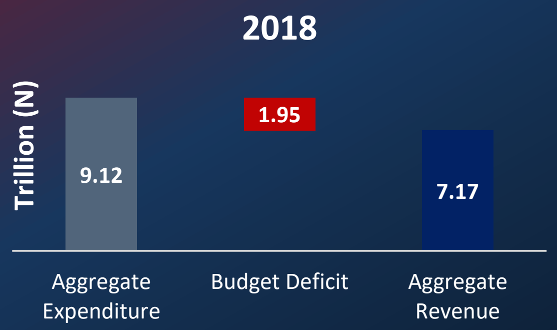
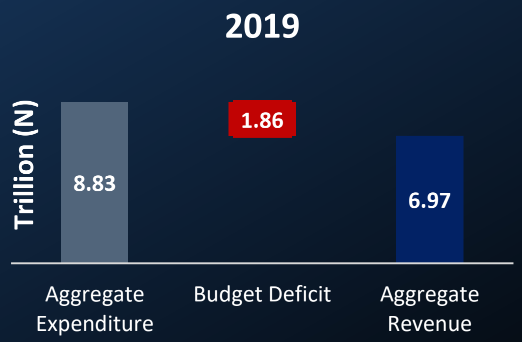
FINANCE BILL AND BUDGET 2020 ANALYSIS

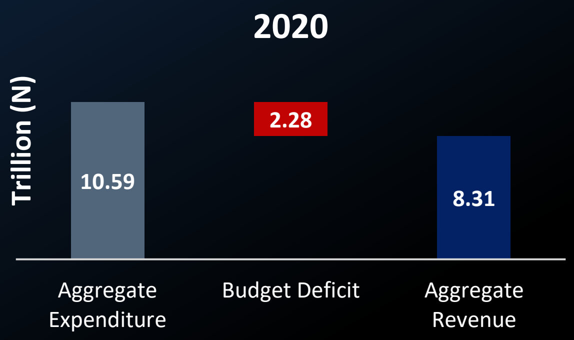
2020
Budget Proposal

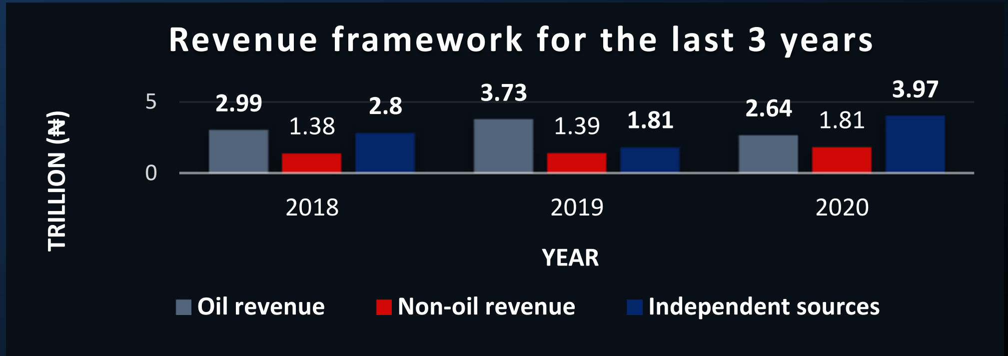
The 2020 Appropriation Bill tagged "budget of sustainable growth and job creation", was presented to the National Assembly by Mr. President alongside the Finance Bill. The two documents have since been signed into law. The Finance Act is intended to effect crucial changes to the existing fiscal laws that will enable the Federal Government increases its revenue generation capacity among other objectives.

