

REVIEW AND COMPILATION OF
EXISTING STUDIES AND

REPORTS

ON TAX INCENTIVES IN NIGERIA

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It is with a deep sense of responsibility and honour that I consent to write the foreword to the publication: Review and Compilation of Existing Studies and Reports on Tax Incentives in Nigeria. Particularly, at this crucial period in the Nigerian economy, when there is diversification from sole reliance on petroleum resources to non-oil resources as a means of funding the economy. The Chartered Institute of Taxation of Nigeria has always been an advocate for positive developments and reforms in the sphere of taxation in the Country. Therefore, we have no doubts that the book will be a necessary resource for relevant revenue functionaries and tax related agencies in their review of related laws and regulations on appropriate grant of waivers and concessions in the country.

Generally speaking, waivers, concessions and exemptions are sound and ideal arrangements both as economic tools and from the viewpoint of competitive international trade. This is because local businesses/industries need to be positioned for improvement of their fortunes for attainment of international competitiveness. However, the Nigerian case appears bedeviled with lots of challenges including abuses observable to the Nigerian public. A regime wherein concessions and waiver beneficiaries are themselves inclined to abuse of same leaves a lot to be desired. Such situations and reports of indiscriminate waivers and concessionary approvals have all contributed in questioning the bearing and economic sustainability of this initiative of government.

Permit me to highlight one of the policy recommendations in this book which has to do with building and institutionalization of capacity in tax policy analysis towards improving comprehension of the effectiveness of the current tax incentive measures in achieving its intended objectives (Item 8f).

This in fact is the crux of the matter. Building capacity, especially human capacity of the implementers of this policy and institutionalizing the policy in such a way that it cannot be arbitrarily changed, applied or implemented at will are key. It has also become necessary, in order to identify the root cause of the failure of this investment tool and to enable relevant agencies take necessary steps to block the identified loopholes through research.

ActionAid has taken the pain to carry out a thorough comparative analysis of akin policies that appears to have worked in other jurisdictions and climes and have made recommendations which can be adaptable to the Nigerian situation with a view to making the system more effective and sustainable.

Therefore, as an Institute that regulates the practice of taxation in all its ramifications in Nigeria, we are hopeful that the grant of incentives and concessions would be strictly controlled but with due regard to the following:

- a. The Country's comparative advantage by mitigating losses associated with inequitable grant of incentives
- b. All-inclusive fiscal and monetary policies are in place.
- c. Export subsidization and support.
- d. Import control measures.
- e. Development of local industries.
- f. Attraction of foreign and local investors.
- g. Beneficiaries of the incentives. e.t.c

Once again, I congratulate the ActionAid Nigeria on this laudable project and on behalf of the Chartered Institute of Taxation of Nigeria, endorse same as a useful tool for the Federal Government through the Nigerian Investment Promotion Council, the Federal Inland Revenue Service and other notable fiscal agencies as a resource for research in their grant of incentives and waivers to businesses in Nigeria.

Dame Olajumoke Simplice, FCTI
14th President and Chairman of Council
of the Chartered Institute of Taxation of Nigeria

Foreword

Preface

This account of Survey Findings on Tax Incentives in Nigeria conducted by ActionAid Nigeria (AAN) stemmed from the a project designed with an agreement with Ford Foundation to carry out activities aimed at ensuring that public revenue for taxes are increasingly accounted for, budgeted and spent in a way that benefits citizens and vulnerable groups. Ford Foundation supported AAN for a period of two years for the implementation of carefully conceptualized activities related to the goal of the project.

To deepen the effectiveness of tax provisioning for social protection of the poor and ensuring increased accountability on the part of government and its tax-related agencies we commissioned the desk review and compilation of existing studies and reports on tax incentives in Nigeria. Thus, that was the basis for birthing this report and other publications like position papers, policy papers and infographics on tax incentives in Nigeria.

For so long, Nigeria, like so many developing economies, has been granting tax incentives to multinational companies in order to attract FDI. Exponents of the tax incentives claim that the measures are germane to the development of the country, while critics of tax incentives point to the glaring lack of evidence supporting the claims that incentives have advantages. As the Actionaid Nigeria further expands the frontier of its tax power work, we continually query if tax incentives really work for the masses. All the indicators point to one direction, tax incentives seem to only work a few privileged individuals.

Recently, there seems to be a move towards finding a middle ground between the proponents of tax incentives, usually the organised business sector, and the opponents, the civil society organisations and campaigners. In the course of this work, Actionaid Nigeria organised a forum for civil society organisations to appraise the role of tax incentives in the development of Nigeria. The roundtable was envisioned for the third sector, it also had in attendance representation from the organised private sector and the representatives of the Federal Inland Revenue Service (FIRS). One of the aims of the meeting was to gauge the perception of stakeholders on the issue of tax incentives, to discuss and agree on certain issues, and to chart a course for further action.

The interesting thing about our finding was the diversity that it had. For instance, while the representatives from the third sector were skeptical about tax incentives in general, the representatives of the organised private sector were inclined towards a more positive view about tax incentives. They support the notion that some tax incentives are good, and one example they cited to that effect is that the domestic manufacturing sector in Nigeria will simply cease to exist without tax incentives. However, the distrust of the civil society organisations may not be unconnected to the fact that there is currently little or no evidence that suggests that tax incentives are significant to desired development.

This report thoroughly assesses the different models of tax incentives in Nigeria, the effectiveness of each of the models and a comparison on the achievements of each of the tax incentive models with those of other progressive countries. The effect of tax incentive in Nigeria and its impact on the citizens, especially the poor. It also analysed and established the linkage between tax incentives and its economic improvement in Nigeria.

The report also captures lessons around tax incentives practice with recommendations on how to improve on the current Nigerian tax incentives regime. It is our well-thought-out opinion that this survey findings will be of immense benefits to the duty bearers and law makers at the three-tiers of government, CSOs, global development partners, the academia, the conventional and new media who are sorely needed to give ample publicity to the findings of this survey by way of setting tax incentives as part of the agenda for national discourse.

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ActionAid Nigeria wishes to appreciate all the stakeholders who participated in the preparation for the Survey conducted and the Compilation of Existing Studies on Tax Incentives in Nigeria.

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Similarly, we acknowledge the invaluable roles played by the Board, Management and all Staff of AAN as well as the Tax Justice & Governance Network. We wish to place on record their significant roles, support, advice, ideas and suggestions in the course of conducting the survey and the implementation of the project.

It is correspondingly important to acknowledge the Business Membership Organisations, Civil Society Organisations and Government Stakeholders, especially the FIRS and the SIRS for their cooperation and contributions to the success of this work.

Our gratitude similarly goes to all the Research Assistants and volunteers who went to the field in all the geo-political zones without which this report would not have been achievable. We appreciate all the media outfits, especially Journalists Against Poverty, JAP whose participation and exceptional media coverage and publicity contributed immensely to the actualisation of the goal of this project.

Lastly, we express gratitude to the Tax Management Consultant who midwifed this publication, Mr. 'Niyi O. Akinsanya for the time and energy expended on this publication. We equally treasure the efforts of the “think-tank” constituted by Dr. Tafida Saied, Femi Olarinde and Chinedu Basse that conceptualised the terms and scope of the work and others not expressly mentioned in this acknowledgement but contributed to the success of the project. We remain profoundly grateful to all and sundry.



Ene Obi
Country Director

Acronyms

ACGS- Agriculture Credit Guaranteed Scheme
ACGSF- Agricultural Credit Guarantee Scheme Fund
ACSS- Agricultural Credit Support Scheme
AERC- African Economic Research Consortium
AGOA- African Growth and Opportunity Act
CAC- Corporate Affairs Commission
CACS- Commercial Agricultural Credit Scheme
CBN- Central Bank of Nigeria
CCA- Customs Controlled Area
CGTA- Capital Gains Tax Act
CIP- Critical Infrastructure Programme
CITA- Companies Income Tax Act
CKD- Completely Knocked Down
COFINS- Contribuição para o Financiamento da Seguridade Social
DPR- Department of Petroleum Resources
DTI- Department for Trade and Industry
ECOWAS- Economic Community of West African States
EEG- ExportExpansion Grant
EPZA- Export Processing Zones Authority
ETR- EmploymentTaxRelief
FAO- Food and Agriculture Organization
FAU- Fiscal Analysis Unit
FBU- Fully Built Unit
FDI- Foreign Direct Investment
FIPA- Foreign Investment Protection Act
FIRS- Federal Inland Revenue Services
FITA- Federal Income Tax Act
FMARD- Federal Ministry of Agriculture and Rural Development
FMF- Federal Ministry of Finance
FMFA- Federal Ministry of Foreign Affairs
FMI- Federal Ministry of Interior
FMSD- Federal Ministry of Solid Minerals Development
FWD- Farm Work Deductions
GDP- Gross Domestic Product
GEAR- Growth Employment and Redistribution
GSM- Global System for Mobile Communications
IBA- Industrial Building Allowance
IDA- Investment Deduction Allowance
IDITRA- Industrial Development Income Tax Relief Act
IDZ- Industrial Development Zones
IFC- International Finance Corporation
IMF- International Monetary Fund
IOC- International Oil Companies
IPA- Investment Promotion Act
IPI- Programa de integração social
IPPA- Investment Promotion and Protection Agreement
ITMA- Income Tax Management Act
JV- Joint Venture

KIA- Kenyan Investment Authority
KRA- Kenyan Revenue Authority
LFN- Laws of the Federation of Nigeria
LNG- Liquidified Nigerian Gas
MAN- Manufacturers Association of Nigeria
MDA- Mining Deductions Allowance
METR- Marginal Effective Tax Rate
MFCT- Ministry of the Federal Capital Territory
MFTZ- Manaus Free Trade Zone
MIDP- Motor Industry Development Programme
MoU- Memorandum of Understanding
MuB- Manufacture under Bond
MYTO- Multi Year Tariff Order
NAFDAC- National Agency for Food and Drug Administration and Control
NBS- National Bureau of Statistics
NCoC- Nigerian Copyright Commission
NCS- Nigeria Customs Service
NEITI- Nigerian Extractive Industries Transparency Initiative
NEPC- Nigerian Export Promotion Council
NEPC- Nigerian Export Promotion Council
NEPZA- Nigerian Export Processing Zones Authority
NERC- Nigerian Electricity Regulatory Commission
NIMASA- Nigerian Maritime Administration and Safety Agency
NIPC- Nigerian Investment Promotion Council
NIRSAL- Nigerian Incentive-Based Risk Sharing system for Agricultural Lending
NIS- Nigeria Immigration Service
NNPC- Nigerian Investment Promotion Commission
NOTAP- National Office for Technology Acquisition and Promotion
NPC- National Planning Commission
OECD- Organisation for Economic Co-operation and Development
OGFZA- Oil & Gas Free Zones Authority
OSIC- One-Stop Investment Center
PCN- Pharmacist Council of Nigeria
PIA- Petroleum Investment Allowance
PIS- Imposto sobre produtos industrializados
PITA- Personal Income Tax Act
PPT- Petroleum Profit Tax
PPTA- Petroleum Profit Tax Act
PSA- Production Sharing Agreement
PSC- Production Sharing Contract
QCE- Qualifying Capital Expenditure
R&D- Research & Development
RENAI- National Network of Investment Agencies
REPETRO- Regime Aduaneiro Especial de Exportação e Importação de Bens Destinados às Atividades de Pesquisa e

de Lavra das Jazidas de Petróleo e de Gás Natural
SIP- Strategic Investment Programme
SIPRI- Integrated System for Investment Promotion and Technology Transfer to the Enterprises
SIRS- States Inland Revenue Services
SKD- Semi Knocked Down
SMEDP- Small and Medium Enterprise Development Programme
SON- Standards Organisation of Nigeria
SWF- Sovereign Wealth Fund
TRE- Tax Remission Export
UNCTAD- United Nations Conference on Trade and Development
US- United States
VAT- Value Added Tax
WEAPR- Work Experience Acquisition Programme Relief
WHT- Withholding Tax



Summary

The objective of this review was to assess the current system's bottlenecks and to propose changes to improve efficiency of the tax incentive system in terms of its ability to impact on the growth of businesses- both LSE and SMEs, mobilise revenue and attract investments. Thus, tax incentives itself is a framework introduced by government to attract investments and generate particular economic activities. The primary motivation is usually to stimulate investments, most especially to attract Foreign Direct Investment (FDI).

This study employed review of related literature, Key Informant Interview and Focus Group Discussion methodologies with selected relevant stakeholders and corporate bodies. It also captured the case study of some selected countries like Brazil, Kenya and South Africa with similar peculiarities with Nigeria on the capability of tax incentives.

Nigeria's experience in granting tax incentives is traceable to the inception of British Administration in the territory, when all sorts of reliefs, allowances, and tax holidays were granted to British Companies and individuals as attractions to establish trade links with the country. Specifically, tax incentives for industrial development came on stream in 1958.

Tax incentive models in Nigeria are covered under different laws and in different forms e.g. reliefs, credits, exemptions, allowances, breaks/holidays, drawbacks etc. Most of the tax incentive models are highlighted based on the laws upon which they were promulgated. Tax incentives regime in Nigeria was extensively compared against (OECD)'s principles to enhance Transparency and Governance of Tax Incentives. Effectiveness and efficiency of tax incentives are measured via tax expenditure and the effect of tax expenditure drawbacks on the economy in general.

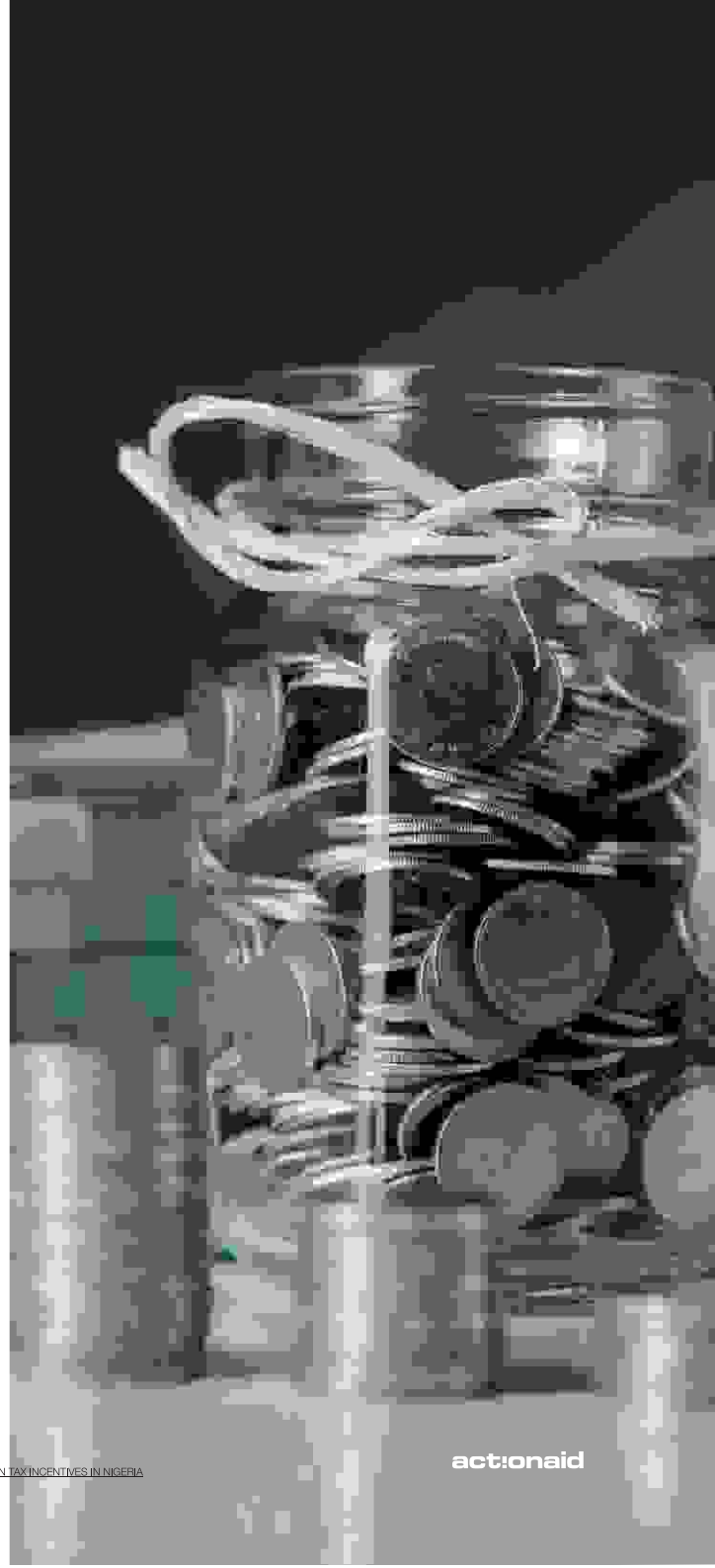
In Nigerian National Tax Incentives, the institutional framework for effective management of tax incentives for investment is vested with the One-Stop Investment Center (OSIC). The OSIC is an inter-ministerial 'committee' that comprises many bodies that regulate and administer tax incentives.

It is of relevance to reiterate that Nigeria has recorded some achievements especially in the area of policy reforms, which were meant to create a conducive environment for private businesses to thrive. However, a careful analysis of policy implications and lessons for Nigeria from the review of other countries' tax incentive system pose some questions. For instance, are tax incentives the only factor that can propel investment? What role can physical and social infrastructure, macro-economic stability as well as strong institutions play in supporting tax

incentives to promote investment, growth and employment generation in the country. These issues obviously present serious challenges to effectiveness and efficiency of tax incentives in Nigeria.

The key findings are based on intensive review of literature and consultations with relevant stakeholders. In order to streamline tax incentives, restore a level playing field for all investors in both Large Scale Enterprises (LSEs) and Small and Medium Scale Enterprises (SMSEs) and improve the investment climate so that it becomes more favourable to high value-added up-market investment which creates permanent high-skilled jobs, reduce all dimensions of poverty, and breaks down the isolation of disadvantaged regions. The following recommendations among others could be taken into account:

- I. An inter-agency data exchange system should be built to break current “information silos” and serve policy analysts in economic and tax analyses and modeling. An important exercise of indexing, classifying and linking information and databases together, including the development of a common data identifier, must be addressed as soon as possible.
- II. Institutionalise the process by which the revenue loss attributable to tax incentives is regularly estimated and reported, ideally as part of an annual Tax Expenditures Report (covering all the main tax incentives).



1.0 INTRODUCTION

Tax incentives are special privileges granted to individuals or corporations with the purpose of attracting and retaining investments. It is a framework introduced by government to attract investments and generate particular economic activities. Tax incentives have always been used to pursue a variety of objectives. The primary motivation is usually to stimulate investments and especially in Nigeria, it is to attract Foreign Direct Investment (FDI). FDI inflows, for instance, are believed not only to bring capital and (high wage) jobs to a country but can also spur competition and increase the efficiency of domestic markets more widely, thus contributing to a country's overall economic development¹.

Empirical growth regressions indeed generally find positive correlations between inward FDI and economic growth; although conclusions about causality remain contentious (Adams, 2009)². Tax incentive policies also often aim to promote specific economic sectors or types of activities as part of an industrial development strategy or to address development needs.

Tax incentives as clearly spelt out in section 2(2) article 5 of the revised version of 2017 National Tax Policy, states: “to attract, retain or increase investment in a particular sector; assist companies or individuals carrying on identified activities and assist businesses carrying on identified activities with main purpose of the policy makers to generate employment; essentially recruitment of fresh graduates, their training and development in order to increase personal and company income taxes with other attendant benefits from these investments to the economy in the long run”³.

Over the last decades, tax incentives have become more widespread in West Africa. For instance, in 1980, less than 40 percent of the countries in sub-Saharan Africa offered tax holidays while free zones were non-existent. By 2005, more than 80 percent offered tax holidays and 50 percent had adopted free zones (Keen and Mansour, 2010)⁴. The number of countries in sub-Saharan Africa granting tax holidays and establishing free zones has grown further since (James, 2014)⁵.

The application of incentives now exists virtually in all sectors of the Nigeria's economy namely industrial, agriculture, manufacturing, petroleum, solid minerals, energy, tourism and others. There are different kinds of incentives; the three basic categories of these incentives are financial, tax and regulatory which are considered by government in power. The financial incentives are public

support mechanisms in the form of grants or repayable subsidies. It is common with developed countries, but Nigeria government prefers tax incentives because they are easily affordable in promoting investment and do not require up-front use of government funds. The regulatory incentives on the other hand are in the form of concessions, exemptions from labour or environmental standards and subsidized infrastructure which are also applicable in force in Nigeria⁶.

In light of Nigeria's efforts at providing conducive environment for Foreign Direct Investment (FDI) inflow, protect the existing investments from unfair competition, stimulate the expansion of domestic production capacity and growth of industries, the Federal Government has continued over the years to provide tax incentives to attract both local and foreign direct investments into various sectors of the economy.

The main objective of this study is to review the existing studies and conduct interviews on relevant people or bodies (especially Tax Authorities), make compilation and report of these studies on tax incentives in Nigeria, and produce a detailed report on the history of tax incentives in Nigeria, the different models of tax incentives, the effectiveness of each of these models and make comparisons with the Nigeria's tax incentives with the other progressive countries and the specific objectives are namely: to assess the efficiency of the Tax incentive regime in Nigeria; evaluate the impact of tax incentives on businesses, its inherent poverty reduction mechanism; to determine its revenue expenditure to the government; to evaluate the level of awareness on tax incentive systems by the supposed beneficiaries; and determine the level of compliance to tax incentives from government and business perspective. This will further provide an expansion of knowledge in the area of packaging tax incentives while the outcome could bring a substantial social change in terms of benefits to the public.

This study employed review of related literature, key informant

interview and focus group discussion methodologies with selected relevant people and bodies as well as case study methodology of some selected countries taking sample from developing and emerging economies with similar peculiarity with Nigeria on the capability of tax incentive. The case study is to provide comparative analyses of tax incentives among these countries and would form a basis for lessons or experience for Nigeria.

