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Motives for Multinational Investments & Taxation Incentives in Turkey and China

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Abstract

Title: Motives for Multinational Investments &Taxation Incentives in Turkey and China

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Key words: Investment motives, taxation, corporate tax, incentives ,foreign direct investments, tax system in Turkey, tax system in China

Purpose: The purpose of this thesis is to describe and analyze the motives for investments with special focus on the impact of taxation and implementation of tax incentives in tax systems of Turkey and China .

Methodology : In order to give an answer to the purpose of our study, we have used a qualitative approach .Primary data is collected through interviews.

Theoretical perspectives: The theoretical base depends on the related literature on books , articles and the laws of the both countries. These theoretical contributions are compared and measured by empirical results.

Empirical foundations: The study we present is based on interviews with relevant managers and controllers of private enterprises.

Conclusions : We have detected less discrepancies between the literature on the motives for investments and the motives in the investment decision of the investors .We have detected complementary connections between the identified motives . We have encountered with influence of taxation from NPV and international competition aspects , with the detection of relatively less incoming FDI s in Turkey compared to China. We have identified the compliance of the tax incentives with the described laws, by four companies in two countries.

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1.INTRODUCTION

1.1 Background

FDI (Foreign direct investment) refers to an investment made to acquire lasting interest in enterprises operating outside of the economy of the investor (UNCTAD) .

FDI plays an extraordinary and growing role in global business. It can provide a firm with new markets and marketing channels, cheaper production facilities, access to new technology, products, skills and financing (Graham,Spaulding,2005).

Changes in FDIs' size, form and structure have taken place in the last decade due to some reasons. The sea change in trade and investment policies and the regulatory environment globally in the past decade, including trade policy and tariff liberalization, easing of restrictions on foreign investment and acquisition in many nations, and the deregulation and privatization of many industries, has probably been the most significant catalyst for FDI's expanded role (Graham,Spaulding,2005).

1.2 Problem Discussion

There are many motives for multinationals to find the need to enter in a new market . These motives can be related with the wealth of the country with sufficient purchasing level or GDP , market size ,access to suppliers, better infrastructure , political stability ,lower cost of production , fiscal incentives .In today's world multinationals are making their investment decisions by taking many of these variables into consideration .

Market access depends both on population and income. It is true to say that there are more opportunities for economies of scale in Eastern countries since there is a greater supply of low cost labour and a larger market size (Floyd, Summan,2007).
Another factor is the political and economic stability. In this respect investors in Eastern countries have often cited infrastructure and corruption as being the main barriers to increasing investment activity (Bitzenis ,2006).However, eastern countries governments have been less dictatorial on the choice of entry made available to foreign firms. These changes have had the affect that the motives for foreign investment are becoming similar for both Eastern and Western countries (Floyd, Summan,2007).

Besides, through capital accumulation in the recipient economy, FDI is expected to be growth enhancing through encouraging the incorporation of new inputs and technologies in the production process. The empirical evidence generally suggests that FDI has a positive impact on economic growth in developing countries, as recent surveys by Lim (2001) and Hansen and Rand (2006) attest . Zhang (1999) investigates the causation in 10 East Asian economies in East Asia and Latin America covering the period 1970–1995 and finds that FDI appears to enhance economic growth in the long run for mainland China, Hong Kong, Indonesia, Japan, and Taiwan and in the short run for Singapore .

However , a number of studies laid out further some conditions for the positive affect of FDIs on growth. First, Blomstrom et al. (1994) argue that FDI has a positive grow effect when a country is sufficiently rich in terms of per capita income .

Bengoa and Sanchez-Robles (2003) show that FDI is positively correlated with economic growth, but host countries require human capital, economic stability, and liberalized markets in order to benefit from long term FDI inflows .

Alfaro et al. (2004) draw attention to financial markets as they find that FDI promotes economic growth in economies with sufficiently developed financial markets .

Incentives on taxation granted in a host country is a major factor affecting inflow of FDIs . Through tax incentives , either reductions , exemptions or tax holidays for a period of time on the tax that every company should pay to government out of the profit , is implied. Through this way governments help to FDIs to reduce their costs ,increase their profitability therefore establish better circumstances for them to invest .

All countries, compete against each other over corporate taxes to attract FDI (Azemar,Delios ,2005).Statutory rates of corporation taxes have fallen considerably over the last decade, leading to substantially lower tax rates in developing countries than in developed countries (Azemar,Delios ,2005).

Our second study area is the implementation of tax incentives in tax systems of Turkey and China .In 1991, the laws were simplified and all forms of FDI (foreign equity joint ventures ,Sino-foreign contractual joint ventures and wholly foreign-owned enterprises)were granted the same tax benefits (Tung,Cho,2000). In addition, since 1984, the Chinese government has sought to attract FDI to designated special tax incentive zones and has done so by providing additional tax incentives to FDI in these areas (Tung,Cho,2000). The incentives in China happened to be in the form of tax holiday periods with exemption of the tax payments and reduced tax rates after the tax holidays ;known as preferential tax policy .

In Turkey some similar tax incentives existed with China such as grants on industry specific investments .However two major differences happened to exist. One is the absence of tax preferential policy and the other is the existence of other incentives on business taxes such as on payroll taxes .

1.3 Problem Formulation

We attempt to provide an answer on four questions such as :

-What are the appealing factors in the investment decisions of the investors?

-What is the effect of taxation in the profitability analysis of the investors (NPV) ?and What is the role of taxation in the international competition of the countries through the collected tax revenues by the governments?

-What are the business tax incentives provided for the investors investing in Turkey and China including special treatments ? and if possible can we formulate an example of a payable tax calculation after the profit figure, according to both Turkey and China's tax systems ?

1.4 Purpose

The purpose of this thesis is to describe and analyze the motives for investments with special focus on the impact of taxation and implementation of tax incentives in tax systems of Turkey and China .

1.5 Delimitations

We have chosen to make a case study that involves two respondents from two private enterprises in each of the country , making four in total which constituted mostly disadvantage in laying out the results of the study areas more extensively , such as the first research area ; motives for investments. More than four respondents would have ensured more dimensions . Moreover , we preferred to obtain the results on the motives for investments without supplying a limited number of factors to the respondents and rather by ad hoc query .If we had supplied the alternatives to respondents , they would have evaluated the inquiry with more options and returned us with more factors , enabling us to have the opportunity to produce more comprehensive results on the research of motives for investments.

Regarding the impact of taxation ,information attained from four respondents helped us to produce relatively more generalized results either on NPV consideration of entities or on international competition of countries ,compared to the motives for investments .However, the analysis of the information was planned to be made within the limitation of the literature only , therefore comment of the respondents was not deliberately inquired further , although it could have been .

We have limited our third purpose; description and analysis of the tax incentives in tax systems of Turkey and China , with the related Laws in the theory and same four respondents from four companies .
We have chosen to select the companies from different industries in order to present different incentives received due to different business properties they possessed. Of course if the respondents were more than four , more alternatives on incentives could have been laid out however the presented theory covered already the regulations extensively .
It should be kept in mind that this research area of our study is based on the various regulations disclosed within the Laws therefore the results derived from four respondents' remarks contributed less to the theory due to the less probability they contain for diversion from the Laws. In other words , because it is about the Tax Laws ,it is more likely that the empirical research resulted in the confirmation of the Laws in terms of applications and less likely to suggest the readers a different dimension. Therefore more than four respondents would not contribute much to the presented theory either , only in this study area.

Furthermore we have made the research within the managers and business controllers and not with the investors although this study mainly concerns about them .However , respondents managed with investment projects .

1.6 Target Groups

This thesis is aimed for all people interested in the motives for an investment decision from an investor point of view. Moreover we target investors or managers & controllers dealing with investment projects in the private and public entities who are thinking of making new investments in Turkey and China .We also target interested researchers and people in the university .We have chosen to establish the information of two countries' tax systems under a classification of the issues with the related headlines from Laws in order to include everybody who has not encountered either with any tax related issue on business or a Tax Law.

1.7 Definitions & Clarifications

We assume we have managed to write our thesis in a simple and clear language with the details of the implications in order not to leave any question in any of the reader's mind. However , despite this fact there might occur some puzzles especially on some frequently used abbreviations such as :

FDI s : Through out the thesis the term will be used for Foreign Direct Investments.
CIT : Indicates Corporate Income Tax ; however mostly will be used as unabbreviated .

2. METHODOLOGY

2.1 Research Approach

We have decided to employ qualitative research approach in our thesis due to the properties of the qualitative approach that we think fits more than the quantitative approach.
Qualitative researchers can consider a high variety of theoretical frameworks which stem from the vast domain of disciplines in both the social and natural sciences (Tavallaei and Abu Talib ,2010). According to Clissett (2008) ,qualitative research covers a wide range of approaches for the exploration of "human experience, perceptions, motivations and behaviors" and is concerned with the collection and analysis of words whether in the form of speech or writing.
Frey, Botan, and Friedman (1992) have also argued that qualitative data take the form of words rather than numbers. Qualitative data are analyzed and presented in the form of case studies, critiques, and sometimes verbal reports (Frey, Botan, and Friedman ,1992).
Denzin and Lincoln (2005) have argued that qualitative research is a situated activity that locates the observer in the world. It consists of a set of interpretive, material practices that make the world visible. These practices transform the world. They turn the world into a series of representations, including field notes, interviews, conversations, photographs, recordings and memos to the self. At this level, qualitative research involves an interpretive, naturalistic approach to the world (Tavallaei and Abu Talib ,2010).

On the other hand Hyde (2000) , makes a key distinction between qualitative and quantitative approaches and declare "Quantitative approach to research might draw a large and representative sample from the population of interest, measure the behaviour and characteristics of that sample, and attempt to construct generalizations regarding the population as a whole .Qualitative methodologies, however, seek to explain the particular. Rather than seeking to reach a general profile regarding the study population, the qualitative study must provide conclusions which account for the particulars of every case."

We have preferred to employ qualitative approach to interpret the particular based on motivations and experiences of the individuals in the form of words such as interviews.

2.2 Reasoning behind the Approach

There are two general approaches to reasoning which may result in the acquisition of new knowledge, namely inductive reasoning and deductive reasoning.

Inductive reasoning is a theory building process, starting with observations of specific instances, and seeking to establish generalizations about the phenomenon under investigation. Deductive reasoning is a theory testing process which commences with an established theory or generalization, and seeks to see if the theory applies to specific instances (Hyde ,2000).

We have chosen deductive reasoning behind the qualitative approach to test the particular if it fits with the theory .However we could have chosen the inductive reasoning either.
While quantitative researchers generally subscribe to a deductive research process, and qualitative researchers generally subscribe to an inductive process, both fields of researchers employ deductive and inductive processes in the practice of their research(Hyde ,2000).
Patton (1991) argues that the qualitative researcher can adopt both inductive and deductive processes.

We have preferred deductive reasoning in our research due to the need we saw for the introduction of the theory first ; in particular for the theory of implementation of the tax incentives in Turkey and China.

On the other hand ,Haruvy and Stahl (2001) mention about an advantage that deductive reasoning carries on the mitigated potential of a pre-set mind as follows: It is important to recognize, however, that their underlying dynamic process occurs in the mind of the player before the first period of play, and so is independent of empirical histories in a given game (Haruvy and Stahl ,2001). During our research , we tried to be as neutral and not guiding in our questions as much as we can however we presume we managed this point in the last study areas more than the first area of motives for investment ,due to the nature of the first area that encouraged us to question reviewed motives in order to expand the limited replies that we had guessed would be given.

