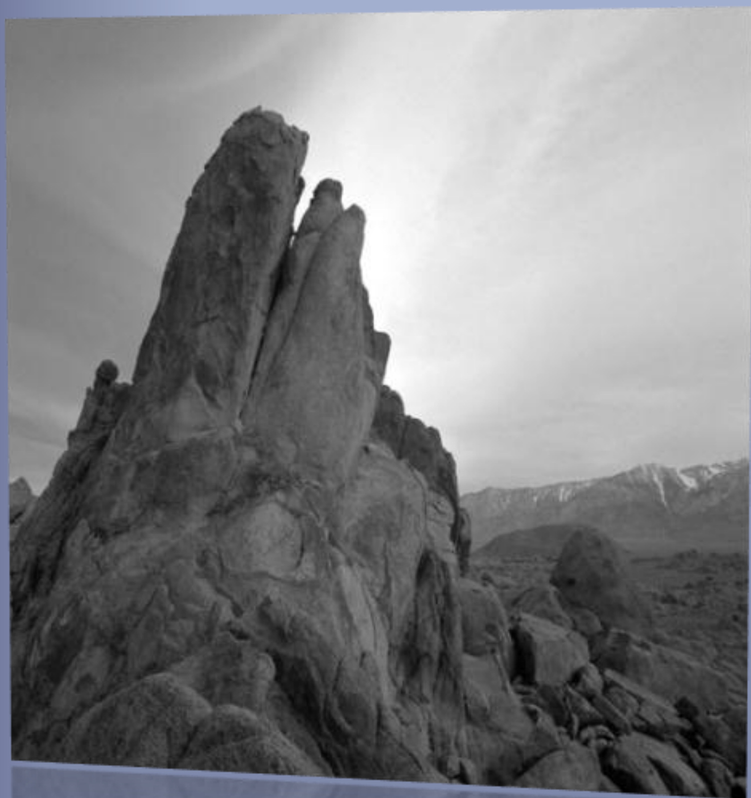

TAX INCENTIVES FOR PUBLIC-PRIVATE PARTNERSHIPS

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Contents

1. Executive Summary

This report was prepared by Michael Curran of the RMIT School of Accounting for the APEC Business Advisory Council. It presents the findings of a desktop research study of tax incentives used by a selection of APEC member countries to encourage the use of Public-Private Partnerships to develop social infrastructure projects.

1.1. Purpose of this Report

It is not the object of this report to provide a detailed analysis of tax incentives used by all APEC member countries to encourage infrastructure development. Instead, the report concentrates on summarizing the tax incentives used by a select number of APEC countries that have made use of Public-Private Partnerships. It is designed to act as a catalyst to stimulate discussion and provide an overview of incentives that countries in the APEC Region may wish to consider if they are using Public-Private Partnerships for infrastructure development. The countries this report concentrates on are Australia, Korea, Indonesia, Thailand, Malaysia, Singapore, the Philippines and Vietnam. An analysis of the tax incentives in these countries has found that there is a diverse range of incentives that have been used to encourage infrastructure development.

The types of tax incentives used to encourage Public-Private Partnerships vary from one jurisdiction to another. Some countries such as Singapore and Malaysia have a very broad based range of tax incentives designed to promote investment across a wide range of industries. Nonetheless, some of these incentives are applicable to Public-Private Partnerships. For instance Malaysia incorporates a broad range of incentives in the *Promotion of Investment Act*[1]. Singapore offers a wide range of incentives in the *Income Tax Act* and the *Economic Expansion Incentives (Relief from Income Tax Act)*[2].

[1] http://www.treasury.gov.my/index.php?option=com_content&view=article&id=279%3Apromotion-of-investment-act-1986&catid=92%3Acatinsentif-cukaiundang-undang&Itemid=200&lang=en (last viewed 27/02/2013)

[2] http://statutes.agc.gov.sg/aol/home.w3p (last viewed 27/02/2013)

This approach can be compared with the legislation that has been enacted in countries such as Vietnam, Korea and the Philippines which is specifically designed to encourage and support infrastructure investment through Public-Private Partnerships. For instance, Korea has enacted *The Act of Private Participation in Infrastructure*[3]*.* The Korean Government has also provided infrastructure tax incentives in *The Special Tax Treatment Control Act (National Tax)*[4].

[3] Korean Government (Ministry of Government Legislation, Centre for national legislation information) 2012, *The Act on Private Participation in Infrastructure*, (last viewed 10.Sep. 2012), <http://www.law.go.kr/LSW/lsSc.do?mouseY=436&menuId=0&p1=&subMenu=1&searchChk=2&lawSearchName=LicLs%2C0&query=%EC%82%AC%ED%9A%8C%EA%B8%B0%EB%B0%98%EC%8B%9C%EC%84%A4%EC%97%90+%EB%8C%80%ED%95%9C&x=22&y=9#liBgcolor0>, **[saved in Korean – 사회간접시설에 대한 민간투자법],**

[4] Korean Government, (Ministry of Government Legislation, Centre for national legislation information) 2012, *Special Tax Treatment Control Act,(*last viewed 10.Sep. 2012), <http://www.law.go.kr/engLsSc.do?menuId=0&subMenu=5&query=%EC%A1%B0%EC%84%B8%ED%8A%B9%EB%A1%80%EC%A0%9C%ED%95%9C%EB%B2%95#liBgcolor0>, **[saved in English – Special Tax Treatment Control Act],**

2. Methodology

In 2011 APEC ministers identified the use of Public-Private Partnership infrastructure development as an important area of interest.

