MENA-OECD INVESTMENT PROGRAMME

INCENTIVES AND FREE ZONES IN THE MENA REGION: A PRELIMINARY STOCKTAKING

- Working Group 2 -

Hans Christiansen, tel. +33 1 45 24 8817, e-mail: hans.christiansen@oecd.org

Contact:
Alexander Böhmer, tel. +33 1 45 24 1912, e-mail: alexander.boehmer@oecd.org

TABLE OF CONTENTS

OECD OCDE

MENA – OECD INVESTMENT ROGRAMME

INCENTIVES AND FREE ZONES IN THE MENA REGION: A PRELIMINARY STOCKTAKING

1. The purpose of the present paper is to take a first step toward a comparative inventory of free economic zones (FEZ) in the MENA region with special regards to the incentives that they offer to investors. The paper is based almost exclusively on open sources, namely the publications listed in the bibliography and the websites of national governments, investment promotion agencies and zone authorities. It will therefore be incomplete, in some cases be short on hard data, and definitely suffer from a reporting bias as not all relevant bodies have been equally transparent or detailed in their reporting. It is hoped that the discussions in Working Group 2 will provide a forum for information gathering and peer review, on the basis of which an inventory reflecting the shared view of the "zone situation" in MENA may eventually be produced.

2. The stocktaking of zones and incentive regimes in Annex 1 covers certain areas of general investment policy as well (most of which drawn from OECD, 2003 and the US Department of State's Country Commercial Guides). This is necessary to put the relative "generosity" of the special arrangements of investors into perspective: where investors are offered derogations from regulatory provisions elsewhere in the economy, the attractiveness of the derogations can be assessed only in light of these provisions. Also, the relevance to investors of the tax incentives that are offered in most countries and in all zones depends on the general levels of taxation of businesses and individuals in the host economy.

I. Toward a common definition of incentives and FEZs

a) Investment incentives

3. There is a grey area between, on the one hand, investment promotion and facilitation, and investment incentives on the other. Investment promoters may make information about their host location, relevant laws and administrative procedures available as a public good, but as soon as they offer facilitation and matchmaking tailored to the needs of individual investors then they are effectively subsidising these investors. The monetary value to investors of such assistance may in some cases exceed the value of outright investment incentives. Conversely, actual investment incentives are normally considered as falling into three categories, namely "regulatory", "fiscal" and "financial" incentives[1]:

- ***Regulatory incentives*** are policies of attracting investment projects by offering derogations from national or sub-national rules and regulation. Where such derogations are offered on an economy-wide basis they tend to focus on the environmental, social and labour-market related requirements placed on investors. In the context of FEZs, they often consist in the relaxation of direct investment regulations (e.g. nationality requirements; screening and authorisation procedures) in place elsewhere in the host economy.

- ***Fiscal incentives*** consist of an easing of the tax burden on the investing companies or their employees. Unlike many other incentives they are most commonly rules-based as changes in

[1] The remainder of this section builds in essence on OECD (2003).

taxation in most cases require legislative action. General fiscal incentives normally take the form of reduced corporate tax rates or tax holidays; encouragement of capital formation (e.g. investment tax credits and accelerated depreciation allowances); and preferential treatment of foreign operators (e.g. lower tax on remittances; reduced personal income tax rates on expatriates). In FEZs fiscal incentives, virtually by definition, also include lower import and export taxes and tariffs.

- ***Financial incentives*** consist of out of hand public spending to attract companies or induce them to invest. They are often formally justified by a need to compensate investors for the perceived disadvantages of a particular location ("site equalisation outlays"), or may take the form of tailoring the infrastructure of a prospective location to the needs of investors. Other financial incentives include subsidising the actual costs of relocating corporate units (e.g. job training cost; expatriation support; and temporary wage subsidies).

4. In the case of FEZs, a second grey area exists between financial incentives and generic spending to enhance the investment climate. Public spending to enhance infrastructure such as the electricity grid, ICT access, roads and sanitation clearly does not qualify as an investment incentive if it applies to most or all of the host country. Conversely, if tailored to the needs of individual investors it constitutes a financial incentive. Outlays to enhance the investment climate locally in FEZs is somewhere between these two extremes. In the remainder of this paper such spending is referred to as ***quasi-incentives***.

b) Free economic zones

5. The terminology applied to FEZs, in literature and common usage, is highly confusing. Words like "free zones", "free trade areas", "customs-free zones", "special economic zones", "export processing zones", etc. are in practice used almost interchangeably. This reflects the implementing authorities' linguistic preferences as much as functional differences between different kinds of zones. However, some main differences can be identified. Again, for the purpose of this paper, the term "free economic zones" has been chosen as the term applying to all such establishments. Common to all FEZs is the fact that they are ring-fenced enclaves exempt from national import and export duties and/or formally operating outside the customs area of their host country. Conversely, ring-fenced areas offering tax concessions other than customs exemptions (e.g. the "industrial parks" that have proliferated in many MENA countries) are not included, on the grounds that they are functionally indistinguishable from investment incentives applied locally[2].

6. Part of the linguistic confusion derives from the way FEZs have developed over time. The first FEZs mostly took the form of free ports – customs free areas within seaports offering little more than warehousing and trade facilities. Over time, some free ports developed into customs-free zones in which light manufacturing and other processing took place. The next step was the development of export processing zones, which encourage more complicated manufacturing operations with the purpose of re-export. Finally, special economic zones (SEZ) evolved, which offered not only customs exemptions but also an entirely separate regulatory environment from the rest of the host economy. In the remainder of this paper, the following three categories of FEZs are identified:

---

[2] This implies that the concept of FEZs in the present paper is somewhat narrower that the commonly quoted definition by Grubel (1984): "a geographically defined area within which certain types of economic activity take place without some of the government taxation and regulation that applies to them in the rest of the economy".

- ***Free zones***. This category covers the ground from free ports to export processing zones – FEZs that are generally accessible to investors, but do not go as far as offering a tailored regulatory environment.

- ***Special economic zones.*** SEZs are basically ring-fenced customs-free areas with a regulatory environment of their own. They are mostly backed by a piece of legislation establishing a governing council for each individual SEZ and mandating it to enact rules that shall apply to investors within the zone.

- ***Industry zones.*** These are basically free zones, but targeted at specific sectors or economic activities. Industry zones (IZ) may restrict the access of companies in non-priority sectors, and their infrastructure is mostly tailored according to their sectoral targets.

7. Finally, it should be noted that the distinction between the different kinds of zones must involve an element of judgement. For instance, most free zones restrict the access of certain categories of investors, without for that reason being classified as industry zones. Also, it is not a priory clear how "special" a free zone's regulatory environment must be before it can be classified as an SEZ.

II. Synthesis of main findings

8. First, referring to practices to attract investment in the MENA region as a whole will frequently be an oversimplification: the intra-regional differences are major. Some of the MENA countries offer a quite good physical investment climate (e.g. modern roads, ports and electricity grids), a reasonably well-educated labour force, and have at least taken steps toward raising administrative and regulatory efficiency. However, more remains to be done, and investors are much stronger attracted to some economies than to others.

9. As a general rule, foreign investors have taken an interest in the oil-rich countries in the Gulf area, largely in the context of market-seeking investment aimed at producing locally for consumption within the region. Several of the North African countries, developing their economies against the background of evolving trade patterns with the European Union, have attracted a fair amount of "efficiency seeking" investment aimed at producing locally for export markets. Other MENA countries show mixed patterns and, as a corollary, their efforts to attract investment follow more hybrid strategies.

10. One aspect that countries in the region appear to have in common (and, as demonstrated by a recent OECD study, in common with Asian economies as well[3]) is that investment attraction strategies have increasingly taken the role of the interventionist industrial policies of the past. As the state in many cases disengages from the private economy, selective or sectoral liberalisation of the access of foreign investors, performance requirements on foreign and domestic investors, subsidisation of prioritised economic activities, selective access to economic zones and regional discrimination between enterprises have moved to the forefronts as tools for targeted economic and industrial development.

11. An important point relates to the restrictions placed on the access of foreign investors. Many MENA countries are comparatively restrictive in this respect. In addition to restrictions on foreign participation in several sectors (some of which not uncommon in OECD countries either), many countries in the Gulf area apply general limits on the degree of foreign participation in joint stock companies and

3 OECD (2004).

joint ventures. Most countries in the region reserve the right to screen, authorise and licence foreign-controlled investment projects prior to entry. This is potentially more problematic than outright discrimination (such as statutory ownership limits), since it is less transparent and more open to irregular practices. It is also linked with the "targeted" policy approaches mentioned above: several national authorities charged with screening foreign investors are requested to base their decision on factors such as local job creation, the effect on incumbent domestic enterprises and expected export earnings.

a) General incentive schemes

12. As demonstrated in Annex 1, the investment incentives offered in MENA countries differ greatly across the region. Nevertheless, certain general lessons can be extracted from the evidence. Table 1 summarises some of the most important incentives that are available to investors in individual countries. The incentive schemes included in the table are not contingent on being located in an economic zone. They represent the maximum generosity foreseen by national legislation; authorities in most countries have it at their discretion to grant less sweeping incentives to individual projects.

Table 1. Investment incentives generally available in MENA countries

	Type of incentives:			Observations
	Regulatory	Fiscal	Financial	
Algeria		Exemption from corporate and personal income tax, and from property tax. Temporarily reduced customs duty and VAT on items related to the investment.	The state may in some cases finance necessary infrastructure works.	Most incentives are only available under the "special scheme" for projects offering particular benefits to the Algerian economy.
Bahrain	Foreign-invested companies" are exempted from minimum capital requirements, and permitted to hold their board meetings abroad	Manufacturers are exempt from import duties on machinery and input goods.		
Egypt	Guarantees against nationalisation, expropriation and price controls.	Corporate tax holidays from 5 to 20 years.[a] Exemptions equal to paid-in capital of publicly listed companies. Exemption for reinvestment of		

		profits from sales of capital assets. Reduced import duty on equipment needed to carry out the investment.		
Jordan		Corporate tax holidays from 2 to 12 years. Reductions in income and social services taxes for a period up to 10 years. No duty and taxes on imported inputs and capital goods.		Additional incentives are available to industrial investment projects.
Kuwait	Enhanced access to employ foreign nationals.	Exemption from income and other taxes for a period up to 10 years.	Land and certain kinds of infrastructure may be allocated for investment projects.	The fiscal incentives largely apply to foreign investors; Kuwaiti and GCC companies pay no income tax.
Lebanon	Easier access to work permits for foreign employees. An exemption of joint-stock companies from legal provisions regarding board compositions.	Exemption from corporate income taxes and dividend taxes for up to 10 years. Lower custom fees and duties. A reduction or wavering of permit and registration fees.		The access to work permits is conditional upon two thirds of the project's payroll being Lebanese nationals.
Morocco	Exemption from formalities for land acquisition (and a reduction in fees).	Reductions in corporate income tax, particularly for exporters, for 5 years. Reduced rates for the next 10 years. 20% investment allowance and capital gains exclusion from 25% to 100%. Reduced import dues and VAT on equipment. Exemptions from		

		urban tax for 5 years.		
Oman		Corporate tax holiday for 5 years, renewable for another 5 years. Exemptions from customs duties on machinery and equipment.	Soft loans from the national development bank.	The soft loans are conditional upon Omani ownership of least 51% of the project and a local employment of at least 35% of total staff.
Qatar	Flexible immigration and nationality rules. A wavering of import quotas.	Corporate tax holiday for 5 years, renewable for another 5 years. Exemptions from customs duties on machinery and equipment. Exemption from export duties.	Preferential rates on energy consumption and land rental. Concessionary financing from the national development bank.	
Saudi Arabia		Corporate tax holiday of up to 10 years.[b] Exemption from customs duties on machinery and equipment, and on input goods not locally available, for industrial projects.	For industrial projects an attractive package of low land, electricity and water rates, and subsidised accommodation is offered.	Foreigners have access to incentives provided the share of Saudi capital in a given project is at least 25%.
Syria	Preferential capital accounts regulation of foreign investors.	Corporate tax holiday up to 5 years, extendable to 7 years in the case of exporters and companies with a government stake. Duty free imports of machinery and equipment.		
Tunisia		Corporate tax holiday for 10 years. Reduced tax rates thereafter. Tax exemption on reinvested earnings. Tax and duty	Projects with a “high job creation potential” may benefit from the use of state-owned land at symbolic prices.	These are the most generous incentives, which apply to “offshore companies” with at least 66% foreign-owned equity, exporting at least 80% of their

		exemption on imported capital and input goods.		production.
United Arab Emirates				Generally, no incentives are offered outside the FEZs.
Yemen		Corporate tax holiday for 7 years, extendable to 16 years. Exemption from real estate taxes, and from tax and customs fees on project fixed assets.		

Notes:
For country details, see Annex 1.
a. Mostly 5-10 years. 20 years' tax holidays are available to investors in certain depressed regions.
b. Repealed in 2004, but existing beneficiaries are grandfathered.

