Examining The Nigerian Government Tax Incentive Policy On Foreign Direct Investment And The Principles Of Taxation

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ABSTRACT
In Nigeria, the federal and state governments in their desire to encourage and attract foreign direct investment introduced various tax incentives and exemption policies designed to boost industrial and agricultural production for exports. Bulk of the tax incentives are statutory taxes and considering that Nigeria operates a federal system of government makes taxation a matter within constitutional consideration. This article in its entirety examines foreign direct investment, taxation. Also focused are the universally known and accepted principles of taxation in relation to their application and compliance with by the Nigerian government particularly the federal government tax incentives policies to foreign direct investors. Findings as revealed indicates that the Nigerian government incentives policy on foreign direct investment undermines the accepted principles /cannons of a good tax system which presently bears on the effectiveness of the incentive policies of the Nigerian government toward placing the Nigeria nation economy on the fast lane towards economy growth and development.

Keywords: Economic, Economy Technology and Fiscal System, Foreign Direct Investment, Growth Investment, Principle of Taxation, Taxation, Tax Incentive.

INTRODUCTION
Foreign Direct Investment
Foreign Direct Investment in Nigeria, Nigeria as a developing nation with respect to foreign direct investment is increasingly looking for best practices and foreign policies towards its promotion for efficiency¹. There is renewed confidence in the positive benefits of foreign direct investment which has led Nigeria like other developing nations to relax the restriction on foreign direct investment experienced in the 60s, 70s and 80s to open foreign direct investment in the 90s and beyond. The government has liberalized foreign direct investment regimes with accompanied technological advancement that have led to rapid growth in foreign direct investment flows over the last three decades. As it is in Nigeria, so it is applicable to other developing countries which have led to gains in share of domestic investment and GDP². Foreign direct investment is direct investment into production or business in a country by individual or company of any other country either by buying a company in the target country or by expanding operations of an existing business in that country. It is the opposite of Portfolio investment which is a passive investment in the securities of another country such as stocks and bonds. The World Bank³ conceptualized foreign direct investment as investment that is made to acquire a lasting management interest (usually 10% voting stock) in an enterprise and operating in a country other than that of the investors and the investor’s purpose being an effective voice in

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1 Foreign Direct Investment has the objective of developing a lasting interest by a resident entity in one economy in an entity resident in an economy other than that of the investor with lasting usually defined as a 10 percent stake in the entity.
the management of earning either long term foreign direct investment which also includes mergers and acquisitions, building new facilities, reinvesting profit earned from overseas operations and intra company loans.

In Nigeria, foreign investment is traced back to the colonial era, when the colonial masters had the intention of exploiting the nation’s resources for research and discovery of oil. Foreign investment has been on the increase as recognized by the Nigerian government owing to its importance in enhancing economic growth and development. In the light of these various strategies involving incentives policies, regulatory measures have been put in place to promote the inflow of foreign direct investment to the Nigerian nation. Privatization was also adopted, among other measures, to encourage foreign investment in Nigeria. This involved the transfer of state-owned enterprise in the manufacturing, agricultural production, public utility, services such as telecommunications, transportation, electricity and water supply sector that was completely or partly owned by or managed by private indigenous individuals or companies in Nigeria to foreign investors. Since the enthronement of democracy in 1999, the government of Nigeria has taken number of necessary measures to encourage foreign investors into the Nigeria. These measures include abandoning the abrogating laws, and various overseas trips for image laundry by the presidency among other measures. Foreign direct investment remains an integral part of the Nigerian nation’s economic policy towards growth and development. It is in the light of the above that this chapter will examine the various incentive measures towards realizing same and in the area of tax incentives in relation to the universally known and accepted principles/cannons of a good tax system expected of every government tax incentives policy towards its economic growth and development.

Importance of Foreign Direct Investment to the Nigerian Economic Growth

Nigeria, an emerging economy and country in transition is increasingly focusing towards foreign direct investment as a source of economic growth, development and modernization in form of income growth and employment resulting from liberalized foreign direct investment regime with determined pursuit of policies geared towards attracting foreign investment. The essence of the domestic pursuit of policies is to maximize the benefits of foreign presence in the Nigerian domestic economy.

