



Value Added Tax (VAT) and 2025 Nigeria Tax Reforms

Key changes and implications for businesses

Background

Value Added Tax (VAT) was introduced in Nigeria in 1993 via the Value Added Tax Decree No. 102 of 1993, replacing the Sales Tax, which was introduced by the military regime. It is a consumption tax imposed on all goods and services consumed in Nigeria except those explicitly listed in Part I & II of the First Schedule to the Act and the VAT Modification Orders issued by the Honourable Minister of Finance through an official gazette of the Federal Republic of Nigeria. VAT has been a major source of non-oil revenue for the government since the increase in the rate from 5% to 7.5% in 2020, and with the implementation of Tax ProMax in 2021 hitting an aggregate of NGN1.56 trillion as at Q2 2024 based on the National Bureau of Statistics (NBS) report. However, structural inefficiencies, compliance issues, low input VAT recovery, especially on services and capital expenditure, and legal ambiguities have hindered its optimal administration, leading to inefficiencies and underreporting.

In a significant stride towards overhauling Nigeria's fiscal framework, the National Assembly has passed pivotal Tax Acts, marking a transformative phase in the administration of Value Added Tax (VAT). These reforms aim to streamline tax processes, enhance compliance, align closely with international best practices, and bolster revenue generation, while

fostering a more equitable economic environment.

Key changes to VAT by the new Acts

The newly signed Acts, effective from January 1, 2026, repealed the VAT Act (VATA), and introduce a modernized framework under the Nigeria Tax Act (NTA) 2025 and Nigeria Tax Administration Act (NTAA) 2025 (jointly referred to as "The Acts"). Although, it is important to state that some sections of the VATA were replicated in the Acts. Some of the key changes introduced under the Tax Reform Acts are as follows:

1. Retention of the VAT rate at 7.5%

Initially, the Presidential Committee on Fiscal Policy & Tax Reforms (PCFPTR) proposed an increase in VAT rate to 10% in 2025, 12.5% between 2026–2029, and 15% by 2030. However, following the consultations with the Nigeria Governors' Forum (NGF) and various stakeholders, the VAT rate remained at 7.5%. The decision aims to balance the government's revenue objectives with the need to avoid overburdening businesses and consumers in the current inflationary climate.

2. VAT payment as a condition for expense deductibility

A significant change in the new reform framework is the requirement for VAT payment on all taxable (VAT-able) transactions/supplies as a basis for expense deductibility for income tax purposes.

Pursuant to section 21(p) of the NTA, any expense on which VAT is due but not charged, or in the case of imported items, any expense on which the applicable import duty or levy was not paid, will not be allowable for deductions.

Similarly, for capital assets, where VAT is due but not charged, or in the case of imported items, where the applicable import duty or levy was not paid, such assets shall not be eligible as qualifying capital expenditures for capital allowances purposes.

This aligns with the principle of accountability and helps curb practices where businesses delay remitting VAT while enjoying deduction benefits and claiming capital allowance on qualifying capital expenditure (QCE). In addition, the requirement that VAT must be charged on QCE, and that all applicable import duties (except where waiver is granted) must be fully paid before capital allowance can be claimed, further strengthens compliance. This provision not only ensures proper tax treatment of capital assets but also helps address and curb smuggling, particularly situations where goods or assets are brought into the country without payment of import duties. It is therefore advisable for companies and business owners to self-charge VAT on any expenses or assets that are VAT-able whenever they become due, even if VAT was not included on the vendor's invoice.

3. Expansion of input VAT claim to services and assets

Based on section 155(4) of the NTA, input VAT is now explicitly claimable on any taxable supply, including services and fixed assets, but only to the extent that the input tax was incurred for consumption, use, or supply in the course of making taxable supply.

For example, where a hotel pays VAT to fix its generators and air-conditioning units, the VAT is considered claimable because the repairs support the hotel's taxable hospitality services; hence, making the input VAT on such repairs to be recoverable. On the other hand, if the generator is used partly for VAT-exempt activities or other purposes for which output VAT is not charged, only the portion relating to VAT-able activities is claimable. Similarly, where a manufacturing company hires an engineering consultancy for plant optimization or calibration services for factory equipment, such VAT

is claimable because the service was consumed, necessary, and directly related to the making of taxable supplies (manufactured goods). Therefore, the input VAT is claimable. If the consultancy covered both taxable and VAT exempt items, the input VAT must be apportioned.