13. One of the main conclusions from Table 1 is that the investment incentives offered by MENA countries are mostly fiscal. Two main categories of fiscal incentives are available in almost all economies. First, in the actual investment phase, most countries offer relatively wide-ranging exemptions from duties, customs and indirect taxes on items related to the investment project. Secondly, almost all countries offer a corporate tax holiday, in many cases extendable in case of supplementary investments. Based on the material surveyed in Annex 1, the most "generous" such schemes are found in Egypt (tax holidays up to 20 years) and Algeria (indefinite tax exemption). In Morocco, on the other hand, tax holidays for exports are only limited to 5 years. In many of the Gulf states – which levy no corporate tax on domestic corporations and generally low rates on foreign ones – the value of the tax holidays to investors may in practice be limited.

14. Among the fiscal incentives that are apparently offered by only a few countries, the exemption of foreign staff from income taxes and/or social security contributions in some countries (including Algeria, Jordan and Kuwait) bear mentioning. Moreover, some of the few countries that levy property tax on corporate real estate offer to wave this tax to attract investors. Specific national approaches include waving of permit and registration fees in Lebanon, an exemption from export duties in Qatar, and an indefinite exemption of reinvested earnings from corporate taxation in Tunisia.

15. Regulatory incentives (outside of the FEZs) do not appear to be very common. Where they occur, they tend to take the form of an exemption of investors from pieces of national regulation that appear tighter than in alternative business locations. Examples include an easing of the access to employ expatriates (Kuwait, Lebanon and Qatar), an exemption from the formalities for land acquisition (Morocco), a wavering of import quotas (Qatar) and a preferential capital accounts regulation for foreign investors (Syria).

16. Financial incentives are not widely used. Where they do occur they tend to take one out of three forms: the allocation of land and infrastructure for free or at artificially low rates (Algeria, Kuwait and Tunisia); soft loans from national development banks (Oman and Qatar); and subsidised public utilities

(Qatar and Saudi Arabia). Financial incentives are in some cases available to foreign investment projects subject to conditions only, including those relating to local capital participation or local staffing requirements.

17. A special feature of the incentive regimes in some MENA countries that is not included in Table 1 is the differentiation between various geographic zones (not to be confused with the FEZs) within individual countries. Egypt, Jordan, Lebanon and Tunisia have statutory systems graduating the generosity of investment incentives according to the perceived need for economic development in different parts of their territory.

b) Free economic zones in MENA countries

18. Reflecting the difference in attractiveness to investors, and the different approaches to investment incentives, mentioned above, MENA countries have taken vastly different approaches to the use of economic zones to attract investors (Table 2). Whereas there are 48 functioning zones in the region as a whole, three countries have no FEZs at all (Oman, Qatar and Saudi Arabia). However, one of them (Saudi Arabia) has been pursuing a strategy of establishing industrial parks that have certain common traits with FEZs.

19. Other economies have established FEZs, but do not rely on them strongly in their investment attraction strategies. These include some examples of FEZs that are essentially free ports offering little more than warehousing, as well as economic zones that were launched amid great expectations but have not yet delivered the hoped for results.

20. The FEZs that are so far considered most successful are those in the United Arab Emirates – not least the famed Jebel Ali Free Zone (JAFZ) in Dubai that has so far attracted more than 2,200 mostly foreign-owned enterprises. Following the establishment of Jebel Ali in 1985, other states of UAE were quick to follow suit (e.g. Fujairah and Sharjahin 1987, Umm Al Quwain in 1988) and the country now has sixteen FEZs in operation. The success of JAFZ has been such that its operating company is now selling know-how to, or is otherwise involved in the development of, several of the other zones mentioned in this paper.

Table 2. Main characteristics of FEZs in MENA countries

	Number and type of zones	Total area (hectares)	Number of enterprises	Observations
Algeria	1 FZ	523	ND	
Bahrain	2 FZs	ND	ND	
Egypt	1 SEZ; 6 FZs; 1 IZ	SEZ: 9,000; FZs: 1,149	ND	
Jordan	1 SEZ; 6 FZs	SEZ: 37,500; FZs: 757	1,722[a]	The SEZ covers the urban area of Aqaba.
Kuwait	1 FZ	60	ND	
Lebanon	2 FZs	27	ND	
Morocco	1 FZ	345	ND	
Oman	None	..	..	
Qatar	None	..	..	
Saudi Arabia	None	..	..	
Syria	7 FZs	339	ND	
Tunisia	2 FZs	83	ND	

United Arab Emirates	9 FZs; 7 IZs	FZs: 12,950; IZs: 1,235[a]	3,978[a]	Several of the industry zones occupy space inside the larger free zone areas.
Yemen	1 FZ	28	29	
Total MENA	2 SEZs; 38 FZs; 8 IZs	63,996		

For country details, see Annex 1.

a) Including only those zones for which data is available.

21. In another apparent consequence of the early successes, the governments of UAE (especially Dubai) have gone further than other economies in the MENA region in using the zone approach as a tool for targeted strategies. The country is host to seven industry zones (with several more under preparation), including the widely acclaimed Dubai Media City. The zones generally target knowledge-intense sectors such as ICT, higher education and health, but also include facilities targeted at the local production of jewellery and the distribution of automobiles.

22. Several MENA countries have expressed the intention of trying to emulate the success of the Emirates with FEZs. Arguably, the most advanced plans can be found in Egypt and Jordan. In the case of Jordan, there is a long-standing tradition for relying on FEZs to encourage investment. The free zone in Zarqa close to Amman has been in operation for decades and is host to more than 1,300 enterprises, most of which domestic companies of a limited size. As part of a new strategy to use zones to attract international investment, in 2001 the free port of Aqaba was turned into a SEZ and greatly expanded to include most of the urban area. Since then, more than 310 companies have established themselves in the zone and invested an estimated US$ 400 million. In addition to Aqaba and Zarha, five zones are now operational in Jordan, three of which established since 2001.

23. Egypt also has a relatively long history of relying on free zones (the oldest ones still in existence were established in 1973), but recent years appear to have brought a change in the overall strategy. No general zones were established since 1993, and more recently the focus has been on SEZs and industry zones. A SEZ was established in 2003 on a large industrial area of 9,000 hectares at the North West Gulf of Suez. It is still too early to gauge the success of this SEZ, which is located near the same main shipping routes as Aqaba and Ali Jebel. An industry zone, the Media Production City, was established in 1995 in an attempt to attract regional producers of radio, television and cinema (similar establishments are found in Dubai and, in the form of a private zone, in Jordan), and additional industry zones service the textile and pharmaceutical industries are under development.

c) Incentives and other subsidies in the FEZs

24. Like other aspects of the MENA countries' investment environments, the characteristics of FEZs differ between countries – not least between the Gulf countries and the rest of the region. However, as a general rule, FEZs rely relatively strongly on regulatory incentives – *inter alia* by cutting red tape and simplifying administrative procedures for companies located inside the zones. In many cases the zone authorities are authorised to act as a one-stop shop with the authority to grant all necessary licences and authorisations and oversee regulatory compliance, thereby shielding investors from a time-consuming and sometime ominous regulatory compliance.

25. In the Gulf countries, one of the main regulatory incentives in FEZs is the exemption from limits on foreign ownership that apply to companies elsewhere in the host economy. Examples of countries

following this strategy include Bahrain, Kuwait and the United Arab Emirates. In addition, these and several other MENA countries that maintain restrictive practices toward foreign land ownership either wave these restrictions inside the zones or offer land on long-term renewable leases. Labour market regulation is eased in some zones, for instance through easier access to hiring expatriates (Jordan and Kuwait), or a wavering of national rules against limited duration employment contracts (Tunisia). Finally, those countries that have foreign exchange restrictions in place generally permit companies located in FEZs to operate outside this part of the regulatory regime (e.g. Morocco, Syria and Tunisia).

Table 3. Incentives offered in FEZs in the MENA region [a]

		Type of incentives:			Observations
		Regulatory	Fiscal	Financial	
Algeria		Establishment requires no authorisation.	Exemption from all taxes, duties and fees, except for taxes on motor vehicles unconnected with the investment and social security contributions.		
Bahrain					
Egypt			Indefinite exemption from all Egyptian taxes. 10% duty on the value of non-domestic components when sold in Egypt.	Preferential rates on land rental, electricity and water.	The blanket exemption on Egyptian taxes applies to the free zones only. In the SEZ certain (low) income tax rates apply.
Jordan	Free zones	Provision of certificates of origin for industrial products with a local input of less than 40%.	Personal income tax holiday of 12 years for non-Jordanian employees. Exemption from taxation of corporate profits earned on manufacturing goods for export, transit trade or trade within the zones. Exemption of real estate from licensing fees and taxes.		
	Aqaba SEZ	Foreigners may own land for some purposes, or lease it for up to 50 years. Staff nationality requirements are released: up to 70%	A low 5% corporate income tax rate on most activities other than finance. Exemption from social services taxes. 10% land transfer	Foreign firms have access to reimbursement for training expenses.	

	foreign labour may be employed.	tax.		
Kuwait	100% foreign ownership is permitted. Improved access to work permits for expatriate staff.	Indefinite exemption from all income taxes.	Moderate utilities rates.	
Lebanon		Corporate tax holiday of 10 years for all companies in the zones.	Low-cost land and building leases. Low utilities rates for "productive activities".	
Morocco	Exemption from all trade and exchange controls in force elsewhere in Morocco.	Corporate tax holiday for 5 years. A reduced rate indefinitely thereafter.	In certain sectors, state aid for the acquisition of land and the construction of production units.	
Oman	..	..	..	
Qatar	..	..	..	
Saudi Arabia	..	..	..	
Syria	Exemption of foreign exchange transactions from the restrictions in place elsewhere in Syria.			
Tunisia	Freedom to operate outside Tunisia's foreign exchange regulation. Access to hire staff on limited duration employment contracts.	A flat individual income tax rate of 20% on the salaries of foreign staff. Tax-free imports of personal belongings, including cars, of foreign staff.	Preferential land rental and utilities rates.	
United Arab Emirates	100% foreign ownership of companies allowed. Access to land through long-term renewable leases.	Complete exemption from taxes, customs and commercial levies.	Low land rates.	
Yemen	100% foreign ownership of companies allowed. Expropriation within the zone is not permitted.	Corporate tax holiday of 15 years, extendable for another 10 years. No personal income taxation of non-		

		Yemeni employees.		

Notes:
For country details, see Annex 1.
a) Only incentives in excess of what is generally offered in the host economy are included. Exemptions from import and export duties, which are presumed to be equivalent across FEZs, are not included.

26. The fiscal incentives offered to investors in the general economy are available to companies in the FEZs as well. However, some zones go beyond this and offer additional fiscal concessions. Four countries offer a complete exemption from corporate and private income taxes in their free zones (Algeria, Egypt, Kuwait and United Arab Emirates), whereas companies located in SEZs (in Egypt – and likewise in Jordan) are requested to pay certain low income taxes. Jordan's free zones offer freedom from the taxation of corporate profits earned on manufacturing goods for imports or trading within the zones. Several countries (Lebanon, Morocco and Yemen) offer corporate tax holidays in their FEZs that are more generous than what is available under their general investment incentive regimes. Some zones also offer reduced personal income taxes on expatriate staff. In Yemen, the income of non-Yemeni employees is completely exempt from taxation; in Jordan's free zones non-Jordanian employees enjoy a 12 years tax holiday, and in Tunisia's FEZs a flat individual income tax rate of 20% is applied to the salaries of foreign staff.

27. In the nature of FEZs, the so-called "quasi-incentives" are on offer almost everywhere: zones are generally advantageously located next to an air- or seaport and equipped with a physical infrastructure that exceeds what is found in many other parts of the host country. In addition to this, some zones offer actual financial incentives, mostly in the form of low land rental and utilities rates (Egypt, Kuwait, Lebanon, Tunisia and United Arab Emirates). More targeted financial incentives include subsidising the training expenses of foreign enterprises (Jordan – Aqaba SEZ) and providing state aid for the acquisition of land and the production of production units (Morocco).

III. CONCLUSIONS AND SUGGESTIONS FOR FURTHER WORK

28. The proposed concluding remarks in this section are consistent with the *Conclusions of the Task Force on Incentives* at the Task Force's meeting on 29-30 June in Bahrain (Annex 2). They moreover draw on the *Checklist for Foreign Direct Investment Incentives Policies* adopted by the OECD Investment Committee to assist governments in assessing the cost-effectiveness of incentives.

29. The overriding consideration for a country seeking to attract investment is putting in place a healthy ***enabling environment*** (infrastructure, human capital, an investment-friendly regulatory environment, the rule of law, good public governance). Incentives and economic zones can, at best, be a supplement to a good enabling environment, or be used to compensate for certain concrete shortcomings that cannot be otherwise addressed.

30. Elements of the enabling environment in some MENA countries are encouraging. For example, several countries offer a modern infrastructure, a generally well-skilled labour force or a favourable geographic location. Many countries have moreover taken steps to make their regulatory environments more investment-friendly by dismantling barriers to international transactions, reducing discrimination between domestic and foreign-owned enterprises and limiting the role of the state in the economy. Conversely, according to corporate representatives in the region, the burden of regulatory compliance, a lack of transparency, limited administrative efficiency and elements of informality continue to hinder the relationship between businesses and the public sector, thereby holding back investment. A sustained effort to address these problems will, in the long run, be more effective in mobilising private investment than investment incentives and economic zones.

31. Virtually all economies in the MENA region offer ***investment incentives*** to domestic and foreign-owned enterprises, either automatically or subject to administrative discretion. The design of the schemes varies across countries. Unsurprisingly, the states in the Gulf that are rather popular with investors have put in place less sweeping or less generous incentive schemes than in other parts of the region. Some of the main considerations for policy makers could include the following.

