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Solutions to Attract FDI into Vietnam in Preparation for Global Minimum Tax

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Abstract From January 1, 2024, the global minimum tax policy of 15% will take effect, significantly affecting the business results of FDI enterprises. This will affect the change of operation methods and investment location strategies of FDI enterprises, so it is necessary to have solutions to attract and retain businesses to invest in the Vietnamese market. The article assesses the current status of FDI investments in Vietnam in the five years from 2018 to 2022. It mainly focuses on analyzing newly licensed FDI projects to propose solutions to attract FDI enterprises in the coming time.

Keywords: *Global minimum tax, FDI enterprises, investment, Vietnam market*

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1. Introduction

Foreign direct investment enterprises (FDI) are essential to the Vietnamese economy. Over the years, FDI has become one of the main driving forces for Vietnam's economic development and integration, increasing the Vietnamese economy's competitiveness, creating more jobs for people, and growing state budget revenues [1].

Vietnam is an attractive destination for FDI enterprises with the advantage of a stable political and security situation; Favorable geographical location, large labor force, Vietnam's institutions, laws, and transparency are gradually improved in association with integration, not only creating favorable conditions for investors to operate in the long term but also help businesses participate in supply chains, global value chains in a good way [1]. Although the world economy, global FDI, and Vietnam's economy were negatively affected by the Covid-19 pandemic, attracting foreign investment and operating the capital-invested economic sector, Foreign investment still achieved encouraging results.

Investment location and operation method of multinational companies; therefore, it is necessary to have appropriate solutions for attracting FDI. Foreign investment inflows have continuously increased over the past time because Vietnam has implemented many preferential tax policies, in which the tax exemption and corporate income tax reduction policies are very competitive, can be exempted from tax for up to 4 years, and 50% reduction in tax payable in the next nine years, along with strengths such as stable political economy, large labor force. However, the Global Minimum Tax Policy, which must be applied from January 1, 2024, with a minimum global corporate tax rate of 15%, will cause many concerns about the trend of strategic disarray in the financial sector.

2. Overview of the Impact of Tax Incentives on FDI Attraction

Foreign direct investment (FDI) is increasingly recognized as a factor in the economic development of countries [2], so countries especially least developed countries give priority to for attracting FDI. Among the tools to attract investment, tax incentives are quite popular. Tax incentives tend to attract FDI looking for efficiency promoted by reducing production costs compared to other forms of investment. Developing country governments use tax incentives in ways by (1) targeting incentives to investors (2) improving institutions and other policies to reduce indirect costs for investors [3].

A study of tax incentives in more than 45 countries from every region of the world, UNCTAD [2] shows that nearly all of the countries surveyed offer incentives targeting the specific sectors. Regional incentives to support economic development in rural or underdeveloped areas are also common in nearly 70% of the countries surveyed. In terms of the types of financial incentives granted, there is clearly a growing trend towards providing full or partial tax exemptions or reduced tax rates for specific types of activities. Nearly 85% of the countries surveyed offer such incentives [4].

Based on the theoretical framework drawn from the eclectic or "OLI" model, the model developed by [5] as well as the development from the study of factors affecting investment market choice by Gilmore et al. [6] confirmed that preferential policies, including tax, are factors that have a strong influence on attracting FDI.

Research in African countries initiates and implements many measures to improve the business-friendly environment to attract capital flows from foreign investors [7]. According to Tuomi [8] measures adopted by African countries include economic liberalization, tax incentives and infrastructure provision to attract foreign direct investment. Tax incentives such as low corporate tax rates, tax exemptions, tax credits, investment subsidies, tax deductions, and more are key tools used by some developing economies to attract foreign investors [9].

In Vietnam, Applying the theory of local marketing, Thọ & Trang, [10] said that there are four factors affecting the satisfaction of businesses in the locality, including: Government support; Skills training; Habitat; Investment incentives. Huyen [11] also confirmed that financial incentives are being used effectively and widely in Vietnam. Thus, from the research overview, it shows that Tax is always an effective tool in attracting FDI of countries, especially developing countries like Vietnam.

The global minimum tax is a tax initiated by the Organization for Economic Cooperation and Development (OECD). 142/142 member countries, including Vietnam, agree with the rule of global minimum tax. With this tax, large corporations and companies with a turnover of 750 million euros or more will all have to pay 15% tax, no matter whether in any country; with this provision, companies enjoying tax rates lower than 15% in the country of investment will have to pay the difference in the country of the parent company [12]. The global minimum tax will create a tax system between countries to ensure a minimum tax rate for MNCs/corporations.