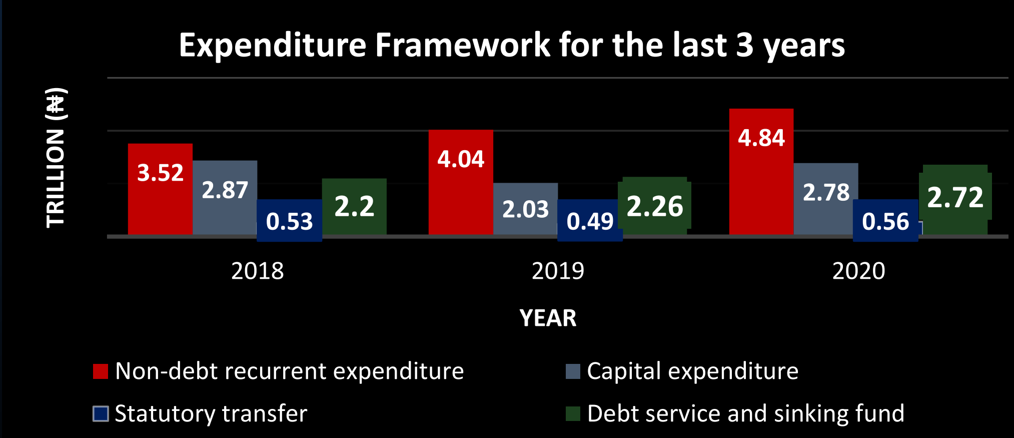
The budget has an aggregate expenditure of N10.59 trillion shared primarily into debt servicing, recurrent expenditure, capital expenditure and statutory transfers and an aggregate revenue of N8.31 trillion giving a deficit of N2.28 trillion. The deficit is expected to be funded with domestic and foreign debts. The comparison of the Nigerian budget for the past three years has been hinged on growth.











The budgets for the three years were based on the following key assumptions:

	2018	2019	2020
Oil price	$51/pb	$60/pb	$57/pb
Oil production	2.3mbpd	2.3mbpd	2.18mbpd
Exchange rate	$1/305	$1/305	$1/305
GDP growth rate	3.5%	3.01%	2.93%
Inflation rate	12.4%	9.98%	10.8%

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Tax impact on the Budget 2020

The main revenue streams elucidated in the budget include Oil revenue which is to generate N2.64 trillion, Non-Oil tax revenue which is estimated at N1.8 trillion and other revenue estimated at N3.6 trillion. Over the years, there has been an inconsistent movement in the expected revenue percentage from the various streams of revenue as depicted below:

	2018	2019	2020
Oil Revenue	41.7%	53.5% (25% increase)	31.4% (29% decrease)
Non-oil tax revenue	19%	20% (7.3% increase)	21.5% (30% increase)
Independent sources	39.1%	26.5% (34% decrease)	47% (115% increase)

The increase in the non-oil tax revenue will bring about an aggressive approach to tax collection by the federal government as this will have a significant effect on the overall actual budget for the year. We have highlighted below, the different taxes and its effect on the budget:

	2018	2019	2020
	N trillion	N trillion	N trillion
Share of tax revenue in the budget (percentage)	1.38 (19%)	1.39 (20%)	1.81 (21.5%)
Share of CIT in the budget (percentage)	0.794 (57.5%)	0.813 (58.5%)	0.839 (46.4%)
Share of VAT in the budget (percentage)	0.208 (15.1%)	0.229 (16.5%)	0.292 (16.2%)
Share of Custom Duties in the budget (percentage)	0.325 (23.6%)	0.310 (22.3%)	0.619 (34.2%)
Share of Federation Levies in the budget (percentage)	0.057 (4.1%)	0.055 (4.0%)	0.055 (3.2%)

The Finance Act

Following the signing of the Finance Act, we have summarized below some of the changes in the Finance Act that are expected to enhance revenue collections.

CITA- Non- Resident with "significant economic presence" (SEP) in Nigeria; and profit can be attributable to such activity are taxable

Increase in monetary penalty for late filing of tax returns (N50,000 in the first month and N25,000 for each subsequent month)
Removal of minimum tax exemption for companies with imported equity

PPTA- The Act repealed the provision of PPTA that exempts dividends paid out of profits derived from petroleum operations from withholding tax. Taxpayers in this space would now be saddled with the responsibility of withholding tax when paying dividends.

Increase of value added tax (VAT) rate from 5% to 7.5%

The additional revenue generated from VAT would be used to fund healthcare, education and infrastructure.

Introduction of a requirement for banks to obtain Tax Identification Number (TIN) from customers before opening bank account.

Vatable goods and services have been expanded to cover intangible items other than land.