32. MENA countries rely in large measure on *fiscal incentives* to attract investors. While fiscal incentives have the advantage of being rule-based and hence relatively transparent (tax concessions having to be foreseen by national legislation), there are problems with relying excessively on them:

- A frequently heard argument is that fiscal concessions are, somehow cheap because they involve no immediate cost to the public purse. However, the budgetary cost in the form of foregone revenue can, especially where incentive schemes are long in duration, be considerable and the implementing authorities need to account properly for this.

- General fiscal concessions can be a "blunt instrument" when it comes to compensating businesses for certain weaknesses in the enabling environment or induce them to increase their investments. Incentives work better when linked with the actual process of capital formation. Fiscal incentives that may have this effect include investment tax credits and duties exemption from capital goods, whereas sweeping measures such as tax holidays often encourage tax planning rather than productive investment.

33. Most of the countries in the region make the generosity of their investment incentives depend on a number of *criteria defining the "desirability" of a given project*. Performance criteria imposed on investors are generally problematic, although they may be defended when linked to concrete investment incentives and intended to ensure that investors fulfil their side of the bargain. However, by going beyond this and attempting to encourage prioritised sectors, authorities discriminate against different parts of the business community, effectively engaging in a policy of "picking winners" that have in the past rarely been effective. Some of the criteria according to which incentives are actually granted in MENA countries are:

- *Sectoral preferences.* In many countries manufacturing and other industrial activities are given top priority. Conversely, large parts of the service sectors are often perceived as sources of employment for the local population, the foreign participation in which is not encouraged. Without calling the developmental priorities of sovereign governments in doubt, it must be re-emphasised that such practices suffer from the same shortcomings as the, somewhat discredited, industrial policies of the past.

- *Macroeconomic outcomes.* According the main macroeconomic preoccupations of the host countries (e.g. unemployment; current accounts) investment projects may be granted special benefits according to their perceived job creation or export potential. In theory, authorities are well-advised to gauge the societal benefits of a project in addition to its private profitability. However, in practice overseeing and rewarding the macroeconomic outcomes of individual business operations usually creates insurmountable monitoring problems.

- *National ownership*. Some governments reserve investment incentives for companies whose domestic equity participation exceeds certain threshold levels, in effect crating competitive distortions and discouraging potential investors.

- *Local considerations.* The practice by some countries of dividing their territory into development zones and differentiating incentives among them may be construed as an attempt at compensating investors for the weakness of the enabling environment in certain parts of the economy. However, experience suggests that subsidising companies to invest where they wouldn't go on their own accord is rarely successful and often leads to rent seeking.

34. Related to the previous point, most countries retain considerable *administrative discretion* to decide about the level of incentives on a project-by-project basis. Again, the incentives listed above are the most generous ones available to investors, mostly subject to the decision by investment boards or government committees. This runs counter to a commonly accepted principle (*inter alia* expressed in the OECD Checklist) that incentives should be as transparent and rules-based as possible. In the context of an enabling environment for investment whose greatest weaknesses include administrative opacity and cumbersome procedures, a strong case could be made for relying on firm rules rather than improvisation.

35. Granting incentives to investors involves an element of *competition between jurisdictions*. The experience so far indicates that competition for individual investment projects is relatively rare and limited to high-profile projects in a few sectors (e.g. automobiles, electronics). However, the so-called "regime competition" between investment locations feeling that they cannot allow themselves to be less generous, overall, than neighbouring countries appears common – including in the MENA region. For instance, one might argue that the pervasiveness of corporate tax holidays offered across the region could reflect a general desire to show goodwill toward investors rather than a targeted or strategic approach. For the MENA countries as a group, it would probably be advantageous to curb the generosity of investment

incentives – at least to the degree that they accrue to projects that would have taken place within the region anyway.

36. The reliance on ***free economic zones*** is on the rise. The most obvious benefit of FEZs to investors is of course that the zones enable them to locate internationally-oriented parts of their value chain outside the national customs areas. Moreover, among the more "successful" examples (in terms of attracting investors) two main models seem to be evolving. One the one hand, in the Gulf countries, and notably in Dubai, zones have been successful against the background of a generally attractive investment environment. The zones have prospered by offering foreign investors a haven of exemption from the generally discriminatory investment policies of host countries.

37. On the other hand, many FEZs attract investors by offering a package of benefits that is even more generous than the general incentive regimes of the host economies. Common to the two models is that investors in the zones have benefited from an administrative simplification following from the establishment of one-stop shops, the lifting of many registration and authorisation requirements compared with the mainland economies and freedom from having to deal with the complicated customs procedures of many countries. Based on the evidence so far, some of the main considerations for policy makers could be:

- *The beneficial economic effects of FEZs could be temporary.* In the short run, host governments may be unable to liberalise their investment policies or raise sufficiently the efficiency of regulatory and administrative systems. If so, a case can be made for using smaller ring-fenced areas as "economic laboratories" or showcases of a generally strong enabling environment for investment. However, such practices should be supported by efforts to broaden the achievements to an ever-wider segment of the host economies. Zones inevitably involve an element of discrimination among the companies that are within the zone vis-à-vis those outside of it, and authorities should take care not to make this uneven playing field a permanent feature of the MENA economies.

- The *discriminatory effects of FEZs* should be kept to a minimum. The basic principle underlying economic zones is that they operate as offshore locations, separate from the host economy. This implies that the trade between companies located in the zones and others is treated like import and exports. However, in practice the distinction is not always so clear. In some countries, zone-based companies can sell to the rest of the economy at preferential duties. In others, only the "non-domestic" component of the zone-based enterprises' production is made subject to import taxes. Great care must be taken to avoid serious distortions of the competition between enterprises in countries that make zones a key element in their investment policies.

- The risk of *using FEZs to pursue activist industrial* policies is equivalent to that mentioned in the context of investment incentives. If anything, the risk could be greater in the case of zones where "undesired" activities may not only suffer from a denial of subsidies but be barred from entry altogether.

- Even in zones operating outside the usual legal environment, certain *regulatory standards should be observed*. In the interest of host countries themselves FEZs should not undermine core labour standards nor derogate from commonly accepted social, health and environmental principles.

38. The MENA-OECD Investment Programme's work on investment incentives and FEZs is still in its early phases. If the members of the Group accept the present, preliminary paper as a basis for ***future work***, then the following activities would seem to suggest themselves:

- *A joint effort to enhance transparency.* Little comprehensive cross-country evidence is available to shed light on investment incentives and economic zones in MENA countries. The Group might, taking Tables 1-3 and Annex 1 as a starting point, agree to collect such information, jointly review it and publish it on the MENA Investment Initiative's website.

- *Self assessments and peer discussions.* Countries are invited to volunteer to make a self-assessment of their incentives policies, as already foreseen in the National Investment Reform Agendas of some nations. The assessment could be based on the OECD Checklist for Foreign Direct Investment Incentive Policies and Conclusions of the Task Force on Incentives, and discuss their national experiences with other members of the Group. As appropriate, the outcome could be made public or shared confidentially among MENA countries.

- *Joint initiatives regarding investment incentives*. Recognising the cross-border implications of incentive policies, a consultative mechanism could be established for discussing how to avoid adverse outcomes for the region as a whole.

ANNEX 1: INDIVIDUAL COUNTRY RESULTS

ALGERIA

General investment climate

Restrictions on foreign direct investment in the Algerian economy (outside the zones) include the following:

- *General restrictions on entry.* Foreign direct investment in Algeria is permitted freely, except in certain specified sectors, provided that it conforms to the laws and regulations governing regulated activities. The 2001 Investment Code did away with the distinction between foreign and domestic investors. No statutory discrimination persists.

- *Sectoral restrictions on entry.* No sectoral restrictions are on record, except for the limitation of certain economic activities to government-owned entities.

- *Land ownership.* Most land in Algeria is owned by the public sector, but it is not always clear whether national or local authority owns a particular piece of land. Purchasing a piece of land for investment purposes can therefore be both time consuming and expensive.

- *Repatriation of investment and profits.* The Investment Code allows foreign investors to repatriate capital and profits within 60 days, even if revenues exceed the amount originally invested. According to a report by UNCTAD, however, foreign investors still face legal and practical obstacles[4]. Although the law allows repatriation, this is limited to profits and dividends made through investments in foreign currencies. Also, the law does not allow the repatriation of payments arising from “immaterial assets” such as royalties generated by licensing patents or trade marks.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Algerian economy:

- *Corporate income tax rates.* The corporate tax rate is 30% of net profits. Certain categories of companies (e.g. construction and small and medium-sized enterprises) benefit from lower rates.

- *Personal income tax rates.* The individual tax system of Algeria is progressive. The highest rate is presently 40%.

- *Property tax rates.* Corporations pay an annual property tax on 2% of the value of their real estate assets.

Investment incentives in the overall economy

The Investment Code provides for two incentive schemes, the “general scheme” and the “special scheme”. To qualify for the special scheme an investment project must be perceived to offer particular benefits to the national Algerian economy. Some of the main elements of the two schemes are:

---

4 UNCTAD (2003).

- *General scheme.* These benefits will almost always be available to investors: A reduced-rate customs duty on imports of equipment; a VAT exemption on goods and services directly involved in realising the investment; and an exoneration of transfer duty on any property assets purchased for the purpose of the investment. The duration of most of these benefits is three years, but in special cases (e.g. in economically depressed areas) it may be extended to 10 years.

- *Special scheme.* This scheme offers substantial incentives to investors. They include all elements of the general scheme plus, for a ten year period:

  – Investment realisation phase: a reduced fee for the registration of rights; and, in some cases, a full or partial state financing of necessary infrastructure works.

  – Exploitation phase: an exemption from corporate income tax; an exemption from individual income tax for non-Algerian staff; an exemption from a 3% social security contribution levied on wages; an exemption from property tax on the fixed assets of the investment; an exemption from the 2% tax on professional activity; and generous allowances for deficit postponement and extensions of depreciation delays.

Zones and their main characteristics

The Algerian government has so far not relied strongly on FEZs, but it has announced an intention of making them an important element in its investment attraction strategies for the future. So far, one zone has been established, namely Bellara Customs-Free Zone. This zone, located next to the port of Jijel, has been in operation since 1997.

With the "Ordinance No. 03-02 of 19 July 2003 on Customs-Free Zones", the Algerian authorities aimed to enhance the legal basis for establishing FEZs. One of the original figures of the new rules is that a customs-free zone may be set up on land in which full right is owned by a private person or corporate entity. Five zones are planned, for the four coastal cities of Ghazaouet, Mostaganem, Annaba and Skikda and for the southern border town of Tamanrasset. Moreover, a "cyber city" is being developed on the outskirts of Algiers.

The free zone in Bellara started as a traditional duty free area next to the port, but authorities have the intention of developing into an export zone attracting light industry from abroad and drawing on locally available resources (e.g. agriculture, fisheries and forestry). According to anecdotal evidence, the zone has not yet managed to attract the number of industrial enterprises initially hoped for.

One aspect that separates the Algerian free-zones law from that of many other countries is the fact that, while formally outside the customs area, the zones remain subject to Algerian exchange control regulations. Another particularity is that up to 50% of the goods and services produced in a zone may be sold freely within the customs area. In important respects, FEZs in Algeria would therefore seem to be less ring-fenced than is the case in most other countries.

Table A1. FEZs in Algeria

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (mill. USD)
Bellara Customs-Free Zone	Free Zone	1997	523	Primary produce, light industry[a]	ND	ND	ND

Note:

[a] According to the law all economic activities are welcome, except polluting ones.

Incentives and quasi-incentives in the Zone

Overall, the incentives that are available to investors in the zone do not appear to differ much from they could obtain under a generous interpretation of the special incentives scheme. Nevertheless, some of the main additional aspects of conditions within the zone are:

- *Regulatory incentives.* Establishment in free zones requires no authorisation. Only a declaration of investment to the National Investment Promotion Agency is required. Investments must be made in convertible foreign currency or convertible dinars.

- *Fiscal incentives.* Investments in FEZs are exonerated of all taxes, duties and fees other than: duties and taxes on personal motor vehicles other than those connected with the business; and compulsory contributions to the social security system.

BAHRAIN

General investment climate

Restrictions on foreign direct investment in the Bahraini economy (outside the zones) include the following:

- *General restrictions on entry.* The law permits 100% foreign ownership in the case where industrial and services companies establish new representative offices or branches in Bahrain (also, there is no requirement of local sponsors). Joint ventures are permitted with Bahraini companies, but a 100% purchase of an existing company would require Ministry of Commerce approval. Foreigners may generally own up to 49% of public joint stock companies. Foreigners may own up to 100% of limited companies and private (non-listed) joint stock companies.

- *Sectoral restrictions on entry.* Banking, insurance and investment management activities can be performed only by public joint stock companies, whereby the 49% foreign-ownership restriction comes into effect. Generally, public joint stock companies are allowed to undertake any lawful economic activity, whereas for other types of incorporation limitations may apply.

- *Land ownership.* Since 1999 GCC citizens have been able to own land in Bahrain. In January 2001, this right was extended to foreign (GCC and the rest of the world) firms. Non-GCC entities are allowed to buy and own land in specifically designated investment areas or otherwise lease government land through the Ministry of Finance.