To date, most of the countries of the European Union (EU); countries and territories, such as Switzerland, the UK, Korea, Japan, Singapore, Indonesia, Hong Kong (China), and Australia... have confirmed to apply the 15% minimum tax rate, starting from 2024. In which Korea, Singapore, and Japan are countries with large amounts of foreign investment in Vietnam, many enterprises are subject to the application of the Global Minimum Tax. According to statistics from the Ministry of Finance in Vietnam, there are currently 1,212 FDI enterprises with parent companies subject to applying the Global Minimum Tax [13]. In this context, Vietnam also needs to have appropriate financial policies to attract investment capital flows from foreign enterprises.

3. Situation of Attracting Foreign Investment in Vietnam

3.1. Operational Status of Enterprises

According to the report on foreign investment attraction in 2022 (Ministry of Planning and Investment), as of December 20, 2022, the total registered FDI capital in Vietnam reached nearly 27.72 billion USD, and the actual FDI capital reached a record of 22.4 billion USD, up 13.5% over the same period in 2021. This is the highest amount of realized FDI in 5 years (2017 - 2022). By the end of 2022, the country will have 36,278 valid projects with a total registered capital of over 438.7 billion USD. The accumulated realized capital of foreign investment projects is estimated at nearly 274 billion USD, equal to 62.5% of the total valid registered investment capital [14] [15].

Foreign investors have invested in 54 provinces and cities across the country in 2022. Ho Chi Minh City led the way with a total registered investment capital of more than 3.94 billion USD, accounting for 14.2% of total registered investment capital, and increased by 5.4% over the same period in 2021. Binh Duong ranked second with a total investment capital of more than 3.14 billion USD, accounting for 11.3% of total capital, up 47.3% over the same period last year. Quang Ninh ranked third with a total registered investment capital of nearly 2.37 billion USD, accounting for 8.5% of total capital and increasing more than two times compared to the same period in 2021. They were followed by Bac Ninh, Hai Phong, and Hanoi.

In 2022, the total newly registered capital, adjusted and contributed capital to buy shares, and purchase capital contribution of foreign investors reached nearly 27.72 billion USD, equaling 89% in 2021. Realized capital of the investment project Foreign investment is estimated at almost 22.4 billion USD, up 13.5% compared to 2021 [15].

Table 1. Realization of foreign investment capital 2018-2022

No.	Criteria	Unit	2018	2019	2020	2021	2022
1	Realized capital	Million USD	19.100	20.380	19.980	19.740	22.396
2	Registered capital*	Million USD	35.465,56	38.019,11	28.530,10	31.153,34	27.718,13
2.1	New registration	Million USD	17.976,17	16.745,60	14.646,42	15.245,40	12.446,22
2.2	Registration for more	Million USD	7.596,65	5.802,03	6.414,49	9.014,77	10.117,81
2.3	Contribute capital, buy shares	Million USD	9.892,73	15.471,48	7.469,20	6.893,16	5.154,10
3	Number of projects*						
3.1	New	Projects	3.046	3.883	2.523	1.738	2.036
3.2	Increase capital	Project turn	1.169	1.381	1.140	985	1.107
3.3	Contribute capital, buy shares	Project turn	6.496	9.842	6.141	3.797	3.566
4	Exports (including crude oil)	Million USD	173.964	185.278	204.432	246.877	276.462
5	Import	Million USD	141.939	149.411	169.014	218.480	234.660

Source: Ministry of Planning and Investment (2018, 2022).

Export situation: Export (including crude oil) was estimated at nearly 276.5 billion USD, up 12% over the same period, accounting for 74.4% of export turnover. Exports excluding crude oil were estimated at more than US$274.1 billion, up 11.8% over the same period, accounting for 73.8% of the country's export turnover. Import situation: The import turnover of the FDI sector is estimated at nearly 234.7 billion USD, up 7.4% over the same period and accounting for 65.1% of the import turnover of the whole country. In 2022, the foreign investment sector will have a trade surplus of $41.8 billion, including crude oil, and a trade surplus of nearly $39.5 billion, excluding crude oil. Meanwhile, the domestic business sector had a trade deficit of more than 30.8 billion USD.

