

**TAX INCENTIVES IN SELECTED ASIAN COUNTRIES:
A COMPARATIVE STUDY**

By

Parthasarathi Shome

and

Woo Sik Kee*

Introduction

Tax incentives to promote private investment has been a major feature of fiscal policy of many Asian developing countries. These incentives include tax holidays, deductions, credits, accelerated depreciation in computing taxable income and lowered customs duties on capital goods and raw material imports, and are utilized to serve a variety of objectives. This paper attempts a comparison of the principal tax incentive schemes in four Asian countries: Korea, Malaysia, the Philippines and Thailand, evaluates their relative merits and draws general conclusions on the advisability of such policies, bearing in mind that there is little agreement in the literature on their effectiveness [Lent (1967); Chen-Young (1967); Tanzi (1969); Harberger (1974); Bilsborrow and Porter (1972); Levy and Sarnat (1975)]. Section II studies the key industries in the economic development of the four Asian countries under consideration, setting a perspective for the intended analysis of tax incentives. Section III provides a comparison of the incentives legislation along two dimensions: the objectives and criteria of tax incentives, and the administrative mechanisms involved. Finally, Section IV attempts an evaluation of the incentive plans in the different countries.

Key Sectors in Economic Development

The general industrial policies followed by the four Asian countries have provided the context for their specific incentive schemes. A discussion of these policies, therefore, seems appropriate. The

*Assistant Professor of Economics, American University and Senior Economist, The World Bank, respectively.

specification of certain leading sectors as the 'engine of growth' and as the recipients of special tax treatment is a universal feature of the countries under study. These may be broadly classified into three groups as described below.

The first key sector is the *capital-intensive heavy industries* which are presumed to generate accelerated capital formation in the economy. Iron and steel, machinery, electronics, cement and chemical industries may be cited as common examples in this category. In Korea, capital-intensive heavy industries are systematically encouraged and capital formation has been one of the major goals of the Korean Five-Year Plans. Malaysia and Thailand are also shifting their prior emphasis solely on traditional, export-oriented industries towards engineering goods, chemicals and metals. The Philippines, which stresses almost all sectors and industries, also encourages industrial chemicals, machinery and capital equipment, electrical equipment, and metal products.¹

The second is the *export and import-substitution industries*, which help towards a balance in the international payments accounts of the countries, and are universally specified as key industries. In Korea, export-oriented mining and manufacturing are liberally encouraged as well as fisheries and the fishery-oriented ship-building industry. In Malaysia, until the 1960s non-agricultural income was mainly derived from the production and export of rubber and tin and expenditures related to these activities. Though Malaysia launched a planned economic development program in the mid-1960s, stressing manufacturing and engineering industries, the importance of the traditional export products towards the maintenance of its historic trade surplus has not diminished. During the 1960s. Thailand's industrial expansion was geared towards domestic production substituting the import of consumer goods such as textiles, food and beverages, and exports such as paper, rubber and basic metal. In the Philippines too, the industrial development strategy of the 1950s and the 1960s placed strong emphasis on import substitution, indeed, resulting in a

¹ Refer, for Korea: *Investment Opportunities in Korea*, Economic Planning Board, Republic of Korea, 1972; and *Investment Guideline*, Ministry of Commerce and Industry, Republic of Korea, 1973; for Malaysia: *Recent Economic Developments and Long-Term Issues*, World Bank Report, 1975; for Thailand: *Current Economic Position and Prospects of Thailand*, World Bank Report, 1974; and for the Philippines, G.P. Sicat, *Economic Policy and Philippine Development*, University of the Philippines Press, 1972; and *Current Economic Position and Prospects of the Philippines*, World Bank Report, 1973.

domestic market heavily protected by tariffs. The investment in these protected industries tapered off with the exhaustion of possibilities of easy import substitution, and export industries had to be identified. Thus from the late 1960s, several features of a new industrial policy evolved in this direction. Today, export production, export trades and service exports are all regarded as leading sectors.

The third consists of certain *traditional industries* which in each economy are specified as key industries. These sectors may have a historical comparative advantage in production; they may be the traditional export sectors, as well as a life-sustaining occupation for the rural masses utilizing local skills and resources. Examples of these industries are coconut related industries, bananas, pulp and paper in the Philippines; animal husbandry and agriculture in Thailand; fishery in Korea and rubber and agriculture in Malaysia, to name a few. These traditional occupations generally employ a significant proportion of the total working force of these economies. The government may specifically encourage such industries which are generally rural-based, in order to achieve a regionally balanced development.

