MENA-OECD INVESTMENT PROGRAMME

Organisation for Economic Co-operation and Development

Tax Incentives and FDI Performance

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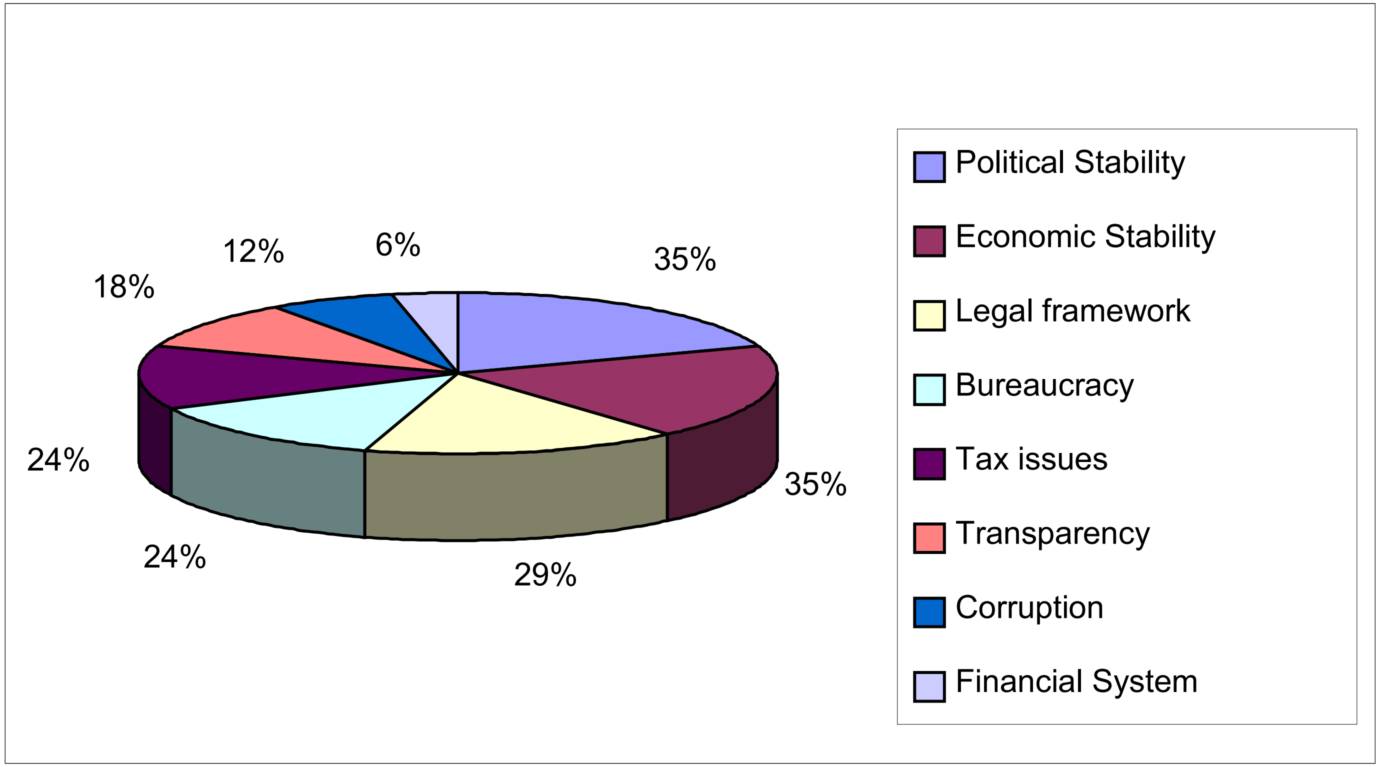
Centre for Tax Policy and Administration

Major Obstacles to Investment

- Strategic investors



Source: OECD(2003): from Investors Survey in SEE

Important Tax Policy Factors for Investment

FIGURE 5.1 – TAX POLICY ASSESSMENT FRAMEWORK

Tax Policy Assessment Framework

Tax Policy and Legislation

- Statutory Corporate Tax Rate
- Tax Incentive Scheme
- Tax Treaty Network
- Transfer Pricing
- Depreciation Allowances
- Loss Carry Forward

Tax Administration

- Revenue Agency
- Tax Inspection Authority
- Right to appeal
- VAT (Value Added Tax) Reimbursement

Compliance Costs

- Filing Taxes: Time Required and Complexity
- Stability of the Taxation Framework

Transparency

- Public/Private Consultations
- Monitoring and Evaluation
- Communication and Information Access

Source: OECD Investment Compact.

