FEDERAL INLAND REVENUE SERVICE

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INFORMATION CIRCULAR

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Subject: CLARIFICATION ON THE AMENDMENT TO SECTION 16 OF COMPANIES INCOME TAX ACT IN RELATION TO TAXATION OF INSURANCE COMPANIES

This circular is issued for the information and guidance of the general public, taxpayers, tax practitioners and particularly, insurance companies in line with the provisions of the relevant tax laws.

1.0 Introduction

Section 16 of Companies Income Tax Act (CITA), Cap. C21, LFN 2004 (as amended), revised the rules for the taxation of life and non-life insurance businesses. The amendment also aligned the carrying forward of losses with the provisions of **Section 31 (2) of CITA** such that losses incurred by an insurance company may be carried forward indefinitely for both life and non-life insurance businesses. Moreover, the amendments provided clarity on what constitutes Gross Premium and Gross Income, and the basis for the computation of minimum tax.

2.0 Non-Life Insurance Business

The provisions of **Section 16(8)(a) and 16(8)(b)** specify how to determine reserve for unexpired risk, and estimated amount of all outstanding claims and outgoings.

2.1 Reserve for Un-Expired Risk

Based on the provisions of section 16(8)(a) of CITA, un-expired risk shall be determined on a time apportionment basis of the risk accepted in the year.

Illustration 1

An extract from the financial statement of Insurance PLC for the year ended December 2020 shows the following:

Reserve for un-expired risk brought forward from 2019 - ₦2,000,000
Reserve for expired risk as at 31st Dec 2020 - ₦5,000,000

The un-expired risk that is attributable to the risk accepted in the year is ₦3,000,000 (5,000,000 - 2,000,000).

NOTE:

An insurance company shall maintain details and schedule of policies or risks accepted in a given year and the computation of un-expired risks associated with them. The schedule shall include:

a. the name of the policy holder,
b. type of policy,
c. period covered by the policy
d. amount of the premium, and
e. un-expired risk.

2.2 Estimated Amount of Outstanding Claims and Outgoings

The amendment allows for an estimated amount of outstanding claims and outgoings during a given year instead of a percentage of total premium.

The "estimated outstanding claims" include verified but unpaid claims and an estimate for unverified claims for the accounting period. The estimated claims and outgoings of an accounting period is deductible in that same year and added to the assessable profits of the immediate following year. As such, any shortfall or excess of estimated claims and outgoings is adjusted for.

NOTE:

Estimated amount of outstanding claims and outgoings must be supported with detailed schedule of specific items making up the total.

<u>Illustration</u> 2

An extract from the tax returns of XYZ Insurance Ltd. for YOA 2020 and 2021 show the following:

	2020 ₦	2021 ₦
Estimated claims and outgoings	7,000,000	3,500,000
Actual claims and outgoings for the year	4,000,000	9,000,000
Net Profit Before Claims **NOTE:** Actual claims and outgoings paid in 2021 include: i. 2020 Accepted Claims 5,000,000	12,000,000	9,500,000

ii. 2021 New Claims 4,000,000		

XYZ Insurance Ltd
Computation of Assessable Profits

For 2020 year of assessment:	**₦**	**₦**
Net Profit (per account)		12,000,000
Less: Actual claims and outgoings	4,000,000	
Estimated claims and outgoings	7,000,000	11,000,000
Assessable Profit		**1,000,000**

For 2021 year of assessment:		
Net Profit		9,500,000
Add: Unutilsed Estimated claims and outgoings (2020)		2,000,000
		11,500,000
Less: Actual claims and outgoings	4,000,000	
Estimated claims and outgoings (2021)	3,500,000	7,500,000
Assessable Profit		**4,000,000**

NOTE:

Insurance companies should maintain a schedule of estimated claims and outgoings that constitute the amount deducted yearly.

2.3 Minimum Tax Computation for Non-Life Insurance Business

Section 16 (12) (a) of CITA, prescribes a fixed 0.5% of the gross premium as minimum tax for non-life insurance business. Moreover, Finance Act 2020 introduced subsection (13), which provides clarity on what constitutes "gross premium" and "gross income" for the purposes of taxation of insurance companies.

2.4 Gross Premium

Gross premium which is the base for computation of minimum tax for non-life business is defined by section **16(13) of CITA (as amended),** as "the total premiums written, received and receivable excluding unearned premium and premium returned to insured".

Note that no further deductions shall be allowed against the gross premium besides those specified by the Act.

<u>Illustration</u> 3

ABC Insurance PLC has the following extract from its financial statement for the period ended Dec. 2021.

The minimum tax payable for 2022 year of assessment is as follows:

	N	
Total Premium Received	15,000,000	
Premium Receivable	7,500,000	
Premium Returned to Insured		1,000,000
Premium paid on reinsurance		2,000,000
Un-Earned Premium (premium received in advance)		1,500,000

Compute the minimum tax payable

Solution:

Total Premium Received	15,000,000	
Premium Receivable	7,500,000	
		22,500,000
Less:		
Premium Returned	1,000,000	
Un-Earned Premium	1,500,000	2,500,000
Gross Premium Liable to Min Tax		**20,000,000**
Minimum Tax @ 0.5% X 20,000,000		**100,000**

2.5 Temporary Reduction in Minimum Tax Rate from 0.5% to 0.25%

Finance Act, 2020 granted a reduced minimum tax rate of 0.25% on tax returns prepared and filed for any year of assessment falling due on any date between 1st January 2020 and 31st December 2021. This is a temporary reprieve that is applicable to both life and non-life insurance businesses.