- *Repatriation of investment and profits.* Investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Bahraini economy:

- *Corporate income tax rates.* The only corporate income tax is levied on oil, gas and petroleum companies at a rate of 46%.

- *Personal income tax rates.* There is no individual income tax in Bahrain.

Investment incentives in the overall economy

Outside the FEZs, incentives, as defined in this paper, are mostly not offered. The Bahraini authorities pursue a policy of attracting foreign investors by means of its comparatively permissive regulation of foreign ownership, low taxation and fast-track registration, regulation and administrative procedures. (This policy has been termed “turning the whole country into a free economic zone”.) However, a few special measures do qualify as investment incentives. “Foreign capital companies” are exempted from the minimum capital requirements established under Bahraini law, and permitted to hold their board meetings abroad. Manufacturers are exempt from import duties on materials and machinery.

Zones and their main characteristics

Bahrain has a number of industrial parks (or “industrial estates”) which, while not ring-fenced or customs-free, provide favourable conditions for selected economic activities. In terms of actual FEZs, the country presently has two – both of them basically operating as traditional customs-free areas. Mina Salman, the country's major port, provides a free transit zone to facilitate the duty-free import of equipment and machinery. The North Sitra Industrial Estate includes a free zone as part of its operations. Raw materials intended for processing in Bahrain, and equipment and machinery imported by Bahraini-registered firms are exempt from duty. The same facilities in the two free zones are used for the temporary import of goods for re-export.

Table A2. FEZs in Bahrain

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (mill. USD)
Mina Salman	Free Zone	[Early 1960s]	143	Production of sponges, paints, plastics and air-conditioning equipment	ND	ND	ND
North Sitra	Free Zone	ND	ND	Heavy industry, small and medium-sized enterprises	ND	ND	ND

Incentives and quasi-incentives in the Zones

Apart from habitual exemptions from import and export duties in FEZs, no investment incentives are on record.

EGYPT

General investment climate

Restrictions on foreign direct investment in the Egyptian economy (outside the zones) include the following:

- *General restrictions on entry.* There are no general restrictions on foreign ownership of Egyptian companies. According to Egyptian law, foreign investors may own up to 100% of businesses categorised in a positive list guaranteeing approval (for sectoral restrictions – see below). The company registry (part of GAFI) may, however, reject registration on account of non-compliance with the law or lack of qualifications to conduct business.

- *Sectoral restrictions on entry.* Foreign investors are allowed to hold up to 100% of most financial service providers. However, the economic needs test is used to determine commercial presence in Banking, and no new commercial banking licence has been issued in almost 20 years. Commercial agents and importers for resale in Egypt must be Egyptian nationals. In manufacturing, all projects involving military products and tobacco and tobacco products require prior approval from the relevant ministries in addition to the General Authority for Investment and Free Zones (GAFI).

- *Land ownership.* Foreign individual or corporate ownership of agricultural land (defined as traditional agricultural land in the Nile valley, delta and oases) is explicitly prohibited by Law No. 15/1963. Law No. 143/1981'which stipulates that Egyptians must have a majority share in any desert land, defined as land beyond two kilometres from the border of a city. However, companies and citizens of other Arab countries have customarily received Egyptian national treatment in this area.

- *Repatriation of investment and profits.* Foreign investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Egyptian economy:

- *Corporate income tax rates.* The standard rate of corporate profit tax is 40%. However, industrial companies and profits derived from export operations are taxed at 32%. An additional 2% "development duty" is levied on net profits that exceed a certain threshold level.

- *Personal income taxes and social contributions.* The personal income tax system is progressive, with rates starting at 20% and ending at 33%. Enterprises contribute 26% of the wage sum to social security.

Investment incentives in the overall economy

The main law guiding foreign investment in Egypt (Law No. 8/1997) authorises public authorities to offer a wide range of incentives to investors. Some of the main elements are:

- *Regulatory incentives.* Investors are guaranteed against nationalisation and expropriation of their project. They are also given assurances that the outcome of the project will not become the subject of price controls.

- *Fiscal incentives.* Imported capital assets and construction materials required to establish an approved project are subject to a unified import duty rate of 5%. Moreover, tax holidays from 5 to 20 years (according to the location of the project) are accorded to new investors. Foreign experts' salaries are exempt from income tax if their stay in Egypt is for less than one year. Exemptions from taxation of reinvested capital gains and of the paid-in capital in publicly listed companies are also offered. All investment projects are granted exemptions from notarisation and notification fees.

Zones and their main characteristics

Egypt presently has 6 fully functioning free zones, one industry zone (with another 3 under development) and one special economic zone. The SEZ, named Economic Zone of the North West Gulf of Suez, is located next to the harbour of Sokhna, 45 km southeast of Suez City. It is subject to the administration of the General Authority for Economic Zone North West Gulf of Suez (SEZONE). A further SEZ is for consideration in the area of East Port Said.

Table A3. FEZs in Egypt

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (bn. USD)
North West Gulf of Suez	SEZ	2003	9,000	Chemicals, pharmaceuticals and metals	ND	ND	ND
Alexandria	Free Zone	1973	541	Oil, chemicals and textiles	ND	ND	ND
Nasr City	Free Zone	1973	67	Diverse industrial activities	ND	ND	ND
Port Said	Free Zone	1975	73	Ship building, marine equipment and textiles	ND	ND	ND
Suez	Free Zone	1975	32	Petroleum, fertilizers and ship building	ND	ND	ND
Ismailia	Free Zone	1979	320	Electronics, ICT and metal products	ND	ND	ND
Damietta	Free Zone	1993	116	Chemicals, textiles and maritime services	ND	ND	ND
Media Production City	Industry Zone	1995	ND	Radio, television and cinema	ND	ND	ND
Under development:							
Tenth of Ramadan	Industry Zone	..	64	Textiles	..	..	..
Shibin el Koum	Industry Zone	..	8.5	Textiles	..	..	..
Keft	Industry Zone	..	78	Pharmaceutical products	..	..	..

The location of Egypt's free zones traditionally reflects an objective of decades of industrial policy to locate productive activities outside the Nile Valley. Five of the first seven zones are located on the Mediterranean coast or by the Suez Canal. The free zones are the responsibility of GAFI, and all of them enjoy broadly similar regulatory and administrative conditions. One zone that merits special mentioning is the Media Production City Free Zone in Gizah near Cairo, which is essentially an industry zone specialising in media production and related activities. Among other things it offers investors access to 29 studio complexes and ten outdoor "shooting areas".

Most of the zones currently being developed have a strong sectoral orientation. This is not least the case for the Tenth of Ramadan, that was designated for the production of textiles following Egypt's access to establish Qualified Industrial Zones from 2005 (see further under Jordan). Other FEZs, and several industrial areas outside the zones, will, however, also enjoy QIZ privileges.

The use of zones in Egypt comes on top of a regulatory environment that is generally geared to encouraging private investment. As mentioned, Law No. 8/1997 provides for favourable treatment of investors, in a number of prioritised sectors, even outside the zones. For example, 41 Industrial Parks have been established subject to this law, offering investors tax holidays of 10 years (in some cases extendable to 20 years) and certain import duty exemptions. Private free zones are also extensively used. GAFI is authorised to grant permission to a private zone when an investor is qualified to enter a public zone, but no suitable location can be found.

Incentives and Quasi-incentives in the Zones

Given the already quite generous incentives package offered to foreign investors, the main additional benefits that free zones and SEZs offer is their location near transport hubs and outside the Egyptian customs – and in the case of SEZs, regulatory – area. As table A4 illustrates, the fiscal incentives in the free zones are actually more generous than in the country's only SEZ. On the other hand, a constant concern by businesses in Egypt has been red tape and administrative opacity, and the most frequently heard complaints have been directed at the Customs Authority. It appears that the prospect of operating in a tailor-made regulatory environment is expected to be sufficient to make investors accept slightly higher levels of taxation. One unknown factor, however, remains the export performance requirements in the Special Economic Zone(s). Companies in free zones are required to export at least 50% of their production, but in the case of the "North West Gulf of Suez" such requirements are left for the zone's regulatory board to decide.

Table A4. Incentives in the Egyptian Economic Zones[5]

<table>
<tr><th></th><th>Free Zones</th><th>Special Economic Zone</th></tr>
<tr><td>Regulatory incentives</td><td>Projects are exempted from all regulations related to import/export.</td><td>Projects are exempted from all regulations related to import/export.</td></tr>
<tr><td rowspan="2">Financial incentives</td><td>Life time exemption from all Egyptian taxes[6].</td><td>Standard 10% corporate income tax on all projects.

Standard 5% personal income tax at all income levels.</td></tr>
<tr><td colspan="2">No import duties.

No duties when exporting outside of Egypt and no duties on domestic components when sold in Egypt.

10% duty on the value of non-domestic components when sold in Egypt.</td></tr>
<tr><td>Fiscal incentives</td><td>Preferential rates on land rental, electricity and water.</td><td>Preferential rates on land rental, electricity and water.</td></tr>
<tr><td>Quasi-incentives</td><td>Limitation of red tape.</td><td>Limitation of red tape.

Integration of project with the Port of Sokhna.</td></tr>
</table>

5 Based on van der Zande (2003) and unpublished material.

6 However, companies located in free zones pay certain fees and charges. Industrial companies pay 1% of the value-added on outgoing goods. Services companies pay 1% of their profits.

JORDAN

General investment climate

Restrictions on foreign direct investment in the Jordanian economy (outside the zones) include the following:

- *General restrictions on entry.* There are no general restriction on foreign ownership of Jordanian companies (for sectoral restrictions – see below). Neither is there any formal screening or host government selection process for foreign investment. The amount of investment in any one project must total at least JD 50,000.

- *Sectoral restrictions on entry.* Foreign investors may not own more than 50% of projects in: construction and contracting; wholesale and retail; sea, air and train transport; wastewater treatment; food services; travel agencies; important and export services; advertising; and a number of business-related and commercial services (including in finance). No foreign participation is allowed in: security services; sports clubs; stone quarrying; customs clearance services; and land transport other than trains.

- *Land ownership.* Non-Arab foreign nationals are permitted to own or lease property, provided that their home country does not discriminate against Jordanians. The Cabinet is the authority on licensing foreign ownership of land and property.

- *Repatriation of investment and profits.* Foreign investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Jordanian economy:

- *Corporate income tax rates.* Mining and manufacturing, transportation, construction, hotels and private hospitals: 15%. Insurance, foreign-exchange dealers, telecommunications, trade and other non-financial services: 25%. Banks and finance companies: 35%.

- *Personal income taxes and social contributions.* The personal income tax system is progressive, with rates starting at 5% and ending at 30%. Enterprises contribute 8% of the wage sum to social security.

- *Property tax*. A tax on commercial property is levied at a rate of 15% of the rental value[7].

Investment incentives in the overall economy

A large number of incentives schemes are generally available to investors in Jordan. The country is divided into three development areas, Zones A, B and C. Investment in Zone C, the least developed part of the country, receive the greater incentives. Exceptions from income and social services taxes are granted for a

[7] However, the rental value of owner-occupied property is presently assessed extremely conservatively. The taxable value of such property has only increased by 12.5% over the past 20 years and is considered to represent only a fraction of the market value (Chen, 2004).

period up to ten years for projects approved by the Investment Promotion Committee (IPC): 25% exemption in Zone A; 50% in Zone B; 75% in zone C. An additional year of exemptions is granted to projects each time they undergo an expansion resulting in a 25% expansion of their proactive capacity for a maximum of four years. Some of the main elements are:

- A corporate tax holiday from 2 to 12 years may be offered to investors.
- Capital goods are exempt from duties and taxes if delivered within three years from the data of IPC's approval. Moreover, capital goods used for expansion and modernisation of an existing plant are exempt, provided they result in at least a 25% increase in capacity.
- Industrial projects are granted property tax exemptions throughout their lifetime. They are also exempted from most municipality and planning fees.
- Exporters enjoy a full exemption of net profits generated from most export revenues from corporate income taxation. Foreign inputs used in the production of exports are exempt from custom duties and import fees.

Zones and their main characteristics[8]

As per early 2005, Jordan has one special economic zone and six public free zones. The SEZ was established in 2001 by greatly enlarging the old (established in 1973) Aqaba Free Port to encompass the surrounding urban area, and transferring economic regulatory responsibility for the Zone to the newly established Aqaba Special Economic Zone Authority (ASEZA).

The free zones are administered by the Jordanian Free Zones Corporation and are subject to broadly similar regulatory conditions. The oldest, and economically most important, is the Zarqa Free Zone 35 km northeast of the capital Amman. Common to all economic zones in Jordan is a broad sectoral scope. Zones are generally open to companies involved in industrial production, trade, tourism and other services. In addition to the public free zones, private free zones, often tailor-made to one specific company, can be established subject to the approval of the Council of Ministers. At the end of 2003 there were 15 such private zones in Jordan[9].

One interesting recent development relates to the development of the so-called Qualified Industrial Zones (QIZ), which essentially extend the benefits of the US-Israel Free Trade Agreement Implementation Act of 1985 to include exports from geographically circumscribed areas in Jordan. The QIZ rules stipulate that a minimum of 35% of the exported goods' value must represent local content. There are currently QIZs in Jordan, three of which are publicly owned. Export originating in the QIZs amounted to US$ 590 million in 2003 (largely textiles and garments), and an estimated 26,500 persons were employed in these zones[10].

