

COMPARATIVE ANALYSIS OF TAX INCENTIVES IN SPECIAL ECONOMIC ZONES IN THE COUNTRIES OF THE ASIA-PACIFIC REGION

Olga Sinenko – Igor Mayburov

Abstract

The article analyses theoretical grounds for tax incentives provided by special economic territories in the Asia-Pacific Region. The main research methods were analysis, synthesis and comparative analysis. All types of tax incentives were broken down into groups and the purpose of each group was identified in relation to the type of the SEZ. The authors prove that there is a prevalence of technology development zones that take the form of science and industry clusters aimed at the creation of hi-tech production facilities. The authors argue that fiscal instruments have become an indispensable part of a package of measures for luring investors in SEZs. A conclusion is drawn that today tax incentives in special economic zones play a much bigger role in investment decision making than in previous years. The underlying causes of this development are analyzed. The authors show that the size of tax incentives and the duration of tax holidays for investment projects have been growing; they also observe that nontax barriers are being removed, thus facilitating trade liberalization and capital mobility. A conclusion is made that each class of special economic zones employ specific tax incentives that are best suited for their goals. It is shown that as a result of competition between the countries of the Asia-Pacific Region, they offer a nearly standardized package of tax incentives that tends to be further unified.

Key words: tax incentives, special economic regime, Asia-Pacific region, comparative analysis

JEL Code: H21, H25

Introduction

Today, the countries of the Asia-Pacific Region (APAC) are home to a large part of the world population (57 percent, or 4.1bn people) and account for 40 percent of global industrial output. They produce over one third of the gross world product. The region spreads from Turkey in the west to the island republic of Kiribati in the East, and from the Russian Federation in the north to New Zealand in the south. Being the fastest developing area in the world, over the past few decades

the Asia-Pacific Region has put emphasis on the development of special economic zones (SEZ). Tax incentives are the most commonly used tool of attracting foreign investment to such zones.

1 Literature review

Transformations that are taking place in the Asia-Pacific have been an area of academic interest. More specifically, the experience of the Asia-Pacific countries in building mechanism of tax incentives in special economic zones and the results of luring investors in such zones are an attractive subject for scholars. A number of studies by the International Monetary Fund (IMF, 2016) and the Asian Development Bank are devoted to the peculiarities of fiscal policies and tax administration in the Asia-Pacific economies (Araki, S. & Claus, I., 2014). The taxation of investments and the problem of determining effective average tax rates in the Asia-Pacific Region were investigated by (Wiedemann, V. & Finke, K., 2015). In the Asia-Pacific countries, foreign direct investments are subject to a tax that ranges from 10.6% in Hong Kong to 40.4% in India. There are, however, tax incentives for private investors that lower the effective average tax rate by around 8.6%. The most generous tax incentives are offered in the hi-tech industry. An overview of tax incentives available to producers in the Asia-Pacific and ASEAN can be found in reports by UNIDO and EY (UNIDO, 2014), (EY, 2014).

2 Methods and materials

The key methods utilized by the authors were analysis, synthesis and comparative analysis. An analysis of tax incentives available in SEZs was performed. The types of tax incentives were systematized and the goals of tax incentives were identified in relation to the type of each free zone: free trade zones, technology implementation SEZs, export processing zones, special purpose free trade zones. A comparative analysis of tax incentives offered by the leading SEZs in the Asia-Pacific was performed and a summary was produced of tax incentives that are available in the main types of China's industrial parks. The study used data from the websites of SEZs in the Asia-Pacific Region and scholarly journals. The study covered a period from 2013 to 2016. A comparative analysis of tax incentives available in Chinese SEZs was performed. The analysis that included different types of free zones was done over a list of the main fiscal incentives provided to these territories.

3 Analysis of tax incentives in special economic territories in Asia-Pacific countries

3.1 Special economic territories in Asia-Pacific countries.

According to the International Labour Organization, the number of SEZs grew from 176 in 46 countries in 1986 to 3.500 in 135 countries in 2013. The success of economic transformations in Singapore, Korea and Hong Kong are often attributed to SEZs. (Sinenko, O. & Mayburov I., 2017).

