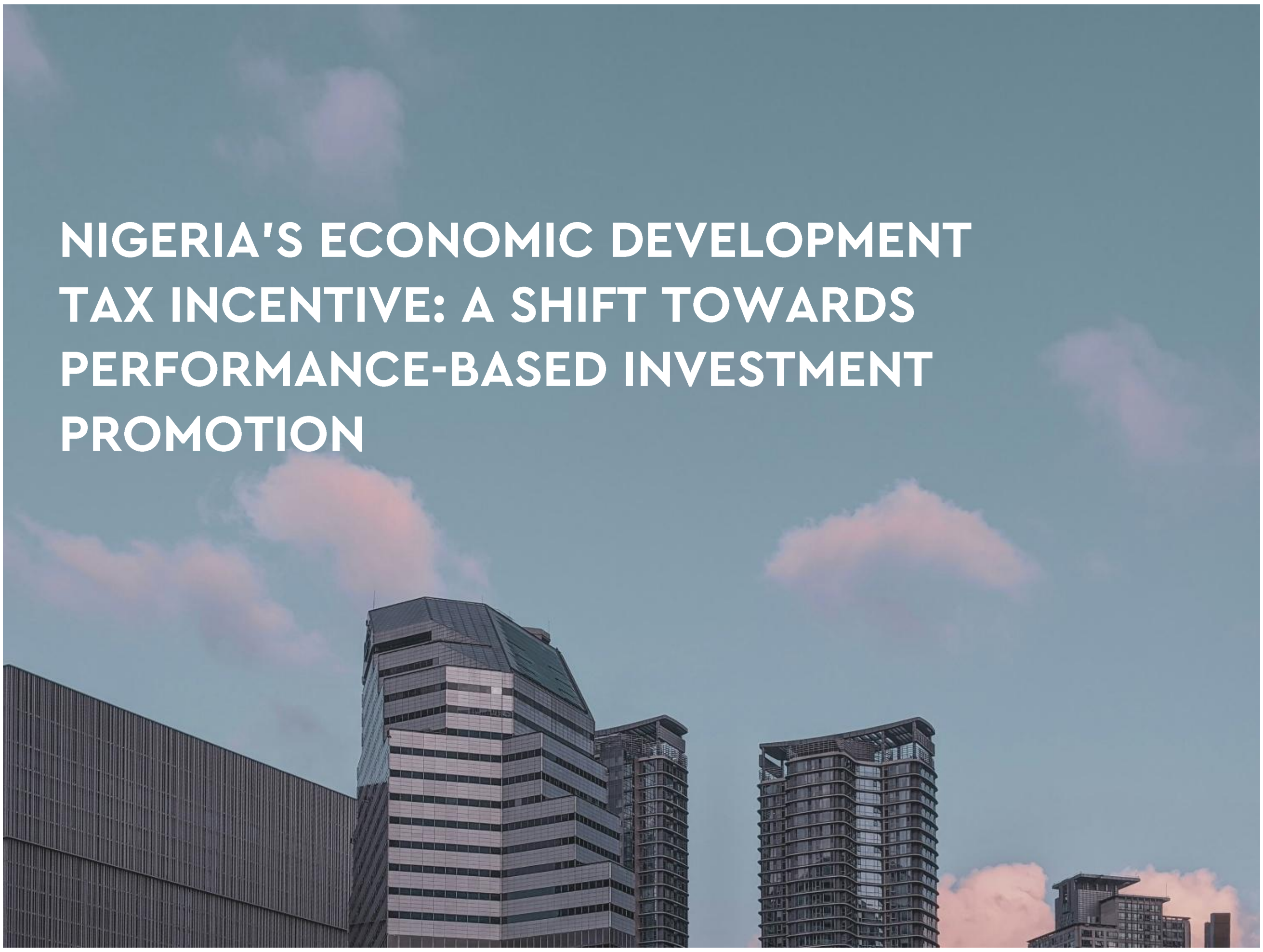


NIGERIA'S ECONOMIC DEVELOPMENT TAX INCENTIVE: A SHIFT TOWARDS PERFORMANCE-BASED INVESTMENT PROMOTION

Introduction

Tax incentives are widely used by governments around the world as a tool to influence economic behaviour and drive development objectives. These incentives can take various forms, including reduced tax rates, tax holidays, accelerated depreciation allowances, or tax credits. The purpose is often to attract foreign direct investment (FDI), stimulate domestic investment, promote economic growth, and diversify the economy.