Table A5. FEZs in Jordan[a]

---

8 Main sources: www.free-zones.gov.jo and www.aqabazone.com. Outside the zones authorities have at their discretion the granting of partial corporate income tax exemptions for a period up to ten years, selected economic activities (notably in manufacturing) enjoy preferential tax treatment, and the import of capital and input goods is generally exempted from duties.

9 Free Zones Corporation (2003).

10 Kardoosh and al Khouri (2004).

Name	Type	Established	Size (ha.)	Number of companies	Total employment	Cumulative investment (mil. USD)
				End-2003, unless otherwise stated		
Aqaba	SEZ	2001	37500	310[b]	>18,000	423[(b]
Zarqa	Free Zone	1983	520	1,360	ND	696
Sahab	Free Zone	1997	7	41	ND	35
Queen Alia International Airport	Free Zone	1998	3.5	11	ND	10
Al-Karak	Free Zone	2001	15	ND	ND	ND
Al-Karama	Free Zone	2004	200	..	..	..
Al-Muwaqar	Free Zone	2004	12	..	..	..

Notes:
a. Sources: Free Zones Corporation, Annual Report 2003; unpublished material from FIAS.
b. Change between the establishment of the SEZ in 2001 and mid-2004. Source: Harahsheh (2004).

Incentives and quasi-incentives in the Zones

In addition to the incentives listed in Table A6, authorities also provide streamlined registration and other administrative procedures inside the zones to raise transparency and minimise red tape. Modern power grids, telecommunications infrastructure, road networks and water supply are assured inside the zones.

Table A6. Incentives in the Jordanian Economic Zones

	Aqaba Special Economic Zone	**Jordanian Free Zones Corporation**
Regulatory incentives	Foreigners may own land for certain purposes and otherwise lease it for up to 50 years. Staff nationality requirements are eased; up to 70% foreign labour may be employed.	The provision of certificates of origin for industrial products with a local input of less than 40%.
Financial incentives	Foreign firms have access to reimbursement for training expenses, up to a limit of US$ 700 per employee.	None.
Fiscal incentives	ASEZ is a duty-free area (except for motor vehicles) falling outside the Jordanian customs territory. Certain "qualified" enterprises may import automobiles duty-free. A low 5% corporate income tax rate is applied to all net business income, except banking, insurance and land transport that are subject to prevailing rates. No social services tax. No sales tax on most goods and services consumed within the zone. 10% land transfer tax.	Exemption of imported goods and goods exported outside of Jordan from custom duties, taxes and fees. Exemption from customs on sales to the domestic Jordanian market up to the limit of the value of materials and local costs involved in their manufacturing. No corporate income tax on profits earned on manufacturing goods for export, and on profits made from transit trade or selling goods inside the free zones. For the first 12 years, no income and social services tax on the salaries and allowances of non-Jordanian employees. Exemption of buildings and real estate constructions from licensing fees and building and land taxes.
Quasi-incentives	Access to the Aqaba deep sea port.	Opening branches of banks, insurance and clearance companies inside the zones to facilitate financial services for investors.

KUWAIT

General investment climate

Restrictions on foreign direct investment in the Kuwaiti economy (outside the zones) include the following:

- *General restrictions on entry.* As a general rule, government approval is necessary for the participation of non-resident capital in resident corporations. However, a new Direct Foreign Capital Investment Law (DFCIL) came into effect in November 2003, which effectively establishes a positive list of activities in which 100% foreign-majority ownership is allowed. The list includes infrastructure projects; investment and exchange companies; insurance; information technology and software; hospitals and pharmaceuticals; air, land and sea freight; tourism, hotels and entertainments; housing projects and urban development.

- *Sectoral restrictions on entry.* Foreign entry into other sectors than the ones listed above is conditional upon approval by the Council of Ministers. Projects involving oil discovery or oil and gas production are not authorised for foreign ownership. Real estate investment, other than in the context of housing projects and urban development, is restricted to GCC nationals.

- *Land ownership.* As a general rule, non-GCC citizens may not own land in Kuwait. However, the DFCIL authorises land grants to foreign entities for the purpose of investment.

- *Repatriation of investment and profits.* Investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Kuwaiti economy:

- *Corporate income tax rates.* No income tax is imposed on companies incorporated in Kuwait or in other GCC countries and wholly owned by nationals of these countries. Foreign “corporate bodies” carrying on trade or business in Kuwait are subject to taxation on a progressive basis. Rates range from 5% to 55%.

- *Personal income tax rates.* There is no individual income tax in Kuwait.

Investment incentives in the overall economy

DFCIL established an Investment Commission, which is authorised to grant a number of investment incentives. The Commission retains discretion to adjusting the generosity of the incentives according to certain performance criteria, notably the employment of Kuwaiti citizens. The incentives include:

- Exemption from income and other taxes (e.g. taxes on the part of the profits that accrue to foreign nationals) for a period not exceeding ten years, along with the same exemptions in the case of additional investments in a given project.
- Full or partial exemption from customs duties on the following items: machinery, equipment and spare parts required for the establishment or extension of the project; raw materials, semi-finished goods and wrapping and filling materials required for production purposes.

- The allocation of land and certain kinds of infrastructure needed for the project.
- Enhanced access to bring in foreign employees, according to approved ratios set by the Council of Ministers.

Zones and their main characteristics

There is one free economic zone in Kuwait. In 1998, the privately owned National Real Estate Company signed a contract to establish and manage the Kuwait Free Trade Zone (KFTZ) at Shuwaikh Port. The zone came into operation in 1999 and initially covered 24 hectares of land. This soon became occupied and in 2001 another 36 hectares were added. The zone is estimated to be presently operating at 90% of its capacity. The companies located in the zone are mostly domestic, but they include foreign-owned enterprises.

KFTZ operates in large measure like a traditional free zone, providing a ring-fenced customs free area with warehousing facilities and commercial property aimed at services and light production. In the generally low-tax environment of Kuwait, the fiscal and other incentives offered within the zone may not have been of decisive importance to investors. Rather, and especially prior to the passing of DFCIL, it would appear that many investors have been attracted by the relatively more permissive regulatory environment (together with a favourable location and a high-quality infrastructure) in KFTZ.

Table A7. FEZs in Kuwait

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (mill. USD)
Kuwait Free Trade Zone	Free Zone	1999	60	Light industry, trade and services	63	ND	ND

Incentives and quasi-incentives in the Zone

On the whole, the incentives available inside the zone are equivalent to the ones offered to investors in the rest of the Kuwaiti economy. However, they tend to be more far-ranging, and they do not depend on staff nationality. Some of the main incentives are:

- *Regulatory incentives.* 100% foreign ownership is permitted and encouraged. The access to work permits for expatriate staff is easier than in the rest of the country.
- *Fiscal incentives.* Indefinite exemption from taxation on all corporate and personal forms of income. Exemption from taxation on all imports and exports from the zone.
- *Financial incentives.* Moderate utilities rates.
- *Quasi-incentives.* A modern infrastructure including IT and multimedia facilities.

LEBANON

General investment climate

Restrictions on foreign direct investment in the Lebanese economy (outside the zones) include the following:

- *General restrictions on entry.* There are no general limitations on foreign ownership of Lebanese companies. However, entrants must seek the approval and licensing of the Investment Development Authority of Lebanon (IDAL) in accordance with the applicable Investment Development Law 360.

- *Sectoral restrictions on entry.* The only sectoral ban on foreign involvement is broadcast media, which are restricted to Lebanese joint stock companies, all shares of which should be nominally owned by Lebanese. Foreign participation in banking is subject to screening by the Central Bank of Lebanon and foreign participants in the insurance sector benefit from national treatment only if they operate through a fully incorporated subsidiary.

- *Land ownership.* Foreign investors are generally allowed to acquire up to 3,000 square metres of real estate without a permit. They may acquire more than 3,000 square metres subject to Cabinet Decree and upon payment of a registration fee amounting to 5% of the price of the property. However, the law prohibits acquisition of property by Palestinians.

- *Repatriation of investment and profits.* Foreign investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Lebanese economy:

- *Corporate income tax rates.* Companies are taxed at a flat rate of 15% of net profits (7.5% on profits from real estate). Lebanese holding companies and offshore companies are exempt from corporate income tax, as are air and sea transport companies.

- *Personal income tax rates.* The personal income tax system is progressive, with rates starting at 2% and ending at 20% (wages and salaries). However, taxation of "movable capital" (which is defined broadly to include, among other things, directors' fees) takes place at a flat rate of 10% of gross receipts.

Investment incentives in the overall economy

Investors in Lebanon have access to incentive schemes. The country is divided into three Zones A, B, and C, according to supposed levels of economic development. In the most highly developed Zone A investors benefit from: automatic work permits to foreign workers, provided two thirds of the total payroll are Lebanese nationals; and exemption from income tax from two years, provided that its shares are listed on the Beirut Stock Exchange. In Zone B, in addition to the incentives provided in Zone A (and regardless of whether the investors' shares are listed), a 50% reduction in income taxes and taxes on project dividends for a period of five years. In Zone C, in addition to the incentives provided in Zone A (and regardless of whether the investors' shares are listed), a full exemption from income taxes and taxes on project dividends for a period of 10 years.

In addition, a "package deal" contract is foreseen, whereby the Lebanese government may grant investors addition incentives, exemptions and reductions. The maximum generosity of such a package deal, stipulated by law, is:

- A full exemption from income taxes and taxes on project dividends for up to 10 years.
- Work permits for foreign employees provided two thirds of the project's payroll is Lebanese nationals.
- A reduction up to a maximum of 50% of work and residence permit fees, and of permit fees for construction needed for the execution of the project.
- An exemption of joint-stock companies from legal provisions regarding the nationality composition of boards of directors.
- A full exemption from fees related to land registration and from fees for annexation, sub-division, mortgage and registration of lease contracts.

Zones and their main characteristics

Investor attraction strategies in Lebanon have so far not related strongly to establishment of economic zones. Only two zones are in operation, both of them traditional (and long-standing) free-trade zones in the ports of Beirut and Tripoli. The government is, however, considering establishing two additional zones in the northern parts of the country (provisionally named Selaata Free Zone and Qlaiaat Free Zone).

Table A8. FEZs in Lebanon

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (mill. USD)
Beirut Port	Free Zone	1954	12	Storage, trade and light assembly activities	ND	ND	ND
Tripoli Port	Free Zone	1971	15	Storage, trade and light assembly	ND	ND	ND

Incentives and quasi-incentives in the Zones

The fact that the port zones in Beirut and Tripoli are aimed mainly at traders and other light activities reflects upon the (relatively limited) range of incentives offered inside the zones. Some of the main elements are:

- A 10-year corporate tax holiday to companies located inside the zones;

- Total exemption from import duties, and from export duties when exporting to locations outside the Lebanese customs area;
- Long-term low-cost land and building leases. Low-cost utility rates for productive activities;
- Exemption from the obligation to register employees with the social security service (if better or equal benefits are offered to them).

MOROCCO

General investment climate

Restrictions on foreign direct investment in the Moroccan economy (outside the zones) include the following:

- *General restrictions on entry.* The Investment Charter, in place since October 1995, generally puts Moroccan and foreign investors on an equal footing. Private investment is permitted in most sectors, but a few (including phosphate mining) are reserved for the public sector.

- *Sectoral restrictions on entry.* Morocco reserves the rights under GATS to limit foreign participation in the capital of large banking institutions. Approval to perform as an insurance intermediary is only given to natural persons of Moroccan nationality and to legal persons governed by Moroccan law with their headquarters in Morocco and with at least 50% of their capital held by Moroccan nationals. The person in charge must moreover be a Moroccan national.

- *Land ownership.* Foreign national may purchase real estate, except farmland, with funds from foreign exchange accounts. Farmland may be leased for a period up to 99 years and permission can also be given for foreigners to buy farmland in order to use it for purposes (e.g. tourism) other than agriculture.

- *Repatriation of investment and profits.* There are no controls on transfers made directly though the banking system of the proceeds of liquidation or sale of foreign investments, including capital gains, when such investment is governed by the convertibility arrangement (e.g. financed by the sale of foreign exchange or comparable methods). For the liquidation of any investment not falling under this category, the relevant proceeds must be deposited in a convertible deposit account denominated in dirhams. Funds placed therein may be transferred over a five-year period.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Moroccan economy:

- *Corporate income tax rates.* Companies are taxed at a flat rate of 35% of net profits. In addition, they must pay a so-called National Solidarity Levy. The levy is calculated by applying a 10% rate to the amount of the corporate tax. If a company is fully exempt from corporate tax, the levy has to be paid in an amount of 25% to a theoretical corporate tax.

- *Personal income tax rates.* Individuals, regardless of nationality or activity, who have their habitual residence in Morocco are subject to a personal income tax on their worldwide income on a progressive scale between 13 and 44 percent.

Investment incentives in the overall economy

The Investment Charter established a number of incentives, giving broadly the same preference to all sectors except for agriculture. These incentives differentiate between the installation phase and the operational phase of a project. Some of the main elements are:

- Incentives offered for the installation phase:

– *Regulatory incentives.* Exemption from formalities for land acquisition. The application of a limited registration fee of 2.5% for the acquisition of for land. The application of a 0.5% registration fee for inputs in capital formation of companies or increases in capital.