Tab. 1: Number of SEZs in Asia-Pacific countries (2016)

Type of zone	Varieties	Number	Asia-Pacific countries that have the indicated zones
Free trade zones	Free customs zones, foreign trade zones, free investment zones	784	China, USA, South Korea, Japan, et al.
Technology development zones	Economic and technological development zones, technology parks, industrial parks	1,111	China, USA, Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand, Vietnam, Japan, South Korea, et al..
Export processing zones	Export zones, hi-tech industry development zones, industrial development zones, science and industry clusters, enterprise zones	108	China, Myanmar, Vietnam, et al.
Specialized zones	Special economic zones, border development zones, eco-industrial parks, innovation districts	295	China, Cambodia, Indonesia, Malaysia, Myanmar, Vietnam, Singapore, South Korea, Japan, et al.

Source: Authors' own calculations according to listed APAC countries: China, USA, Brunei, Cambodia, Indonesia, Malaysia, Myanmar, Philippines, Singapore; Thailand, Vietnam, South Korea.

In China, industrial zones were created as testing grounds for gradual liberalization of the economy and export-led industrialization. Chinese SEZs brought about a 7-percent growth in foreign investment a year and boosted regional economic growth by 12 percent a year. The success of the East Asian countries inspired many developing countries to establish various types of free zones (Sinenko, O., 2017).

The term "special economic zone" is a generic one and encompasses various classes of economic entities. They can be grouped according to their functional specialization (Tab. 1). Technology development zones are a dominant class among the SEZs in the Asia-Pacific Region. It is a new generation of special economic zones that take the shape of science and industry clusters oriented to hi-tech production. The list of vivid examples of technology parks in the Asia-Pacific Region includes Silicon Valley, Boston's Route 128 in the USA, technology parks in China's Shenzhen and Guangdong, and Tsukuba in Japan.

3.2 Tax incentives in special economic zones in Asia-Pacific countries

Tax incentives in SEZs have a much bigger influence on investment decisions because the size of tax breaks has been growing and longer tax holidays are being offered to investment projects.

Tab. 2: Prevalence of tax incentives around the world

	Number of countries surveyed	SEZ/free zones/EPZ/free ports	Tax holiday/tax exemption	Reduced tax rate	Investment allowance/tax credit	VAT exemption/reduction	R&D tax incentive
East Asia and Pacific	12	83%	92%	92%	75%	75%	83%
Eastern Europe and Central Asia	16	94%	75%	31%	19%	94%	31%
Latin America and the Caribbean	24	75%	75%	29%	46%	58%	13%
Middle East and North Africa	15	80%	73%	40%	13%	60%	0%
OECD	33	67%	21%	30%	61%	79%	76%
South Asia	7	71%	100%	43%	71%	100%	29%
Sub-Saharan Africa (SSA)	30	57%	60%	63%	73%	73%	10%

Source: (Zolt Eric M, 2015)

Tab. 2 shows prevailing tax incentives and types of SEZs in the regions of the world. The data in Tab. 2 indicate the prevalence of SEZs (free zones, export processing zones and free ports) in the countries of Central Asia and the Pacific (over 80 percent of all countries surveyed). The most commonly employed tax policy tools are tax exemption (in over 70 percent of SEZs), reduced tax rates and tax incentives.

Tab.3: Tax incentives offered by major technology SEZs and export processing zones in Asia-Pacific countries

	Corporate income tax	VAT	Customs duties
Tax incentives in technology SEZs			
China: China-Singapore Suzhou Industrial Park (CS-SIP)	Exemption for the first two years upon making profit. Half the normal rate for the following three years. Companies exporting 70% of their output are entitled to 15% -rate Innovative companies are charged 10%	Exemption of imported materials, equipment and components for producing goods to be exported	
Brunei: Sungai Liang Industrial Park (SPARK)	Exemption for 5, 8 or 11 years depending on the nature of industry. Self-employed individuals and cooperatives enjoy exemption indefinitely.		
Thailand: Bang Chan Industrial Estate	Exemption from 3 to 8 years. Half the normal rate for the following five years.	Exemption	Exemption from import duties
Tax incentives in export processing zones			

China: Shanghai Jinqiao Export Processing Zone (JEPS)	Reduced rate of 15%. Hi-tech companies are charged 10% for three years. 10-percent rate levied for one year on companies exporting over 70% of their output.	Exemption for products sold in the zone.	Exemption from export duties
South Korea: Masan Export Processing Zone	Exemption for 3 years. Half the normal rate for the next two years provided that the resident invests over 10m dollars.	Exemption	Exemption of goods imported for zone purposes.

