direct effect, indirect effect, economies of scale and switching costs. With direct network effects, users depend on other end users to benefit whereas, with indirect network effect, it is a product of social interactions between people in the platform. With direct network effect, the larger the number of end users, the higher is the end-user utility. The larger the number of followers of an entity or person, for example on Facebook and Instagram, the wider the reach and possible effects. The cost of fixed assets for digital infrastructure do not vary and so, with increased output, the unit costs will decline thereby creating more value to end users. It is in this sense that it can be said that value may be created through the manufacturing and/or distribution processes.

Theoretical Review

There are several theories in the science of taxation which explain the *raison d'être* for MNCs to pay taxes. These include the benefits theory, equity theory, profit shifting theory, cost of service theory and legitimacy theory. The thrust of these theories is the need for legal and natural persons to pay fair taxes not only to support the government's various developmental initiatives but also, as a civic responsibility. Additionally for an MNC, this is to enhance its legitimacy. This study is predicated two theories: profit shifting and benefits theories.

Profit Shifting theory

Profit shifting is one of the corporate tax planning strategies used by MNCs to shift their taxable profits from high-tax jurisdictions to low-tax jurisdictions (Devereux & Vella, 2018; Dharmapala, 2014). The theory holds that taxes are paid outside the environments where values are created due to tax planning strategies. The implication of this strategy is that the tax base of the high-tax jurisdiction is reduced making it difficult for it to raise enough taxes to finance its expenditure. Although the practice of shifting profits from high-tax to low-tax jurisdiction, is perfectly legal, it is now tending towards tax evasion because, with digitization, transaction are done electronically making it easy for MNCs to shirk tax payment in environments where taxable income is generated. The implication is that MNCs utilize resources of a given environment to generate profits but they pay taxes in other jurisdictions which do not bear any burden. This practice is both inequitable and unfair as it makes entities to prosper at the expense of society. Essence, digitisation is not just about high tax and low tax environment. It is a moral burden which provokes legitimacy challenge to affected MNCs. It is instructive to note that Uber generates revenue from several countries but pays taxes in USA where it is resident even when the tax rates in USA are not lower. This is tax nationalism which less developed countries must take a cue from.

Benefits theory

This theory is based on the benefit principle which has its foundation in the Equity and Fairness Canons of Taxation espoused by Smith (1776). Multinational corporations leverage the resources of their host environments to create value. These resources include infrastructural facilities of roads, rails, telecommunication, electricity and security architecture. The provisions of these public goods are costly and capital-intensive. Based on residence rule, local corporate entities are readily accessible to company income tax which they mandatorily pay to support the provision and maintenance of these facilities. Citizens also pay personal income taxes as part of their civic responsibilities. However, digital MNCs do not have significant presence in their host environments where they create value. In their operations, they adopt the advertising, merchant or the brokerage models. In each of these cases, they do not need to have physical presence to create value. They deploy technology to do so with ease. As a result of this and the complexities associated with their activities and business models, they cannot be easily charged. Yet the benefit

principle holds that, “the taxes which an agent pays should reflect the benefit that he receives from the mix of goods and services supplied by the state (Neil, 1999, p.118).” These BEPS practices belie the thrust of this theory.

Digital MNCs do not pay taxes in environments where they earn their profits. Although taxes are paid without *quid pro quo*, fairness demands that entities and citizens should pay taxes where they generate the taxable income. It is inequitable for an entity to utilize the resources of a given environment to create value and earn profit but pay taxes in another environment. The benefit theory in taxation which opines that profits should be taxed where values are created, aligns with best practices and promotes fairness and inclusiveness. In other words, it would be unfair and inequitable for any corporate citizen not to pay taxes or pay taxes to authorities other than where it generates taxable income. Since MNCs draw their resources including profits from a given jurisdiction, it is only fair that they pay taxes in that jurisdiction as responsible corporate citizens. Where they deliberately deny the environment, in which they create value and make profit, of taxes, through aggressive tax planning and tax avoidance techniques, their legitimacy will be threatened.