One of the ways in which the governments encourage development of the important industries is to provide tax incentives, the role of which is the main focus of this study. The use of tax incentives may be simple and more or less similar over all key industries as in Korea, or it may involve a complex system of rules and regulations regarding tax exemptions, deductions and special allowances as in the Philippines.² Despite these differences, the basic purpose of development through industrialization, using lower effective tax burdens as an incentive remains true in all the countries. Section III discusses the objectives of the tax incentives adopted by these countries and the way they have been administered.

Comparative Analysis of Tax Incentive Laws

The major investment incentives of the different countries are embodied in their different statutes, as follows: (1) Investment Incentives Act (IIA) and Export Incentives Act (EIA) in the Philippines; (2) Foreign Capital Inducement Act (FIA) and Tax Exemption Control Law (TEC) in Korea; (3) Industrial Investment Act (IIA) in

²The Philippines annually identifies new industries according to national priorities with sometimes overlapping sections and subsections, each with a different incentive statute.

Malaysia; and (4) Investment Promotion Act (IPA) in Thailand. To evaluate their relative merits and to draw conclusions on the advisability of the tax policies embodied in these laws, we will divide this section into two, the first studying the incentive objectives and criteria, and the second studying how the administrative mechanisms of the incentives have affected their working, often giving rise to complex and perhaps unintended effects.

A. Major Objectives and Criteria:

In pursuance of the key sectors for economic development categorized in Section II, tax incentives are provided to (i) industries strategic to growth, or 'priority' sectors,³ (ii) export and import substitution industries, and (iii) certain traditional industries providing the mainstay for the development of backward areas as well as domestic participation (including employment generation, local resources use, domestic equity ownership, etc). Sometimes, incentive laws may also be written for related economic goals such as (iv) raising the overall rate of investment, for example, through foreign investment. In order to assess the working of these tax incentive schemes we provide a tabular comparison of the different tax incentive laws in the four countries on the basis of these broad classifications. Table 1 describes the tax incentives provided to the 'priority' sectors in the four countries; Table 2 does the same for foreign-exchange earning industries; Table 3 categorizes the remaining tax incentive provisions on the basis of other objectives and criteria. Comparisons of the actual performance and experience with these laws are available from Tables 4, 5 and 6 for the Philippines, Malaysia and Thailand respectively. Below we attempt an analysis by different objectives and criteria.

(i) *Industries strategic to growth i.e. 'priority' industries:* The promotion of certain key industries through tax incentives is common in all four countries under study. Table 1 provides a detailed comparison of the laws covering such industries; indeed, these industries may be discerned by the wide relief they receive with respect to tax payments. Table 5 shows that, in Malaysia, capital intensive engineering industries may receive as much as a seven year tax holiday. From available data similar instances may be drawn for Thailand

³ Priority sector industries may, of course, differ from country to country, as described in Table 1. For an insight into how tax incentives have affected the development of priority sectors in developing countries, see Herschel (1965).

and Korea. In the Philippines, however, several sectors appear to be encouraged simultaneously through the use of fiscal incentives precluding us from identifying any one key sector. Thus agricultural products, rural banking and cottage industries are all encouraged through the use of tax incentive laws in the Philippines. Between 1970 and 1972, the most substantial tax relief, in terms of revenues foregone, had been accorded to agro-industries (Table 4).⁴

(ii) *Export Industries*: Tax incentives are used to encourage export industries in all the countries under discussion. They are exempted from payment of the export tax, from the tariffs ordinarily levied on the import of capital goods and raw materials, as well as extended periods of tax holiday (Table 2). Since export and import substitution industries comprise a major key sector of development in the four countries as elaborated in Section II, liberal tax incentive laws for export industries are commensurate with such a policy. For the first objective of 'industries strategic to growth', as we saw above, there are, sometimes, unclear incentive policies regarding which sectors are being encouraged. Export industries, however, are universally encouraged through straightforward tax incentive statutes.

(iii) *Development of Backward Areas and Domestic Participation*: All the countries encourage regional development through tax incentives. The Philippines not only provides tax credits and rebates to manufacturing industries moving away from urban industrial areas (Table 3), but also encourages cottage industries located in rural areas through tax incentives. Malaysia too provides special incentives to enterprises operating in areas where industrial infrastructure is not yet available. Indeed, the proportion of new projects going to such 'Development Areas' has increased from 43 per cent in 1971 to 53 per cent in 1974 indicating that this policy has been successful in Malaysia. Table 3 clearly indicates how Korea and Thailand also try to develop backward areas through tax incentives. However, in Korea, the time discount (effective interest rates of 3% to 4% a month) is so high that a manufacturer may find it difficult to face a

⁴ One should note, however, that this is mostly due to the extremely high 1971 figure of P70.2 million for agro-industries. In 1972 it fell off to P19.6 million. On the other hand, the encouragement of the chemical and processing industries seems to have steadily increased while that of mining and engineering has decreased. All this points to the anomalous nature of the Philippine laws in terms of objectives. Further, though the number of reporting firms varies in the three years (1970-72), that should not effectively qualify these conclusions if one assumes an equal distribution of incentives to the different firms.

deficit in the early stages of production despite reduced tax rates (on a reduced profit) at a regional location when one considers the share of financial costs in total production cost.