This report documents the outcome of a desktop research study of a number of selected Asian countries with the view of summarizing the more common types of tax incentives used to encourage the use of Public-Private Partnership infrastructure development. Most countries offer a range of tax incentives. However, this report concentrates on summarizing the more common types of incentives that are applicable to infrastructure development in the countries that were examined.

A summary of the tax incentive has been provided together with examples of countries using that particular incentive.

3. Summary of Main Findings

This study found that the most common tax incentives used to encourage infrastructure development in Australia, Indonesia, Korea, Malaysia, Singapore, the Philippines, Thailand and Vietnam were as follows:

- **Tax Holidays**
- **Reduced Corporate Tax rates**
- **Accelerated Depreciation, Investment Allowances and Infrastructure Allowances**
- **Location Based Incentives**
- **Reduced Taxes on Interest and Dividends**
- **Reduced Withholding Tax**
- **Carry Forward Loss Provisions**
- **Additional Deductions for Qualifying Expenses**
- **Reduction of Indirect Taxes**
- **Other Ancillary Incentives**

4. Overview of Public-Private Partnerships

The use of Public-Private Partnerships to develop infrastructure projects has grown significantly over the last few decades. One of the key arguments for the use of Public-Private Partnership is that they reduce the burden on taxpayers by introducing private capital, private expertise and competitive business practices to the provision of public services.[5] They provide the provision of public goods and services at lower cost and lower risk to government.

The main feature of the Public-Private Partnership is that the public partner does not own the infrastructure at the beginning of the agreement but buys it over time from the private partner or leases it for the duration of the agreement. The most common types of Public-Private Partnerships are:

- **Build – Own – Operate (BOO)** - here the private sector bills, owns and operates a facility deriving income through user charges
- **Buy – Build – Operate (BBO)** - here the private sector buys an existing public facility, renovates it and derives income through user charges
- **Build – Own – Operate** – **Transfer (BOOT)** - here the facility is transferred to the public sector at the end of a predetermined period
- **Build – Transfer – Operate (BTO)** - here the private sector builds the asset and transfers legal ownership to the state. The asset is then leased back to the private sector which operates the asset, deriving income by charging a fee.[6] The success of Public-Private Partnership projects depends on the ability of government agencies to identify, plan and manage these projects. In order to enhance the success of Public-Private Partnerships some governments in the APEC region have created

[5] Adams J, Young A and Zhihong W (2006) *Public Private Partnerships in China -Systems, Constraints and Future Prospects*, International Journal of Public Sector Management, Vol. 19, No 4, 2006, p. 385

[6] Lehman G Tregoning I, *Public – Private Partnerships, Taxation and a Civil Society*, The Journal of Corporate Citizenship, Autumn 2004, p.78

dedicated Public-Private Partnership bodies to assemble the skills necessary to assist in developing successful Public-Private Partnership infrastructure projects

As an example, the Government of the Philippines has adopted a policy of encouraging private sector participation in infrastructure development. *The Build – Operate – Transfer (BOT) Law (Republic Act No 6957) of 1991* as amended by *Republic Act (Number 7718 of 1994)* sets out the policy and regulatory framework for private sector participation in infrastructure projects. A government agency, the BOT Centre, was established to manage and coordinate the implementation of the BOT. [7] The BOT Centre has now been renamed as the Public Private Partnership Centre (PPP Centre).

In the Republic of Korea the government enacted the *Act on Private Participation Infrastructure 1999* (as amended). This was designed to attract investment in infrastructure projects.[8]

In Indonesia the government has established the Directorate of PPP Development.

[7] Quium A, *Private Sector Participation in the Transportation Sector: Trends, Issues and Institutions in the Asia-Pacific Region*, Transport and Communication Bulletin Asia and the Pacific, No.72, 2003, p.20

[8] Ibid at p.21

5. Infrastructure Tax Incentives – General Overview of Selected APEC Countries

5.1. Indonesia

The Indonesian government has a policy on Public-Private Partnerships as part of its five-year national development plan 2010 – 2014. It is intended to streamline the Public-Private Partnership process. In September 2011, the deputy national planning Minister identified total infrastructure needs in the 2010 to 2014 period at $225 billion, half of which will be funded by the state budget, with the remainder coming from state owned enterprises and the private sector through Public-Private Partnership Schemes.[9] No single leading agency exists in Indonesia for Public-Private Partnership projects. However, a number of institutions closely collaborate for Public-Private Partnership development. One such unit is the Public-Private Partnership central unit which provides guidance for project preparation, procurement and project implementation.[10]

The Ministry of Economic Affairs has published a Public-Private Partnership investor's guide, which states that the government will assist with land acquisition and tariff reduction in certain circumstances.[11]

The Coordinating Minister for Economic Affairs has announced that tax incentives for infrastructure projects will be similar to those in manufacturing in the form of tax holidays and tax allowances.[12]

In May 2011, President Yudhoyono announced *the Master Plan for the Acceleration Expansion of Indonesian Economic Development 2011 – 2025*. Public-Private

[9] http://www.nortonrose.com/news/56717/looking-east-investment-in-indonesia (last viewed 27/02/2013)