2.3 Working with a case study

We have used case study for the research of our study areas. In explaining what a case is, Yin (1989) suggests that the term refers to an event, an entity, an individual or even a unit of analysis. It is an empirical inquiry that investigates a contemporary phenomenon within its real life context using multiple sources of evidence (Yin, 1989).

We assumed a case study would ensure a better understanding of the presented theory .
Yin (2008) argues that the case study research needs identification of the theoretical perspective at the beginning of the investigation because it affects the research questions, analysis, and interpretation of findings.

Qualitative inquiry often takes the form of a case study. Case study is simply an in-depth study of a particular instance, or a small number of instances, of a phenomenon (Hyde ,2000). Noor (2008) and Flyvbjerg (2006) draw attention to the advantages of case study as follows: Case studies become particularly useful where one needs to understand some particular problem or situation in great-depth, and where one can identify cases rich in information (Noor ,2008).

Flyvbjerg (2006) claims that a case study contains no greater bias toward verification of the researcher's preconceived notions than other methods of inquiry. On the contrary, experience indicates that the case study contains a greater bias toward falsification of preconceived notions than toward verification (Flyvbjerg ,2006).

Another advantage is that case study can be useful in capturing the emergent and immanent properties of life in organizations and the ebb and flow of organizational activity, especially where it is changing very fast (Hartley, 1994) .

2.4 The method for the case study

Generalization is an act of reasoning that involves drawing broad conclusions from particular instances -that is, making an inference about the unobserved based on the observed (Polit and Beck, 2010).Generalizing to a theory or conceptualization is a matter of identifying evidence that supports that conceptualization (Firestone ,1993).
The goal of most qualitative studies is not to generalize but rather to provide a rich, contextualized understanding of some aspect of human experience through the intensive study of particular cases (Polit and Beck, 2010).

However there are other researchers who support generalization.
Ayres et al.(2003) observed that, "Just as with statistical analysis, the end product of qualitative analysis is a generalization, regardless of the language used to describe it".
Even a single case, if studied in sufficient depth and with sufficient insight, may provide the basis for a theoretical explanation of a general phenomenon (Hyde ,2000).
Yin (2003) also entertains the possibility of generalizations being made in qualitative research. He refers to such generalizations as representing replication logic, which is similar to that used in experimental studies.
Without generalization, there would be no evidence-based practice: research evidence can be used only if it has some relevance to settings and people outside of the contexts studied (Polit and Beck, 2010). According to Flyvbjerg (2006) ;one can often generalize on the basis of a

single case, and the case study may be central to scientific development via generalization as supplement or alternative to other methods. But formal generalization is overvalued as a source of scientific development whereas "the force of example" is underestimated (Flyvbjerg, 2006).

In our thesis , we did not intend for generalization in any study area of the research .We focused on making an analyze by a comparison of the replies of different respondents and by an analogy between the replies and the presented theory. Even in the results complying to the presented theory we tried not to make a generalization attempt. However we believe that it mostly depends on the reader or to the tendency to make a generalization by the reader.On the other hand , in our second study area which is the tax incentives implemented in Turkey and China , we believe a generalization for the entities carrying the same properties with the respondents, can be made due to the attribute of that research area which takes it's roots from regulations that applies equally to the target groups. Therefore we support that depending on the research specific topic, generalization can be made sometimes in the results which would reveal more reliability of the theory .

2.5 Choice of Interviewees

We incorporated a case study consisting of foreign investors investing in both of the countries to test either the motives for investment ,significance of taxation among these motives and tax incentives described in tax systems of two countries .
In order to do so we have selected four foreign enterprises ; two from Turkey and two from China to hold an interview . Companies from China take their places among biggest medical care enterprises around the world with manufacturing activity ;Abbott and Novo Nordisk these are ; while companies from Turkey operate in chemistry and textile industries with importation and manufacturing respectively ;Lord Chemicals and Delta Galil Co. these are. We made the interviews with one manager from each company , making four in total.
These managers were ; from Abbott in China ,a project manager , from Novo Nordisk in China a business controller , from Lord Chemicals in Turkey an area manager and from Delta Galil in Turkey a general manager .We intended to find the investors to hold the interviews however due to the difficulty it contained we decided to proceed with some top managers who were dealing with investment decisions either through the projects and the business they were carrying out or the area they have been responsible from .

We made all the interviews in English , therefore no translation was needed to be done.

We asked the same questions to all the respondents because there was no need for asking different questions for conducting our research.
We made the interviews via e-mails. We did not receive the answers back right after 15-20 minutes we sent the questions but rather in one or even two weeks time after we sent them .We had assured the respondents that we had sufficient time so that they would not have the need to hurry up for quick answers. Therefore we guess , the reason it may have taken 1-2 weeks time for receiving the answers was not due to our long list of questions but rather due to a free time we allowed them to have .

2.6 The criticism of the method

We preferred structured interviews in our case study . Structured interviews can also be used as a qualitative research methodology (Kvale & Brinkman, 2008).
There are some features of the structured interviews. These are : All respondents are asked the same questions in the same way.[1] There is a formal relationship between the researcher and the respondent with the latter knowing exactly what is required from them in the interview. [2]
However ,in the semi-structured interview ,it is generally beneficial for interviewers to have an interview guide prepared, which is an informal "grouping of topics and questions that the interviewer can ask in different ways for different participants ”(Lindlof and Taylor, 2002).

For structured interviews ,it is relatively quick and easy to create, code and interpret (especially if closed questions are used). [3] For structured qualitative interviews, it is usually necessary for researchers to develop an interview schedule which lists the wording and sequencing of questions (Patton,1991) .
On the other hand it is just the opposite for the semi-structured interviews which are generally organized around a set of predetermined open-ended questions, with other questions emerging from the dialogue between interviewer and interviewee (Noor ,2008).

We used structured interviews because (a) we asked all the respondents the same questions in the same way under a formal relationship between us and interviewees. (b)we used closed questions without “how” and “ why” s, prepared before the interviews in a sequence .(c)we did not add any question later other than the planned ones .
The reason we preferred structured interviews with closed questions was that the information we were seeking mostly was in the answers in response to our questions of “what” , such as

1 http://www.sociology.org.uk/methsi.pdf

2 http://www.sociology.org.uk/methsi.pdf
3 http://www.sociology.org.uk/methsi.pdf

what the motives or the tax incentives were for the respondents. We almost had not even one "how" and " why" question when we planned our questions to ask and we believed also it would be unnecessary to add "why " or " why not" questions during the interviews either , as it would not fit to our research purpose .However we support that semi-structured questions with open questions can be more efficient depending on the research type in particular for more detailed researches.

Interview schedules are sometimes considered a means by which researchers can increase the reliability and credibility of research data (Lindlof and Taylor, 2002).

Besides there is another reason for us to assume that closed questions would be better for our study , which is the availability it would provide us to make a comparison between the companies in Turkey and companies in China that we aimed also in our thesis other than revealing some facts specific to these countries. These types of interviews are best suited for engaging in respondent or focus group studies in which it would be beneficial to compare/contrast participant responses in order to answer a research question(Lindlof and Taylor, 2002).

Moreover we have chosen to hold the interviews via email although we were concerned that face –to –face interviews would be more efficient to collect the necessary data .However due to the fact we preferred closed questions , we believed emails would help us to gather the same data received by face-to –face interviews. We did not consider making phone interviews at all due to the probability of a misunderstanding or a lack of understanding. We requested to have the answers back again via emails.

3. FRAMEWORK

3.1.INTRODUCTION TO INVESTMENTS

3.1.1.Motives for Investments

Why do companies invest overseas ? Companies invest overseas to increase their overall profitability .

There are several reasons for foreign direct investments (FDIs) however; four basic reasons for companies establishing subsidiaries in foreign countries are : obtaining natural resources, protecting or expanding sales in lucrative markets, seeking low-cost production for an export platform, or acquiring strategic assets (Cohen ,2007).Geographic location is related to business objective.

Those countries with the world's best-paid workers—the United States, Canada, Germany, France, the United Kingdom, the Netherlands, and Switzerland—dominate the list of largest recipients of FDI, whether measured as percentage of GDP or in absolute terms (Cohen ,2007). These countries are the principal actors in a vigorous economic cycle with: high wage levels, rising productivity, increasing consumer buying power, and robust economic growth.

The world's top 30 host countries account for 95 per cent of total world FDI inflows and 90 per cent of stocks. The share of China and just the next four largest recipients (Hong Kong, Singapore, Mexico, and Brazil) is 58 percent of all FDI (Cohen,2007). With recorded direct investment inflows exceeding $50 billion in the early 2000s, China alone has been taking more than 30 percent of the annual FDI total .Additionally same nine countries (the United States, the United Kingdom, France, Germany, the Netherlands, Switzerland, Japan, Canada, and Italy) accounted for 84 percent of the $7.3 trillion in total outward FDI stock owned by developed countries (Cohen,2007).

Globerman and Shapiro (2002) argue that the same factors should have an impact on both inward and outward FDI .

Depending on whether government policies are encouraging or discouraging , unbiased or discriminatory , the volume of the inflowing FDI s may differ. Companies are concerned to go into politically stable ,transparent markets where there are nondiscriminatory, honest institutions with clear regulations as well as private enterprises under free prices in the host country.

Labor cost is only one of the several components of total production costs; raw material and transportation costs are the others. Priorities in labor force characteristics differ between efficiency-seeking investors trying to minimize costs of producing labor-intensive goods and market seekers trying to increase sales of high value-added goods in prosperous markets (Cohen,2007).

Tax is a question that investors has to consider as a factor increasing the costs ,lowering the profitability hence carrying the potential to lead to unprofitable investments .Fiscal incentives reduce a foreign corporation's tax liabilities by means of any or all of the following: reduction in the standard corporate tax rate, tax holidays in which corporate income taxes are deferred for a number of years, accelerated depreciation allowances, tax credits for reinvestment of profits, and exemptions in either corporate income or employee payroll taxes .

The second category of financial incentives consist of non repayable subsidies that can reduce the cost of land acquisition ,construction, or factory equipment purchases. The third category of incentives include ;modernized or expanded transportation and telecommunications infrastructure, subsidized power and water, exemption from import duties on raw materials and capital equipment, preferential access to government contracts, closing the domestic market to future direct investment by competing foreign companies, and preinvestment feasibility studies (Cohen ,2007).

According to the survey done with access to customers; by 77 percent of the 191 responses received; other widely cited influential factors, in descending order of importance, were a stable social and political environment, ease of doing business, reliability and quality of physical infrastructure (transportation, telecommunications, and utilities), ability to hire technical professionals, ability to hire management staff, level of corruption, cost of labor, crime and safety, ability to hire skilled laborers, corporate tax rates at the national level, costs of utilities, and quality of roads (Cohen,2007).Identified by less than 25 percent of respondents as very influential factors were access to raw materials, availability and quality of university and technical training, available land with connected utilities, local taxes, access to suppliers, labor relations and unionization, and air freight and passenger service(Cohen,2007).

When considering possible sites, Ericsson, the Swedish-based multinational telecom equipment maker, has said it attaches greatest weight to market size, quality of the bureaucracy, quality of infrastructure (including customs clearance procedures), the tax system, trade policies, level of political risk, production costs including labor, and the availability of suitable contractors and suppliers (UNCTAD World Investment Report).

3.1.2. Investments in developing Countries

Indicators of LDC s (less developed countries) are ; per capita GDP, average level of education, and life expectancy.[4]

Statistics have shown that many of the least developed countries to this day have received negligible FDI .There is more symmetry than meets the eye when it is noted that the largest recipients of FDI have an approximately equally large share of the GDP, employment, and exports of all countries (Cohen ,2007).