Increasing domestic participation in local firms is becoming an important objective of tax incentive laws. In the Philippines, in order to qualify for tax incentives under the IIA, a firm must have 60% ownership by Philippine nationals. Similarly the Aliens in Business Act in Thailand increasingly stresses domestic participation. From Table 6, it can be seen that while qualified Thai firms increased from 22 to 47, i.e. more than doubled, between 1970 and 1973, joint ventures have increased by less than fifty percent. Similarly it may be noted that domestic registered capital has increased substantially while foreign capital has not increased significantly in the same time span. In Malaysia, 'Malaysian Content', interpreted as the total Malaysian labor, raw material, capital, etc. used, extends the period of tax holiday available to the qualified firm by an additional year. Only in Korea are considerations of domestic participation relatively unimportant.⁵

Local resource use and employment generation are other important objectives of the Philippine and Malay laws. In the case of the Philippines many of the tax incentives are based on local labor use. Special credits and depreciation allowances are also given for domestic capital use.⁶ In Malaysia, incentives are given to firms according to the total wages and salaries paid under the 'Labor Utilization Relief' scheme (Table 2). In Korea, however, while domestically produced capital equipment⁷ is granted higher depreciation rates than that allowed imported equipment, the overall emphasis on domestic resource use and employment generation seems low.

(iv) *Foreign Participation*: The encouragement of foreign participation through tax incentive laws is diminishing except in Korea

⁵ This may be due to historical preferences in Korea regarding foreign participation.

⁶ For example, in the case of imports, 200% deduction of shipping costs from taxable income is allowed if shipments are made in Philippine vessels and only 150% if foreign vessels are used. Also, registered export producers are allowed to deduct, from taxable income, an amount equal to their export revenue multiplied by a domestic labor and domestic raw material component.

⁷ The production of the equipment, however, may be in a foreign firm located in Korea.

where, under the Foreign Capital Inducement Law, blanket encouragement is provided to foreign investors, extending a 100% personal income tax to expatriate employees employed under this law. This aspect of Korean tax incentives may be interpreted as a reflection of political preferences for a significant foreign participation in Korea's foreign trade. On the other end of the scale is the Philippines, where the laws have stressed the Philippine content of any industry applying for preferential treatment. Although foreign investment is not discouraged, especially in the export industries, there seems to have been no systematic channel for encouraging foreign participation in the process of industrialization.

In Malaysia, as in the Philippines, no law has been enacted for the express purpose of inducing foreign investment. Yet, foreign companies have predominated over Malaysian companies in the government-encouraged manufacturing sector. Foreign investors from many developed countries⁸ have successfully operated in pioneer industries, with the Malaysians holding less than half (47%) of the total equity in 1973. Malaysia, as compared to other countries, has maintained a stable attitude towards foreign investment which has not changed from regime to regime. Malaysia also has abundant raw materials (rubber, tin). These favourable circumstances seem to have created a congenial atmosphere for foreign investors in Malaysia, despite the absence of any laws explicitly encouraging foreign investment. Malaysia's approach towards tax incentives has to be distinguished from Korea's. In Korea, the encouragement of foreign investment seems to have been an end in itself, with encouragement of industries not only regarded as helping the balance of payments but also 'social welfare'. In Malaysia, such incentives are carefully oriented towards the establishment of 'pioneer' industries. Also within the Malaysian framework, increases in Malaysian shareholding are encouraged and only industries with 100% export orientation may be entirely foreign owned.

In Thailand, while foreign investment has played an important role historically, the recent Aliens in Business Act (1972) has tried to shift this emphasis towards encouraging domestic content. It may be seen from Table 6 that purely foreign 'promoted' firms are negligible in number (two in 1970, one in 1973), and, as mentioned above, foreign capital has not increased significantly.⁹ Foreign investment is

⁸ The U.S.A., Britain and Japan predominate the foreign ventures in Malaysia.