[10] EAIC Advisory - Economic Research Institute for ASEAN and East Asia(ERIA) –*PPP Country Profile for Indonesia*

[11] http://www.bi.go.id/NR/rdonlyres/3112CCDF-1B05-413F-BE01-89C4D47A1212/20232/PPPinvestorguide.pdf (last viewed 01/10/2012)

[12] http://www.indii.co.id/news_daily_detail.php?id=4644 (last viewed 01/10/2012)

Partnerships are expected to play an important part in infrastructure development of Indonesia.[13]

The Income Tax Law provides various incentives to encourage companies to invest in certain qualifying business sectors and or regions.[14] The main concessions are:

- a 30% investment allowance
- accelerated depreciation of fixed assets (twice as fast as the normal rate)
- longer tax loss carry forward period (extended from five years to ten years)
- a reduction of withholding tax on dividends paid to foreign shareholders from 20% to 10%
- tax holidays - In August 2011, the government announced tax holidays should be provided to firms in Pioneer Industries which have a wide range of connections, provide additional value and high externalities, introduce new technologies and have strategic value for the national economy. Eligible taxpayers may enjoy an income tax exemption for a period of five to ten years from the start of commercial production. At the end of the tax holiday period, the tax payers are given a 50% income tax reduction for a further period of two years.

[13] EAIC Advisory - Economic Research Institute for ASEAN and East Asia(ERIA) –*PPP Country Profile for Indonesia*

[14] PWC, *The Report Indonesia 2012*, p.286

5.2. Malaysia and Singapore

Malaysia

Malaysia has established the Public-Private Partnership unit within the Prime Minister's Department. This unit is responsible for coordinating and executing Public-Private Partnership projects.

Malaysia has traditionally offered a wide range of investment incentives. These are contained in the *Promotion of Investment Act 1986*. Incentives available under this legislation are set out on the Ministry of Finance website.[15]

The main incentives applicable to Public-Private Partnerships are as follows:

- **Pioneer Status** - the most important advantage of acquiring pioneer status is the partial exemption from income tax for a period of five years. The status is granted to companies participating in promoted activities producing promoted products. Companies are granted a tax exemption on 70% of statutory income. However, a company located in Sabah, Sarawak and the designated Eastern Corridor of Peninsula Malaysia will be granted tax exemption on 85% of statutory income for five years[16]

- **Investment Tax Allowance** - this is an alternative incentive that companies can opt for, rather than pioneer status. Companies will be granted an allowance of 60% in respect of qualifying capital expenditure. Companies located in Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia, will be granted an allowance of 80% in

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15 http://www.treasury.gov.my/index.php?option=com_content&view=article&id=279%3Apromotion-of-investment-act-1986&catid=92%3Acatinsentif-cukaiundang-undang&Itemid=200&lang=en (last viewed 27/02/2013)

16 http://www.treasury.gov.my/index.php?option=com_content&view=article&id=704&Itemid=200&lang=en (last viewed 27/02/2013)

respect of qualifying capital expenditure incurred within five years from the date the first capital expenditure is incurred[17]

- **Infrastructure Allowance** - this is available for any company resident in Malaysia engaged in manufacturing, agriculture, hotel, tourist and other industrial and commercial activity in Sabah, Sarawak, and the Designated Eastern Corridor of Peninsular Malaysia. A company will be granted an allowance of 100% in respect of capital expenditure on infrastructure such as reconstruction, extension or improvement of any permanent structure including bridges, jetty, port or road. The allowance can be offset against up to 85% of statutory income in the year of assessment. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilized allowances can be carried forward to the subsequent years until they are fully utilized[18]

- **Industrial Building Allowance** - in order to encourage participation in Public-Private Partnership programs, an amendment was made to schedule 3 of the *Income Tax Act, 1967*. This amendment allows Public-Private Partnership projects to enjoy the benefits of the industrial building allowance[19]

- **Stamp Duties Remission** – this is given on service agreements signed between companies and the government, thereby reducing transaction cost[20]

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17 http://www.treasury.gov.my/index.php?option=com_content&view=article&id=703&Itemid=200&lang=en (last viewed 27/02/2013)

18 http://www.treasury.gov.my/index.php?option=com_content&view=article&id=701&Itemid=200&lang=en (last viewed 27/02/2013)

19 http://www.treasury.gov.my/pdf/economy/er/9900/Investor.pdf (last viewed 27/02/2013)

20 EAIC Advisory - Economic Research Institute for ASEAN and East Asia(ERIA) –*PPP Country Profile for Malaysia*

Singapore

Singapore does not have specific legislation designed to provide tax incentives to encourage Public-Private Partnerships. However, Singapore has traditionally offered a wide range of tax incentives for many years. These are contained in the *Income Tax Act* and the *Economic Expansion Incentives (Relief from Income Tax Act).*[21] The *Economic Expansion Incentives Legislation* is specifically designed to promote Singapore's economic and industrial development. It provides incentives such as:

- pioneer incentives
- investment allowances
- development and expansion incentives

These incentives are similar to those outlined above in the Malaysia legislation. These incentives can be utilized by companies involved in infrastructure development.