Foreign direct investment has impacted greatly on the different sectors of the economy such as technology spillovers, human capital formation, international trade integration, availability of more competitive business environment and enhancement enterprise development within the economy. All these briefly explained below are functions of economic growth, a potential tool of poverty alleviation resulting from foreign direct investment in varying dimensions.

i. Trade and Investment

In Nigeria, the main trade related benefit impact of foreign direct investment lies in the long-term contribution of integrating the host economy more closely into the world economy in the process likely to include higher imports as well as exports. In other words, trade an investment is increasingly recognized as mutually rein-enforcing channels for cross-border activities. The ability to use foreign direct investment as a means to increasing exports in short and medium terms depend on the relationship.

ii. Technology Transfer

There is the presence in Nigeria of identified technology transfer as one of most important channels which foreign corporate presence has yielded positive externalities in the Nigerian economy. Multinational Enterprises are the developed world’s most important sources of corporate research and development (R & D) activity and they generally possess a higher level of technology that is available in developing countries. Thus, they have the potential to generate considerable technological spillovers. Equally, is for technological transfer to generate externalities, that is, technologies need to be relevant to the host communities’ business sector beyond the company that receives them first. Foreign direct investment has yielded more positive impact on the economy in Nigeria than domestic investment in productivity. The “technology gap” between

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5 Ibid
domestic enterprise and foreign investors is relatively high resulting from a great impact of foreign direct investment with regards to technology transfer in Nigeria.

iii. Human Capital Enhancement
In Nigeria, foreign direct investment has impacted greatly on human capital enhancement directly, occurring not principally through the efforts of the multinational enterprises, but rather from government policies in attracting foreign direct investment via enhanced human capital. When individuals are employed by multinational enterprise subsidiaries, their human capitals are enhanced further through training and on-the-job training. These sometimes extend to the subsidiaries impacting positively on human capital enhancement in other enterprises with which they develop links, including suppliers. Such enhancement can have further knocked-on effects as labour moves to other forms and in some cases the employees becoming entrepreneurs. This makes human capital development intimately related with other broader development issues which impact greatly on the economic growth of the nation.

Another area of human capital development or enhancement is in the area of general education and other generic human capital with its utmost importance in creating an enabling environment for foreign direct investment. Achieving a certain minimum level of educational attainment is paramount to a country’s ability both to attract foreign direct investment and to maximize the human capital spillovers from foreign enterprise presence. The indirect impact of foreign direct investment on human capital enhancement is realized through opportunities of the Nigerian economy (host community) to upgrade their human capital and strengthen their incentives for doing so. Also, a labour market such as in Nigeria where participants have access to a certain degree of security and social acceptance lends itself more readily to the flexibility that is a key to the success of economic strategies based on human capital. It provides an environment in which multinational enterprises based on social acceptance and application of the national home country standards and contributing to human capital development. One strategy to further this goal is a wider adherence to the OECD Declaration on International Investment and Multinational Enterprises.

In Nigeria, human capital levels and spillovers appear closely interrelated with technology transfers particularly in technologically advanced sectors and host countries. Like Nigeria are more likely to see human capital component lend themselves more easily to technology and human capital spillovers. The implication of this is that efforts to reap the benefit of technology and human capital spillovers could gain effectiveness when policies of technological educational improvement are undertaken constantly.

iv. Competition
Foreign direct investment and presence of multinational enterprises in Nigeria have significantly influenced competition in market despite the fact that there is no accepted way of measuring the degree of competition in a given market. The presence of foreign enterprises has greatly assisted economic growth and development by spurring domestic competition thereby leading eventually to high productivity, lower price and more efficient resources allocation.

v. Enterprise Development
In the area of enterprise development, foreign direct investment has significantly spurred enterprise development. The direct impact on the targeted enterprise includes the achievement of synergies with the acquiring multinational enterprise, and the development of new activities. In addition, efficiency gains had occurred. The strongest evidence of improvement is found in industries with economics of scale foreign orchestrated takeover in most sectors has led to changes in management and corporate governance where the foreign enterprise impose their own company policies, internal reporting systems and principles of information disclosure on acquired enterprises and the benefits of a number of foreign managers taking over and integrating foreign corporate practices considered superior to that of the Nigeria practices.

