

A magnifying glass with a black handle and frame is positioned over a small, white, torn-edged piece of paper. The paper has the words "Windfall Profits" written on it in a black, handwritten-style font. The background is a light green color with numerous green banknotes scattered around, some appearing to be falling or floating. The overall theme is financial and related to unexpected gains.

Windfall  
Profits

**Banking Sector Update:  
Taxing Times, Windfall Worries**

The Nigerian government has recently proposed a windfall tax targeting banks' foreign exchange gains, initially set at 50% but now increased to 70% following amendments by the Senate. This tax will be applied retrospectively to profits realised in 2023FY and will extend to all foreign exchange profits accrued from the implementation of the new forex policy until the end of 2025FY.

The Federal Inland Revenue Service (FIRS) will oversee the assessment, collection, and enforcement of this levy, allowing banks to enter into deferred payment agreements with an option to settle the tax in installment. However, banks that default on these payments will incur a penal charge of 10%p.a on unpaid taxes, in addition to interest at the prevailing CBN minimum rediscount rate.

## Our Thoughts:

In 2023, the 48.76% devaluation of the Naira, coupled with the unification of foreign exchange windows, yielded substantial unrealised revaluation gains for Nigerian banks. This positively impacted their operating income and profitability, primarily due to their sizable holdings of foreign exchange assets.

However, we suspect that the proposed windfall tax was pre-meditated, as evidenced by the CBN's earlier directive to deposit money banks to retain

revaluation gains in their reserves rather than distributing them as dividends, suggesting that the CBN had already planned to tap into these gains.

Furthermore, it is worth noting that at the onset of the recapitalisation exercise, the CBN mandated fresh capital raises, prohibiting the use of retained earnings. This suggests that the windfall tax may be a deliberate attempt to capture the benefits of the revaluation gains.

We believe that the steep hike in the windfall tax imposes a substantial financial strain on banks, effectively amounting to double taxation when combined with the existing 30% corporate income tax. This dual taxation threatens to significantly erode banks' profitability, hindering their capacity to reinvest in operations and potentially leading to a credit crunch especially coming at a time when banks are racing to raise capital.

The retroactive imposition of taxes on Nigerian banks in July, seven months into the new financial year, raises concerns about regulatory unpredictability. This comes after banks have already completed their financial year (Jan-Dec), undergone audits, and paid taxes. The sudden and unexpected application of taxes may have far-reaching consequences, potentially deterring

both local and international investors from investing in the banking sector.

Nigeria's fiscal challenges are longstanding, and the government is seeking different means to plug the revenue shortfall, given the country's alarmingly low tax-to-GDP ratio of 11%. However, the latest amendments to the Finance Act have introduced ambiguity around the treatment of revaluation reserves, potentially raising concerns about the government's plans to fund its NGN6.20trn supplementary budget. The uncertainty is exacerbated by the fact that the revaluation gains reported by listed Nigerian banks in 2023FY only totals NGN475.90bn, with most of these gains remaining unrealised.

This uncertainty casts doubt on the availability of the necessary cash to support the government's funding plans.

The windfall tax extension to 2025 sparks debate about its long-term viability and potential entrenchment. In conjunction with the CBN's recent regulatory overhaul, this move may compel banks to reexamine their business models. Meanwhile, investor confidence has been shaken, with major banking stocks experiencing losses despite recent capital infusions.

**Table: Revaluation Gains of Nigerian Banks in 2023FY (NGN'bn)**

	2022FY	2023FY	Applicable tax (70%)
ACCESSCORP	-31.83	17.25	12.08
ETI	10.41	-45.95	-
FBNH	9.11	-341.56	-
FCMB	4.30	83.96	58.77
FIDELITYBK	2.68	44.09	30.86
GTCO	57.94	441.79	309.25
JAIZBANK	-0.14	0.06	0.04
STANBIC	0.19	7.10	4.96
UBA	5.74	26.58	18.61
WEMABANK	1.59	13.60	9.52
ZENITHBANK	25.20	228.98	160.28

Source: **Bank Financials, Meristem Research**

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