

WHAT IS PAYE? PAYE means Pay As You Earn

Taxation of individuals in employment is operated through the Pay-As-You-Earn (PAYE) scheme. Under the scheme, the employer is regarded as an unpaid agent of the Tax Authority and as such is expected to deduct taxes on salaries, wages, bonuses, allowances and benefits in kind.

The system ensures that tax withheld monthly from employee's salaries and wages are remitted to the relevant tax authority's Internally Generated Revenue account.

The following are the processes and procedures provided in the Personal Income Tax (Amended) Act 2011, to ensure the smooth running of the PAYE scheme.

1.0. STEP 1: REGISTRATION

1.1. All employers of labour are expected to register with the relevant Tax Authority as an agent of the State Government, for the purpose of deducting and remitting PAYE tax from the employee's pay as stipulated in Regulation 1 of Operation Pay As You Earn (PAYE) regulations which states that:

'An employer shall register with the relevant tax authority for the purposes of deducting income from his employees with or without formal notification or direction by the relevant tax authority'

Regulation 2, paragraph 1 and 2 of Pay As You Earn Regulations also states that:

'The employer shall within six months of the commencement of these regulations, or within six months of commencing a business, deduct tax from emoluments of his employees and remit to the relevant tax authority'

'Without prejudice to the provision of regulations 21 of these regulations, an employer who fails to or refuses to register with the relevant tax authority within the time specified in paragraph (1) of this regulation commits an offence and is liable on conviction to pay N25,000 in addition to the payment of arrears of the tax due'

1.2. The application to the relevant tax authority for consent to operate the PAYE scheme must include:

- a. A Letter of application to register the establishment. (The nature of business should be indicated in the letter of application) as provided for in paragraph 1 of "Operation Of Pay As You Earn (PAYE) Regulations.
- b. Evidence of registration / incorporation of the business enterprise.

- 1.3. After the approval of the application, the business enterprise is allocated a reference number which must be quoted in all correspondence with the tax authority.

The enterprise is also issued Form 'G' which is the employer's remittance form.

2.0. PROVISION OF PITA ON PAYE RETURNS

- 2.1. There are basically two (2) types of returns and two (2) forms are mainly used in rendering these returns. They are Tax form H1 and H3. The two types of returns are:

- a. Return on income, tax relief and total tax deducted in the preceding year (Tax Form H1).
- b. Return for the year of assessment: This is return on the income and claim for allowances, bonuses, benefits in kind or perquisites e.t.c. (Tax Form H3)

2.2. FILING OF RETURNS

The filing and return process, is a core process in tax administration, therefore Tax payers are expected to file returns in compliance with tax laws.

At the beginning of the tax year, every employee is expected to fill tax Form 'A', the employer is also expected to fill form H3 or any prescribed form for return of income and claim for allowances and reliefs on behalf of its employees for the year of assessment (period of twelve (12) Months commencing from the 1st day of January of the year of assessment)

The form H3 must be signed and stamped by an officer in the establishment duly assigned to do so and be filed with the relevant tax authority within the time specified in the notice as stated in regulation '13' of Operation Of Pay As You Earn (PAYE) Regulations.

- 2.3. The submitted forms must be examined by the relevant tax office to ensure full compliance of the information demanded, before proceeding to the next stage known as coding.

3.0. THE CODING PROCESS

This is the process of determining the reliefs and allowances due to each employee for the year of assessment.

- 3.1.** The coding process commences with the submission of properly filled, signed and stamped form H3 by employers through the various tax offices in the state to the Information, Communication and Technology Unit (ICT) of the Internal Revenue Service. (Coding is done centrally in the Services' Headquarters to ensure uniformity, eliminate leakages in the system due to errors or misconduct on the part of tax officials)

For proper tax computation, the following details are required;

- a. Name of establishment
- b. Names of employees
- c. Employee's employment details i.e., employment year, grade level and step
- d. Employee's salary details i.e. salary and taxable allowances.

- 3.2.** The tax authority will usually ask for documentary evidence to support claims for reliefs and allowances deducted in form 'A' and Form H3.

NOTE: The following deductions are tax exempt, that is, they are not taxable.

- a. National Housing fund:- 2.5 % of annual basic salary.
- b. National Health Insurance Scheme:- 5% of annual basic salary.
- c. Life assurance premium, a deduction of the actual amount of any premium paid by the individual during the year preceding the year of assessment.
- d. National pension scheme:- 7.5% of annual basic, housing and transport.
- e. Gratuities:

Any employee who is not a contributor to any of the schemes listed above cannot enjoy the reliefs granted.

3.3. PRACTICAL GUIDES TO CODING:

The following are the steps towards effective coding as provided for in the Personal Income Tax (Amendment) Act, 2011.