[21] http://statutes.agc.gov.sg/aol/home.w3p (last viewed 27/02/2013)

5.3. Australia

In Australia income tax incentives are contained in the *Income Tax Assessment Act 1936 (Cth)* and in the *Income Tax Assessment Act 1997(Cth).* Australia has traditionally offered a range of tax incentives to the mining industry and the primary production industry. These are two of the biggest export earning sectors of the Australian economy. However, the Australian government has established Infrastructure Australia, which is a statutory body established under the *Infrastructure Act 2008* which came into effect on 9 April 2008. This is the peak infrastructure body in Australia and its focus is on assisting Australian governments to modernize the nation's economic infrastructure.[22]

In November 2008, the Council of Australian Governments endorsed the National Public-Private Partnership Policy and Guidelines. All Australian State and Territory government agencies now apply the National Policy and Guidelines.[23] Other bodies such as Infrastructure Partnerships Australia are also designed to promote infrastructure development in the country.[24]

The main tax incentive relating to infrastructure development has been a broad range of depreciation deductions available in the *Income Tax Assessment Act 1997(Cth*). In particular, Division 43 provides a tax deduction for the capital expenditure incurred in constructing capital works, including buildings and structural improvements. Generally, these provisions provide for a deduction to be spread over 40 years. However, it has been suggested that infrastructure projects should be written off over a shorter period such as 20 to 30 years[25]. It has also been suggested that targeted infrastructure bonds which were tax-exempt would make infrastructure projects more attractive to investors.[26] Managed Investment Trusts are often used in infrastructure and property

[22] http://www.infrastructureaustralia.gov.au/about/ (last viewed 27/02/2013)

[23] http://www.infrastructureaustralia.gov.au/public_private/ (last viewed 27/02/2013)

[24] http://www.infrastructure.org.au/ (last viewed 26/02/2013)

[25] Ford S, *2012 Financial Services Taxation Conference Infrastructure Incentives and PPP Financing Structures*, Taxation Institute of Australia, National Division Conference, February 2010, p. 4

[26] Ibid at p.4

projects. The final withholding tax rate used to be 7 ½%. However, in 2012 the government legislated to increase this withholding tax rate to 15%. This has been criticized by Infrastructure Partnerships Australia[27]. The lower rate had been designed to attract investment.

In 2011, the Australian government announced that it will legislate a new tax incentive designed to make it easier to claim a tax deduction for losses incurred in the early years of infrastructure development. Designated infrastructure projects will be able to uplift the value of project losses at the Government Bond rate and exempt these losses from the continuity of ownership test and the same business test (these are anti-avoidance provisions which are designed to make it difficult to claim losses where there is a change in ownership of the asset).[28]

[27] http://www.infrastructure.org.au/Content/SubmissiontotheInquiryonMITWithholdingTax.aspx (last viewed 27/02/2013)

[28] http://www.futuretax.gov.au/content/Content.aspx?doc=FactSheets/infrastructure_tax_incentive.htm (last viewed 27/02/2013)

5.4. Korea

In Korea the government has enacted specific legislation in respect of Public-Private Partnerships. The legislation is *The Act of Private Participation in Infrastructure*[29]. However, the tax incentives are contained in *The Special Tax Treatment Control Act (National Tax)*[30].

The overall structure of Tax Incentives for Public Private Partnerships in Korea is summarized in the following diagram:

[29] Korean Government (Ministry of Government Legislation, Centre for national legislation information) 2012, *The Act on Private Participation in Infrastructure*, last viewed 10.Sep. 2012, <http://www.law.go.kr/LSW/lsSc.do?mouseY=436&menuId=0&p1=&subMenu=1&searchChk=2&lawSearchName=LicLs%2C0&query=%EC%82%AC%ED%9A%8C%EA%B8%B0%EB%B0%98%EC%8B%9C%EC%84%A4%EC%97%90+%EB%8C%80%ED%95%9C&x=22&y=9#liBgcolor0>, **[saved in Korean – 사회간접시설에 대한 민간투자법]**

[30] Korean Government, (Ministry of Government Legislation, Centre for national legislation information) 2012, *Special Tax Treatment Control Act (*last viewed 10.Sep. 2012), <http://www.law.go.kr/engLsSc.do?menuId=0&subMenu=5&query=%EC%A1%B0%EC%84%B8%ED%8A%B9%EB%A1%80%EC%A0%9C%ED%95%9C%EB%B2%95#liBgcolor0>, **[saved in English – Special Tax Treatment Control Act]**

The Act on Private Participation in Infrastructure
- Tax Exemption and Reduction **(Article 57)**

Special Tax Treatment Control Act (National Tax)

- Separate Taxation on Interest income from global taxation system. **(Article 29)**
- Separate Taxation on Dividend income from global taxation system **(Article 91-4)**
- Application of zero rating to Value-Added Tax with respect to urban Railway construction services or infrastructure facilities and construction services. **(Article 105)**
- Exemption of Value-Added Tax with respect to School facilities **(Article 106)**
- Foreign Investment Promotion
  - Reduction or exemption from each of corporate tax, income tax, acquisition tax, registration tax and property tax for the PPP project under Foreign Investment Zone **(Article 121-2)**

Local Tax Act

- Acquisition tax exemption with respect to PPP **(Article 9)**

Special Local Tax Treatment Control Act

- Acquisition Tax Reduction (50%) Property Tax Reduction (50%) for the construction of Complex Logistics Centre and its property **(Article 71)**

It can be seen from the above outline that the following incentives are designed to attract private participation in infrastructure development:

- **Separate Taxation of Interest Income**

  Article 29 of *The Special Tax Treatment Control Act* specifies a separate taxation on interest income from social infrastructure bonds.[31] The interest income is not included in the global income tax base.