⁹ This may not be a result solely of the recent laws. The reason for the slight increase in foreign capital may be due to extra-economic reasons such as the

encouraged only in areas where foreign expertise and finance are especially required.¹⁰

B. Administration of Tax Incentives:¹¹

The administrative requirements of particular tax incentives schemes often have an important bearing on their effectiveness. The administrative system may vary from a strict codification of incentives for specific industries and individual firms, as in the Philippines, to a wide discretionary system with the decision power lying with a government agency as in Thailand. An advantage of the discretionary system is that each investment project can be evaluated on its own merits and economic benefits may be weighed against revenue loss. This approach, however, requires a high degree of administrative competence, and may give rise to corruption. Some of these administrative difficulties can be avoided by a non-discretionary approach. However, this approach has also some shortcomings in that, unless the scope of benefits is limited, it may involve substantially larger revenue losses compared to the discretionary approach; also the non-discretionary approach has been known to be rather cumbersome to operate, involving high administrative costs.

In the Philippines, where the legislation regarding tax incentives is the most complex, the BOI prepares an annual Investment Priorities Plan which contains a list of 'eligible' industries, within which 'pioneer' and 'non-pioneer' categories are distinguished. Also a list of 'over-crowded' industries is prepared, in which the government discourages incentives and disallows foreign exchange for necessary imports. No clear industrial policy seems to have emerged out of the constant modification of policies. Thus from Table 1 one can discern the anomalous nature of incentives provided in any sector over time: engineering industries have fluctuated from P14.6 million in 1970 to P20.8 million in 1971 to P3.7 million in 1972. Mineral processing has

overall secular decline in net foreign capital in certain groups of developing countries, the recent political changes in Thailand, etc.

¹⁰ For a comprehensive study of the extent to which domestic tax laws affect foreign investment, see Yair Aharoni, *The Foreign Investment Decision Process*, (Boston: 1966).

¹¹ The government authorities responsible for administering tax incentives are the Board of Investment (BOI) in the Philippines; the Office of Investment Promotion (OIP) in Korea; the Federal Industrial Development Authority (FIDA) in Malaysia; and the Board of Investment (BOI) in Thailand.

steadily declined whereas chemicals have received increased incentives. It is not possible to discern, under such circumstances, what the BOI goals are.¹² Even if the goal is towards balanced development, some clarity regarding the exact process is called for so that private investors may be assured of priorities. The long annual list of 'preferred' and 'pioneer' industries may in fact be a reflection of the lack of such an overall plan. Though it is generally suggested that countries without an efficient and experienced administrative machinery are better off if they adhere to a non-discretionary system so that important decisions need not be left in the hands of immature bureaucrats, the Philippines seems to be an example of a case trying to correct this unwanted possibility by an extreme measure of non-discretion, resulting in a highly cumbersome set of rules and regulations.

The other extreme is that of Thailand where the tax incentive laws are overly simplistic, and most of the decisions are left in the hands of the BOI. The definition of a 'promoted' industry, for example, has remained too broad. The time period of which incentives are granted may also remain unspecified in several cases. The expediency with which decisions have been made by the BOI is especially questionable since it has done hardly enough research on the infrastructure needed for the growth of an industry on its future market demand. The granting of incentives on the sole basis of discretion¹³ by an agency which has little experience and information in the specified areas may be equally suboptimal.

Korea and Malaysia seem to have operated more efficiently. Their administrative mechanisms clearly lay out the sectors to be encouraged, discretion for certain decisions lying with the Economic Planning Board in Korea and FIDA in Malaysia. The FIDA also undertakes research and provides information regarding the domestic investment infrastructure for potential investors. It issues annual reports on the tax incentive schemes as well as new objectives and criteria. It provides advisory assistance to industrial ventures in plan-

¹² The anomalous nature of the administration is also reflected through how the use of the different instruments of tax incentives has fluctuated between 1970-72 (Table 4).

¹³ At least, with all the cumbersomeness of the Philippine BOI's set of rules and regulations, it is primarily a 'one-window system' so that all applicants can directly be channelled through one agency. In Thailand, even this is unclear and several ministries are involved in the decision process.

ning and coordination, lacking in the Thai administration. It studies projects, holds national and international seminars and undertakes research in order to recommend policies. However, in contrast with the Philippines BOI, the FIDA does not issue such detailed annual lists demarcating 'preferred', 'pioneer' and 'export' areas to be encouraged with different intensities (under distinct Lists A and B) according to priorities. This makes the FIDA operate more on a discretionary basis. The contrasting complications of the Philippine BOI is exemplified by the overlapping of industries under both IIA and EIA, without any clear indication as to whether the incentives provided under them are additive.