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3.2. Situation of Attracting New Investment Projects

As of December 20, 2022, the total newly registered capital, adjusted and contributed capital to buy shares of foreign investors, reached nearly 27.72 billion USD, equaling 89% compared to the same period in 2021. Although newly registered investment capital decreased, new investment projects and adjusted investment capital increased over the same period. Specifically:

Newly registered capital: There were 2,036 new projects granted investment registration certificates (up 17.1% over the same period), and the total registered capital reached nearly 12.45 billion USD (down 18.4% over the same period).

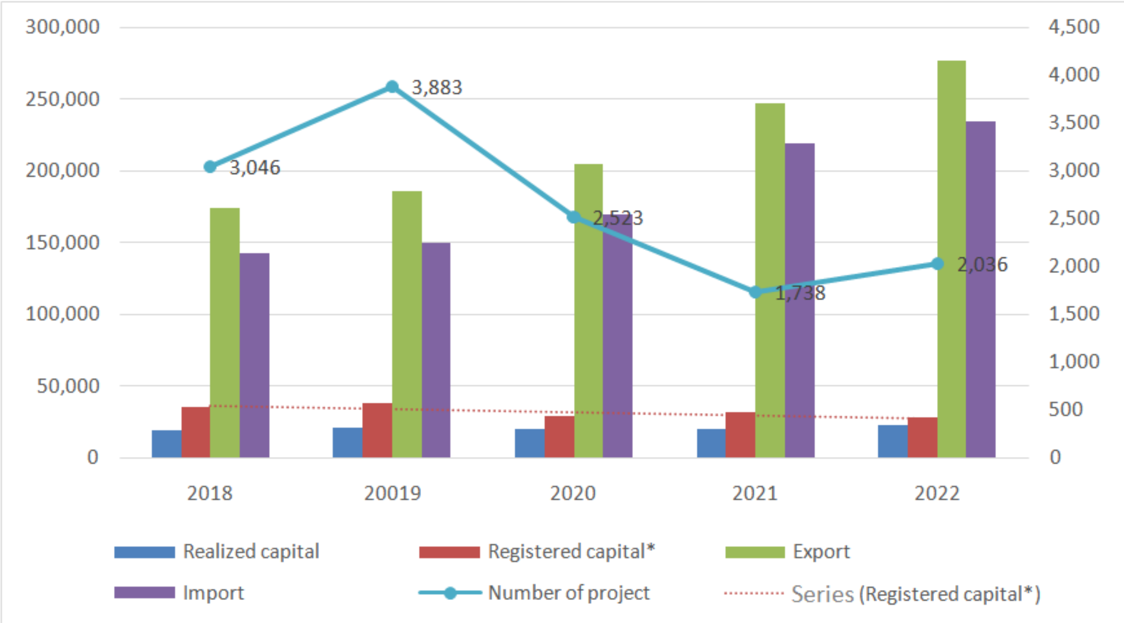

Figure 1. Situation of attracting new investment capital 2018-2022 (Source: Ministry of Planning and Investment (2022))

However, considering the past five years, the number of investment projects has decreased markedly in 3 years, 2020, 2021, and 2022, due to the impact of the covid epidemic. Notably, in 2021, the number of newly invested FDI projects is only equal to 44.76% of the recently granted projects in 2019. In 2022, the number of freshly awarded projects increased by 17.1% compared to 2021, but the registered capital decreased by 18.4%. This shows that in the post-covid context, solutions are necessary to attract foreign businesses to invest in Vietnam.

By industry:

Foreign investors have invested in 19 industries out of 21 national economic sectors. The processing and manufacturing industry took the lead with a total new investment capital of more than 7,213 million USD, followed by electricity production and distribution industries; the Real estate business ranked third with total newly invested capital of 1,868 million USD [15].

In terms of the number of new projects, the wholesale and retail sectors, the manufacturing and processing industries, and professional science and technology activities attracted the most, accounting for 30%, 25.1%, and 16.3% of total projects, respectively.