Pros and cons of main tax incentives

	PROS	*CONS*
Tax Holidays	Relative low compliance and administrative costs	Only targeted to new investment Deny certain deductions Tax planning opportunities
Reduction of CT rate	Attractive for mobile investors Easy to administrate	Discriminate against other businesses Effects on debt finance (↑cost) and capital allowances (↓PNV) Tax planning opportunities
Accelerated capital allowances	Helps with liquidity constraints	Advantages only with loss carry-forward provisions
Investment Tax Credits	Large impact on ETR at lower revenue cost	Only targeted to new investment Large impact with short-lived assets
Reduced taxes on dividends and interest	Incentives for co-investment between domestic and foreign investors	Tax-shifting

Main tax incentives used in the MENA region, 2004

	Tax holidays (years)	Reduced CIT	Exemption CIT for exports	Accelerated depreciation	Location-based incentives	Exemption from indirect taxes/ duties	Export/ free zones
Algeria	10	no	yes	yes	yes	yes	no
Bahrain	-	-	-	-	-	manufacturers	yes
Egypt	5-10-20	for exports	no	yes	yes	in specific zones	yes
Jordan	2-12	sector specific	yes	yes	yes	sector and location specific	yes
Kuwait	10	no	no	no	no	on production items	yes
Lebanon	10	location specific	no	no	yes	sector specific	yes
Morocco	5	exports and sector specific	yes	yes	yes	export and sector specific	yes
Oman	5 + 5	no	no	no	no	some imported goods	yes
Qatar	5 + 5	no	no	no	no	on particular production inputs	no
Saudi Arabia	10	no	no	yes	no	for industrial projects	no
Syria	5	no	no	no	no	on production inputs	yes
Tunisia	10	sector specific	yes	yes	yes	exports only	yes
UAE	-	-	-	-	-	in free zones	yes
Yemen	7	no	no	no	no	on project fixed assets	yes

Source: OECD (2005), Investment climate statements of the US State Department, United Nations (2000), and National countries investment and tax laws.

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Effectiveness of tax incentives

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- Other Regions
  - **Uganda (1997)**
    - Elimination of tax holidays
    - 30 % CIT, generous capital allowances and unlimited loss-carry forward
    - *Results*: ↑1ppt ratio investment to GDP, 70% ↑ in FDI inflows and ↑ tax revenue by 1% of GDP
  - **Indonesia (1984)**
    - CIT: 45%→35%
    - Elimination of selective tax incentives (tax holidays, preferential rates, special investment allowances and selective accelerated depreciation)
    - *Results*: ↓FDI inflows (in value terms) but quickly ↑after 1987