Korea utilizes a 'one-window' system and encourages foreign investment, its clear objective, with little bureaucratic red tape and swift efficiency. The decision making process reduces much of the administrative burden on investors. An optimal combination of discretion and rules for the administration of tax incentive schemes as in Korea and Malaysia thus seems to have worked the best. Complete reliance on rules, as in the Philippines, may defeat the purpose of not requiring an experienced administration, while total reliance on discretion, such as in Thailand, may result in inefficiency and corruption.

Appraisal of Tax Incentives

One of the main questions cited regarding the effectiveness of tax incentives is whether investment actually does rise because of them. The net effect of tax incentives on investment is difficult to surmise. In a nutshell, as a result of tax incentives, the IS curve of the familiar Keynesian analysis must shift to the right, thereby raising both income as well as rate of interest. These have conflicting effects on the demand for investment¹⁴ so that theoretically it is even possible that investment falls in the net as a result of tax incentives. Several attempts at empirical work on this issue, with respect to the U.S.¹⁵ have yielded startlingly different results. To quote Harberger (1974, page 195):

¹⁴ As long as $\frac{\partial I}{\partial r}$ and $\frac{\partial I}{\partial Y}$ are of opposite signs, where I is investment, r is rate of interest, and Y is income.

¹⁵ Cf. Harberger (1974) pp. 193-205, for a concise discussion of some of these papers by Klein and Taubman, Hall and Jorgenson, Bischoff, Coen etc. appearing in G. Fromm edited, *Tax Incentives and Capital Spending*, The Brookings Institution, (Washington D.C.: 1971).

. . . I cannot help reflecting on the disparities of the results emerging from the four treatments of the relation of tax incentives to investment behaviour. It is naive to expect there to be only one way in which economic science can be brought intelligently to bear upon a given set of data to answer a given question. Several models, each soundly based, may still have differing implications, because theory has yet to achieve — if, indeed, it ever will — a unique set of propositions on which all professional economists agree. And where divergent theories are tested on a given body of data, the data might not be sufficiently extensive or robust to show that one approach is superior to another.

Some other approaches, for example Tanzi (1969), have interpreted the change in investment in an incentive-receiving industry as the sole result of that incentive. This is clearly questionable since a change in investment may not be the result of that incentive alone, but a multiplicity of other factors. The limitation of data, therefore, severely constrains any meaningful analysis in this area. The shortcoming may be the very nature of the calculations involved, based on introspective concepts regarding time discount rates, social welfare functions, etc. which have to therefore be arbitrarily chosen. The countries under study in this paper do not even allow us to attempt any single meaningful empirical investigation, let alone choose among alternatives. However, from the experiences of the different countries, it is possible to note some general features and their implications for reform.

It is not easy to comment on the secular importance of tax incentives. In the Philippines, for example, where tax incentives are granted to almost all sectors, the amount of incentives has fluctuated over time: P83.3 million in 1970, P130.4 million in 1971, P70.6 million in 1972 (Table 4). In Malaysia, taking the number of firms receiving incentives as an index, the importance of tax incentives has declined while the number of firms with incentives there has decreased from 207 in 1970 to 169 in 1974, those without incentives increased from 127 to 196 (Table 5). These figures raise the question of the importance of incentives. It is quite possible, for example, that Malaysia's naturally congenial investment climate^{1 6} brings forward investment capital, without much dependence on the scheme of tax incentives. This may be the cause of the reduction of the number of firms choosing to apply for incentives in Malaysia. On the other hand, in Thailand, the number of 'promoted' firms receiving incentives has increased from 54 in 1970 to 97 in 1973 (Table 6). Thus the importance of tax incentives seems to have increased in Thailand.

Similarly, Korean tax incentives may have attracted foreign investment, helping to create a viable investment climate. Thus the importance of the use of tax incentives seems to have varied from country to country.

Unless the entire incentive program is carefully worked out with all the different objectives in mind, the incentives may be administered in such a way that the objectives may conflict, reducing their effectiveness. For example, in Malaysia, while employment generation is an important objective, so is capital investment. This gives rise to a conflict in the chosen factor-intensities in industry. The years of tax holiday given on the basis of capital investment and labor utilization cover the same range: therefore, the government's policy goal regarding factor-intensities remains unclear. In Korea, the clear emphasis in the tax incentive legislation is on the heavy industries. However, the aggregate investment objectives may be faster realized if a traditional sector such as textiles is encouraged more, provided that the comparative advantage in production lies here.¹⁶ Thus the objectives of encouraging heavy industries specifically may pose a potential conflict with that of overall industrialization. It is, therefore, necessary to recognize and to resolve these conflicts.

