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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
- Hunker, H.L. and A.J. Wright (1963), "Factors of Industrial Location in Ohio" Ohio State University, Nigeria.

**CONTRIBUTIONS TO BOOKS**

- Sharma T., Kwatra, G. (2008) Effectiveness of Social Advertising: A Study of Selected Campaigns, Corporate Social Responsibility, Edited by David Crowther & Nicholas Capaldi, Ashgate Research Companion to Corporate Social Responsibility, Chapter 15, pp 287-303.

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- Schemenner, R.W., Huber, J.C. and Cook, R.L. (1987), "Geographic Differences and the Location of New Manufacturing Facilities," Journal of Urban Economics, Vol. 21, No. 1, pp. 83-104.

**CONFERENCE PAPERS**

- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–23

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- Kumar S. (2011): "Customer Value: A Comparative Study of Rural and Urban Customers," Thesis, Kurukshetra University, Kurukshetra.

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# ASSESSMENT OF TAX IMPLICATION ON MERGER AND ACQUISITION IN NIGERIA

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**ABSTRACT**

*This paper intends to assess the tax implication on merger and acquisition. Merger is the coming together of two or more entities. Merger and acquisition could be used interchangeably. Acquisition arises when an entity takes over another entity. The global economic distress forced some corporate organizations to naturally die as many were unable to fulfill their obligations to various stakeholders. Many organizations adopted merger and acquisition options without taking cognizance to the impact of taxation on such schemes. In lieu of this, the paper showcases various tax effects and provisions relating to merger and acquisition in Nigeria. The author appraises existing journals as a secondary source of information. Before the merger and acquisition it is statutorily mandatory for consolidating entities to seek for the approval from the Federal Inland Revenue Service. It has been observed that many consolidated organizations failed to consult tax authority for approval and many tax advantages that ought to have enjoyed eluded such organizations. It concluded that there is a tax impact on merger and acquisition and the organizations were not taken advantage of the tax incentives underlining the schemes.*

**KEYWORDS**
merger, acquisition, tax legislation.

## INTRODUCTION

Merger and acquisitions are used interchangeably. The term merger is the joining or coming together of two or more companies to form a larger company that can face the global economic challenges. Merger is defined as any amalgamation of an undertaking or any part of the undertaking or interest of two or companies or the undertaking (FIRS, 2006). Merger and acquisition provides many advantages to the entity concerned like technology, finance and many more benefit to be derived. Acquisition however is different from merger as it is viewed a scenario where an entity buy over another entity. Balogun (1999) defined merger as a situation where two or more companies appropriately of the same size come together with the shareholders and directors of all the companies supporting the combination and continuing to have an interest in the combined business. According Akinsulire (2014), he used the word consolidation for both the two concept. he further defined consolidation as the joining of two or more companies, generally of equal size and market power, to form an entirely new entity. Merger is a scheme adopted by entities to achieve synergy. Kusum (2014), viewed merger as unification of two entities into single entity while he opined that acquisition is when an entity takes over another entity and absorbs the same.

There are various reasons for merger and acquisition entities in Nigeria. Foreign investors see it as an avenue to gain entrance into Nigerian capital market. Acquisition provides access to existing structures, possibly with any required permits and assets in place. Entity may equally merge to increase market share through merging with or buying smaller rivals. Merger and acquisition is another way of making an entity to remain in the market.

There are many tax consequences as many entities come together to form a single entity. Such consequences ranging from cost cutting, tax advantage, formation of synergies and lager market participation etc. The Federal Inland Revenue service in 2006 sanctioned about seven banks for neglecting their legal obligation relating to tax on mergers and acquisition. The tax implications still vary from various types of strategies adopted for the M&A. The buyers and sellers perspective with reference to neutrality of tax should be properly dealt with in the subject matter concerned. According to Kumu (2014), opined that the tax law starts from the transfer of assets during amalgamation of the companies. He furthered cited the stand of the Indian tax law on the merger and acquisition to start from the capital gains tax. In Nigeria, before consolidation of two or more entities there must be approval from the various regulatory bodies, such regulatory bodies are: security and exchange commission, Federal Inland Revenue service, corporate affairs commission, Nigerian stock exchange and federal high court.

The area of concerned in this paper is the various provisions available to entities that adopt option of merger and acquisition.