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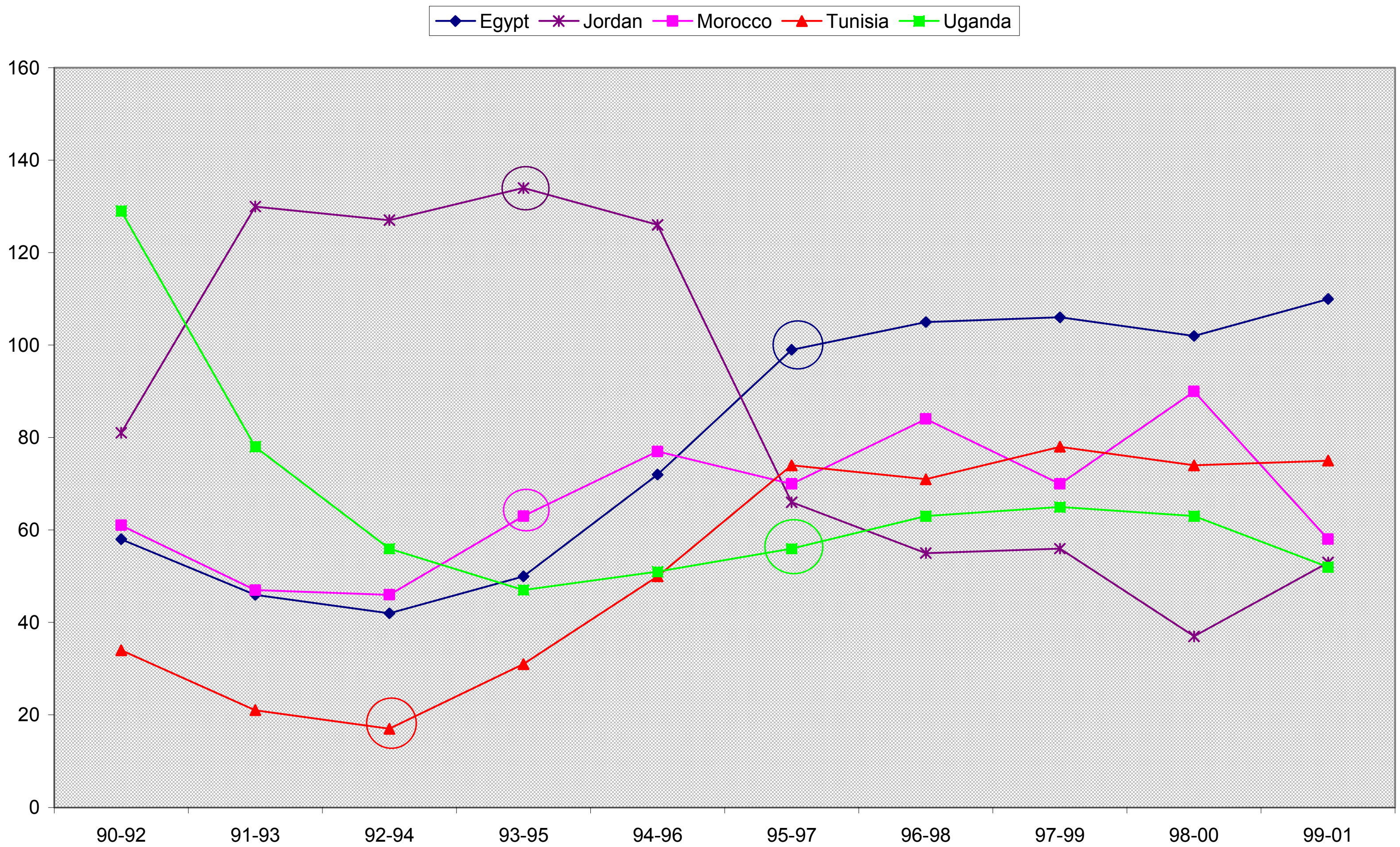
Effectiveness of tax incentives (cont'd)

- MENA
  - **Morocco (2006)**
    - Introduction of Tax Expenditure Report
    - *Results*: Positive but decelerated effect of tax incentives on private investment
  - **Egypt (2005)**
    - New Income Tax Law:
      - CIT 40% →20%
      - Elimination of income tax exemptions
      - Unified corporate tax rates across industries
    - *Results*: 2005-2006 FDI flows almost double in value terms
  - **Tunisia,** *FIAS Study (2002)*
    - 1996-2001:↓ effectiveness of incentives due to distortions (in access, among assets and across sectors), duplication of instruments to reduce CT and non-coherence between the multiple system of incentives and other aspects of economic policy
  - **Jordan,** *Institute for International Business-University of Toronto*
    - Incentives system too complicated and inefficient
    - Not success in attracting investments and eroding tax revenues

FDI Performance Index



Source: Own elaboration using FDI Performance Index from World Investment Report 2006 UNCTAD

