

# Value Added Tax In Nigeria: A beginner's guide



## OUTLINE

Definition

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In our daily lives, we usually come across people who sell goods and services to buyers at a price. The volume of sales could be on a small, medium, or even on a large scale. If you purchase an item from a retail store, you will notice a certain amount called Value Added Tax (VAT) on the receipt. The seller often adds VAT, as a separate line item, to the cost of taxable goods and services. Also, the VAT amount can be included in the total price of a commodity. Service providers have their slice of VAT when rendering services to customers. Therefore, a good grasp of the Nigerian VAT system will help foreign and local businesses in Nigeria to know how to optimize their sales.

The Value Added Tax (VAT) Act LFN 2004, as amended, governs the VAT administration in Nigeria. Other relevant laws are the VAT section of the Finance Acts 2019, 2020, 2021, 2022 and 2023. This guide looks at the twenty-four (24) frequently asked questions on the Nigerian VAT system.

The article contains six sections.

- Definition, rate, and scope
- Persons exempt and threshold
- Registration, de-registration, and relevant tax authority
- Input and output VAT, deduction at source
- Returns and filing requirements
- Two examples of how to calculate VAT in Nigeria

## SECTION I: DEFINITION, RATE, AND SCOPE

### 1. What is Value Added Tax (VAT)?

VAT is a tax levied on the supply of taxable goods and services except the items listed in the First Schedule of the VAT Act. It is a multi-stage levy on value-added on each production or distribution stage of a good or service. Value added in a manufacturing company begins from buying raw materials until the sale to the final consumers. As the tax burden passes to the final consumers, VAT belongs to the group of indirect taxes.

## 2. What is a taxable supply?

A taxable supply of goods occurs in Nigeria when the

- 1.goods are physically present in Nigeria or
- 2.beneficial owner is a taxable person in Nigeria and the right in or over the goods is located in Nigeria.

Goods are all tangible properties excluding land, building, money, or securities.

A taxable supply of services in Nigeria arises when the service is;

- 1.rendered locally by a person physically present in Nigeria,
- 2.provided to and consumed by a person in Nigeria, or
- 3.connected with an immovable property located in Nigeria.

Services are anything except for goods, or services rendered under an employment contract. Services include any intangible or incorporeal property to which a person has transferable rights; except interest in land, building, money, or security.

An incorporeal arises where;

- 1.exploitation of the right is made by a person in Nigeria,
- 2.right is registered in or acquired by a person in Nigeria,
- 3.right is connected to an intangible or immovable asset in Nigeria.

## CATEGORIES

**1** VAT exempt

**2** VATable

**3** Zero rated

- Plant, machinery, and goods imported for use in the export processing zone or free trade zone
- Tractors, ploughs, and agricultural equipment and implements purchased for agricultural purposes
- Locally manufactured sanitary towels, pads, and tampons
- Commercial aircraft; including its engine and spare parts
- Renewable energy equipment
- Raw materials for the production of baby diapers and sanitary towels
- Raw materials for the production of pharmaceutical products
- Locally produced animal feeds
- Military hardware, arms, ammunition, and locally manufactured uniforms used by the Armed forces, para-military, and other security agencies of governments in Nigeria
- Agricultural seeds and seedlings
- Interest in land and building, money, or security
- Motorcycle (CKD)/Bicycle (SKD - Semi Knocked Down) and parts

## 3. What is the rate for value added tax in Nigeria?

The VAT rate in Nigeria is 7.5%, but there are zero-rated and exempt items that do not attract a 7.5% rate.

Goods exempt include;

- Medical and pharmaceutical products
- Basic food items: Basic food items are agro-based and aqua-based staple food
- Educational books and materials
- Baby products
- Petroleum products
- Oil exports
- Fertilizers, locally-produced agricultural chemicals, and veterinary medicine
- Plant, machinery, and equipment purchased for utilization of gas in downstream operations

- Gas supply by gas-producing companies to Electricity Generating Companies (GENCOs), Electricity generated by GENCOs and supplied to National Grid or Nigeria Bulk Electricity Trading Company (NBET), and Electricity transmitted by Transmission Company of Nigeria (TCN) to Electricity Distribution Companies (DISCOs)

On the other hand, services exempt are;

- Medical services
- Services rendered by Unit Micro-Finance Banks and Mortgage Institutions
- Plays and performances conducted by educational institutions as part of learning
- Exported services
- Commercial airline transportation ticket
- Lease or rental of a residential accommodation
- Shared passenger road-transport service
- Tuition of a nursery, primary, secondary, and tertiary education

Zero-rated goods and services are;

- Non-oil export
- Goods and services purchased by diplomats
- Goods purchased for use in humanitarian donor-funded projects

## SECTION 2: PERSONS EXEMPT AND THRESHOLD

### 4. Apart from goods and services, are businesses exempt from VAT?

Yes.