The Nigerian Government on Tax Incentives
Nigeria has for long pursued a policy of encouragement and stimulation of private investment both in the indigenous and foreign private sectors of the economy. Indeed, it is true to say that Nigeria has always

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6 Ibid
7 Ibid, p.15
adopted a liberal economic policy towards private enterprise in order to encourage industrialization, wide accelerated depreciation, tariff protection and custom duty drawback amongst others as adopted incentive measures to encourage foreign direct investment.

Over the past three decades, the Nigeria government has been actively involved in promoting the country’s economy as investment location to attract scarce private capital, associated technology and managerial skills in order to help her development goals. To this end, she has increasingly adopted measures to facilitate the entry of foreign direct investment. Examples of such measures include liberalizing the laws and regulations for the admission and establishment of foreign investment projects through providing guarantees for repatriation of investment and profits; and establishing mechanisms for the settlement of investment disputes, and particularly tax incentives and other vital promotional efforts.

The role of incentives in promoting foreign direct investment has been the subject of many studies, but their relative advantages and disadvantages have never been clearly established. There are notable spectacular successes as well as notable failures in their role as facilitators of foreign direct investment. As a factor in attracting foreign direct investment, incentives are secondary to more fundamental determinants, such as market size, access to raw materials and availability of skilled labour. Investors generally tend to adopt a two-stage process when evaluating countries as investment locations. In the first stage, they screen countries based on their fundamental determinants. Only those countries that pass these criteria go on to the next stage of evaluation where tax rates, grants and other incentives may become important. Thus, it is generally recognized that investment incentives have only moderate importance in attracting foreign direct investment. In some cases, and with some types of investment, however, their impact may be more pronounced. For some foreign investors, such as export-oriented investors, tax incentives can be a major factor in their investment location decision. Also, among countries with similar attractive features the importance of tax incentives may be more pronounced. In addition, the Nigerian government quickly and easily changes the range and extent of the tax incentives she offers. However, changing other factors that influence the foreign investment location decision sometimes appear more difficult and time consuming, or even outside government control entirely.

For this, investment experts, particularly from investment promotion agencies, view incentives as an important policy variable in their strategies to attract foreign direct investment. Basically, incentives being a measurable advantage accorded to specific enterprises or categories of enterprises by (or at the direction of) a government, in order to encourage them to behave in a certain manner most times include measures specifically designed either to increase the rate of return of a particular foreign direct investment undertaking, or to reduce (or redistribute) its costs or risks. They do not include broader non-discriminatory policies, such as infrastructure, general legal regime for foreign direct investment general regulatory and fiscal regime for business operations, free repatriation of profits or national treatment. It is important to note these policies bear strongly on the location decision of Transnational Corporations (TNCs), which are not foreign direct investment per se.

Developing countries like Nigeria, irrespective of their stage of development, employ a wide variety of incentives to realize their investment objectives on the other hand, developed countries however; more frequently employ financial incentives such as grants, subsidized loans or loan guarantees. It is generally recognized that financial incentives are direct drain on government budget, and as such, they are not generally offered by developing countries to foreign investors. Instead, these countries tend to use fiscal incentives that do not require upfront use of government funds.

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10 United Nation Conference on Trade and Development Op cit, p 12; UNCTAD (2001:6-7) report that nearly 95 percent of the 1,185 changes in national foreign direct investment Legislation during the period of 1991 – 2000 was favourable to Foreign Investors. A significant share of these charges focused on incentives and FDI Promotion.
As stated above tax incentives being incentives that reduce the tax burden of enterprises in order to induce them to invest in particular projects or sectors. They are exceptions to the general tax regime. Tax incentives as known include, for example, reduced tax rates on profits, tax holidays, accounting rules that allow accelerated depreciation and loss carry forwards for tax purposes, and reduced tariffs on imported equipment, components, and raw materials, or increased tariff to protect the domestic market for import substituting investment projects.

Tax incentives are intended to encourage investment in certain sectors, or geographical areas as a result, they are rarely provided without conditions attached. Very often most countries including Nigeria, design special incentives regimes that detail the tax benefits as well as the key restrictions. For instance, these regimes may require that a facility be established in a certain region(s), have a certain turnover, require the transfer of technology from abroad or employ a certain number of individuals. Like the case of China that offers foreign-invested firms a tax refund of 40 percent on profit that are reinvested to increase the capital of the firm or launch another firm. The profits must be reinvested for at least five years. If the reinvested amounts are withdrawn within five years, the firm has to pay the taxes. In the case of India, the government offers a tax exemption on profit of firms engaged in tourism or travel, provided their earnings are received in convertible foreign currency.

