A Review of Central Bank of Nigeria's Guidelines on Shared Services Arrangements

Background

The increased presence of Multinational Enterprises (MNEs) across various jurisdictions has, among other things, created the need to centralise certain functions within the MNE Group. Many MNEs have adopted a shared services arrangement to centrally provide certain business support services to members of the group. Such shared services arrangements typically include services such as accounting, finance, procurement, Human Resources (HR), Information Technology (IT), Legal etc. The reasons for such arrangements are not far-fetched.

Adopting a shared services arrangement enables MNEs to achieve cost efficiency, improve their processes and leverage existing expertise. Another reason for such arrangements by MNEs may be the need to ensure uniformity/standardisation of their business processes, especially for MNEs with a global brand. Shared services arrangements are mostly common between related parties.

Therefore, it is important for shared services to be conducted in line with the arm's length principle, and the charge for such services allow for the appropriate allocation of profit among various jurisdictions.

Overview of the Guidelines and Approved Services

In May 2021, the Central Bank of Nigeria (CBN) issued Guidelines on the operations of shared service arrangements between banks and other financial institutions in Nigeria and their parent company or group members ("the Guidelines"). The introduction of the Guidelines was informed by the apex institution's concerns on governance, financial and tax management practices related to shared services.

This article reviews the Guidelines, highlights the compliance requirements and the implications of the Guidelines for Banks and other financial institutions.

The Guidelines were introduced to set a supervisory expectation concerning shared service arrangements, ensure that fees charged under such arrangements are reflective of the services rendered, ensure compliance with the Transfer Pricing (TP) Regulations in Nigeria, and reduce operational costs of recipients of those services.

The Guidelines, which has an effective date for full compliance of 1 June 2022, applies to:

- Commercial banks
- Merchant banks
- Financial holding companies
- Other financial institutions
- Payment services banks, and
- Other payment services providers licensed by the CBN

The Guidelines provide a list of approved services that banks and other financial institutions can engage in under a shared service arrangement. Such services include HR, risk management, internal control, compliance, marketing and corporate communications, IT, legal, facilities, and any other services that may be approved by the CBN from time to time.

The Compliance Requirements

1. Establish Policies and Procedures for Shared Services

   Financial institutions are expected to establish policies and procedures to ensure that shared services arrangements are conducted in a manner consistent with the arm's length principle. This policy is to be approved by the board of the financial institution, reviewed annually, and submitted to the CBN.

   The policy should include, at a minimum, specific information such as details of the services to be shared, how the services would be shared, including the roles and responsibilities of the parties involved, methodology for pricing the services and the governance structure for reporting exceptions to the policy.

2. Prepare a Shared Services Agreement

   The financial institution should enter into a shared services agreement with the provider of the shared services. This agreement should state the terms and conditions of service, including duration. Fees, a

clause requiring parties to adopt the recommendations arising from the review by the independent consultant, Transfer Pricing methodology used to analyse the arrangement, etc. This agreement is to be reviewed yearly to reflect current economic realities and submitted to the CBN for approval.

The board of the financial institution is responsible for the oversight of the arrangement and may delegate the responsibility of monitoring and managing the shared services to a board committee, which should be headed by an independent director.

3. Appoint an Independent Consultant

The board of the company is required to commission an independent consultant to determine the efficiency of the shared service arrangement on an annual basis. The report from the independent consultant, which should show the extent of compliance with extant laws and regulations, should be submitted to the CBN annually, not later than 31 January of the relevant financial year.

4. Disclosure in Annual Report

Financial institutions are to disclose in their market reports and website, the shared services within the group, and their importance to their institutions.

5. Compliance with TP Regulations

Financial institutions are required to comply with the provisions of the income tax (Transfer Pricing) Regulations, 2018, particularly concerning the methodology used to analyse the arrangement.

6. Maintain Relevant Documents

Financial institutions are required to keep all necessary documents required to demonstrate that the shared services arrangement has been conducted in a manner similar to that of independent parties, and the fee charged is at arm's length. Such documents could be in form of journals, ledger, contracts, invoices, bills.

All financial institutions are expected to comply with the guidelines. Failure to do so is punishable under sections 95 and 96 of the Banks and other financial institutions Act, 2020 (BOFIA). Officers of non-compliant companies may be liable to administrative sanctions.

Commentaries

✓ Increased Compliance Requirements

The introduction of the guidelines increases the compliance requirements for financial institutions in Nigeria. Financial Institutions need to be aware of the various compliance obligations and the board's role in ensuring compliance and engaging independent consultants to aid compliance. Increased compliance requirements may result in increased compliance costs.

✓ Link with the TP Regulations

It is noteworthy that the Guidelines makes specific reference to the TP Regulations. The guidelines do not contradict but complement the provisions of the TP Regulations by focusing on the arm's length principle and referencing the TP methods in the TP Regulations. As such, the treatment of the shared services should be in line with the provisions of the Regulations 6 of the TP Regulations and Chapter 7 of the OECD Guidelines

✓ Cooperation Among Government Agencies

The link between the guidelines and the TP Regulations is a welcome development as it indicates cooperation between the CBN and the Federal Inland Revenue Services (FIRS). This type of cooperation among government agencies should be encouraged to ensure consistency when treating TP issues.

For example, where the FIRS, the Nigeria Customs Service or the National Office for Technology Acquisition and Promotion use different methods to determine the pricing of related party transactions, this can lead to double taxation, which is detrimental to the business operations of taxpayers especially manufacturing companies. Where the government agencies work together to determine uniform approaches to analysing similar transactions, it provides comfort to taxpayers by providing certainty in

the treatment of related party transactions and reduces the risk of double taxation risks.

- ✓ Provision of Approved Services

  The guidelines state that the approved services can be provided under a shared services agreement where the recipient entity does not have the expertise and capacity to carry out these services. It should be noted that in practice, companies enter into shared services arrangements due to the benefits of centrally providing services, not necessarily due to a lack of capacity in the local entity. However, it is important that there is no duplication of services where similar services are provided centrally and locally.

Conclusion

With the introduction of the guidelines by the CBN, Nigeria has taken yet another step towards ensuring compliance with the arm's length principle and with a view to enlarge the country's tax base. As such, affected taxpayers should evaluate their shared services arrangement in light of the Guidelines and proactively work with independent consultants to avoid undue regulatory risks and sanctions by the CBN.

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