Sources: Compiled by the authors according to listed SEZ: China-Singapore Suzhou Industrial Park, Sungai Liang Industrial Park, Bang Chan Industrial Estate, Jinqiao Export Processing Zone, Masan Export Processing Zone.

The key feature of the incentives offered to residents of technology parks is that they are aimed at promoting small venture business. Tax and administrative incentives are accompanied with the possibility of implementing projects in cooperation with universities, research laboratories etc. In most cases, tax incentives are offered in the form of exemptions from taxes for a limited period of time or indefinitely (Tab. 3).

Tab.4: Tax incentives offered by major free trade zones and specialized economic zones in Asia-Pacific

	Corporate income tax	VAT	Customs duties
Tax incentives in free trade zones			
China: Shanghai Pilot Free Trade Zone (CSPFTZ)	might be paid by installments over a period of up to five years	Reduced rate of 5%. Export VAT refund	Exemption of imported industrial equipment
China: Waigaoqiao Free Trade Zone	Exemption for revenues earned by foreign-invested companies in shipping, warehouse, and international shipping	Reduced rates	Goods carried in and out of the zone are exempt from customs duties and import related taxes and free from inspection
South Korea: Jeju Investment Promotion Zones	Tax holidays of three to five years depending on invested capital. Half the normal rate in subsequent two years	Exemption	Exemption for three to five years
Japan: Okinawa Special Free Trade Zone (OSFTZ)	Reduced rate of 35%; 19% for SMEs with at least 20 employees.	Exemption	Exemption
Tax incentives in specialized economic zones			
Philippines: Philippine Economic Zone Authority (PEZA)	Tax holiday for new projects for six years; four years for existing projects.	Exemption	Exemption granted to imported equipment, raw materials and spare parts and all exported products
China: Shenzhen Special Economic Zone	Reduced rate of 15%. 10%- rate levied for one year on companies exporting over 70% of their output. Hi-tech companies are charged 10% for three years.	Exemption for products made and sold in the zone.	Exemption for imported commodities to be used in production of goods for export

Thailand: Narathiwat Special Economic Zone	Exemption for three to eight years. Half the normal rate for the next five years.	Exemption for materials, machinery, equipment etc.	Exemption of imported materials, equipment and components etc.
-----------------------------------------------------	-----------------------------------------------------------------------------------------	-------------------------------------------------------------	----------------------------------------------------------------------

Sources: Compiled by the authors according to listed SEZ: Shanghai Pilot Free Trade Zone, Waigaoqiao Free Trade Zone, Jeju Investment Promotion Zones, Okinawa Special Free Trade Zone, Philippine Economic Zone Authority, Shenzhen Special Economic Zone, Narathiwat Special Economic Zone.

Export processing zones are typically found in developing countries where labor is inexpensive. Tax and customs incentives for citizens of such zones are usually offered depending on specific industries. As a rule, they have one thing in common: they all offer reliefs from customs duties.

Free trade zones are designed to provide a range of foreign trade services: warehouse storage, shipping, loading and unloading, sale of goods, repair of vessels (Tab. 4). Preferential tax treatment in such zones usually includes exemptions from customs dues and VAT for goods that were finished and processed in the zone, export tax refunds and other incentives. Specialized zones are created with the purpose of promoting FDI and employment, spurring the growth of underdeveloped regions and the economic development of the area as a whole. The list of the main tax incentives offered by the zones in the Asia-Pacific Region encompasses corporate income tax holidays, reduced rates of corporate income tax, VAT exemption and other concessions.

China stands out among other countries of the Asia-Pacific Region thanks to its fast economic growth that many associate with industrial parks. Industrial parks were at their peak in 2002 when the country had 6,866 of them. However, in 2003, China launched a program to normalize land usage, and the number of industrial parks was cut drastically.

Tab. 5 presents an analysis of tax incentives offered by the main SEZ types of China: Economic and Technological Development Zones (ETDZs), High-tech Industrial Development Zones (HIDZs), Free Trade Zones (FTZs), Export processing zones (EPZs).