The rest of this work is organised into Eight sections. Following this introduction, section two covers the review on the history of tax incentives in Nigeria, while section three focuses on the review of different models of tax incentives and organizations that have enjoyed/are enjoying the incentives. Evaluate the effectiveness and efficiency of tax incentive; determine the guiding principles and the driving force of the tax incentives. While section four analyses the impact of tax incentives on businesses and its effects on macro-economic indicators (essentially, reduction in poverty rate), and determine the revenue expenditure to government. Section five reviews the national tax incentives and assess the criteria and approval process (i.e. assessing the efficiency of the tax incentive regime) in Nigeria. Section six reviews the tax incentives of other progressive countries and make comparison with that of Nigeria and establishes the linkage between tax incentives and the economic improvement in Nigeria which identify the challenges to effectiveness of tax incentives and lessons for Nigeria. Section seven reviews challenges to effectiveness of tax incentives in Nigeria. Section eight provides policy recommendations.

¹ IMF (2015). Options for Low Income Countries' Effective and Efficient Use of Tax Incentives for Investment; a Report to the G-20 Development Working Group by the IMF, OECD, UN and World Bank

² Adams, & Samuel, (2009). Foreign Direct Investment, Domestic Investment, and Economic Growth in Sub-Saharan Africa", Journal of Policy Modeling, Vol. 31, pp. 939-949.

³ http://blog.deloitte.com/ng/inside-the-new-national-tax-policy/?utm_source=Mondaq&utm_medium=syndication&utm_campaign=inter-article-link Development Working Group by the IMF, OECD, UN and World Bank

² Adams, & Samuel, (2009). Foreign Direct Investment, Domestic Investment, and Economic Growth in Sub-Saharan Africa", Journal of Policy Modeling, Vol. 31, pp. 939-949.

³ http://blog.deloitte.com/ng/inside-the-new-national-tax-policy/?utm_source=Mondaq&utm_medium=syndication&utm_campaign=inter-article-link

⁴ ^{Reer}, M., & Mansour, M., (2010). Revenue Mobilization in Sub-Saharan Africa: Challenges from Globalization II – Corporate Taxation, Development Policy Review, Vol. 28, pp. 573-596.

⁵ James & Sebastian, (2014). Tax and non-tax incentives and investments: Evidence and Policy Implications. Investment Climate Advisory Services. World Bank Group, June 2014.

⁶ CBN, (2013). Fiscal Incentives in Nigeria: Lessons of Experience, Occasional Paper No. 47



2.0. HISTORY OF TAX INCENTIVES IN NIGERIA

Historically, Nigeria's experience of taxation predates the colonial period. The history of taxation in Nigeria dates back to the era of the Saharan trade and the introduction of Islamic religion in Nigeria between 800 AD and 1400 AD. The rulers in the Northern Nigeria were known as "Safawa" kings, who grew rich due to gifts and levies paid to them by their subordinates as taxes on cattle and agricultural crops. The Islamic religion later introduced various forms of taxes namely: Zakat, Kurdin, Kasa, Shukka Shukka, Jangalia, Kharant⁷.

The Zakat was imposed on educational and charitable purpose (Azubike, 2007)⁸. Moreover, the Obas and Ezes in the South relied on tributes, arbitrary levies, special contributions at special festivals or events, fees, presents, all collected through the head of families as its system of taxation (Olatunji et al ,2001)⁹. The first legal backing of taxation was in 1904 when Sir Fredrick Lugard introduced the Native Revenue Proclamation. This proclamation was further enhanced in 1906. The tax revenue proceeds were shared equally between the local or native authorities and the British or Central government authority. These enactments were followed by much other legislation which the colonial masters introduced during their era.

After the independence in October 1960, the Nigerian government enacted three major tax laws namely:

- a. Federal Income Tax Act (FITA) 1961
- b. Income Tax Management Act (ITMA) 1961
- c. Companies Income Tax Act (CITA) 1961.

These enactments form the bedrock of modern taxation in Nigeria. The Income Tax Management Act (ITMA) 1961 served as model for all the Personal Income Tax laws operational in regions, with amendments in some regions. However, in 1993 through Decree 104 the Federal Government of Nigeria enacted the Personal Income Tax Act 1993 to repeal all previous tax laws on Personal Income Tax in Nigeria. The 1993 Act was also repealed and replaced with the Personal Income Tax Act Cap P8 LFN 2004.

The Companies Income Tax Act (CITA) 1961 was applied to

⁷ Akinyomi O. J., & Akinyomi R. M., (2011). Tax Incentives and Revenue Productivity of the Nigerian Tax System, International Journal of Development and Management Review (INJODEMAR) Vol. 6 June, 2011

⁸ Azubike, J. B. U., (2007). A Review of Pioneer Income Tax in Nigeria, ICAN Student Journal July/Sept Vol 11 No 3

⁹ Olatunji L. A., Olaleye M. O. & Adesina O. T., (2001). Principles of Taxation in Nigeria, 2nd Edition. Osoybo: Mighty Baba Production

companies in Nigeria. The law was repealed and later replaced with the Companies Income Tax Act (CITA) in 1979 with amendments in 1993 up to 1999. The Companies Income Tax Act (CITA) in 1979 was also later repealed and replaced with the Companies Income Tax Act Cap C21 LFN 2004. The administration of CITA is the exclusive responsibility of the Federal Inland Revenue Service (FIRS).

Aguolu, (1999) defines tax incentive as an exemption or relief granted to an individual or a company to reduce the effect of taxation and thus encourage savings and investment¹⁰. These incentives are granted to individuals or companies whose income or profit is accruing in, derived from, brought into or received in Nigeria. They include

(i) Personal Allowance

(ii) Investment Allowance

(iii) Capital Allowance

(iv) Loss Relief

(v) Roll over Relief

(vi) Pioneer Relief

(vii) Exploration incentives. These incentives are however backed by various Government legislations. They are granted to enhance the growth and development of industries as well as empowering individuals and corporate taxpayers economically. In Nigeria, there are various forms of tax such as personal income tax, companies' income tax, capital gains tax, value added tax and petroleum profit tax to mention but a few. In view of promoting indigenous investment in Nigeria, tax incentives are put in place to encourage the growth of local manufacturing industries that will in turn reduce the amount of importation, generate employment essentially for fresh graduates and tax revenue for the government via personal and company income taxes in the long-run. Tax incentives include tax holidays, tax reduction, capital allowances, the right of taxpayers to election and incentives on processing zones.

The broadening of a country's taxable capacity is often linked in economic literature to the generous incentives prevalent in tax system. The discussion of exemptions is important since

they have a significant impact on the effective tax base. The provisions of generous exemptions often tend to erode the tax base, which in turn, affects income elasticity of a tax through tax-to-base elasticity (Osoro, 1993)¹¹.

Tax incentives in Nigeria have been in existence since, 1949 and they are still very much in existence in modern day governance (Fowowe, 2013)¹². Nigeria's experience in the granting of tax incentives is traceable to the inception of British Administration in the territory, when all sorts of reliefs, allowances, and tax holidays were granted to British Companies and individuals as an attraction to establish trade links with the country. Specifically, tax incentives for industrial development came on stream in 1958 and included¹³:

i. Pioneer Companies Relief, which exempted companies operating in pioneer industries for up to 5 year from paying company income tax;

ii. Companies Income Tax Relief which gave capital allowances regarding investments in machinery, building, loss carry-forward facility, etc.;

iii. Import duties relief which exempted selected pioneer companies from paying import duties on imported inputs;

iv. Approved user scheme, under which import duties were refunded to approved enterprises, which imports in the export-tuned production.

This is evident from the fact that from 2005 to date, there have been different technical institutions formed by the Finance Ministry to oversee and assess the tax incentives/structure in the country and make recommendation that will attract foreign investors, encourage local investors such as to promote growth and development of the country's economy by reducing the percentage of Nigerians population living on less than a dollar per day via generation of employment and tax revenue for government.

¹⁰ Aguolu, O., (1999). Taxation and Tax Management in Nigeria. Enugu: Meridian Associates

¹¹ Osoro, N.E., (1993). Revenue Productivity Implications of Tax Reform in Tanzania, AERC Research Paper 20, September, Nairobi, p.24

¹² Fowowe b., (2013). Do Fiscal Incentives Promote Investment? Empirical Evidence from Nigeria, J. Dev. Area 47: 17-35

3.0 DIFFERENT MODELS OF TAX INCENTIVES IN NIGERIA

Tax incentive models in Nigeria are covered under different laws and in different forms e.g. reliefs, credits, exemptions, allowances, breaks/holidays, drawbacks, etc. Those highlighted below have been categorized based on the underlying law¹⁴

3.1: Tax Based Incentives: Personal Income Tax Act

Administering agencies are: Federal Inland Revenue Service (FIRS) and State Internal Revenue Services (SIRS) and tax base incentives of Personal Income Tax Act is classified under different heads as follow:

- Tax credit allowable against tax payable on income derived from outside Nigeria Section 11
PITA: where a resident derives income from a source outside Nigeria and the income is brought into Nigeria through Government approved channels, he shall be allowed a tax credit against the tax payable by him, but the tax credit shall not exceed the proportion of his total tax for the year of assessment which that income derived from outside and brought into Nigeria bears to his aggregate income chargeable to tax in Nigeria;
- Consolidated relief allowance Section 33 (1) PITA allows a Consolidated Relief Allowance of N200,000 subject to a minimum tax of 1% of gross income whichever is higher, with the balance taxable in accordance with the Income table in the Sixth schedule to this Act.
Returns not to be filed where income is N30,000 or less
Section 43 PITA: no return of income shall be filed by a person whose only source of income in any year of assessment is employment in which he earns N30,000 or less from that source.

Income Exempted Section 19(1) PITA specifies several incomes that are exempted from tax, in the Third Schedule to the Act.

Exemption of Interest on loan granted by banks Section 19(7) PITA exempts interest on any loan granted by a bank to a person engaged in: (a) agricultural trade or business; and (b) the fabrication of any local plant and machinery.

Exemption of Dividend from tax The Third Schedule PITA lists incomes exempted from Personal Income Tax Paragraph 25 of the Third Schedule PITA exempts some dividends from tax:

(a) Dividends paid to a person by a company incorporated in Nigeria, provided that:

- The equity participation of the person in the company paying the dividends is either wholly paid for in foreign currency or by assets brought into Nigeria between 1 January 1987 and 31 December 1992
- The person to whom the dividends are paid owns not less than 10 per cent of the equity share capital of the company.

(b) For the purpose of the exemption referred to in 1, the dividend tax-free period shall commence from the year of assessment following the year in which the new capital is brought into Nigeria for the real purpose of the trade or business in Nigeria of the company paying the dividends and shall continue for five years if the company paying the dividends is engaged in agricultural production within Nigeria or processing of Nigerian agricultural products produced within Nigeria or production of petrochemicals or liquefied natural gas, and in any other case, the tax-free period shall be limited to three years.

¹³Dickson E. O., & Presley K. O., (2013). Tax Incentives and Revenue Productivity of The Nigerian Tax System, International Journal of Development and Economic Sustainability Vol. 1, No. 1, March 2013, pp.31-44, Published by European Centre for Research Training and Development, UK (www.ea-journal.org).

¹⁴NIPC & FIRS (2017). Compendium of Investment Incentives in Nigeria, first edition: October 31, 2017.

3.2: Tax Based Incentives: Capital Gains Tax Act

Administering agency is Federal Inland Revenue Service. It is applicable at 10% in different principles as described below:

- Exemption on retirement benefits schemes Section 28 CGTA: a gain shall not be a chargeable gain if income is accrued:
 - (a) As part of any superannuation fund (retirement or benefits fund) approved under Section 20 PITA;
 - (b) As part of any national provident fund or other retirement schemes established under the provisions of any Act or enactments for employees throughout Nigeria;
 - (c) Of any of those funds that is exempted under Third Schedule of PITA and;
 - (d) As a result of the disposal of a right to, or to any sum payable out of any superannuation fund.
- Exemption of gains accruing on securities, stocks, shares Section 30 CGTA: gains accrued to a person from disposal by him of Nigerian Government securities, stocks and shares shall not be chargeable gains.
- Tax exemption on gain arising from takeover, absorption or merger Section 32 CGTA: gains arising from acquisition of shares taken over absorbed or merged by another company as a result of which the acquired company loses its identity as a limited company, provided no cash was exchanged in respect of the shares.
- Tax exemption on proceeds re-invested Section 33 CGTA: gains accruing to unit holders in a trust in respect of disposal of securities shall not be chargeable on tax provided the proceeds are re-invested.
- Double taxation relief Section 41 CGTA: Any arrangement set out in an order made under Section 38 PITA and Section 45 CITA so far as they provide (in whatever terms) for relief from tax chargeable in Nigeria on capital gains by virtue of this section, have effect in relation to CGT.

3.3: Tax Based Incentives: Companies Income Tax Act

Administering agencies include Nigerian Investment Promotion Commission, Industrial Inspectorate Department, Federal Ministry of Industry, Trade and Investment Federal Inland Revenue Service depending on the incentive to be granted and the applicable rate is 30%.

- Pioneer Status Incentive: The granting of this incentive is premise on eligibility criteria and application guidelines are available on NIPC website among other things are:
 - Applications must be made within the first year of operational activities;
 - Applicant must be engaged in activities listed as pioneer industry or product. Kindly refer to the qualified list of industries and products on NIPC's website;
 - A non-current tangible asset of over one hundred million naira (N100 million) shall be deemed as satisfactory;
 - Applicant must demonstrate the tangible impact its activity (project) will have on Nigeria's economic diversity and growth, industrial and sectoral development, employment, skills and technology transfer, export development and import substitution; Applicant must provide evidence of all required legal and regulatory compliance documentation;
 - Applicant must make full payment of fees promptly, when due; and
 - During the pioneer period, a performance report must be submitted to NIPC annually for monitoring and evaluation purposes

When these conditions are met Under IDITRA, companies engaged in industries/products approved as 'pioneer industries/products' shall be

- Granted income tax relief for a period of three years, which can be extended for a period of one year and thereafter; another one year, or for one period of two years (Section 10(2)(a)(b) IDITRA);

- Exempted from paying tax on dividends paid by the pioneer company during the pioneer period to the extent that they are paid out of income exempted from tax (Section 17(3) IDITRA);
- The loss incurred during the tax relief period is also deemed to be incurred on the first day following the expiration of the tax relief period and can be carried forward to offset profits after the tax-exempt period.
- Interest on bonds and short-term securities, and proceeds of the disposal of Government and corporate securities CIT (Exemption of Bonds and Short Term Government Securities) Order 2011 provides tax exemption for interest earned on:

Short term Federal Government securities such as treasury bills and promissory notes;

 - Bonds issued by Federal, State and Local Government and their agencies; and
 - Bonds issued by corporate bodies including supra-nationals for a period of 10 years, with the exception of bonds issued by the Federal Government, which shall continue to enjoy such exemption from tax effective from 2011 on the interest.
- Exemption of interest on loan Section 11(2) CITA provides exemption from tax interest on any loan granted by a bank to a company engaged in: (a) agricultural trade or business; or (b) the fabrication of any local plant and machinery; or (c) providing working capital for any cottage industry. But before this exemption is granted; the eligibility condition is such that: the moratorium shall not be less than 18 months; and the rate of interest on the loan shall not be more than the base lending rate at the time the loan was granted.
- Exemption of profits Section 23(1) CITA: exempts the profits of the following companies from tax:
 - a) A statutory or registered friendly society, in so far as such profits are not derived from a trade or business carried on by such society;
 - b) A co-operative society registered under any enactment or law relating to co-operative societies;
 - c) Engaged in ecclesiastical, charitable or educational activities of a public character;
 - d) Formed for the purpose of promoting sporting activities;
 - e) Being a trade union registered under the Trade Unions Act;
 - f) dividend distributed by Unit Trust;
- g) A body corporate established by or under any Local Government Law or Edict in force in any State in Nigeria;
- h) Body corporate being a purchasing authority established by an enactment and empowered to acquire any commodity for export from Nigeria from the purchase and sale (whether for the purposes of export or otherwise) of that commodity;
- i) Company or any corporation established by the law of a State for the purpose of fostering the economic development of that State.
- j) A company other than a Nigerian company, would be chargeable to tax by reason solely of their being brought into or received in Nigeria;
- k) Dividend, interest, rent, or royalty derived by a company from a country outside Nigeria and brought into Nigeria through Government approved channels;
- l) The interest on deposit accounts of a foreign non-resident company;
- m) The interest on foreign currency domiciliary account in Nigeria;
- n) Dividend received from small companies in the manufacturing sector in the first five years of their operation;
- o) Dividend received from investments in wholly export-oriented businesses;
- p) Any Nigerian company in respect of goods exported from Nigeria;
- q) Company whose supplies are exclusively inputs to the manufacturing of products for export; and
- r) A company established within an export processing zone or free trade zone.
- Deduction for research and development Section 26 CITA provides for the purpose of ascertaining the profit or loss of any company for any period from any source chargeable with tax under this Act, there shall be a deduction, not exceeding an amount which is equal to 10% of the total profits of that company for that year as ascertained before any deduction is made under this section and Section 25 of CITA. Companies and other organisations engaged in research and development activities for commercialization shall be allowed 20% investment tax credit on their qualifying expenditure for that purpose.
- Reconstruction investment allowance Section 32 CITA makes available to a company an investment allowance of 10% of the actual expenditure incurred on plant and

equipment, in addition to an initial allowance under the Second Schedule of the Act.

- Rural investment allowance Section 34 CITA provides that where a company incurs capital expenditure on the provision of facilities such as electricity, water or tarred road for the purpose of a trade or business, such company shall enjoy an additional allowance under the Second Schedule of CITA at the appropriate rate as follows:
No facilities at all 100% No water 30% No electricity 50% No tarred road 15% Eligibility conditions include:
 - I. The company must be located at least 20 kilometres away from such facilities provided by the government;
 - II. Cannot be enjoyed if already enjoyed provision of Section 32: Reconstruction investment allowance;
 - III. Allowance can only be applied against the profit of the year in which such investment (facility) was completed.
- Gas Utilisation: Investment allowance: For companies in gas utilisation (downstream operations), an additional investment allowance of 35% (which shall not reduce the value of the asset) is allowed, as an alternative to the initial tax-free period granted under Section 39(b) CITA and eligible company which claims the incentive shall not also claim the tax-free dividend during the tax-free period.
- Gas Utilisation: Accelerated capital allowance Section 39© CITA provides for accelerated capital allowance after the tax-free period for companies in gas utilization(downstream operations), as follows:
 - I. An annual allowance of 90% with 10% retention, for investment in plant and machinery
 - II. An additional investment allowance of 15% which shall not reduce the value of the asset
- Gas Utilisation: Tax-free dividend Section 39(d) CITA provides for tax-free dividend during the tax-free period for companies in gas utilization (downstream operations).The Eligibility conditions are:
 - I. The investment for the business should be in foreign currency; or
 - II. The introduction of imported plant and machinery during the period should not be less than 30% of the equity share capital of the company

- Gas Utilisation: Interest deduction Subject to obtaining prior approval of the Minister of Petroleum Resources for such loan, Section 39(e) CITA provides that interest payable on any loan obtained for a gas project shall be deductible.
- Investment tax relief Sections 40 CITA provides that where a company has incurred an expenditure on electricity, water, tarred road or telephone for the purpose of a trade or business carried on by the company, the company shall be allowed an “investment tax relief” at the following rates of expenditure:
No facilities at all 100% No water 30% No electricity 50% No tarred road 15% The Eligibility of this incentive are:
 - I. The company must be located at least 20 kilometres away from such facilities provided by the government;
 - II. The relief shall be for each year expenditure is incurred on each of such facilities;
 - III. A company shall not be allowed to claim the investment tax relief for more than 3 years; and
 - IV. The relief shall not be available to a company already granted the Pioneer Status.
- 20% Income tax rate for companies with turnover less than 1 million Section 40(6) CITA provides for a lower rate of tax of 20% payable by companies in the preferred sector of the economy such as agriculture, manufacturing, solid minerals or wholly export trade for the first 5 years of commencement of business, where the turnover is less than 1 million.

3.4: Tax Based Incentives: Value Added Tax Act

Administering agencies is Federal Inland Revenue Service and under this schedule the applicable rate is 5% but there are exemptions which are:

- Sections 2 & 3 First Schedule VAT Act list the goods and services exempted from VAT:

Part 1: Goods

- a) All medical and pharmaceutical products;
- b) Basic food items;
- c) Books and educational materials;
- d) Baby products;

- e) Fertilizer, locally produced agricultural and veterinary medicine, farming machinery and farming transportation equipment;
- f) All exports;
- g) Plant, machinery and goods imported for use in the export processing zone or free trade zone: Provided that 100 per cent production of such company is for export otherwise tax shall accrue proportionately on the profits of the company.
- h) Plants, machinery and equipment purchased for utilization in gas down-stream petroleum operations; and
- i) Tractors, ploughs and agricultural equipment and implements purchased for agricultural purposes.

Part 2: Services

- a) Medical services;
- b) Services rendered by Community Banks, People's Bank and Mortgage institutions;
- c) Plays and performances conducted by educational institutions as part of learning; and d) All exported services.

Part 3: Zero Rate goods and services.

- a) Non-oil exports
- b) Goods and Services purchased by diplomats
- c) Goods purchased for use in humanitarian donor funded projects." 'Humanitarian Donor Funded Project' includes projects undertaken by Non-Governmental Organizations and Religious and Social Clubs or Societies recognized by law whose activity is not for profit and in the public interest."
- Exemption of commissions on stock exchange transactions Part II First Schedule VAT Act is modified in VAT (Exemption of Commissions on Stock Exchange Transactions) Order, 2014. The order shall be in force for a period of 5 years. There is an exemption from VAT on commissions from the following:
 - a) earned on traded value of shares;
 - b) payable to Securities and Exchange Commission;
 - c) payable to Nigerian Stock Exchange; and
 - d) payable to the Central Securities Clearing System on stocks.