In the Nigerian environment, as in other jurisdictions impacted by digitilisation of the economy, profit shifting practices deny the people the right to enjoy the benefit from taxes that would have been collected from them by the government. The current practice of base erosion and profit shifting (BEPS) aided by digitalization is devoid of equity and fairness. It negates the equal sacrifice principle and diminishes certainty as a canon of taxation (Ok, 1995). Governments which enacted tax laws did not provide that entities will make profit in one jurisdiction and pay in others. What they are prepared for is a situation which precludes double taxation as reflected in various treaties between nations.

In this study, this equity concept is extended to the activities of MNCs. If they earn revenue from an environment, it is fair that they pay equitable taxes in that environment like other corporate entities that operate solely/locally in the same environment. They enjoy the benefits provided by the government in terms of enabling business environment, security of lives and property. It is legitimate for the government to expect “payment” for those social services in the form of tax. To shift their profits to another jurisdiction amounts to inequity in taxation and unfairness to the environment from where they generated the profits. Such practices will actually make an MNC to lose its legitimacy as a corporate citizen that can draw resources from the environment (Orshi, Dandago & Isa, 2019).

The point must be made that, to properly tax an MNC, the tax authorities must take into consideration non-double tax treaty with the entity’s country of origin or residence and other best practices in international taxations in order to prevent retaliatory tax measures against its own companies (PwC, 2020). Here lies the challenge with the current interim measures being adopted by many nations to raise immediate tax revenues in the interim rather than wait for a global solution to the issue of taxation in a digitalized economy. The international community must expeditiously come up with acceptable tax allocation formula to address the issue of base erosion and profit shifting which have been compounded by the emergence of a digitalized economy. However, while BEPS may be viewed as aggressive tax planning measures, some studies (for example, Devereux & Vella, 2018; Endres & Spindel, 2015) have attributed this practice to corporate strategy designed to maximize firm value arising from international tax competition. Thus, the debate on the need for a new international tax order based on anti-BEPS is not conclusive.

Characteristics and Challenges of a Digital Economy

A digitalised economy is basically an economy in which business and commercial activities are largely driven by technology and carried on in a borderless virtual market in which most of the stock in trade are intangible assets. According to UNCTAD (2017, p.157), it is “the application of internet-based technologies to the production and trade of goods and services”. Thus, a digitalized economy is an economy in which business activities results in billions of financial transactions everyday, connections among people, business entities, electronic devices, data exchanges and new business models. The major characteristics of the digital economy include globalization, digital system, information dissemination speed, information overload and intelligent search engines, virtual markets, new business models and processes, innovation, obsolescence, opportunities, fraud, wars, internet of things and virtual organisations. It is the complexity of the digitalized economy that creates problems for the tax revenue authorities. This is made worse by the technical inability of tax authorities in less developed countries like Nigeria to track these complex virtual transactions for purposes of taxation.

According to the OECD (2015), there are three factors that are common to highly digitalized business models and economies. These are cross-jurisdictional scale without mass; reliance on intangible assets; and data, user participation and network effects.

Cross-jurisdictional scale without mass

Many multinational corporations have different aspects of their businesses located in diverse countries to enjoy certain benefits that may be associated with taxes, cost reductions or access to markets. Their production units or processes are spread across different countries and across customers around the globe. In other words, a product is not completely produced from one plant in a country. Its various production stages are located in different countries to gain some economic advantages associated with large scale at that level. Although there is no mass production involved, some economies are enjoyed at that level. With digitalization, these corporations are able to play significant economic roles in a country where they have limited or no physical presence at all. It is instructive to note that digitalization also has a lot of prospects for the small businesses. “As growing numbers of firms invest in digitalisation, e.g., by moving to cloud-based operations, it will become increasingly easy for formerly purely domestic firms to interact digitally with their customers. As a result and as the opportunities of digitalisation are not restricted to large multinationals, small firms are also more capable of reaching a global customer base (OECD, 2018, p.51-52)”.