This is a welcome development as input VAT on services and fixed assets were previously not claimable under the VAT Added Tax Act (VATA).

This new provision addresses the long-standing issues that have always been associated with Section 17 of the repealed VAT Act, whereby input VAT was only claimable on VAT-able goods used for production or which were purchased for resale, and upon which output VAT was charged. According to the NTA, where input VAT is incurred on making both taxable and non-taxable supplies, only the portion incurred in making taxable supplies would be deductible from output VAT. Furthermore, the allowable input VAT shall only be available for deduction within five (5) years after the end of the tax period in which the input tax was incurred.

Notwithstanding, the claimable input VAT on services, fixed asset, and overheads, is limited to taxable supplies made as from the commencement of the NTA (i.e., 1 January 2026).

The expansion of input VAT to services and fixed assets widens the base for VAT credits and encourages capital investments. Businesses investing in assets such as equipment or procuring professional services can now offset the input VAT paid against output VAT, provided it is used for making taxable supplies, thereby reducing their VAT payable and ensuring a healthy cash flow position.

4. Fiscalisation and E-Invoicing

Under section 157 of the NTA and section 23 of the NTAA, businesses making taxable supplies are now required to implement the electronic fiscalisation system deployed by the Service to accurately record and report all taxable supplies. The fiscalisation system may include fiscal equipment consisting of electronic devices, software solutions, or a communication system involving a secured network, or any such combination of the components for electronic invoicing and data transfer as the Service may prescribe or deploy. This requirement is designed to streamline the tax reporting process, enhance compliance, and combat tax evasion.

Non-compliance with the fiscalisation system attracts significant administrative penalties. Specifically, businesses or individuals that refuses to grant access to the relevant tax authority to deploy technology after 30 days of receipt of the notice are liable to an administrative penalty of NGN 1,000,000 for the first day of default and NGN 10,000 for each subsequent day of default. While failure to process taxable supplies through the fiscalisation system will result to an administrative penalty of NGN 200,000, in addition to 100% of the tax due, along with interest at the prevailing Central Bank of Nigeria (CBN) monetary policy rate (MPR) per annum.

Based on the underlying provision, the Nigeria Revenue Service (Formerly the FIRS), introduced the Merchant Buyer Solution (MBS), a digital e-invoicing platform aimed at improving transparency and efficiency in Value Added Tax (VAT) administration. The MBS enables real-time transaction reporting, reduces manual errors and revenue leakages, and curtails tax evasion.

Currently, migration to the MBS platform is in phases starting with companies with an annual turnover of NGN5 billion and above (i.e., large taxpayers), while other categories of taxpayers will migrate at a date as set by the Service based on the recent public notice rolled out on 17 February 2026 (stating the timeline for medium and emerging companies). It is important to note that 1 November 2025, was initially set as the deadline for large taxpayers; however, enforcement has been scheduled between April and June 2026.

We anticipate that the migration process for medium-sized and emerging companies will be streamlined to minimize cost implications and ease the required system integrations. Our firm is also available to support the onboarding process to ensure a smooth transition and full compliance with all regulatory requirements.

5. VAT refunds and credits

Prior to recent tax reform, VAT refund processes were not clearly defined in the enabling legislation; hence it was practically difficult if not impossible to get a refund under the repealed law. Contrarily, the reforms through The Acts clarify the processes for obtaining VAT refunds and the utilization of VAT credits. Pursuant to section 157 of the NTA, where input VAT exceeds the output VAT, companies can utilize the excess as a credit against subsequent months, provided that any excess not utilized as a credit will qualify for refund upon request to the Service. This is to enhance tax efficiency while easing the burden and supporting businesses cash flow position. It is pertinent to state that the refund is not automatic as affected taxpayers are required to request the refund from the NRS not later than 12 months after

the transaction giving rise to the refund and provide relevant documentation as the NRS may require. Where a valid VAT refund request is submitted, the NRS is required to process and refund the tax amount within a period not later than 30 days of the receipt of the request, or the amount shall be eligible for set-off against any tax liability of the taxpayer. The refund process would be expedited without the need to carry out a tax audit, which has often delayed refunds in the past, making it easier for businesses to maintain adequate working capital. Though special audit is not the precondition for granting VAT refund, it is important to note that the Service may conduct some reviews afterwards to confirm the eligibility and accuracy of the amount refunded.