- a. Determine the consolidated salary/ Gross emoluments i.e. add the income from all sources (What the Tax payer earns per annum)
- b. Give as consolidated relief allowance, the sum of ₦200,000.00 or 1% of the consolidated salary whichever is higher plus 20% of the consolidated annual salary as stipulated in section 33 sub-section 1:

'There shall be allowed a consolidation relief allowance of N200,000.00 subject to a minimum of 1 percent of gross income whichever is higher plus 20 per cent of the gross income and the balance shall be taxable in accordance with the income table in the Sixth Schedule to the Act'

After the relief allowance and exemptions have been granted, the balance of income is then taxed as specified below:

INCOME TAX RATES

These tax rates are graduated

- First N300,000 @ 7%
- Next N300,000 @ 11%
- Next N500,000 @ 15%
- Next N500,000 @ 19%
- Next N1,600,000 @ 21%
- Above N3,200,000 @ 24%

PRACTICAL EXAMPLE (1)

Consolidated salary = 1,100,000.00

Consolidated Relief Allowance = $1,100,000.00 \times 20\% + 200,000.00 = 420,000.00$

Chargeable Income. $(1,100,000.00 - 420,000.00) = 680,000.00$

Chargeable income will now be graduated according to the tax rates = 680,000.00

1 st	300,000.00 X 7%	=	21,000.00
next	300,000.00 X 11%	=	33,000.00
next	80,000 X 15%	=	<u>12,000.00</u>

Total Annual Tax = 66,000.00

Monthly tax = 66,000.00/12 = 5,500.00

PRACTICAL EXAMPLE 2:

Salary = 301,000.00

Consolidated relief allowance	=	260,200.00
Chargeable income	=	40,800.00
1 st 40,800 X 7%	=	2,856.00
Annual tax	=	2,860.00
1% of annual gross	= 301,000.00 X 1%	= 3,010.00

NOTE:

From the above, 1% of annual gross is higher than annual tax computed. And the law in PITA Section 37 stipulates that:

... "where the individual has no chargeable income or where the tax payable on the chargeable income of that individual is less than 1% of the total income of that individual, the individual shall be charged to tax at the rate of 1% of his total income"

From on the above computation, the individual's tax on chargeable income is less than 1% of the annual gross. Therefore 1% of the individual's annual gross is taken as his annual tax.

Annual Tax	=	301,000.00 X 1%	=	3,010.00
Monthly tax	=	3,010.00/12	=	250.83

PRACTICAL EXAMPLE 3:

Salary	-	18,760,345.19
CRA	-	3,952,069.03
NHF	-	469,008.62

NHIS	-	938,017.25	
Life Assurance	-	500,000.00	
Pension	-	1,407,025.88	
Total Allowance			7,266,120.78
Chargeable income			11,494,224.41
1 st 300,000.00 X 7%	=	21,000.00	
+ next 300,000.00 X 11%	=	33,000.00	
+next 500,000.00 X 15%	=	75,000.00	
+ next 500,000.00 X 19%	=	95,000.00	
+ next 1,600,000.00 X 21%	=	336,000.00	
8,294,224.41 X 24%	=	<u>1,990,613.85</u>	
Total annual tax	=		2,550,613.85
Monthly tax	=		212,551.15

- c. The reliefs and allowances due to the employee and the tax to be deducted monthly is communicated to the employer in writing.

4.0. APPLICATION OF DEEMED INCOME OR PRESUMPTIVE TAX TABLE

- 4.1.** Deemed income is an assumed or presumptive income used mainly for expatriates working in Nigeria whose income cannot be easily ascertained.

The deemed income chart prepared by the State Internal Revenue Service, cuts across different professions and nationalities and have also been stratified into different categories ranging from Technicians to Managing Directors. The deemed income chart serves as a guide for determining the income earned by these expatriates

5.0. WHAT IS TAX CLEARANCE CERTIFICATE? (TAX FORM 'Z')

Tax Clearance Certificate is an official document issued by the tax authority to a Tax payer certifying that the tax assessed on the income of the person for the three years immediately preceding the current year of assessment has been duly paid.

5.1 A Tax payer can demand for his Tax Clearance Certificate from the relevant tax authority and the certificate is expected to be issued to him within two (2) weeks of demand or the tax authority should give reasons for the denial, (Section 85 sub-section 1)
 A tax Clearance Certificate may not be issued to a person who has settled his tax liability but such taxes have not been remitted to the relevant tax authority (WHT and PAYE Tax)

5.2 The following conditions must be fulfilled before a Tax Clearance Certificate can be issued.

SN.	CHECK LIST	YES	NO
A	Tax payer must apply in writing to the relevant tax authority		
B	Tax payer / establishment must have filed their returns (Tax from 'A' and H3) for the current year and Tax form H1 for the preceding year. There should also be evidence of returns filed for the past three (3) years in the control file of the establishment.		
C	There must be evidence of remittance of taxes paid to the relevant tax authority.		
D	Tax Form H2 or Certificate of payment and tax must be duly filled, signed and stamped by the employer.		
E	Tax identification number card.		
F	Detailed brief on the Tax payers.		
G	2 passport photographs, etc.		