- **Dividend Income**

  Article 91–4 of *The Special Tax Treatment Control Act* provides special taxation of dividend income received by residents possessing stocks of a social fundamental facilities investment and lending company under the *Act on Private Participation in Infrastructure*.[32]

- **Reduced Tax on Foreign Investment**

  Article 121-2 of *The Special Tax Treatment Control Act* provides that foreign investment amounts of more than US$10 million in projects to

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[31] **Article 29 (Separate Taxation on Interest Income from Social Infrastructure Bonds, etc.)**

"With respect to interest derived from social infrastructure bonds and flood control bonds as determined by Presidential Decree, which mature in 15 or more years from the date of their issue and are issued not later than December 31, 2009, notwithstanding Article 14 of the Income Tax Act, such interest income shall not be added in calculating the global income tax base; on the other hand, it shall be subject to the application of the tax rate as provided in Article 129 (1) 1 (c) of the same Act."

[32] **Article 91-4 (Special Taxation on Dividend Income of Stocks of Social Fundamental Facilities Investment and Lending Company)**

"With regard to the dividend income received by the residents possessing the stocks of a social fundamental facilities investment and lending company under the Act on Private Participation in Infrastructure (hereinafter referred to as an "investment and lending company") on or before December 31, 2010, it shall not be added up in the calculation of global income tax base under Article 14 (2) of the Income Tax Act. In such cases, with regard to the dividend income of possessed stocks whose aggregate amount of face values of the relevant stocks possessed is not more than 100 million won by investment and lending companies, the withholding tax rate shall be 6/100 (5/100 up to the part of the taxation period for which liability for tax payment is constituted on or before December 31, 2009) notwithstanding the provisions of Article 129 of the Income Tax Act, and when the aggregate amount of face values of the relevant stocks possessed exceeds 300 million won by investment and lending companies, the withholding tax rate under Article 129 (1) 2 of the Income Tax Act shall apply to the dividend income from the possessed stocks portions of such excesses."

construct social infrastructure facilities shall be eligible to reduction in taxation[33]. This includes acquisition tax and property tax.

- **Reduction in Value Added Tax**
  Article 105 of *The Special Tax Treatment Control Act* provides the application of zero rating to Value-Added Tax with respect to urban railway construction services or infrastructure facilities and construction services. Article 106 of *The Special Tax Treatment Control Act* provides an exemption of Value-Added Tax with respect to school facilities.

Other Incentives

Other incentives are contained in the *Local Tax Act* and the *Special Local Control Tax Treatment Act.* They are designed to provide a reduction in Acquisition Tax and Property Tax.

Paragraph 2 Article 9 *Local Tax Act* says as follows:

"Acquisition tax shall be exempted in cases where the acquisition of relevant property is one of the conditions to undertake a project (including the case as prescribed in paragraph 3 of Article 4 of the Act on Private Participation in Infrastructure) and infrastructure facilities falling under any subparagraphs of paragraph 1 of Article 2 of the Act on Private Participation in Infrastructure which will revert or contribute to the State, local government or domestic corporations"[34]

Paragraph 3 of Article 71 of the *Special Local Tax Treatment Control Act* says as follows:

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[33] Korean Government, (Ministry of Government Legislation, Centre for national legislation information) 2012, *Foreign Investment Promotion Act-the Presidential Decrees* ,(last viewed 10.Sep. 2012), <http://www.law.go.kr/lsSc.do?menuId=0&subMenu=1&query=%EC%A7%80%EB%B0%A9%EC%84%B8%ED%8A%B9%EB%A1%80%EC%A0%9C%ED%95%9C%EB%B2%95#liBgcolor1>, **[saved in Korean –외국인투자촉진법 시행령],**

[34] Korean Government, (Ministry of Government Legislation, Centre for national legislation information) 2012, *Local Tax Act*, viewed 10.Sep. 2012 **[saved in Korean – 지방세법],** http://www.law.go.kr/lsSc.do?menuId=0&subMenu=1&query=Local%20tax%20act#liBgcolor10

> *"The Acquisition tax will be reduced by 50/100 to the property that is acquired for complex logistics centres under the Act on Private Participation in Infrastructure when authorized as prescribed in paragraph 1 of Article 9 of The Act on development and operation of logistics facilities, or the property tax will be reduced by 50/100 to the property which is directly used as of the basic date for taxation on or before December 31, 2014"*[35]

[35] Korean Government, (Ministry of Government Legislation, Centre for national legislation information) 2012, *Special Local Tax Treatment Control Act,* viewed 12.Sep. 2012, <http://www.law.go.kr/lsSc.do?menuId=0&p1=&subMenu=1&nwYn=1&query=%EC%A7%80%EB%B0%A9%EC%84%B8%ED%8A%B9%EB%A1%80%EC%A0%9C%ED%95%9C%EB%B2%95&x=31&y=13#AJAX>, **[saved in Korean – 지방세특례제한법],**