Reliance on intangible assets

Multinational corporations, by definition, operate in the global market and so they invest largely in and thrive on intangible assets like intellectual property, brand names, patented inventions, franchise and algorithms. As a result, they can do business in environments where they have no physical presence, create value, earn profits but pay minimum taxes in other jurisdictions without infringing on any laws. For instance, in 2015, Facebook opened its first and only office in Africa in Johannesburg, South Africa notwithstanding the fact that it had over 200 million users in the continent (Rukundo, 2020)

Data, user participation and network effects

The internet and all its associated social media channels work with data of users. Business transactions done through the internet involve the creation of transaction data on customers that can be analysed and used for marketing and other purposes, subject to privacy laws in the applicable jurisdiction. Thus, in digitalized economy, there are users who are willing to use the various channels. By so doing, contents are developed and shared through networks. “Search engines and social media businesses rely heavily on gathering data about users’ preferences in order to sell highly targeted advertising services to businesses. Network effects occur when the usefulness of a service grows exponentially with the number of users (OECD, 2015)”.

Effectively, data is now the most critical resource of organisations (The Economist, 2017). There is no doubt that the digital economy is revolutionizing business practices and creating new opportunities for growth and worldwide prosperity. Indeed, if properly nurtured, technological advances and digital connectivity can spur innovation in business models, business networking and knowledge transfer while also facilitating access to international markets for businesses, large and small, old and new (International Chamber of Commerce, 2018).

OECD’s Initiatives to Address the Tax Challenge of Digitalisation

The OECD is providing leadership in this direction through its ongoing research work on the taxation in a digitalized economy. In 2016, it established the OECD/G20 Inclusive Framework on BEPS (Inclusive Framework), which brought “together all interested and committed countries and jurisdictions on an equal footing in the Committee on Fiscal Affairs and all its subsidiary bodies. The Inclusive Framework, which already has more than 135 members, is monitoring and peer reviewing the implementation of the BEPS minimum standards as well as completing the work on standard setting to address BEPS issues (OECD, 2020)”. It has produced an interim report and set year 2020 as date for final report. A total of 110 countries have resolved to adopt a consensus based on long term solution (OECD, 2018). Sadly that target was not achieved.

Of great interest are two critical issues: the existing rules that guide the right to tax the income of MNCs among jurisdictions and second, how to resolve the remaining BEPS issues and explore two sets of interlocking rules designed to give jurisdictions a remedy in cases where income is subject to no tax or only very low taxation (OECD, 2019). The former which includes the traditional transfer-pricing rules and arm’s length principle, could be modified in the light of the challenges of digitalization (OECD, 2019). According to the OECD release, the nexus

rules will also be re-examined to determine the connection a business has with a given jurisdiction and the rules that govern how much profit should be allocated to the business conducted there. It was in an effort to address these complex issues that the OECD developed two pillars which would be agreed upon by its members and non-members by mid-2021.

In the view of OECD (2020, p.11), Pillar One and Pillar Two would lead not only to “a relatively small increase in the average (post-tax) investment costs of MNCs” but also, “support global investment and growth through less quantifiable but nonetheless significant channels, which may partly or even fully offset this small negative effect”. Ultimately, the proposals are expected to “increase tax certainty and enhance the efficiency of global capital allocation by increasing the importance of non-tax factors (e.g. infrastructure, education levels or labour costs) in investment decisions”. The propriety of this consensus-based solution should be clear. In their absence, a proliferation of uncoordinated and unilateral tax measures (e.g. digital services taxes) may ensue and this may lead to “an increase in damaging tax and trade disputes. This would undermine tax certainty and investment and also result in additional compliance and administration costs, p.11”. To ensure a broad-based consensus is reached, OECD is also reaching out to business entities, other international organisations, regional tax bodies and members of civil society groups (OECD, 2020).

Given the sizes and peculiarities of the economies of African countries, especially the rudimentary nature of their information technology infrastructure, the African Tax Administration Forum (ATAF) has been making a case for new nexus rules, new profit allocation rules and new anti-global base erosion rules. In the view of ATAF, the new nexus rules should be country-specific while the new profit rule should provide for a fixed minimum return in the jurisdictions of source and residence to guarantee a degree of certainty as a canon of taxation.

