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Finance Act 2020: Impact on Individual Taxpayers

January 2021

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Background

President Muhammadu Buhari, on 31 December 2020, signed into law, the 2021 Appropriation Bill and the 2020 Finance Bill.

The Finance Act, 2020 (the Act) amends portions of various extant tax provisions, including that of the Personal Income Tax Act (PITA), Cap P8, LFN, 2007 (as amended by the Personal Income Tax (Amendment) Act, 2011). In this article, we have highlighted some of the major changes to PITA and how these impact payroll taxes with effect from 1 January 2021.

Amendment to section 33 of PITA

There are two major amendments to this section:

1 Redefining gross income for PAYE tax purposes

The entire wording of subsection 2 of section 33 of PITA was substituted with the following:

> **"For the purposes of this Section, "gross income" means income from all sources less all non-taxable income, income on which no further tax is payable, tax-exempt items listed in paragraph (2) of the Sixth Schedule and all allowable business expenses and capital allowances"**

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The intent is to prevent a situation where non-taxable income (such as reimbursable, employer's contribution to pension), franked investment income (such as dividend) and tax-exempt items are considered in the computation of Consolidated Relief Allowance (CRA). Not excluding such income will lead to an unintended effect of additional 20% relief over and above the initial 100% relief granted.

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The amendment will, however, have a far reaching impact on payroll if the tax-exempt deductions listed under paragraph 2 of the Sixth Schedule to PITA - including contribution by employee to the National Housing Fund Scheme, National Health Insurance Scheme, Life Assurance Premium and National Pension Scheme - were to be deducted from total income (from all sources), in arriving at the gross income on which CRA is computed. The impact will be an increased tax as a result of the increase in chargeable income.

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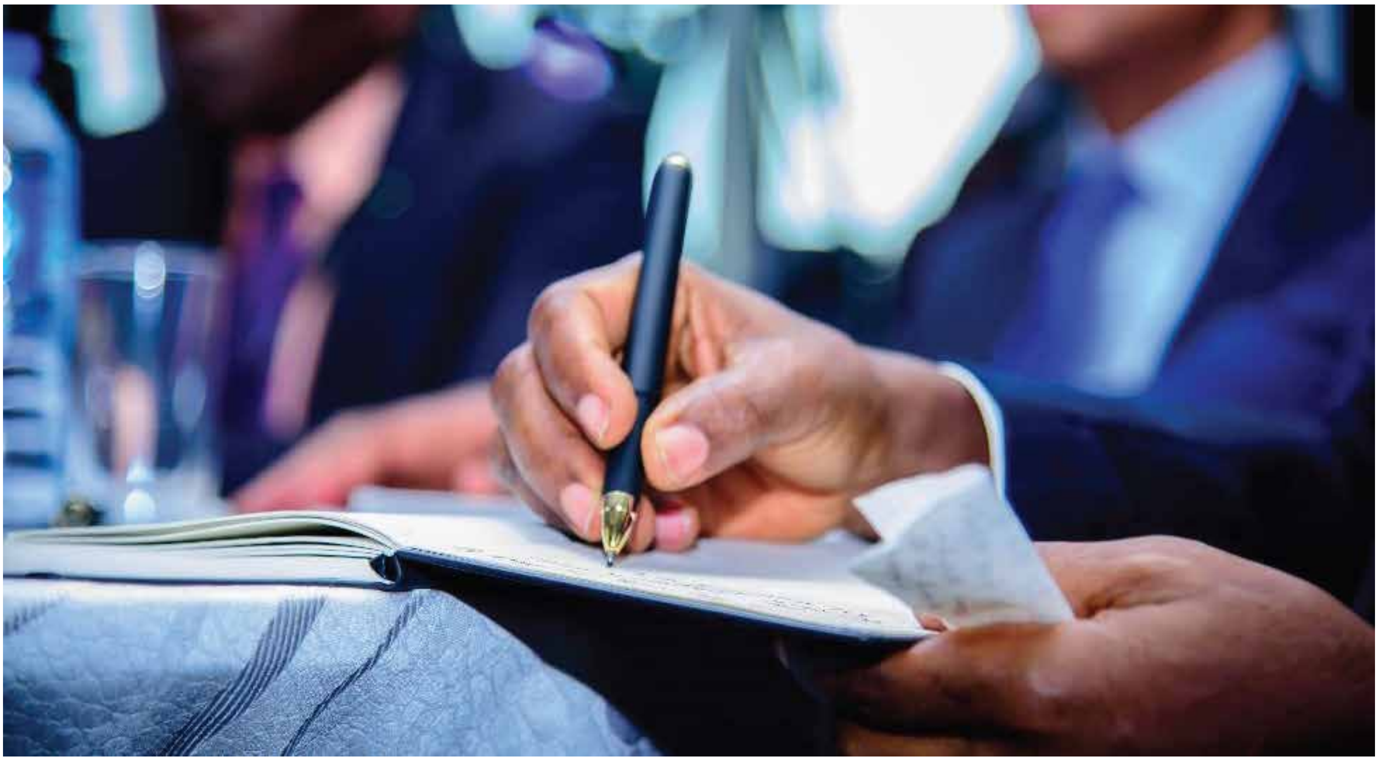
We have provided in table 1 based on the definition of gross income in the Act, a payroll simulation showing 2021 payroll outlook for a hypothetical taxpayer (John Doe), with a total annual income of ₦10,290,000 , as compared with his pre-2021 payroll calculation.