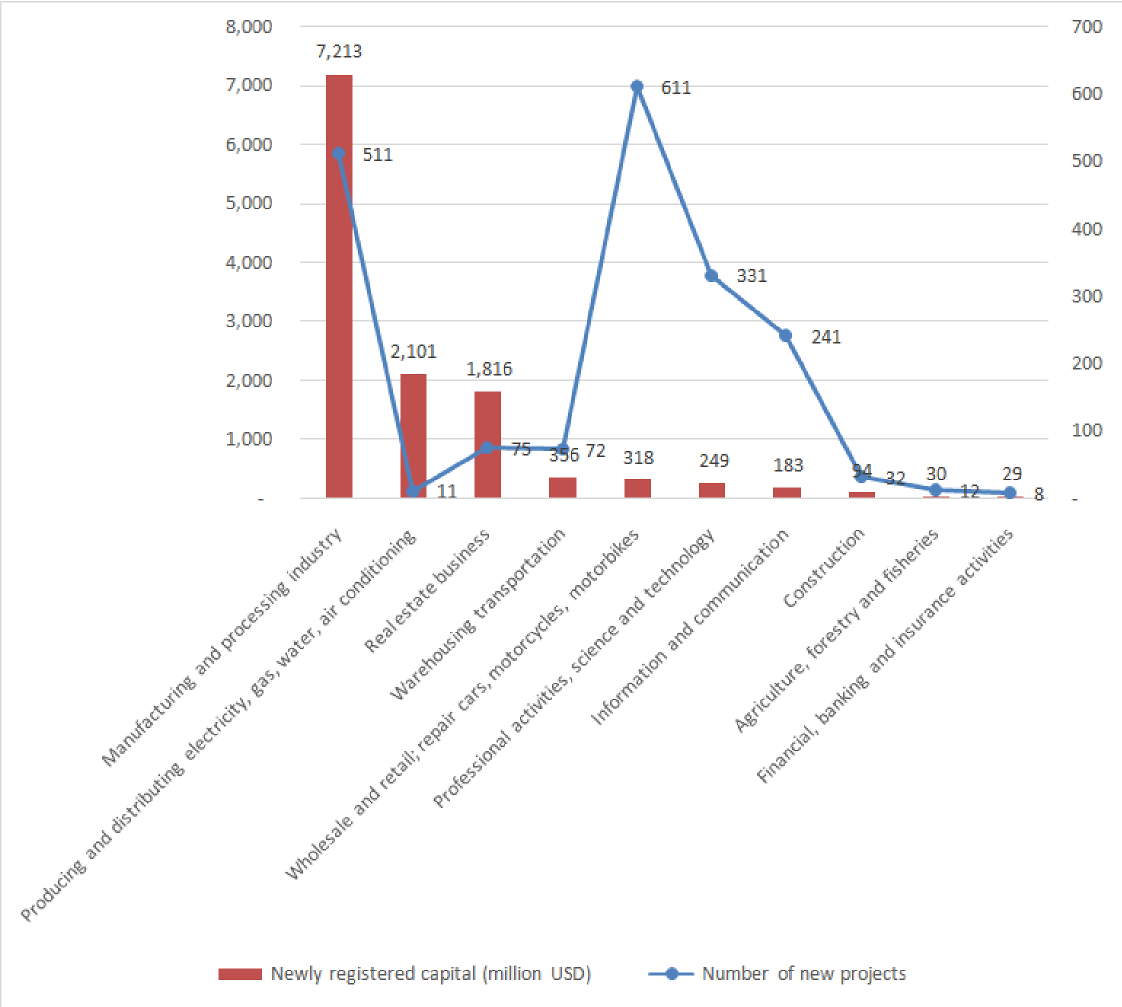

Figure 2. Situation of newly granted FDI projects by industry (*Source: Ministry of Planning and Investment (2022)*)

According to investment partners:

There have been 108 countries and territories investing in Vietnam in 2022. Japan leads with total investment capital of new projects of more than 3,388 million USD, Singapore ranks second, China ranks third, followed by Denmark, Korea, Hong Kong, the United States, and Taiwan [15].

According to the number of projects, Korea is still the partner with investors interested in making new investment decisions, expanding investment projects, and contributing capital to buy shares the most in 2022 (accounting for 20.4 % of new projects), then China, Singapore, and Japan.