Nigeria's previous flagship incentive, the Pioneer Status Incentive (PSI), provided an initial tax holiday for three years, with the possibility of a two-year extension from Companies Income Tax (CIT) for approved activities.[1] The PSI's policy motive was to encourage the growth of nascent businesses and start-ups, especially those involved in local raw material development and labor-intensive processing. However, despite its intentions, the Pioneer Status Incentive has faced criticism and challenges. Specifically, the PSI has been associated with issues such as minimal value addition from beneficiary companies, exploitation of loopholes, and a lack of transparency and measurability regarding its actual impact.

Responding to these challenges and as part of a broader tax reform efforts,[2] Nigeria has introduced the Economic Development Incentive (EDI) as a replacement for the PSI. The EDI represents a fundamental shift from a time-based tax holiday to a performance-based system that directly links tax relief to verifiable investments. This new framework is designed to be investment-driven, aiming to address the shortcomings of its predecessor.

Key Feature and Mechanism of the EDI

The Economic Development Tax Incentive (EDI) is a significant innovation introduced by the Nigeria Tax Act (the "Act"), 2025. It is aimed at fostering economic growth and attracting investment in specific areas tagged "priority sectors" like agriculture and food, energy, transportation, health among other sectors with sunset provisions ranging from ten years to twenty years.[3] The President has the power to amend this list, adding sectors that are not operating on a suitable scale or have favourable development prospects, or removing sectors deemed to have become sufficiently developed.

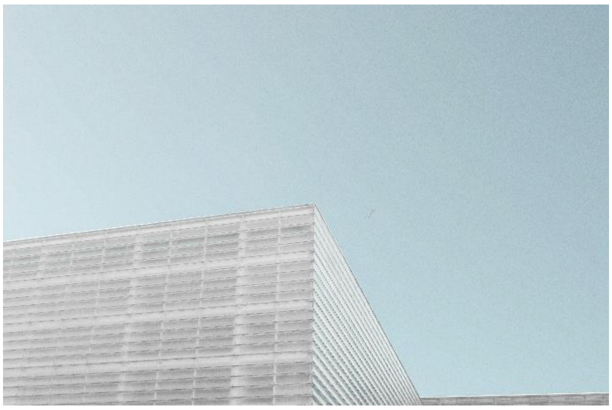
The Act aims to establish a more structured and transparent approach to providing incentives by linking them directly to verifiable capital investment and targeting key sectors perceived as critical for national development and diversification away from oil dependence. To be eligible for the EDI, a company must generally be incorporated in Nigeria, although companies exempted from incorporation and promoters of future companies can also apply. A crucial requirement is that the company must incur qualifying capital expenditure (QCE) on or before its "production day" that meets or exceeds a specified minimum threshold.[4]

The amount of this pre-production QCE must be certified by the Nigerian Revenue Service (NRS), and failure to meet the minimum threshold means the EDI certificate will not be granted. These minimum investment thresholds are introduced to target scalable and impactful projects.

The process for obtaining an EDI certificate involves an application to the Nigerian Investment Promotion Commission (NIPC). The application must include proof of commitment to invest, particulars of QCE, assets, proposed production date, expected output, and ownership structure. This shall be accompanied by a non-refundable fee of 0.1% of the QCE subject to a maximum of ₦5,000,000. The NIPC shall make recommendations to the Minister responsible for industry, trade, and investment, for onward approval from the President. Presidential approval is a mandatory step before the NIPC can issue the EDI certificate.

The most significant feature introduced by the EDI is the nature of the benefit. Instead of a tax holiday, EDI offers a **tax credit.** Eligible businesses in priority sectors would receive a tax credit on qualifying capital investments annually for five years to offset their corporate taxes. The incentive period can be extended for an additional five years if the company demonstrates that it has reinvested 100% of the profits generated from the priority product during the initial five-year period back into expanding the production of that same product. Although, this tax credit cannot be used to offset the additional tax payable under the minimum effective tax rate specified under the Act.[5]

Companies benefiting from the EDI are also required to maintain separate accounting records for their priority and non-priority businesses. This is essential for determining the income and profits attributable to the incentivized activities. Failure to comply with this separate accounting requirement can result in all of the company's income being treated as non-priority, leading to the loss of the economic development tax credit.[6]