3.5: Agriculture/ Agro-Allied Sector Incentives

These categories of incentives are under the Federal Ministry of Agriculture and Rural Development and the administering agencies are: Nigeria Incentive-Based Risk Sharing System for Agricultural Lending, Commercial banks and Federal Inland Revenue Service and are under different schedule:

Enhanced Capital Allowance (Tax Depreciation) regime

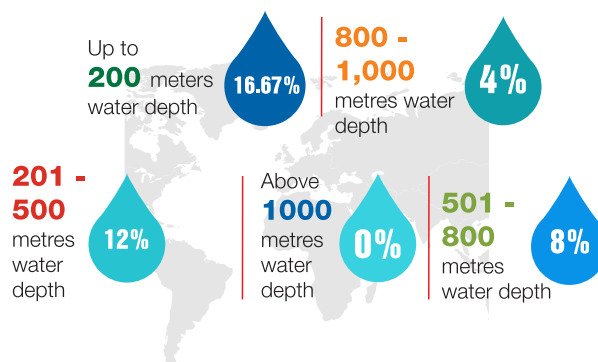
- a) 95% capital allowance is enjoyed in the year a qualifying expenditure is incurred pursuant to Paragraph 24 Table 1 & 2 Second Schedule of CITA
- b) Companies engaged in wholly agricultural activities are entitled to unrestricted capital allowances pursuant to Paragraph 24 (7) CITA
- c) Companies engaged in wholly agricultural activities are entitled to carry forward unutilized capital allowances indefinitely.
- Agricultural Credit Guarantee Scheme Fund- Loan guarantee of up to 75%: This fund provides guarantees on the payment of interest and principal in respect of loans granted by any bank for certain agricultural purposes with the aim of increasing the level of bank credit to the agricultural sector. Eligibility are that applicants must apply for the loan for purposes connected with:
 - I. Establishment or management of plantation for the production of rubber, oil palm, cocoa, coffee, tea and similar crops.
 - II. The cultivation or production of cereal crops, tubers and fruits of all kinds, cotton, beans, groundnuts, shea nuts, beniseed, vegetables, pineapples, bananas and plantains.
 - III. Animal husbandry.
- Exemption from minimum Corporate Income Tax Section 33(3) a CITA, exempts the income of a company carrying on agricultural trade from payment of minimum tax.
- Indefinite carry forward of losses Section 31(3) CITA allows companies engaged in agricultural trade or business to carry forward their losses indefinitely.

3.6: Sector Specific Incentives

- Solid Minerals is under the Federal Ministry of Mines and Steel Development. The incentives are administered by Federal Inland Revenue Service and it consists of the following:
 - I. Exemption from Companies Income Tax Section 36 CITA provides that a new company going into the mining of solid minerals shall be exempted from tax for the first three years of its operation.
 - II. 95% accelerated capital allowance Second Schedule CITA provides accelerated capital allowance at 95% of qualified capital expenditure on Mining in the first year of use of the asset. The Eligibility is for All companies that incur qualifying capital expenditure on mining.
- Manufacturing is under the Federal Ministry of Industry, Trade & Investment; it is by Nigeria Incentive-Based Risk Sharing System for Agricultural Lending and Central Bank of Nigeria and consists of the following:
 - I. Interest drawback programme fund for cassava processing 60% repayment of interest paid by those who borrow from banks under ACGS for the purpose of cassava production and processing. Eligibility is Certified investor business plan by Nigeria Incentive-Based Risk Sharing System for Agricultural Lending (NIRSAL) and Ability to repay back the loan granted under ACGS.
- Tourism/Hospitality is under the Federal Ministry of Information and Culture and it is regulated by Nigerian Tourism Development Corporation but the incentive is administered by Federal Inland Revenue Service.
 - I. 25% of income in convertible currencies exempted from tax Section 37 CITA provides that such income must be generated from tourists and be put in a reserved fund to be utilized within 5 years for the building and expansion of new hotels, conference centers and new facilities for the purpose of tourism development.

- Oil & Gas is under the Federal Ministry of Petroleum Resources and it is regulated by Department of Petroleum Resources, but it is administered by Federal Inland Revenue Service.

- 1) Graduated Royalty Rates approved for oil companies
 - (a) On shore production - 20%
 - (b) Production in territorial waters and continental shelf areas up to 100 meters
Water depth – 18.5%
 - (c) Production in territorial waters of continental shelf areas beyond 100 meters – 16.67%
 - (d) For production sharing contract for deep offshore operation, the royalty rates are:



Petroleum Act Section 5 of Deep Offshore and Inland Basin Production Sharing Contracts Act CAP. D3 LFN 2004 as amended provides royalty rates payable in respect of deep offshore contracts.

- 2) Investment Tax Credit Allowance Section 22 PPTA: Investment tax credit allowance is granted in accordance with the provisions of the production sharing contract. The investment tax credit rate applicable to the contract area is 50% of chargeable profit for the duration of the production sharing contract. Eligibility includes:
 - i. The incentive is available to all the crude oil producing companies which signed the production sharing contract agreements with the NNPC (for deep offshore oil exploration and production) in 1993. It commenced in 1999.

- ii. The companies will be entitled to this allowance throughout the duration of the production sharing contract.
- iii. In computing the tax payable, the investment tax credit shall be applicable in full to petroleum operations in the contract area such that the chargeable tax is the amount of the assessable tax less the investment tax credit. The chargeable tax shall be split between the NNPC and the crude oil producing company in accordance with the proportion of the percentage of profit oil split.

3) Allowable Deductions Chargeable Tax is the amount of

tax paid after deduction of allowable deductions made pursuant to the provisions of Section 10 PPTA. Allowable deductions are treated as charges against income and not as tax offsets and are wholly incurred in the process of petroleum operations.

Eligibility covers allowable deductions which include the following:

- I. Rent incurred by the International Oil Companies (IOC) for the period in respect of land or buildings occupied under an oil prospecting license or an oil mining lease for disturbance of surface rights or for any other like disturbance.



- ii. All non-productive rents, the liability for which was incurred by the International Oil Companies (IOC) during the period.
- iii. All royalties, the liability for which was incurred by the company during that period in respect of natural gas sold and actually delivered to the NNPC or sold to any other buyer or customer or disposed of by any other commercial manner.
- iv. All royalties, the liability for which was incurred by the company during that period in respect of crude oil or of casing head petroleum spirit won in Nigeria.
- v. All sums, the liability for which was incurred by the IOC to the Federal Government of Nigeria during that period by way of customs or excise duty or other like charge(s) levied in respect of machineries, equipment and goods used in the company's petroleum operation.
- vi. Sums incurred by way of interest upon any money borrowed by such company, where the board is satisfied that the interest was payable in capital employed in carrying on its petroleum operations.

3.7: Tariff Based Incentives

The administering agencies are: Federal Ministry of Finance, Federal Inland Revenue Service and Nigeria Customs Service.

Agriculture: Agriculture, Agro-allied and Agro-processing 0% Import duty on agriculture equipment and machinery HS Headings 84, 85 and 90. 0% Import duty rate greenhouse equipment has been classified as agricultural equipment HS Heading 94.06

Agriculture: Agricultural Commodities

10% Import duty rate and 20% Levy on husked brown rice HS 1006.20.00.00



Transportation: Aviation

0% Import duty on commercial aircraft HS Heading 88 only for registered commercial aircraft operators



Power: Electricity Generation, Distribution and Transmission

0% Import duty on equipment & machinery in the power sector HS Headings 84, 85 and 90



Solid Minerals: Mineral Mining

0% Import duty on equipment & machinery in the mineral mining sector HS Headings 84, 85 and 90



Manufacturing: Sugar Processing

5% Import duty rate and 5% levy on raw sugar import for local processing HS 1701.11.00.00 – 1701.12.00.00 Available to sugar refineries that are signed onto the backward integration policy of Government on sugar development



Manufacturing: Iron & Steel

0% Import duty rate on importation of billets HS 7207.11.00.00 and 7207.19.00.00
0% Import duty rate on importation of hot rolled steel sheets/coils HS Heading 72.08





levy on concessionary Fully Built Unit (FBU) import by Assembly Plants (APs): Importation of Fully Built Unit (FBU) cars HS

Heading **87.03** equal to their Completely Knocked Down (CKD)/ Semi Knocked Down (SKD) imports for the period of **2016 – 2018**. Half of their imported CKD/FBU kits for the period of **2019 – 2024**



levy on concessionary FBU import by assembly plants (APs): Importation of FBU commercial vehicles HS Heading **87.02, 87.04, 87.05, 87.06, 87.07 and 87.16** equal to their CKD/SKD imports for the period of **2016 – 2018**. Half of their imported CKD/FBU kits for the period of **2019 – 2024**



Import Duty Rate on local tyre manufacturing plants: Importation of tyres equal to twice the production for two years from the date of commencement of production.

General requirements to access tariff-based incentives

- (a) Evidence of registration with the Corporate Affairs Commission; (b) Tax compliance by means of Tax

- Identification Number; and
(c) Certification by relevant Ministry (where applicable) – agriculture, automotive, greenhouses and power.

3.8: Export Incentives

These incentives are under the Federal Ministry of Industry, Trade and Investment and it is regulated by Nigerian Export Promotion Council. This incentive is administered by Nigerian Export Promotion Council.

- Export Expansion Grant Scheme: Export (Incentives and Miscellaneous Provisions) Act, No.65 of 1992, Cap. E19, Laws of the Federation of Nigeria (LFN) provides for a post-shipment incentive designed to improve the competitiveness of Nigerian products and commodities and expand the country's volume and value of non-oil exports. Validity for EEG application is that Qualifying export transaction must have the proceeds fully repatriated within 300 days, calculated from the date of export and as approved by the EEG Implementation Committee. Incentives Rate covers the following:

- The scheme operates a 'Weighted Eligibility Criteria' to assess applications ii. The Weighted Eligibility Criteria has four bands: **15%, 10%, 7.5%, and 5%**

Eligibility Criteria Threshold	Weight	Local Value Added	Local Content
30%	20%	70%	20%
Employment (Nigerians)	500	10%	
Export Growth	5%	35%	Capital Investment
0%	15%		



Export Credit Certificate: The grant computed shall be settled by issuing negotiable tax credit known as ECC, to the beneficiaries. The instrument can be used to settle all Federal Government taxes such as company income tax, VAT, WHT. Eligibility includes among other things, exporter must:

- a) Be registered with Corporate Affairs Commission;
- b) Be registered with Nigerian Export Promotion Council;
- c) Shall be a manufacturer or merchant of products of Nigerian origin intended for the export market;
- d) Have carried out formal export with its export proceeds repatriated into a domiciliary account in Nigeria and confirmed by Central Bank of Nigeria; and
- e) Submit its baseline data which includes audited Financial Statement, information on operational capacity and Export Expansion Plan to NEPC.

3.9: Special Economic Zone

There are two categories of these zones that are directly under the Federal Ministry of Industry, Trade and Investment but they are regulated by Nigeria Export Processing Zones Authority and Oil & Gas Free Zones Authority respectively. The administering agencies include Federal Inland Revenue Service, Nigeria Customs Service, and Oil & Gas Export Free Zone Authority

EXPORT PROCESSING ZONE INCENTIVES

- i. Export processing zone incentives for enterprises approved by NEPZA under the NEPZA Act and operating within an approved Zone:
 - (a) 100% foreign ownership of investment;
 - (b) Free transferability of capital, profits and dividends by foreign investors;
 - (c) Rent-free land at construction stage; thereafter, rent shall be payable;
 - (d) All industrial undertakings including foreign companies and individuals operating in an Export Processing Zone are allowed full tax holiday from Federal, States and Local Governments;
 - (e) Duty-free, tax free on import of raw materials for goods destined for re-export;
 - (f) Waiver on all import and export licenses; and

(g) Waiver on all expatriate quotas for companies operating in the zones.

ii. 100% capital allowance Section 35(1) CITA provides that a company which has incurred expenditure on its qualifying building and plant equipment on an approved manufacturing activity in an export processing zone shall be granted 100 percent capital allowance in any year of assessment. Eligibility condition is that a company granted capital allowance under this subsection shall not be entitled to an investment allowance under this Act.

iii. Unlimited sale of product within the customs territory: Enterprises operating in the Zones are allowed to export into the Nigerian customs territory up to 100% of their product produced, assembled or packaged within the Zones. The eligibility conditions are that:

- a) There must be valid permit, and on-time payment of appropriate duties; and
- b) Import prohibited goods assembled or packaged within the Zone without meeting the 35% local value addition requirement shall not be allowed into the Customs territory.

Activities permitted in export processing zones

- (a) Manufacturing of goods and services;
- (b) Warehousing freight forwarding and customs clearance;
- (c) Handling of duty-free goods (trans-shipment, sorting, marketing, packaging, etc.);
- (d) Banking, stock exchange and other financial services; insurance and re-insurance; (e) Import of goods for special services, exhibition and publicity;
- (f) International commercial arbitration services; and
- (g) Activities relating to integrated zones.

OIL & GAS FREE ZONE INCENTIVES

- a. Oil & Gas Export Free Zone incentives for enterprises approved by the OGFZA under the OGFZA Act and operating within an approved Zone:
 - (i) 100% foreign ownership of investment;
 - (ii) Free transferability of capital, profits and dividends by foreign investors;
 - (iii) Rent-free land at construction stage; after which rent shall be payable;

- (iv) All industrial undertakings including foreign companies and individuals operating in an Oil & Gas Export Free Zone are allowed full tax holiday from Federal, States and Local Governments;
 - (v) Duty-free, tax free on import of raw materials for goods destined for re-export;
 - (vi) Waiver on all import and export licenses; and
 - (vii) Waiver on all expatriate quotas for companies operating in the zone.
- b. 100% capital allowance Section 35(1) CITA provides that a company which has incurred expenditure in its qualifying building and plant equipment on an approved manufacturing activity in an export processing zone shall be granted 100 percent capital allowance in any year of assessment. The Eligibility is that a company granted capital allowance under this subsection shall not be entitled to an investment allowance under this Act.
 - c. Unlimited export into the customs territory Part 1, 3.7 OGFZA Regulations provide unlimited export of any product or goods manufactured, assembled, prepackaged in the Zone into the customs territory. Eligibility conditions are that:
 - i. There must be valid permit, and on-time payment of appropriate duties;
 - ii. Import prohibited goods assembled or packaged within the Zone without meeting the 35% local value addition requirement shall not be allowed into the Customs territory.
 - d. 75% duty rebate FZO 2015 provides for a 75% duty rebate on raw materials processed in the OGFZA. The Eligibility condition is that appropriate license must be obtained from OGFZA.

ADDITION TAX INCENTIVES

1. Employment Tax Relief (ETR)¹⁵
This is an income tax relief on the employment of persons that do not possess any previous work experience within three years of graduating from school or any vocation. To qualify for this, a company must have a minimum net employment of 10 employees in an assessment year of which 60% must be a new graduates who must have no previous work experience within three years of graduating. 'Net Employment' is defined as "the difference between

incoming and outgoing employees of the company within the assessment period." The relief to be enjoyed is 5% of the company's assessable profit and shall be limited to the gross salary of the qualifying employees. It should also be noted that, in line with the order, the tax exemption (relief) shall only be utilized in the year of assessment in which the employees were first employed and any unabsorbed deduction shall not be carried forward to another assessment period.

2. Work Experience Acquisition Programme Relief (WEAPR)
This is a relief on the employment and retention of experienced employees. The basic criterion is that a company must have a minimum net employment of five new experienced employees and retain such employees for a minimum of two years from the year of assessment when the employees were first employed. The company shall enjoy an exemption from income tax of 5% of its assessable profits in the assessment period in which the company qualifies. The tax exemption (relief) shall only be utilised in the year of assessment in which the company qualifies and any unabsorbed deduction shall not be carried forward to another assessment period.
3. Labour Intensive Mode of Production
There is a 15% tax concession for five years. The rate is graduated in such a way that an industry employing 1,000 persons or more will enjoy the 15% tax concession while an industry employing 100 will enjoy only 6%, while those employing 200 will enjoy 7% and so on.

BENEFICIARIES OF TAX HOLIDAY

The list of organisations that have enjoyed/are enjoying the incentives in Nigeria is endless but vis-à-vis pioneer status, Federal government of Nigeria on August 9th 2017 clarifies 27 businesses to enjoy tax break under pioneer status. The list was published by the Federal Ministry of Industry, Trade and Investment. Here is the full list of the 27 industries to enjoy the pioneer status¹⁶.

1. Mining and processing of coal;
2. Processing and preservation of meat/poultry and production of meat/poultry products;

3. Manufacture of starches and starch products;
4. Processing of cocoa;
5. Manufacture of animal feeds;
6. Tanning and dressing of leather;
7. Manufacture of leather footwear, luggage and handbags;
8. Manufacture of household and personal hygiene paper products;
9. Manufacture of paints, vanishes and printing ink;
10. Manufacture of plastic products (builders' plastic ware) and moulds;
11. Manufacture of batteries and accumulators;
12. Manufacture of steam generators;
13. Manufacture of railway locomotives, wagons and rolling stock;
14. Manufacture of metal-forming machinery and machine tools;
15. Manufacture of machinery for metallurgy;
16. Manufacture of machinery for food and beverage processing;
17. Manufacture of machinery for textile, apparel and leather production;
18. Manufacture of machinery for paper and paperboard production;
19. Manufacture of plastics and rubber machinery;
20. Waste treatment, disposal and material recovery;
21. E-commerce services;
22. Software development and publishing;
23. Motion picture, video and television programme production, distribution, exhibition and photography;
24. Music production, publishing and distribution;
25. Real estate investment vehicles under the Investments and Securities Act;
26. Mortgage backed securities under the Investments and Securities Act; and
27. Business process outsourcing.

4.0: Review of the Tax Incentives Regime Against the Principles to Enhance Transparency and Governance

This section compares the tax incentives regime in Nigeria against the Organization for Economic Co-operation and Development (OECD)'s Principles to Enhance the Transparency and Governance of Tax Incentives¹⁷. Our goal is to identify the institutional, structural and technical bottlenecks that:

- (i) Impede high-value investment and inclusive economic growth;
- (ii) limit the country's ability to realize its revenue potential.

The need to better manage the country's revenue potential is well recognised by the Nigerian authorities. It is particularly pronounced today, with weaker public finances of the post military era on one hand, and a greater need for domestic financial resources to create an enabling environment for investment on the other.

Principle 1. Make public a statement of all tax incentives for investment and their objectives within a governing framework¹⁸. This principle calls for the government of Nigeria to provide justification for granting tax incentives, both in terms of costs and intended benefits, in order to promote transparency in decision-making processes, limit discretion and allow the government

¹⁵ Embassy of Federal Republic of Nigeria, Washington D.C. <http://www.nigeriaembassyusa.org/index.php?page=investment-incentives>

¹⁶ <https://www.premiumtimesng.com/news/headlines/239548-exclusive-...>

to be held accountable for the incentives it grants. In qualitative terms, Nigeria adheres to Principle 1. The new National Tax Policy sets clear objectives for investment incentives.

However, no systematic, institutionalized mechanism exists to quantify the effectiveness of the tax incentive measures nor to communicate the costs and benefits of the current or proposed system to policy makers or the public at large. The lack of any form of evaluation of the effectiveness of tax incentives compromises the ability of the Nigerian authorities to adequately and comprehensively assess whether the Investment Incentives will achieve the intended and stated objectives.

With the survey conducted, the revelation shows that 72.6 percent of the respondents admit that the Nigerian government has no single mechanism in place to determine the cost-benefit of tax incentives since inception but 27.4 percent agreed that there is. This is shown in the pie chart below:

8 The government has no single mechanism in place to determine the cost-benefit of tax incentives since inception



Thus, Nigeria would be well advised to establish, at the highest level, preferably within the Ministry of Finance, a well-staffed Fiscal Analysis Unit (FAU) which would have as one of its principal responsibilities, monitoring tax policy and the special provisions that deviate from standard tax treatments in order to determine their revenue consequences and likely economic effects. Indeed, on a more general level, any efforts to reform Nigeria's tax system, if they are to lead to sustainable long-term benefits, should include establishing an institution with staff trained in the techniques of modern fiscal analysis and equipped with the necessary tools for putting those techniques to practical use. The role of an FAU in tax policy analysis can be critical to both

supporting sound tax policies and exposing the deficiencies in flawed tax reform proposals. To analyse the effectiveness of tax incentives, the FAU needs to determine whether:

1. The incentives have the desired effect on investment;
2. These effects are achieved at a reasonable price; and finally,
3. The resulting changes in investment actually help achieve the ultimate goals.

Fiscal Analysis Tools. Two of the most important evaluation tools that have to be developed and systematically maintained by the FAU are effective tax rate modeling and comprehensive tax expenditure reporting.

Effective Tax Rate Modeling: To evaluate the extent that various tax incentive measures can have on investment trends in the country, the Nigerian government is advised to develop a Marginal Effective Tax Rate (METR) model. The METR model would allow the authorities to assess the impact of the various tax incentive measures on the rate of return for representative investment projects (at the margin). In addition, METRs can be used in empirical analysis of the sensitivity (elasticity) of investment to taxation, to evaluate the amount by which the level or rate of investment will be affected in response to tax reform. Clear understanding and assessment of the impact of various tax design scenarios is especially critical at the present time.

Nigerian authorities are strongly advised to draw on the OECD's extensive experience in METR modeling to build a robust model that would support policy makers in understanding the impact of the changes that are currently being contemplated for inclusion in the new Investment policy against the intended objectives of the tax incentive system.