The beauty of the VAT refund system under the NTA is that it can be used to offset income tax liability or any other tax liabilities such as WHT, Stamp Duties, PAYE, Development Levy, etc. This is a positive development, as the previous system only allows taxpayers to offset tax refunds with the same tax type. This will undoubtedly assist manufacturing companies that may have accumulated input VAT on capital assets and purchases. It is important to note that any input VAT incurred in making VAT-exempt supplies does not qualify for input VAT claims or refund, as the input VAT paid in making VAT-exempt supplies is required to be expensed.

While this system will be beneficial, it is imperative for businesses to maintain adequate records to benefit from the refund mechanism. The tax refund process will be automated, subject to guidelines to be issued by the Service.

6. VAT compliance thresholds for small businesses

The Acts introduce compliance thresholds, exempting businesses that meets the defined criteria from VAT registration, collection, and filing obligations. This move aims to reduce the compliance burden on small businesses to enhance their growth.

According to the Nigeria Tax Administration Act (NTAA) 2025, a small business is defined as one with an annual gross turnover of NGN 100 million or less and total fixed assets not exceeding NGN 250 million, excluding businesses that provide professional services, which are not eligible for this classification. Businesses that meet the specified threshold are not required to register, charge VAT, pay and submit monthly returns to the Service.

This represents a significant departure from the NGN 25 million revenue threshold introduced under the Finance Act 2019, which required businesses exceeding NGN 25 million in annual turnover to comply with VAT obligations.

This exemption would allow small businesses to focus on their core operations without the added strain of complying with VAT obligations, potentially stimulating growth and encouraging more informal businesses to formalize their operations.

Additionally, businesses below the threshold must still maintain proper records and remain compliant to other relevant tax obligations.

Notwithstanding the above, subject to section 22 of the NTAA, small business may, subject to a written notice addressed to the Service, choose to opt out of the exemption granted, including registration, charging of tax on its taxable supplies, payment of VAT, and filing of returns. Where a company has ceased to be a small company, such company is required to file monthly VAT returns and comply with all VAT obligations.

It is important to note that the exemption of small businesses from VAT obligations does not imply blanket tax exemption for the contracting parties, as the taxable persons dealing or transacting with small businesses are required to self-charge and remit VAT on the receipt of a taxable supply from small businesses.

Considering that small businesses are exempt from VAT registration, filing, and payment under Section 22 of the NTAA, the requirement for large businesses to charge output VAT on taxable supplies may create a significant compliance bottleneck when dealing with such exempt entities. Large suppliers are obligated to charge VAT on taxable supplies, yet the contracting party being a small business is legally exempt from paying VAT, creating a practical mismatch in the transaction flow. This disconnect may expose large businesses to potential VAT risks or administrative challenges and could consequently pressure small businesses to opt out of the exemption in order to maintain seamless transactions with their larger suppliers. This challenge does not arise in transactions between large businesses, as output VAT is charged, collected, and remitted in the normal course of business.

7. Reclassification of taxable supplies

One of the significant changes introduced in the Tax Reform Acts is the reclassification of taxable supplies to reflect the prevailing socio-economic realities.

Under the VATA, essential items such as basic foodstuffs, medical supplies, and educational materials, were listed as VAT-exempt. However, the Acts reclassified these essential goods and services as zero-rated. The implication of this shift is that while these items will still not attract VAT, businesses involved in their production and supply can now claim the input VAT incurred in supplying

these zero-rated items, thereby reducing their cost of production, preventing the hike in price and improving cash flow efficiency.

Conversely, goods and services purchased by diplomatic missions, which were previously treated as zero-rated, are now classified to be VAT-exempt. This means that while such purchases will not be charged VAT, the suppliers will no longer be able to claim input VAT on the supply of these items, representing a shift in the tax benefit structure available to them.

Also, Airline transportation tickets issued and sold by commercial airlines registered in Nigeria which were previously exempted from VAT is no longer included in the VAT exemption list, creating increased tax obligations for businesses operating in this sector and which might also lead to increase in the prices of airline ticket.