A significant point to note is the principle of exclusivity. A company with EDI status cannot transfer this incentive to an acquiring company through a merger or acquisition and they are also generally precluded from benefiting from other similar tax incentives available under Nigerian law. However, existing incentives granted under the repealed legislation are intended to be honored for their remaining term.[7]

Potential Implications for the Nigerian Economy: Comparing Structures

The EDI is expected to have several benefits for the Nigerian economy. By tying tax relief directly to verifiable capital investments in priority sectors, the EDI is designed to stimulate real economic activity, attract quality investments, drive job creation and skills development, and promote economic diversification. This shift aims to ensure that the incentives provided result in tangible benefits for the economy, rather than merely reducing the tax burden without corresponding growth. A study on the effect of reduced company income tax incentives on FDI in listed Nigerian manufacturing companies found a significant positive link, suggesting favorable tax treatment can attract foreign investors.[8] The EDI's targeted approach could potentially enhance this effect by focusing investment on sectors deemed crucial for growth. The challenge lies in ensuring that the benefits of attracting investment through incentives outweigh the forgone tax revenue.

Furthermore, the EDI is expected to contribute to ensuring sustainable government revenue by not only being more transparent and measurable than the PSI, but that it comes alongside existing capital allowances, ensuring some taxable base remains. Overall, the EDI, as part of broader tax reforms including efforts to improve tax administration and potentially lower CIT rates could boost Nigeria's global competitiveness and contribute to increased revenue generation from non-oil sources.

Comparing Nigeria's approach with the proposed EDI and other sector-specific incentives found in some prominent African countries reveals different structures and focuses. **South Africa** offers tax incentives such as the Research and Development ("R&D") tax incentive, incentives for Greenfield and Brownfield expansion projects (Section 12I) with minimum investment thresholds, Special Economic Zones and Energy Efficiency Tax Deduction. In **Liberia**, some sectors like Manufacturing, Energy, and Housing require a minimum investment capital of US$500,000. For larger investments exceeding US$10 million, tax incentives may be granted for a longer period, up to fifteen years, subject to high-level government approval. Liberia's incentives include a maximum benefit of up to 30% of the purchase price of qualifying assets in certain sectors.[9]

Unlike South Africa's Section 12I or Liberia's high-cap threshold-based concessions, Nigeria's EDI uniquely introduces a reinvestment clause and stricter pre-production certification, emphasizing not just capital inflow but operational continuity.

Notably, the focus on priority sectors is prevalent across board. The EDI's emphasis on measurable investment as the basis for the tax credit is intended to address the transparency and effectiveness issues noted with the PSI, potentially offering a more direct link between the incentive granted and the desired economic activity compared to a simple tax holiday.

Challenges and Considerations for Effective Implementation

Despite the promising design, the EDI faces potential challenges in implementation. Capacity issues within relevant government agencies responsible for verification and administration, as well as the inherent risk of misuse or corruption, are acknowledged concerns. These are common hurdles for tax incentive regimes in developing economies.

Effective implementation requires transparency and a clear legal framework. The issues observed in other countries, such as poor coordination among agencies granting exemptions or the lack of transparency in negotiating special concessions underscore the importance of robust governance mechanisms for the EDI. Ensuring that eligibility criteria, application processes, and compliance checks are clear and consistently applied will be vital.

Furthermore, the structure of the EDI needs careful consideration to avoid negatively impacting investment and profitability, while also recognizing that tax incentives are not always the primary driver for investment decisions. Policymakers are encouraged to strategically optimize incentives, perhaps targeting marginal projects that would not be viable without the incentive.

Learning from the experiences of other African nations is crucial. While many offers various forms of tax relief, the move towards a performance-based incentive linked to verifiable investment, as proposed by the EDI, represents an effort to ensure that tax expenditures deliver tangible economic benefits. However, the ultimate success of the EDI will depend not just on its design but on the transparency, efficiency, and integrity of its administration, navigating the common challenges faced by tax incentive regimes across the continent.

Conclusion

The Economic Development Incentive marks a significant departure from Nigeria's traditional tax holiday system (PSI), aiming for a more performance-based, transparent, and effective approach to investment promotion. However, like many incentive programs across the continent, its success will hinge on effective design, robust and transparent administration, and the ability to mitigate associated risks and potential misuse that have historically affected the effectiveness and perceived fairness of tax incentive policies across Africa. If executed with rigor and transparency, the EDI could redefine the investment climate in Nigeria, positioning it as a regional leader in modern, outcome-based tax policy.