Again, in the Philippines, while employment generation, or labor intensity in production, seems to be a clear criterion in most tax incentive legislation, the government's policy of a high exchange rate with a low interest rate has contributed to relatively low cost of capital and indeed, a capital bias in factor intensities. To encourage employment, the Philippines BOI has imposed a new condition on selected industries included in the IPP. This condition specifically requires that a new project should generate at least one job for a given value (\$4000) of imported capital equipment. However, the criterion is too simplistic and rather arbitrary. Such uniform requirement in a variety of industries with different capital-labor ratios is not very efficient. In order to be effective, the requirement should be more refined, for example, the above link should depend on the particular industry.

It is also important, however, that in designing tax incentives, the purposes of individual objectives be kept in mind. An incentive

¹⁶This argument is being put forward only on a theoretical level. In practice this would not be sensible, given the high tariffs this industry has faced historically and continues to face from most developed economies.

should be as directly related to its objective as possible. Otherwise it may turn out to be an inefficient means of achieving the intended objective. If, for example, the objective is to increase exports, the incentive scheme should be based on the net value of the exports, accounting for the imported equipment used in its production. If the objective is to increase output of selected industries, the incentive should be based on the value of output instead of investment in those industries. Sometimes, however, if the objectives themselves are inherently conflicting, then the selection of incentives for specific objectives may not be the optimum solution. Finally, given that foreign investment is an objective, it seems to be increasingly agreed that the overall investment climate is extremely important in order to attract the foreign investor. If a congenial investment climate is lacking, blanket incentives may be necessary even though they may not fully compensate for an unfavorable investment climate.

Conclusion

Tax incentive laws in the Asian countries under study viz. the Philippines, Malaysia, Thailand and Korea, have been enacted primarily to encourage certain key sectors in economic development: heavy industries, foreign exchange earning industries and certain traditional industries which promote local skills and participation, employment, domestic resource use, etc.. Only Korea seems to have encouraged foreign investment unilaterally to raise the overall rate of investment in the economy.

In the area of administration of tax incentive statutes, Thailand has used an extremely loose, discretionary policy which may not have worked well, especially in a country where an experienced bureaucracy in this area is yet unestablished. The other extreme cumbersome method, based on minutely detailed lists of industries and corresponding regulations, has been pursued in the Philippines. Malaysia, on the other hand, has followed an innovative method of administration based on an optimal mix of discretion and rules. If increasing investment is a criterion, Korea too seems to have performed with efficiency.

An appraisal of incentive schemes is difficult since it is difficult to measure the effects of these incentives in isolation. From the experiences of these countries, however, it seems that general economic environment may be an important factor in determining investment, rather than tax incentives alone. For example, in spite of a lack of special incentives for foreign investment, Malaysia has drawn it

abundantly. Similarly, one may question whether Korea might not have attracted foreign investment given the congenial labor environment, even in the absence of such liberal foreign investment inducement laws it has enacted. Inasmuch as these laws will continue to be enacted, however, it is important that the whole set of laws is consistent and not conflicting with different objectives for the overall development plan of the country.

Table 1
Tax Incentives for Priority Sectors*

Country	Philippines	Korea	Malaysia	Thailand
Type of Incentive				
	<i>Preferred</i> (demand exists, not supply); <i>Pioneer</i> (demand and supply must both be generated)	<i>Key</i> (government determined)	<i>Pioneer</i> (exports; also socially desired goods not already produced on commercial	<i>Promoted</i> (development oriented industries based on decisions by the Board of Investment)
Tax Holidays	All taxes, except <i>cit</i> are exempt on a diminishing basis up to 1981; loss carry forward to a maximum of 10 years	All taxes: <i>cit</i> ; <i>it</i> on unincorporated units; <i>dit</i> ; <i>pt</i> ; <i>pat</i> -for 5 years plus 50% reduction for 3 additional years	5-10 years based on investment, location and employment: <i>cit</i> , <i>dit</i> , <i>dt</i> (2-8 years); indefinite loss carry-over	3-8 years plus 50% reduction for 5 more years; includes <i>bt</i> , <i>cit</i> .
Deductions	Organizational and pre-operating costs from taxable income	Does not apply due to exemptions	Does not apply due to exemptions	25% of installation costs from net profits
Tax Credit:				
(i) Equipment	100% on domestic and imported equipment; penalty of twice the credit for unauthorized resales	100% on domestic and imported equipment; no penalty law	Post-exemption period: 25-40% of capital expenses incurred during exemption period	100% exemption of <i>bt</i> on equipment
(ii) Interest Payments	Conditionally, on foreign loan interest	Full exemption from tax on interest on foreign loans	Information unavailable	Information unavailable
Accelerated Depreciation	Allowed to a maximum of twice the usual rate of 20%	Domestic equipment may receive up to 4 times usual rate	Conditionally available	Conditionally available
Tariffs on Machinery and Raw Materials	<i>cd</i> exemption on machinery locally not available; not so for raw materials	<i>cd</i> exemption on 'capital goods' interpreted to include raw materials	<i>cd</i> exemption on raw materials and machinery not available locally	<i>cd</i> exemption on raw materials and machinery not available locally

