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KEY HIGHLIGHTS OF THE CBN GUIDELINES ON SHARED SERVICES ARRANGEMENTS FOR BANKS AND OTHER FINANCIAL INSTITUTIONS IN NIGERIA.

Introduction

The Central Bank of Nigeria (the CBN) released an Exposure Draft on Shared Services Arrangements in November 18, 2019 for stakeholders' comments before the final release of the guidelines. The Exposure Draft was issued in response to the absence of standard on shared services and transfer pricing arrangements in the Nigerian Banking industry.

The Central Bank of Nigeria (the CBN) has now issued the Guidelines for Shared Services Arrangements (The Guideline) for Banks and Other Financial Institutions in Nigeria dated May 26, 2021 in exercise of its powers under the Central Bank of Nigeria Act, 2007 (CBN Act) and the Banks and Other Financial Institutions Act, 2020 (BOFIA).

The Guideline has been issued as part of the CBN's intervention to streamline the activities of institutions engaged in shared services and transfer pricing. The Guideline in addition to the CBN's Guidelines for Licensing and Regulation of Financial Holding Companies in Nigeria, will guide Nigerian banks with foreign parents and banks within the non-operating financial holding companies (HoldCos) and other entities in the group on the initiation and evaluation of shared service arrangements and other matters connected thereto. The Guideline sets the operational standards for banks and other financial institutions in line with best practice and ensures compliance with Executive Order 5 of the Federal Government of Nigeria, signed on February 12, 2018, which seeks to promote the development of indigenous capacity and local

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content in contracts and science, engineering and technology, as a necessary tool to drive national competitiveness and productivity.

This article highlights the key provisions of the Guidelines on Shared Services Arrangements vis-à-vis applicability to the operations of financial institutions in Nigeria.

KEY PROVISIONS OF THE GUIDELINES

The Guideline covers the general principles that guide shared services arrangements in Nigeria, approved shared services, transfer pricing and regulatory reporting requirements in Nigeria's financial services industry.

General Principles, Scope and Objectives

The provisions of the Guideline is applicable to commercial banks, merchant banks, financial holding companies, other financial institutions, payment service banks and other payment services that are either a parent company operating in Nigeria and licensed by the CBN or a subsidiary company licensed by the CBN and carrying its operation in Nigeria. The above listed financial institutions are expected to establish policies and procedures to ensure that shared services are conducted at arm's length. They are also expected to submit their shared services policies as approved by the board to the Central Bank of Nigeria. The approved policies must detail the services to be shared, indicate how the services would be shared including the roles and responsibilities of the parties involved, indicate the methodology for pricing shared services including standards for timely recording and settlement, and specify the governance structure for reporting exceptions to policy.

The objectives of the Guidelines include setting out supervisory expectation in respect of shared services arrangements between a parent company and its subsidiary, ensuring that the fees received or paid reflect the services rendered taking into account the assets used and the risks assumed, ensuring that financial institutions comply with the extant transfer pricing regulation in Nigeria, and reducing operational cost of benefitting institutions.

Approved Services

The Guidelines will have significant impact on shared service structure of foreign owned institutions, transfer pricing and taxation coupled with certain key governance obligations to the institution. The Guideline specifically identifies the types of shared services that can be undertaken by the financial institutions subject to the approval of the CBN.

Under the Guidelines, a financial institution may enter into Shared Services Agreement with its parent company in respect of

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1. Human Resources services;
2. Risk Management services;
3. Internal Control services;
4. Compliance services;
5. Marketing and Corporate communications;
6. Information and Communication Technology;
7. Legal services;
8. Facilities (Office Accommodation including Electricity, Security, Cleaning Services in that accommodation); and
9. Any other services as may be approved by the CBN from time to time.

The Guideline also imposes another requirement on the sharing of the services listed above, specifically, the services can only be shared where the recipient entity does not have the expertise and capacity to carry out the aforementioned shared services. Also, any other services provided outside the scope of the shared services as detailed under the Guideline shall not be charged to the recipient entity.

Furthermore, the Guideline makes provision for financial institutions seeking to acquire technology on behalf of their foreign subsidiaries. In this instance, such associated cost shall be allocated based on the actual volume and complexity of services consumed by the subsidiary. This provision is however, subject to the local regulation of the host country. In the case of foreign companies transferring technology to the local financial institutions, the Guideline stipulates that such technology transfer agreements must expressly convey the beneficial rights for the use of the technology.

Governance Obligations

Under the Guideline, the board of directors of the relevant financial institutions have obligations to ensure that all approved shared services agreements are in line with extant laws and regulations. Additionally the board must perform the following;

1. Ensure approval of Shared Services Agreements by the CBN;
2. Set performance goals and metrics including viability of a shared service;
3. Commission an independent firm to determine the efficiency of the Shared Service Arrangements or significant deviation from the arrangement;
4. Ensure transparency and disclosure in the viability of the Shared Service Arrangement or significant deviation from the arrangement;
5. Monitor compliance with transfer pricing requirements and documentation;
6. Submit independent firm's validation/review of the fees and services to be rendered to the CBN annually but not later than 31st January of each accounting year;
7. Yearly review of Shared Service Agreement to reflect economic realities ;

Contents of Shared Services Arrangements

A Shared Services Agreements shall be executed between the recipient

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institution and the provider company, and should at the minimum contain commencement clause, agreement to provide services, scope of services, applicable costing methods, compensation and cost sharing, reporting and timing of payments, standards for performance of service, access to employees and information, dispute resolution mechanism/procedure, confidentiality, notices, force majeure, indemnification, duration, termination, governing law, capacity building, and general Provisions.

Transfer Pricing

Generally, the provision of the Federal Inland Revenue Service Income Tax (Transfer Pricing) Regulations, 2018 (the Income tax Regulations) regulates and provides guidance on the treatment of related party transaction. Therefore, both the provider and recipient entities are to comply with the provisions of the Income Tax Regulations.

Specifically, the Guideline provides that the transfer pricing method applied in line with Section 5 of the Income Tax Regulation, shall be considered in the shared services agreement. Accordingly, the permitted transfer pricing methods have been specified as follows;

1. Comparable uncontrolled price method;
2. Resale price method;
3. Cost plus method;
4. Transactional net margin method;
5. Transactional profit split method; and
6. Any other method as may be approved by the CBN.

The Guideline stipulates that shared services shall be documented between the provider and the recipient as if they were unrelated entities. In other words, the terms of the agreement must be such that is consistent with similar agreements concluded between unrelated parties.

Regulatory Reporting

The Guideline requires that the shared services agreement and the report of an independent consultant be submitted to it, for approval. Similarly, all shared services agreement must be reviewed yearly to reflect the current economic realities and be submitted to the CBN.

Compliance

All financial institutions having shared services arrangements within their group shall comply with the provisions of the Guidelines. Failure to comply with the Guidelines is an offence punishable under Section 96 of the BOFIA. Failure to comply with the Guidelines may also render the officers of the concerned financial institution liable to administrative sanctions.

Conclusion

The effective date for the full compliance with the provisions of the Guidelines shall be June 1, 2022. Banks and other Financial Institutions are expected to commence internal review of all their shared services arrangements, and implement arm's length internal policies that align with the requirements of the Guidelines

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