Additionally, the reform introduces a new category for specific items whose VAT is suspended or delayed. These include:

- Petroleum products
- Renewable energy equipment
- Compressed Natural Gas (CNG)
- Liquefied Petroleum Gas (LPG) and
- Other gaseous hydrocarbons

These items are classified as VAT-suspended, meaning VAT will not be charged on their supply until a date to be specified by the Minister of Finance or when it is deemed necessary in the public interest, as determined through an Order published in the Official Gazette. This provision gives the government the flexibility to manage fiscal impacts while responding to sectoral needs, especially in critical areas like energy, transportation, and environmental sustainability.

These reclassifications reflect a strategic fiscal policy approach aimed at boosting critical sectors of the economy, enhancing the affordability of essential goods, and reducing tax-induced distortions in sectors with high social and economic impact.

8. Distribution of VAT Revenue

Due to the significant rise in VAT revenue since its increase from 5% to 7.5% in 2020, State Governments continue to benefit from monthly VAT allocations from the Federation Account. Based on section 40 of the VAT Act, 15% of the VAT revenue goes to the Federal Government, 50% to states and 35% to local governments. The 50% and 35% allocated to states and local governments are further distributed based on three criteria: 50% equality, 30% population, and 20% derivation.

However, this distribution method has faced sustained criticism. Some States argue that the model is unfair, as it does not reflect their actual contributions to VAT revenue. They believe the criteria favor less economically active States, thereby widening the fiscal imbalance. Particularly, the “equality” component, which takes the higher percentage, means all States receive the same amount regardless of how much VAT they generate.

The population factor also raises concerns, as the last official census was conducted in 2006. With current figures based on outdated data and no recent national census, many believe the population estimates used for distribution are no longer accurate, especially in light of recent migration trends across States for economic reasons.

The derivation principle, while intended to reward States where VAT was generated, has mostly benefited states who host company’s headquarters. This is because VAT collection was linked to the location of the taxpayer’s tax office rather than where the actual transaction or consumption occurred.

To address these issues, the VAT allocation formula has now been revised to 50% equality, 30% consumption, and 20% population. This new structure seeks to balance fairness, encourage economic activity, and maintain national cohesion.

For the purpose of collating accurate and reliable VAT figures attributable to each State, taxpayers are required to comply fully with VAT attribution rules. Accordingly, VAT returns must disclose detailed information on the consumption of taxable supplies, regardless of the State in which the VAT return is filed. Failure to comply with this requirement attracts an administrative penalty of NGN 1million (Section 106 of the NTAA).

To facilitate smooth implementation, the tax authority is expected to issue a guideline prescribing the required reporting format, detailed implementation guideline to support taxpayers and configure the tax portal to enable seamless compliance with the VAT attribution requirements.

In conclusion, the revised formula for VAT distribution reflects Nigeria’s ongoing effort to build a more equitable and transparent fiscal framework.

Strategic implementation guidelines for businesses and individuals

These tax reforms signal a shift toward a more digitalized, transparent, and equitable VAT system. Businesses should:

- Reassess their accounting systems to align with e-invoicing, and other fiscal tools and guidelines to be released by the NRS.
- Update accounting systems to reflect new VAT classification.
- Ensure timely filing and payment of VAT to avoid penalties as well as keeping proper books/ records for claiming input VAT deductions.
- Keep track of input VAT and revisit cash flow models to adjust procurement/investment strategies to fully leverage the expanded scope of claimable input VAT.
- Stay updated on the circulars or guidelines to be issued by the NRS or Minister for the administration of VAT.
- Ensure training of finance personnel or tax schedule officer on the new compliance requirements, documentation standards, and audit preparedness. Failure to adapt promptly could expose businesses to penalties, missed refund opportunities, or denial of tax credits.

Conclusion

The tax reforms mark a transformative phase in Nigeria’s approach to VAT, both from administrative and compliance perspectives, as it remains one of the major sources of tax revenue for the Government. As implementation kick starts, we hope that the Nigeria Revenue Service (The NRS) will issue the relevant guidelines that will enhance administrative efficiency, provide clarity to taxpayers, increase taxpayers’ confidence, and simplify compliance mechanism.

To ensure compliance and support strategic financial planning, businesses and individuals must have a clear understanding of the relevant provisions relating to VAT, maintain accurate documentation, and implement the electronic fiscal system (EFS). As implementation progresses, stakeholders are encouraged to collaborate and comply in pursuit of a fair, efficient, and growth-oriented tax system. It is therefore necessary for companies and business owners to seek expert advice and guidance and stay updated through official publications and implementation guidelines that may be released by the Service from time to time.