– *Fiscal incentives*. Reduced import dues (between 2.5% and 10% *ad valorem*). Exemption from import tax levy. Exemption from urban tax for first five years after the completion or installation of new buildings. Exemption from VAT on equipment, material and tools acquired locally or imported.

- Incentives for the operational phase are:

– *Fiscal incentives.* Profits and income liable to corporate tax are not subject to the National Solidarity Levy. Exemption from corporate tax for exporting enterprises for five years; a reduction in corporate tax or income tax during the first 10 years thereafter. A 20% investment allowance and capital gains exclusion from 20% to 100% are also offered. Profits and income completely exonerated from corporate tax pay a contribution at a rate of 25% of the normal corporate tax. Enterprises are allowed to create an annual investment reserve free of tax. A preferential sliding-scale depreciation scheme for equipment is in place.

Zones and their main characteristics

Presently one free-zone area is operational, located in the northern city of Tangier. The Tangier Free Zone (TFZ) is located in the vicinity of both Tangier Port, less than 20 kilometres from the European continent, and Boukhalef Airport. Originally established as a traditional free trade zone, TFZ now increasingly operates as an EPZ with several important industrial operations located inside the zone. The zone is being further developed in cooperation with JAFZA of Dubai. The Moroccan authorities reportedly consider establishing a new zone in the port of Nador.

Table A9. FEZs in Morocco

Name	**Type**	**Established**	**Size (ha.)**	**Main economic activities**	**Number of companies**	**Total employment**	**Cumulative investment (mill. USD)**
Tangier Free Zone	Free Zone	..[a]	345	Industrial, real estate, selected services and trade	65	>6,700[b]	ND

Notes:
a. TFZ is the legacy of the Tangier International Zone prior to Morocco's independence.
b. Based on TFZ's website, which provides an incomplete list of the companies in the zone.

Incentives and quasi-incentives in the Zones

Like other free trade zones, TFZ offers exceptions from import duty and taxes, as well as taxes on goods for re-export. In addition to this, the following incentives are offered[11]:

11 Source: www.tangerfreezone.com. .

- *Regulatory incentives.* An exemption from all exterior trade and exchange controls pertaining to the Moroccan economy. Simplified customs procedures.

- *Financial incentives.* For certain sectors, the Moroccan government can provide state financial aid to subsidise the acquisition of plots and the construction of production units.

- *Fiscal incentives.* Exemption from corporate income tax for five years and a rate reduction to 8.75% indefinitely thereafter. Exemption from urban tax and licence tax for 15 years. Exemption from registration tax and stamp duty in connection with the initial investment and subsequent expansion. Exemption from VAT on goods.

OMAN

General investment climate

Restrictions on foreign direct investment in the Omani economy (outside the zones) include the following:

- *General restrictions on entry.* Automatic approval is offered to joint ventures with a majority foreign ownership up to 70%. Registration of these joint ventures is treated in the same manner as that common to all registrants. New entities with more than 70% ownership are subject to the approval of the Minister of Commerce and Industry. In addition, companies establishing a wholly-owned subsidiary in Oman are often required to obtain approval from other ministries, such as the Ministry of Regional Municipalities and Environment.

- *Sectoral restrictions on entry.* New majority foreign-owned entrants are barred from most professional service areas, such as the engineering, architectural, legal, or accounting fields.

- *Land ownership.* With the exception of GCC nationals, who are allowed to own property subject to government approval, foreign individuals and companies may lease but not own real estate.

- *Repatriation of investment and profits*. There are no restrictions on the flow of capital and the repatriation of profits.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Omani economy:

- *Corporate income tax rates.* Foreign owned-companies are subject to taxation on a progressive scale. Rates range from 5% to 30%. Joint ventures with up to 70% foreign participation are subject to the national corporate tax rate of 12%.

- *Personal income tax rates.* There is no taxation of personal income.

Investment incentives in the overall economy

The authorities may grant a range of investment incentives to licensed industrial installations upon the recommendation of the Industrial Development Committee. "Industrial installations" include not only those for the conversion of raw materials and semi finished parts into manufactured products, but also mechanized assembly and packaging activities. The incentives include:

- Soft loans from the Oman Development Bank. To qualify for such loans, the Omani share of the project capital should not be less than 51% and at least 35% of the project's employees should be Omanis.

- Tax holidays for the first five years after setting up a production site, renewable for another five years.

- Customs duty exemptions for capital equipment, raw materials and semi-finished products imported for the sake of the investment project.

- Customs protection by way of imposing or increasing custom tariff on imported goods competing with those produced locally.
- Provision of commercial land, water and power for industrial usage at below-market rates.

Zones and their main characteristics

Oman presently has no economic zones in the definition of the word applied elsewhere in this paper. However, in 1999 the government opened a new free trade zone at an interior border crossing point with Yemen (al-Mazyounah). Oman is reportedly planning to develop a free trade zone in Salalah, adjacent to the international container trans-shipment port that opened in November 1998. The government has also expressed its intention to establish a free zone at Sohar port, in conjunction with plans to expand the existing port and industrial zone.

QATAR

General investment climate

Restrictions on foreign direct investment in the Qatari economy include the following:

- *General restrictions on entry.* In general, foreign participation in a business project is limited at 49%, with the Qatari partner(s) holding at least 51%. Qatar has, however, taken steps toward liberalising its investment regime. Law No. 13/2000 allows for 100% ownership by foreign investors in a number of economic activities, including in services, agriculture, industry, health, education and tourism, and the development and exploitation of natural resources. In 2004, Qatar put in place Law No. 31/2004 which allows foreign investment in the banking and insurance sectors. Both laws are pending approval by decree from the Cabinet of Ministers. When approving majority foreign ownership in a project, Law No. 13/2000 states that the project should "fit into the country's development plans".

- *Sectoral restrictions on entry.* Foreign investors are not allowed to invest in banking, insurance and commercial representation in Qatar.

- *Land ownership.* Ownership of real estate is generally limited to GCC nationals. However, in 2004, Qatar passed a law allowing foreigners to own residential property in select parts of the Pearl of the Gulf Real Estate Development Project.

- *Repatriation of investment and profits.* Investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects[12].

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Qatari economy:

- *Corporate income tax rates.* No income tax is imposed on companies incorporated in Qatar or in other GCC countries and wholly owned by nationals of these countries. Foreign-owned companies are subject to taxation on a progressive basis. Rates range from 10% to 35%.

- *Personal income tax rates.* There is no taxation of personal income.

Investment incentives in the overall economy

Subject to the discretion of the authorities, the following incentives (among others) may be offered to investors:

- Regulatory *incentives.* Flexible immigration and employment rules to enable the employment of foreign labour. Waving of import quotas is also commonplace.

- *Financial incentives.* Preferential energy rates (including natural gas and electricity) and rental of industrial land. Concessionary financing through Qatar Industrial Development Bank.

12 In practice, investors have been complaining about lengthy delays of payments due to red tape (Country Commercial Guide, 2005, US Department of State).

- *Fiscal incentives*. Exemption from customs duties on imports of machinery, equipment and spare parts. Exemption from export duties. Exemption from corporate earnings taxes for five years extendable to ten years.

Zones and their main characteristics

There are currently no FEZs or free ports in Qatar. However, there are plans to develop a free trade zone at the site of the new Doha International Airport, which could be operation by 2008.

SAUDI ARABIA

General investment climate

Restrictions on foreign direct investment in the Saudi Arabian economy include the following:

- *General restrictions on entry.* The Foreign Direct Investment Law permits foreigners to invest in all sectors of the economy, except for specific activities contained in a "negative list" (see sectoral restrictions). Investors need to obtain a license from the Saudi Arabian General Investment Authority (SAGIA).

- *Sectoral restrictions on entry.* The negative list, formulated by the Supreme Economic Council, includes (among other things) the following activities: Oil exploration and production; fisheries; manufacturing of military equipment and civilian explosives; security services; recruitment and employment services; real estate brokerage; printing and publishing; distribution services, wholesale and retail trade; audiovisual and media services; telecommunication; land and air transportation; satellite transmission services.

- *Land ownership.* The purchase of real estate is in principle restricted to Saudi Arabian citizens, corporations and institutions, plus citizens of the GCC. However, under the Foreign Investment Law, foreign investors are allowed to own real estate as needed for their business, including housing for their staff.

- *Repatriation of investment and profits.* Foreign investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Saudi Arabian economy:

- *Corporate income tax rates.* No income tax is imposed on companies incorporated in Saudi Arabia or in other GCC countries and wholly owned by nationals of these countries. Foreign-owned companies are subject to a flat tax rate of 20% (except for the hydrocarbons sector where rates are higher).

- *Personal income tax rates.* Foreign individuals pay tax at a flat rate of 20% on income sourced in Saudi Arabia. Saudi citizens and citizens of member states of the GCC do not pay income tax. They are, however, subject to Zakat, a religious tax based on 2.5% of equity less fixed assets.

Investment incentives in the overall economy

A number of incentives are generally available to investors in Saudi Arabia. Foreigners have access to the incentives, provided that the share of national capital in a given project is at least 25%. Some of the main elements are:

- An income tax holiday of up to 10 years from the commencement of commercial production. (This incentive was repealed in 2004, but is grandfathered for existing investors.)

- For industrial projects, the same privileges as those enjoyed by Saudi capital under the National Industries Protection and Encouragement Regulations. Often linked to the allocation to dedicated industrial parks, these include:

  – Exemption from customs duties on machinery, equipment, tools and spare parts imported for industrial products.

  – Exemption from customs duties on primary raw materials, semi-finished goods, containers, etc., necessary for industrial projects (provided that similar items are not sufficiently available locally).

  – Provision by the government of plots of land at a nominal rate for factories and residential quarters for workers.

  – Low electricity and water rates.

  – Preferential treatment for local products in government procurement in addition to preferential treatment accorded to national products by Arab League and Saudi Arabian bilateral trade agreements.

Zones and their main characteristics

Saudi Arabia does not have FEZs or free ports. It has, however, begun to permit trans-shipment of goods through its ports in Jeddah and Dammam.

SYRIA

General investment climate

Restrictions on foreign direct investment in the Syrian economy include the following:

- *General restrictions on entry.* Applications for investment are screened by a government commission, the Higher Council for Investment, which meets once a month. No definitive criteria for approving investment are made explicit, but the council is reportedly more likely to approve a project if it: maximizes the use of local resources; utilises advanced technologies; boosts exports; creates many jobs; advances the government's development plans; or is located in remote underdeveloped areas.[13]

- *Sectoral restrictions on entry.* Almost all sectors of the economy are open to foreign direct investment. The exceptions are power generation and distribution, air transport, sea port operation, bottling of water, telephony, and oil and gas production and refineries. Foreign ownership of banks is limited to 49%.

- *Land ownership.* Non-residents and foreign nationals may acquire real estate only after presenting evidence that they have converted into Syrian pounds the foreign exchange equivalent of the price of the property at an authorised local bank.

- *Repatriation of investment and profits.* There are relatively heavy restrictions on the repatriation of capital and a wide scope for official discretion. In accordance with Article 24 of Investment Law No. 10 of 4 May 1991, investors who are Syrian expatriates or of foreign nationality are allowed, after the elapse of five years from the investment of the project, to re-transfer abroad the net value of their share of the project in foreign currencies on the basis of the actual value of the project, provided that re-transfer of funds does not exceed the capital brought in by them in foreign currencies, and according to executive instructions issues by the Council in this regard. Profits and revenues realised annually by the investment of external funds may be transferred abroad.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Syrian economy:

- *Corporate income tax rates.* The net profits of incorporated companies are taxed at the following rates. Industrial shareholding companies: 32%; non-industrial shareholding companies: 40%; industrial limited liability companies that use equipment valued at more than 5 million Syrian pounds: 42%[14].

- *Personal income tax rates.* Personal incomes are taxed at variable rates, the highest presently being [20%].

---

13 Based on the 2004 Country Commercial Guide, by the US Department of State.

14 In addition there is a defence tax surcharge, valued at about 30% of the total income tax, and municipal administrative levies ranging from 5% in Damascus to 10% in other areas.

Investment incentives in the overall economy

The Syrian Investment Laws contains provisions regarding investment incentives that authorities have adiscretion to grant, provided the project corresponds to the government's criteria for to be qualified as a relevant sector. Some of the main elements are the following:

- *Regulatory incentives.* The profit repatriation scheme outlined above actually represents an incentive, because it weighs less heavily on investors than the capital accounts regulation otherwise in place in the Syrian economy. The rule that foreign exchange capital can be repatriated after five years, and another rule allowing expatriate staff to repatriate half of their salaries and all of their severance pay, were put in place to encourage investors.

- *Fiscal incentives.* Duty-free import of production inputs such as machinery, equipment and vehicles. Mixed-sector companies in which the Syrian government's stake is at least 25 percent or companies that export 50 percent of their products, are eligible for a seven year tax holiday; private-sector companies may qualify for a five years tax holiday.

Zones and their main characteristics

There are six free zones in Syria. Somewhat unusually for a coastal country, none of these operates in conjunction with a free port. The zones are found near the border town of Dar'a (a joint venture between Syria and Jordan); in Adra (north of Damascus); in Aleppo; in Damascus, and at Damascus International Airport. In addition, free zones are located in the ports of Latakia (intended mainly for storage of goods away from the port area where clearing the items is more difficult) and Tartus. A project for the creation of a free zone port in the Tartus area is being planned.