Tab. 5 Comparative analysis of preferential policies in China's main special economic zones

	ETDZs	HIDZs	FTZs	EPZs
Corporate Income Tax Rate (for foreign-invested production enterprises)	25%			
Corporate Income Tax Rate (for high-tech enterprises)	15%, for the high-tech industries encouraged by the nation			
Custom Duty and Value-Added Tax (VAT) (on self-use equipment and spare parts)	For the enterprises belonging to the category of encouraged industries, custom duty and VAT will be exempted.		Exempted	
Custom Duty and Value-Added Tax (VAT)	No exemptions		Exempted	

(on office appliances)			
Custom Duty and Value-Added Tax (VAT) (on raw materials and parts)	Only enterprises involved in the processing trade are exempted.	Exempted	
VAT rate	13% for agriculture-related projects 17% for others		
Tax on finished products using duty-free materials (sold domestically)	Levy on finished products	Levy on imported raw materials and parts only.	Levy on finished products.
VAT Refund for finished products made using domestic raw materials	VAT will be refunded following departure of shipment from China.		Immediate VAT refund for domestic raw materials upon entering the zone..

Source: (Chinaknowledge, 2017).

There is tough competition, in terms of tax incentives too, between Chinese SEZs that in Shanghai alone numbered 41 in 2016. In order to fight for businesses migrating between special economic territories, in 2000 some cities close to Shanghai announced an 'X+1' plan for policy support, meaning these cities offered one extra form of policy support in addition to the policy support offered by Shanghai. In response, Shanghai expanded the planning area of the Economic and Technological Development Zones (ETDZ) from 67 square kilometres to 173 square kilometres (ADB Asian, 2015).

Located in Shanghai, China's financial hub is the runner-up among all global free zones and is considered the best zone in Asia and East Asia. Waigaoqiao Free Trade Zone came in second in the fDi's Global Free Zones of the Year for 2016 (FDi, 2016). The zone is close to the Port of Shanghai, the world's largest port according to the World Shipping Council, offering investors a free trade regime and duty free and duty delaying options, exemption from customs duties on exports and imports (Ftz-shanghai, 2017).

Korean SEZs, too, have a sophisticated system of incentives. Tax concessions are offered to foreign invested resident firms and developers of such territories. The exemptions are different and are subject to certain investment requirements. These investment requirements vary across industries. The developers of free economic zones are entitled to corporate income tax exemptions. For example, developers get a 100 per cent exemption for the first three years and 50 percent for the next two years. The investment conditions are a foreign investment of over 30m dollars, or a foreign investment ratio of over 50 percent, and the total development project budget exceed 500m dollars. In the case of foreign invested domestic firms, a 100 percent corporate and income tax exemption is given for first three years and 50 percent exemption is given for the next two years. These exemptions are subject to a minimum investment requirement of 10m dollars in the case of

manufacturing, tourism or services industries; 5m dollars or more for logistics and medical institutions, and 1m dollars or more for R&D industries. Corporate and income tax exemptions can also be extended to seven years (100 percent for first five years, 50 percent for the next two years), if the investment amounts to 30m dollars million or more in manufacturing; 20m dollars million or more in the tourism industry; 10m dollars or more in logistics and 2m dollars or more in the R&D industry (Mukherjee, A. & Bhardwaj, B., 2016).

Conclusion

Over the past few decades there has been a trend towards the removal of nontax barriers: trade is being liberalized, capital becomes increasingly mobile, and business itself is changing. The change is due to the development of logistics and communications as fewer companies limit their production operation to the boundaries of one country only. Fiscal instruments have become an indispensable part of a package of measures for luring investors in SEZs. Each type of SEZs has its peculiar tax incentives that help to reach their specific goals. As a result of competition between the countries of the Asia-Pacific Region, they offer a nearly standardized range of tax incentives that tends to be further unified. These include corporate tax exemptions, duty free imports and exemption from foreign exchange controls. The most common taxation measures of support for investors are tax holidays or tax reliefs. Tax incentives have been playing an increasing role in investment decision making, leading to a bigger number of cross-border deals and spurring tax competition and the expansion of Duty Free and Duty Delaying regimes in the Asia-Pacific. More generous tax incentives, longer tax holidays for investment projects and the removal of nontax barriers facilitate trade liberalization and capital mobility in the Asia-Pacific Region.