The implication of merger and acquisition start from the approval of merger and acquisition by the Federal Inland Revenue Service. The Company Income Tax Act in Section 29(12) Cap 21, LFN, 2004 provides that “no merger, take-over, transfer or restructuring of the trade or business carried on by a company shall take place without having obtained the Service’s direction under sub-section 9 of this section and clearance with respect to any tax that may be due and payable under the Capital Gains Tax Act”. The implication of this provision is that the approval of the Federal Inland Revenue Service is a necessary condition for the completion of the process in a merger or acquisition bid. Therefore, no merger or acquisition bids would be fully consummated without the companies involved having obtained consent from the FIRS. This is also applicable the entities in the case of the demerger.

## LITERATURE REVIEW

Merger and acquisition are global business term used to achieve growth and survival of entities. Merger entails coming together two or more firms to become a bigger firm while acquisition is the taking of a small by a big firm which are both pursuing similar motive (Amedu, 2004; Bello, 2004; Katty, 2004). According to Soludo (2002) opined that the mergers and acquisitions are aimed at achieving cost effectiveness through economies of large scale and diversification and expansion of business activities to improve performance. Thomas (2013) opined that mergers and acquisition take place primarily to take ownership advantage. Ownership advantages emanate when a change in ownership of a target company is expected to provide a source of value creation either by increase the target company cash flow or decrease the risk. The potential of tax management has been totally ignored. There is a tax advantage that can be taken by the acquiring entity that will definitely increase the cash flow ( Martynova and Renneboog, 2008).

Decreasing the tax burden of the target firm is an important way the acquiring firm can generate ownership advantage. It was discovered that both predator and the target companies do focus their interest on the cost effectiveness of the economies of large rather than the tax advantage imbided in mergers and acquisition. Though, mergers and acquisitions are recent phenomenon in Nigeria. The provision has not been really made in the confine of the tax law. Consolidation activity has so much increase in the recent time in Nigeria. Consolidated entities are being compelled to comply with the available provision within the confine of the Company Income Tax Act. Osayaba and Oluwole (2012) concluded that tax legislation has not been made to cater for the merger and acquisition. Kusum (2014) suggested that legislation start from capital transfer which has been catered for under the Capital Gains Transfer Act of the tax legislation with reference to Indian Tax Legislation. Swiss tax system and switcherland's extensive network of tax treaties offer attractive structure for merger and acquisition. For example in Switzerland, individuals holding their shares as private assets benefit tax exeption from capital gain tax when selling their shares but dividends income is subject to tax (KPMG International,2014). In contrary to the above contributors, FIRS in its information circular issued in 2006 made it clear under CITA provision that no entities should merged without the prior approval from the Service.

## METHODOLOGY

Desk research has been followed to complete this paper. The author exploited the existing journal and articles written by various contributors in the subject matter concerned. The author also used applies research in line with the desk research via internal. The researcher sought for materials and published articles on the internet. Reference was also made to newspapers and circulars from the Federal Inland revenue Service.

## THEORETICAL FRAMEWORKS

The most efficient two theories of mergers and acquisitions are synergetic and disciplinary theories propounded by Manne (1965); Mead (1968) and Jensen, (1988) which was termed as efficiency theory of mergers and acquisitions. Synergetic merger theory holds that firm managers achieve efficiency gains by combining an efficient target with their businesses and then improve the target performance. Disciplinary theory opined that merger and acquisition disciplined the target firms' managers who pursue the objectives other than profit maximization. Another theory supporting mergers and acquisitions is that empire- building which was propounded by Baumol (1967) and later developed by Mueller in 1969. Baumol and Mueller opined that the mergers and acquisitions were schemes used to build business empire. Non of the theorist stated above had not viewed tax implication on mergers and acquisition. In order to make this piece effective the writer adopted synergizing theory to support this write up. There are a lot of tax incentives that can be claimed by both the acquired and the acquiring companies. It is suggested that through the synergy of mergers and acquisitions both the prey and predator companies can effective reduced their tax burden. Kumu (2014), suggested that the combining firms may also facilitate more efficient behavior on their own part by reducing their taxes. Through merger and acquisition an entity could effectively reduce their tax liabilities and then increase firm incentive to invest in another business.

## EMPIRICAL REVIEW

Merger and acquisition could be used interchangeably. Merger is simply coming together of two more entity form a single entity. Acquisition is a situation whereby an entity absorbed another entity to form a bigger entity which could stand the challenges in the market. Acquisition is the take- over of one entity by one company of sufficient share in another company to give the acquiring company the control over the acquired entity (FIRS, 2006). Consolidation could also be used to refer to scheme of merger and combination. Essence of merger ranges from one entity to another which may be synergy. The reason is best known to the entities concerned. Synergy is the working together of two or more organizations especially when the result is greater than the sum of their individual effects or capabilities.

