

## FIRS issues circular on tax treatment of foreign exchange transactions

June 2024

The Federal Inland Revenue Service (FIRS) recently issued an information circular (“the Circular”) to guide the tax treatment of foreign exchange transactions.

The issuance of the Circular, dated 24 June 2024, has been necessitated by the devaluation of Nigeria’s Naira and the impact of the devaluation on the performance and position of Nigerian businesses. The Circular supersedes the FIRS circular of 14 June 2024 on the same subject.

We have provided below, highlights of the Circular and our comments on the guidance provided by FIRS.

### Highlights of the Circular

#### 1. Classification and general tax treatment of exchange differences

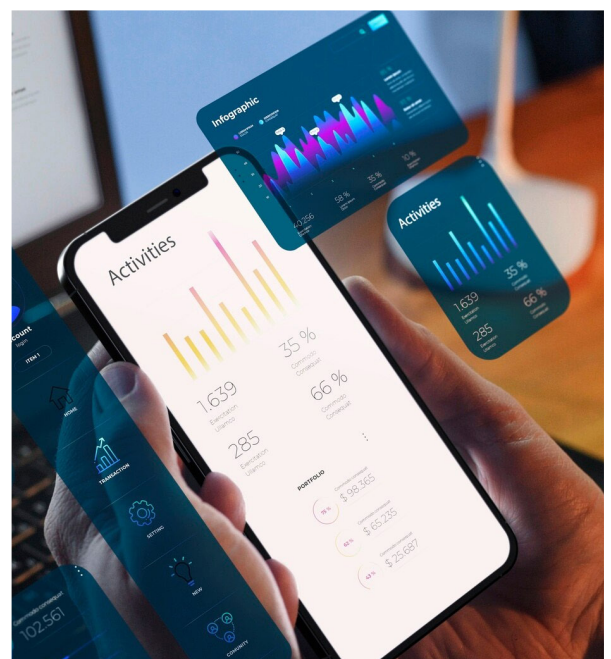
The Circular classifies exchange differences into realised and unrealised. This is generally in line with accounting treatments of exchange differences. However, for tax purposes, while realised exchange differences are to be treated as non-adjustable items in ascertaining a company’s assessable profits<sup>1</sup>, unrealised exchange differences should be adjusted.

#### 2. Treatment of exchange differences relating to monetary and non-monetary items

Realised exchange differences arising from the settlement or recovery of monetary items may result in taxable income or deductible expense for income tax purposes. For example, realised exchange losses on the settlement of trade payables will be tax-deductible, while realised exchange gains will be taxable.

#### 3. Treatment of hedging transactions<sup>2</sup>

Unrealised foreign exchange differences arising from hedging transactions are to be adjusted to determine a company’s assessable profit until the hedged item is recognised.



1. Income of a company adjusted for income tax purposes

2. Hedging transaction is a strategic approach for the management of risk such as risk from fluctuation in foreign exchange.

## 4. Implication of unrealised exchange differences on corporate taxes

### a. Tertiary Education Tax (TET):

The tax treatment of exchange differences for Companies Income Tax (CIT) purposes extends to TET. Hence, unrealised exchange differences would be adjusted in ascertaining a company's assessable profit for TET purposes.

### b. National Agency for Science and Engineering Infrastructure (NASENI) levy<sup>3</sup>, National Information Technology Development Agency (NITDA) Levy<sup>4</sup> and Minimum tax:

The Circular noted that unrealised exchange differences recognised for accounting purposes should not be adjusted when computing NASENI levy, NITDA levy, and Minimum tax.

## 5. Implication of exchange differences on tax-exempt items

Exchange differences arising from tax-exempt items (e.g., Federal Government of Nigeria's Eurobonds) are not taxable (in the case of a gain) and not deductible (in the case of a loss). However, tax computations should adequately disclose all incomes and expenses relating to such tax-exempt items.

## 6. Obligation to maintain relevant documentation and returns

Companies are required to provide a reconciliation of exchange differences recognised in their financial statements. Further, companies are advised to maintain records of all foreign currency transactions.

