Local content guidelines introduced for the Information and Communications Technology (ICT) sector

May 2014

In brief

The National Information Technology Development Agency (NITDA) recently released guidelines on Nigerian content development in information and communications technology (ICT).

Based on the guidelines, the NITDA will seek to achieve a target of 50% local content in the industry and will require all ICT companies to register Nigerian entities with predominant Nigerian representation. The guidelines are controversial as there is no clear basis in the law for NITDA to impose local content requirements on companies operating in the sector.

In detail

Effective date

The guidelines have a commencement date of 3 December 2013.

Legal basis for the guidelines

The guidelines were issued by NITDA to introduce content requirements for all companies operating in the Nigerian ICT industry and referenced to the powers conferred on it by section 6 of the National Information Technology Development Agency Act of 2007. The release of the guidelines was made public by the Minister of Communication Technology at the e-Nigeria 2013 conference.

The guidelines raise questions on whether NITDA has the powers to introduce local content requirements, tax incentives and minimum capital requirements.

In our view, the powers of NITDA on the above issues are as follows:

- Tax incentives – S.6(g),(h) and (i) allows NITDA to create and introduce tax incentives.
- Minimum capital requirement – S.6(i) allows NITDA to introduce regulatory policies to encourage private sector investment
- Local content requirements – There are no specific provisions to introduce restrictive regulations.

Based on the above, it is not clear whether the powers of NITDA extend to introducing pure local content regulations. However, most of the guidelines that have been introduced do not appear to be restrictive but aimed at encouraging local value creation except the introduction of 51% shareholding for ICT companies which is not clearly defined but appears to include 'Telcos' that provide data and telephony services. In any event, we expect affected operators to challenge any restrictive provisions of the guidelines that may be considered illegitimate.

Focus areas of the guidelines

The guidelines focus on three main areas which are:

- driving indigenous innovation;
- developing the local ICT industry; and
- establishing intellectual property regulation and protection standards.

These focus areas are expected to stimulate the restructuring of the industry, as well as create opportunities for local companies.

The performance of the strategies will be measured against the real economic value contributed by the industry to the Nation's GDP, the number and quality of jobs created within the industry and quality standards among local ICT companies among others.

Impact of the guidelines

The key areas of the ICT business impacted by the guidelines are:

- Minimum capital requirements
- Local content requirements
- Grace period for compliance with regulations
- Various tax incentives
- Purchases by Government Ministries, Departments and Agencies ("MDAs")
- Additional registration and certification requirements

(See enclosed appendix for detailed impact analysis).

Introduction of minimum market capitalisation

The guidelines introduce a minimum share capitalisation for Original Equipment Manufacturers ("OEMs") and Original Design Manufacturers (ODMs) of N2 billion and N5 billion respectively.

Until the release of the guidelines, there was no specific market capitalisation provision for ICT companies in Nigeria other than the capital requirements of the Companies and Allied Matters Act (CAMA).

The requirement to increase the minimum share capital and local content could inhibit the expansion of local businesses or dilution of control as the current owners would have to consider mergers if they cannot raise the required capital alone.

Local content requirements

Generally, the guidelines require all companies operating within the industry to provide a local content plan.

The guidelines provides that OEMs are now expected to maintain at least 50% local content by value either directly or through outsourcing to local manufacturers engaged in any segment of the product value chain. The guidelines sets out a 3-year time frame during which such companies are expected to comply with this requirement.

The guidelines provide that companies under 'ICT services' category should register Nigerian entities for the purpose of providing services in Nigeria. Although ICT services were not defined, reference to ICT services in the guideline excludes (OEMs, ODMs, software developers, network and data management companies and training companies). ICT in this sense may therefore include Telcos (including GSM and CDMA companies). The conditions for use of local SIM cards under this category also suggest that Telcos are the main targets.

The shareholding requirements for the 'Nigerian entity' was not clearly outlined however, it could be inferred based on the definition of 'Nigerian companies' that 51% Nigerian shareholding may be required.

Ban on importation of SIM cards

The guidelines indirectly impose a ban on importation of SIM cards. Telecommunications companies within the industry are expected to use only locally manufactured SIM cards in providing their services and are expected to comply within 18 months of the guidelines coming into effect.

Tax incentives and grants

Some tax incentives were introduced such as:

- 120% tax deduction for R&D expenses incurred by ICT training companies
- 5 years import duty waiver on computer components used for assembly of hardware.
- Possibility for access to grants and seed capital for smaller software companies (potentially from the NITDA fund arising from the 1% of profit before tax being collected from certain companies).

Other provisions

Other provisions of the guidelines include:

- Maintenance of active certification with NITDA by OEMs and ODMs, which are renewable every four years based on specified conditions;
- NITDA's partnership with various global quality controls organisations to assess the quality of ICT products and services offered in Nigeria, as well as provide training to local ICT companies;
- Consideration of all ICT projects as turnkey

deployments rather than mere supply of components;
- design, production, assembly and maintenance of all computer hardware within Nigeria for OEMs and ODMs;
- Sourcing and procurement of all computer hardware by all ministries, departments and agencies of government from only NITDA approved OEMs; and
- NITDA's partnership National Copyright Commission, National Office for Technology Promotion and Acquisition, as well as non-governmental and civil organizations to achieve the harmonization of intellectual property rights. This is expected to provide an incentive for innovation and creativity.