A host country's internal conditions are a decisive factor in corporate decisions on where to invest and what kind of manufacturing facility to build. Multinationals choose to locate in enhancing economies; where favorable economic conditions with higher growth rates convince foreign-based companies to establish subsidiaries in a developing country.

According to Borensztein et al. (1998) ; the effect of FDI on growth depends on the level of human capital in the host country, where FDI has positive growth effects only if the level of education is higher than a given threshold.

Using data on 80 countries for the period 1979–98, Durham (2004) fails to identify a positive relationship between FDI and economic growth, but instead suggests that the effects of FDI are contingent on the “absorptive capability” of host countries .

Balasubramanyam et al.(1996), using cross-country data for a sample of 46 developing countries, find that trade openness is crucial for acquiring the potential growth impact of FDI. On the other hand, their estimates indicate that FDI has stronger effects on growth than domestic investment, which may be viewed as a confirmation of the hypothesis that FDI acts as a vehicle of international technology transfer.Foreign companies create relatively high-paying jobs, bring with them advanced levels of technology , possess value added products or services and educated management staff which all affect the growth of the economies of developing countries .They can alter the economical balance in an incoming country in a positive way on behalf of the citizens of a nation through the cash flows generated .

UNCTAD, the only major global economic organization ,stated in its World Investment Report for 1999 that “FDI can play an important role in complementing the efforts of national firms to improve a country's international competitiveness. ”

Therefore there is another point we have to emphasize which is about the mutual relationship between the FDIs and growth or whether one causes another and which one it is.

[4] http://www.unohrlls.org/en/ldc/related/59/

Nair-Reichert and Weinhold (2001) examined the relationship between FDI and growth and found ;given that rapid economic growth usually generates higher demand and better profit opportunities for FDI, a positive correlation can also be compatible with causality running from growth to FDI .
By using data on 80 countries for the period 1971–95,Choe (2003) detects two-way causation between FDI and growth, but the effects are more apparent from growth to FDI.
"The cointegrating vectors reveal a bidirectional causality between GDP and FDI for more open economies. For relatively closed economies, long-run causality appears unidirectional and runs from GDP to FDI, implying that growth and FDI are not mutually reinforcing under restrictive trade and investment regimes" (Basu, Chakraporty and Reagle,2003).
The empirical results of the research done by Li and Liu (2004) suggest the following :FDI may have a positive impact on economic growth leading to an enlarged market size, which in turn attracts further FDI. Given the possible interdependency of these two variables, there is a need for a proper test of endogeneity. In our sample, endogeneity was not detected in either the first half or whole sample period, but occurred in the second half thus showing FDI and growth becoming increasingly interdetermined in relatively recent years (Li and Liu ,2004).
Finally , according to the empirical evidence derived from a sample of 31 developing countries for the period 1970–2000, Hansen and Rand (2006) indicates that FDI has a lasting impact on GDP, whereas GDP has no long-run impact on FDI. They also find that a higher ratio of FDI in gross capital formation has positive effects on GDP. Hansen and Rand (2006) interpret this finding as evidence in favour of the hypotheses that FDI has an impact on GDP via knowledge transfers and adoption of new technologies .

Therefore ; the results from these bilateral causality tests are mixed as Li and Liu (2004) states .They suggest that ; "This again indicates that the relationship between FDI and economic growth is far from straightforward. It varies across countries and time periods."

On the other hand for China that has a special role in FDIs ;Hsiao and Shen (2003) find a feedback association between FDI and GDP in their time-series analysis of the data from China ; whereas Xiaohui et al.(2002) use quarterly data for China from 1981 to 1997 and find cointegration as well as bi-directional short-run and long-run causality between FDI and GDP

According to UNCTAD data, FDI as a percentage of total capital flows to LDCs rose from 6 percent in 1980 to 60 percent in 2000. The book value of FDI in developing countries jumped from an estimated $302 billion in 1980 to $2.4 trillion in 2004 and to $4.9 trillion in 2009. [5]

[5] http://unctadstat.unctad.org/TableViewer/tableView.aspx

3.1.3. China Example

China, as already noted, is by far the largest recipient of FDI among emerging market countries and in most recent years has been the second largest destination (after the United States) for direct investment flows. However the conditions for investment in 1980s were very different from the present time.

"The country holds the reputation in the United States and elsewhere of being the world's most prolific and brazen violator of foreign companies' intellectual property rights. Some foreign companies have discovered partners illegally selling counterfeit versions of products produced by their joint ventures. In the early years, it was common for Beijing to demand that foreign companies team up with a local partner and transfer up-to-date technology .Yet another negative factor is China's banking system being insolvent by Western standards because of extensive nonperforming loans. The country's physical infrastructure is viewed as being woefully inadequate with clogged roads, trains, and ports delaying shipments and causing unacceptable increases in production costs "(Cohen,2007).

Chinese government recognized the immense need of the foreign investments in the country for a more developed economy that would enable the raise of the living standards of it's 1.3 billion people and started to take actions for the sake of this purpose.

China remained as a socialist , largely state-owned market economy .The country began to attract FDIs with the establishment of special economic zones in the early 1980s.These zones with the grant of fiscal privileges ,made the start of the private market economy .By the second half of the 1990s, China's partial acceptance of market economics had opened up the country to trade extensively.[6]

China attracted FDI s with various incentives such as : tax incentives granted foreign enterprises with several years of tax holidays and reduced tax rates following tax holidays , extremely low-wage labor with absence of unions, improved infrastructure and duty free imports.

"The China price" ; with a meaning of extremely lower prices made it a very irresistible factor for FDI s to enter in China market .It affected the competition between the foreign companies in all over the world through the aspiration it created for MNCs to invest in the country for more profitable businesses.

[6] http://www.chinability.com/FDI.htm

Few major manufacturing companies anywhere in the world could ignore China's rapid growth with the potential of its consumer market and increasing number of foreign companies establishing subsidiaries .

The country received annual FDI flows of $92.4 billion and invested abroad with a total outward FDI of $52.2 billion , in 2008 [7]. Most of this increase was in the form of overseas acquisitions by companies partly or wholly owned by the government. China's increasing outward direct investments have come in two forms: resource-seeking, mainly in developing countries, and market- and asset-seeking, mainly in high-wage industrialized countries (Cohen ,2007).

“The Chinese government encourages local enterprises to make positive moves overseas because the rise of China as a major economic power is dependent upon the evolution of Chinese companies into world-class enterprises ” explained a senior Chinese executive.

3.2.THEORY ABOUT INVESTMENTS RELATED TO TAXES

3.2.1. International Competition to attract investments through tax incentives

Firms incur additional costs with overseas investments in addition to their home investments.Operating in the home country is less costly than investing abroad due to the firm’s familiarity with the legal and cultural factors in the domestic economy.

According to Panteghini ‘s (2007) assumption the representative firm can decide whether to invest immediately (thereby exercising its option to expand) or wait until new information on the state of the world has been gathered on how costly it is for the firm to shift income from one country to another and whether the present discounted value of future profits is less than the net discounted cost of investment or not . Indeed, FDI would be unfeasible for low-income firms, i.e. for those firms who incur losses from international activities irrespective of the quality of the news received.

Reduction in technical barriers such as national standards and other factors lower investment costs such as transportation costs leading to a rise in average profitability .

However increased volatility affects profitability in an adverse way and must be compensated by higher profits (Panteghini, 2007). In particular, Chen and So (2002) showed that the 1997 Asian financial crisis (which caused an increase in exchange rate variability) discouraged FDI undertaken by US MNCs. Further evidence is provided by Aizenman and Marion (2004), who focused on the foreign operations of US MCNs since 1989. They showed that uncertainty affects both vertical and horizontal FDI s. In particular, they showed that greater supply

[7] http://www.chinability.com/FDI.htm

uncertainty reduces the expected income from vertical FDI but increases the expected income from horizontal FDI. Greater demand uncertainty adversely affects the expected income under both production modes. Moreover, volatility and sovereign risk are shown to have a greater adverse impact on vertical FDI than on horizontal FDI (Panteghini, 2007).

According to Panteghini's model ,in order for the firm to invest abroad at time 0, profits must cover the effective tax-inclusive cost of investing abroad plus the value of the call option to expand. High-income firms would invest abroad at time 0 irrespective of the existence of the option to delay. Thus, a firm can shift profits to low-tax countries, thereby raising its after-tax profitability .It is thus necessary to investigate how taxes are set in order to attract FDI when firms can time their investment decisions and countries compete to attract resources.

Therefore the first argument which deserves attention is that if investment costs fall and/or profitability rises, the number of firms that undertake FDI will increase.

Secondly Panteghini (2007) claims in his model that ,each government maximizes the welfare function by the sum of taxes on overall gross profits for MNCs with a home base country plus tax revenues from subsidiaries located in home base country of MNCs . The maximization of is part of a sequential game, where at stage 1 each government sets its tax rate; at stage 2, the firms in country decide whether to invest at time 1 or at time 2. Therefore from governmental point of view , he builds an assumption as follows :A rise in FDI s leads to a rise in the equilibrium tax rate , widens tax bases and, if it is high enough, an increase in tax revenue.

At third, Panteghini (2007) takes a further approach as follows: a decrease in the cost of shifting profit decreases the equilibrium tax rate and vice versa.According to this proposition , a decrease in investment costs makes income shifting less costly and thus stimulates tax competition: this induces the governments to set a lower tax rate.

Last proposition is on the increase in the volatility of a country specific shocks that lowers the equilibrium tax rate , and reduces tax revenue.The reasoning behind this proposition is as follows : An increase in volatility induces firms whose profits at time 0 are in the interval to delay. At time 1,however, only a fraction of the firms who delayed will receive good news and then invest. The remaining firms will decide not to invest . Therefore volatility reduces the overall number of firms involved in FDI activities. The governments' policy response is thus to lower the tax rate in order to partially alleviate the negative impact of increased volatility (Panteghini, 2007).

Moreover, the reduction in the number of MNCs leads to a drop in the sum of all firms' tax bases. Therefore, both the reduced tax rate and the narrower aggregate tax base leads to lower tax revenue .

These findings may help to explain why, despite the fact that tax rates for large samples of countries are declining, it is however possible to find countries where the tax on capital has risen. The fall in tax rates fits with the interpretation that, under some circumstances, the globalization process may raise volatility (Panteghini, 2007).

On the other hand according to Panteghini (2007) ,tax policy uncertainty arises either when a government announces a tax rate change which will not be implemented after (i.e., the future tax rate is unknown but remains constant) or when an unexpected tax change takes place (i.e., the tax rate is unknown and variable) .It is worth noting however that firms are usually aware that the government can undertake actions different from those initially planned and try to anticipate its tax choices. This commitment failure leads to the well-known "capital levy problem" (Panteghini, 2007), which is related to the fear that a government can decide to raise taxes on capital already invested.

The capital levy problem deserves particular attention in an international setting. As pointed out by Mintz (1995, p. 61): "When capital is sunk, governments may have the irresistible urge to tax such a capital at a high rate in the future. In other words governments may wish to take actions in the future that would be different from what would be originally planned". As pointed out by Eichengreen (1990), if the delay between proposal and implementation of the levy is substantial, capital mobility could make this additional tax burden ineffective.

It is worth noting that the existing literature accounts for both investment irreversibility and (policy) uncertainty in a foreign country where a representative MNC can decide whether and when to invest abroad.

3.2.2. Taxes in line with NPV

Taxes should be included in the analysis of investment projects since they affect profitability. Imposing business income tax for FDIs is to impose tax on business operation revenues , that is to be deducted from the company's profits ,hence reducing the FDIs' net revenue. If the business income tax is low or free, it will encourage the FDIs while high tax rate will suppress FDIs.