Tax Expenditures Reporting: Tax expenditure reports are a useful tool that supports policy makers in addressing economic and social policy objectives. Their primary purpose is to identify the revenue losses associated with tax incentives and, consequently, focus policy makers' attention on the fact that tax expenditures are quite similar to direct spending programmes and (in theory) have to compete with other government spending priorities when the government makes its budget decisions. The Ministry of Finance is capable of calculating the cost of its budgetary tax incentives but there is:

¹⁷For additional information on the OECD's Tax and Development Programme see:

www.oecd.org/ctp/globalrelationsintaxation/taxanddevelopment.htm.

www.oecd.org/ctp/globalrelationsintaxation/Principles_international_engagement_Revenue_Matters.pdf

¹⁸ www.oecd.org/ctp/tax-global/transparency-and-governance-principles

- i. no policy-making conclusions or recommendations which seem to originate based on those reports;
- ii. no capacity to build a micro-simulation model to simulate the cost of the “to be” system of tax incentives, to evaluate the burden of various tax incentives proposals; and
- iii. no institutionalized mechanism in existence to communicate the cost of either the current or the “to be” tax incentive system to either Nigerian policy makers or the public at large.

At the moment a World Bank/ International Finance Corporation team has completed a comprehensive tax expenditure analysis. The government of Nigeria would be advised to benefit from the World Bank/IFC team in building its own capacity in tax expenditure reporting and micro-simulation modeling.

Furthermore, the country would be strongly advised to institutionalize a mechanism for disclosing the cost and intended benefit of the current and/or proposed tax incentive regimes to the key stakeholder groups, to seek feedback and allow for stakeholders' involvement in the design of tax incentive measures prior to their adoption (see the section entitled “Stakeholder Roles and Responsibilities for more information on the latter point).

Principle 2. Provide tax incentives for investment through tax laws only¹⁹

One of the most essential aspects of the reform package undertaken by the democratic government in Nigeria is the preparation of a New National Tax Policy. This is in response to investors' perception that the current tax incentive Acts are excessively complex, as well as the Nigerian authorities' recognition that the lack of transparency and undue complexity of the legislative and regulatory frameworks must be addressed to enable a conducive and dynamic business environment.

The current government in power has fully engaged in developing the new Investment Incentive policy. A meaningful evaluation of Nigeria's adherence to Principle 2 can now be conducted in the light of tax incentives compendium prepared by NIPC and FIRS in 2017. The result of the survey we conducted projects that 84.9 percent granting of tax incentives in Nigeria is usually void of due process and often time against the core policy. This is shown on the figure below:

84.9% of tax incentives is usually void of due process and often time against the core policy objectives



The Nigerian authorities are advised to consolidate all legislative elements related to investment incentives within the body of one single new Act. Ultimately, all laws with tax implications should be reflected within the body of the Tax law (even if the provisions are duplicated).

Principle 3. Consolidate all tax incentives for investment under the authority of one government body, where possible.

One striking feature of the Nigeria investment landscape is the presence of a number of institutions responsible for investment promotion and facilitation, including but not limited to:

1. Nigerian Investment Promotion Council;
2. Nigeria Export Processing Zones Authority
3. Oil & Gas Free Zones Authority
4. Nigerian Export Promotion Council

It has to be noted that most of these agencies operate as a network and have numerous branches and representations, either domestically or abroad.

An obvious question is whether, for a country like Nigeria, consolidating these institutions would help to avoid unintended waste and overlap. Furthermore, and perhaps more importantly, consolidating these institutions will help to avoid inconsistent application of investment incentive measures, which is unavoidable under the current New National Tax Policy. The survey revealed that 83.4 percent of the respondents admit that the government agencies responsible for granting tax incentives do not adhere to the constitutional provisions by allowing most especially the smaller companies enjoy them due to inherence complexity of investment incentives Acts; see the figure below for more detail.

¹⁹ www.oecd.org · ctp · tax-global · transparency-and-governance-principles

23 The government agencies responsible for granting tax incentives do not routinely conduct audit and monitoring of the target objectives of which the incentives were granted



As an example, submitting an investment declaration (which entitles one to tax incentives) to NIPC could grant an investor a set of tax incentives which is different from the incentives the investor would have been granted had the investment declaration for the same investment been submitted to other agencies. The investor must himself figure out which agency will grant him a better “treatment”. Clearly, smaller investors, with limited capacity to evaluate the intricacies of a complex Investment Code, are most disadvantaged by the current arrangement.

27 Agencies empowered by law to oversee the tax incentives do not periodically conduct audit and monitoring of the target objectives of which the incentives were granted



This is an indication that, there is a need for an inter-agency co-ordination and therefore, Nigeria authorities are strongly advised to institutionalize an inter-agency electronic information exchange system, with an inter-agency registry of investment declarations accessible by tax authorities in real time. This will increase transparency, help to avoid inconsistencies in the application of incentive policies, limit discretionary power and rent seeking, and help to address problems that may arise with the governance of tax incentives.

Principle 4. Ensure tax incentives for investment are ratified through the law-making body or Parliament²⁰

The tax incentives legislation process in Nigeria is largely

transparent. Common and specific tax incentives are defined in the Investment Incentives Acts. The National Tax Policy Implementation Committee (NTPIC or the Committee), on Friday 2 February 2018, presented its progress report on the review of tax laws, tax incentives and regulations, and proposed tax reforms to then Minister of Finance (MoF), Mrs. Kemi Adeosun. The Committee was constituted following approval of the revised National Tax Policy (NTP or the Policy) by the Federal Executive Council in February 2017 to drive implementation of the Policy²¹.

The mandate of the Committee was to carry out reviews of tax laws on Industrial Development (Income Tax Relief) Act (IDITRA) and Tertiary Education Trust Fund (Establishment, Etc.) Act and in order to extend the tax relief granted under IDITRA to Tertiary Education Tax, National Information Technology Development levy and other taxes imposed on profits of companies and restriction of capital allowance claimable on capital expenditure incurred during the tax relief period of a company to annual allowance upon expiration of the tax holiday in accordance with the recommendations of the NTP, while taking into consideration the Economic Recovery and Growth Plan (ERGP) and the Ease of Doing Business Plan. Efforts of the Committee were focused on reforms that could be implemented within a short time without unnecessary controversy while other desirable reforms were deferred to the future. The recommendations of the Committee have been put together in 2 Executive Orders and 5 Amendment Bills as follows²²:

- Executive Orders Value Added Tax Act (Modification) Order.
- Review of Goods Liable to Excise Duties and Applicable Rates Order, 2017.
- Amendment Bills Companies Income Tax Act (Amendment) Bill.
- Value Added Tax Act (Amendment Bill) Customs, Excise, Tariff etc. (Consolidation) Act (Amendment) Bill.
- Personal Income Tax Act (Amendment) Bill.
- Industrial Development (Income Tax Relief) Act (Amendment) Bill.
- It is expected that the draft Executive Orders and Bills will be exposed for engagement of key stakeholders while being considered by the Federal Executive Council

²⁰ www.oecd.org/ctp/tax-global/transparency-and-governance-principles

and before they are presented to the National assembly for ratification²³.

However, as discussed above, the lack of any form of evaluation of the effectiveness of the proposed tax incentives measures handicaps the legislative process. It compromises the ability of Nigerian policy makers to adequately defend the proposed measures and of Nigerian legislators to adequately assess whether the new Investment Incentives Acts will indeed achieve its intended objectives.

Principle 5. Administer tax incentives for investment in a transparent manner²⁴

Incentives regimes are prone to tax avoidance. As such, an assessment of the impact of tax incentives on the administrative capacities of tax administrations and the compliance behavior of taxpayers cannot be overemphasized. Tax incentives that do not take into account the limitations of the tax administration's capabilities have been proven to be cost-ineffective (i.e. bring in less than a dollar of investment for each dollar lost in government revenues). They frequently result in the development of creative schemes to pass along tax benefits to other activities or in outright fraud through improper accounting, such as reporting expenditures for activities that are not entitled to the incentives as if they were so entitled.

As an example, the provision of the Nigerian Tax incentives Acts that allows for tax relief of reinvested earnings and profits granted on the basis of a declaration of investment intent, is easily subject to abuse by Nigerian taxpayers. A simple declaration of intent to reinvest industrial activity earnings into an agricultural activity affords an effective tax rate reduction of at least 10%. The anecdotal evidence suggests that the problem of Aladdin's lamp ("new firms for old") is also common as old firms are reconstituted as new ones at the end of their holiday period, so that they can continue to be tax-exempt. Similarly, channeling asset purchases through qualifying companies on behalf of non-qualifying ones is evidently a "popular" technique in Nigeria.

From the interview, talking about the tax administration's capacity, one of the key Nigerian government officials who had previously be at management cadre of tax administration in

Nigeria at different levels noted that: "Tax administration capacity is weak but we are lucky that most of the tax incentives provided by the old tax incentives Acts are not being used by investors."

We conclude this section by recommending that:

- i. Nigerian policy makers should design incentive framework that is commensurate with the capabilities of the tax administration to manage and administer it. Poorly designed tax incentives can impose additional indirect costs on society which should be considered in the analysis of their effectiveness.
- ii. Any provisions over which tax authorities have discretion as to their application create opportunity and incentives for corruption as firms try to "convince" authorities to accept their applications. Firms involved in other activities will spend resources trying to convince government officials to grant them special treatment. These are issues for the legal system and monitoring them involves definite costs to society. Currently in Nigeria, where monitoring of such activity is limited, such opportunities should be minimized by the government.
- iii. Tax authorities should build capacity to effectively monitor tax incentives claims (including access to an electronic registry of investment declarations) and periodically carry out audits of cases where tax incentives have been claimed to ensure that they are not misused.

Principle 6. Calculate the amount of revenue forgone attributable to tax incentives for investment and publicly release a statement of tax expenditures.

Tax expenditure budgeting is a valuable method for monitoring the amount of foregone revenue from tax incentives. There are several powerful reasons for governments to document and track their tax expenditures:

- i. Efficiency. Tax expenditure estimates permit a comparison of the indirect costs of programmes with alternative means of achieving similar objectives. These alternatives may be either direct expenditures or other tax expenditures.
- ii. Accountability. Tax expenditure estimates increase public knowledge of government activities and objectives and permit the public to more easily track and assess changes in

<http://www.mondaq.com/Nigeria/x/673942/tax+authorities/National+Tax+Policy+Implementation+Committee+Presents+Report+On+Tax+Law+Reforms>

22 <http://blog.deloitte.com.ng/national-tax-policy-implementation-committee-presents-progress-report-on-tax-law-reforms/>

23 http://blog.deloitte.com.ng/national-tax-policy-implementation-committee-presents-progress-report-on-tax-law-reforms/?utm_source=Mondaq&utm_medium=syndication&utm_campaign=View-Original

reforms/?utm_source=Mondaq&utm_medium=syndication&utm_campaign=View-Original

24 www.oecd.org/ctp/tax-global/transparency-and-governance-principles

government policy.

iii. Equity. Since the benefits of a tax expenditure are directly related both to the tax status of the potential recipient and to other provisions in the tax Acts, their effect is frequently uneven across taxpayers, violating the tax principles of horizontal and vertical equity. Tax expenditure quantification helps to focus attention on the tax system's structure and forces policy makers to question whether each of the various deviations is justifiable.

iv. Effect policy through the tax system. Finally, the identification and quantification of tax expenditures results in government's realisation that economic and social policy may be affected not only through direct expenditures and transfers, but also indirectly through the tax system.

The Ministry of Finance calculates the cost of its budgetary tax incentives based on the revenue loss (foregone) method, which is an ex post quantification of the extent to which a provision reduces revenues. The immediate revenue losses only represent the direct costs to the economy that the tax incentives introduce. Further distortions, indirect costs, include administrative costs from running tax incentives and prevention measures against fraudulent incentives schemes, as well as the social costs of rent-seeking behaviour, including corruption.

Even though, the direct revenue costs of incentives are difficult to quantify, if the investment would not have been made in the absence of tax incentives, the direct revenue loss is effectively zero. However, if incentives have no effect on investment, then the entire forgone tax revenue constitutes a revenue loss; the survey conducted indicates that 59 percent of tax incentives constitute revenue loss that are avoidable by government if the incentives have no effective on investment; however, 41 percent of the respondent disagreed and opined that the true amount of direct revenue losses is likely to be between these two extremes. This is shown on the figure below:

28: Tax incentives constitute revenue loss that are avoidable by Government



The mixed feeling from the opinion of the respondents about whether the tax incentives constitute revenue loss that are avoidable by government may largely be attributed to lack of mechanism to estimate and document tax expenditures in our yearly budgeting process.

A new report by ActionAid and Tax Justice Network Africa has revealed that governments in four member-countries of the Economic Community of West African States, ECOWAS, lose an average of \$9.6billion revenue every year through corporate tax incentives and waivers.

The report, which examined tax incentives granted over the years by Nigeria, Ghana, Côte d'Ivoire and Senegal, to attract foreign investment, noted that despite the huge revenue losses involved, there was little evidence that the policy actually increased investments in the region. Rather it said it was causing a “race to the bottom” in the affected economies. Of the four countries, Nigeria recorded the biggest loss of about \$2.9 billion (N577 billion) to waivers every year, more than the Federal Government's annual budget to the education sector²⁵. The survey conducted revealed that 92.7 percent of the amount of revenue loss attributable to tax incentives are not regularly calculated and publicly reported in the yearly budgeting to reflect the revenue expenditure to the government. This can be seen in the figure below.

29: The amount of revenue loss attributable to tax incentives are not regularly calculated and publicly reported in the yearly budgeting to reflect the revenue expenditure to the government



This is an indication that, the country tax incentives management process creates a huge revenue loss to the government; therefore, the government of Nigeria is advised to institutionalize the process by which the revenue loss attributable to tax incentives is regularly estimated and reported, ideally as part of an annual Tax Expenditures Report (covering all of the main tax incentives).

²⁵<https://www.premiumtimesng.com/news/more-news/188796-nigeria-losing-2-9bn-yearly-to...>

The development and publication of a yearly tax expenditure budget would be one of the particularly useful undertakings of the FAU (discussed under Principle 1). Moreover, capacity needs to be built to create and maintain micro-simulation models that would allow revenue losses due to various tax incentive proposals to be evaluated by Nigerian policy makers.

Principle 7. Carry out a periodic review of the continuance of existing tax incentives by assessing the extent to which they meet the stated objectives²⁶.

Constant vigilance is the price to be paid for a tax law that includes investment incentives and other tax preferences. A review of the current tax structure in Nigeria reveals that the system creates an incentive to substitute capital for labour. A bias in favour of capital-intensive production may be appropriate under certain circumstances, depending on the nature of the presumed externalities that justify the granting of tax preferences, for example a technology transfer embodied in capital goods. This bias could have been appropriate in the 1970s, but it has been showing its limitations in the face of consistent rise in unemployment rate with an emergence of a new, educated and skilled workforce in Nigeria, at a time when the creation of high-skilled jobs is one of the main priorities for the country²⁷. Furthermore, highly incentivized sectors do not do enough in terms of technology transfer to justify preferential treatment.

The previous tax incentives Acts before New National Tax Policy institutionalized an asymmetrical regime between Large Scale Enterprises (LSEs) and Small and Medium Scale Enterprises (SMEs), under which the former benefits from financial and tax advantages and exemption from approvals. We systematically conducted and assessed the current tax incentives system and it was revealed that the impact of the special status granted to the LSEs is modest in terms of job creation and the quality of those jobs. There is little effect on real wages and the system did not induce many indirect jobs. What's more, the favorable treatment accorded to the LSEs, in fact, came at the expense of the SMEs, i.e. SMEs do not receive comparable support from the authorities. The survey conducted revealed that SMEs do not enjoy much of tax incentives. The result shows that 59.0 percent respondents disagreed that SMEs enjoy tax incentives as much as large organisation. The figure below reflects the opinion of the respondents.

20 Small and Medium Scale Enterprises enjoy Tax Incentives as much as large organizations



Lastly, “fly-by-night” or short-lived investments are in a more favourable situation in the current tax incentives environment compared to long-term investment. Since LSEs most time make profit during the tax holiday period, they become major beneficiaries of this tax incentive therefore, a favourable tax bias exists against SMEs.

We conclude this section by recommending that periodic assessment of the performance of tax incentives be conducted systematically in Nigeria. Performance reviews should include an analysis of both the costs and the benefits of the tax incentives with a goal to understand:

- I. Whether the current system meets its intended goals of job creation and poverty reduction;
- ii. If other measures could have achieved the same goal in a more cost-efficient manner;
- iii. What measures could be proposed to address the most pressing priority of the country such as job creation and poverty reduction and what will be the burden of the proposed measures.

Also, the Nigerian authorities are strongly advised to build capacity in effective tax rate analyses. The Marginal Effective Tax Rate (METR) modeling can be used to assess the impact of tax policy reforms to the level of investment across different:

- a) Types of capital (machinery, buildings, inventories, land);
- b) Sectors/industries (manufacturing, agriculture, services, other);
- c) Shareholder groups (taxable, tax-exempt, non-resident);

²⁶ www.oecd.org/ctp/tax-global/transparency-and-governance-principles

²⁷ <https://nigerianstat.gov.ng/download>

d) regions;

e) size.

Of critical importance at the present time, the Nigerian policy makers should design the new Investment Incentives modalities, an METR model could be used by tax incentives policy analysts in understanding the impact of various design scenarios against the intended objectives of the system.

Principle 8. Highlight the largest beneficiaries of tax incentives for investment by specific tax provision in a regular statement of tax expenditures, where possible.²⁸

It has been widely recognised that pioneer tax incentive in Nigeria allowed Large Scale enterprises (LSEs) to benefit from significant exemptions and incentives. The surveys we conducted across the six regions in October 2019 revealed that the lion share of the advantages was captured by a minority of large firms, whose owners have direct access to the government in power to the detriment of 'smaller firms' that the owners cannot access the Executives in government that grant the incentives. A lack of transparency on the cost and benefits of tax incentives prevents policy makers and the public alike to adequately scrutinize them. Our analysis suggests that the LSEs is the largest beneficiary of the Nigerian tax incentives system at the expense of the SMEs and indeed of the country as a whole. The revenue loss due to special tax provisions translates into less available money for other public expenditures, such as infrastructure development of disadvantaged regions, investments in public education, health, poverty alleviation programmes, job creative projects and security.

The Nigerian authorities are advised to conduct a thorough analysis of the winners and losers of the tax incentives system. Tax expenditure reporting could list the major beneficiaries and the amount by which they benefit from tax incentives. Making such information public can enhance the legitimacy of the government and the revenue authorities in the eyes of citizens, which in turn can broadly enhance compliance the more.

Principle 9. Collect data systematically to underpin the statement of tax expenditures for investment and to monitor the overall effects and effectiveness of individual tax incentives²⁹

Accurate, complete, current, consistent and reliable data is

crucial in enhancing the effectiveness and efficiency of a tax incentives policy. At this stage, the Nigerian authorities are experiencing difficulties in attempting to integrate and leverage common inter-agency data. Various agencies, holders of relevant information, have different classification systems, which lack common definitions and structure. This complicates data integration and necessitates mapping one classification system against another.

The technological foundation is lacking in Nigeria to establish a reliable single-source data store and framework. According to the 2018 United Nations E-Government Survey, Nigeria ranks very low among African countries in the application of ICTs in government, and 143th worldwide among 193 countries evaluated³⁰. What is needed now is an important technological foundation and exercise of indexing, classifying and linking information and databases together. A common data identifier must be developed as soon as possible. A holistic, unified data and centralised data storage infrastructure that breaks current "information silos" will serve analysts in economic and tax analyses and modeling. That, in turn, will support Nigerian policy makers in taking effective strategic decisions with regard to both specific tax incentive measures and in addressing broad macro-economic goals.

Principle 10. Enhance regional co-operation to avoid harmful tax competition.

Open economy considerations and increasing globalisation impose constraints on Nigeria's ability to pursue independent policies and puts pressure on policy makers to keep effective marginal rates in line with other countries. That is why the issue of tax incentives cannot be tackled in isolation. The government of Nigeria is advised to work together on a regional basis with other Maghreb countries to increase co-operation in the area of tax to avoid competing tax incentives.

Stakeholder roles and responsibilities³¹

The current mechanisms for stakeholder consultation, including for the development of the Incentives modalities that benefit the poor, do not allow for effective discussion and adequate consideration of private sector concerns on investment incentives issues. As Nigeria moves away from its former regime, new opportunities exist to build a broad-based consultative process and ownership around the government's visions

²⁸ www.oecd.org/ctp/tax-global/transparency-and-governance-principles

The Nigerian authorities are advised to institute a consultation process involving stakeholders (a Stakeholder Consultative Committee) where the private, public, civil society and academic sectors work together to enhance the country's competitiveness. Broader stakeholders' participation validates the relevance of the reforms of tax incentives, conveys ownership and ensures that reform activities are sustained. In addition, the stakeholders become change agents as they participate in a consultative process contributing to the government's priorities and supporting implementation. Nigerian policy makers are strongly encouraged to reinvigorate consultations and strengthen their roles in the development and implementation of the new code. Public-private dialogue is essential to identify areas of concern and develop collaborative solutions to continue to sustainably improve Nigeria's investment environment.

4.1: Effectiveness and Efficiency of Tax Incentives

How tax incentives are designed and governed is critical to their effectiveness and efficiency. This section discusses principles and good practices in these areas, and elaborates on issues of reform of tax incentives. Effective use is taken here to mean that tax incentives realise their stated objectives; this can be assessed irrespective of associated costs.

Raising domestic investment or FDI is usually a necessary but not a sufficient condition for 'effectiveness', as the higher investment should be of the kind envisaged to yield the desired social benefits in broader welfare terms. Empirical evidence finds that taxes matter for investment, although most likely less so in Nigeria. Empirical studies on the relationship between effective tax burdens and FDI generally conclude that host country taxation significantly affects investment (De Mooij and Ederveen, 2008)³². Most of these evidences, however, refer to advanced economies. Recent studies report similar results for Nigeria,

although the effects tend to be somewhat smaller on average (James & Van Parys, 2009³³; Abbas & Klemm, 2013³⁴). One reason might be that Nigeria does not offer attractive general investment conditions for most multinational companies, due to for instance poor infrastructure, macroeconomic instability, unclear property rights, and weak governance or judicial systems. In these circumstances, tax incentives do not effectively counterbalance such poor conditions and are largely ineffective (Kinda, 2014)³⁵. At the same time, however, tax incentives might be one of the few (albeit second-best) instruments for Nigeria to offset disadvantaged circumstances, address regional disparities and mitigate market failures, such as lack of financial access.