5.3 **CONTENTS OF A TAX CLEARANCE CERTIFICATE**

A Tax Clearance Certificate shall disclose in respect of the last three (3) years of assessment.

- a. Chargeable Income
- b. Tax payable
- c. Tax paid
- d. Tax outstanding (if any)
- e. Tax payer Identification Number.

5.4 **TRANSACTIONS REQUIRING TAX CLEARANCE CERTIFICATE.**

Section 85(4) requires all MDAs or commercial banks to demand from any person having any dealing with the establishment, a Tax Clearance Certificate and also verify the

genuineness of the Tax Clearance Certificate by referring same to the issuing tax authority.(section 85(2) of the Personal Income Tax Act) 2011)

The following are the grounds for which a TCC can be issued:

- i. Application for Government loan for industry or business;
- ii. Registration of motor vehicle;
- iii. Application for firearms licence;
- iv. Application for foreign exchange or exchange control permission to remit funds outside Nigeria.
- v. Application for certificate of occupancy;
- vi. Application for award of contracts by Government, its agencies and registered companies;
- vii. Application for approval of building plans;
- viii. Application for trade licence;
- ix. Application for transfer of real property;
- x. Application for import and export licence;
- xi. Application for agent licence;
- xii. Application for pools or gaming licence
- xiv. Application for registration as a contractor;
- xv. Application for distributorship
- xvi. Confirmation of appointment by Government as chairman or member of a public Board, institution, commission, company or to any other similar position made by Government.
- xvii. Stamping of guarantor's form for a Nigerian passport;
- xix. Application for registration of a limited liability company or of a business name;
- xx. Application for allocation of market stall;
- xxi. Appointments or election into public office
- xxii. For change of ownership of vehicle by the vendor;
- xxiii. Application for plot of land;
- xxiv. Any other transaction as may be determined from time to time.

6.0 END OF YEAR RETURNS

At the end of each tax year, every employer is required to file returns by completing the employers Annual declaration form (Form HI) in a prescribed manner, showing the total emoluments of each employee during the preceding year, the tax reliefs granted and the

total tax deducted not later than 30 (thirty) days of the end of the year to the relevant tax authority.

7.0. CHECKLIST FOR CONTROL FILE

SN.	CHECK LIST	YES	NO
a	Letter of application to operate the PAYE scheme		
b	Letter of approval giving a reference number to the establishment which must be quoted in all correspondences		
c	Remittance form known as form 'G'		
d	Tax form H1 used to file returns on income, tax relief and total tax deducted in the preceding year		
e	Tax Form H3 used for returns for the year of assessment on the income and claims for allowances, bonuses, benefits in kind or perquisites, etc		

8.0 COMMONLY USED TERMINOLOGIES:

- a. **Relevant tax authority**- Means the tax authority of the territory in which the individual is deemed to be resident in that year.
- b. **"Year of assessment"**- Is the year for which the taxpayer is assessed to tax i.e. the period of twelve (12) months commencing on the 1st day of January.
- d. **Basis of assessment**- The basis for assessing individuals to tax depends on the source of income accruing to the individual as follows :
 - a) Income from employment such as salaries, wages, allowances, bonuses benefits in kind or perquisites are assessed to tax on actual year basis.
 - b) Income derived from investments such as dividend, interest, annuities, rent and royalty e.t.c. is assessed to tax on preceding year basis.
 - c) Income derived from trade, business, vocation or professions are assessed to tax on preceding year basis.
- e. **Earned Income**- This is defined as income received from actual work done or service rendered. It includes income earned from trade, business, vocation or profession and income received from salaries, allowances, perquisites e.t.c.
- f. **Unearned Income**- This is defined as income received from investments such as dividend, interest, rent, royalty e.t.c.
- g. **Benefits-in kind or Perquisites**- These are expenses incurred by an employer for the personal benefit of the employee. They are regarded as the non-monetary remuneration of

an employee. For the purpose of tax, the employee is deemed, to have earned income which is liable to tax.