*Abbreviations used for different taxes:

it = income tax

cit = corporation income tax

dit = dividend income tax

bt = business tax

dt = development tax

pt = property tax

pat = property acquisition tax

cd = customs duty

et = export tax

SOURCES:

1. *Guide to Investment in Korea*, Economic Planning Board, Republic of Korea, 1975.
2. *An Outline of Korean Taxes*, Tax System Bureau, Ministry of Finance, Republic of Korea, 1972.
3. *Investment Opportunities in Korea*, Economic Planning Board, Republic of Korea, 1972.
4. *An Appraisal of Major Tax Incentive Laws in the Philippines*, Technical Staff-Joint Legislative-Executive Tax Commission, Manila, 1971.
5. *Comparison of Tax and Other Incentives Before and During Martial Law*, National Economic and Development Authority of the Philippines, National Tax Research Center, Manila, August 1974.
6. *A Summary of Investment Incentives*, Federal Industrial Development Authority of Malaysia, 1973.
7. *Annual Reports*, FIDA of Malaysia.
8. *Summary of Investment Incentives*, Board of Investment of Thailand, February 1973.

Tax Incentives for Export Industries

Type of Incentive	Country	Philippines	Korea	Malaysia	Thailand
		Export Incentives Act does not specify whether the following incentives are additive	All foreign exchange earning industries are defined within 'key' sectors; the following are additional incentives	All export industries are included in the 'pioneer' category; the following incentives are additional	All export areas are not 'promoted'. Following incentives related to exports (promoted as well as traditional exports)
Tax Holidays		<i>et</i> exemption if revenues exceed U.S. \$5 million within 5 years from the registration	<i>bt</i> exemption	4-7 years holiday for capital investments (instead of usual 2-5 years for pioneer industries)	Exemption from <i>bt</i> and <i>et</i> on exportation of manufactures
Deductions		<i>it</i> base reduced by a certain portion of export revenue, based also on domestic content	Not applicable due to total exemptions	Expenses such as foreign advertising, export market research, transport costs deductible from tax base	Not available
Tax Credit		Export producers: tax credit equivalent to the sales, compensating and specific taxes and raw material duties	50% for <i>it</i> and <i>cit</i>	Not available	7/8 of <i>et</i> on raw materials
Accelerated Depreciation		Same as in Priority Sectors	Same as in Priority Sectors	Additional 40% of the residual value of capital assets	Same as in Priority Sectors

SOURCES: Refer Table 1.

Table 3
Other Major Tax Incentives

Type of Incentive	Country	Philippines	Korea	Malaysia	Thailand
Development of Backward Areas		Rural-based agro-industries, mineral products, salt and fish exempt from sales tax indefinitely; reduced sales tax on local export industries and cottage industries	Full exemption of <i>pit</i> and <i>pat</i> within local Industry Inducing Area; three year exemption of <i>it</i> and <i>cit</i>	Development Area enterprises receive one year additional exemption	Promoted firms in Industrial Promotion Areas receive 50% <i>cit</i> reduction, 25% investme allowance of cost of installation, 90% reduction of <i>bt</i> on sales and 50% of <i>cd</i> and <i>bt</i> on imported raw materials for 5 years
Domestic Resource Use and Foreign Participation		'Philippinization' and employment constitute important components of tax deduction calculations	Domestic equipment gets 4 times usual depreciation allowance; very easy treatment of foreigners, for example, 100% exemption of <i>it</i> for expatriate employees	'Malay Content' is incorporated in several deduction calculations; Labor Utilization Relief allows maximum of 5 years exemption from taxes to firms with a minimum number of employees	'Aliens in Business' Act (1972) groups industries according to the extent of foreign participation allowed, thereby stressing Thai participation

SOURCES: Refer Table 1.