Acknowledgments

The work was supported by the Humanitarian Scientific Foundation of the Russian Federation, contract № 17-22-21001.

References

ADB Asian (2015). *ADB Asian economic integration report 2015*. (2017, April). [online], Available at: <https://www.adb.org/sites/default/files/publication/177205/asian-economic-integration-report-2015.pdf>

Araki, S. & Claus, I. (2014). *A comparative analysis of tax administration in Asia and the Pacific*. Mandaluyong City, Philippines: Asian Development Bank, (2017, April). Retrieved from <https://www.adb.org/sites/default/files/publication/41792/tax-administration-asia-pacific.pdf>

Chinaknowledge, (2017). *Comparative analysis of preferential policies in China's main special economic zones*. Retrieved March 15, 2017, from <http://www.chinaknowledge.com/Manufacturing/Introduction.aspx?subchap=3&content=11>

EY (2014) *Second edition: Incentives in the ASEAN region 2014*. Ernst & Young. Manufacturing and Regional Corporate Support/Headquarter. (2017, April). Retrieved from [http://www.ey.com/Publication/vwLUAssets/Incentives_in_the_ASEAN_region_2014/\\$FILE/EY-asean-incentives-publication-2014.pdf](http://www.ey.com/Publication/vwLUAssets/Incentives_in_the_ASEAN_region_2014/$FILE/EY-asean-incentives-publication-2014.pdf)

FDi (2016). *fDi's Global Free Zones of the Year for 2016*. (2017, April). Retrieved from <http://www.fdiintelligence.com/Rankings/Global-Free-Zones-of-the-Year-2016>

Ftz-shanghai (2017) China (Shanghai) Free Trade Zone. (2017, April). Retrieved from http://www.ftz-shanghai.com/Biz-Setup-SHFTZ/Tax_Policy.html

IMF. (2016). *Regional economic outlook. Asia and Pacific. Building on Asia's Strengths during Turbulent Times*. Washington, D.C.: International Monetary Fund (2017, April). Retrieved from <http://www.imf.org/external/pubs/ft/reo/2016/apd/eng/pdf/areo0516.pdf>

Mukherjee, A. & Bhardwaj, B. (2016) *Imposition of MAT on SEZs: Concerns and the Way Forward*. Working Paper 314. Indian Council for research on international economic relations. (2017, February). Retrieved from http://icrier.org/pdf/Working_Paper_314.pdf

Sinenko, O. (2017). Methods of assessing of tax incentives effectiveness in special economic zones: An analytical overview. *Journal of Tax Reform*. 2016 Vol. 2, no. 3 p. 168-179.

Sinenko, O. & Mayburov, I. (2017). Comparative Analysis of the Effectiveness of Special Economic Zones and Their Influence on the Development of Territories. *International Journal of Economics and Financial Issues*. 2017. 7(1). p. 115. - 122.

UNIDO (2014). *Economic zones in ASEAN: Industrial parks, special economic zones, eco industrial parks, innovation districts as strategies for industrial competitiveness*. UNIDO country office in Viet Nam. (2016, August). Retrieved from https://www.unido.org/fileadmin/user_media_upgrade/Resources/Publications/UCO_Viet_Nam_Study_FINAL.pdf

Wiedemann, V. & Finke, K. (2015) *Taxing investments in the Asia-Pacific region: The importance of cross-border taxation and tax incentives*. ZEW. Discussion Papers, No. 15-014. (2017, February). Retrieved from <http://hdl.handle.net/10419/107420>

Zolt, Eric M. (2015). *Tax Incentives: Protecting the tax base. Paper for Workshop on Tax Incentives and Base Protection*. New York. United Nations. Department of Economic and Social Affairs. 23-24 (2017, April). Retrieved from http://www.un.org/esa/ffd/wp-content/uploads/2015/04/2015TIBP_PaperZolt.pdf

Contact

Olga Sinenko

Far Eastern Federal University, 690950, Vladivostok, Suhanova St. 8, Russia. E-mail:
sinenko.olga@gmail.com

Igor Mayburov

Ural Federal University named after the first President of Russia B.N.Yeltsin, 620002,
Ekaterinburg, Mira st. 19, Russia; Far Eastern Federal University, 690950, Vladivostok, Suhanova
St. 8, Russia.

mayburov.home@gmail.com