Hirko and Associates (HALO) Legal Update

Investment Incentives Regulation No. 586/2026

A Comprehensive Reform Introducing a Performance-Based, Contract-Driven Investment Incentive Framework Designed to Strengthen Fiscal Discipline and Ensure Measurable Economic Contributions

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1. INTRODUCTION AND REGULATORY CONTEXT

On 20 January 2026, the Council of Ministers approved a new legal framework governing investment incentive as part of broader reforms aimed at strengthening fiscal discipline, customs administration, and private sector development. The enactment of Investment Incentives Regulation No. 586/2026 repeals and replaces the prior regime under Investment Incentive Regulation No. 517/2022, marking a fundamental restructuring of Ethiopia's tax and customs incentive architecture.

The Regulation introduces a performance-based incentive model that directly links tax and customs benefits to measurable economic contributions, including capital deployment, employment creation, technology transfer, export generation, and value addition

2. STRUCTURAL SHIFT TO A PERFORMANCE-BASED MODEL

The most significant reform under the new Regulation is the shift from a broadly entitlement-oriented system to a conditional and contract-based regime. Incentives are no longer automatically secured upon sector qualification; rather, they are contingent upon demonstrable performance and subject to continuous oversight.

This approach reflects a policy objective of ensuring that tax expenditures translate into tangible economic outcomes while preserving fiscal sustainability.

3. OBJECTIVES AND GOVERNING PRINCIPLES

The Regulation is designed to promote strategic sectors and national development priorities, including agriculture, manufacturing, import substitution, environmental protection, mining and energy development, technology-driven enterprises, and balanced regional growth.

4. MANDATORY PERFORMANCE AGREEMENTS

At the center of the new regime is the mandatory Performance Agreement. The government's Investment Institution is required to conclude a legally binding contract with each eligible investor before incentives are granted.

The Agreement must clearly define measurable performance indicators, such as investment capital committed, employment targets, production capacity, export performance, and technology transfer commitments. Failure to meet these obligations may result in suspension or revocation of incentives, with recovery mechanisms to be determined by directive of the Ministry of Finance.

This contractual mechanism represents a decisive enforcement innovation compared to the previous regulatory framework.

5. GENERAL CONDITIONS APPLICABLE TO ALL INCENTIVES

Incentives are subject to uniform baseline requirements.

- An investment must create additional production capacity or measurable value addition.
- Beneficiaries must be registered taxpayers and maintain separate accounting records for each incentivized project through ring-fencing.
- Incentives are time-bound and non-transferable unless expressly permitted, and overlapping incentives are prohibited except where explicitly authorized.

6. INCOME TAX INCENTIVES

A. Special Economic Zones

Special Economic Zone Developers and Sub-Developers recognized by the Investment Board benefit from a reduced income tax rate of 5 percent for ten years from business license issuance. They are also granted dividend tax exemption for five years and exemption from Minimum Alternative Tax for ten years.

Enterprises operating within Special Economic Zones in designated sectors are subject to a reduced 15 percent income tax rate, with sector-specific durations to be clarified by Ministry directive. Fertilizer manufacturing enterprises within SEZs receive a preferential 5 percent rate for ten years.

B. Startups and Ecosystem Builders

Recognized startups benefit from a 5 percent income tax rate for ten years beginning from commencement of business, together with a five-year dividend tax exemption.

Startup ecosystem builders enjoy capital gains tax exemption on disposal of startup shares and dividend exemption for five years. Investors in startups who can demonstrate financial losses may claim exemption from Minimum Alternative Tax for up to three years, limited to the extent of losses incurred.

C. Environmental and Renewable Energy Incentives

Companies participating in recognized carbon or emissions trading systems qualify for a reduced 15 percent income tax rate for ten years. Investors transitioning to at least 50 percent renewable self-generated energy, or utilizing at least 50 percent locally sourced recycled materials, qualify for a 15 percent rate for five consecutive years, subject to certification and annual audit verification.

D. Scientific Research and Capital Market Incentives

Expenditures incurred for scientific research connected to business activities are deductible, excluding capital assets, land, buildings, and natural resource exploration costs. Companies that publicly list shares on a securities exchange licensed by the Ethiopian Capital Market Authority are entitled to a reduced 25 percent income tax rate for three years from the date of initial public offering, provided continuous regulatory compliance is maintained.

7. INVESTMENT CAPITAL ALLOWANCE

Investors in priority sectors making a minimum capital investment of USD 2 million may deduct qualifying capital expenditures on capital goods and building materials. The allowance applies only to assets owned by the taxpayer and used for generating taxable income, commencing when such assets are placed into service. In the case of leased assets, deductibility is limited to actual lease payments made.

8. CUSTOMS DUTY AND TAX INCENTIVES

Special Economic Zone Developers (SEZs), Administrators, and Enterprises may import capital goods and construction materials free of customs duty and taxes without quantitative or temporal limitations.

Investors outside SEZs operating in approved sectors may import capital goods and construction materials duty-free for new investment projects, subject to prior approval of item lists and supporting documentation. Transfers of incentivized goods are permitted upon payment of applicable duties, re-export, or transfer to similarly entitled beneficiaries in accordance with Ministry directives.

Local manufacturers supplying eligible investors may obtain refunds of import duties paid on raw materials used in producing qualifying goods.

9. MINING, PETROLEUM, AND ENERGY SECTOR INCENTIVES

Exploration and production license holders in mining, petroleum, and geothermal sectors may import machinery, drilling equipment, aircraft, specialized vehicles, fuels, and other operational inputs free of customs duties in accordance with approved work programs.

Value addition activities, including refinery and processing operations, qualify for incentives for limited periods. The Investment Board retains discretion to grant additional incentives for strategically significant projects. Alternative thermal energy projects, including biofuel initiatives, qualify for incentives for up to five years from license issuance.

10. INSTITUTIONAL ADMINISTRATION AND OVERSIGHT

The Regulation establishes a structured oversight system involving Investment Institutions, the Tax Authority, the Customs Commission, and the Ministry of Finance.
Investment Institutions are responsible for processing applications, concluding Performance Agreements, conducting monitoring inspections, and submitting annual performance reports. The Tax Authority and Customs Commission maintain records of granted incentives, track forgone revenue, conduct audits, and submit periodic reports. The Ministry of Finance exercises directive authority, consolidates fiscal impact data, conducts cost-benefit analysis, coordinates complaint resolution, and submits annual reports to the House of Peoples' Representatives.

11. ENFORCEMENT MECHANISMS

Investors whose licenses are revoked must return improperly obtained incentives in accordance with procedures to be determined by directive. Public officials who fail to submit required reports without good cause may be fined up to three months' salary. Institutions failing to submit mandatory annual reports will have pending incentive applications deemed rejected until compliance is restored.