## TYPES OF MERGER AND ACQUISITION SCHEME

Acquisition could be coming together of companies but different stages in the process of producing and selling of products in the industry, this is referred to as vertical acquisition. It could involve combination of two or more in the same level in the industry; this is referred to as horizontal integration. Organizations in different lines of business could come together to form a business empire this is often called conglomerate merger.

## REASONS FOR MERGER AND ACQUISITION

There are various reasons why entities merged. These reasons are determined by various challenges rocking such entities. Many foreign investors see merger and acquisition as an avenue to gain an entry in to Nigeria capital market. Another reason may be to increase the market share of the entity this was in the case of many banks in Nigeria. For example United Bank for Africa and Standard Bank Plc in 2006 merged and became a major key player in the banking industries. Surviving entities may also adopt merger and acquisition scheme to remain in the market. Many banks in Nigeria adopted this method in order not to be push out of the industry. Merger and acquisition could used to build Business Empire. In respectful of various reasons for amalgamations it is pertinent to know the impact tax on the activities. Kumu (2014), suggested that whether the tax incentives encourage merger activities is important to know their implication on merger activities. He furthered juxtaposed that tax impact on the properly structuring of the disposition and acquisition of company can have impart on the economic transaction of both parties.

### TAX IMPLICATION

There various regulatory authorities involved in the merger and acquisition. Business combinations are always subject to the approval of Securities and Exchange Commission. According to Investment and Security Acts, 2007, entities must seek for the approval of SEC before such scheme could be adopted. Registered companies are subject to the authority of Corporate Affairs Commission in respect of all entities operations. Federal Inland Revenue Service comes in the aspect of the taxation. The commercial activities involved in the scheme of M& A make the tax consideration to be difficult. Even though the tax implication has the advantage and disadvantage, but the entities are expected to allow tax to have effect on various transactions taken place during merger and acquisition.

From the start, the merging companies are required to submit to the FIRS, copies of the scheme of merger and acquisition scheme of arrangement on the consolidation request for its study and proper evaluation in order to ensure that taxes which may result from the companies' transactions are correctly assessed and collected. Herein lies the relevance of the Service's powers under section 29(9) (i) to require either of the companies directly affected by any direction which is under the consideration of the Service to guarantee or give security to its satisfaction for payment in full of all tax due or to become due by the company which is selling or transferring such asset or business.

Among the procedures to be followed in merger and acquisition is the approval from the FIRS. The implication could be viewed in three major headings: The formation of new company and cessation of the acquired.

### COMMENCEMENT OF NEW COMPANY

Merger and acquisition mark an end of merged entities and a new company emerges. The commencement is applicable to the new company. New entity is expected to file a return to the Federal Inland Revenue Service. This return must be filed within eighteen months of the incorporation or six months after the first accounting year. Section 29(3) recommended whichever is earlier for the filing of the audited financial statement.

Basis of assessment of the new entity will be: for the first year of assessment, the basic period start from the date the new entity commenced to 31st December of the same year, the following year of assessment shall be from the date of commencement till twelve months calendar. The third year of assessment shall be base on preceding year basis. There is also right of election that could be exercised by the new company base on the effective tax planning.

There are circumstances whereby the company's Board of Directors may set aside the commencement rule. Firstly, if the merged parties are connected persons and the new entity could be presented as an on-going business. Lastly where the new company is reconstituted business the company may set aside the commencement rule.

Company Income Tax Act does not specify whether there is a capital allowance claimable. Since the assets are transferred based on the carrying amount not at fair value it is assumed that there is no capital allowance that can be claimed by the new company but could claim the annual allowance on the tax written down value of the assets transferred.
Likewise the new company may acquired losses, this has been permitted by the Act to be absorbed into the new entities.

**CESSATION OF THE OLD BUSINESSES**

The merger and acquisition lead to cessation merged parties. The cessation rule is applicable to the ceased entities unless the entities are connected and where the company is reconstituted to take over a particular trade. The capital gains arising from the disposal of shares during merger has been exempted from the capital gain tax unless the shareholders are paid in cash.(Capital Gains Tax Act,2004, S.32A).
Taxes and Deductibility of Related Expenses Stamp Duties
Duty payment will arise on the share capital of the new company, subject to the provisions of Section 104 of the Stamp Duties Act, in relation to capital and duty relief.

**CONSOLIDATED EXPENSES**

Fees paid to statutory bodies such as SEC, NSE, CBN, Land Authorities etc, including professionals like accountants, stockbrokers, issuing houses, and solicitors are regarded as capital in nature and will therefore not be allowed as deductible expenses by virtue of Section 27(a) of CITA.