Table 4

Distribution of Incentives for Registered Projects in Philippines (Million Pesos)

	1970	1971	1972	1970-72
Total Amount of Incentives	83.3	130.4	70.6	284.3
(i) Sector-wise Distribution				
Engineering Industries	14.6	20.8	3.7	39.1
Chemical and Processing	6.0	9.6	34.9	50.5
Mining and Mineral Processing	43.1	29.7	12.4	85.2
Agro-Industries	19.6	70.2	19.6	109.4
(ii) Incentive Type-wise Distribution ^{1/}				
Income tax deductions ^{2/}	49.4	50.6	14.8	114.8
Tax Credit ^{2/}	2.0	4.4	0.2	6.6
Customs Duties & Compensating Taxes ^{4/}	20.0	73.3	51.1	144.4
Sales tax (Pioneer Industries)	12.3	2.1	4.5	18.9

^{1/}The 1970 figures are for 75 reporting firms, 1971 for 105, 1972 for 70.

^{2/}Based on 35% tax rate assumption; includes reinvestment allowance, accelerated depreciation, net capital loss carryover, pre-operating expenses, and double deduction of shipping costs and promotional expenses.

^{3/}Includes tax credits for the purchase of domestically produced equipment, for exported finished products, and interest withheld on foreign loans.

^{4/}Includes customs duties on imported equipment as well as compensating tax on imported equipment and raw materials.

Source: BOI, Statistical appendix to the Fourth, Fifth and Sixth IPP.

Table 5

Distribution of Incentives for Approved Firms in Malaysia

(i) Number of Firms	1970	1971	1972	1973	1974 ^{1/}
Firms with Incentives	207	190	186	237	169
Pioneer	173	150	158	179	125
Labor Utilization Relief	—	—	9	17	15
Investment Tax Credit	31	22	10	26	26
Other Incentives ^{3/}	3	18	9	15	3
Firms without Incentives	127	115	169	236	196
(ii) Number of Years of Tax Holiday					
Capital Investment ^{2/}	2-5 years				
Export Industries ^{2/}	4-7 years				
Development Area	1 year				
Malaysian Content	1 year				
Labor Utilization Relief ^{4/}	2-5 years				

^{1/}Includes number of firms approved during January through August.

^{2/}Includes accelerated depreciation allowance, industrial building allowance, abatement of chargeable income, and increased capital allowance.

^{3/}The exact number depends on the amount of capital investment.

^{4/}Depends on the number of employees.

Source: Ministry of Trade and Industry; and FIDA, Annual Reports for the various years.

Table 6

Basic Statistics of Promoted Investments in Thailand

Item	1970	1971	1972	1973
Total Number of Certificates	79	59	70	115
Total Number of Promoted Firms	54	50	61	97
Thai Firms	22	30	33	47
Foreign Firms	2	—	—	1
Joint Ventures	30	20	28	49
Total Registered Capital	902.1	457.0	1,007.9	1,284.0
Thai (B.000,000)	615.0	320.9	772.3	988.4
Foreign (B.000,000)	287.1	136.1	235.6	295.6
Total Investment				
(B.000,000)	2,726.1	779.1	4,078.7	7,764.6
Machinery and Equipment				
(B.000,000)	1,511.6	449.4	2,444.4	2,486.6
Estimated number of Thai Employees	16,590	12,079	19,719	21,640

Source: Office of the Board of Investment, Research Division.

REFERENCES

- Aharoni, Y., *The Foreign Investment Decision Process*, Little, Brown. (Boston:) 1966
- Bilsborrow, R.E. and R.C. Porter, "The Effects of Tax Exemption on Investment by Industrial Firms in Columbia," *Weltwirtschaftliches Archiv*, June, pp. 396-426.
- Fromm, G., edited, *Tax Incentives and Capital Spending*, The Brookings Institution (Washington D.C.) 1971
- Herschel, F.J., "Comment on N. Kaldor, 'The Role of Taxation in Economic Development,'" in *Fiscal Policy for Economic Growth in Latin America*, Johns Hopkins Press (Baltimore).
- Harberger, A.C., *Taxation and Welfare*, Little, Brown and Co., (Boston), pp. 1974 193-205.
- Lent, G.E., "Tax Incentives for Investment in Developing Countries," *IMF Staff Papers*, July, pp. 249-323.
- Levy, H. and M. Sarnat, "Investment Incentives and the Allocation of Resources," *Economic Development and Cultural Change*, April, pp. 1975 431-451.
- Tanzi, V., "Tax Incentives and Economic Development: The Ecuadorian Experience," *Finanzarchiv*, March, pp. 1969 226-235.