Investment surveys conducted confirm that tax incentives usually do not top the list of investment factors in Nigeria. We conducted a business survey of 50 companies in the six geopolitical zones of Nigeria active in agriculture, mining, manufacturing, utilities, construction, and services sectors. Investors were asked to rank the importance of twelve location factors and to assess how they might have changed, improved and worsened, in the last three years. The results suggest that tax incentives packages ranked 11th out of 12 in importance and this importance will fall over time given the current state of infrastructure. For comparison: transparency of the legal framework ranked 5th in investors' concerns and will grow in importance. Investors thus seem to care much more about deficient legislation and onerous regulations than about the availability of tax incentives.

Where tax incentives increase FDI, domestic investment may be displaced. Displacement reduces effectiveness in terms of the net impact of the incentive on the domestic capital stock. This happens, for instance, if FDI reflects a mere transfer of ownership, through mergers and acquisitions, or if domestic investment is 'round tripped' through a foreign entity to take advantage of the tax incentive. Displacement can also occur in labour markets, where jobs in new firms come at the expense of employment in other sectors of the economy.

²⁹ www.oecd.org/ctp/tax-global/transparency-and-governance-principles

³⁰ <https://publicadministration.un.org/egovkb/Data-Center>

³¹ www.oecd.org/ctp/tax-global/transparency-and-governance-principles

³² De Mooij, R. A., & Sjöf E., (2008). Corporate Tax Elasticities: A Reader's Guide to Empirical Findings, Oxford Review of Economic Policy, Vol. 24, pp. 680-97.

³³ James, S., & Van Parys, S., (2009). Investment Climate and the Effectiveness of Tax Incentives, World Bank Group.

³⁴ Abbas, S. M. A., & Klemm, A., (2013). A partial race to the bottom: corporate tax developments in emerging and developing economies, International Tax and Public Finance, Vol. 20, pp. 596-617.

³⁵ Kinda, T., (2014). The Quest for Non-Resource-Based FDI: Do Taxes Matter? IMF Working Paper no. 14/15 (Washington: International Monetary Fund).

Efficient use in this work means that objectives are achieved at low social costs. Such costs include revenue losses for government and other social costs, for example due to less efficient resource allocation. Redundancy matters for efficiency too, since it implies a loss of government revenue from projects that would have been undertaken also without tax incentives.

Redundancy implies that the tax incentives are a mere cash transfer to the investor: a net social loss to the extent that the marginal cost of public funds exceeds unity (and an even greater loss in national terms if the investor is foreign). On the other hand, for projects that would not have been undertaken without the incentive, there is no direct revenue loss so long as taxation of the incentivized activity is not entirely eliminated, there may in fact be a net revenue gain from those projects. To minimize the revenue cost of tax incentives, the goal would thus be to offer tax incentives only to those marginal investors who would not have invested otherwise.

Indirect revenue costs arise from taxpayers abusing the tax incentive regime (Zolt 2014)³⁶. For example, if tax incentives are only available to foreign investors, local firms may use foreign entities to route their local investments in order to qualify. Similarly, if tax benefits are available to only new firms, taxpayers may reincorporate or set up new corporations to be treated as a new taxpayer under the tax incentive regime. Other leakages occur where taxpayers use tax incentives to reduce the tax liability from non-qualified activities, for instance, by shifting taxable income to a related firm that qualifies for a tax holiday or that resides in a tax-free economic zone (McLure, 1999³⁷; Eason, 2004³⁸). Preventing such losses requires proper anti-abuse rules and strong administrative capacity to enforce them.

Additional resource costs arise for the government in administering tax incentives and for businesses in complying with the associated requirements. Of course, any tax comes along with such costs. However, they generally increase with the complexity of the assessment processes of tax incentives, and with the opportunities for rent seeking and corruption they might create. The additional administrative costs are one of particular concerns in this work, where administrative capacity is often

limited. Indeed, scarce resources might be diverted away from core aspects of a country's tax administration, undermining other efforts to mobilize revenues.

A first step to understanding the public revenue forgone as a consequence of tax incentives is to calculate the implied 'tax expenditure'. Tax expenditures are usually defined as a government's estimated revenue loss that results from giving tax concessions or preferences to a particular class of taxpayer or activity. Investment tax incentives are only one form of tax expenditure, by which is meant a provision in the tax code that deviates from some benchmark tax system in a direction favorable to the taxpayer. A tax expenditure review quantifies the revenue forgone for each provision, including for investment tax incentives analyzed in this paper. Conceptual complexities arise when performing a tax-expenditure review, including in defining the relevant benchmark to which tax incentives are to be compared. Importantly, a tax expenditure review does not take into account either any effect of the incentive on investment or the leakage and abuse to which it can give rise to. The former may imply an overstatement of actual revenue cost, since elimination of the incentive might lead to a reduction in the tax base and hence to less additional revenue (if the rate would still be positive) than a 'static' calculation implies. The latter implies an understatement. As methodologies differ, international comparisons of tax expenditures are usually difficult.

Tax expenditure analyses are increasingly being used by developing countries, with strong encouragement by and support from the International Organizations (IMF, OECD, UN and World Bank, 2011)³⁹, including through technical assistance. The International Budget Partnership's Open Budget Survey indicates that tax expenditure reporting is undertaken by the following middle and low-income countries: Argentina, Chile, Columbia, Dominican Republic, Guatemala, India, Jamaica, Jordan, Kenya, Lebanon, Malaysia, Morocco, Nepal, Pakistan, Peru, Philippines, Russia, Serbia South Africa, Sri Lanka, Tanzania, Trinidad and Tobago. Some other countries like Nigeria carry out such analyses, but her score is low, indicating weak methodological frameworks.

³⁶ Zolt, E., (2014). Tax Incentives: Protecting the Tax Base, Paper Prepared for the UN Project: Protecting the Tax Base for Developing Countries.

³⁷ McLure, Jr., C., E., (1999). Tax Holidays and Investment Incentives: a Comparative Analysis, Bulletin for Int'l Fiscal Documentation, Vol. 53, pp. 326-339.

³⁸ Eason, A. J., (2004). Tax Incentives for Foreign Direct Investment, Kluwer Law International

³⁹ IMF, OECD, UN & World Bank, (2011). Supporting the Development of More Effective Tax Systems, Report to the G-20 Development Working Group



Tax expenditure index of Nigeria as at 2011 stood at 0.24 percent which increased marginally to 0.36 percent in 2012 and went back to 0.24 percent in 2013 and as at 2014 and 2015 the indexes were 0.17 percent and 0.27 percent respectively⁴⁰.

Six drawbacks of tax expenditures

In general, tax expenditures harm the efficiency and effectiveness of a tax system. But not all tax concessions are detrimental to the economy. For example, tax credits for research and development when properly administered can generate positive gains for the economy.

The economic literature has identified six key drawbacks associated with tax expenditures⁴¹:

1. They narrow the tax base. This is an important concern in countries where the tax base is already compressed because of large informal and agricultural sectors.
2. Tax expenditures create inequities across taxpayers as those with similar incomes and assets end up paying different levels of taxes.
3. Tax expenditures invite corruption since several exemptions tend to be discretionary, encouraging officials to grant concessions in exchange for a bribe.
4. Benefits from tax preferences accrue disproportionately to middle and high-income households, thereby contributing to income inequality. By lowering the revenue take, they further limit the government's capacity to spend on inequality-reducing programmes.
5. Tax expenditures have been found to be redundant in

attracting foreign investment. Many investors have reported that they would have invested in a country anyway and tax incentives were not crucial determinant in their decision.

6. Tax expenditures tend to be less transparent than a typical (direct) spending programme in the annual budget, which is debated by the parliament. They thus permit "spending" that is outside the agreed-upon budget.

Open Budget Survey (OBS) in 2017 made a declarative statement that large numbers of countries in Africa are lagging in reporting tax expenditures most especially Nigeria and this seriously undermine the ability of Nigerian citizens to hold government accountable for using public funds efficiently and effectively⁴².

This report draws on the ample experiences and insights that International Organisations have gained from interactions with countries. International Organisations and many other observers have often found tax incentives to be ineffective, inefficient and associated with abuse and corruption. As a result, they have frequently advised countries to remove them or to improve their design, transparency and administration.

5.0: National Tax Incentives

The institutional framework for effective management of tax incentives for investment is vested with the One-Stop Investment Center (OSIC). The OSIC is an inter-ministerial 'committee' which comprises the Nigerian Investment Promotion Council (NIPC), Corporate Affairs Commission (CAC), Nigeria Immigration Service (NIS), Nigeria Customs Service (NCS), Federal Inland Revenue Service (FIRS), National Office OR Technology Acquisition and Promotion (NOTAP), National Agency For Food and Drug Administration and Control (NAFDAC), Standards Organization of Nigeria (SON), Federal Ministry of Solid

⁴⁰ IMF (2018). Country Report No. 18/64-Nigeria selected issues,

<https://www.imf.org/media/Files/Publications/2018/cr1864>

⁴¹ <https://www.cgdev.org/blog/time-pay-more-attention-tax-expenditures>

⁴² <https://www.internationalbudget.org/open-budget-survey/>

Minerals Development (FMDS), Federal Ministry of Foreign Affairs (FMFA), Federal Ministry of Interior (FMI), Nigerian Electricity Regulatory Commission (NERC), Nigerian Export Promotion Council (NEPC), Nigerian Maritime Administration and Safety Agency (NIMASA), National Planning Commission (NPC), Department of Petroleum Resources (DPR), Nigerian Copyright Commission (NCoC), Manufacturers Association of Nigeria (MAN), Pharmacist Council of Nigeria (PCN), National Bureau of Statistics (NBS), Ministry of the Federal Capital Territory (MFCT), Federal Ministry of Finance (FMF), Central Bank of Nigeria (CBN) and three regional bodies responsible for investment promotion at their respective regions (Odu'a Investment Company, South-East/South-South Desk and the New Nigeria Development Company)⁴³.

In line with modern tax regimes, aimed at boosting investment and economic development through private sector initiatives, tax incentives in Nigeria cut across various sectors of the economy that are considered crucial to rapid economic growth. These incentives can be classified as both general and sector specific incentives (see Compendium of investment incentives)⁴⁴.

5.1: General Incentives

These are incentives that are applied to stimulate and attract both foreign and domestic investments in all sectors of the economy and they include:

5.1.1: Pioneer Status

This is a tax incentive exempting qualifying companies in certain industries and service sectors from paying company income tax in their formative years so as to enable them to make appreciable profit for re-investment into the business. This comes in form of a seven-year tax holiday for industry in economically disadvantaged areas such as lack of access roads, pipe borne

water, electricity, telecommunication and transportation while five-years for industries in areas with the necessary infrastructure. To qualify, a joint venture or wholly foreign owned company and an indigenous company must have incurred a capital expenditure of not less than N5.0 million and N150,000.00 respectively. Also, the application for pioneer status is expected to be submitted within one year of commencement of operations.

Parameters for Accessing Pioneer Status by Companies

The Nigerian Investment Promotion Commission considers the following parameters in granting pioneer status to companies⁴⁵:

1. Employment Generation: In processing pioneer status for any prospective investors, job creation is one of the criteria. The company is expected to provide jobs in the economy as well as show evidence for capacity building, transfer of technology as well as develop local know-how for indigenous employees to boost entrepreneurship and investment in the economy.
2. Value Addition: This involves the transformation of primary product into finished goods within the economy without necessarily assembling those goods in Nigeria. The value addition a business creates in the production process is weighted and scored in the granting of pioneer status. The higher the value addition, the more acceptable in the issuance of pioneer status.
3. Local Content: The Nigerian local content simply focuses on the promotion of value addition in Nigeria through the utilisation of local raw materials, products and services in order to stimulate the growth of indigenous capacity. This item is considered in the granting of pioneer status by the Nigerian Investment Promotion Council (NIPC).
4. Export Potential: In the determination for the granting of pioneer status, the export potential is taken into consideration on the belief that such investment will generate inflow of foreign exchange into the economy.
5. Corporate Social Responsibilities: This is the potential that a company would contribute to the sustainable development

⁴³CBN, (2013). Fiscal Incentives in Nigeria: Lessons of Experience, Occasional Paper No. 47

⁴⁴ NIPC & FIRS (2017). Compendium of Investment Incentives in Nigeria, first edition: October 31, 2017.

⁴⁵NIPC (2009). 'Investment Policies in Nigeria', Nigerian Investment Promotion Commission (NIPC) <http://www.nipc.gov.ng/>

in the community in which it is established. Such corporate responsibilities include building of schools, provision of portable water, electricity, road network etc. for the host communities.

It is a set of standards by which companies subscribe in order to make its impact on the society.

6. Investment in infrastructure: This is an incentive granted to industries that provide certain facilities that should have been provided by the government, access roads, pipe borne water and electricity. Twenty per cent (20 per cent) of the cost of providing these infrastructures where they do not exist is tax deductible.
7. Investment in Economically Disadvantaged Areas: A 100 per cent tax holiday for seven years is granted to a pioneer industry in economically disadvantaged local government of the Federation. Such a company is also entitled to 5 per cent depreciation allowance in addition to the initial capital depreciation allowance.
8. Companies Income Tax: It is used to encourage potential and existing investors and entrepreneurs. The current rate for all sectors of the economy excluding petroleum is 30 per cent.
9. Local Value Added: To encourage local fabrication and production of goods within the economy with greater local content, a 10 per cent concession for five (5) years is granted essentially to engineering industries.
10. Access to Land: Any company incorporated in Nigeria is allowed to have access to land right for the purpose of its operations in any state of the Federation. Land lease is usually for a term of 99 years unless the company stipulates a shorter duration.
11. Investment Promotion and Protection Agreement (IPPA) In an effort to foster foreign investors' confidence in the Nigerian economy, government enters into bilateral investment promotion and protection agreements with countries that do business with Nigeria. This is to grant safety of the investment of the contracting parties in the event of war, revolution, expropriation or nationalization. It also grants investors the transfer of interest, dividends, profits and other incomes as well as compensation for dispossession or loss.

12. Capital Allowance: Allows companies to write off the capital cost on qualifying assets for tax purposes in a given accounting period. The rate is restricted to 75 per cent of assessable profit per annum for companies in the manufacturing sector and 66 per cent for others, except those in the agro-allied industries. Companies in the agro-allied industries are granted 100 per cent on leased assets, while an additional investment allowance of 10 per cent is granted on leased assets for agricultural plants and equipment. Below are the current rates applicable in respect of capital allowances.
13. Tax Relief for Research and Development (R&D): Industrial establishments are expected to engage in research and development for the improvement of their processes and products. Up to 120 per cent of expenses on (R&D) are tax deductible, provided that such (R&D) activities are carried out in Nigeria and related with the businesses from which income is derived. Also, 140 per cent is allowed as R&D on local raw materials. However, where the research is long-term, the expenses on R&D is taken as capital expenditure and written off against profit. The results of such research would be patented and protected according to international property rights.
14. In-Plant Training: Industries with in-plant training facilities are entitled to a two per cent tax concession over a period of 5 years.
15. Minimum Local Raw Material Utilization: Attainment of a targeted minimum utilization level of local raw material qualifies an industry for a 20 per cent tax credit for a five-year period.

5.2.1: Sector Specific Incentives

5.2: The Oil and Gas Industry

Given the importance of oil and gas sector to the Nigerian economy, it became imperative to design tax incentives that

would encourage investment in the sector, in order to maximize its potential and government revenue. These incentives as provided by the subsisting fiscal regime in the sector include:

5.2.1.1 Incentives in the Memorandum of Understanding (MoU)

- **Tax Inversion:** This is a strategy that allows the companies under the Joint Venture (JV) to enjoy reduced tax rates as a result of the reduction in operational cost arising from per unit cost efficiency. The tax inversion rate is currently 35 per cent and it is only applicable to producers with operating cost below US\$1.70 per barrel contingent upon a smooth production not impeded by quota restrictions, interruptions arising from sabotage and/or community disruption.
- **Restriction on Penalty Charges:** Penalties are not exempted on operating cost below US\$2.30/bpd for companies producing more than 175,000 billion barrel per day (bpd) and operating cost below US\$3.00/bpd for companies producing below 175,000 bpd.
- **Minimum Guaranteed Notional Margin:** This is designed to guarantee a definite profit margin after tax and royalty payments for the Joint Venture (JV) companies on their equity crude or NNPC crude intake regardless of market conditions. The margin is applied as follows:
 - A. **Company's Equity Crude:** US\$2.50 per barrel was increased to US\$2.70 per barrel for companies that incurred capital investment cost above US\$2.00 per barrel; while
 - B. **NNPC Crude:** US\$1.25 per barrel was increased to US\$1.35 per barrel for capital investment cost above US\$2.00 per barrel.
Thus, the margin is contingent upon the Technical Cost (TC) of operations not exceeding the fiscal technical cost of \$4.00/bbl (4.00 US\$ per barrel)

(Omoregbe, 2005)⁴⁶. Furthermore, it is expected that if the market price of crude oil is below US\$15.00/bbl., the minimum guaranteed margin decreases by US\$0.18 for every US\$1.00 drop and increases by US\$0.10 for every US\$1.00 increase if the price is above US\$19.00/bbl.

5.2.1.1: Incentives in the Petroleum Tax (PPT) Act and other Acts

Capital Allowance (CA): As outlined in the PPT Act, capital allowance is claimable on four categories of assets or Qualifying Capital Expenditure (QCE) items.

- i. Capital Expenditure on Plant, Machinery and fixtures;
- ii. Capital Expenditure on Pipelines and storage tanks;
- iii. Capital Expenditure on Building construction or works of permanent nature on buildings; and
- iv. Capital Expenditure on Drilling activities like acquisition of rights in or over petroleum deposits, searching, discovering and testing deposits and construction of any works or structure likely to be of little use when petroleum operation ceases.

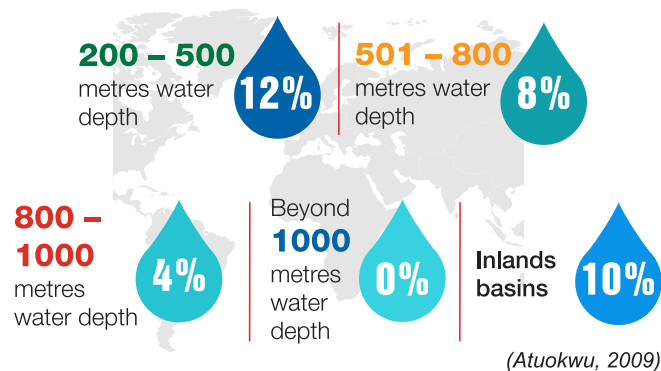
Capital Allowance includes:

- **Annual Allowance:** This is granted to companies in respect of the depreciation to the QCE to encourage crude oil exploration. This is computed on a straight line basis by writing off 20 per cent of the cost of the asset annually in the 1st to 4th year and 19 per cent in the 5th year. The balance of 1 per cent remains in the books until the asset is sold. However, Capital Allowance deductions in any accounting period are limited to the extent that the actual tax payable by the company is not less than 15 per cent of the assessable tax in the absence of capital allowances (Atuokwu, 2009)⁴⁷.
- **Petroleum Investment Allowance (PIA):** It is a one-off allowance available to the JV companies as well as the indigenous or sole risk operators and claimable in the accounting period in which an asset with QCE was first used. The PIA rates are applicable on graduated basis as follows:

⁴⁶ Omoregbe Y. (2005). 'Fiscal Regimes,' Being a Paper Presented at the Nigerian Extractive Industries Transparency Initiative (NEITI) Civil Society Capacity Building Workshop, Rivers State Nigeria.

⁴⁷ Atuokwu, C. (2009). 'Taxation for Sustainable Development in Africa; A Case Study of Taxation in the Nigerian Oil and Gas sector.' Presentation at Integrated Social Development

- On-shore Operations are 5 per cent of the asset cost
- Off-shore Operations
 - Water depth of up to 100 meters – 10 per cent;
 - Water depth of between 100 - 200 meters - 15 per cent;
 - Water depth of beyond 200 meters - 20 per cent
- PSC Companies that signed their contract agreements prior to 1st July 1998- 50per cent.
- Investment Tax Credit (ITC): This is a tax-offset, which is deductible from assessable tax and claimable by the PSC companies in deep water exploration and production that signed their contract agreements prior to 1st July 1998. The applicable rate under the Deep Offshore and Inland Basin Production Sharing Contract Act is currently 50 per cent for companies with QCE.
- Investment Tax Allowance (ITA): This is granted to Production Sharing Contract (PSC) Companies that signed their contract agreements after 1st July 1998. It is computed by applying 50 per cent flat rate on QCE which is added to capital allowance and deducted from assessable profit.
- Balancing Allowance: This is an allowance granted to petroleum companies if the tax written- down-value exceeds the income received on disposal of a QCE asset.
- Provisions for Losses: Losses can be carried forward and recouped from future profits indefinitely for the companies.
- Concessionary Profit Taxes: These are reduced tax rates granted to PSC companies in order to encourage and increase investments and cushion the effect of high cost and risks involved in the upstream sector/deep offshore waters (water depths over 200 meters) and the inland basin areas. New companies in the onshore waters are also granted reduced tax rates to encourage operations. The applicable rates are:
 - PPT at 50.0 per cent instead of 85.0 per cent for the duration of the PSC in deep offshore waters
 - PPT at 65.75 per cent instead of 85.0 per cent for the first five years for new companies in onshore operations.
 - Royalties for deep shore PSC are graduated according to water depth as against the 20 per cent for onshore waters as follows;



5.2.1.3 The Gas Sub-Sector

The incentives in the gas sub sector are embedded in the PPTA, Companies Income Tax Act (CITA) and gas policy. While the gas policy mainly provides for incentives that would encourage investments in gas utilisation so as to eliminate gas flaring, the MoU, Gas Finance (Miscellaneous Tax Provision) Act of 1998, PPTA and CITA provide incentives for both upstream and downstream gas operations, including gas utilization. Below are the fiscal incentives available for gas operations:

Gas Transmission, Distribution and LNG Projects

Income Tax: A CIT rate of 30.0 per cent instead of the PPT rate of 85.0 per cent is applicable to transmission and distribution companies, while a PPT of 45 per cent is applicable to LNG projects;

Capital Allowance: This is a tax deductible and applicable at 20.0 per cent annually in the 1st – 4th year of operation, 19 per cent in the 5th year and 1 per cent in the books for transmission and distribution companies, while for LNG projects it's applicable at 33 per cent per annum on straight-line basis in the 1st -3rd year with 1 per cent in the books;

Investment Tax Credit: This is also tax deductible and its applicable at 5.0 per cent for companies in the first two phases and 10.0 per cent for LNG projects;

Royalty: This is applicable at 7.0 per cent onshore operations and 5.0 per cent offshore operations for all phases;

Tax Holiday: This is a period of exemption from tax payments granted a company in its formative years under a pioneer status in Nigeria, so as to enable it to make appreciable profit for re-investment into the business. The applicable period is 3 years which is renewable for another 2 years on the basis of satisfactory performance by transmission and distribution companies.