Efforts by Nigerian Government to address the Tax Challenges of a Digitalized Economy

To promote the development of information technology in the country as well as enhance its tax revenue from the sector, Nigeria promulgated the National Information Technology Development Levy (NITDL) Act no. 28 of 2007 which requires all GSM Service Providers and all Telecommunications Companies, Cyber Companies and Internet Providers, Pensions Managers and Pension-related Companies; Banks and other financial institutions and insurance companies to pay 1% of their profit before tax. Entities affected must have a minimum of N100m turnover.

In 2017, the Nigerian Communication Commission reported that over 90 million Nigerians had access to the internet implying that many of them had the opportunity to engage in online business through the worldwide web. However, the growth in use of technology, especially by MNCs, started to impair government revenue from taxes as businesses engaged in base erosion and profit shifting activities through aggressive tax planning. It became expedient for the government to beam searchlight on BEPS with a view to addressing its negative effects. Thus, beyond taxing the turnover of telecommunications and related companies, there are more fundamental issues of taxation in virtual transactions. Given the level of technological development of the country, the tax authority and the various regulatory agencies do not have the technical capacity to monitor these virtual transactions and internet users. With the recently resolved case between MTN and the CBN on the alleged illegal repatriation of funds from the economy which was discovered years after, it became clear that there is no framework to track e-commerce and e-business activities in the country. These are issues that should rightly engage the regulators and practitioners.

At the beginning of year 2019, the Federal Inland Revenue Service (FIRS) had a retreat with its major stakeholders with the theme, “Parliamentary Support for Effective Taxation of the digital economy”. The Retreat signaled the creation of awareness about the phenomenon of taxation challenges in digitalized economy. From the presentations, discussions and final communique of the retreat, the dearth of information about value creation in a digitalised economy and how taxes are to be levied were demonstrated. The Service admitted through the address of its Chairman at the Retreat, that huge VAT revenues were lost through virtual transactions as they could not be effectively tracked. Given the intricacies of the issues involved, it is expedient for the FIRS to set up a special task force to develop a framework that will provide guidance on how to address the issues without breaching its double tax treaties with other nations.

As part of these measures, the FIRS is pressing forward with the implementation of the Common Reporting Standard (CRS) which is a fallout of the Yaounde Declaration signed by Nigeria and many countries in August, 2018. The Declaration includes a commitment to implement exchange of information tools which Nigeria was required to state by September 1, 2019. The CRS legislation will allow FIRS to obtain information such as bank

balances that Nigerian tax residents including companies and individuals have in offshore banks. These CRS Regulations were published with effective date of July 1, 2019 and they allow Nigeria access to information from 105 countries. FIRS must also reciprocate by providing these countries with the required information from qualifying financial institutions.

In contrast to the focus of CRS Regulations, OECD (2018) noted that the challenge of digitalization is clearly that of base erosion and profit sharing. In its 2018 Interim report, OECD considered the “nexus” and “profit allocation” rules as they relate to digitalization. According to the Report, these are fundamental concepts which determine “the allocation of taxing rights between jurisdictions and the determination of the relevant share of the multinational enterprise’s profits that will be subject to taxation in a given jurisdiction (OECD, 2018, p.1)”. In essence, it shows how profits are to be allocated amongst jurisdictions and the proportion of profits of multinational corporations to be taxed in a given jurisdiction. Understanding how digitalization is changing the way the businesses operate and how they create value is fundamental to ensuring that the tax system responds to these challenges.