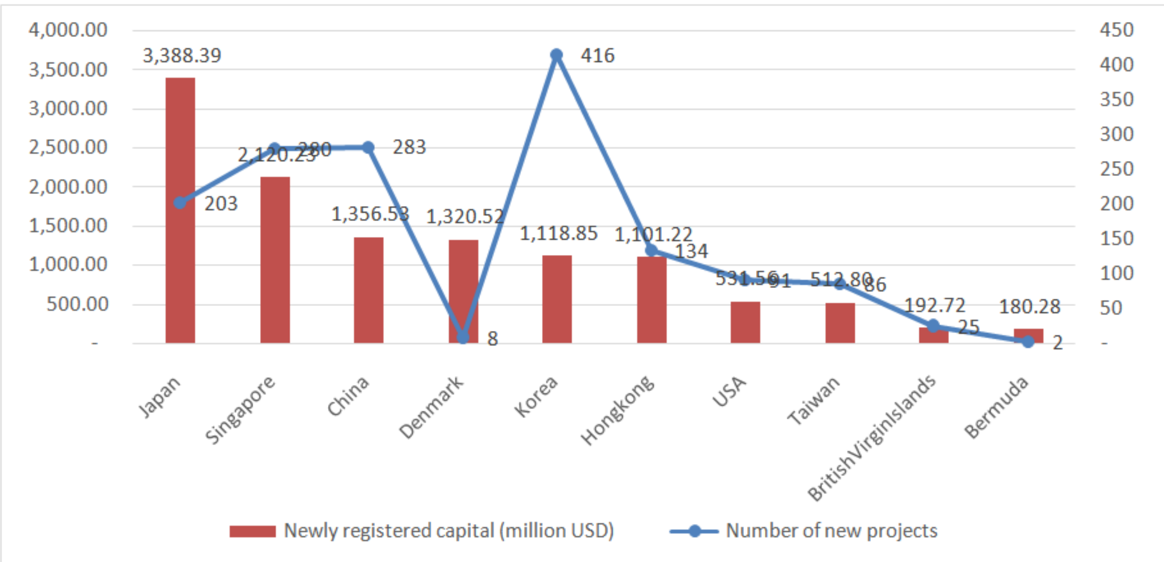

Figure 3. Status of newly granted FDI projects by partner (Source: Ministry of Planning and Investment (2022))

By investment area:

Foreign investors have invested in 54 provinces and cities across the country in 2022. Quang Ninh leads with a total newly registered investment capital of more than $2,181 million, Binh Duong ranks second with a total investment of more than $1,909 million, Hai Phong ranked third, next is Ho Chi Minh City, Tay Ninh, Bac Ninh.

Regarding the number of new projects, foreign investors focused on investing in big cities with convenient infrastructure, such as Ho Chi Minh City, Binh Duong, and Quang Ninh. Ho Chi Minh City leads in the number of new projects, with 893, accounting for 67.6% of new projects nationwide in 2022.

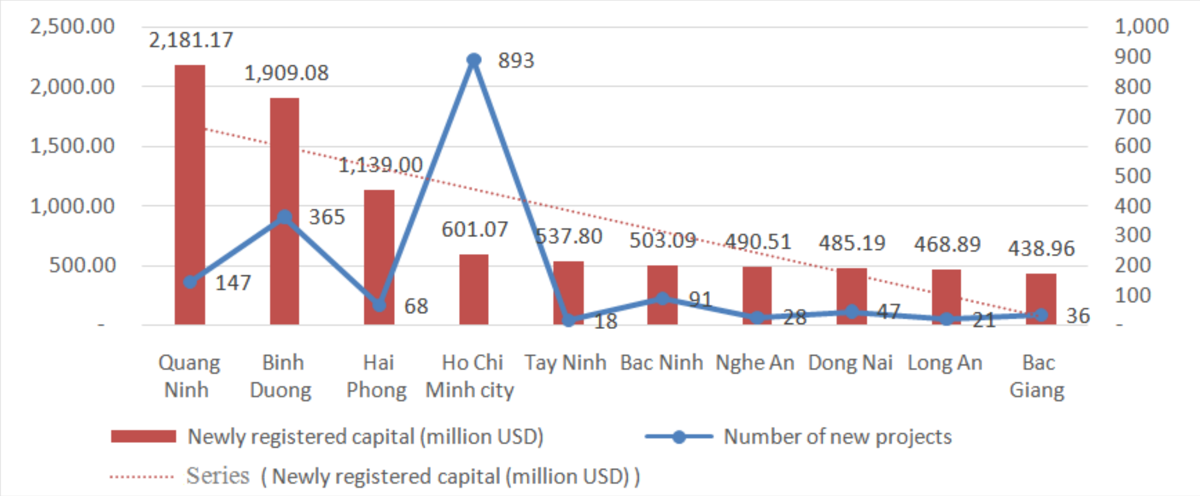

Figure 4. Situation of newly granted FDI projects by investment location (Source: Ministry of Planning and Investment (2022))

4. Vietnam's Tax Incentives and Opportunities - Challenges of the Global Minimum Tax in Attracting Foreign Investment

4.1. Current Status of Tax Incentives for FDI Enterprises in Vietnam

According to the contents of Article 19 of Circular 78/2014/TT-BTC as amended in Article 11 of Circular 96/2015/TT-BTC, FDI enterprises or foreign-invested enterprises are entitled to CIT incentives when implementing new investment projects in industries or areas eligible for investment incentives. Currently, in Vietnam, there are many preferential CIT policies to attract FDI enterprises. FDI enterprises will enjoy preferential tax rates of 10% and 15% with investment encouragement projects such as newly established enterprises operating in the fields of socialization of health, education, sports, agriculture, forestry and fisheries, hi-tech development enterprises, production of new materials, investment projects in the area of environmental protection, projects in supporting industries such as the production of electronic components, leather, and footwear, garment [13,16].