The benefits taxable are;

- Provision of accommodation: Where an employee is provided with an accommodation or official residence anywhere in Nigeria, the taxable benefit that is deemed to have accrued shall be the annual ratable value of the premises or the actual rent paid.
 - Provision of assets: Where an employee is provided with assets such as a vehicle, furniture and fittings, air conditioners e.t.c. the taxable benefits is 5% of the cost of the asset.
 - Where the asset is hired or rented the taxable benefit shall be the actual rent paid.
 - Where the employee is provided with service of support staff such as drivers, cooks, gardeners the benefit-in kind shall be the actual amount incurred to provide such service.
- i. **Itinerant Worker-** Includes an individual irrespective of his status who works at anytime in any State during a year of assessment (other than a member of the armed forces) for wages, salaries or livelihood by working in more than and working for a minimum of twenty (20) days in at least three (3) months of every assessment year.
- j. **Basis Period:** Is defined as the period for which the Tax payer's income is being assessed to tax. It is the period under focus in any year of assessment.
- k. **Place of Residence:** Means a place that is available for the domestic use of an individual in Nigeria on a relevant day, and does not include any hotel, rest house or other place at which he is temporarily lodging unless no more place is available for his use on that day.
- l. **Principal Place of Residence** – where an individual has two or more places of residence in Nigeria and these places are not within the same territory. He is deemed to be resident in the territory in which he has his principal place of residence.
- m. **Total Income:** Means in relation to an individual for a year of assessment his aggregate assessable income for that year.
- n. **Tax Avoidance** - The act of arranging a Tax payers affairs in such a manner that he reduces his tax liability without contravening the law.
- o. **Tax Evasion** – An illegal means adopted by a tax payer to escape payment of tax or reduce his tax liability.

- p. **Tax Investigation** – an in-depth inquiry or examination of the records books, document activities, etc of the tax payer by the tax authority where the tax authority has evidence or strong suspicion that the Tax payer has committed tax fraud or tax evasion.
- q. **Best of Judgment (BOJ)** – This is an estimated assessment which is raised at the discretion of the tax authority where a taxable person has not filed his tax return within the stipulated time or where the tax return filed has been rejected by the tax authority.

9.0. OFFENCES, PENALTIES: Various penalty provisions for offences committed in the Act have been increased upwards as detailed below.

OFFENCES AND PENALTY			
Section	Offences	Old Penalty	New Penalty
S.74(1)	Failure to deduct / remit tax	10% of taxes not deducted or N5,000 whichever is higher	10% of tax not deducted / remitted plus interest at the prevailing monetary Policy of the CBN.
S.81(3)	Failure to file returns by Employers		N500,000 (Body Corporate) N50,000 (Individual)
S.85(7a & b)	Giving of incorrect information for the purpose of obtaining Tax Clearance Certificate or obtaining Tax Clearance Certificate through misrepresentation, forgery or falsification		Fine of N50,000 plus twice the Tax Payable by him or three years imprisonment or both, such fine and imprisonment.
S.85(9)	Failure to demand and verify Tax Clearance Certificate		N5,000,000.00 or 3 years imprisonment or both.
S.94	Failure to furnish a return, statement, information or to keep records required.	N200 in the 1 st instance N40 for everyday.	N5,000, a further sum of N100 daily during which the failure continues,

			and in default of payment, to imprisonment for six (6) months.
S.95(I) a.	Making Incorrect returns by omitting or understating any income liable to tax.	10% of the correct tax	Fine of N20,000 in the first instance and double the amount of tax which have been under charged in consequence of incorrect return or information.
b.	Giving of incorrect information affecting the liability to tax		
S.96(I)(a)	Making false statements and returns for the purpose of obtaining a deduction, set-off, relief or overpayment in respect of tax for himself or any other person.	N5,000 or 5 years imprisonment	N500,000 for Corporate body N50,000 for individuals or imprisonment for 6 months.
b.	Any Person who aids, abets, assists, counsels, incites or induces any other person to:	N5,000 or 5 years imprisonment	N500,000 for Corporate body N50,000 for individuals or imprisonment for 6 months.
(i)	deliver a false return or statement		
(ii)	To keep and prepare false accounts or particulars concerning any income on which tax is payable		
(III)	Any person who unlawfully refuses or neglects to pay tax is guilty of an offence		

	and is liable on conviction		
S.97	Offences by authorized and unauthorized persons	N1,000 or 3 years imprisonment or both	N100,000 or 3 years imprisonment or both

(a) A person appointed for the due administration of this Act or employed in connection with the assessment or collection of the tax:

- i. Demands from a person an amount in excess of the authorized assessment of the tax or
- ii. Withholds for his own use or otherwise, a portion of the amount of tax collected or
- iii. Renders a false return, whether orally or in writing, of the amount of tax collected or received by him; or
- iv. Defrauds a person, embezzles his money or otherwise uses his position to deal wrongly with the relevant tax authority or

(b) not being authorized under this Act to do so, collects or attempts to collect tax under this act: is liable to a fine of N 100,000.00 or to imprisonment for three (3) years or both such fine and imprisonment (see box for section 97).