Current survey finds that reduction in the standards rates of corporate income tax and tax holidays are the most widely used fiscal incentives. These are followed by exemptions from import duties on capital equipment, raw materials and semi-finished components, duty drawbacks, accelerated depreciation, specific deductions from gross earnings for income-tax purposes, investment and reinvestment allowances and deductions from social security contributions.

Relief/Tax Incentives in Nigeria
As stated above, tax incentives can take the form of a tax holiday, a tax credit proportional to the amount of capital investment, accelerated depreciation or an interest subsidy etc. These are offered by the Nigerian government as incentives.

Objectives of Tax Incentives in Nigeria
The question usually asked is why are so many countries competing to attract foreign direct investments? The answer to this question seems to be the objectives of tax incentives, because each country desires to induce foreign investment and wishes to utilize positive externalities from foreign direct investment for development of her national economy hence the introduction of the various legislations and policies in realizing this target. These objectives are considered in the following regards:

i. Rural/Regional Investment Development Objectives
Nigerian government employs a mix of incentives to channel investment for development of a particular area rural or region. This is because regional development objectives include support for rural development, building industrial centers away from major cities and reducing environmental hazards, over-urbanization and concentration of population. Incentives schemes geared towards reclamation and cultivation of barren and desert land also fall in this category of objective. The Nigerian government has adopted this regional incentive system aiming at the above objectives when it gives allowances of high percentage to companies that establish operations in rural areas where there are no facilities such as electricity, tarred road, telephones and water supply.

ii. Sectoral Investment Development Objectives
The Nigerian government employs tax incentives as a means of promoting sectors of the industries or activities considered crucial for development. These are sometimes and mostly targeted at the mining and industrial parks, export-led activities, as well as industries and businesses with new technologies.

Nigeria as a developing nation, considers mainly tax incentives be granted to related investment in manufacture, exploration and extraction of mineral reserves. Research also showed that developing countries like Nigeria generally do not attract headquarters of companies and service activities and therefore the incentives are usually aimed at the service sectors.12

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12 UNCTD Incentives and Foreign Investment, United Nation Publication New York and Geneva p.68
iii. **Performance Enhancement Development Objectives**

In Nigeria, one of the objectives of government towards Relief /Incentives is the target of enhancement of certain areas and issues such as export promotion, employment/skills training, and domestic value added and headquarters location. The creation of Free Trade Zones typically covers incentives for export-oriented manufacturing. Qualified/qualifying enterprises in these zones are exempted from direct and indirect income tax, import duties and value added taxes.

iv. **Transfer of Technology Development Objectives**

The Nigerian government considers it an important objective of using incentives to attract investment into the country via the transfer of technology. Certain types of tax incentives are designed specifically for this purpose through a scheme called Research and Development (R&D) activities and technology projects (Pioneer industries). It is achieved through tax-exempted technology development fund and tax credit for expenditure on R&D, and for upgrading human resources related to research and development. It is where a particular reduction is allowed for certain types of expenditure, and income tax exemption is offered for a period of time, while machinery, equipment and raw materials are exempted from import duty and sales tax. For import of technology, tax incentives provided may take the form of deductions allowed for transfer costs of patent rights and import fees, exemption of income from consulting and granting of tax privileges to research and development projects.

**Forms of Tax Relief/Incentives in Nigeria**

Tax incentives can take the form of a tax holiday, a tax credit proportional to the amount of capital investment, accelerated depreciation or an interest subsidy amongst others in whatever form they are granted, they are supposed to generate more current investment, hence higher future production. As such, the least discriminatory form of tax incentives is the one that is so designed to increase the rate of return on all investment in the country like a reduction in all corporate and personal tax rates. In some cases, you may have an incentive programme restricted to a few selected firms in the same industry, usually those considered most desirable on its goals (like value-added by domestic processing, contribution to employment, exports, technology transfer etc).