Upstream Gas Utilization: This is defined as activity involved in the separation of oil from petroleum in the reservoir for usable products, or the delivering of the gas to designated points for use by downstream users and includes gas production (Atuokwu, 2009)⁴⁸. Section 10A of the PPTA as amended, specified the fiscal incentives in this phase as follows:

- **Allowable Deductions:** All funds invested in the separation of crude oil and gas from the reserves into suitable products are considered as part of the oil field development and taken as deductibles for tax purposes. Capital investment on facilities and equipment used to deliver associated gas in usable form at utilization or transfer points is treated, for tax purposes, as part of the capital investment for oil development, though section 11c of the PPTA provides that capital employed in improvement, as distinct from repairs, is not an allowable deduction (Atuokwu, 2009);
- **Capital Allowances:** Capital allowances, operating expenses and basis of tax assessment, which can serve as reimbursable expenses against oil income are subject to the provisions of the Petroleum Profit Tax Act (PPTA) and the Nigerian National Petroleum Corporation (NNPC) revised MOU with the joint ventures.

Gas Utilization (Downstream Operations): This is defined under Section 28G (3) of Company Income Tax Act (CITA) (as amended) and Section 4 of the Finance (Miscellaneous Tax Provisions) Act, 1998 as the marketing and distribution of natural gas for commercial purposes, including the establishment of power plants, liquefied natural gas plants, gas to liquid plants, fertilizer plants, and gas transmissions and distribution pipelines (Atuokwu, 2009). The incentives applicable in the sub-sector include:

- **Tax Holiday:** This is applicable as in the upstream

gas utilisation

- **Petroleum Investment Allowance (PIA):** A company is qualified to make a claim of 35 per cent PIA on Qualifying Capital Expenditure (QCE) if it did not take advantage of the tax holiday or 15 per cent if it had taken advantage of the tax holiday;
- **Accelerated Capital Allowances:** Allows greater deductions for capital allowance in the earlier years of an asset with a qualifying capital expenditure. It is applicable at 90 per cent on plant and machinery with 10 per cent retention in the books after the tax holiday period.
- **Tax Deductible Interest on Loans:** Applicable tax to companies is 30 per cent CIT instead of the 85 per cent PPT and interest on loans for gas projects is to be tax deductible provided that the prior approval had been obtained from the Federal Ministry of Finance before taking the loan;
- **Tax Free Dividends:** All dividends distributed during the tax holiday are not taxable provided that the downstream investment is in imported capital or plant and machinery that is not less than 30 per cent of the companies' equity share capital.
- **VAT Exemptions on Plant and Machinery:** VAT is charged at 0 per cent for plants, machinery and equipment purchased for gas utilisation.

5.2.2: Power Sub-Sector

To harness the potentials of the power sub sector, certain tax incentives have been put in place to encourage investors into the sector. The incentives as outlined by the Nigerian Electricity Regulatory Commission (NERC) and Nigerian Investment and Promotion Council (NIPC) include:

- **New Multi Year Tariff Order (MYTO):** The Nigerian Government provides a 15-year commercial tariff path for the electricity industry with minor and major bi-annually review arising from changes in inflation rate, exchange rate, gas prices etc. The review is also done every five years so as to ensure adequate returns on investments. The MYTO is based on the building blocks approach,

⁴⁸ Atuokwu, C. (2009). 'Taxation for Sustainable Development in Africa; A Case Study of Taxation in the Nigerian Oil and Gas sector.' Presentation at Integrated Social Development

which combines the positive attributes of rate of return regulation and price caps.

- **Tax Holiday:** It is used to encourage enhanced return for the expansion of the business during the formative years of a company. Manufacturers of electrical products, including parts or equipment for other appliances, electrical wires, transmission cables or cable sets etc. are exempted from the payment of income tax or given a period of graduated tax holiday of 10-20 years based on the amount of investment ranging between US\$50 million and US\$200 million.
- **Corporate Income Tax (CIT):** All companies in the industry are subjected to 30 per cent corporate income tax, however, independent power generation companies utilizing gas, coal and renewable energy sources are entitled to 50.0 per cent reduction in CIT on net profits for five year after expiration of the tax holiday.
- **Import Duty Exemption:** Zero per cent (0per cent) import duty is granted on power generation equipment that uses Nigerian gas as source of power as well as machinery, spares and consumables for the installation and commissioning of projects before the start of the business, excluding test runs.
- **Tax Relief for Research and Development (R&D):** Companies are expected to improve their products and services through research and development. Up to 150 per cent of the expenses on research and development in the electricity industry is tax deductible for both existing and new companies.
- **Tax Concession on Nigerian Employees:** Companies are encouraged to hire and train indigenous employees through the tax concession on in-plant training initiative. Companies that engage in manufacturing in the power sector are granted 20.0 per cent tax deduction on the cost of local staff employed, directly or through contracts, based on a minimum of 100 employees. A 2 per cent tax concession between 5 and 15 years based on the quantum of investment is also granted to these companies for in-plant-training.
- **Incentives for Providing Infrastructure:** Companies in the electricity industry are also encouraged to invest in the provision of infrastructure that should have been provided by the government through specified tax incentives. Tax

concession to the tune of 35.0 per cent of the cost of the infrastructure facility is granted and distributed over a five-year period. The tax concession is capitalized during the period of the tax holiday.

5.2.3: Manufacturing Sub-Sector

A number of fiscal incentives have been mapped out by government to stimulate the growth in the manufacturing sub-sector and reposition it as the engine of growth in the economy. The goal is to achieve both social and economic benefits, among which increased investment, industrialisation, job creation, value addition, local content development etc. The incentives in the sector include:

- Capital Allowance:** The rate of capital allowance per annum is restricted to 75.0per cent of assessable profit for companies in the manufacturing sector.
- Reduced Company Income Tax:** Companies with turnover of less than N1.0 million in the manufacturing sector pay CIT of 20 per cent instead of 30 per cent in the first five years of operations. Also, dividends from such companies are tax free for the first five years. In addition, dividends from manufacturing companies in the petrochemical and liquefied natural gas sub- sector are tax free.
- Reinvestment Allowance:** Manufacturing companies that incur qualifying capital expenditure for approved expansion of production capacity, modernization of production facilities and diversification into related products are entitled to a generalized capital investment allowance on their capital expenditures.
- Manufacture-In-Bond Scheme:** The scheme is designed to encourage manufacturers to import raw material inputs and other intermediate products duty-free for production of exportable goods, backed by a bond issued by any recognized financial institution. The bond is discharged after evidence of exportation and repatriation of foreign exchange has been produced (NIPC, 2009)49.
- All equipment for processing cassava flour for composite flour blending shall be imported duty free (effect from 31st March 2012)**

vi. Corporate tax incentives rebate of 12 per cent shall be enjoyed by Bakers on attainment of 40 per cent cassava blend within a period of 18 months.

5.2.4: The Agricultural Sub-sector

The agricultural sector is central to Nigeria's economy; accounting for 40 per cent of the Gross Domestic Product (GDP) and providing employment for over 60 per cent of the labor force in order to encourage investment in agricultural sector the following incentives are applicable:

1. With effect from 31st January 2012 agricultural machinery and equipment shall attract zero per cent (per cent) duty in order to support the development of the sector.
2. A five-year tax holidays for companies that are granted pioneer status;
3. Interests earned by financial Institutions on loans granted for agricultural trade or business are tax exempt;
4. Company is entitled to unrestricted capital allowances;
5. Machinery and equipment purchased for agricultural purposes are exempted from Value Added Tax (VAT);
6. Losses can be carried forward indefinitely;
7. Agro-allied plant and equipment enjoy enhanced capital allowance of up to 50 per cent;
8. All agricultural and agro-industrial machines and equipment to enjoy 1 per cent duty;
9. Interest Drawback Programme (IDP); under the IDP, farmers could borrow from lending banks at market-determined rates, while the programmes pay an interest rebate of a determined percentage (40.0 per cent) to farmers who repay their loans on schedule;
10. Agricultural Credit Guarantee Scheme Fund (ACGSF) administered by the Central Bank of Nigeria provides up to 75.0 per cent guarantee for loans granted by the commercial banks for approved agricultural activities;
11. Commercial Agricultural Credit Scheme (CACs), The Scheme was established in March 2009 by the CBN in partnership with the Federal Ministry of Agriculture and Rural Development (FMARD) to fast track the development of commercial agriculture in the country. The applicable interest rate under the fund is retained at 9.0 per cent. The fund is disbursed through the deposit money banks (DMBs).

12. Agricultural Credit Support Scheme (ACSS), the ACSS is granted at 14.0 per cent interest rate, while beneficiaries who fully repaid their loans on schedule are entitled for a refund of 6.0 per cent of interest paid.
13. The Nigerian Incentive-Based Risk Sharing system for Agricultural Lending (NIRSAL) is a five pillar programme to be addressed by an estimated US\$ 500 million of CBN fund that will be invested as follows:
14. Risk-sharing Facility (US\$300 million). This component would address banks' perception of high risks in the sector by sharing losses on agricultural loans.
15. Insurance Facility (US\$30 million). The primary goal is to expand insurance products for agricultural lending from the current coverage to new products, such as weather index insurance, new variants of pest and disease insurance etc.
16. Technical Assistance Facility (US\$60 million). This is to equip banks to lend substantially to agriculture, producers to borrow and use loans more effectively and increase output of better-quality agricultural products.
17. Holistic Bank Rating Mechanism (US\$10 million). This mechanism rates banks based on two factors, the effectiveness of their agricultural lending and the social impact and makes them available for the public.
18. Bank Incentives Mechanism (US\$100 million). This mechanism offers winning banks in Pillar four, additional incentives to build their long-term capabilities to lend to agriculture. This will be in terms of cash awards.

5.2.5: The Telecommunications Sub-sector

The statutory framework for investments provides specific measures that are meant to encourage investors, guides investments in the Nigerian telecom market. The government has provided an enabling environment to attract investors, with the introduction of a package of incentives in the telecommunication subsector. These include:

1. Pioneer status for five years under the industrial development income tax relief Act 1990 for interested investors who want to set up plants for the manufacture of telecom equipment in the country;

2. Exclusivity period for licenses (e.g. 5 years for GSM licenses, 3 year for long distance international gateway operators);
3. Import duty for all telecom equipment reduced from 25 per cent to 5 per cent for two years from August 2001;
4. A tariff structure which enables investors to recover their investment over a reasonable period of time;
5. Measures to ensure speedy clearance of goods at the ports etc.
6. The Nigerian Investment Promotion Commission Act of 1995 which regulates foreign investment provides for the unconditional transferability of funds into and out of Nigeria, on the condition that this is done through an authorised agent;
7. Guarantee of long-term loans at minimal interest rates for telecom operators;
8. Granting of exclusivity to telecom operators, typically to provide fixed telecom services for specified number of years. This implies some sort of monopoly status for the operators.

5.2.6: Export Incentives and Free Trade Zone

5.2.6.1: Export Incentives

- A. Duty Drawback Scheme: This provides for refund of duties/charges on raw materials including packing and packaging materials used for the manufacture of products upon effective exportation of final products (NIPC, 2009)⁵⁰. The scheme allows for a 60 per cent refund on duties/charges, which is automatically granted to the exporter at the initial screening by the Duty Draw Back Committee. The refund amount is liquidated after the final processing of the application, while the Committee is authorised to approve the request for claim of any payment where applicable.
- B. Duty Drawback Facility: This scheme provides for both fixed and individual drawback facilities. The fixed drawback facility is for those exporters/producers whose export products are listed

- in the fixed drawback schedule to be issued from time to time by the Committee, (NIPC, 2009). On the other hand, the individual drawback is for producers/exporters that do not qualify under the fixed drawback facilities. It is therefore a straightforward traditional drawback mechanism under which duty is paid on all inputs. The duties are consequently rebated on inputs used for export production (NIPC, 2009).
- C. Export Expansion Grant (EEG) Scheme: This is an incentive with the main objective of stimulating export-oriented activities that will bring about significant growth in the non-oil export sector. The exporter shall be a manufacturer or merchant of product of Nigeria origin for the export market. The export must be registered with the Nigerian Investment Promotion Council (NIPC) and must have a minimum annual export turnover of N5.0 million and evidence of registration of products for export. The weighted eligibility criteria in assessing the EEG have four Bands: 25 per cent, 20 per cent, 10 per cent and 5 per cent (NIPC, 2009).
 - D. Export Development Fund Scheme: The scheme provides financial assistance to private sector exporting companies to cover part of their initial expenses in respect of the following export promotion activities:
 1. Advertising and publicity campaigns in foreign markets;
 2. Export market research and studies;
 3. Production design and consultancy;
 4. Participation in trade missions, buyer-oriented activities, Overseas trade fairs, exhibitions and sales promotion;
 5. Cost of collecting trade information; and
 6. Backing-up the development of export oriented industries (NIPC, 2009).
 - E. Trade Liberalisation Scheme: This is an export liberalisation incentive primarily geared towards export activities within the ECOWAS sub-region. The aim is to considerably enlarge intra-community trade activities in the region through the elimination of tariff and non-tariff barriers in trade emanating from member countries. The scheme offers preferential access to the ECOWAS market from Nigeria.

<https://www.cbn.gov.ng/Publications/guidelines/dfd/acgsfdpguideline>

⁴⁹ NIPC (2009). 'Investment Policies in Nigeria,' Nigerian Investment Promotion Commission (NIPC) <http://www.nipc.gov.ng/>

⁵⁰ NIPC (2009). 'Investment Policies in Nigeria,' Nigerian Investment Promotion Commission (NIPC) <http://www.nipc.gov.ng/>

5.2.7: Free Trade/Export Processing Zones

In order to create a business-friendly environment, the Federal Government in 1991 passed an aggressive Free Trade Zone law which allows interested parties to set up industries and businesses within the designated zones. This is with the objectives of exporting the goods and services manufactured or produced within the zones. Incentives include tax holiday; unrestricted remittance of profits and dividends earned by foreign investors; no import or export licenses required; up to 100 per cent foreign ownership of enterprises; permission to sell up to 25 per cent of production in the domestic market; etc.

The Oil and Gas Export Free Zone was established by Decree No. 8 of 1996. The Decree provides for an incentive-driven and attractive environment for business in the oil and gas sector. The objective of the zone is to motivate both foreign and local investors for increased investments in the oil and gas sector so as to increase the nation's oil reserves, enhance government to take and provide basis for technological transfer. There are currently three oil and gas free zones in Nigeria with enhanced stacking and warehousing facilities for investors. They comprise: the Onne, Calabar, and Warri Oil and Gas Free Zones. Fiscal incentives in the zone include:

- i. All companies operating in the zones are exempted from payment of all Federal, State and Local Governments taxes, including rates and levies;
- ii. All goods imported into the zones are duty free;
- iii. There is 100 per cent guarantee on foreign capital, profits and dividends repatriation;
- iv. There is no expatriate quota and foreign exchange regulation;
- v. There is no pre-shipment inspection for goods imported into the free zones;
- vi. The operators in the zone are not required to process import or export License;
- vii. Companies are to enjoy rent free land at the construction stage;
- viii. There is no restriction on profits and dividend remittances by foreign investors;
- ix. There would be no strike and lock-out for ten-years after the commencement of operations in a zone (Elebiju, 2008)⁵¹;
- x. There is 100 percent foreign ownership of company/investment.

6.0: Tax Incentives of other Progressive Countries and Comparison with Nigeria

6.1: Brazil

The Brazilian government is making efforts at improving the climate for foreign investment as it seeks to develop a more market-oriented economy. Import barriers have been reduced and many state-owned enterprises have been privatised. Over a decade ago, the federal government increased foreign investment and export incentives. State and municipal governments also continue to provide tax and other incentives for investments in their regions. Many local governments, especially those in the North and Northeast of Brazil, offer significant incentives to attract businesses to their regions. Some of the incentives include deferment or reduction of the state-based value added tax (VAT), free land or frees building leases, and exemption from municipal service tax (ISS), in addition to the regional or industry-specific incentives.

There are three basic laws supporting investment incentives in Brazil. These are;

- (i) Law No. 4131/62 (Foreign Direct Investment Law) and Law No. 4390/64, (ii) Executive Order No. 55762/65, and
- (iii) The constitution of Brazil (Elisiode, 2004)⁵².

Investment promotion strategy began in Brazil in 1990 with the establishment of the Ministry of External Relations' System of Investment Promotion – SIPRI (Immigration Consulting Services, 2012)⁵³. Also, in 1991, the Asuncion Treaty was signed between Argentina, Brazil, Paraguay and Uruguay with the ultimate aim of creating a common market. The Treaty later eliminated import/export duties and legalized a customs union among member countries in 1994 (Foreign Trade Information System, 2009)⁵⁴. When Brazil amended its constitution in 1998, the distinction between local and foreign investors was eliminated. Since then, sectors that were hitherto restricted to foreign investors such as petroleum, telecommunications, mining and power was declared open to foreign investment (Encyclopedia of the Nations, 2012)⁵⁵.

Similarly, Amendment Act No. 123 of 2006 strengthens the principles guiding investment activities. The new Act thus created a special tax regime, which allows small companies to enjoy a simplified tax system and more favorable investment conditions (Elali & Zilveti, 2006)⁵⁶.

In 2004, the Commission for the Promotion of Private Productive Investment, popularly referred to as the 'Investors Room' was established within the Presidency with the objective of facilitating domestic and foreign investment in Brazil. In addition, the Commission is made to coordinate the activities of public investment promotion institutions. These institutions include:

- Investment unit of the APEX-Brazil in the Ministry of Trade and Industry set up in December 2004 to promote foreign investment;
- National Network of Investment Agencies (RENAI) which was set up in 2003 for state and regional investment promotion; and
- Integrated System for Investment Promotion and Technology Transfer to the Enterprises (SIPRI), which is an information network for articulating investment strategies to attract investment (Immigration Consulting Services, 2012)⁵⁷.

6.1.1: General Incentives

Overall, Brazil offers a lot of incentives as means of attracting investment and fostering the development of less developed regions in the country. A corporate income tax reduction of 12.5 per cent is granted to companies engaged in ventures considered to be a priority for the development of these underdeveloped areas. Such companies are also entitled to deposit of up to 30.0 per cent of the income tax due.

⁵¹ Elebiju, A. (2008) 'Free Trade Zone and Nigerian Tax Regimes.' Being Presentation at CITN MPTP, Ibadan, 25.06.08. Retrieved from http://www.templars-law.com/media/citn_presentation.pdf

⁵² Eliside Souza (2004). Doing Business in Brazil, 2004, <http://www.ejupes.adv.br/ingles/1.pdf>.

⁵³ Immigration Consulting Services, (2012). 'Investment Incentives in Brazil,' 2012, <http://www.imigrabrazil.com/Market-Analysis/Investment-Incentives-in-Brazil.html>

⁵⁴ Foreign Trade Information System (2009). Treaty Establishing a Common Market Between Argentina, The Federal Republic of Brazil, the Republic of Paraguay and the Eastern Republic of Uruguay, retrieved from http://www.sice.oas.org/trade/mrcsr.TreatyAsun_e.asp#CHAPTER_1

⁵⁵ Encyclopedia of the Nations, 'Brazil—Foreign Investment,' 2012, http://www.nationsencyclopedia.com/Americas/Brazil_FOREIGNINVESTMENT.html

⁵⁶ Elali, P.A. and Zilveti, F. (2006). 'Tax Incentives for National and Regional Development in Brazil'. ISSUU Publications, http://issuu.com/midiadesk/docs/palestra_-_and

In order to promote technological development, agro-industrial technology development programmes allow for:

- I. Accelerated depreciation and amortization of domestically produced equipment of twice the applicable depreciation rate;
- II. Deduction of research and development expenses for industrial and agriculture technology calculated on the total income tax due limited to 4.0 per cent;
- III. Withholding tax credit of 10.0 per cent on the cross-border remittance of royalties, technical assistance and specialized services fee; and reduction of 50.0 per cent of withholding taxes on remittances of royalties and technical services fees, (Ernst & Young, 2011)⁵⁸.

