

FROM EXEMPTION TO EXPOSURE: HOW THE MINIMUM EFFECTIVE TAX RATE RESHAPES TAX EXEMPTIONS & INCENTIVES UNDER NIGERIA'S TAX ACT 2025

Ibezimako Wogu & Michael Okuwobi

Introduction

The Nigeria Tax Act 2025 (NTA) introduces a range of fiscal incentives and tax exemptions which is intended to stimulate investment in priority sectors and promote export-oriented activities. However, when these incentives are considered alongside the Minimum Effective Tax Rate (METR) regime under Section 57, significant questions arise as to their practical effectiveness and continued relevance.

In particular, the interaction between incentive provisions and the METR framework suggests a shift in Nigeria's fiscal system one in which minimum taxation may, in substance, supersede traditional incentive based policy tools.

ECONOMIC DEVELOPMENT INCENTIVE AND THE CONSTRAINT OF SECTION 57

Section 176 of the NTA establishes an economic development incentive in the form of a 5% annual tax credit on qualifying capital expenditure for companies operating within designated priority sectors. This regime replaces the former Pioneer Status Incentive (PSI), which granted qualifying entities a tax holiday of up to five years.

Section 176 of the NTA establishes an economic development incentive in the form of a 5% annual tax credit on qualifying capital expenditure for companies operating within designated priority sectors. This incentive effectively replaces the erstwhile Pioneer Status Incentive (PSI), which granted qualifying companies a tax holiday of up to five years.

The PSI regime, offered a clear and predictable benefit full exemption from corporate income tax during the relief period, thereby supporting early-stage cash flows and enhancing project viability, particularly in capital intensive sectors.

By contrast, economic development tax credit under Section 176 is subject to a critical limitation. Section 176(2), provides that the incentive is subject to and subordinate to the Minimum Effective Tax Rate (METR) framework. Under section 57(1)(a), any Company whose effective tax rate (calculated as "covered taxes as a percentage of net income") falls below 15% in any year of assessment, is required to recompute and pay additional tax sufficient to bring its effective tax rate up to the METR threshold. Notably, "covered taxes" for this purpose include companies income tax, petroleum profits tax, hydrocarbon tax, development levy, and importantly, priority sector tax credits.

The combined effect of these provisions is that the economic development tax credit, although intended to reduce a company's tax liability, cannot be applied where doing so would reduce the company's effective tax rate below the statutory minimum of 15%. This limitation is particularly relevant for companies within the scope of the METR, namely; constituent entities of multinational enterprise groups with aggregate turnover of at least £750 million, and companies with annual turnover of ₦50 billion or more. For such companies, any use of the tax credit that brings their effective tax rate below 15% will trigger an obligation to pay additional tax to meet the minimum threshold. In effect, the benefit of the tax credit is restricted, as it cannot reduce the company's tax liability beyond that point. The incentive therefore operates as a benefit only to the extent that it can be used without reducing the company's effective tax rate below the minimum threshold

Although section 176(3) allows companies to carry forward unutilised tax credits during the priority period and for a further five years after that period, this does not fully address the issue. Where, throughout the utilisation period, applying the credit would consistently reduce the effective tax rate below 15%, the credits may remain unused and may eventually lapse. This raises a legitimate question as to whether the economic development tax credit, in its current form, provides any meaningful benefit to the companies it is intended to support..



Departure from the Pioneer Status Regime

The shift from a full tax holiday framework to a constrained tax credit mechanism represents a material recalibration of the Nigeria's investment incentive strategy. Under the PSI regime, investors were afforded a clear and predictable exemption from income during the qualifying period. This predictability was valuable for investments that had long gestation cycles. The current framework, however, when viewed in light of the METR constraint, appears less compelling, particularly for:

- Capital-intensive sectors with long gestation and payback periods;
- Large domestic companies exceeding the ₦50 billion turnover threshold; and
- Foreign investors benchmarking Nigeria against jurisdictions that continue to offer tax holidays or unconstrained incentives.