The General Establishment of Free Zones (GEFZ) is responsible for administering the zones. GEFZ was established in 1972 to promote foreign investment in Syria and to exploit Syria's economic potential and historic role as a "commercial bridge" between East and West. Foreign-owned firms share the same investment opportunities in these areas as indigenous entities.

The zones of Syria are essentially classic free zones, available to all investors domestic and foreign (and mainly used by domestic businesses), providing warehousing and storage facilities, commercial space and space for light manufacturing activities. Most of the zones include “free markets” where imported goods and other merchandise is traded retail or wholesale.

Table A10. FEZs in Syria

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (mil. USD)
					2003, unless otherwise stated		
Damascus	Free Zone	1952	7	Trade, light industry	ND	ND	ND
Tartus	Free Zone	1974	44	Trade and industry	ND	ND	ND
Aleppo	Free Zone	1974	115	Trade, light industry	ND	ND	ND
Lattakia	Free Zone	1974	27	ND	ND	ND	ND
Damascus International Airport	Free Zone	1976	2.5	Metal industries, textiles and appliances	ND	ND	ND
Adra	Free Zone	1977	78	Trade (esp. cars), light industry	ND	ND	ND
Lattakia Port	Free Zone	ND	65	ND	ND	ND	ND

Incentives and quasi-incentives in the Zones

The investment incentives generally in force can be, again subject to the authorities' discretion, be made available to investors in the zones. In addition to this:

- *Regulatory incentives.* No import licensing requirement for inputs and goods entering the zones; importers need only present a manifest as documentation and for inspection purposes. No re-export regulations or restrictions are imposed except for military and internationally prohibited items. All foreign exchange operations are free of applicable currency restrictions. Manufacturers in the free zones are permitted to export 25% of their production to the local market (subject to customs duties).

- *Fiscal incentives.* All goods entering and being stored in the zones are exempt from Syrian taxes and duties.

- *Quasi-incentives.* Access to private banks operating in the free zone areas.

TUNISIA

General investment climate

Restrictions on foreign direct investment in the Tunisian economy (outside the zones) include the following:

- *General restrictions on entry.* Foreigners may invest in most economic sectors. However, authorities screen potential foreign investment to minimise the impact on domestic competitors, employment and foreign currency outflows. For "onshore" projects (not principally directed at exporting) government authorisation is required if the foreign capital share exceeds 49%.

- *Sectoral restrictions on entry.* In much of the service sector (other than tourism) foreign equity is limited to 49%. Agricultural land cultivation is possible by public limited companies in which the equity is at least 34% Tunisian-held.

- *Land ownership.* Real estate purchases by non-residents require prior approval from the Central Bank. Foreign ownership of agricultural land is prohibited, although land can be secured through long-term (up to 40 years) lease.

- *Repatriation of investment and profits.* Foreign investors may freely repatriate profits and proceeds from the sale of equity. Royalty payments must be approved by relevant government ministries in consultation with the central bank on a case-by-case basis.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Tunisian economy:

- *Corporate income tax rates.* Companies are taxed at a flat rate of 15% of net profits. Lebanese holding companies and offshore companies are exempt from corporate income tax, as are air and sea transport companies.

- *Personal income tax rates.* Foreign individuals are subject to Tunisian income tax on income that arises in Tunisia. The tax rates increase progressively from 15% to 35%.

Investment incentives in the overall economy

Investment incentives are available to foreign investors. However, the Tunisian investment code divides potential investment into two categories: (i) offshore, in which foreign capital accounts for at least 66% of equity and at least 80% of the production is destined for the export market; and (ii) on-shore, in which foreign equity is limited to 49% in most non-industrial projects (on-shore industrial investment may have up to 100% foreign equity). Overall, Tunisian practices toward direct investment display a strong preference for attracting export businesses.

The 1994 Investment Incentive Law, and subsequent related provisions, offers the following fiscal incentives for all types of investment: (i) tax relief on reinvested revenues and profits; (ii) VAT limitation to 10% on many imported capital goods; (iii) favourable depreciation schedules for production equipment.

Offshore investment projects (or "fully-exporting companies") may benefit from the following additional inducements:

- *Fiscal incentives.* Full tax exemption on corporate profits for the first ten years; 50% reduction in profit taxes thereafter. Full tax exemption on reinvested profits and revenues. Full tax and duty exemption on raw materials and semi-finished goods and services necessary for the business. Duty-free import of capital goods with no local equivalent.

- *Financial incentives.* Large investments that have a high job creation potential may benefit, under certain conditions to be determined by the High Commission on Investment, from the use of state-owned land at a symbolic price.

Moreover, a number of special incentives are available to investors allocating to certain parts of the country considered to be in need of economic development. These are subdivided into two categories, the "Encouragement Zone" and the "Priority Zone", in which investors may benefit from a direct subsidy of 15% and 25% of the investment value. Many of the fiscal incentives available to offshore companies may also be made available to them. In addition, the State may assume the employers' contribution to the social security scheme and undertake certain infrastructure expenses in support of the investment.

Zones and their main characteristics

Tunisia has two free zones, one in the north at Bizerte and one in the South at Zarzis. The two areas have been officially reclassified from free zones to "economic activities parks", partly reflecting the fact that most of the traditional fiscal advantages accorded to free zones are equally available to offshore projects in the Tunisian economy at large. The Economic Activities Park of Bizerta is spread on two sites, Bizerta located next to the commercial port and Menzel Bourguiba bordering on the national shipyards. The Zarzis Park of Economic Activities is located adjacent to the port of Zarzis.

While certain additional incentives are available in the zones (see below), a major benefit to investors seems to be the fact that they operate as one-stop shops. Tunisia is relatively open to foreign investment, but its system of dual investor categories, foreign exchange accounts and administrative approval procedures makes many foreign investors opt for the reduced regulatory compliance burden inside the zones.

Table A11. FEZs in Tunisia

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (mill. USD)
Bizerta	Free Zone	1972	51	Mechanic and electrical industry, shipbuilding, food processing, services.	ND	ND	ND
Zarzis	Free Zone	ND	32	ND	ND	ND	ND

Incentives and quasi-incentives in the Zones

According to publicly available material, the incentives offered to investors in Bizerta and Zarzis do not differ very much. In addition to the incentives offered to offshore companies, some of the main elements are:

- *Regulatory incentives.* Freedom to operate outside Tunisia's relatively complex system of foreign exchange regulation. Flexibility in employment owing to limited duration employment contracts.

- *Fiscal incentives.* Exemption from VAT on local purchases. Fixed individual income tax rate of 20% on foreign staff salaries. Tax exemption on imports of personal effects and a private car for each non-resident staff.

- *Financial incentives.* Preferential land rental and utilities rates inside the zones.

UNITED ARAB EMIRATES

General Investment Climate

Restrictions on foreign direct investment in the UAE economy (outside the zones) include the following:

- *General restrictions on entry.* At least 51% of companies, other than branches of foreign enterprises, must be held by nationals of the Emirates. GCC nationals are permitted to hold (1) up to 75% of the equity of companies in the industrial, agricultural, fisheries and construction sectors; and (2) up to 100% of the equity of companies in the hotel industry.

- *Sectoral restrictions on entry.* Foreigners are effectively excluded from the distribution sector. The Commercial Agencies Law requires that foreign principals distribute their products in the UAE only through exclusive commercial agents that are either UAE nationals or companies wholly owned by UAE nationals.

- *Land ownership.* Until recently, only GCC nationals were permitted to own land in UAE. In May 2002, the Emirate of Dubai announced that it would permit so-called “free hold” real estate ownership for non-GCC nationals by giving permission to three companies to develop and sell freehold properties on government-designated pieces of land.

- *Repatriation of investment and profits.* Foreign investors are entitled to remit abroad, in convertible currency, foreign capital invested, including returns, profits and proceeds arising from the liquidation of investment projects.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the UAE economy:

- *Corporate income tax rates.* The federal government has not promulgated any tax laws. Most of the individual emirates have issued corporate tax decrees, but they are mostly limited to the hydrocarbons sector and to branches of foreign banks, which are taxed at fixed rates.

- *Personal income tax rates.* There is no taxation of personal income.

Investment incentives in the overall economy

Outside the zones, no incentives are generally offered. However, the ability to purchase property as freehold in certain favoured projects in Dubai – and promises that foreign owners of such property would be granted residence permits as long as they remained in possession of title – might qualify as a regulatory incentive aimed at attracting foreign investment.

Zones and their main characteristics

The UAE has become an important destination for investment and this is largely due to the country’s FEZs. Quoting from a recent study, they have “transformed the economic scenario of the Emirates and brought about tremendous change in the industrial scene of this nation”.[15] The country’s zones are presently host to more than 5,000 companies that have invested an estimated US$ 4 billion.

[15] SIMEST (2004). (The translation is that of the author)

The pioneer in this respect – and by far the largest and most well-known zone – is Jebel Ali Free Zone (JAFZ), which was started in Dubai in 1985. The free zone concept was at the time a novel concept in the Gulf region. Twenty years later, UAE has essentially based its foreign investment strategy on the zones. Sixteen free zones and industry zones are in operation, and several more are under preparation. The success of JAFZ has been such that its operating company is now selling know-how to, or otherwise involved in the development of, several of the other zones mentioned in this paper.

An interesting recent development is the proliferation of industry zones – essentially intended as centres of innovation – that have been established in Dubai since 2000. One example is the TECOM (Technology, Electronic Commerce and Media) free zone. TECOM offers a modern multimedia infrastructure; it houses both Internet City and Media City, two subdivisions which cater to the IT and media sectors. Another example is the Health Care City, specialising in medical products.

Table A12. FEZs in UAE

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employ -ment	Cumulative investment (bn. USD)
Jebel Ali	Free Zone	1985	10000	Trade activities, processing, manufacturing, packaging and assembly activities, storage	2,200	ND	ND
Dubai Airport	Free Zone	1996	1200	Manufacturing, processing and assembly activities, trade activities and selected services	300	ND	ND
Fujairah	Free Zone	1987	150	Storage, manufacturing, processing, assembly and packaging activities, trade activities	220	ND	ND
Hamriyah	Free Zone	1995	1200	Manufacturing, processing, packaging, assembly and trade activities, selected services	269	ND	ND
Ajman	Free Zone	1996	100	Trade activities, processing, manufacturing, packaging and assembly activities, selected services	700	ND	ND
Ras Al Khaiman	Free Zone	2000	188	Storage, manufacturing, packaging, processing and assembly activities, consulting and services activities, trade activities	289	ND	ND
Dubai Internet City	Industry Zone	2000	400	Business from Web based, Back Office, Consultancy, IT Support, Software development, sales and marketing	ND	ND	ND
Dubai Media	Industry	2001	30	Business from broadcasting, production, advertising,	ND	ND	ND

City	Zone			public relations, recruitment, music, publishing, marketing, consultancy, Web-casting/New Media, post-production, research			
Dubai Gold and Diamonds Park	Industry Zone	2001	4,75	Gold and diamond trading, designing, manufacturing and crafting of gold and diamond jewellery	ND	ND	ND
Dubai Customs & Automobile Free Zones	Industry Zone	2000	800	Trading in cars	ND	ND	ND
Ahmed Bin Rashid Free Zone - Umm Al Quwain	Free Zone	1988	11,8	Manufacturing, trading and consultancy	ND	ND	ND
Sharjah Airport International Free Zone	Free Zone	1995	100	Trade activities, processing, manufacturing, packaging and assembly activities, selected services	ND	ND	ND
Dubai Development & Investment Authority	Free zone	2002	ND	Selected services	ND	ND	ND
Dubai Metals & Commodities Centre	Industry Zone	2002	ND	Gold, diamond and commodities trading	ND	ND	ND
Knowledge City	Industry Zone	2003	ND	Education, Training and Research activities	ND	ND	ND
Dubai Health Care City	Industry Zone	2003	ND	Healthcare services	ND	ND	ND

Incentives and quasi-incentives in the Zones

The zones' attractiveness to foreign investors largely hinges on the fact that they provide a permissive regulatory environment. Offering "classic" inducements to investors, such as tax breaks and subsidised infrastructure, would in itself be unlikely to have much effect in the low-taxing and generally modern economies of UAE. However, the opportunity to get around the country's strict rules on foreign control on corporate entities and land has made investors flock to the FEZs. Some of the main incentives can be thus summarised:

- *Regulatory incentives.* 100% foreign ownership and unrestricted access to the zones. Access to land through long-term renewable leases.
- *Fiscal incentives.* Complete exemption from taxes, customs and commercial levies.
- *Financial incentives.* Low land rates.
- *Quasi-incentives.* Access to ports and a large and well-educated labour force.

YEMEN

General investment climate

Restrictions on foreign direct investment in the Yemeni economy (outside the zone) include the following:

- *General restrictions on entry.* Article 42 of Yemen's Investment Law states that non-Yemeni subscription to the capital of an investment company shall not exceed 45 per cent of paid in capital, except where the proportion is increased by decree of the Council of Ministers.

- *Sectoral restrictions on entry.* Foreigners are excluded from investing in banks and exchange bureaus; the manufacture of weapons and explosive materials; and industries that harm the environment and health. The Investment Law explicitly excludes the exploration and extraction of oil, gas and minerals, which are governed by special agreements.