The influence of taxes on the profitability of investment projects is affected by several factors, including: the form of the tax laws; the legal form of the company (in particular whether it has limited or unlimited liability); and the perspective from which the appraisal is made (particularly whether from the perspective of the company or the shareholders). (Götze , Northcott &Schuster ,2008)

In addition the following assumptions can be made:

• The company pays profit-dependent tax at the same time as the profit is reported: at the end of each period.

• Tax payments are proportional to the profit made.

The consideration of the assessment of investment projects by the investors is illustrated using generally the net present value (NPV) (Götze , Northcott &Schuster ,2008).

According to Götze , Northcott &Schuster (2008) ,the NPV calculation requires two additional steps to account for taxes:

• The original cash flow profile must be modified by payments directly resulting from taxation.

• The uniform discount rate must be adjusted to recognize the effects of tax paid on the yields of alternative (financial) investments.

For example, if an alternative project yields a 10% pre-tax return and the company's tax rate is 30%, the relevant after-tax yield is 7% (i.e. 10% – 10% · 30%) (Götze , Northcott &Schuster ,2008)

In the tax-adjusted NPV model, the same decision rules apply as for the basic model that does not consider taxes. As a rule, the consideration of taxes changes the value of the NPV calculated. This may lead to different absolute and/or relative profitability results. For example, an investment project may or may not be profitable with inclusion of taxes (NPV > 0) (Götze , Northcott &Schuster ,2008). Such changes in profitability can be explained by two effects. On the one hand, a negative effect on NPV typically arises because the net cash flows are lower due to tax payments. On the other hand, the smaller tax-adjusted discount rate acts to increase the NPV (Götze , Northcott &Schuster ,2008).

It should be noted that only profit-dependent taxes that are proportional are considered. Moreover, the rate of taxation is not always constant.

3.3. FACT OF SOCIAL SECURITY AND EMPLOYEE INCOME TAXES

3.3.1.Contributions of Social Security and Employee Income Taxes

We should mention now a little about how things work in real life for employees and employers , how they are taxed , who carries the tax burden , what we see in payroll of the employees.

Elscher and Schweger (2005) explain the application clearly as follows:
Social security charges and payroll taxes add a noticeable amount to the tax wedge. The contributions to the general public social security system are levied together with the personal income tax. For a firm located in a region which taxes labor more heavily than others, this requires to increase the gross income before taxes and social security contributions payable by the employee so as to compensate for the high charges (Elscher & Schweger, 2005).

Gross income is usually the quantity being negotiated and written down in the labor contract. (Elscher & Schweger, 2005).For this reason, gross income mostly serves as the base for calculating income tax and social security liabilities paid by employers the on behalf of the employees under employee's taxes.

Income after taxes, that is, the amount of money the individual can spend for his own consumption or saving. This is the disposable income of the employee.

In all countries, the employer also has to pay charges on the employee's gross income, e.g., employer's contributions to social insurance or special payroll taxes . Thus, total expenses of an employee consist of disposable income, employee's taxes as well as employer's taxes based on the employee's income. (Elscher & Schweger, 2005).
When deriving disposable income from gross income, we deduct all taxes relevant with the employment .

Income tax schedule is generally based on income brackets with a constant rate applying to each bracket. Rates are likely to start with 15% and can rise up to 35-40% with increases of 5 percentage points depending on the gross income level. In other words it results in a strong increase as one passes from the low to the standard level of disposable income. (Elscher & Schweger, 2005).

A high payroll tax therefore increases the total remuneration required in order to achieve a given disposable income. With a fixed disposable income, the expenses necessary to remunerate a highly skilled worker are the higher, the higher the tax wedge (Elscher & Schweger, 2005) .Thus, the higher the EATR (The Effective Average Tax Rate), the less attractive is a country or region for companies employing highly qualified employees. Or, to express it from the perspective of the company, the higher the EATR, the more the employer has to spend in order to compensate an internationally mobile employee. Symmetrically, a high EATR of one country does not mean that the highly skilled employee has a lower disposable income than in other countries with low EATRs (Elscher & Schweger, 2005).

Contributions by employer and employee to company pension plans are invested in the period of remuneration into pension plans and yield interest (Elscher & Schweger, 2005). Together with contributions from other periods during working life they result in pension payments during retirement. In other words, at the end of his working life the employee has capital at his disposal which results from all previous old-age contributions. This capital has to be distributed over all following years of retirement to secure the living standard. Usually, the resulting annual pensions are calculated as annuities (Elscher & Schweger, 2005).

4. STATE AID ON TAX TREATMENTS IN INVESTMENTS IN TURKEY

Tax , being one of the most significant aspects of the economic activity ;plays an important role in collection of revenues and development of an economy .It is a remarkable financial tool to conduct macro-economic regulation which does not affect only economic development but also relates to every enterprise and citizen by its three main features : being compulsory, free of charge and stable.

Corporation income tax is a tax levied on the profits of the enterprises' through their business operations with the aim of distributing wealth between state and enterprises.
The regulation entails from Corporation Income Tax Law in Turkey (Law No.5520).

Here is a list of corporate tax income figures in Turkey through years 1994- 2009.

(Unit:Million TL)

Year	Total of Taxation Income	Corporation Income Tax	Rate %
1994	534	44	8,2
1995	1084	103	9,5
1996	2244	189	8,4
1997	4745	396	8,3
1998	9232	749	8,1
1999	14.802	1550	10,5
2000	26.503	2357	8,9
2001	39.736	3676	9,3
2002	59.632	5575	9,3
2003	84.316	8645	10,3
2004	101.039	9619	9,5
2005	119.254	11.402	9,6
2006	151.271	12.447	8,2

2007	171.099	15.718	9,2
2008	189.980	18.658	9,8
2009	196.313	20.702	10,5

Before we start with different investment incentives provided to different industries ,on different tax types we should mention about the current tax rates which will be subject to either discounts or exemptions in the proceeding sections .

Corporate income tax rate in Turkey is 20% (fixed and independent of any industry or corporation specific), that is rather lower than most of the European countries .

Social security employer premium is decreased 19,5% to 14,5 % in general independent of any industry or cooperation specific .Therefore the mentioned discounts or exemptions are implied to be applied over these rates .

Social security employee premium is 14% with a base applied.

Social security unemployment employee premium is 1% , while social security unemployment employer premium is 2%.

Income tax on employees starts from 15 % for the minimum taxable income bracket and increases 5 % in each of the rising taxable income segment , reaching maximum up to 35%.

4.1. REGIONAL/LARGE SCALE INVESTMENTS

Due to the policy of the government which aims to urge investments for sustainable economic development , more employment opportunities and enhanced international competitiveness ; several types of tax exemptions and discounts based on various type of investment projects such as regional, local, foreign industry or zone based investments are identified .
We will begin with incentives on regional investments , then go on with support for local firms with foreign affiliates ,support for foreign entities and then finish with the support for industry based investments .

The purpose of this decision (regional support) in Development Plan and Annual Program with the proposed objectives in accordance with international agreements is ; to direct the savings to higher value added investments, to increase production and employment, to ensure continuity of investment trend and sustainable development, to encourage and support large – scale investments with larger content of technology ,research, development and environment protection facilities that will increase international competitiveness, to expand foreign direct investments and to eliminate regional disparities.[8]

In the Law[9] for implementation of investment support ;regions are divided into four groups by their socio-economic development level in accordance with each of the city's investment potential and competitiveness .

In order for an investment to obtain the advantages from the regional support issues ,minimum fixed investment value in regions I and II should be one million Turkish Lira ,whereas in regions III and IV it should be five hundred thousand Turkish Lira .

Investments that will be made through financial leasing companies ; total values of machines and equipments that are subject to financial leasing should be minimum two hundred thousand for each of the financial leasing companies.

Additionally within the same Law[10] , conditions and incentives for large scale investments are identified as follows:

a) Large scale investment: investment over 50 million Turkish Lira[11] ,

b) Incentive Certificate: Investment incentive certificate,

c) Investment property: Fixed expenditures like all kinds of machine ,equipment , plant and furnishing dependable on the type of investment excluding building and land that will be utilized for the production of goods and services within the incentive certificate ,

are as defined.

Investments that will benefit from the regional support can get use of the ; corporate tax reduction, social security employer premium and investment location assignment while in large scale investments Vat exemption [12] is included among these elements .

Now we will review social security employer premium support , corporate tax reduction and assignment of investment location for both regional and large scale investments .

4.1.1.Social Security employer premium support

For the large scale investments and investments that receive the support of regional incentives , social security employer premium on minimum wages of employees declared in the monthly

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[8] Decision Date:14.07.2009 (Updated)

[9]Dated 28.08.2002 ,Law No 4720 (Added-1 of Territorial Units for Statistics in Categories)

[10] Law No 4720

[11] As additionally stated in Corporate Income Tax Law 5520 , article 32/A

[12]Vat Exemption refers to the value added tax ; that importation and local deliveries of machines and equipments will be exempt from (within the Value Added Tax Law no of 3065).

premium declaration to the Social Security City Management, is subsidized by the Treasury for the periods mentioned as below:

Investments started until 31/12/2010

Regions	Periods
I	2 years
II	3 years
III	5 years
IV	7 years

Investments started after 31/12/2010

Regions	Periods
I	-
II	-
III	3 years
IV	5 years

For the entities getting use of these supports , within the content of this decree no additional premium support can be applied .

4.1.2.Corporate Tax Reduction

For the large scale and regional investments, based on CIT (Corporate Income Tax Law) [13] , reductions that will be applied in corporate income tax with regard to contribution of government to investments are as below ;

	Regional investments		*Large Scale investments*	
Regions	Rate of Contribution to Investment (%)	Corporate Income tax Reduction (%)	Rate of Contribution to Investment (%)	Corporate Income tax Reduction (%)
I	10	25	25	25
II	15	40	30	40
III	20	60	40	60
IV	25	80	45	80

In other words; the government grants a contribution to the investments as in specified rates according to regions ,and also a reduction as in specified rates from corporate tax , however does not grant both ,allows only reductions to go on until the total value reaches to investment contribution rate .For example in region 1, if a company invests 1.000.000 ytl ,it will get a subsidy of 100.000 ytl (1.000.000*0.10=100.000) by reductions from taxes .If a tax to be paid appears to be 60.000 ytl in the first year , it will pay 45.000 (60.000-60.000*0.25=45.000) and will go on to have reductions in following years, until 85.000 (100.000-60.000*0.25=85.000) ytl is covered.

[13] Corporate Income Tax Law No.5520 article (32/a)

4.1.3.Assignment of Investment Location

Based on the Law [14] , for the large scale investments and investments that will get use of the regional supports within the incentive certificate prepared by the Ministry, investment locations can be assigned under the conditions and methods specified by the Fiscal Ministry . Investments can be transferred to other regions under the permission of the Ministry and the support condition of the investment in the regions they aim to be transferred ,if only they are activated in the location they take place initially for minimum five years following the start of the business .

4.2. EXEMPTION ON AFFILIATES

Besides from the large scale and regional investments that are subject to special incentives ; there are some other articles in either the same law (CIT)[15] or in different laws regarding for foreign investments of Turkish companies or multinationals' investments in Turkey .
We will begin with Turkish investments abroad and go on with the incentives provided for foreign investments in Turkey.

Exemption means exclusion of real or corporate individuals' income from taxation through laws. Exemption can be temporary or continuously .Institutions that are exempt from taxation are not responsible for submitting tax declarations. An institution's exemption of corporate taxes does not affect the bookkeeping , book approving or other duty and accountabilities .