Whatever forms an incentive program takes, one is to look at the relative merits and demerits based on equity and efficiency consideration. Suffice it to mention that the most efficient incentive is the one that does not distort the allocation of capital among investment of different types and durability’s. This contention becomes clearer when it is realized that tax incentives affect capital spending in two main ways:

(a) By reducing the firm’s capital stock and
(b) By increasing the rate of adjustment of the existing capital stock to the desired level through purchases of new capital.

We shall now examine the form and nature of tax relief /incentives in the Nigerian industries.

**Tax Exemption**

Tax exemption otherwise known as “Tax holiday” is the most widespread tax incentive. Many investment incentive laws seem to be more commonly associated with it than with any other system of tax incentives. Tax exemption simply means a period of exemption from the payment of taxes imposed by the government and this exemption may be complete or partial. Tax exemption is generally regarded as an industrial investment device.

Countries that observe tax exemption policy argue that tax exemption is a neutral point between capital-intensive and labour intensive types of business and seems therefore to be a convenient tool that can be used in countries with surplus labour in extracting industries to help solve unemployment problem.

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13 For a discussion about the effect of export processing Zones, see e.g. H. Johnson and L Nilson Vol. 25. 2115-2128. It should be noted that there is surprisingly little contact between that literature on the effect of FDI subsidies and the literature on export processing zones, C.T. Taylor “The Impact of Host Government Policy on US Multinational Investment Decision World Economic Vol. 23 (2000) 635-648.


That apart from its economic effects, tax exemption has an important psychological effect in the sense that it implies that foreign capital is wanted, welcome and will be well treated.\textsuperscript{16}

Thus, tax exemption can be a very useful tool in the hands of the developing country like Nigeria to attract foreign capital as the foreign firms may be reluctant in the first instance to come because of poor investment climate as experienced in Nigeria. Tax exemption therefore reassures them that their presence and operations are needed and welcomed.

For the anti-tax exemption policy, they hold the view that grants disproportionate benefits to firms which enjoy a higher rate of profit since the greater the profit, the greater the savings out of the postponement of tax payments thereby discriminating against the need and the profit-less companies.\textsuperscript{17}

Moreover, because there is a greater risk of providing large benefits for risk for highly profitable, and enterprises, since tax exemption involves revenue losses and for developing countries like Nigeria, this may likely deplete the treasury further.\textsuperscript{18} In some countries, there has been an attempt to avoid this result by limiting the exemption to profits not in excess of a state rate of return on invested capital. As desirable as this may be, it makes simple to confine successfully to a maximum rate of return on invested capital that may not bear any direct relationship to the firm for new capital.

Furthermore, where tax exemptions is offered to new firms, which is usually the case because they are recognized as facing initial difficulties or to profit earned on new investments, considerable difficulty is usually encountered and usually encouraged in identifying a genuinely new business and in allocating the profits of an existing firm between old and new capital, thereby presenting formidable accounting and agreement problems.\textsuperscript{19} On the whole, tax exemption has been criticized as an ineffective and inefficient stimulus to investment, particularly in developing countries, complicating the regular company tax legislation and increasing avenues for tax evasion.

Finally, the resulting proliferation of tax exemptions and keen competition among developing countries like Nigeria in offering these tax incentives for new industries has largely diluted its promotional appeal. It is note-worthy, from the above position that if tax exemption incentive policy is properly used on a selective basis, will have the potential to influence investment decisions of firms. Be that as it may, besides tax exemption, the other tax incentives measure commonly associated with taxation is the accelerated Depreciated Allowances.

### Accelerated Depreciation Allowances

The term ‘Accelerated Depreciation Allowances’ covers all methods of rapidly writing off the original cost of new capital equipment less any salvage value in the early year of investment. This is done by deducting the less cost from taxable in-come. For this purpose, several methods are employed. The common methods are:

1. (i) The straight-line method, under which the cost of depreciable property is written off in equal annual installments over its expected useful life; and

2. (ii) The declining-balance method, under which the deduction is a constant fraction of the unauthorized balance of the cost of the asset but a declining fraction of original cost.

The straight-line method is used mostly in the United States and Nigeria whilst the declining balance method is used commonly in the British Commonwealth.