For such taxpayers, the 5% tax credit may offer limited incremental value where it cannot materially reduce the effective tax burden below the METR floor

“

The “notwithstanding” clause in Section 57 recasts Nigeria's fiscal incentives—not as independent reliefs, but as subordinate mechanisms constrained by the Minimum Effective Tax Rate.

”

FREE ZONE ENTERPRISES: CONDITIONAL EXEMPTIONS

A similar situation arises in relation to Free Zone Enterprises (FZEs). Paragraph 3 of the Second Schedule to the NTA provides that - the profits of an export processing zone entity shall be fully exempt from tax, subject to certain conditions.

- its total sales arise from the export of goods or services, or serve as inputs into goods or services exclusively for export
- not more than 25% of its sales arise from the sale of goods or services to the customs territory in Nigeria ; and
- the goods and services are sold to persons engaged in upstream, midstream or downstream petroleum or gas operations.

However, this exemption is expressly made subject to Section 57. For proper understanding, a cursory look will be taken at pertinent provisions of Section 57 as it relates to the FZE.

- Section 57(1)(a) provides that, notwithstanding any other provision of the Act, companies must meet a minimum effective tax rate of 15%. Section 57(2)(a) extends this requirement to constituent entities of MNE groups above the specified global turnover threshold.
- While Section 57(3) appears to preserve the exemption for approved free zone enterprises in respect of their approved activities, it introduces two significant exceptions:
 - Transactions within the customs territory; and
 - Entities falling within the MNE scope under Section 57(2)(a).

“

The Free Zone exemption limitations, outlined in the Act, confine Nigeria's fiscal concessions within boundaries of the Minimum Effective Tax Rate.

”

The second exception is particularly consequential. It effectively brings MNE-affiliated free zone entities within the METR regime, notwithstanding their otherwise qualifying exemption status. In practical terms, this means that a free zone enterprise that is part of a qualifying multinational group may still be required to pay additional tax to achieve the 15% effective rate even were it does not make sales in the Customs territory. The statutory tax exemption is thereby qualified, and for such entities, substantially eroded. As a result, a company that would ordinarily enjoy full tax exemption under the free zone framework may still be required to pay additional tax to meet the 15% minimum effective tax rate.

This significantly limits the benefit of the free zone incentive for large multinational groups and raises questions as to how effective the exemption is in practice.

The Ascendancy of the Minimum Effective Tax Rate

Across both the economic development incentive and the free zone regime, a clear pattern emerges: fiscal incentives operate subject to, and within the limits imposed by the METR framework. The expansive wording of section 57 particularly the use of “notwithstanding any provision of this Act or any other enactment” clause, indicates a deliberate legislative intention to accord primacy to the minimum tax rule. As a result tax exemptions and incentives no longer operate as standalone reliefs but as subordinate mechanism whose effectiveness is contingent on the METR threshold.

From a policy perspective, this raises important considerations. Tax Incentives have historically been deployed to attract investment and support industrial development. Where incentives are systematically overridden by the METR framework, their effectiveness as tools for attracting investment becomes questionable. In practical terms, METR may now function as the dominant tax rule, and may have a negative influence on investor behavior.

Conclusion

The introduction of the METR regime under the NTA reflects Nigeria's alignment with global tax developments aimed at ensuring a minimum level of taxation, particularly for large and multinational enterprises. However, its interaction with domestic incentive frameworks appears to have unintended consequences.

The subordination of incentives such as the economic development tax credit and free zone exemptions to the METR threshold significantly diminishes their practical value, especially for large and multinational enterprises. This, in turn, raises legitimate concerns as to whether the current framework strikes the appropriate balance between revenue protection and investment promotion.

Accordingly, investors and advisers should carefully assess the interaction between incentive provisions and the METR framework when evaluating project economics. From a policy standpoint, further clarity or refinement may be required to ensure that Nigeria's incentive regime continues to serve its intended role in promoting sustainable economic development.

Contact Us

 Hermon Legal Practitioners
 @Hermonlaw
 hermon@hermonlaw.com
 Hermon Legal Practitioners
 hermonlaw.com

 Penthouse Suite, Theodolite House, 306 Ikorodu Road Anthony, Anthony, Lagos.

 +234-818-8210-444