Exception is about the special items that are kept out of taxation .

Corporations with their legal or business centrals located in Turkey are considered as " full fledged taxpayer" and are taxed over their income made in Turkey and foreign countries .

Corporations with both of their legal or business centrals are not located in Turkey are considered as " foreign-based taxpayer" and are taxed only over their income made in Turkey. Examples to these entities are ; capital stock companies ,cooperatives, representatives, organizations, parties, societies and associations .

4.2.1. Exemption of Foreign Affiliate Earnings

According to CIT Law[16] ; local institutions with commercial , agricultural or professional earnings (except the ones with the main facility subject of financial leasing and securities) that affiliate with 10% or more percent to the capital of the entities' that do not locate in

[14] 29/6/2001 dated , Law No 4706
[15] Corporate Income Tax Law No.5520 (KVK 5520 in Turkish)
[16] Corporate Income Tax Law No.5520 (KVK 5520 in Turkish) Article 5/b

Turkey legally and as of business centers, for at least one year until the profit is made ,are exempt from corporate income tax if they transfer their earnings related to relevant taxation period to Turkey until the submission date of the corporate income tax declaration .Legal or business centers of these affiliates should carry at least 15% corporate income tax burden in the located countries .

Through this article , first profit share from the foreign affiliate is added to the profit made in Turkey subject to submission , then corporate income tax on profit of foreign affiliate is aimed to be deducted from the corporate income tax payable in Turkey .
By this exemption of foreign affiliate earnings from taxation; foreign earnings is aimed to be transferred to Turkey .

Additionally gains from the sales of buildings that are kept at least two or more years are exempt from corporate income tax.[17]

On the other hand for the local companies , income made from construction ,repair and technical services performed in foreign countries (without having an affiliate)and transferred to general final accounts in Turkey ,are exempt from corporate tax .[18]

4.2.2.Exemption for foreign entities with affiliates in Turkey

Earnings that institutions (foreign) gain through affiliates to full fledged taxpayers' (pls see above) capital ,are exempt from corporate income tax. [19]
In order to get use of this exemption , the profit share gained through the entity , the affiliate in other words must carry the obligation of being a "full fledged taxpayer ". Therefore entities receiving a profit share through foreign –based taxpayers will not get the advantage of this exemption .Here , the taxpayer type of the entity receiving the profit share is of no significance. However it shall not mean the entity arising from the association is not liable for tax payment. It rather means the foreign entity's (subject to the joint venture) activity is exempt from taxation. For example Carrefour is a French origin supermarket chain company and Sabanci is a Turkish origin group company .They have built an association through an affiliate under a name CarrefourSa in Turkey. Here in Turkey, CarrefourSa is a taxpayer for corporate taxes , however Carrefour is not liable for tax payments.

[17] Corporate Income Tax Law No.5520 (KVK 5520 in Turkish) Article 5/e
[18] According to CIT Law No. 5520 Article 5/h
[19] According to CIT Law No. 5520 Article 5/a

4.3. OTHER LAWS ABOUT EXEMPTIONS ON INVESTMENTS

4.3.1.Investment Discount [20] :

Investment discount is a system that puts a part of the fixed assets out of taxation through deducting a specified portion (40%) from the profit subject to tax (since 01.01.2006).

Lands are not taken into investment discount .Economic properties that are subject to investment discount will loose their property in case they are sold out before 2 years .

Investment discount is started in the year of the expenditures made .The discount value can not exceed the 25% of the profit (after all deductions).Exceeding amount will be subject to the discount in the following year .Therefore to calculate the deductable value ;

First ,discounts on expenses made in prior years but transferred to current year due to exceeding amount ,

Secondly, discounts on investment expenditures of current year ,

At third , discounts calculated on expenditures that are aimed to be made in the following year ,

have to be taken into consideration.

For example a company purchasing a machine to use in their production for 100.000 ytl , will have the opportunity to deduct 100.000*40% =40.000 ytl from the current year profit unless 40.000 ytl exceeds the 25% of the current year profit.

4.3.2. Tax exemption in Extraordinary State Regions with priority for development [21]

Until the end of 31.12.2007 ,profit made by entities in specified 11 cities (increased to 22 later) ,will be subject to calculated corporate income tax discount for 5 taxation periods including the investment period , under the condition of employing physically and permanently 10 or more labor in these entities .

Discount Rate ;

Employers with 10 labor force : %40

Employers with 51 and more labor force : %60

The law is then updated for investments that not have fulfilled completion until the end 2007 , and allowed for the discount further on.

[20] Based on ; Income Tax Law No. 193, article 19

[21] Based on Law No .4325

4.3.3.Tax exemption from production facilities based on software,research and development in technology development regions [22]

Profit made from the production facilities based on software and R&D in technology development regions , is exempt from the corporate income tax until 31.12.2013, independent from the facility start date .

4.3.4.Tax exemption on the income gained in free zone regions [23]

According to the Free Zone Law [24] , income of the entities gained through the facilities performed in free zone regions is exempt from the corporate income tax within the period specified in their certificate .

Exemption is related with the facilities performed in free zone areas. Therefore , income of taxpayers in free zone regions , gained through the facilities in business place, branch, legal or business centrals out of the free zone area ,is not within the exemption content .

According to the Free Zone Law , salaries paid by the taxpayers to the personnel employed in the free zone areas are exempt from employee income tax until 31.12.2008. However if their certificate includes time period after this date , they are allowed for further exemption.

4.3.5. R&D Discount [25]

According to CIT Law[26] , 40% of the research and development expenditures based on new technology and information research , will be calculated as R&D discount and be discounted in the tax declaration . CIT Law is then amended with 100% exemption of the expenditures with an extended date until 31.12.2023 with another Law .[27]

The difference of this Law from the Law on R&D facilities in technology development regions (reviewed in section 4.3.3.) is that, this incentive is granted to every type of taxpayer in their business place .

Additionally ,80% of employee income taxes is exempt from taxation.

R&D facilities end in the process of final attempts and first production. From the point R&D product becomes marketable , R&D project can be considered to have finalized. Expenditures made after this date can not be considered within R&D content .

[22] Based on Law No .4691
[23] Based on Law No .3218
[24] Based on article 3 .The law was specified initially as of 06.02.2004 , but later it is extended with law no 5810

[25]Based on Law No .5746
[26] Corporate Income Tax Law No. 5520 Article 10/1/a
[27] Law No .5746

Meanwhile facilities with the intention of the aims specified below will be considered as R&D facilities:

-To obtain new technical information that will enable science and technology development with the aim of removing the ambiguities in scientific and technologic fields .
-Research and development of new productions ,methods, process and facilities with the aim of developing new products, goods , materials, tools, instruments, facilities and systems .
-Research of technology and new techniques that will decrease the cost of a product, increase the quality ,standard and performance .
-Software facilities based on new and original designs.

Research expenditures related with market search , sales promotion, quality control or start up costs in the first establishment process ,will not be considered within the R&D facility content.

4.4. OTHER IMPORTANT TREATMENTS ON TAXATION

4.4.1. Prior year losses

Losses incurred in prior years can be deducted from the entity's current year profit for at most 5 following year [28]. Prior year losses should be deducted in the first accounting period available for deduction. In case they are not deducted ,the taxpayers will loose their right for the further periods .

4.4.2. Legally not accepted expenses

Legally not accepted expenses are the expenses that are not allowed for deduction from the income , therefore constitute a disadvantage in terms of tax calculation . These expenses are ;

1- Profit distributed to board members and head .
2- Losses arising due to stealing , getting lost or fraudulent activities.
3- Expenses that are not related with the income earned by the entity
4- Expenditures without invoices or receipts
5- Insurance premiums that are not paid
6- Donations to institutions that are different than the ones specified by the law.
7- Expenses that do not belong to current accounting year
8- Expenses recorded double
9- Expenses related to exceptional earnings
10- Provisions for employee indemnities
11- Vat on expenses above

4.4.3. Donations

Conditions for deducting donations and aids from the profit before tax are ;

Donation and Aid ,

- Should be made to the entity and institutions specified in the Law ,
- Should be made in return of a receipt ,
- Should be made without any return ,
- Can be in cash or material ,
- Should belong to the related accounting period .

Donations to governmental institutions i.e. educational , scientific , military or health institutions can be deducted 100%.[29]

[28] Corporate Income Tax Law No. 5520 Article 9/1/a
[29] Corporate Income Tax Law No. 5520 Article 10/1/d/10

4.5. EXAMPLE TO CORPORATE TAX CALCULATION

Here we will examine an example of a Turkish company for it's corporate tax calculation after the profit figure appeared in it's profit/loss statement .

Profit and loss statements happen to calculate the companies' profit or losses through deducting all expenses from the total of all income figures .
Income figures mainly generate from income from sales, however income such as interest income, rental income, dividend income ,donation income or other income are also included in the total .
Similarly, expenditures contain all kinds of expenditures such as marketing expenditures, general administration expenses or financial expenditures , however other expenses such as extraordinary expenses are added to the total either.
Deducting all the expenses from total of all income figures gives us a company's either profit or loss figure .If the figure is positive , there is an income still at the end that implies to a profit and if the figure is negative , it shall imply expenses are bigger than the total of incomes ,with a meaning of loss figure .

In the example we will review the company incurs a profit and we will go beyond that figure in order to calculate the corporate tax amount the company has to pay .
Normally corporate tax rates are determined independently by every country government according to their fiscal or monetary policies and they are fixed and unchangeable for any company operating within the country . As we have reviewed the tax rate in Turkey is 20% and the tax amount our company will pay can simply be calculated with 20% of the profit.
However there are some specific advantages granted by Turkish government as our thesis focus on this chapter .These advantages refer either discount or exemption of some income items from the final profit figure in order to reduce the profit figure subject to tax thus to lower the payable tax amount.
These incentives may refer to specific gains such as income from free zone, technology development or extraordinary regions or facility generated income such as R&D gain or affiliate income as we have examined in this chapter and we will see in our example .

Prior year losses if existed are always deducted from the current profit figure regardless of the mentioned incentives .
On the other hand ,when we initially mentioned about the profit figure calculated as all expenses deducted from the total of all incomes we did not separate the legally not accepted expenses which should be separately considered in the tax calculation .

The content of legally not accepted expenses are defined in this chapter , in section 4.4.3 with the specific properties they should contain .These expenses are not allowed to be deducted from the total of income items.However they take place among all the expenses (to be deducted) thus in the corporate tax calculations the first thing to do , is to add back these expenses to the profit figure (which is a disadvantage for the calculation of tax amount).

It is the same for donations which is a part of legally not accepted expenses that is deducted first among other expenses and added back later . However there are deductable donations defined by the law as we have seen in section 4.4.4 ;therefore they should be deducted again (after addition) if they fit to the properties for deductable donations .

Now we will examine a Turkish company as an example for corporate tax calculation .
The key point is to make the calculation and deductions in the order specified by the law .
First of all we will present this order .