2.6 Format for Computing Non-Life Insurance Business Tax

This format may be used as a guide for the computation of CIT of Non-Life Insurance Business.

	₦	₦
TOTAL PREMIUM WRITTEN*		XXXXXXXX
LESS: UN-EARNED PREMIUM FOR THE YEAR (IF ANY)		(xxxxxxx)
LESS: PREMIUM RETURNED (CANCELLED INSURANCE POLICIES)		XXX
GROSS PREMIUM		**XXXXXXX**
ADD:		
ESTIMATED INSURANCE CLAIMS FOR PREVIOUS YEAR (IF ANY)	XXXXXXX	
INVESTMENT INCOME	XXXXXXX	

FEES AND COMMISSION	XXXXXXX	
RENT RECEIVED	XXXXXXX	
OTHER INCOME	XXXXXXX	XXXXXXX
NET INCOME		**XXXXXXX**
LESS: NON-TAXABLE INCOME (**IF ANY)**		(XXXXXXX)
NET TAXABLE INCOME		**XXXXXXXX**
LESS:		
RE-INSURANCE PREMIUM PAID	XXXXXX	
RESERVE FOR UNEXPIRED RISK	XXXXXX	
TAX ALLOWABLE OUTGOINGS	XXXXXX	
INSRUANCE CLAIMS: - ACTUAL FOR THE YEAR	XXXXXX	
- ESTIMATED FOR THE YEAR	XXXXXX	(XXXXXX)
ASSESSABLE PROFIT		**XXXXXXXX**
LESS: LOSS BROUGHT FORWARD (IF ANY)		XXXXXX
		XXXXXXXX
ADD BALANCING CHARGE		XXXXXXX
LESS: CAPITAL ALLOWANCES		XXXXXXX
TOTAL PROFIT		**XXXXXXXX**
COMPANIES INCOME TAX @ 30% OF TOTAL PROFIT (A)		**XXXXXXXX**
MINIMUM TAX @ 0.5% OF GROSS PREMIUM (B)		**XXXXXXX**
COMPANIES INCOME TAX IS THE HIGHER OF (A) and (B)		**XXXXXXXX**

3.0 Life Insurance Business

A "new subsection 16(6)" was inserted into CITA which defines "**investment income"** as *"income derived from investment of shareholders' funds".*

A new subsection 16(12) was also introduced into the Act which prescribes 0.5% of **gross income** as minimum tax for a life insurance business.

3.1 Gross Income

Section 16(13) of CITA as amended by the Finance Act 2020 defines gross income as "total income earned by a life insurance business including all investment income (excluding franked investment income), fees, commission and income from other assets but excluding premiums received and claims by re-insurers".

For the purpose of the above provisions, other deductions besides frank investment income, premiums received and claims paid by re-insurers shall not be allowed as a deduction against gross income.

NOTE:
Only dividend that has suffered Withholding Tax (WHT) shall be allowed as a deduction against gross income for the computation of minimum tax. As such, evidence of WHT suffered is a condition to be met before treating dividend income as Franked Investment Income for the purpose of minimum tax computation.

3.2 Format for Life Insurance Business Tax Computation

Based on the new provisions introduced in the amendment, this format may be used as a guide for the computation of CIT payable by Life Insurance Business.

NOTE:
Any income earned that is not attributed to life business shall be subject to tax under non-life business.

		₦	₦
INVESTMENT INCOME (LESS FRANKED INVESTMENT INCOME)			**XXXXXXX**
ADD:			
FEES AND COMMISSION INCOME		XXXX	
DIVIDEND DISTRIBUTION FROM ACTURIAL REVALUATION		XXXX	
ANY OTHER INCOME		XXXX	XXXXX
GROSS INCOME			**XXXXXXX**
LESS:			
GENERAL RESERVE FUND:		XXXXX	
SPECIAL RESERVE FUND – THE HIGHER OF:		-	
1% OF GROSS PREMIUM	XXXXX	-	
10% OF TOTAL PROFIT	XXXXX	XXXXX	
TAX ALLOWABLE NORMAL BUSINESS OUTGOINGS		XXXXX	(XXXXX)
			(XXXXX)
ASSESSABLE PROFIT			**XXXXXX**
ADD BALANCING CHARGE			XXXXX
LESS: CAPITAL ALLOWANCES			(XXXXX)
TOTAL PROFITS			XXXXXXX

COMPANIES INCOME TAX @ 30% OF TOTAL PROFIT (A)		**XXXXXXX**
MINIMUM TAX @ 0.5% OF GROSS INCOME (B)		**XXXXXXX**
COMPANIES INCOME TAX IS THE HIGHER OF (A) and (B)		**XXXXXXX**

4.0 Amendment or Revision of the Circular

The Service may, at any time, withdraw or replace this Circular or publish an amended or updated version.

5.0 Enquiries

Any request for further information or clarifications on this Information Circular should be directed to the:

Executive Chairman,
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Revenue House,
15, Sokode Crescent,
Wuse Zone 5, Abuja.

Or

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