Small businesses with an annual turnover of below ₦25 million are exempt from accounting for VAT. A small business can issue an invoice without including the VAT on sales (output VAT). However, the business will pay (input) VAT on the purchase of taxable goods and services.

### 5. How is the threshold determined?

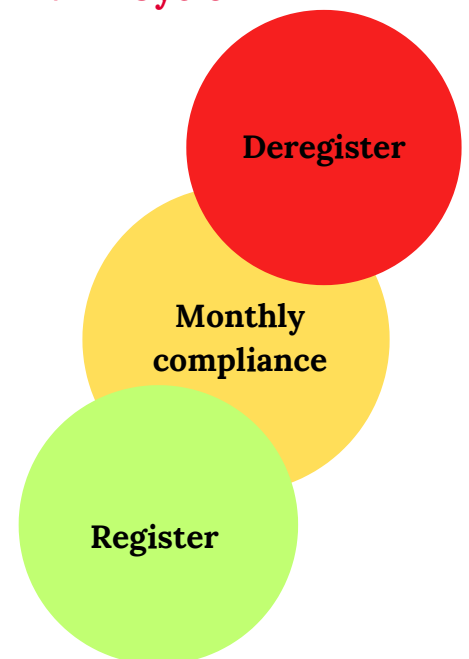
A taxable person who:

- made taxable supplies of ₦25 million before February 1, 2020 will continue to account for VAT, even if the person has taxable supplies below ₦25 million in the current year.
- did not attain ₦25 million taxable supplies before February 1, 2020, must account for VAT immediately after it reaches the threshold within the year.
- has an annual turnover below ₦25 million but expects to reach the threshold at a future date within the calendar year and shall immediately commence accounting for VAT.

- makes taxable supplies of ₦25 million and above within a calendar year will file monthly VAT returns even though a part or the entire supplies are exempt.

A calendar year is 12 months starting from the first day of that year.

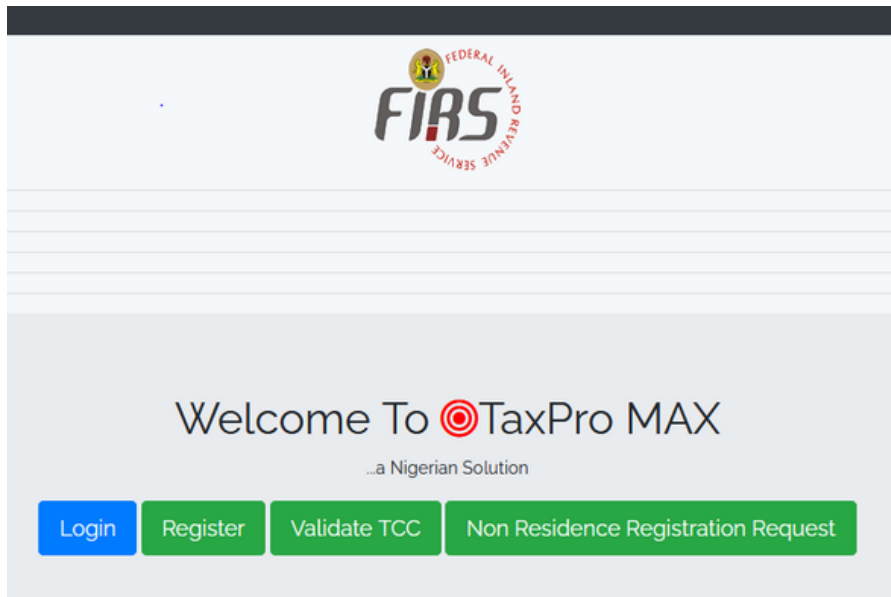
## VAT Cycle



## SECTION 3: REGISTRATION, DE-REGISTRATION, AND THE RELEVANT TAX AUTHORITY

### 6. Who is the relevant agency for VAT administration?

The Federal Inland Revenue Service (FIRS) is the sole agency for administering value added tax in Nigeria.