1. Corporate Profit
   - Balance sheet profit /loss

2. Additions (+)

   - Legally not accepted expenses

3. Profit / Loss after Additions (1+2)

4. Exceptions and discounts even if in the case of loss

   - Affiliate earnings

   - Gains from portfolio on investment funds and partnerships

   - Gains from foreign construction and repair Works

   - Gains from the sales of affiliate shares and buildings

   - Gains made in free zone areas

   - Gains made in extraordinary regions with priority of development

   - Gains made in regions of technological development

   - R&D discount

   - Other discounts (Exceptions taking place in international agreements and from the sales and running of the ships registered in International Turkish Shipping)

5. Profit /Loss after exceptions (3-4)

6.Prior Year Fiscal Losses (can not be higher than the income after exceptions)

7. Profit /Loss after deductable prior year losses (5-6).

8. Exemptions and and discounts to deduct in case of a profit (-)

- Donations and aids to educational and health institutions and related with dormitory constructions
- Donations and Aids with the aim of Culture and Tourism
- Expenditures of Sponsorships
- Investment Discounts
- Other discounts

9.Profit subject to Corporate Tax (7-8)

Example: Data related to COKMEZ Construction Company (Turkish) as of 2005 is as follows: 1. Balance sheet profit	800.000 YTL
2. Legally not accepted expenses	65.000 YTL
3. Investment Discount (truck purchased to the factory at 13.5.2005 , according to income tax law article 19 , 100.000 YTL x %40=)	40.000 YTL
4. Foreign Construction work gain :	85.000 YTL
5. Affiliate Gain from company Hizir	20.000 YTL
6. Gain from sales of buildings	25.000 YTL
7. Gain from free zone area	300.000 YTL
8. Donation to dormitory institution for student dormitory construction :(with 100 bed capacity)	50.000 YTL
9. Taxes paid during the year through stoppage	10.000 YTL
10. Paid provisional tax	40.000 YTL
11. Total Prior Year Losses Losses due to exceptions in 2004; 5.000 YTL -Other Losses10.000 YTL	15.000 YTL

According to these data corporate tax will be calculated as follows:

Balance sheet profit 800.000 YTL

Legally not accepted expenses 65.000 YTL

-Dormitory institution donation..50.000
- Other……………………… 15.000

Affiliate Gain	20.000 YTL
Foreign Construction work gain	85.000 YTL
Gain from sales of buildings	25.000 YTL
Gain from free zone area	300.000 YTL
Total of profits and additions	865.000 YTL
Current Year exceptions and discount Total	430.000 YTL
Profit	435.000 YTL
Total Prior Year Losses subject to deduction	15.000 YTL
Amount subject to exemptions	420.000 YTL
Donation for dormitory construction	50.000 YTL
Investment Discount	40.000 YTL
Total	90.000 YTL
Current year profit (subject to corporate tax)	330.000 YTL
Corporate income Tax (Profit x %20)	66.000 YTL
Taxes paid during the year through stoppage	10.000 YTL
Paid provisional tax	40.000 YTL
Total deductable taxes	50.000 YTL
Corporate income tax that should be paid	16.000 YTL

5. STATE AID ON TAX TREATMENTS IN INVESTMENTS IN CHINA

Tax is an important method for the governments to participate in income distribution (Zuo Liu, 2010). In the construction of national economy the governments collect tax to gather capital in order to meet the need for public goods and economic development (Bifeng Long, 2010).

Tax legislation is an irreplaceable method for the state to adjust and control the tax revenues. The adjustment and control of revenues through tax is ensured by the government's political power by imposing various rates of taxes that aim to redistribute national income, alter the material benefits and encourage or stop some kinds of social and economic activities (Yin Wen, 2006). If the tax is imposed without the law and evidence governments cannot have the right to impose tax and people cannot be imposed for the duty to turn in tax ,therefore the implementation of such rights and duties according to relevant tax laws is a process for the government to adjust and control tax revenues (Yin Wen, 2006).

Through the tax system that has been under a reform for five times in recent years, China has established a tax policy adjustable to the socialist market economy that has been playing a positive role (Bifeng Long, 2010). The regulation for Corporation Income Tax take it's roots from Corporation Income Tax Law. In the tax system of China, it is the second largest tax source (following VAT).

Here is a list of corporate tax income figures in China from 1994 to 2007.

(Unit: Billion)

Year	Total of Taxation Income	China Corporation Income Tax	Rate %	Foreign Corporation Income Tax	Rate %
1994	507	63	12.62	4.8	0.95
1995	597	75	12.61	7.4	1. 24
1996	705	81	11.51	10.4	1. 48
1997	822	93	11. 33	14.3	1. 74
1998	909	85	9.42	18.2	2.01

1999	1031	100	9.79	21.7	2.11
2000	1266	144	11. 41	32.6	2.57
2001	1516	212	13.99	51.2	3.38
2002	1699	197	11. 61	61.6	3.62
2003	2046	234	11. 44	70.5	3.45
2004	2571	314	12.22	93.2	3. 63
2005	3086	436	14.14	114.7	3.72
2006	3763	554	14.74	153.4	4.10
2007	4944	772	15.62	195.1	3.95

In September 1980, the first law of Corporation Income Tax was made by the Chinese government with a tax rate of 30%. According to new laws a revised standard tax rate of 25% is applicable to Chinese and foreign firms beginning from 2008.

Regarding other taxation rates in China , for the pension insurance the rate for the enterprises paying the pension insurance fee normally should not be over 20% of the total wages of the enterprises. The rate for employees shall be 8% of the wages at maximum.

For the basic medical insurance the employers should pay the fee about 6% of the total wages of the units and the employees should pay the fee equal to 2% of the wages of the employees.

For the unemployment insurance the enterprises should pay the fee at 2% of the total wages of the enterprises and the employees should pay the fee at 1% of their wages.

There is additional industrial injury insurance with the base of the total wages of the employee units subject to calculation with the average rate around 1%.

The tax on an individual's income is progressive. As at 2010, an individual's income is taxed progressively at 5% - 45%.

5.1. REGIONAL/SMALL & MEDIUM SIZED INVESTMENTS IN CHINA

In China there are also regions according to different socio-economic levels of development with investment potential and competitiveness of the cities in each of them . However ,apart from the administrational laws in China there are regulations set by the local provinces like;

Local regulations and rules: Based on the specifications of jurisdiction ;the People's Congress , it's Standing Committee and relatively large cities may enact local regulations under the conditions that they are not in conflict with the Constitution, Laws and administrative regulations (Zuo Liu, 2010).
Autonomous regulations and single regulations: Based on the political, economic and cultural features of the local regions; the People's Congress of the autonomous localities has the power to make autonomous regulations and single regulations.

For the income tax payable by the enterprises under the autonomous jurisdictions, the autonomous department of the autonomous regions may sanction the tax reduction or exemption on the part shared by the jurisdictions.

Minimum investment amounts are not set as a condition for regional investment incentives .

Within the application of this law ;
a) Operation form:Operation incentive form ,
b) Investment property: Fixed expenditures i.e. all kinds of machine ,equipment , plant and furnishing depending on the type of investment excluding building and land that will be utilized for the production of goods and services within the operation form ,
are as defined.

5.1.1.Social Security employer premium support

Unlike Turkey , regional incentives on social security taxes are not given.
However the administrative practices are varied in the implementations of the social security contributions throughout the country. It is observed that the application of those rules is varied from city to city. For instance in Shanghai, the municipal government has not required the employer to pay work-related injury insurance except for the employees without household registrations. In cities of Shenzhen and Beijing, the applicable rates for work-related injury are varied depending on the type of industries and the level of risk at the workplace.

5.1.2.Corporate Tax Reduction

According to the Law [30] there are special incentives provided by the local provinces to the foreign investments which maybe different than the government incentives . These incentives include either exemptions or discounts or both of them with some specific tax treatments like

[30] Circular 40 released by the State Council

“ three free, three half ” with a meaning of corporate tax exemption of three years and a half tax payment of another three years .

For instance for the high –tech enterprises in five national economic development zones (Shenzhen, Zhuhai, Shantou, Xiamen, and Hainan Hainan) and in Shanghai’s Pudong district ;from the first year the company generates income, the first two years of income will be exempt from CIT (corporate income tax) and tax will be removed 50% (be at 12.5%) for the next three years. After that, 15% rate for the new high-tech enterprises will apply.
A significant example to regional corporate income tax incentive is as follows:
Intel Co , a famous information technology company has been transferred to other Chinese cities ; Wuhan and Dalian after a while from the activity in Shanghai . The cities of Wuhan and Dalian are China’s major cities and the Chinese government proclaimed a "five free and five half" tax incentives to Intel for its arrival to Wuhan and Dalian (National Taxation Bureau, 2004).

Secondly in some other special zones a reduced 15%-24% corporate income tax is applicable to foreign direct investments with an available corporate income tax refund on reinvestment.

Additionally for the small and thin-profit enterprises the tax is reduced to 20% according to the Law.[31] However an article [32] in the implementation regulations sets these conditions out as follows:
a.For industrial corporations, annual income should not exceed RMB 300,000, there should be fewer than 100 employees and total assets should not exceed RMB 30 million.
b. For non-industrial corporations, annual income should not exceed RMB 300,000, there should be fewer than 80 employees, and total assets should not exceed RMB 10 million.

5.1.3.Assignment of investment location

For the investments that will get use of the regional supports within the operation form prepared by the State, investment locations can be assigned under the conditions and methods specified .
They can be transferred to other regions under the permission of the Ministry and the support condition of the investment property in the regions they aim to be transferred .

[31] CIT Law Article 28
[32] Article 92

5.2.EXEMPTION ON AFFILIATES

In China ,the enterprises are in two types: resident enterprises and non-resident enterprises.

Non-resident enterprises are the enterprises established under foreign laws , with their place of effective management outside China but have organizations or establishments or representative offices within the territory of the People's Republic of China (PRC).These enterprises should pay the corporate income tax only on their China sourced income (Zuo Liu, 2010).
Resident enterprises are the enterprises established in China under PRC laws or established under foreign laws but has its place of effective management in China .

5.2.1. Exemption of foreign affiliate earnings

The resident local enterprises should pay the corporation income tax on their worldwide income therefore there is no exemption of taxation to Chinese companies on the income they make through foreign affiliates .

5.2.2. Exemption / Discount for foreign entities(residents) in China

Foreign taxation is to impose tax on the income, wealth and other operating activities for the foreigners in China. The sound foreign taxation policy is not only about bases for some tax revenues but also it has a special role in the open-up of a country. It has an important role in attracting foreign capital , enhancing participation of the companies to international competition; controlling the import and exports, protecting national industry , increasing competency and the national economic development. Mostly, the anti-tax-avoidance clauses in the mentioned policies are to guarantee for a healthy open-up (Hai Lian, 2007).

At first we should mention about preferential tax rate which is the most widely used policy tool to encourage investment in developing countries. Tax free period also known as tax exemption is one special form of preferential tax policies and it is usually practiced by developing countries to promote capital investment. The most common way of the application is the corporate income being completely or partially freed from tax in the official engagement of business. This can last for several years. When the tax exemption is over, tax should be paid on the basis of regulated tax rates.

In 2010, the tax exemption that Chinese government provided to Intel plant in Shanghai for six years, has been officially over. Six years ago, when Intel just settled plant in Shanghai, the Chinese government provided Intel Co. one preferential tax policy called "Three free and three half". "Three free and three half" policy means corporation income tax of 25%tax rate has been completely freed in the former three years, and removed half in the later three years. So Intel Co. has delivered relatively small amount of tax to the Chinese government during its operation in Shanghai for six years, which dose a big favor to increase income. By now, since the Chinese government's tax incentives are ceased , Intel Co. has abolished the production plant in Shanghai...

For the manufacturing foreign direct investments five year tax holiday prevails .
Extension of tax holidays to export-oriented foreign direct enterprises is granted.