- *Land ownership.* The undertakers of an investment project, Yemeni or foreign, are entitled to purchase or lease land and buildings to be used for the purposes for which the project is registered. In practice, however, most foreign companies have found it more convenient to operate via a Yemeni agent.

- *Repatriation of investment and profits.* Article 15 of the Investment Law states that an investor may transfer abroad foreign currency funds and net profits earned by investment or any of its accrued returns to any transferable currency, and that the foreign investor may retransfer abroad invested capital upon liquidation or disposal.

Elements of the tax regime applying to foreigners or foreign-owned enterprises in the Yemeni economy:

- *Corporate income tax rates.* Resident and foreign-owned companies are subject to a flat tax rate of 35%.

- *Personal income tax rates.* Tax rates are progressive. The highest rate is presently 35%.

Investment incentives in the overall economy

The Investment Law provides a set of incentives, largely fiscal, that apply to investment projects in general. Some of the main elements are:

- Exemption from corporate profit tax for 7 years, extendable to 16 years according to the decision of the Council of Ministers. (The Council may designate priorities sectors or activities that shall enjoy extensions from the standard 7 years.)

- Exemption from real estate tax and taxes imposed on capital and contract documentation fees.

- Exemption from tax and custom fees on project fixed assets.

- Exemption from tax on the proceeds of licensing of technology use for 5 years.

Zones and their main characteristics

There is one economic zone in operation in Yemen, namely the Aden Free Zone located next to Aden Port. While Aden has a long history as a free port, the present zone was established in 1991 under the administration of the Yemen Free Zone Public Authority. There are plans to greatly expand the free zone to include 15 areas of Aden Cite with a total area of around 32,500 hectares (and concomitantly to expand the size of the container port). However, in the aftermath of the terrorist attacks in Yemeni waters these plans were set back somewhat.

Table A12. FEZs in Yemen[16]

Name	Type	Established	Size (ha.)	Main economic activities	Number of companies	Total employment	Cumulative investment (mill. USD)
Aden Port	Free Zone	1991	28[(a]	Industrial, real estate, service and trade	29		

a) Including only parts of the Industrial & Warehousing Estate already developed.

Incentives and quasi-incentives in the Zone

The Aden Free Zone offers the usual advantages of a free zone, including customs-free imports and exports out of the Yemeni customs area.

- *Regulatory incentives*. 100% Foreign Ownership permitted and encouraged. Nationalisation and expropriation of projects operating in Aden Free Zone are not permitted.
- *Fiscal incentives*. Exemption from taxation on corporate profits for 15 years with a possible extension for subsequent 10 years. Salaries, wages and bonus of non-Yemeni employees working on projects in Aden Free Zone are exempt from income tax.
- *Quai-incentives.* Location adjacent to Aden Port.

16 Main source: www.aden-freezone.com.

ANNEX 2: CONCLUSIONS OF TASK FORCE ON INCENTIVES, 29-30 JUNE, BAHRAIN

Fiscal transparency and policymaking

1. Investment incentive policies need to be co-ordinated. All tax and non-tax incentive policies to promote investment should be coordinated with one another, within a coherent policy framework designed to improve the investment environment.

- As incentives are just one policy tool of the Government to promote investment, these policies must be coordinated with other policies aimed at promoting the investment climate, including macroeconomic policies, trade and industry policies and governance reforms.

- All investment incentives should be set in an overall strategy developed by the Ministries with responsibility for incentives. This will avoid the problem of competing or contradictory policy aims and legal inconsistencies. MENA countries should consider ensuring that a budgetary ceiling is set on the amount of incentives that can be granted each year, as a way to prevent unintended government spending or revenue loss.

2. Investment incentive policies should be transparent. MENA countries should consider adopting greater transparency in the provision and delivery of incentives for investment. Transparency would be enhanced through ensuring that:

- The specific goals and objectives of each incentive scheme are clear and publicly disclosed.

- Information about each incentive scheme is published and posted on relevant Government websites, including comprehensive descriptions of each scheme, procedures and criteria for obtaining incentives, and the estimated cost of each scheme, where relevant information is available to support reliable estimates.

- Both estimates of future costs of incentives and costs incurred by existing incentives should be made in order to inform policymaking and to support ongoing capacity building to evaluate incentives.

- Incentives should, to the greatest extent possible, be rules-based. In practice this means that administrative discretion in the awarding of incentives should be limited and the criteria for exercising discretion are publicly disclosed. Incentives prone to abuse will require more oversight.

3. Expenditure reporting frameworks and procedures should be developed to publicly report the cost of investment incentives where the requisite information is available. Annual tax and non-tax expenditure reporting of the cost of incentives will help ensure proper management of public funds and reduce the scope for corruption.

Designing the incentives framework

1. Investment incentives should be designed to maximise efficiency. Incentives should be designed to maximise the benefits and minimise the costs of each incentive offered. To maximise efficiency, policymakers should:

- Chose the types of incentives they offer with a view to ensuring efficiency. Subsidies are usually most effective when linked closely to the activity that they are meant to promote. Also, when incentives are motivated by a need to compensate for weaknesses in the enabling environment, a more efficient outcome can be secured by tackling these shortcomings directly. Both considerations would seem to favour targeted, financial incentives over general, fiscal ones. However, this needs to be balanced against budgetary constraints.

- Avoid stacking of incentives. Offering multiple incentives (e.g. by different Ministries) tends to be counterproductive, as it increases not only program costs but also complexity, contributing to compliance and administrative costs. It also leads to unintended patterns of relief and subsidies across different investors and asset types, leading to inefficiencies in resource allocation. Furthermore, offering a myriad of incentives can create the impression that the country is compensating for a lack of a proper enabling environment for investment

- Choose incentives that can be adequately administered by programme administrators. When considering alternative incentive mechanisms, an important requirement is a workable set of rules and regulations that are understandable not just to investors, but also to those responsible for the administration of the incentive. Internal capacity of relevant Ministries should be further developed to strengthen tools and techniques to evaluate incentives.

- MENA governments should consider eliminating or phasing-out, with “grandfathering”[17], tax holidays, which are most prone to tax-planning abuse and revenue loss. For these existing incentives, a transparent approval and monitoring process should be put in place to detect potential abuse and firms should be required to file annual profit statements. Existing holidays must also be coupled with strong and transparent anti-abuse rules. Specific base protection rules include robust transfer pricing rules, thin capitalisation and controlled foreign corporation rules. Countries are also encouraged to utilise the exchange of information procedures in their double tax treaties, (Article 26 of the OECD Model Tax Convention).

[17] Grandfathering concerns providing tax relief made available in the past to investors that previously qualified and accessed such relief.

2. Duty free zones and special economic zones must be carefully designed. Zones can be an efficient way to develop an export industry, and to minimise the costs of doing business and simplify administrative procedures in parts of a country. To ensure that zones achieve their objectives, authorities need to take into account the following consideration:

- Discrimination between companies on the basis of nationality and/or sectors should generally be avoided. Access to the zones should be based on objective criteria.
- Adequate policies should be designed to encourage linkages between enterprises located in special economic zones and the rest of the host society. The ultimate goal should be to widen the economic achievements of the zones to the whole economy.
- Performance requirements, while sometimes justified by the presence of incentives and other subsidies, need to be carefully assessed. Performance requirements are often second-best to rethinking the generosity of other schemes.
- Where a specific regulatory environment is created for the zone, care must be taken to ensure that core labour and reporting standards together with other recognised international standards are not violated.

Evaluation and monitoring of incentives

1. The ability of the administering body to effectively monitor incentives should be ensured. One frequent complaint is that government agencies responsible for incentives are at a disadvantage vis-à-vis better staffed and resourced multinational enterprises. Even where this is not the case, they often lack the analytical ability to conduct in-depth impact and cost-benefit analysis of the schemes they administer. Sufficient resources must be allocated to administration of the incentives to ensure they are effectively monitored.

2. The costs and benefits of current and proposed investment incentives should be assessed. MENA countries should work towards developing frameworks and capacities to analyse the costs and benefits of existing and proposed incentives. Such cost/benefit assessments would involve:

- The hoped-for direct and indirect benefits of incentive schemes need to be specified and, wherever possible, quantified.
- The effectiveness of incentives in achieving authorities' stated policy goals (e.g. additional investment, jobs and exports) should be documented.
- Estimated direct and indirect costs of the incentive (cash or cash-equivalent outlay, revenue foregone and administrative costs) must be accounted for.
- Broader-based efficiency considerations need to be taken into account. In particular, even when a scheme is found to be effective, in that benefits exceed costs, authorities need to assess whether even better results could have been obtained at a similar cost.

3. All investment incentives should have "sunset clauses"[18]. To facilitate monitoring and evaluation of incentives as well as curb unintended abuse, investment incentives should be introduced for a fixed period and be renewed only after evaluation and enactment of new legislation. For those incentives particularly susceptible to abuse, such as tax holidays, the fixed period should be no longer than 5 years, beginning in the year of production.

Policy forum and capacity building

1. Establishing a regional MENA tax and incentive policy forum. To share experience and results of studies in tax and incentive policy and promote regional co-operation, MENA countries should consider active participation in MENA-OECD policy roundtable discussions, held through both physical and electronic meetings with the results and information disseminated to all participants. Possible topics could include consideration of criteria for assessing incentives and possible policy frameworks for supporting small and medium sized enterprises and entrepreneurship.

2. Strengthening capacity to analyse investment incentives should be a priority. In addition to addressing the concerns about administrative ability raised above, MENA countries should further consider strengthening their analytical capacities. There is a need to develop analytical frameworks, databases and technical expertise of officials working in the incentive policy area, through national and regional programs and forums. Specific topics could include:

- Empirical and case study analyses of linkages between incentives and investment
- Alternative incentive types and designs
- Databases for incentive analysis, simulation models to estimate the revenue cost of tax incentives
- Expenditure reporting, alternative benchmark choices and reporting practices
- Guidelines for monitoring incentives
- Anti-abuse rules
- Double tax treaty negotiation
- Exchange of information.

[18] Sunset clauses are provisions requiring the automatic termination of incentives after a specified number of years.

BIBLIOGRAPHY

Alessandrini, S. (2000), "FDI in the MENA Region", *Paper presented at the third Mediterranean Development Forum in Cairo*, March 2000.

Chen, D. (2004), "Reformulating the Tax Incentive Program in Jordan: Analysis and Recommendations", *paper commissioned by the US Agency for International Development*.

Economic Development Board (2004), *Investor's Guide to Bahrain*, Manama.

ESCWA (2004), "Policies Aimed at Attracting Foreign Direct and Interregional Investment in the ESCWA Region: Improving the Climate for Foreign Direct Investment and Mobilising Domestic Savings", *Case Studies of Bahrain, Jordan and Yemen*, United Nations.

Ernst & Young (2003a), "Corporate Taxation in the Middle East", *Paper issued in the International Tax Services series*.

Ernst & Young (2003b), *An Executive Guide to Doing Business in Bahrain*.

Free Zones Corporation (2003), *Annual Report 2003*.

Grubel, H. (1984), "Free Economic Zones: Good or Bad", *Aussenwirtschaft*, Vol. 39.

Harahsheh, A. (2004), "Public-Private Free Zones: Policy, Institutions and Physical Characteristics", paper presented at the Roundtable on An Enabling Environment and Economic Zones for Private Sector Development in Bangladesh, organised by FIAS on 14-15 December 2004.

International Monetary Fund (IMF) (2004), *Annual Report on Exchange Arrangements and Exchange Restrictions 2004*, Washington DC.

Investment Development Authority of Lebanon (2004), *Investor's Guide to Lebanon*.

Kardoosh, M.S. and R. al Khouri (2004), "Qualifying Industrial Zones and Sustainable Development in Jordan", mimeo.

Kusago, T. and Z. Tzannatos (1998), "Export Processing Zones: A Review in Need of Update", *Social Protection Discussion Paper*, No. 9802, World Bank.

Kuwait Free Trade Zone (2001a), *Investor Guide*, Third Edition.

Kuwait Free Trade Zone (2001b), *Bylaws,* First Edition.

OECD (2003), *Checklist for Foreign Direct Investment Incentive Policies*, Paris.

OECD (2004a), "Regulatory Environment for International Investment in MENA Countries", *Paper tabled for the meeting of the OECD-MENA Investment Steering Group in Amman on 30 June 2004*.

OECD (2004b), "Investment Incentives and FDI in Selected ASEAN Countries", *International Investment Perspectives*, Paris.

Oman Chamber of Commerce and Industry (1999), "Investment Incentives in the Sultanate of Oman", mimeo.

SIMEST (2004), "Free Zones in Aree Estere: Elementi conoscitivi per Progetti di internaziolizzazione di Sistemi di Impresa", *Paper prepared for the European Union.*

Singa Boyenge, J.-P. (2003), *ILO database on export processing zones*, International Labour Organisation, Geneva.

Tahir, J. (1999), "An Assessment of Free Economic Zones in Arab Countries: Performance and Main Features", *Working Paper 9926*, OAPEC.

UNCTAD (2003), *Investment Policy Review: Algeria*, United Nations, Geneva.

United States Commercial Service, *Country Commercial Guides*, (2004 or 2005 edition).

van der Zande, J. (2003), "Free Zones and Special Economic Zones in Egypt", *Paper by the Netherlands Ministry of Foreign Affairs.*