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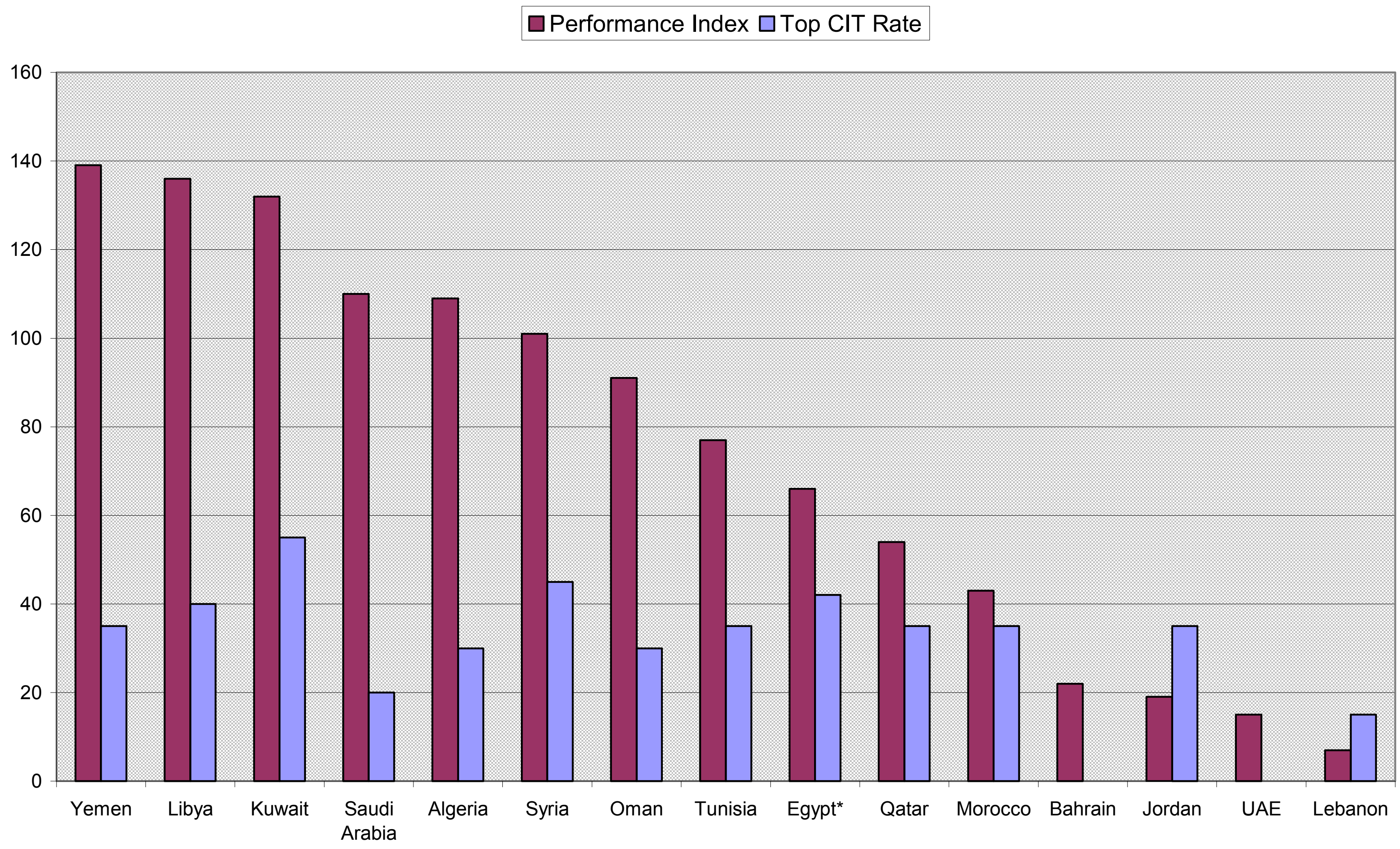
Statutory Corporate Tax Rate and Inbound FDI Performance Index, 2005