Tax preferential policy that establishes a relation between enterprises and local economical development is of great importance from the business point of view. However, there exist some unsolved questions in the preferential tax rate. Since the preferential tax rate can not be changed with the change of investment, it's not the most effective tool to use preferential tax rate in the provision of investment. To solve the problem there is an other tool of investment incentive.
Secondly our topic is tax credits and deductions on investments.
A deduction is to deduct income from the total earnings subject to income tax, its effect is similar to tax credits. The corporation income tax is based on the taxable income.
The taxable income equals to the balance of the gross income (profit) minus the non-taxable income, tax-free income, all kind of deductions. The applicable tax rate is 25%.
The tax may be free for the income of interest from the State bonus, the equity investment income of dividend, bonus between the qualified resident enterprises and non-profit making organization revenues .Further will be provided in the corporate tax calculation example .

Non-resident enterprises have no establishment or place in China , and are taxed over their China sourced income like" foreign-based taxpayer " in Turkey ; however unlike Turkey a benefit granted for non –resident enterprises which is the applicable tax rate of 20%(instead of 25%) for the income obtained by non-resident enterprises (Zuo Liu, 2010).

5.3. OTHER LAWS ABOUT EXEMPTIONS ON INVESTMENTS

5.3.1.Investment Discount

In order to encourage for investment , Chinese government allowed some companies in certain industries to deduct their cost of purchasing fixed assets ,in the name of tax credits. Deductions depend on the operation forms that are divided into two ; direct and indirect investment . The former means investment in commercial assets such as acquiring operational assets and establishing new companies. Indirect investment refers to financial investment of corporate shares and bonds .

5.3.2.Tax exemption from production facilities for high –tech companies

China imposes 15% income tax for foreign investments in special hi-tech industry zones , 24% tax for southern developing cities and 33% for elsewhere.
What's more for those manufacturing FDI s enjoying the lower tax rate is that, they can also enjoy the "Two Years Free Three Years Half", or "Five years Free, Five Years Half " preferential tax policy.

5.3.3.Tax exemption for dock and harbor construction industry

In China , for the companies engaging in dock and harbor construction with an operation period of 15 + years, tax preferential policy of "Five-years Free; Five-years Half" applies beginning from the year the company begins to make profits ,under a tax rate of 15% after the half tax payment period of second five years .

5.3.4. R&D Discount [33]

Companies incurring R&D (research and development) costs that meet the requirements can enjoy certain tax incentives by a certain percentage on the basis of technology development policy. R&D expenses are deductible in the year they are incurred. Meanwhile such companies also enjoy tax refund on re-investing of their profits.

5.3.5 Tax exemption for agriculture,forestry and the livestock industry[34]

Another industry is agriculture, forestry and the livestock industry where preferential tax policy applies with the condition of an operation period over ten years . "Two Years Free ,Three Years Half" policy applies where the first two years are free of business income tax and following three years are charged with half of the normal tax rate. For those industries under no preferential tax policy business income tax is levied on 33% rate with no tax-free and no tax-discount periods .

5.3.6 Tax exemption for animal husbandry, fishery, environment protection, water saving and energy saving industry [35]

Animal husbandry, fishery, environment protection, water saving and energy saving industries are granted with corporate tax exemption in the first three years of operation and a discount of 50% tax for the subsequent three years, starting from the year the project first generates operating income. These reductions apply only to income generated by these specific projects, not to the entire income of the company.

[33] Circular 49
[34] According to Article 27 of CIT Law
[35] Based on Article 27 of CIT Law

5.4. OTHER IMPORTANT TREATMENTS ON TAXATION

5.4.1.Interest Income Exemption

The interest income is tax exempted for those foreign investors according to Chinese tax law.

5.4.2.Prior year losses

The losses incurred in the current year may be carried forward to the future for a maximum of five years. Prior year losses should be deducted from corporate profit in the first accounting period available for deduction.

5.4.3. Non –deductible expenses

The following expenditures shall not be deducted in the calculation of taxable incomes:

1. Investment gains paid to investors, such as share interest, dividends, etc,

2.Provisions,

3. Overdue charges of taxation,

4. Fines, and losses caused by properties confiscated,

5. Expenditure in the form of donation beyond what is specified in the law,

6. Sponsorship expenses of a non –advertising nature and not relevant to business operation,

7. Management fees between enterprises,

8.Rental and royalty fees paid between business units,

9. Other expenditures that are not related to the obtaining of income

5.4.4.Donations

Charitable donations incurred by an enterprise are allowed to be deductible up to 12 percent of the total annual accounting profit.

5.4.5. Accelerated Depreciation

Rapid amortization of fixed assets known as accelerated depreciation is allowed to be listed as cost ,lowering income subject to tax much more than the straight amortization thus carrying an advantage for the taxpayers. Accelerated depreciation is seen as a way of large subsidies the government provides .

5.4.6. Multilateral tax agreements

Many multi-national companies sign multilateral tax agreements to benefit from a stable tax rate for several years.

5.5. EXAMPLE TO CORPORATE TAX CALCULATION

Here we will review a foreign company example in China in order to display a corporate tax calculation set according to Chinese laws.

Same specific rules apply here like in the example in the chapter for Turkey.
The company we will review incurs a profit with total of incomes higher than the expenses leading a positive profit figure after deducting all the expenses from the total of incomes.

Corporate tax rate is 25% in China like we reviewed and here we will see the deductions of some gains from the profit ,granted by the Chinese government like we examined in this chapter , in order to lower the tax base for the foreign companies .
There are some common gains to deduct from the profit according to both Turkish and Chinese systems like R&D discounts or investment discounts . However there are also different applications like gains made in technology development regions . In Turkey when the profit is exempt from corporate tax , in China preferential tax policy is applied for these companies with a reduced corporate tax rate further from some tax free and half tax payment years.
Furthermore as two countries' laws and specifications differ from each other , here we will see some additional income generated gains to deduct from the profit , such as interest income ,dividend income or non profit making organization revenues like we reviewed in this chapter in section 5.2.2.

Previous year losses are deducted from the current profit in China either, as reviewed in 5.4.2., irrespective of deductable gains .

On the other hand same treatment for non-deductible expenses apply here and added back to the profit as they are not allowed for deduction that constitutes a disadvantage for the company. If they are checked to fit to deduction properties later, they are deducted again .

Now we will examine our example of a foreign company in China .
Similarly the key point is to follow the order of deductibles as specified by the Chinese Law.
We will begin with presentation of this order .

1. Corporate Profit
    - Balance sheet profit /loss

2. Additions (+)

    - Non-deductible expenses

3. Profit / Loss after Additions (1+2)

4. Exceptions on Non-taxable income

- Financial subsidies
- Government funds

5. Profit/loss after exceptions (3-4)

6.Exemptions on Tax-free income

- State bond interest income
- Corporate dividend income
- Non-profit making organization revenues

7.Profit/loss after exemptions (5-6)

8.Deductions to deduct in case of a profit (-)

- Donations and aids made for charity purpose
- Expenditures of Sponsorships
- Investment Discounts
- R &D discounts
- Other discounts

9.Profit /loss after deductable deductions (7-8)

10. Losses carried forward from previous years (can not be higher than the income after deductions)

11.Profit subject to Corporate Tax (9-10)

Example: Corporation data (Unit: RMB)

Example: Data related to a resident foreign hi-tech company in China is as follows: 1. Balance sheet profit	800.000
2. Donations made out of charity purpose	30.000
3. Income from Government funds	55.000
4.Income received from a public hi-tech company	100.000
5. Dividend gain received from the partner co.	25.000
6.State bond interest income	20.000
7. R&D expenditures	40.000
8. Donation to a public hospital for welfare increasing purpose	20.000

9. Fixed asset investment	60.000
10. Total Prior Year Losses	10.000

According to these data corporate tax will be calculated as follows:

Balance sheet profit	800.000	
Non-deductible expenses		50.000
- Donations made out of charity purpose………………………30.000		
-Donation for charity purpose ……………………………….20.000		
Income from Government funds		55.000
Total of profits and additions		850.000
Total of exceptions		55.000
Profit		795.000
State bond interest income		20.000
Dividend gain received from the partner co.		25.000
Income received from a non-profit company		100.000
Total of exemptions		145.000
Profit after exemptions		650.000
Donation to a public hospital for welfare increasing purpose		20.000
Fixed asset investment		60.000
R&D discount		40.000
Total of deductions		120.000
Profit after deductions		530.000
Total Prior Year Losses subject to deduction		10.000
Current year profit (subject to corporate tax)		520.000

Tax reduction or credit (Corporation income *10%)	52.000
Corporation income tax to be paid (Corporation income * 25% - Corporation income * 10%)	78.000

This is a foreign high-tech company resident in China ,in hi-tech industry zone , earning a tax incentive of a 10 % or liable to pay tax at the rate of 15%.

Moreover high –tech companies have the advantage of receiving a preferential tax incentive policy with a “five free, five half” method enabling the company exempt from corporate taxes for the first five years , carry the tax burden for the first year of the next five years with a figure of 65.000 (520.000*0.25=130.000/2=65.000) under a rate of 12.5% , and pay a tax figure of 78.000 (under 15% rate) if these figures happened out to take place in the 11 th year of the company.

6. EMPIRICAL FINDINGS

6.1. Case study for the motives for investment decision

6.1.1.Appealing Factors

We begin with inquiring the investment reasons for the four companies in both of the countries . Both of the medical companies in China displayed the market , the large number of population for making investment with a production facility in basic human need and consumptions in health care sector. According to the project manager in Abbott in China;

"*Abbott Company is pluralistic medical care company. Our products include Drugs, nutritional supplements, medical devices and diagnostic equipments. People use our products from birth to dead. The important point is China has large number of population and clients. China's large medicine market is our investment reason. "*

while the business controller from the Novo Nordisk in China supported the idea as ;*" China has large number of diabetics, comes second after India globally. This urgent demand is the main reason we wanted to invest here .Our goal is to fight against diabetics. we are also the first medicine company who has built an R&D center in China, since Beijing is an important part of our global R&D strategy."*

Authority from the Lord Chemicals in Turkey went on as ;
"*As being one of the biggest emerging markets in the world with its young population we have decided to invest in Turkey."*

while the general manager from the Textile company in Turkey said *;" Turkey is a large and dynamic market with young generation and perfect geographical position."*

6.1.2. Influence of geographic location

We went on with the extent of the importance of the geographical location for their investment decisions in both of the countries .
Lord Chemicals in Turkey answered as ; "*We can say that Istanbul is located in the center of the world which gives you a geographic advantage to make business with companies in Europe, Asia and Middle East."*
Delta Galil in Turkey replied as ;" *It is important to have the advantages of location . We are satisfied because we are in free zone ."*

For both of the medical companies in China ,geographical location holded an important factor for their investment decision due to the low transportation cost .

Abbott in China stated as;"*Our investments spreaded in various cities in China like Shangai,Beijing, Guangzhou, Nanjing, Xiamen, Hangzhou, , Wuhan, Shenyang and Shenzhen in order to serve the local market better due to large number of population and our location choice depended on also to the harbor cities . We were firstly set up in Shanghai in 1998, and then had a new factory in Shanghai in 2006 .Shanghai is a seaport city .It has convenient establishment and makes transportation easy also for exportation."*

While Novo Nordisk in China told *;"Our headquarter is Beijing, and we also set up regional centers, such as Shanghai, Tianjin, Guangzhou, Wuhan, Shenyang and Hongkong. Based on these centers, our market network in China has been established. Nevertheless, location is a factor that influences our investment decisions. We have to consider the cost and potential profit when we take a decision."*

6.1.3. Influence of low costs

We then wanted to inquire about the significance of the low costs in both of the countries especially low labor costs .