[1] We have assumed the individual contributes 8% of the aggregate sum of his basic salary, housing and transport allowances to the contributory pension scheme.

Table 1

John Doe's annual PAYE computation	Pre-2021	2021
Annual income:	**₦**	**₦**
Basic Salary	6,100,000.00	6,100,000.00
Housing Allowance	1,400,000.00	1,400,000.00
Transport Allowance	1,200,000.00	1,200,000.00
Medical	440,000.00	440,000.00
Utility	440,000.00	440,000.00
Entertainment	710,000.00	710,000.00
Total income	**10,290,000.00**	**10,290,000.00**
Less: non-taxable income & tax-exempt item		
Pension (8% of aggregate sum of Basic, Housing, Transport)	0.00	696,000.00
NHF (2.5% of Basic)	0.00	152,500.00
Gross income (for CRA purposes)	**10,290,000.00**	**9,441,500.00**
Less: Reliefs		
Fixed Consolidated Relief Allowance	200,000.00	200,000.00
Variable Consolidated Relief Allowance (20% of Gross Income)	2,058,000.00	1,888,300.00
Employee pension	696,000.00	696,000.00
NHF deduction	152,500.00	152,500.00
Total reliefs	**3,106,500.00**	**2,936,800.00**
Chargeable income (Total income less Total reliefs)	**7,183,500.00**	**7,353,200.00**
Tax payable	**1,516,040.00**	**1,556,768.00**
Deductions:		
PAYE	1,516,040.00	1,556,768.00
Employee pension contribution	696,000.00	696,000.00
NHF	152,500.00	152,500.00
Total deduction	**2,364,540.00**	**2,405,268.00**
Net pay (Total income less Total deduction)	**7,925,460.00**	**7,884,732.00**

From the above simulation, the amendment means the taxpayer would be paying ₦40,728 higher in tax than the pre-amendment period.

2 Re-introduction of life assurance premium tax relief

The Act re-introduced tax relief on any premium paid in respect of life insurance on self and/or spouse in the preceding year.

> The newly re-introduced subsection 3 of section 33 PITA reads: "There shall be allowed a deduction of the annual amount of any premium paid by the individual during the year preceding the year of assessment to any insurance company in respect of insurance on his life or the life of his spouse, or of a contract for a deferred annuity on his own life or the life of his spouse".

It should be recalled that the provision, which had been in place until early 2019, was inadvertently deleted by the enactment of the Finance Act 2019. With this re-introduction, any such premium paid in 2020 is claimable in 2021 as a relief to the taxpayer.

Pension Reform Act recognition of pension, provident and retirement benefits funds

By the Finance Act 2019, section 20(g) of PITA was amended such that the requirement to get the Board's approval before contribution to a pension, provident and retirement benefits fund can be tax deductible was deleted. The Finance Act 2020 has further amended this section to mandate that Schemes to which such contribution is made to, should be recognized under the Pension Reform Act.

This implies that taxpayers and especially employers, must ensure that Schemes or Societies to which they make pension, provident and retirement benefits funds, are recognised by the Pension Reform Act

Minimum wage earners' exemption from tax

1. Finance Act 2020 further introduced a proviso to section 37 of PITA which reads "provided that minimum tax under this section or as provided for under the Sixth Schedule to this Act shall not apply to a person in any year of assessment where such a person earns the National Minimum Wage or less from an employment". Also, there was an insertion of a new paragraph 33 to the Third Schedule to PITA which reads "the income of a person from an employment where such person earns gross income of National Minimum Wage or less from such employment".

2. The implication of the above is that any individual earning National Minimum Wage; currently ₦360,000 annually or less, is exempted from payment of personal income tax.

3. Please note that minimum tax of 1% of total income still applies to any individual earning above the National Minimum Wage but whose chargeable income is zero or where the tax payable on the chargeable income is less than 1% of the total income.

Redefining the threshold of Capital Gains Tax (CGT) exemption on compensation for loss of office

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The Act has re-worded section 36(2) of the Capital Gains Tax Act to clearly define the extent of exemption of any compensation for loss of office from CGT. By the redefinition, only payment above ₦10 million is chargeable to CGT at the rate of 10%.

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The amended section now reads "sums obtained by way of compensation for loss of office, up to a maximum of ₦10,000,000, shall not be chargeable gains and subject to tax under this Act. Provided that any sum in excess of ₦10,000,000 shall not be so exempt but the excess amount shall be chargeable to gains and subject to tax accordingly"

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Additionally, employers are now mandated to deduct the CGT on any compensation for loss of office paid and remit same on or before the 10th day of month following that of payment to the relevant tax authority.

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Conclusion

In conclusion, employers are advised to critically evaluate the impact of the amendments, update payroll tax calculators and engage staff vis-à-vis the expected reduction in the latter's take home pay.

Deloitte is willing to assist with the process and also provide further clarification if needed.

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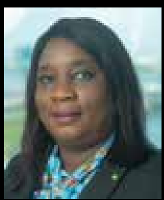

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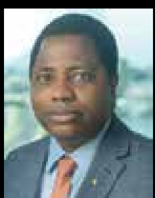

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