The takeaway

The introduction of the significant share capital requirements for certain types of business in the industry may discourage potential investors, particularly local investors. It will be helpful if the capital requirements are reviewed downwards to facilitate the growth of the industry. Unlike banks where significant capital is required to protect depositors, this is not the case for ICT firms. Many of the global ICT companies today started with barely any capital.

The proposed introduction of 51% Nigerian shareholding has no legal basis and is therefore likely to be challenged.

We expect that NITDA would issue clarification on whether Nigerian entity falls under the same definition of Nigerian companies which requires 51% Nigerian shareholding.

The tax incentives being introduced to the sector should be carefully considered to prevent abuse and to drive the desired outcome. As NITDA is not involved in tax administration, the incentives being granted must be communicated to the different tax authorities including the Federal Inland Revenue Service and the Nigerian Customs Service. NITDA has also not addressed one of its key responsibilities under S.6 of the NITDA Act to introduce special technology parks where operations can be carried out tax-free to stimulate the much needed capacity building for local ICT firms.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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Summary of NITDA Guidelines

Type of ICT company	Original Equipment Manufacturers (OEMs)	Original Design Manufacturers (ODMs)	Independent Software Vendor (ISV)	Software Development Firm (SDF)	ICT Services	Networking companies	Data and Information Management Firms	Human Capital ICT Companies
Description	A firm that makes functional computer devices from component parts bought from other organizations	A firm that produces hardware, which other companies sell under their own brands	Any individual or firm that makes and sells software products that run on one or more computer hardware or operating system platforms	A firm that consists of at least 5 active developers with competencies across popular technologies and platforms	Not defined	Not defined	Not defined	Not defined
Minimum capital requirement	NGN 2 billion	NGN 5 billion	N/A	N/A	N/A	N/A	N/A	N/A
Some local content requirements	- Assemble all hardware within Nigeria and maintain fully staffed facilities for this purpose - Maintain at least 50% local content by value either directly or through outsourcing to local manufacturers - Maintain local R&D facilities - Employ local engineers (not sales people). - Provide a local content plan to NITDA.	- Maintain local capacity to assemble and install minimum of one million devices per annum for multiple form factors - Provide a local content plan to NITDA	- MNCs and their Nigerian subsidiaries are required to submit local content plan as part of requirements for registration within Nigeria and pre-qualification for MDA projects.	- MNCs and their Nigerian subsidiaries are required to submit local content plan as part of requirements for registration within Nigeria and pre-qualification for MDA projects.	- Register as a Nigerian entity (assumed 51% Nigerian shareholding) and submit a local content plan. - Use only locally manufactured SIM cards, host subscriber and consumer data locally. - Use only indigenous companies to build towers with 50% local value add. - Use Nigerian companies (assumed with 51% Nigerian shareholding) for 80% of VAS. - Migrate internet peering t locally available services	- Some requirements have been introduced to protect consumers and content providers.	- Host government data locally within the country and shall not for any reason Host any government data outside the country without an express approval from NITDA and the SGF	- Change from a sales division to carrying out value adding activities in country that contribute to job creation and the empowerment of Nigerians.
Grace period for compliance	2 years grace period to meet certification requirements and 3 years grace period for meeting 50% local value	None specified	None specified	None specified	18 months for SIM card requirements and 3 years for VAT	None specified	18 months to host government data locally.	None specified

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Tax incentives or grants	5 year duty waiver on computer components, which is for integration into locally assembled devices.	5 year duty waiver on computer components, which is for integration into locally assembled devices.	Access to seed capital and grants for start-ups, incubation programs and other forms of government-backed schemes.	Access to seed capital and grants for start-ups, incubation programs and other forms of government-backed schemes.	None specified, but scope introduced for incentives to ICT service providers to develop local content offerings	N/A	N/A	Tax deduction for R&D activities of up to 120% of qualifying expenses.
Some MDA requirements	- Must Source and procure all computer hardware only from NITDA approved OEMs. - Must Purchase all hardware products locally.	- Must Source and procure all computer hardware only from NITDA approved OEMs. - Must Purchase all hardware products locally.	- Source and procure software from only local and indigenous software development companies. - Where there is no local capacity, a Nigerian company (with 51% shareholding) must support the foreign firm.	- Source and procure software from only local and indigenous software development companies. - Where there is no local capacity, a Nigerian company (with 51% shareholding) must support.	N/A	- Source for services from local providers - Host their websites on .gov.ng	- Mandatory system logs for troubleshooting and forensic audits. Insist on hosting all public data locally.	N/A
Some registration/ certification requirements	- Maintain active certification with NITDA, renewable every four years - ISO 14001, ISO 9001, Windows Hardware Certification, Android Compatibility Test Suite (CTS) Certification as well as comply with the Android Compatibility Definition Document (CDD)	- Maintain active certification with NITDA, renewable every four years - ISO 14001, ISO 9001, Windows Hardware Certification, Android Compatibility Test Suite (CTS) Certification as well as comply with the Android Compatibility Definition Document (CDD)	- Indigenous firms are required to register products, capabilities and organisation on the NITDA portal.	- Indigenous firms are required to register products, capabilities and organisation on the NITDA portal. - CMM or ISO 9001 or any other standard certification.	Host their website on .ng	- Hold and maintain ISO/IEC 27001:2005 certification. - Register their products, capabilities and organizations on the NITDA portal	- Hold and maintain ISO/IEC 27001:2005 certification. - Register their products, capabilities and organizations on the NITDA portal	N/A