### 7. When should a taxable person register for VAT?

VAT registration will arise when a taxable person commences operations in Nigeria. The commencement date is the earliest date of any of the following activities:

- (i) Advertises its products or services for sale or
- (ii) Obtains an operating license in Nigeria or
- (iii) Makes a first sale or purchase or
- (iv) Performs its first trading contract after incorporation or
- (v) Sends or receives the first invoice or set of goods or
- (vi) First renders services to customers.

### 8. How do I register a business or an individual for VAT?

A taxable person can register for VAT by submitting a duly completed taxpayer registration form and questionnaire, incorporation or registration documents from the Corporate Affairs Commission (CAC), and an application letter to register for VAT at the designated FIRS office. In addition, FIRS will require an approved means of identification to register an individual or business name.

Entities registered with the CAC after 1 September 2023 can make use of the online self-registration option with FIRS.

Eservices Portal  
— For your TCC and Receipts



Apply For TCC



Verify TCC



Verify Receipt

Upon a successful registration, FIRS will grant the taxpayer access to electronic portals such as TaxPro Max for filing tax returns and EServices for tax clearance certificate, credit notes, and receipts.

### 9. Are non-resident persons exempt from registration?

Where a non-resident person (NRP) makes taxable supplies to a person in Nigeria or a Nigerian resident, the NRP will register for VAT and state the address of the customer as its Nigerian address.

### 10. Are small businesses also required to register for VAT?

A small business may voluntarily register, charge, collect, remit the tax, and file monthly returns to the FIRS. However, such a person must notify the FIRS first and will comply with the provisions on VAT for non-exempt persons.

### 11. When is a business required to deregister from VAT?

A taxable person who permanently ceases operations in Nigeria shall deregister with FIRS within 90 days of cessation.

## SECTION 4: INPUT AND OUTPUT VAT, AND DEDUCTION AT SOURCE

### 12. What is the difference between input VAT and output VAT?

Input VAT is payable on raw materials or goods and services used for production purposes or resale or imported directly for resale. Furthermore, a taxable person cannot use input VAT that can be expended through an income statement or capitalized with an asset to reduce output VAT. On the other hand, output VAT is payable on goods and services supplied. Where the output VAT is higher than the input VAT, the balance will be payable to FIRS. However, where input VAT is more than output VAT, the taxable person claims a refund.

### 13. Is a company allowed to withhold VAT?

The responsibility to withhold VAT depends on the parties involved. When a business issues VAT invoices to a customer, the customer is required to pay the contract sum as well as the VAT amount. For instance, Seller Company renders technical service to Buyer Limited for the sum of ₦645,000 (Fee – ₦600,000, VAT – ₦45,000). Buyer Limited will be required to pay the sum of ₦645,000 to Seller Limited. Let's ignore withholding tax for simplicity.

However, the payment structure will differ:

- **if the Seller Company issues a tax invoice to specific organizations.**

Government agencies, ministries, parastatals, oil and gas companies, MTN, Airtel, and money deposit banks must withhold the VAT at source. It implies that this type of organization should pay contractors the cost of the goods/services and withhold the VAT portion. Next, the taxpayer will remit VAT to FIRS.

We shall look at another illustration using Smart Company's details above and a different customer and a Government agency. The Government agency will be required to pay ₦600,000 to the Seller Company and withhold VAT of ₦45,000.

The Government agency will remit the VAT withheld to FIRS. Therefore, the Government agency is the collection agent of FIRS.

- **under the self-account provision**

The self-account provision requires a taxable person who receives goods or services in Nigeria to withhold and remit tax in the prescribed format where the supplier is exempt from (or fails to charge) VAT.

Persons exempt from VAT include businesses with annual turnover below ₦25 million as well as NRPs without a PE in Nigeria.

For example, Seller Limited (a small company) issues an invoice to Buyer PLC. (a large company) for the sum of ₦600,000 only without VAT amount. Buyer PLC will pay ₦600,000 to Seller Limited, self-account for the VAT, and remit ₦45,000 to FIRS.