Increase in penalty for failure to register and file VAT returns to N50,000 in the first month and N25,000 for each subsequent month in which the failure continues)

STAMP DUTY ACT- Increase of the stamp duty on receipts to ₦50 on every transaction from ₦10,000 and above; and, expansion of the definition of receipt to cover electronic transactions.

Analysis of the new VAT regime

The Finance Act contains several long-awaited changes to the tax framework which seek to address issues of low tax revenue growth, such as an increase in the VAT rate to 7.5% and the introduction of tighter deductibility rules.

The 2020 budget is anchored on the policy framework of the Finance Act, that intends to amend the existing VAT regimes and subsequently generate substantial revenue stream from tax and crude oil. Furthermore, Nigeria's tax to GDP ratio at 6% is very low when compared to other African companies, as its broader tax to GDP ratio, which is a major priority for the government.

Some of the factors highlighted as contributing to the poor tax to GDP ratio are a sub-optimal VAT system (which deviates from modern consumption tax designs), comprising a low standard VAT rate of 5% and restricted recoverability of input VAT. A weak tax administration system coupled with high cost of taxpayer compliance has also resulted in a systemic non-compliance and a lack of faith in the tax system.

The new VAT regime' main objective is to free Micro, Small and Medium Enterprises (MSMEs) from the administrative burden of VAT compliance. The regime Introduces a ₦25million revenue threshold for taxable persons required to register for VAT and file returns. Anyone who does not fall within the threshold above would be exempted from registering, issuing tax invoice, collecting, remitting and filing of VAT returns. The threshold of ₦25million within the calendar year will reduce the tax compliance burden for small companies.

Analysis of the new VAT regime (Cont'd)

The exempted companies are not required to charge VAT on their sales but are not exempted from incurring VAT on their own purchases from companies with turnover above N25million. Thus, implying that MSME's will have to absorb the input VAT on purchase of stock-in, trade or raw materials, machinery and other items of capital expenditure which will subsequently increase their cost of production. For manufacturing companies, the issue becomes worse off as they are currently unable to recover the VAT input on certain items of expenditure.

The big question here will be "what becomes the fate of the struggling MSMEs?". According to the Ministry of Industry, Trade and Investment, Nigeria has over 37.07 million MSMEs, and they account for more than 84 percent of total jobs in the country. The ministry also claimed that the MSMEs in Nigeria also account for about 48.5 percent of the gross domestic product, GDP, as well as about 7.27 percent of goods and services exported out of the country. Where their cost of production is increased, there might be a reduction in business profit which might eventually affect the sustainability of the companies. Also, the effect of this will be that companies in this category may decide to hike prices of their products to mitigate the effect of the VAT increase on their businesses.

Implications of the increased VAT rate

During the compilation of the Finance Act, the following was not considered:

1. VAT Recovery: MSMEs are required to pay input VAT on their purchases but the Act has no mechanism in place on its recovery as they are not allowed to charge the corresponding output VAT due. Thus, making the MSME incur additional cost on VAT which it cannot claim or utilize. The government is thereby enjoined to provide clarification on the following:

   i. If there is a restriction as to how long the MSMEs will carry the irrecoverable input VAT in its books.

   ii. If the MSMEs will be able to claim VAT refund and the process involve in claiming it.

   iii. If the MSMEs can utilize the irrecoverable VAT input against its future CIT liability when it becomes a large company.

2. Proof of company size: What mechanism will be put in place to determine or proof that a company is below the threshold of N25Million

Accounting Implication

Based on the interpretation of the Finance Act, MSMEs are not required to charge VAT on their invoices when they transact with companies that fall above the threshold. However, the large companies are required to self-account for the VAT due on such transaction and remit such to the government. Thus, supposed large companies are expected to create a separate VAT payable ledger to account for such transactions and either remit the amount at the due date to the government or net it off against corresponding VAT output.

Conclusion

An increase in the VAT rate has the potential to increase government revenue and further enhance the development of the tiers of government based on the sharing formula of the VAT proceeds. However, where the implementation is not adequately monitored, it might become a burden to the economy.