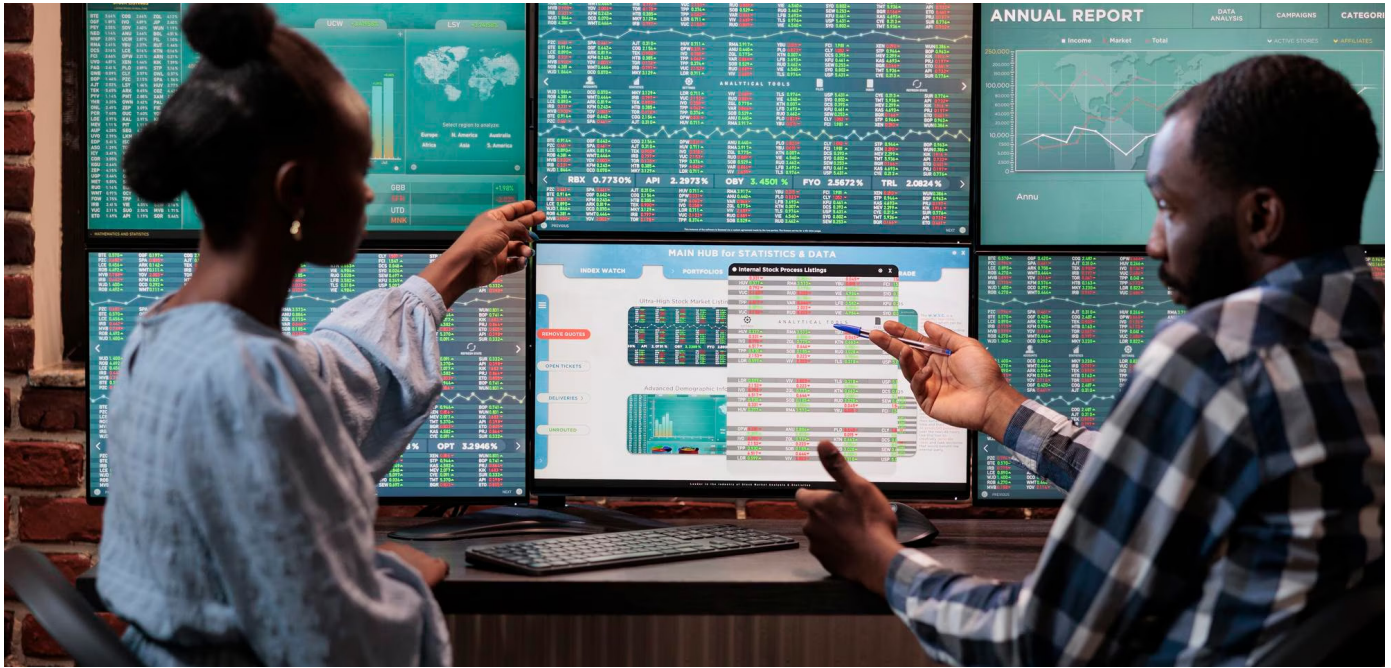
## 7. FIRS' power to adjust artificial transactions

The Circular restates the general power of FIRS to adjust artificial transactions, especially where the transactions are between related parties. This is in line with Section 22 of the Companies Income Tax Act (CITA).

3. 0.25% of the profit before tax (PBT) of eligible companies.

4. 1% of PBT, payable by companies specified in the NITDA Act.





## Commentary

The Circular highlights what is already obtainable, hence taxpayers already familiar with the correct tax treatment of foreign exchange transactions need not fundamentally change their current practice. This notwithstanding, there are aspects of the Circular that need clarifying. These are outlined below:

- While FIRS' request for reconciliation of exchange differences recognised in a company's financial statements is understandable, the mode of receipt of the information is unclear.

Since 2021, income tax returns are filed via the TaxPro-Max platform, which does not have a provision for the attachment of other documents other than audited financial statements. Therefore, does FIRS' request imply that companies should start filing printed copies of income tax returns, or file the requested reconciliation separately or would the TaxPro Max platform be improved to accommodate additional information request by FIRS?

- The statement "offsetting of exchange gains or losses shall be segregated by line of business and by tax regimes" per Paragraph 12 (d) of the Circular may imply that our tax system may be moving closer to a full line of business/segmented computations and returns. This is not new and would be in line with the law.

## Conclusion

We implore companies to pay attention to the FIRS clarification of tax treatment of foreign exchange transactions and reflect the same in their tax returns, as may be necessary.

If you require further clarification or seek to understand how this would impact your business, please reach out to [ngtaxpartners@deloitte.com](mailto:ngtaxpartners@deloitte.com)

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