The investment subsidy commonly associated with the above methods is: investment allowance and initial allowance. Investment allowance provides for a write off depreciation property in addition to that provided by ordinary depreciation allowances thereby perverting depreciation in excess of the cost of the asset. Under the initial allowance however, the amount deducted in the first period is subtracted from depreciation assets, thus reducing the amount of depreciation in subsequent periods. Apart from their treatment of depreciable property after initial year, the two forms of investment subsidies are similar in that they grant a given amount in the

\textsuperscript{16} Ibid.


\textsuperscript{18} Ibid.

initial year though companies will prefer investment allowance since it permits depreciation in excess of the cost of the asset.

From the above it is clear to deduce that an accelerated depreciated system has several advantages. First and foremost, under accelerated depreciation allowances, a company realizes interest free loan in the form of postponement of taxes and so long as the company continues to expand, there is tax savings. This enhances the profitability and liquidity of companies and in this way stimulates investment by increasing the availability of financial resources.

Moreover, where tax rates are high, an expanding company will be able to finance a substantially large fraction of its investments accelerated depreciation depending on the behaviour of the individual firm and the amount of benefit that is directly related to the rate of its expansion as measured by acquisition of new depreciable assets. Also, it effectively assists the level of investment required in manufacturing industries particularly in a developing country like Nigeria by equipment which should lead to industrial expansion, faster modernization and to greater output.

Further still, an acceleration system is relatively easier to operate without any major administrative problems associated with it. It also lends itself to be conveniently used to achieve specific national objectives as its benefits can automatically be restricted to those who invest in approved productive facilities. Accelerated depreciation can therefore be rated to types of investment, which the government wishes to promote, and withhold from other types of investment without causing any serious accounting and administrative problems.

Finally, accelerated depreciation may stimulate investment through its influence on risk or uncertainty. Businessmen usually make allowance for risk of uncertainty in investment decisions and one of the ways in which they do this is by insisting that a new asset ‘Pay for itself’ in a considerably shorter period than it’s normal physical or economic life. Whatever misgiving can be raised against this practice, in the commercial world, this pay-off approaches seem to be a very desirable method of allowing for risk and uncertainty. This view seems to be predicated on the premise that risk increases with the duration of commitment and that uncertainty of the distant future are much greater than those of the near future. Accelerated depreciation therefore assists investors to a the capital assets out of their yield within the investor’s planning period thereby giving investors a better picture of prospects for their industries and the confidence to make their plans without too much regard to the deterrent influence of taxation on new investment. From the foregoing, it seems that Nigeria, a country involved in the encouragement and development of manufacturing industry particularly in the production of intermediate and capital goods will find the accelerated depreciation system a very useful tool.

Accelerated depreciation system does, however, have its own disadvantages. Accelerated depreciation will only be advantageous to the firms if it can be set off against taxation income. It will therefore be harmful where there is inadequate taxable income. Thus, its effectiveness can only be enhanced by liberal provisions for averaging accounting losses and profits through liberal carry back or carry forward of losses. Apart from the fact that accelerated depreciation is likely to be less effective in time of depression than during prosperity (with taxable income and tax liabilities tending to lower in years when investment is large and higher in years of depreciation). Its adoption will decrease government revenue unless it results into a net increase in activity large enough to offset the reduction in the effective rate of taxation. There is also the possibility that accelerated depreciation may result in a permanent loss of revenue to the government as against a mere postponement of tax revenue asset decline or disappearance. New assets will become eligible for accelerated depreciation.

Finally, accelerated depreciation is biased in favour of firms in capital-intensive industries and industries in which the ratio of depreciation assets to total investment is high. This may be regarded as questionable in developing countries like Nigeria where there is labour supplies.

Notwithstanding these criticisms of the accelerated depreciation, it does seem that it will offer a greater stimulus to investment than tax exemption and seems particularly appropriate to Nigeria whose priorities now include encouraging investment in the intermediate and capital goods industries.

Long-Term Fiscal System
A major and primary distinguishing element of long-term fiscal system incentive policy by Nigerian government from other incentives is the stabilization of tax charges. It usually entitles the approved entity or enterprise to the following benefits:
(i) Stabilization of all tax rates at the level prevailing when the enterprise was approved and for an extended period of say 25 years.
(ii) Exemption from modification in tax assessment and collection procedures during this period; and
(iii) Exemption from new taxes introduced during this period.