5.5. Philippines

The government of the Philippines has adopted a policy of encouraging private sector participation in infrastructure development. *The Build – Operate – Transfer (BOT) Law (Republic Act No 6957 of 1991 as amended by Republic Act Number 7718 of 1994)* sets out the policy and regulatory framework for private sector participation in infrastructure projects. A government agency, the BOT Centre, was established to manage and coordinate the implementation of the BOT. [36]

In September 2010 President Aquino issued an executive order to reorganize and rename the BOT Centre as the Public-Private Partnership Centre (PPP Centre). Previously the BOT Centre was attached as an agency of the Department of Trade and Industry. However, the PPP Centre is now attached as an agency of the National Economic Development Authority (NEDA). This authority is a central planning agency for social and economic development. The Public-Private Partnership Centre serves as a governance facilitator and catalyst in organizing and delivering PPP projects. The government is pursuing a wide range of infrastructure projects in strategic areas such as water, power and transport and is relying on the BOT Law and the NEDA joint-venture guidelines to implement the PPP program.[37]

Overview of Incentives

Enterprises may register with the Board of Investment (BOI) under the Omnibus Investment Code (OIC) or with the Philippine Economic Zone Authority in order to obtain incentives. The Philippine government has also designated certain areas of the country as special economic zones which have further tax incentives attached to them. An example is the Subic Special Economic and Free Port Zone. The Board of Investment, through tax incentives and other

[36] Quium A, *Private Sector Participation in the Transportation Sector: Trends, Issues and Institutions in the Asia-Pacific Region*, Transport and Communication Bulletin Asia and the Pacific, No.72, 2003, p.20

[37] Quisumbing Torres Lawyers, *Client Alert Newsletter*, November 2010

benefits, encourages investment in areas specified by the Board of Investment in the investment priorities plan.[38]

A foreign investor is guaranteed repatriation of investments, remittance of profits, freedom from expropriation and requisition of investment, protection of patents, and other proprietary rights.

Tax Incentives[39]

Enterprises registered with the BOI can obtain the following tax incentives:

- Income tax holiday concessions which exempt income taxes from 4 years (non-pioneer enterprise) to 6 years (for pioneer enterprise). This incentive can be extended upon approval by the BOI, but cannot extend more than eight years. A pioneer enterprise either manufactures goods that have not been produced in the Philippines on a commercial scale, or employs a formula, or production scheme which has not yet been tried in the Philippines
- Exemptions from tax and duties on machinery, equipment, spare parts, and accessories, imported by new and expanding registered enterprises
- In the first five years from registration, an additional deduction from taxable income of 50% of wages of additional skilled and unskilled workers in the direct labor force. However, the enterprise must meet prescribed capital to labor ratios
- Exemptions from local taxes to six years from the date of registration for pioneer enterprises, and four years from the date of registration for non-pioneer enterprises

[38] Quisumbing Torres Lawyers, *Doing Business in The Philippines* ,2012,p16

[39] Ibid. at p.19

- Projects in less developed areas also obtain extra deductions for labor and infrastructure work construction

Additional Incentives[40]

A number of additional incentives have also been provided:

- Simplified custom procedures for the importation of equipment, spare parts, raw materials and supplies
- Employment of foreign nationals in supervisory, technical and advisory positions.

Special Economic Zones

The government has designated certain areas of the country as special economic zones in order to disperse industry and generate employment in non-urban areas.

Tax Incentives and Other Incentives in these Zones[41]

- Income tax holidays for four years for non-pioneer firms and six years for registered pioneer firms
- Preferential tax rate of 5% of gross income applies to echo zone enterprises when the income tax holiday expires. This is in lieu of all national and local taxes
- Zero rated VAT on sales

[40] Ibid, at p.20

[41] Ibid, at p.22

- exemptions from duties and taxes on importation of merchandise, raw materials, supplies and equipment and machinery
- exemptions from wharfage dues and export tax
- additional deductions for training expenses
- additional deductions for labour expenses
- employment of foreign nationals in the executive, supervisory, technical and advisory positions

The Clark Special Economic Zone and the Subic Special Economic and Free Port Zone

The government has designated the former US military bases as special economic zones with the aim of developing these areas as industrial, commercial, financial and investment centers. Tax incentives have been designed to encourage this development. For instance, in the Clark Special Economic Zone a tax rate of 5% on gross income earned is payable in lieu of all national and local taxes and the importation of raw material and capital equipment is duty-free.[42]

[42] Ibid, at p.23

5.6. Vietnam

In July 2011, Mr Dang Huy Dong, the Vietnamese Deputy Minister of the Ministry of Planning and Investment, stated that Vietnam needs $15 billion each year until 2020 to develop its infrastructure if it intends to realize its target of becoming an industrial nation.[43]

The government encourages the use of Public-Private Partnerships to develop infrastructure in the transport, water, waste and power sectors. The participation in infrastructure development in the form of the BOT, BTO and BT projects was incorporated under the basic framework established in *Decree 77 (1997)* and *Decree 62(1998)*. *Decree 78 (2007)* and *Decree 108 (2009)* have further developed the BOT legal framework. The government has also introduced legislation which has created a legal framework for the introduction of Public-Private Partnerships in Vietnam. The regulations on Pilot Investment under the form of Public-Private Partnerships (*PPP Regulations)* became effective in January 2011. These regulations provide a framework for selecting PPP projects.

