INTRODUCTION

Following the passage of the Finance Act 2019, the Federal Inland Revenue Service (FIRS or the Service) has released several circular providing clarification on certain provisions of extant tax laws that were amended by the Finance Act 2019 (the Act). By a circular dated April 29, 2020 (the Circular) the FIRS provided clarifications on the application of sections 9, 19, 23, 24, and 80 of the Companies Income Tax Act (CITA) Cap. C21 LFN 2004 (as amended) which provides for the tax treatment of Real Estate Investment Companies (REIC) in Nigeria.

We have set out below our analysis of the provisions of this Circular and have examined whether it accords with the provisions of CITA.

HIGHLIGHTS OF THE CIRCULAR

Definition of REIC, Real Estate Investment Scheme (REIS) and Real Estate

The Circular restates the definition of REIC under CITA as a company duly approved by the Securities and Exchange Commission (SEC) to operate a REIS in Nigeria. It defines REIS to include a company, trust or other corporate structure approved by the SEC, primarily engaged in and invests in income generating real estate assets or real estate related asset and is expected to distribute not less than 75% of its income within 12 months of the receipt of the income. The Circular also defines Real Estate as income generating property consisting of land and building, including special purpose vehicles holding same.

Income of REIC

The Circular identifies 4 classes of income from REICs, namely: (x) rental income; (y) dividend from another REIC; (z) gains from the disposal of assets; and (xx) others (i.e. fees and other income not related to REIS).

Exemption from Excess Dividend Tax

The Circular provides that the distributions made by a REIC to its shareholders from rental income and dividend income received on behalf of its shareholders will not constitute dividends for the purposes of section 19 of CITA. As such, rental and dividend income redistributed by REIC to its shareholders would be backed out from the total dividend received by REIC before arriving at the net amount of dividend that is relevant for the purposes of section 19 of CITA.

The Circular, however, noted that such exemption will only apply where: (x) a minimum of 75% of the rental or dividend income received is redistributed as dividends to the shareholders; and (y) such redistribution is done within 12 months after the end of the financial year in which the rental or dividend income was received.
**Exemption from Income Tax**

The Circular restates the provisions of section 23(1)(s) of CITA that exempts the rental or dividend income received by a REIC from income tax. It further clarifies that the gross amount of rental income and dividend received by a REIC will be treated as a non-taxable income because the amount is deemed to have been received on behalf of its shareholders.

The Circular also subjects a REIC’s exemption from income tax under section 23(1)(s) of CITA to the conditions stated above for excess dividend tax exemption.

Importantly, the Circular stated that even where a company has met the conditions to qualify for income tax exemption, any undistributed rental or dividend income will be chargeable to income tax.

**Non-exemption for Fees and Other Income**

The Circular provides that the income of the REICs from gains, fees, and other income of a REIC other than dividends or rental income are taxable in accordance with the provisions of the CITA.

**Allowable Expenses for REIC**

Given that the rental or dividend income received by a REIC is exempt from income tax under section 23(1)(s) of CITA, any expense of the REIC incurred for the purposes of earning this tax exempt income (including any dividend distributed to its shareholders), is treated as a non-allowable expense for tax purposes.

The Circular, however notes that where the conditions that will allow a REIC to enjoy the tax exemption provided in section 23(1)(s) of CITA are not met, rental or dividend income received by the REIC will constitute a taxable income under section 9 of the CITA, and thus all expenses incurred for the purposes of earning the rental and dividend income, including dividend payments to shareholders, shall be allowable expenses for tax purposes.

**WHT on Dividend Payment to REIC**

The Circular clarifies that distribution or dividend payment made to a REIC pursuant to a REIS is not subject to WHT. Thus, given that it is exempt from WHT, it is not considered as franked investment income. It should be noted however that where a REIC receives distribution or dividends otherwise than under a REIS, such payment shall be subject to WHT.

**WHT on Dividend Payments by REIC to Shareholders**

The Circular clarifies that distributions or dividend payment by REIC to its shareholders is subject to WHT at the rate of 10%. However, where such a shareholder is also a REIC, the Circular provides that WHT shall not apply to such payment.

**OUR TAKE**

From the analysis above, we note that some of the issues that may give rise to debate in respect to the Circular includes the conditions for the exemption of the income of REIC from excess dividends tax, and the taxation of the undistributed rental or dividend income of a REIC where 75% of such income have been distributed to its shareholders within 12months.

As it relates to the exemption of REIC from excess dividends tax, it appears that the FIRS has adopted a purposive interpretation of section 19 of CITA. This is because, whilst no such express condition for the exemption is contained in CITA, it is the case that the exemption is premised on the fact that REIC is exempt from income tax under section 23 (1)(s) of CITA.
Accordingly, it stands to reason that the conditions prescribed under section 23(1)(s) of CITA should necessarily apply in interpreting section 19 of CITA.

With respect to the provision in the Circular that the undistributed rental or dividend income of a REIC will be chargeable to income tax even where the REIC complies with the conditions prescribed under section 23(1)(s) of CITA, we are of the view that this is consistent with the mischief that CITA seeks to address in ensuring that the income of REIC is not subject to double taxation. Accordingly, where the REIC retains such dividend or rental payment, the REIC should not enjoy any income tax exemption on such income. Our conclusion is further bolstered by section 23(1B) (c) of CITA that provides that REIC will not be exempt from tax on the dividend and rental income not distributed after 12 months from the end of the financial year that the dividend or rental income was earned. In essence, where part of its dividend and rental income is distributed within 12 months and the remainder is distributed after 12 months, only the dividend and rental income distributed within 12 months will be exempt from income tax. By extension, the same rule should apply where only 75% of its dividend and rental income is distributed to its shareholders.

In sum, given the complexity surrounding the tax treatment of REIC, the clarification by the FIRS is a welcome development and a necessary guide for all stakeholders to follow in determining, planning and ensuring compliance with their tax obligations under the law.

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