### 14. Do non-resident companies pay VAT in Nigeria?

A non-resident company (NRC) that makes a taxable supply to a person in Nigeria or a Nigerian resident is required to register and remit VAT. It also applies to NRC rendering service through electronic channels to persons in Nigeria.

### 15. Is the VAT compliance procedure for a resident company similar to the one for a foreign company?

Yes. Non-resident companies that carry out taxable supplies in Nigeria must comply with the Nigerian VAT law in the same way as local entities.

Overseas International Limited (Overseas Ltd) and its employees are located outside Nigeria. Overseas Ltd renders taxable services to customers in Nigeria through electronic channels.



### 16. Are non-resident companies required to comply with the Nigerian VAT rules?

Yes. The VAT compliance process for NRC is in electronic form and NRC can comply with the local VAT law from offshore. Alternatively, a foreign company may appoint a local tax representative for expert guidance.

### 17. Who are VAT collectors for foreign businesses?

VAT collectors are authorized agents of FIRS for collecting VAT. FIRS can appoint a non-resident supplier (NRS) to collect and remit VAT where the supply is performed via electronic means. A Non-Resident Supplier is a person making the supply directly or the intermediary through which the supply was made to Nigeria. NRS will be required to comply with the filing obligations.

### 18. What is the basis of accounting for VAT - Cash or accrual?

An accrual basis of accounting for VAT means that VAT will be payable when a taxable person issues an invoice to a customer. It does not consider whether the supplier has received payment.

The accounting basis for VAT in Nigeria is cash. A cash basis of accounting for VAT means that VAT is payable when a taxable person

receives payment rather than when an invoice is issued.

## SECTION 5: RETURNS AND FILING REQUIREMENTS

### 19. What are the documents required to file VAT returns?

VAT return is filed electronically on TaxPro Max portal. Taxpayers can complete the VAT return and upload schedules online.

### 20. How do I remit VAT?

After filing the return, the next step is to generate a payment reference code via the TaxPro Max portal for Naira tax payments. The online option to remit VAT in foreign currency is not yet active.

### 21. Am I required to file a return for a month with zero sales?

Yes. FIRS requires a taxpayer to submit a VAT return for a month with no revenue. The sales and tax payable will be zero.

### 22. What is the due date for filing VAT returns?

There are two deadlines depending on the type of return.

- For withholding VAT returns, the due date is the 14th day of the month following the month of the transaction.
- For other returns, the deadline is the 21st day of the month following the month of the transaction.

### 23. Can a taxpayer still file returns after the deadline?

Yes. A taxpayer can file a return after the due date. Late filing fee is ₦50,000 for the first month and ₦25,000 for each subsequent month of default.

### 24. What is the penalty for the following activities?

- Non-registration: ₦50,000 for the first month and ₦25,000 for subsequent month.
- Non-remittance: The unpaid sum plus a penalty of 10% and interest at a minimum rediscount rate (CBN).

## SECTION 6: TWO EXAMPLES ON HOW TO CALCULATE VAT IN NIGERIA

### Illustration 1: Transaction between two large companies

Company ABC, a large company, bought raw materials at ₦2,150,000 (VAT inclusive) in November 2023.

Later, Company ABC converted the raw materials into finished goods at a selling price of ₦3,063,750 (VAT inclusive) in January 2024. How much VAT is payable?

#### **Solution 1:**

₦63,750 that is output VAT ( $₦213,750 = 3,063,750 / 107.5 * 7.5$ ) less input VAT ( $₦150,000 = 2,150,000 / 107.5 * 7.5$ ). The return is due in February 2024. As the invoice is VAT inclusive, the denominator is 100 percent plus VAT rate.

#### **Illustration 2: Professional service firm**

TeeMee Firm & Co. has an annual turnover of ₦43 million. The Firm bought a printer at ₦268,750 (VAT inclusive) in May 2023. TeeMee Firm & Co. used the printer to print a professional report for a client engagement worth ₦860,000 (VAT inclusive) in December 2023. Assuming the invoice of Tee Firm & Co. contains only fee and VAT, how much VAT is payable?

#### **Solution 2:**

₦60,000 which is  $(7.5/107.5 * ₦860,000)$ . Recall our explanation of input VAT in Section 3 above. The VAT paid on the printer purchase can be expensed or capitalized with the asset. Hence, the amount cannot reduce output VAT. The return is due in January 2024.



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