In addition, according to Article 20 of Circular 78/2014 of the Ministry of Finance, as amended in Circular 96/2015, FDI enterprises are also entitled to tax exemption for up to 4 years from the date of commencement of business activities, a reduction of 50% of the tax amount. Taxes must be paid for the next nine years, depending on the industry and investment area.

4.2. Opportunities and Challenges of Attracting FDI When Vietnam Applies the Global Minimum Tax

Participating in the implementation of the global minimum tax is an opportunity for Vietnam to change its strategies to attract FDI; instead of creating conditions to reduce the amount payable to the state budget for FDI enterprises in the first years and increase in the coming years, Vietnam has the opportunity to reform the tax policy system related to FDI to create a stable and sustainable business and investment environment, in line with international practices, contributing to enhancing international integration, creating peace of mind for large investors who are intending to invest in Vietnam. At the same time, applying the global minimum tax will limit transfer pricing and tax evasion, contributing to increasing tax revenues for infrastructure development, human resource training, and technology investment and creating a favorable investment environment for foreign investors when entering Vietnam.

Applying the Global Minimum Tax will also create many challenges for Vietnam. The rule of Global Minimum Tax will affect Vietnam's competitiveness in attracting FDI in the short term because the average income tax rate applied to multinational enterprises is currently around 12.3%, even from 2.75 - 5.95%, much lower than the general regulations. When using Global Minimum Tax, companies may have to pay additional taxes at home, no longer benefit from tax incentives, and lose Vietnam's competitive advantage in attracting foreign enterprises [13]. At the same time, when applying the global minimum tax, there will be costs related to the reform of the tax system and administrative procedures in the field of investment before applying the global minimum tax, while it is uncertain whether this application will generate commensurate revenue and benefits. Therefore, it is necessary to have suitable solutions.

5. Some Solutions to Support Investors when Applying the Global Minimum Tax

5.1. Solutions on Supporting Policies for Investors when Applying the Global Minimum Tax

Firstly, Direct support in investment costs, research and development costs, and supporting the production of products prioritized to attract investment. In addition, to support investment costs in the construction of environmental protection works, emission reduction activities encourage ecological protection.

Secondly, in an economic downturn, it is possible to consider supporting costs related to employee welfare, such as building dormitories, kindergartens, and medical stations serving workers in the industrial zones. In addition, it is possible to consider supporting expenses to reduce production costs, such as supporting electricity bills, transportation costs for workers, etc.

Third, indirect support through incentives for VAT, CIT, fees applied to supporting industries, early promulgation of preferential policies on import and export taxes, taxes related to land, and finance environmental resources…

5.2. Related Solutions

Besides preferential policies, creating a legal corridor and other measures are also necessary to attract FDI into Vietnam, specifically:

Vietnam needs to review soon, update and make appropriate changes to relevant legal regulations (such as the Law on Enterprise Income Tax, the Law on State Budget, the Law on Investment, etc.), adjust preferential policies, and support investment in Vietnam to accommodate the application of a global minimum tax while continuing to create a competitive investment attraction environment in the region.

Second, it is necessary to pay attention to the quality and implementation of institutions, infrastructure, human resources, labor productivity, reform of administrative procedures, drastic reduction of informal costs, etc., instead of applying tax incentives like now.

Third, prioritize solutions to connect FDI and domestic enterprises, focusing on developing supporting industries, diversifying markets, and partners, being strategic and selective to take advantage of opportunities, and limiting concentration and supply chain disruption risks.

6. Conclusion

Imposing a global minimum tax creates many challenges for attracting foreign investment. However, in addition to tax incentives, FDI investors will consider options based on advantages in terms of geographical location, labor, land, and level of economic integration through participation in free trade agreements (FTAs). Therefore, in addition to finding options, new tax incentives help reduce losses for investors when applying the global minimum tax policy. In addition, improving other factors such as administrative procedures, quality of infrastructure, human resources, visa policy, and supply chain also contributes to attracting FDI into Vietnam.

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