**TAXATION OF CONSOLIDATION FEES**

Fees paid to professionals for services rendered in connection with consolidation will be subject to VAT and WHT at the rates of 5% and 10% respectively.

**TAX INDEMNIFICATION**

Section 29(9)(i) of CITA provides that the Service may require the new company to guarantee or give security for payment in full, for any tax due or that may become due by any of the ceased companies.
Approval for Pension Scheme The new company will need to obtain a Joint Tax Board (JTB) approval for its staff pension scheme.

**STATUS OF A SURVIVING COMPANY IN RELATION TO TAXATION**

It is a possibility that one of the merging companies survives and its old name or a new name to inherit the assets, liabilities, reserves and entire operations of the merging parties. Where this happens, the following points must be noted:
The surviving company must file its returns in line with the provisions of section 55(3)(a) of CITA. Commencement rules under section 29(3) of CITA will not apply to the surviving company, as it will be regarded as an existing company.
The surviving company will not be allowed to claim investment allowance on the assets which were transferred to it and will also not claim initial allowance on such assets.
The surviving company may however claim annual allowance only on the tax written down Values (TWDV) of the assets transferred to it. The surviving company may not inherit the unabsorbed losses and capital allowances of the merging companies, except it is proved that the new business is a reconstituted company. All fees payable on merger bids or consolidation will be liable to VAT and WHT just like it is applicable on the emergence of a new company. Stamp duties will be paid on the increase in share capital and the company will have to obtain its own staff pension scheme approval from the JTB.

## TAX IMPLICATION TO SHAREHOLDERS OF THE MERGED ENTITY

Shareholders of the merged companies are assessable to tax incentives for selling their share or investment. The receipts from the disposal of their investments could be taxable and non taxable. If they are taxable the shareholders are expected to pay capital gain tax to the relevant tax authority. Allotment of shares by the merging company to the shareholders are often exempted from take . Kumu (2014) opined that there is an argument on whether there is going to be imposition of tax on the shares allotted to the shareholders. This will be determined by the tax legislation relating to the merger and acquisition in each country. According to Company Income Tax Act Section 25(9), if the shares are transferred with the payment of full amount to the transferor then capital gain tax will be levied on the gain arising from the transfer. Asset may also be transferred once the full amount has been paid by the merged to the acquired companies, the gain arises should be charged under Capital Gain Tax Act. However, S.32 of the Capital Gain tax Act, 2004, provides that person shall not be chargeable under capital gain tax Act in respect of any gain arising from the transferring of shares
Capital allowance could also be claimed on the asset transferred to the new company. Company Income Tax Act do not made provision for the capital allowance on merger and acquisition. International Accounting Standard 22, provide that the assets, liabilities and reserves must be recorded at their carrying balances, implying that merger does not permit asset to be written down in their fair value at consolidation. The new company will therefore be entitled to claim initial allowance and annual allowance is claimable on the tax written down value.
Losses could be absorbed by the new company if it can be proved that the new company carries on the same business and losses incurred have not be absorbed by the new company. These could carry forward and set off against the income of the entity concerned in future.
It is also required for the stamp duty to be raised if the new entity issue new shares. According to stamp duty Act, 2004 Section 104, the duty share be paid on new shares issued by the new company.

## DISCUSSION

It was discovered that there is no specific provision for mergers and acquisitions scheme. Various provisions made were either under the Capital Gain Tax Act and other related tax laws. This was furthered found by the various contributors to tax implications of merger and acquisition. Many entities involved in the scheme did not even aware of the tax advantage of the scheme. Many were even sanctioned before they were compelled to seek for the approval of the tax authority. If the approval stage is really observed by the entities involved in mergers' scheme they would have saved the extra cost from court cases for failing to comply with provision of the tax law.

## RECOMMENDATIONS

This paper suggests that the Federal Inland Revenue Service through its board enacts a tax legislation that would be specific and applied on the scheme. Such legislation should be published in the national dailies. This will serve as awareness to all entities that would be found in such scheme in future. The demerger scheme will soon be taken place as many would be recovering from the global economic distress, therefore adequate and proper tax legislation should be made available for this future scheme.

## CONCLUSION

The Federal Inland Revenue Service should enforce tax issue from the start of the scheme as many approving organizations could not be escaped. Tax issues have major impact on the successful completion of merger and acquisition schemes, post integration. Early involvement and development of a tax efficient plan will maximize the return on the arrangement. Tax legislation could be simplified and rationalized in respect merger and acquisition as found that complexity of the tax effect could lead to tax evasion.

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