Free Trade Zones are also created in Brazil. According to Ernest and Young, the Manaus Free Trade Zone (MFTZ) was created as a free trade area offering special tax incentives in order to attract investment to remote areas in the Amazon region. Foreign goods used in the Zone for consumption, manufacture, assembly, or for storage and re-export, are exempted from import duties, (imposto sobre produtos industrializados): tax on industrialized goods, a federal excise tax (PIS) and (Contribuição para o Financiamento da Seguridade Social): social contribution for social security (COFINS) and federal VAT (programa de integração social): employees' profit participation program (IPI). In order to enjoy these benefits, however, a company must obtain prior approval from relevant authorities. Such approvals are usually granted for projects with minimal manufacturing process or those that meet other requirements in the tax legislation. They include:

- a. Import Duty exemption for products for local consumption in the zone;
- b. Import Duty exemption for goods produced for the Western Amazon region;
- c. Import Duty reduction of up to 88.0 per cent is granted on raw materials that are imported through the Zone and used in the manufacturing of goods that are produced for the Brazilian market;

- d. Federal VAT – IPI suspension for goods entering the Zone in addition to a suspension of import duties until goods leave the MFTZ;
- e. Exemption of IPI for products manufactured outside the Zone and destined for the MFTZ; and
- f. Exemption of IPI for manufactured goods destined for domestic consumption in the MFTZ or in the Occidental Amazon region. However, only certain products benefit from this latter provision (Ernest and Young Terco, 2011)

6.1.2: Special Free Trade Zones

Special Free Trade Zones created by Federal decree were formed for foreign companies that invest in plants manufacturing goods for export. For the purposes of customs control, these Zones are not considered to be Brazilian territory. A maximum of 20.0 per cent of the products manufactured in the Zones may be destined to the Brazilian market. However, the following tax and customs exemptions are offered for a period of 20 years to companies operating in the zones:

- a. Suspension of the Import duty, IPI, PIS, PIS-import, COFINS, COFINS-import and AFRMM;
- b. Exemption from customs and administrative restrictions and controls for certain goods imported or exported;
- c. Exemption from withholding tax due on payments for services rendered by foreign companies; and
- d. Exemption from corporate income tax payments during a period of 5 years (Ernest and Young Terco, 2011)⁵⁹.

Similarly, export processing zones were created by state governments in order to reduce the existing regional differences and further promote country's development. Companies established as manufacturers of goods for export are exempted from import duties, social contributions on turnover and financial transactions tax. Warehouse spaces are also provided at

concessionary rates. Also, companies that have gross revenue derived from exports in the preceding year equal to or higher than 70.0 per cent of total export revenue for the following two calendar years are entitled to a special tax regime for the acquisition of capital goods. Such companies will also be exempted from corporate income tax for a period of 5 years beginning from the date of establishment. (Ernest & Young Terco, 2011). Double Taxation Agreement (Tax Treaties) purposely for the avoidance of double taxation was signed by Brazil government with a number of other countries notable among are Argentina, Austria, Belgium, Canada, Chile, China, France, India, Israel, Italy, Japan, Korea, Mexico, Norway, South Africa and Spain (Franco Caiado Guerreiro & Associates, 2011)⁶⁰.

6.1.3: Specific Incentives

6.1.3.1: Oil and Gas Sector

The Oil and Gas sector in Brazil was liberalised with the passage of the Petroleum Investment Law in 1997. The liberalisation scheme has attracted a number of investments in the sector. In order to properly regulate the activities of the sector, the National Petroleum Agency (ANP) was established and incentives were provided by government to foster growth in the sector. Some of these incentives include the removal of state monopoly of oil and gas exploration and subsidy grants. The government has also put in place a special custom regime for importation of materials to be in the exploitation of petroleum and natural gas, which ensures that materials are duty free, Ernest and Young Terco, (2011). The Brazilian government has adopted a Production Sharing Agreement (PSA) with investors in the Oil and Gas sector where the oil company bears all the costs and risks of exploration, evaluation, development and production. When oil is discovered in commercial quantity, the oil company is thus granted the right to recover costs, the right to the volume of production and the right to a profit based on an agreed sharing formula (Deloitte, 2011)⁶¹.

<https://home.kpmg › home › insights › 2018/10 › brazil-indirect-tax-guide>

⁵⁹ Immigration Consulting Services, (2012). 'Investment Incentives in Brazil,' 2012, <http://www.imigrabrasil.com/Market-Analysis/Investment-Incentivesin-Brazil.html>

⁵⁸ Ernest & Young Terco. (2011), 'Doing Business in Brazil. FAO (2011). 'Foreign Agricultural Investment Country profile - United Republic of Tanzania', Retrieved from http://www.fao.org/fileadmin/user_upload/tcsp/docs/Tanzania_Country_Profile_Final.pdf

In order to foster the growth of the oil and gas industry, a special custom regime known as REPETRO (Regime Aduaneiro Especial de Exportação e Importação de Bens Destinados às Atividades de Pesquisa e de Lavra das Jazidas de Petróleo e de Gás Natural) was formed. The REPETRO is applicable to certain products listed in the Law. The REPETRO allows for the importation of raw material to be used in the industrialization process with import duty, PIS, COFINS and IPI suspension. In addition, it grants import duty, PIS, COFINS and IPI suspension upon importation of finished goods under the temporary admission regime (Ernst and Young Terco, 2011).

6.1.3.2: Manufacturing Sector

In the manufacturing sector, the Brazilian government introduced incentives such as tax benefits, credits and exemptions to stimulate the industrial sector so as to foster manufacturing and ensure economic growth. They include:

The Inovar-Auto, which was created solely for promoting technological development and innovation for automotive manufactures. This incentive grants tax credits to companies engaging in the manufacturing of cars;

The Padis, which was introduced in 2007 to improve technological development of the semi-conductor industry. The Padis provides a reduced income tax for manufacturing companies as well as tax exemptions to purchase raw materials to companies in this industry; and the reduction of social security contribution rates from 2.5 per cent and 1.5 per cent to 2.0 per cent and 1.0 per cent, respectively, depending on the type of manufacturing company (KPMG, 2012).

6.1.2: Telecommunication Sector

Incentives are also provided for investors in the telecommunication sector. These incentives include the provision of credit and customs duties relief. Law No. 176 of

2001 exempted companies from the payment of taxes on industrialized products. Currently, the exemptions have been converted into reductions of the rates, and the percentage reduction is due to be gradually reduced (Foreign Relations Ministry Brazil, 2006).

6.1.3.4: Outcomes

An evaluation of the implementation of tax incentives in Brazil indicates that it has been successful in attracting investment and raising the level of exports in the country. Prior to the creation of the Free Zone, the entire area was remote and underdeveloped. With the implementation of tax incentives, however, the zone attracted a lot of manufacturing companies and has succeeded in increasing the exports of the country. This development largely resulted from the exemption granted on income tax. Notwithstanding the remote location and substandard infrastructure, the zone now has a strong industrial base and has attracted a significant number of immigrants to the region. In addition, goods manufactured within the region currently compete favorably with similar foreign products.

Also, the amendment of the constitution in 1995, which eliminated the restriction of foreign investors from investing in the petroleum, telecommunications, mining and power sectors, attracted more foreign investment. Thus, following the implementation of these policies, the contribution of exports of goods and services to GDP recorded a remarkable increase from 9.9 per cent in 2007 to 11.4 per cent in 2008 (OECD, 2012)⁶².

The Inovar-auto incentive in the manufacturing sector has been very instrumental for attracting foreign investment to automotive manufactures. The Brazilian auto sector is currently the 4th largest sales market globally. From the period 2005 to 2011, the market averaged 12.0 per cent annual growth (Price Waterhouse Coopers, 2012)⁶³. More job opportunities have also been created as there is a requirement for all

⁵⁹Ernest & Young Terco. (2011), 'Doing Business in Brazil, FAO (2011). 'Foreign Agricultural Investment Country profile - United Republic of Tanzania', Retrieved from http://www.fao.org/fileadmin/user_upload/tcsp/docs/Tanzania_Country_Profile_Final.pdf

⁶⁰ Franco Caiado Guerreiro & Associates (2011). 'Investor's Guide to Brazil', Retrieved from www.fcguerreiro.com

⁶¹ Deloitte (2012). 'International Tax: Ghana Highlights, <http://www.deloitte.com/assts/DcomGlobal/Localpercent20>

and percent20Investmentpercent20Guides/2012/dttl_tax_highlight_2012_Ghana.pdf

companies, whether local or foreign to hire local (Brazilian) personnel as employees to a proportion of two-thirds, while the remaining one-third could be foreign employees. With the increase in the number of investors, more job opportunities have been created (Latin Lawyer, 2013)⁶⁴.

In general, incentives in Brazil have generally impacted positively on the economy as evidenced by the performance of key macroeconomic indicators. For instance, the contribution of exports of goods and services to GDP improved significantly

From **9.9%** in 2007 to **11.4%** in 2008. **9.0** per cent in 2009 and rose slightly to **9.3** per cent in 2010. Overall, the GDP grew consistently from **1.1** per cent in 2003 to **5.7** per cent in 2004. It declined to **3.2** per cent in 2005 and thereafter rose to **6.1** per cent in 2007. With global economic crisis in 2007, the growth rate of GDP declined to **5.2** per cent and **0.6** per cent in 2008 and 2009, respectively, but increased to **7.5** per cent in 2007 (OECD, 2012)⁶⁵.

Though Brazil's tax incentives have performed very well, there still remain a few challenges. Some of these challenges include the

difficulty in controlling the existing internal contraband which has led to violence and bribery of government officials (Byrne, 2002)⁶⁶. This has hindered the full actualisation of the potentials of incentives in the country. In addition, benefits of incentives provided in the Amazon and Northeast regions remain highly controversial as the two regions still remain at very different levels of development.

In addition, inadequate infrastructure limits the potential of the tax incentives to attract more investments. However, the Brazilian government in mitigating this provides incentives to companies investing in the development of infrastructure. Such companies are exempted from payment of social contribution and federal contribution taxes on local acquisition and importation of machinery to be used for the development of infrastructure.

6.2: Kenya

The Kenyan Investment Authority (KIA) is the institution vested with the statutory responsibility of promoting and coordinating investments in Kenya. It was established in 2004 by the Investment Promotion Act (IPA) No. 6 of 2004 (Kenyan Investment Authority, 2004)⁶⁷. Kenya's constitution provides guarantees against expropriation of private property for security or public interest and ensures that compensation is guaranteed. Similarly, the Foreign Investment Protection Act (FIPA) also guarantees capital repatriation, as well as remittance of dividends and interest (Kenya Embassy, Moscow).

⁶² OECD (2012). 'Country Statistical Profiles', http://www.oecdlibrary.org/economics/country-statistical-profile-brazil_csp-bratable-en

⁶³ Pricewaterhouse Coopers (2012). Autofacts; Brazi: Inovar Auto Overview. <http://www.fkg.se/wp/wp-content/uploads/2014/02/PWC- brazilinnovar- auto-overview.pdf>

⁶⁴ LatinLawyer (2013), The Business Law Resource for Latin America, Retrieved from latinlawyer.com/reference/topics/47/jurisdictions/6/brazil

⁶⁵ OECD (2012). 'Country Statistical Profiles', http://www.oecdlibrary.org/economics/country-statistical-profile-brazil_csp-bratable-en

⁶⁶ Byrne, P. (2002). 'Tax Incentives for Foreign Direct Investment in Seven Latin American Countries, Inter-American Development Bank, Washington,

Retrieved from <http://publications.iadb.org/bitstream/handle/11319/1243/Tax%20incentives%20for%20FDI%20in%20seven%20Latin%20American%20Countries.pdf?sequence=1>

⁶⁷ Kenyan Investment Authority (2004), Invest in Kenya, <http://www.investmentKenya.com/about-keninvest/theorganization>

⁶⁸ Deloitte (2012). 'International Tax: Ghana Highlights, http://www.deloitte.com/assts/DcomGlobal/Localpercent20andpercent20Investmentpercent20Guides/2012/dtt_tax_highlight_2012_Ghana.pdf

⁶⁹ Institute of Economic Affairs (2012). 'Tax Incentives and Exemption Regime in Kenya. Is it working?'

6.2.1: General Incentives

Kenya offers a lot of incentives as a means of attracting investment. These incentives include:

- a. Income Tax Deductions for local and foreign companies which are levied at 30.0 per cent and 37.5 per cent, respectively. Newly listed companies are levied between 20.0 - 27.0 per cent for 3–5 years after the year of listing, which is calculated as a percentage of the capital listed;
- b. Carry forward losses which have no time limit (Deloitte, 2012)⁶⁸;
- c. Provision of Capital Investment Allowances (CIA) for companies investing in capital projects. Within the CIA, the Investment Deduction Allowance (IDA) was introduced in 1991 to encourage investment in physical capital. It is currently fixed at 100.0 per cent but attracts an extra 50.0 per cent for investments with values above Kshs.200 million operating outside the urban municipalities of Nairobi, Kisumu or Mombasa (Institute of Economic Affairs, 2012)⁶⁹.
- d. Depreciation Allowance as follows: (i) 2.5 per cent on industrial buildings; (ii) 4.0 per cent on hotels; (iii) 12.5 per cent on plant and machinery; 25.0 – 37.5 per cent on motor vehicles, trucks and tractors; and (iv) 30.0 per cent on office equipment (King'etich, n.d.)
- e. Import Duty Set-off allows import duty paid on the importation of capital goods to be set off against payable income tax (USA-Kenya Chamber of Commerce, 2008)⁷⁰.

Incentives geared towards export promotion have been provided by the Kenyan Government. The main scheme is the Export Processing Zones (EPZs) which were established in 1990 with the enactment of the Export Processing Zones Act of Parliament Cap. 517. The EPZs which are managed by the Export Processing Zones Authority (EPZA) provide incentives to export-oriented investments. Companies operating within the EPZs enjoy the following incentives:

- i. 10-year Corporate Tax holiday and thereafter 25.0 per cent tax;
- ii. 10-year Withholding Tax holiday on remittance of dividends;
- iii. Exemption from Import duties and VAT on raw materials and intermediate inputs;
- iv. Exemption from Stamp duty; and,
- v. 100.0 per cent investment deduction over 20 years on initial investment.

Currently, there are more than 40 companies operating in the EPZs and are mandatorily required to export at least 80.0 per cent of their products (Kenya embassy, 2005)⁷¹. Other incentives include the signing of a Double Taxation Treaty by the Kenyan Government with a number of countries for the avoidance of double taxation. Countries that are engaged in such treaties with Kenya include Canada, Denmark, Germany, India, Norway, Sweden, United Kingdom and Zambia. Treaties by other countries, such as Italy, Tanzania and Uganda have been signed but not fully ratified (Kenya Revenue Authority).

6.2.2: Sector Base Incentives

In order to promote investment in the manufacturing sector, the Kenyan government introduced the following incentives:

- a. The Manufacture under Bond (MUB) was introduced in 1986 in order to encourage both local and foreign manufacturers to increase production and exports. The MUB is administered by the Kenya Revenue Authority (KRA). Manufacturing companies operating under the programme are exempted from Import Duty and VAT on imported raw materials, as well as 100.0 per cent investment allowance on plant and machinery;
- b. The Tax Remissions Export (TRE) is granted to local manufacturers operating outside the EPZs in order to encourage them to increase production as well as export. The scheme essentially involves refunds on VAT incurred by an investor on the

⁷⁰ USA-Kenya Chamber of Commerce, (2008). Retrieved from http://www.senacare.com/sites/senacare/res/kenya_pressrelease.pdf

⁷¹ Kenya Embassy (2005), Handbook on Importing and Exporting in Kenya, Trade Facilitation Project, available at <https://www.kenyaembassy.com/pdfs/handbookimportingexporting.pdf>

⁷² Institute of Economic Affairs (2012). 'Tax Incentives and Exemption Regime in Kenya. Is it working?'

- purchase of raw materials and goods utilized in the production of goods for export. A tax remission certificate is then issued to manufacturers;
- c. The Duty Drawback is granted to exempt payment of Import Duty on goods imported for use in the manufacture of exports or goods to be transferred to a free port or an EPZ (Kenya embassy, 2005)
 - d. Industrial Building Allowance (IBA): This was introduced in 1974 as an incentive to encourage investment in buildings for industrial purposes. The IBA attracts 2.5 per cent and 10.0 per cent for investment in buildings used for manufacturing and hotels, respectively. This is usually calculated on a straight-line basis (Institute of Economic Affairs, 2012)⁷².

In the agricultural sector, the Farm Works Deductions (FWD) was introduced in 1985 to enhance capital accumulation and equipment modernization in the agricultural sector. It is also calculated on a straight-line basis for 5 years of income at a rate of 20.0 per cent (Institute of Economic Affairs, 2012).

In the mining sector, the major tax incentive provided for investors is the Mining Deductions Allowance (MDA). This is granted as a form of reduction in the capital expenditure of mining explorers. For the first year, it is calculated at a rate of 40.0 per cent, and thereafter 10.0 per cent for the next 6 years (Institute of Economic Affairs, 2012). Government is in the process of reviewing its mining and mineral laws to provide for more incentives.

In addition to the general incentives provided by the Kenyan Government to attract investors, investors in tourism are entitled to waivers of Customs Duties and VAT, particularly those interested in building hotels. Investors in tourism are also allowed to import cars for personal use which are duty free (Tourism Investment Conference, 2007)⁷³.

6.2.3: Outcomes

Tax incentives in Kenya as in other countries are meant to promote both local and foreign investment. The Mining Deductions Allowance MDA has resulted in the reduction of cost

of production for investors in the mining sector, thus, attracting more investors. Exploration has been diversified to include a wider range of mineral resources such as titanium. Similarly, exploration has been extended to different parts of the country including the Indian Ocean coast and more companies have been granted licenses for gold and base metal exploration. The investment incentives granted in the agricultural sector have been instrumental in attracting investment as the sector has witnessed tremendous growth. Over 30.0 per cent of agricultural produce are exported, with output comprising about 60.0 per cent of total exports in Kenya. The sector currently contributes about 24.0 per cent of GDP. The Livestock sub-sector which is one of the largest within the agricultural sector currently accounts for almost 90.0 per cent of employment and 95.0 per cent of family incomes within the arid and semi-arid lands.

The investment incentives provided in the EPZs have had a positive outcome on investment. There are currently more than 40 EPZs with a large number of foreign investors. In 2003 the total number of companies operating in the EPZs was 66 and rose slightly to 68 in 2005. By 2007, the number increased to 72 and rose to 83 in 2009. Also, the EPZs have witnessed steady growth especially with the passage into law the African Growth and Opportunity Act (AGOA) which ensured duty-free access to the US. Currently, more than half of the manufactured products from the EPZs are exported to the US market under the AGOA.

Tax incentives in Kenya have, however, resulted in significant revenue losses. Revenue losses resulting from tax incentives have been estimated to be over Kshs. 100 billion (US\$1.1 billion) annually. From the period 2003 to 2009, revenue loss as a percentage of corporate tax collected averaged 21.10 per cent. Similarly, revenue loss from trade related incentives, specifically, the EPZs, MUB and TREO as a percentage of total import duty averaged 37.30 per cent during the same period (Institute of Economic Affairs, 2012)⁷⁴.

Overall, investment incentives in Kenya though laudable, have not attracted the expected and desired level of investment. The dismal level of investment notwithstanding the attractive investment incentives is as a result of the hostile investment

⁷³ Tourism Investment Conference (2007). 'Country Profile. Kenya,' East Africa and Indian Ocean, Kampala, Uganda, 27-29 June. http://www.bkconseil.com/espacainformation/documentation/tourism/Kenya_Country_Profile.pdf

⁷⁴ Institute of Economic Affairs (2012). 'Tax Incentives and Exemption Regime in Kenya. Is it working?'

⁷⁵ Tax Justice Network-Africa & Action Aid International (2012). 'Tax Competition in East Africa. A Race to the Bottom? – Tax Incentives and Revenue Losses in Kenya,'

climate caused by political stability, poor governance, corruption, insecurity and inadequate infrastructure. The major attractions for investors include access to local and regional market as well as favourable bilateral trade agreements (Tax Justice Network-Africa and Action Aid International, 2012)⁷⁵.

6.3: South Africa

The Government of South Africa mapped out its macroeconomic policy strategy under the Growth Employment and Redistribution (GEAR) document published in 1996. The GEAR proposed a wide range of policy reforms, the most important of which were gradual trade liberalisation, deregulation of capital control, deficit reduction and stabilisation of the exchange rate. Within this broad orthodox approach, the GEAR also included specific reference to the need for incentives to stimulate 'labour intensive manufacturing investment' as there is a good case for subsidizing this sector in South Africa.

Following the GEAR, the government has adopted a cautious and well-informed approach on incentives, offering both up-front grant and tax relief incentives. There are also a number of parastatal lending institutions offering loans at sub commercial rates. The balance to spend is heavily skewed towards off-budget tax incentives and subsidised finance rather than on budget grants. Since 1994, two ineffectual schemes - the General Export Incentive Scheme and the Tax Holiday Scheme – have been phased out and two significant new incentives targeted at the manufacturing sector – the Motor Industry Development Programme (MIDP) and the Strategic Investment Programme (SIP) – introduced in their place. The processes and procedures surrounding the implementation and execution of these two schemes were in line with international good practice based on international experience. Basically, these incentives are classified under two categories namely general and specific.

6.3.1: General Incentives

Under the Income Tax Act of South Africa, the general incentives scheme grants companies with branches located in South Africa freedom from secondary taxes payable on declared dividends, and levied the taxes on such companies declaring the dividends and not the shareholders. Secondary tax is a tax on dividends by companies that are resident in South Africa. It is

payable on the net amount, which is the dividend declared less the sum of dividend received or accrued during the dividend cycle. It is normally assessed independently of the liability due on corporate tax, making any company with tax losses that declares dividend to be liable to the secondary tax. Accordingly, from March 1993 to June 1994, secondary tax attracted 15.0 per cent, and from June 1994 to March 1996, it attracted 25.0 per cent, while from March 1996 to September, 2007, it was 12.5 per cent.