References

[1] Available at: https://www.nipc.gov.ng/pioneer-status-incentive/
[2] https://placng.org/i/wp-content/uploads/2-25/01/Analysis-of-the-Nigerian-Tax-Reform-Bills.pdf
[3] 11th Schedule to the Nigeria Tax Act, 2025

[4] The "production day" means the date when the company begins commercial-scale production or provision of the priority service. A company may forfeit its incentive status if it fails to begin production within 12 months of its proposed production date.
[5] Section 57 National Tax Act, 2025
[6] Section 180 National Tax Act, 2025
[7] Section 184 National Tax Act, 2025
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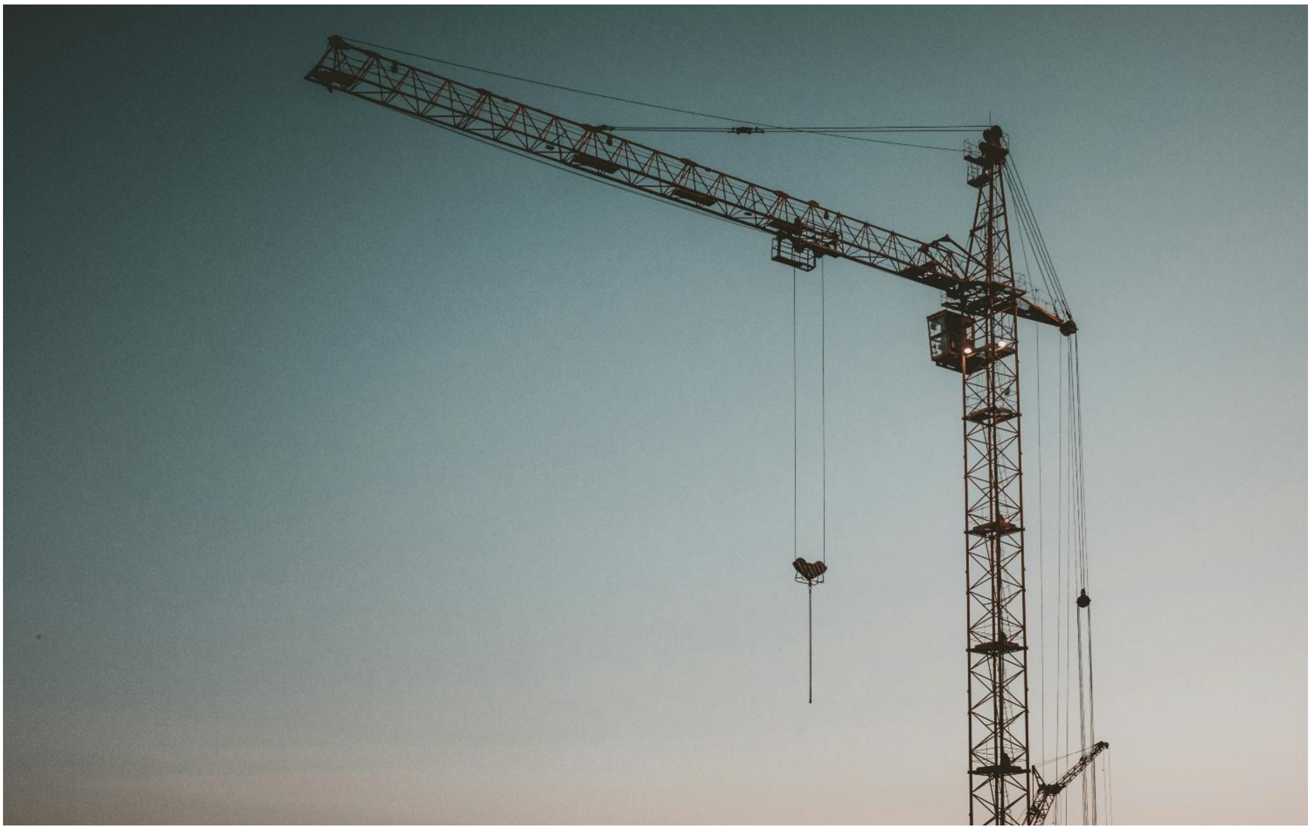

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