Duties Relief on Importation
As one of the incentives by the Nigerian government for foreign investors, duties relief on importation covers custom duties of equipments and firms’ capital equipments with respect to relief from duties on imports of raw materials and semi processed materials. These incentives enhance the competitiveness of the firm in establishing a domestic or foreign market. It also takes the form of differentiation between types of industries and the destination of the products produced by these industries whether for internal use or for the export market.

One major consequence of the import relief is that, it creates for the government to suffer undue revenue loss and negative balance of payment situation resulting adverse effect on the economy, because the imported equipment are paid for out of the country’s currency reserves.

Enterprise Agreements
A critical examination of this incentives measure reveals that the scope of enterprise agreement is wider than that of long-term fiscal system in the sense that the long-term fiscal system can be regarded as a variation of the enterprise agreement. Hence, the scope of tax stabilization under enterprise agreement is wider and extended such that it includes many other benefits such as financial guarantees that provides for repatriation of capital, profits and economic guarantees which cover almost everything regarding the carrying on of business such as tax free importation of primary materials and capital equipments for the activities of the enterprises. Enterprise agreement often includes the right of the investors’ company to employ foreign personnel as regular employees.

This incentive measure seems to be over generous as the stabilization for an increasing number of enterprises especially the large ones will seriously undermine the revenue structure of Nigeria as a developing nation where there is scarcity of revenue source not to be avoided by a developing nation particularly in the industrial sector of the economy. Moreso, to freeze taxes at relatively low levels in the large enterprise is bound to invite public hostility to the private enterprise and to provide fertile ground for radicals to press for the expropriation of private enterprise which may not be either in the national interest nor in the interest of the sector.

Sectors Covered by the Nigerian Government Tax Relief/Incentives Policies
Under Nigerian laws, the federal government relief/incentives do not include certain aspects of taxation, and no law or laws have been legislated to alter the constitutional provisions that give that power to the various levels of government. Therefore, it is only the Federal and State governments that possess the powers over foreign policies. Local governments do not possess such powers.

As part of the efforts to provide an enabling environment, conducive to the growth and development of industries, and an inflow of foreign direct investment, the Federal government has developed incentive packages for the various sectors of the economy with the hope that these incentives will revive the economy, speed up the rate of growth and development and reduce the poverty rate.

The government accepts the private sectors as the engine of growth and creators of wealth while the government’s major responsibility is to ensure the enabling environment for the private investors to operate. In this result, effective laws have been either amended or repealed to guarantee the federal government laudable programme.

21 Andic, Op cit.
22 Ibid.
On the strength of the above, and within the past fifteen years following the end of military dictatorship in Nigeria Federal and State governments have either legislated, initiated and implemented a number of incentives aimed at encouraging and promoting foreign direct investment in Nigeria within the various sectors. Some of these incentives and affected sectors are:

1. **Pioneer Status:**
   - Tax exemption granted for a period of three years in the first instance but may, or likely to be extended to a further period of two years under the industrial development (Income Tax Relief Act) and qualification for these incentives include:
     - (a) The applicant must be a public company
     - (b) The Investment must be in respect of industry or products, designed as pioneer e.g. agro allied, export goods and solid minerals; and
     - (c) The estimated cost of qualifying capital expenditure on or before production date must not be less than N50,000.00

2. **Tax Relief:** under Companies Income Tax Act. These incentives provide:
   - (a) Non incentives of co-operative society, religious/charitable, etc organizations and sporting activities. Similarly, the profit of any Nigerian company in respect of goods exported from Nigeria are exempt from tax, provided that the proceeds from such exports are repatriated to Nigeria and are used exclusively for the purchase of raw materials, plants, equipments, and spare parts.
   - (b) Relief in respect of interest on foreign loan bank loans for agriculture, grants for companies engaged in agricultural business, the fabrication of local plant or machinery or as working capital for any cottage industry established under the Family Economic Advancement Programme Establishment, etc.