Land issues can be an impediment in infrastructure projects and government support is therefore crucial[44]. In Vietnam land is regarded as public property and only Vietnamese citizens have the right to use the land. Foreign investors cannot own or use land[45]. However, rental of land by foreign investors is an option. As part of the investment incentives granted by the government, the PPP Regulations provide that a private investor is entitled to be exempted from a land use fee for the allocated area or be exempted from land rent for the project duration.[46]

[43] Ashurst, Frasers Lawyers, A*shurstinsight Infrastructure Opportunities,* January 2012

[44] EAIC Advisory - Economic Research Institute for ASEAN and East Asia(ERIA) –*PPP Country Profile for Vietnam*

[45] Ibid p.2

[46] *PPP Regulations* Chapter 8, Article 41

The BOT regulations and the PPP regulations provide that corporate income tax incentives are available for infrastructure projects. Most of the incentives are contained in the *Law on Investment*.

Tax and Investment Incentives

Examples of incentives[47] are as follows:

- A concessional 10% tax rate for the duration of the project
- A reduced level of withholding tax on the remittance of profit overseas
- Exemptions from certain import and export duties
- Exemptions from paying land use fees
- Preferential tax rates apply for BOT, BTO and BT infrastructure projects in industrial zones and export processing zones for the entire duration of the investment project
- Losses on the project can be carried forward up to 5 years from the first year in which profit is made
- Assets that form part of the capitalization of the investment are exempt from import duties
- Enterprises which reinvested profits in encouraged sectors in Vietnam may be entitled to a full or partial enterprise income tax refund
- Investment projects in investment incentive sectors, and geographical areas and business projects with high economic efficiency shall be subject to accelerated depreciation of fixed assets[48]

[47] See Vietnam Department of Planning and Investment, Laws and Regulations, *Frequently Asked Questions*

[48] Article 35, *Law of Investment*, Vietnam

Other Relevant Incentives

- The *Law of Investment* guarantees that the lawful assets and invested capital of investors should not be nationalized or confiscated
- The State shall protect intellectual property rights during investment activities

5.7. Thailand

In 1992 the Thai Government passed T*he Act on Private Participation in State Undertaking, B. E. 2535(1992)*. This act has been designed to deal with Public-Private Partnerships as well as governing all kinds of participation in projects exceeding 1 billion baht. Furthermore, the Ministry of Finance has drafted a new *Public-Private Partnership Act*, with the object of providing better support for Public-Private Partnership development.[49]

The objective of *The Act on Private Participation State Undertaking* is to set requirements and procedures regarding concessions in private participation in State undertakings and grant concessions[50]. Investment privileges have long been one of the measures used by the Thai government to attract foreign investment in Thailand and support the government's goal of decentralizing Thailand's industrial base. The Board of Investment is the agency directly responsible for investment promotion. The Thai Customs Department also has the power to grant relief from import duty and taxes.

The Board of Investment promotion scheme provides assistance by offering the following incentives to eligible activities:

Tax Incentives[51]

- exemptions in import duty on machinery regardless of zone
- eight year corporate income tax exemption regardless of zone

[49] EAIC Advisory - Economic Research Institute for ASEAN and East Asia(ERIA) –*PPP Country Profile for Thailand*

[50] Chalongphob Susangarn, *Public-Private Partnership in Thailand: Past Experiences and Future Prospects*, presented at the Asia Pacific Ministerial Conference on PPPs in Infrastructure, Republic of Korea, 4 October 2007

[51] See Sections 28 to 36 of *The Investment Promotion Act B. E. 2520*

- double deductions for the cost of transportation, electricity and water supply
- exemptions in import duty on raw research materials for use in production and export
- an additional 25% deduction for cost of installation or construction of facilities
- reduction of import duties for raw research materials

Other Incentives[52]

The Investment Promotion Act B. E. 2520 also provides some relevant non-tax incentives. For instance:

- permits to bring into the kingdom skilled workers and experts to work in investment promoted activities
- permits to own land
- permits to take or remit money abroad in foreign currency
- guarantees that the state will not nationalize the activity of the promoted person

[52] http://www.boi.go.th/index.php?page=guides (last viewed 20 February 2013)

6. Broad Summary of Common Infrastructure Tax Incentives in Australia, Indonesia, Korea, Malaysia, the Philippines, Singapore, Vietnam and Thailand

6.1. Tax Holidays

Overview

Tax holidays are designed to encourage investment by not requiring a qualifying entity to pay tax for a specific period. Rules are required in order to define a qualifying entity and the specific period of the tax holiday.

Examples

In Indonesia tax holidays are available for five to ten years. In the Philippines, Non-Pioneer Enterprises can obtain a tax holiday of four years and a Pioneer Enterprise can obtain a tax holiday of six years. Thailand provides an exemption from tax for up to eight years.

6.2. Reduced Corporate Tax Rates

Overview

Here the corporate tax rate is reduced based on the type of activity and other parameters, such as the location or region of the country.

Examples

In Vietnam a concessional tax rate of 10% applies for the duration of the project. Reduced tax rates also apply in special economic zones in this country. In Malaysia entities with Pioneer Status are granted an exemption on 70% of Statutory Income. Companies located in special regions such as Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia are granted a tax exemption on 85% of Statutory Income.

6.3. Accelerated Capital Allowances and Investment Allowances

Overview

The entity is allowed to write-off capital costs over a period of time shorter than the economic life of the asset. The present value of the expenditure is increased by allowing the deduction at a time closer to the investment.