In an attempt to address this challenge in Nigeria, the Parliament enacted the Finance Act 2020 which sought to introduce the concept of digital “permanent establishment (PE)”. The thrust of this concept, which is an amendment of Section 13(2) of Companies Income Tax Act, 2019 by the Finance Act, is that a foreign company which, “transmits, emits or receives signals, sounds, messages, images or data of any kind by cable, radio, electromagnetic systems or any other electronic or wireless apparatus to Nigeria in respect of any activity, including electronic commerce, application store, high frequency trading, electronic data storage, online adverts, participative network platform, online payments”, and has a “significant economic presence” in Nigeria with activities to which profit can be attributable, would be subject to companies income tax (CIT). According to the Finance Act, what constitutes significant economic presence is to be determined by the order of the Minister of Finance. Pursuant to this power, the Minister of Finance issued the CIT (Significant Economic Presence) Order which became effective from February 3, 2020. On what constitutes significant economic presence (SEP) and the threshold that nations should set, OECD recommends three parameters: the amount of revenue generated within a given time frame, say, a year; the quantum of use of digital factors (e.g., use of local domain name, creation of digital platform and payment options); and number of users and data collected in a given time frame (Rukundo, 2020).

In order to further clarify the provisions of the CIT Order, the FIRS recently issued guidelines which provide that the tax liabilities of SEP companies is dependent on a minimum derived turnover of 25 million Naira (64,320 USD). These SEP companies are required not only to annually file tax returns with the FIRS indicating the income derived from Nigeria in their financial statements but also, pay tax on revenues in excess of the threshold of 25m in line with existing CIT tax rates (as amended by the Finance Act): 20% of income derived where taxable income is between ₦25,000,000 and ₦100,000,000, and 30% tax rate where above ₦100,000,000.

The Nigerian business environment is not as sophisticated as its peers in Europe and Asia notwithstanding the size of its GDP and population. Although, the growth of e-commerce in Nigeria is commendable, ability to monitor the volume and value of online trade as well as where values are created for purposes of taxation in Nigeria, remain an uphill task. Given the global pervasiveness of digitalization which facilitates profit shifting by MNCs to other jurisdictions through some tax planning practices, it is fair to state that Nigeria should be ready to leverage the windows of ATAF and OECD to enhance its tax revenues.

Conclusion and Recommendations:-

With technology-driven globalization, business models are changing with values being created in virtual space. The borderless nature and complexities of these value creating opportunities have increased the challenges faced by tax authorities to raise taxes in various jurisdictions. Characterized by trade in intangibles, building of huge customer data base, the creation of values and earning of profits in environments different from where taxes are paid, digitalized economy has become a challenge to government’s ability to raise tax revenues to meet developmental needs. It has also raised the issue of equity in international taxation as it promotes base erosion and profit shifting which benefit MNCs at the expense of jurisdictions where resources are sourced, used to create values and earn profits. In many jurisdictions, interim measures are being taken to impose and raise taxes immediately until an acceptable international framework being championed by OECD comes to fruition in 2021.

Although the tax authorities in Nigeria are aware of the emerging digitalized economy and challenges it poses to revenue generation, they are hampered by dearth of technical knowledge and absence of adequate legislative

framework. Instead of the Parliament issuing a holistic legislation, FIRS is required to be issuing guidelines, which in certain cases are devoid of clarity. In a sense, they are not prepared or ready for the complex challenges of taxation in a digitalized economy.

It was to prepare the Parliament for the need to amend the subsisting tax laws to capture emerging technology-driven issues, that FIRS organized a stakeholders' retreat at the beginning of the year 2019. As commendable as this measure is, it is not sufficient. There is need to set up a think tank made up of regulators, chartered accountants, tax practitioners, information technology experts, members of the academia and organized private sector to develop a comprehensive framework for addressing the problem as OECD is currently doing for the European Union and G20 countries. As it pursues its integration agenda, the proposed OECD model could be the basis for ECOWAS to engage the world on taxation of digitalized economy. Except urgent measures are taken, the Nigerian nation will continue to lose huge tax revenues while MNCs will continue to prosper at the expense of jurisdictions where they earn profits which are different from where taxes are paid. Furthermore, multi-regulatory and inter-ministerial approach should be adopted so that all facets of government are on the same page on the issue of taxation in a digitalized economy. Lastly, the point must be made that digitalisation is not all negatives. It also has its positives. Therefore operators must leverage its benefits and opportunities to overcome its challenges. Here lies the need for human capacity building. The FIRS must invest in human capacity building to prepare its staff to overcome the emerging challenges that lie ahead.

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