The incentive also provides for duty drawback suspension scheme on the following activities in Nigeria:
- a. Raw materials including packaging materials used in manufacturing goods that are exported.
- b. Paper used for the manufacturing of goods supplied for educational purposes to education establishment recognized by the federal adviser on education.
- d. Investment in economically disadvantaged area.
- e. Local raw materials utilization.
- f. Investment in solid minerals: a company going into mining of solid mineral shall be exempted from tax for the first three years of its operation which may be extended for one further period of two years.
- g. Research and Development (R&D) for companies engaged in research and development activities for commercialization are allowed certain percentage investment tax credit on their qualifying expenditure Companies Income Tax Act.
- h. Expenses incurred on research and development including the amount paid to the National Science and Technology Fund are allowed deducted expenses.
- i. Rural Investment Allowance which provides graduated allowances for capital expenditure on such facilities as electricity, water, tarred road and telephone located at least 20 kilometers away from such facilities provided by the government.
- j. Investment in the Export Processing Zone (EPZ) which provides that export oriented undertaking established within and outside an Export Free Zone shall be exempted from tax for the first three

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23 Cap 17 LFN 2011.
24 Cap C21 LFN 2011. Also 47 Profit Exempted from Taxation (Section 19); 48 Relief from Tax for the, First 6, 000.00 Naira of the Total Profit (section 29); 49 Relief in Respect of Commonwealth Tax (section 33); Relief from double Taxation.
27 Section 22(2) Minerals and Mining Act Cap M12 LFN 2011. Also, section 18 of same Act
28 Section 22(3) (as amended by Finance (Miscellaneous Taxation Provisions) Degree No 3 1996.
consecutive assessment years provided, among other conditions that it manufacturers, provided and export articles during the relevant year and the export proceeds from 75% of its turnover.

Tax Incentives Administration
Nigeria, a federation with three levels of government, creation of the constitution, has the administrative bodies or agencies to administer tax at the various levels of government, but on tax incentives such as income tax exemption or company pioneer relief, the administrative responsibility is shared between the Federal Ministry of Industries and the Federal Board of Inland Revenue at the federal government level. Under the Venture Capital (Incentives) Act\textsuperscript{30}, the administrative responsibility falls on Federal Inland Revenue Service, also a federal agency as it provides as follows:

1. The Federal Inland Revenue Service shall; from time to time determine the purpose of this Act, a person as a venture capital company or venture projects company.

The federal inland revenue service is responsible for general policy which, \textit{inter alia} entails the selection of pioneer products whilst the Federal Ministry of industries and the Federal Board of Inland Revenue perform the more routine functions like ensuring that the applicants comply with the amount of qualifying capital expenditure as well as ensuring that the terms of pioneer certificate are complied with.

Principles of Taxation
Tax revenue provides one of the easiest and most convenient means of meeting the ever-increasing public expenditures. Quite a reasonable percentage of people do not freely pay taxes. Tax introduction had resulted in several riots in the societies such as Ghana when VAT was introduced; about 85 persons lost their lives. Also, the Aba women protest in 1929 caused by the introduction of payment of tax by women. The ‘Ijemo’ Massacre of 1914 that resulted from revolt against, The Egba United Government was as result of planned imposition of taxation.\textsuperscript{31} One of the reasons for which is the inability to see the dividends of tax collection. This is why it is imperative that every government irrespective of its nature and type should put in place an efficient, effective, just, and equitable tax system. Smith put forward some principles that called Cannons of Taxation for a good tax system to exhibit. These cannons of taxation according to him are the principles of taxation that serve as rules of references to which good tax policy can be formulated\textsuperscript{32} for effective tax system. They are put forward by Smith as a basis for tax imposition now universally accepted. This will be discussed in addition to other principles as follows:

\textbf{a) Cannon of Equity and Proportionality}

By this principle, Smith postulated that while the government has the authority to demand a certain percentage of the income of the citizens to finance itself, the percentage demanded should not be such that would amount to an extortion, but one proportionate to the income of the taxpayer, and at the same time ensure conformity of liability.\textsuperscript{33}

On the postulation of Smith, Akande stated that:

While subjects of a state ought to contribute to the support of the government, such contribution should as nearly as possible be proportionate to their respective abilities. Since one of the cardinal functions of government is to offer protection to those living within its territory, presumable therefore, it is incumbent on government not to demand

\textsuperscript{30} An Act to Provide for Grant or Tax Relief and Other Incentives on Personal Investments in the National Risk Fund, Venture Capital Companies and Venture Capital Projects and Other Matters Related Thereto [1993 No 89].