Examples

This is one of the most common tax incentives relevant to infrastructure investment. A good example of this incentive is found in Malaysia. Here an investment allowance of 60% of capital expenditure is available. This rises to 80% in special economic zones such as Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia. Malaysia also offers an infrastructure allowance and an industrial building allowance. The infrastructure allowance can be offset against up to 85% of statutory income in the year of assessment. Vietnam and Indonesia also allow for accelerated depreciation on infrastructure projects. Australia allows a write off of construction costs, usually over a 40 year period.

6.4. Location Based Incentives

Overview

Here tax incentives are targeted to apply to apply to investments in specific regions within the country and are designed to stimulate infrastructure development in those regions.

Examples

The Philippines, Malaysia and Vietnam provide good examples of this incentive. In the Philippines there are special economic zones such as the Clark Special

Economic Zone and Subic Special Economic Zone. A reduced tax rate of 5% on gross income earned is payable in lieu of all national and local taxes. Other incentives are also available such as reduced Value Added Tax and Customs Duty. Additional deductions are available for training expenses and labor expenses. Malaysia offers higher investment allowances in special economic zones such as Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia. Reduced tax rates also apply in special economic zones in Vietnam.

6.5. Reduced Taxes on Dividends and Interest

Overview

This incentive is designed to stimulate infrastructure investment by reducing the tax payable on dividends and interest received from companies involved in infrastructure development.

Examples

In Korea the *Special Tax Treatment Control Act* provides for a special taxation on interest from infrastructure bonds and special taxation of dividend income received by residents possessing stocks in a social fundamental facilities investment and lending company. In Australia it has been suggested that tax-exempt infrastructure bonds should be considered by the government.[53]

6.6. Reduction in Withholding Tax

Overview

The reduction or elimination of withholding tax on dividends and interest for non-residents is designed to encourage foreign investment.

[53] Ford, Op. cit. at p.4

Examples

Vietnam provides a reduction of withholding tax on profits remitted overseas. Indonesia also provides a reduction in withholding tax on dividends paid to foreign shareholders from 20% to 10%.

6.7. Carry Forward Losses

Overview

Infrastructure projects usually incur losses in the early years of operation. It is common for countries to allow these losses to be carried forward and offset against future income.

Examples

In Australia the government proposes that designated infrastructure projects will be able to uplift the value of project losses at the Government Bond rate and exempt these losses from the anti-avoidance provisions (the continuing of ownership test and the same business test) thereby allowing them to be deducted in future years. The uplifting of the losses at the Government Bond rate will mean that the losses do not lose value over time. Indonesia and Vietnam allow losses to be carried forward for between five and ten years.

6.8. Deductions for Qualifying Expenses

Overview

Specific expenses are deductible in order to encourage and target specific investments.

Examples

In the Philippines extra deductions are available for training expenses and labor expenses.

6.9. Reduction in Indirect Taxes

Overview

In order to encourage investment, exemptions are given in respect of customs duties and import tax and other indirect taxes, such as Value Added Tax. This is a common incentive and has been widely used to encourage infrastructure development.

Examples

In Korea acquisition tax and property tax are reduced for Public-Private Partnership infrastructure projects. Korea also provides for a reduction in Value Added Tax. In special economic zones of the Philippines, Value Added Tax and Customs Duties are reduced to zero. The Philippines also reduces Customs Duty on equipment, machinery and raw materials and exempts companies from local taxes. In Malaysia, Stamp Duty remission is given on service agreements signed between companies and the government, thereby reducing transaction costs.

6.10. Other Related Incentives

Overview

A number of the countries surveyed have legislated a number of non-tax incentives to encourage infrastructure development. Although they are not specifically tax incentives, they are designed to encourage foreign investment.

Examples

- Vietnam and Thailand have legislated to guarantee that infrastructure projects will not be nationalized
- Vietnam has also provided guarantees to protect intellectual property rights
- In Thailand *The Investment Promotion Act B.E. 2520* permits skilled workers to be bought into the kingdom to work on investment promotion activities. The legislation also permits the ownership of land and the remittance of money abroad in foreign currencies

7. Concluding Observations

This report outlines a wide range of infrastructure incentives found in Australia, Indonesia, Korea, Malaysia, the Philippines, Singapore, Thailand and Vietnam. It is designed to be used as a catalyst to stimulate discussion in countries using, or contemplating the use of, Public-Private Partnerships for infrastructure development.

Different social, political and economic objectives determine the types of tax incentives adopted. Nonetheless, tax incentives infrastructure development should not be looked at in isolation as unintended results can ensue. For example, after the Civil War in Lebanon, tax incentives were offered to encourage building construction. Unfortunately, no incentives were offered to the developers of destroyed or damage property. This resulted in an oversupply of new buildings, a lack of liquidity in the market and damaged buildings remaining unrepaired.[54]

Infrastructure tax incentives are designed to encourage investment and have to be balanced with their impact on revenue collection. In the short-term infrastructure incentives reduce the flow of revenue. However, the development of infrastructure provides social and long-term economic benefits which have to be balanced with the political, budgetary and economic objectives of the government.

[54] Abou Nasr W, *Tax Incentives in Lebanon*, A paper submitted at the UNCTAD Ad Hoc Meeting on Tax Incentives, 8 July 1999