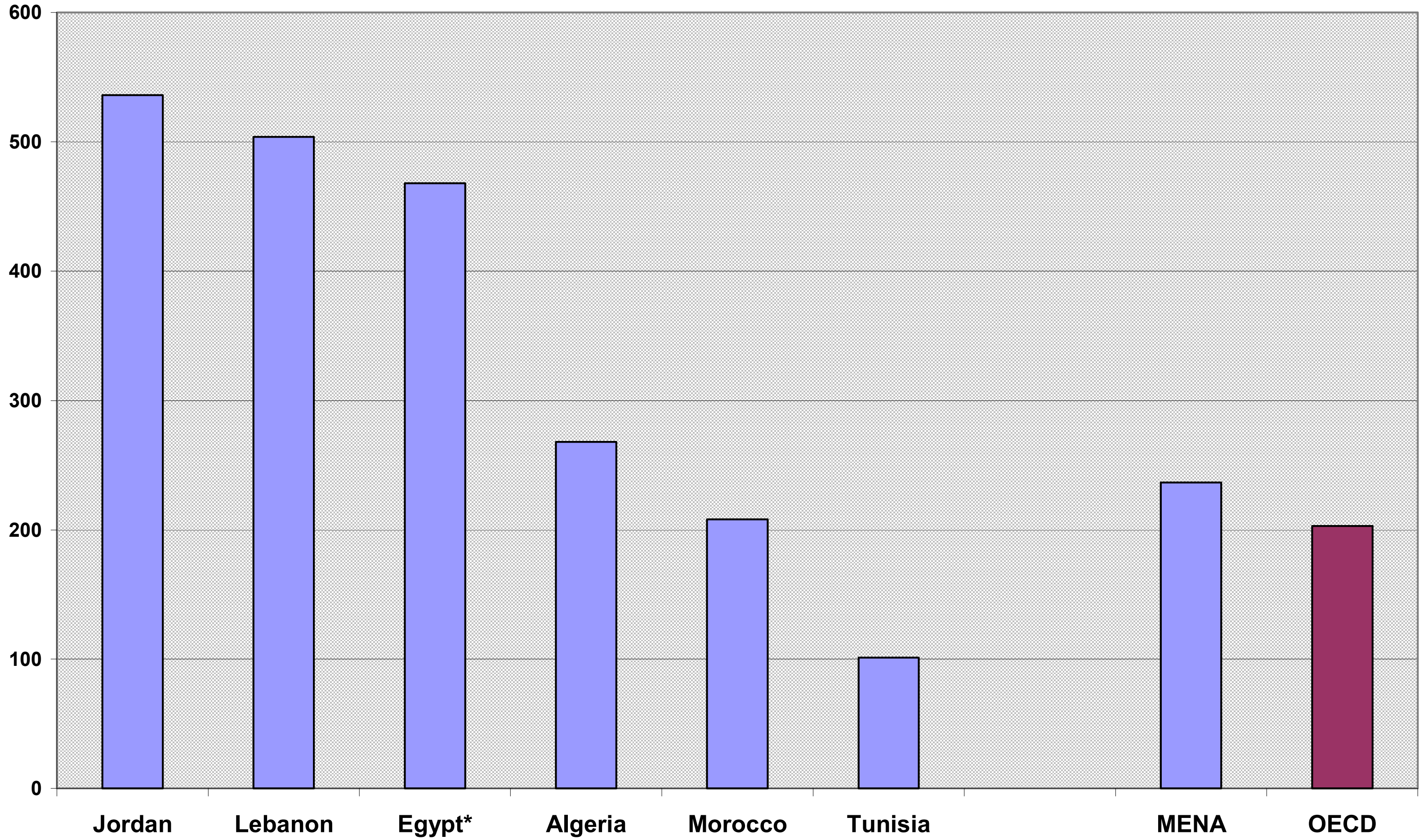
Source: OECD (2005), FDI Performance Index from World Investment Report 2006 UNCTAD, Investment climate statements of the US State Department, and National countries investment and tax laws.

Overview of tax characteristics affecting FDI in MENA countries as host countries

Country	Top CIT Rate	Non-resident withholding tax: dividends	interests	royalties	Capital Cost Write offs	Loss carry forward (years)	Transfer pricing rules	Thin capitalisation rules
Algeria	30	15	10	20?	acc	yes		
Bahrain	-	-	-	-	-	-	no	no
Egypt	42	-	32	32	acc	5	no	no
Jordan	35	-	10	10	acc	indefinitely	no	no
Kuwait	55	-	-	-			yes	no
Lebanon	15	10	10	7.5			no	no
Libya	40							
Morocco	35	10	20	10	acc	4		yes
Oman	30							
Qatar	35						no	no
Saudi Arabia	20	5	-	5-20	acc		no	no
Syria	45							
Tunisia	35	-		15	acc	4		
UAE	-	-	-	-	acc	indefinitely	no	no
Yemen	35	-	-			4	no	no

Source: OECD (2005), Investment climate statements of the US State Department, United Nations (2000), and National countries investment and tax laws.

Compliance time (hours), 2005



Source: : Doing business, World Bank, 2005.

Conclusions

- Wide range of incentives in MENA countries
- Investors prefer transparency, simplicity, stability and certainty in application of tax law and in tax administration
- Tax incentives not very effective attracting investment
- Best practice: discourages use of incentives in favour of reduced CTI rate on broad base
- When tax incentives offered, need of reviewing design and assessing effectiveness

Thank you for your attention

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