From October 2007 to March 2012, it was 10.0 per cent, (UNCTAD, 2000)⁷⁶. The Motor Industry Development Programme (MIDP), which commenced in 1995, brought about the reduction in tariffs and the elimination of the requirements on local content as well as partial exemption from import duties. Exporters of automotive goods and services are exempted from VAT, while rebates exist on customs and excise duty on locally produced goods for exports. Duty credits are tradable and could be used to import local content duty-free or sold to provide additional sources of revenue for exporters. Dividends are also exempted from income and withholding taxes on services sub-sector. Thus, manufacturing companies operating branches in South Africa but having effective management outside the country are also exempted from secondary taxes. Exemptions from withholding tax are equally granted on interest accruing to non-residents. To a large extent, exemptions from income tax are likewise granted on interests accruing to non-residents and on companies that are administered from abroad but having branches inside the country.

6.3.2: Specific Incentives

Strategic tax incentives were introduced in South Africa under the backing of the Revenue Laws Amendment Act 2002, which provided the basis for the introduction of strategic fiscal incentives to facilitate industrial investment and promote job creation. The sectors that benefited from these incentives include:

6.3.2.1: Manufacturing

Under the manufacturing sector, investments are expected to be in excess of R50m for it to qualify for tax relief of up to 100per cent for investments into the sector, including information technology.

The strategic investment project incentive covers all manufacturing activities with the exception of tobacco related products; computer related activities and consultancy in areas like hardware, software and data related activities including data processing and database management. The country also provides a 2-year tax holiday for newly established manufacturing companies, provided they meet certain criteria outlined for qualification under the scheme. These criteria include the ability of such companies to provide funding in excess of R3 million for investment in machinery, equipment, plants including buildings, land and construction. Such activities must be new and must not have started before the application for the scheme.

Intending investors are allowed to acquire existing assets but they must make fresh investments in unexploited assets, amounting to the qualifying funding provided above.

Thus, new investments that qualify for the scheme must fall under the eligible areas and must meet the guidelines provided by the Department for Trade and Industry (DTI). Customs duties rebate and exemption of Value Added Tax (VAT) on imported goods, raw materials and components used in manufacturing, processing for exports are granted to all manufacturers and exporters located in the Customs Controlled Area (CCA) designated zones classified under the Industrial Development Zones (IDZs) programme and aimed at promoting manufacturing and competitiveness of the South African exports (Deloitte, 2010)⁷⁷. Furthermore, companies could apply for a maximum tax holiday of six years if they undertake to use it within 10 years of approval and the tax holiday takes effect the same year the investment begins to yield income. The period of tax holiday must run consecutively, such that companies would not discount the years that losses are incurred. Preferential corporate income tax also exists for small business enterprises whose annual turnover does not exceed R14 million beginning from April 2010 to small and medium enterprises development in the country. The following income taxes exist: R0 – R57,000 (0 per cent); R57,001 - R300,000 (10 per cent); and over R300,001 = R24,300 + 28 per cent of amount greater than R300,000 (Deloitte, 2010).

6.3.2.2: Agriculture

A three-year accelerated depreciation of 50, 30 and 20 per cent is granted for specific sectors including agriculture over the period. Companies that attain a certain level of exports can import products free of import duties under a textile, clothing and footwear programme. Such companies are also allowed to use 30 per cent of their export value for textile importation. Under the Small and Medium Enterprise Development Programme (SMEDP), tax free incentives are granted to small and medium enterprises that undertake new projects or expand ongoing projects in large-scale agricultural projects, aquaculture and agro-processing, including manufacturing, communication technology, tourism and biotechnology. Competitive, risk related interest rates are also available for investors willing to invest or expand their investments in the agriculture, beverages and food based on the prime bank overdraft rate. Loans, suspense sales, equity and quasi-equity are also available for medium term finance requiring R1m to promote the establishment of permanent infrastructure in the agricultural and aquaculture sectors and establishing new or expanding on existing undertakings in the food and beverages sector (Deloitte, 2010).

6.3.2.3: Infrastructure

Under the Critical Infrastructure Programme (CIP), cash grant incentives are provided covering 10 per cent to 30 per cent of the cost of infrastructural development. New investments, including expansions in infrastructure like roads, power, railways, water, telecommunications and sewage systems are eligible investments under this scheme. The facility which is available to both public and private sector enterprises as well as municipal authorities is aimed at reducing costs to curtail risks for enhanced financial aid to boost investment in physical infrastructure (Deloitte, 2010).

⁷⁸ UNCTAD (2000). Tax Incentives and Foreign Direct Investment. A Global Survey,' ASIT Advisory Studies, No. 16

6.3.2.4: Energy

Incentives in the energy sector are also on the way with a proposed tax deduction of 45c/kw hour saved, aimed at inspiring taxpayers to implement energy conserving methods to promote energy efficiency.

6.3.2.5: Telecommunications

A 5 per cent depreciation allowance exists over a period of 20 years to provide relief for the depreciation of underwater telecommunication cables.

6.3.2.6: Tourism

A 15 per cent– 30 per cent tax exempt cash grant exists for qualifying investment cost up to a maximum grant of R30m in favour of new investments or expansion of existing facilities aimed at encouraging the growth of the tourism subsector. Competitive risk-related interest rates also exist based on the prime bank overdraft rate for investments not less than R1m. Loans, suspended sale agreements, equity and quasi- equity schemes are also available for medium-term to large-scale finance for the creation of new, or the upgrading and renovation of tourism facilities, including hotels, guest houses, lodges, cultural villages, conference and convention centers (Deloitte, 2010)⁷⁸.

6.3.2.7: Outcomes

Tax incentives have had a mixed impact on investments in South Africa. The key macro-economic policy document, the Growth, Employment and Redistribution (GEAR) Strategy under which the incentives are implemented had envisaged improvements in private savings (capital formation) and employment. However,

these aspirations are yet to be meaningfully realized as FDI to South Africa which hovered around 1.5 per cent of GDP since 1993 remained below the 3 per cent average recorded for other middle- income countries. The latest Inward FDI Performance Index of the United Nations Conference on Trade and Development (UNCTAD) ranked South Africa at 103 out of the 141 economies surveyed (Kransdorff, 2010)⁷⁹. Moreover, a larger chunk of the FDI was market-seeking instead of being directed at manufacturing and services, and largely driven by privatisation rather than incentive structures (Lewis, 2002⁸⁰; Barbour, 2005⁸¹).

However, the MIDP programme has further enhanced investments in the motor industry and encouraged higher exports of motor vehicles with substantial investments by major vehicle manufacturers like BMW, Volkswagen and Toyota (Black and Mitchell, 2002). Exporters of motor vehicles are able to obtain relief from duties payable on intermediate goods that are essential for manufacturing exports, while the privilege given to exporters in the Industrial Development Zones (IDZ) to source for capital inputs duty free has provided additional impetus for the growth of manufacturing exports.

Notwithstanding the above positive impacts, the South Africa's tax incentives scheme has suffered from implementation problems occasioned by the poor awareness among potential investors of the existing incentives, especially the small and medium-scale enterprises. Only about 35 per cent of South Africa's small businesses are said to be aware of the existing incentives for which they are eligible (Kransdorff, 2010). The application and approval processes are also said to be excessively bureaucratic and complex, specifically for the small and medium-scale enterprises. Also, the cost of securing the incentives far outweighs the expected benefits. Contrary to the initial objective of supporting the labour-intensive manufacturing enterprises with some incentive, the incentives ended up benefiting the capital intensive industries (Kransdorff, 2010). The tax incentive schemes also failed to promote the economic development of poorer regions in line with the designed objectives as 78 per cent of the incentives were noted to have been absorbed by investors in the country's three wealthiest provinces of Gauteng, Kwazulu-Natal and the Western Cape.

⁷⁸ Deloitte (2012). 'International Tax: Ghana Highlights, http://www.deloitte.com/assts/DcomGlobal/Localpercent20and percent20Investmentpercent20Guides/2012/dttl_tax_

Similarly, in Kenya the application and approval processes involved in the administration of the tax incentives in the country have been excessively bureaucratic and complex, specifically for the small and medium-scale enterprises, making the cost of securing the incentives to far out-weigh the expected benefits. Rent seeking and corruption are some of the attendant problems associated with the operation of the scheme. The overall incentive programme was open to abuse of tax avoidance with free riders benefiting at the expense of the country (Kransdorff, 2010).

7.0: Challenges to Effectiveness of Tax Incentives in Nigeria

It is of relevance to reiterate that Nigeria has made some achievements especially in the area of policy reforms, which were meant to create a conducive environment for private businesses to thrive. However, a careful analysis of policy implications and lessons for Nigeria in the preceding sections pose some questions. For instance, are tax incentives the only factor that can propel investment? What role can physical and social infrastructure, macro-economic stability as well as strong institutions play in supporting tax incentives to promote investment, growth and employment generation in the country. These issues obviously present serious challenges some of which are highlight below:

7.1: The Infrastructure Challenge

The importance of physical and social infrastructure to the private sector is that they lower the cost of doing business and where they are deficient, not only foreign investors but also domestic ones tend to move their businesses elsewhere. A major challenge facing the Nigerian economy is inadequate physical and social infrastructure. Nigeria must make concerted efforts to develop the nation's physical and social infrastructure to meet modern

standards. Certain infrastructures that are critical to a nation's take-off such as power, transport and skilled labour cannot be left to the vagaries of government revenue. Furthermore, the reliance on so-called public-private partnership and other forms of private sector involvement in building critical national infrastructure will not create the desired pool of assets needed. In the immediate, government must drastically cut down the cost of governance and free resources in order to build world- class energy, transport and social infrastructure.

7.2: The Regulatory, Corruption and Insurgency Challenge

Another major challenge to attracting domestic and foreign investments is weak institutions and poor regulatory environment. Irrelevant, duplicative and more often than not, rent seeking government agencies abound. These make it extremely difficult for potential investors to determine the sustainability and profitability of their investments. Nigeria's corruption ranking remains high at 144 out of 180 countries surveyed by the Transparency International in 2018⁸². The country's CPI score that year was quite low at 27 over 100, making it one of the most corrupt countries in the world. The corruption problem of Nigeria has been persistent, as the country has been constantly ranked among the most corrupt countries in the world.

More so, Nigeria is the 3rd most terrorised country in the world, behind Iraq and Afghanistan, and the most terrorised country in Africa (Global Terrorism Index, 2018)⁸³. According to Financial Nigeria (2018, paragraph 3)⁸⁴, Boko Haram Jihadist and armed Fulani Herdsmen accounted for 63% of terror attacks and 88% of terror related deaths in 2017. The Boko Harm group had been the deadliest terrorist group in the country.

Similarly, 2019 Economist Intelligence Unit's Quality of Life index ranked Nigeria 225th out of 226 countries in the world with a score of 51.31 as against South Africa 123th with a score of 146.52, Brazil 131th with a score of 143.16 and Kenya 219th with

⁷⁸ Deloitte (2012). 'International Tax: Ghana Highlights, http://www.deloitte.com/assts/DcomGlobal/Localpercent20and percent20Investmentpercent20Guides/2012/dttI_tax_highlight_2012_Ghana.pdf

⁷⁹ Kransdorff, M. (2010). 'Tax Incentives and Foreign Direct Investment in South Africa,'Consilience. The Journal of Sustainable Development, Vol. 3, Iss.1, pp. 68-84.

⁸⁰ Lewis, J. (2002). Policies to Promote Growth and Employment in South Africa.World Bank Africa Regional Working Paper Series No. 32, Pretoria. World Bank.

⁸¹ Barbour P. (2005). 'An Assessment of South Africa's Investment Incentive Regime with a focus on the Manufacturing Sector.'ESAU Working Paper 14, Overseas Development

a score of 71.32 respectively⁸⁵. The lower the score the poorer is the quality of life in Nigeria. The World Bank Ease of Doing Business Report rankings for Sub-Saharan Africa are benchmarked to May 2019 which ranked Nigeria 131, South Africa 84 and Kenya 56 respectively. A high ease of doing business ranking means the regulatory environment is more conducive to the starting and operation of a local firm⁸⁶. In addition, owing to weak institutions and less-than-ideal governance at the three tiers of government, corruption has persisted both within the political office holders and within the bureaucrats. Such public sector inefficiency has been associated with poor private investments and growth (see Mauro, 1995⁸⁷; and Drury, Kriekhaus & Lusztig, 2006⁸⁸). For instance, where the regulatory institutions that protect rights such as that of intellectual properties as well as medium of seeking redress are weak (election judgments passed in recent time which obvious manipulation as against the reputation of judicial system), investors would be reluctant to respond to tax incentives no matter how attractive it is made. Unfortunately, in Nigeria and many other developing countries, it is more often than not, the case.

7.3.: Weak Macro-economic Structure

The monolithic nature of the Nigerian economy where oil revenue accounts for most of the revenue to the three tiers of government and the high import dependency also pose challenges to macro-economic stability and thus, to the efficacy of tax incentives. Although, the rule-based tax policy of oil price benchmark introduced in 2003 had somewhat helped to stabilise macro-economic indicators, much still need to be done in order to insulate government budgeting from the fluctuations in the international price of oil. This is important because the current arrangement cannot withstand a heavy external shock as was seen in the wake of the global economic crisis of 2008. A more serious challenge here, however, is the utilisation of the current oil revenue being earned. If the revenue could be ploughed back into critical infrastructure as suggested under the infrastructure challenge, private sector cost of doing business would be reduced and more investors would respond to tax incentives. In

this regard, the Sovereign Wealth Fund (SWF) could achieve this through its infrastructure arm if properly managed.

7.4: Lessons for Nigeria

This section draws lessons for Nigeria from the implementation of tax incentives in other jurisdictions. The experience drawn would enhance the application of tax incentives in the various sectors of the Nigerian economy.

1. The Brazil (EPZ) has proper infrastructure, high grade logistics, efficient use of regional and local resources, and integration with a diversified Brazilian industrial base and advantageous business environment. Also, tax suspension on importation or domestic procurement of goods and services are provided. The Nigerian government could improve on EPZ by emulating the Brazilian model through the provision of infrastructural facilities to attract investors.

2. The special custom regime for importation of materials to be used in the exploitation of petroleum and natural gas by the Brazilian government provides useful lessons for Nigeria. The adoption of a similar initiative by the Nigerian government will certainly encourage and promote investment in the oil and gas sector.

3. The Farm Work Deductions incentive provided in Kenya in order to modernize the agricultural sector and enhance output has attracted huge investment resulting in the sector contributing about 24.0 per cent of GDP and about 60.0 per cent of exports. Given that agriculture is the mainstay of the Nigerian economy, incentives to boost agricultural outputs should be provided. The provision of Capital Investment Allowances in Kenya, particularly the Investment Deduction Allowance which is fixed at 100.0 per cent for investments above certain thresholds and located outside the three largest municipalities has been instrumental in ensuring that investments are evenly spread in the country. This is very important in ensuring a reasonably uniform development in the country.

⁸² T. I. (2018). Corruption Perception Index Database, Berlin: Transparency International

⁸³ IEP. (2019). Global Terrorism Index, Sydney: Institute for Economics and Peace

⁸⁴ Financial Nigeria (2018). Nigeria ranks as most terrorised African country – GTI. Retrieved From <http://www.financialnigeria.com/nigeria-ranks-as-most-terrorised-african-country-gti-news-1658.html> on 26 July 2019. Finite-sample properties. Journal of Econometrics, 108 1-24.

⁸⁵ https://www.numbeo.com/quality-of-life/rankings_by_country.jsp

⁸⁶ <https://www.doingbusiness.org/en/rankings>

4. It is observed in most of the countries studied that bureaucratic bottle neck and official red-tapism have been drastically reduced to the barest minimum. These frameworks have instilled investors' confidence and avoid loss of time in the business transaction as well as unhealthy practices. These lessons would reduce the menace of corruption and induce real time business transaction in the application of tax incentives in Nigeria.

5. It is instructive to note that the Motor Industry Development Programme (MIDP) of South Africa provides useful lessons for Nigeria in terms of the elimination of the requirements on local content. The adoption of a similar initiative by Nigeria will go a long way in promoting the automobile industry in Nigeria.

8.0: POLICY RECOMMENDATIONS

In order to streamline tax incentives, restore a level playing field for all investors in both Large Scale Enterprises (LSCs) and Small and Medium Scale Enterprises (SMEs) and improve the investment climate so that it becomes more favourable to high value-added up-market investment which creates permanent high-skilled jobs, reduce all dimensions of poverty, and breaks down the isolation of disadvantaged regions, the following recommendations could be taken into account:

- a. The current provisions that allow for tax relief of reinvested earnings and profits granted solely on the basis of a declaration of investment intent, is easily a subject of abuse by Nigerian taxpayers, and should be revised;
- b. General incentives in form of well-designed investment tax credits or accelerated depreciation could be applied as they encourage longer term investments and incur less revenue loss to the government.
- c. A well-staffed Fiscal Analysis Unit (FAU) should be established at the highest level, preferably within the Ministry of Finance. One of its principal responsibilities should be monitoring

tax incentives policy, audit and the special provisions that deviate from standard tax treatments to determine their revenue consequences and likely economic/investment effects.

d. An inter-agency data exchange system should be built to break current "information silos" and serve policy analysts in economic and tax analyses and modeling. An important exercise of indexing, classifying and linking information and databases together, including the development of a common data identifier, must be addressed as soon as possible.

e. Various investment agencies and their associated networks could be consolidated as they create unintended waste and overlap. Consolidation of the numerous agencies currently present on the Nigeria investment scene will also help avoid the inconsistent application of investment incentive measures, which is inevitable under the current arrangement.

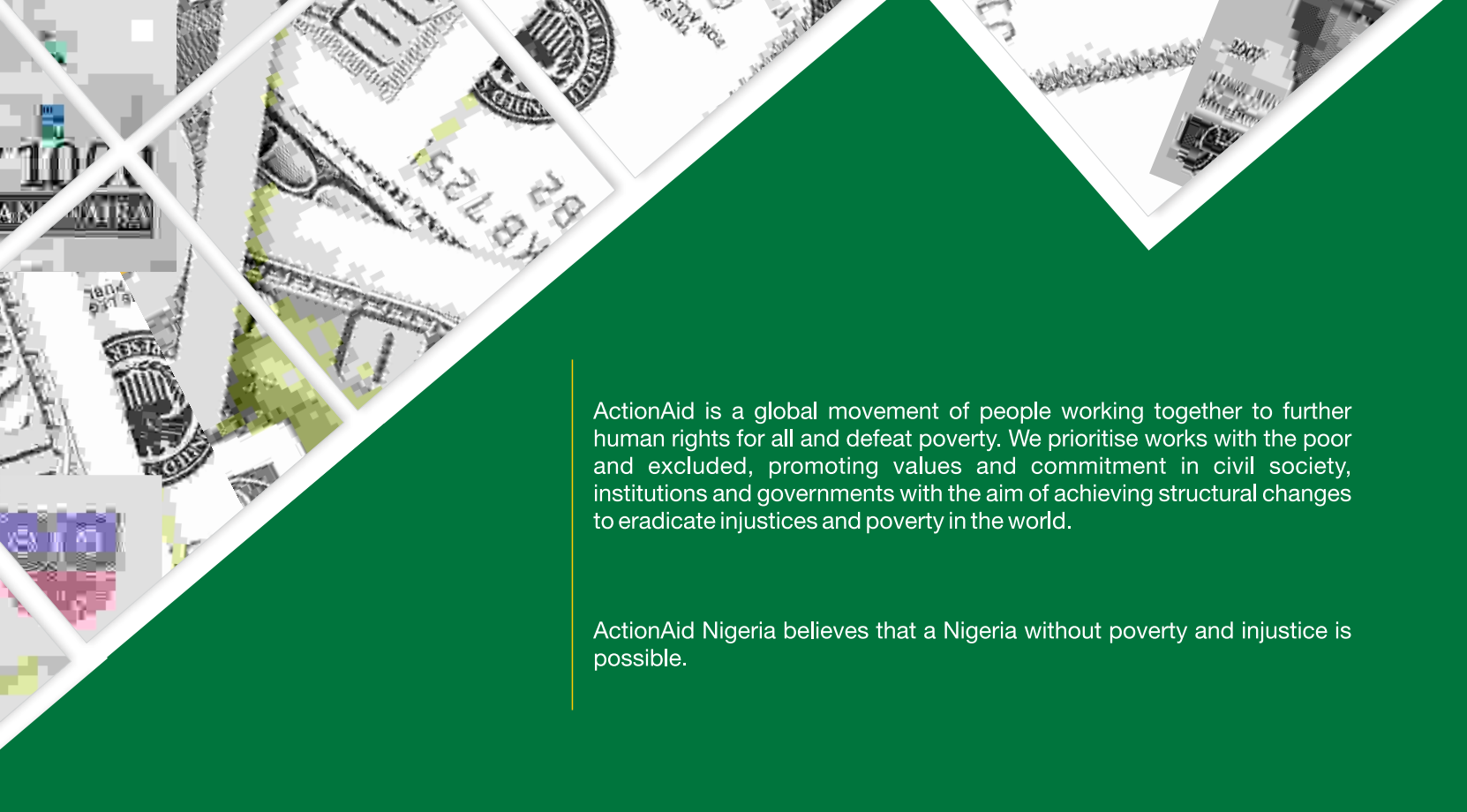
f. Build and institutionalise capacity in tax policy analysis to improve comprehension of the effectiveness of the current tax incentive measures in achieving the intended objectives.

g. Address the lack of transparency and undue complexity of the current legislative and regulatory framework in order to enable a conducive and dynamic business environment.

h. Institutionalise the process by which the revenue loss attributable to tax incentives is regularly estimated and reported, ideally as part of an annual Tax Expenditures Report (covering all of the main tax incentives).

⁸⁷ Mauro, P. (1995). Corruption and Growth. *The Quarterly Journal of Economics*. Vol. 110, No. 3, Aug. 1995.

⁸⁸ Drury, J., Krieckhaus, J., & Lusztig M. (2006). 'Corruption, Democracy, and Economic Growth.' *International Political Science Review*. Vol.27, No. 2, pp. 121-136



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