The Chemical company area manager in Turkey points out ;" *As Turkey is not a EU member, importation of raw materials from EU countries will be subject to VAT. Importation of raw materials from countries other than EU countries may be subject to customs tax.*
Labor costs in developed cities such as Istanbul, Izmir, Ankara, Bursa etc..is lower than European countries but much higher than Asian companies. Manufacturing companies are supposed to be located in Eastern part of Turkey in which they can make benefit of investment incentive and the labor cost significantly decreases when compared to West part."

The general manager from Delta Galil Textiles in Turkey supports the importance of the low labor costs with an addition ;"*Turkey has lower costs and we know that it is a big advantage .We are pleased for our investment here also for low raw material costs."*

Both of the medical companies in China agreed on the importance of the low costs for investing in China." *China has unique advantage in this aspect. The cost here is much lower compared with in DK. This is also one of the main reasons we came here* " said the authority from Novo Nordisk.

According to Abbott, "*Labor costs are very different by different locations. Our Shanghai factory has to pay more salary than other cities in China. But the salary is lower than US. Transportation costs decreased as well due to the better infrastructure now compared to the* *past time we entered to the market first .China showed a big progress and is continuing on to its progress."*

6.1.4. Influence of stable government policy

Later we continued on inquiring the satisfaction level of all the four companies on the stability of the governments of the two countries as we had seen that it came in the top five reasons for investments.

According to the Lord Chemicals in Turkey *;" Privatization plays a big role in recent years and quite a lot of foreign companies have invested in Turkey especially in Real Estate and Energy markets. And Turkish government encourages foreign investors to take part in privatization which is the fastest way to bring foreign capital to the country."*

The manager from the Textile company in Turkey asserts as ;" *There is a strong government in Turkey with stable policy ,regulation and institutions ."*

Project manager from Abbott in China declares as ;"*Chinese government has been undertaking some changes and improvements on industrial policy, regional guide, and regulations.";*

while for Novo Nordisk *;"Reform and opening-up is the developing strategy for the Chinese government. They had endeavored to attract more foreign investment and gave foreign investors special treatments. We appreciate their effort and this helped to our business."*

6.1.5. Influence of taxation

We then moved on with the extent of the influence of taxation in their investment decisions Abbott in China declares as ;"*Tax rate is a crucial element when we make decisions but not the only one .We expect more to invest in a country like stability of the politics, labor costs, access to suppliers and raw materials , quality of physical infrastructure , skilled labor..";*

when Novo Nordisk business controller in China says ;"*Low tax rate can reduce the cost and make us more competitive ."*

The area manager in Lord Chemicals in Turkey tells;" *It is effective , when you learn it is lower it urges you more to come here ." ;*

while Delta Galil general manager from Turkey thinks as ;"*Low tax rate is effective and encouraging , especially if applied with some other incentives ."*

6.2.Tax Systems of Turkey &China

6.2.1. Incentives on Corporate Taxes

We started asking about the corporate tax rates in comparison with Europe and the special treatments they obtained to all the companies to check the laws described in chapter 4 and 5.

Lord Chemicals in Turkey pointed it out as; "*It is lower than most of the European countries with 20% rate .We don't get any special treatment."*

Delta Galil's manager mentioned as ;"*It is lower in Turkey .We are operating in the free zone and we are exempt from the corporate tax* ."

Abbott in China mentioned as;" *It is 25% in China that is generally lower compared to Europe. We found it was a excellent opportunity to invest in China since they carried out the "Five-year Free and Five-year Half" taxes policy. This means for the foreign investments in China, the government would not levy the taxes for the first five years and then only levy half taxes for the next five years in the condition of obtaining profit. This policy attracted us."*

Novo Nordisk approved the idea as ;"*The special tax treatment China offered was really beneficial to us. We could reduce our cost and therefore reduce the risk we faced when investing in foreign countries ."*

6.2.2. Other tax incentives

We continued with inquiring other tax incentives .i.e. incentives of social security and employee income taxes ,whether these companies were benefiting from in order to preserve the consistency with the theory we presented in chapters 4 and 5 .

The Lord Chemicals' area manager from Turkey replied as ;"*No, we don't get any. ";*
while Delta Galil' s general manager went on as ;"*We have an advantage of exemption from employee income taxes other than the corporation tax because of the free zone area.* " ;
and Novo Nordisk's business controller in China replied as ; "*We must act according to Chinese law on social security and employee income tax."*

Abbott's project manager in China uttered similar saying as *;" Regarding to the social security for employees, we bear the same responsibility as China's domestic companies, for example, we pay Social Security Fund like medical care insurance, endowment insurance, unemployment insurance and housing fund according to relevant laws in China."*

6.3. Impact of Taxation on NPV considerations and International competition

6.3.1. Effect of taxes in investment decisions

Further we asked to all the four companies whether they investigated about the corporate tax rates and the incentives in these countries before they made their investment decisions .
We intended to learn about their curiosity and inquiry on taxation in these countries before they made their investment decision .
We learned that they all did either through their local authoritative market research companies or consulting agencies .

6.3.2. Tax policy of governments

We went on inquiring about the tax rate increases or decreases they encountered during the period their companies were established .
We intended to investigate about the stability on the governments' policies once again with this question ; however stability on the tax policies this time in order to compare with the theory related to impact of taxes on the international competition .

We have been informed that in Turkey there has not been a change during the period they were activated , while in China it was reduced to 25% not long before the current time .

6.3.3. Other factors

Later we asked the companies whether they found what they expected in their investments in terms of profitability . We realized that those companies were big and profitable companies having subsidiaries in all over the world and we intended to learn whether they maintained their profitability in these two developing countries .
But the main motive behind this query was the main leading factors they would provide us perhaps ; factors other than the specific ones we interrogated at the beginning .
These factors would be probably concerning about the industry or the market they were making business in when it is about the profitability we asked.
However it constituted no problem to have additional information which would enable us to proceed with the next related question that would help us analyze international competition .

Novo Nordisk business controller from China continued as ;"*Yes . China's economic development has motivated our business. It enhanced our satisfaction."*
Abbott from China shared almost the same opinion as *;"Yes, generally the profit we obtained from China market is steadily rising within the expected range."*

The Delta Galil's manager in Turkey told ;"*We knew it would not be very easy in textile sector in Turkey ,however we managed to operate with profits ."* ;
while the Lord Chemicals in Turkey replied as *;" We received more than we expected."*

6.3.4. Competition on macro base through tax revenues

We then wondered about the market so questioned about the competition in the market . This question concerns also about the industry they are in and the information they would provide this time would be within the frame of their knowledge about their industry for sure. However we still thought it would be one of the most crucial questions which would help us analyze later the incoming FDI s , within a macro point of view .

Novo Nordisk in China stated as *;"It is getting more and more competitive these years, and we are trying our best to survive."*
Abbott's project manager said *;" Of course, the competition is in everywhere which gives us pressure in taking more market share."*
According to Lord Chemicals in Turkey ;"*Competition was not very harsh compared to other countries* ."
However for Delta Galil textiles in Turkey ; "*It is not an easy market and there is harsh competition."*

6.4. Developing Countries

Coming to the end of our interview we inquired what they learned from both markets and if they would suggest other foreign enterprises to invest in these countries .
We intended to query this issue because they invested in developing countries which may give us an idea about the causality relationship from GDP to FDIs or FDIs to GDP.

Abbott 's project manager replied as;"*The China's preferential policies and the market have brought us great business opportunities. In such fine business situation, we could set up high standards for products and improve our managerial expertise in order to provide consumers with great products and services and be more competitive in our business fields."*

Novo Nordisk 's business controller went on as;" *China is a unique market with huge population and it's own cultural characteristic. .It is still a developing country , continuing to make progress .We want to serve here with our products in this growing economy* ."

Similarly in Turkey ,Delta Galil general manager replied as *;"There is a dynamic young generation with various consumer buying behaviors contributing in a growing economy more each year."*

As well as Lord Chemical's area manager uttering as ;"*the growing economy here contributes back to our growth ."*

All the four of the companies would suggest to other foreign companies to invest in Turkey and China within the research and due diligence study of the industry they would operate .

7.ANALYSIS

It is always important to bring the theory into practice in the real world and get other individuals' opinions and knowledge to make a sound comparison , therefore now we should start to analyze the results of the empirical research within the theory and the regulation we studied so far that can enable us identify the applications in a better way .

7.1. Case study for the motives for investment

7.1.1. Appealing Factors

Starting with the first question , all the four investors believe that large number of population as well as young population and the geographical position of a country are appealing factors in making investment decisions .

Large number of population or young population are seen to be effective factors in investment decisions which may be due to the consumer capacity of the market , the exploitable employment conditions investors may get use of and the advantage for the companies to conduct R&D facilities .
Especially for China , we have encountered with the , potential size of its consumer market, as one of the top determining factors that seems to be approved here .Alternatively the reason for a relatively younger people within the dense population must be equivalent to the objective of higher consumptions.

In our theory for motives for investment we did not encounter with geographical location as an attractive factor as much as other factors and we studied it as a motive related to the business objective .However this empirical research provided that it may be as significant as other factors .But the ground for that factor was not provided in details by the investors. Only one of the investors in Turkey had pointed out in a context of Turkey's perfect geographical location which urged us predict the effect behind . Therefore , as we had prepared our next question with the influence of geographic location we decided to analyze it there.

On the other hand , we estimated in the first question investors would consider the most determinant factors for them , therefore we had decided to direct some other top motives in the following questions.

7.1.2 . Influence of geographic location

Second question made us see the importance of geographical location of a country due to being close to other markets .

Investors believe that it is beneficiary to be close to other geographies such as Asia, Europe and Middle East , which would increase the business opportunities via available access .Thus it is confirmed to be related with the business objective ; profitability in other words.

On the other hand the Textile company in free zone is satisfied with their location because of the incentives they receive, like we reviewed in other investment incentive laws under the title “tax exemption for the income gained in free zone regions.” We did not inquire the details of the incentives here as we planned further to investigate on this issue.

Medical companies in China support the argument of the cost efficient transportation behind the convenient geographical location .It makes us realize that the closer the geographic locations are to other markets , the lower the transportation costs are in distribution , importation and exportation of goods .
China is a country in East Asia which is already distant from US and Europe thus we are informed that investors prefer provinces with feasible locations like in cities with harbors to alleviate the China’s inconvenient geography for making business and to save from transportation costs . Thus in here also it is confirmed to be related with the business objective ; profitability in other words and therefore can considered to be as remarkable as other motives .

In addition ,by this query we are informed that two or even three motives of investment can be interconnected sometimes ,supporting each other as an addition to the theory we studied. In the literature we studied geographic location and lower transportation costs as separate investment motives however here we witnessed to a link between these two motives directly or indirectly .In other words when one motive is embedded in another motive, either one can cause the other desirable motive or the other can arise from the first motive ,like we encountered here .

7.1.3.Influence of low costs

We went on querying the importance of the low costs for investors in order to be relevant with the literature we reviewed .
We encountered that low production costs such as low labor, raw material or transportation costs constitute a major role for investors like we have reviewed in the literature.

For investors in Turkey lower labor costs compared to Europe as well as lower raw material costs existed .

However we can not claim the same for the transportation costs especially for the importing companies due to the customs tax payments as we understand from the Lord Chemical's reply .Therefore we can consider that , for the companies making importation in Turkey when Turkey's eligible geographic location provided an advantage to the enterprises in terms of transportation costs , the customs taxes made transportation costly for them .

Additionally China constituted one of the the best examples in the world for low labor costs according to the investors that made irresistible for them to invest which complies with the theory we presented in the "China example" from other investors' point of views. It seems the theory of "The China price" is true in the real world . The issue played a very important role in the rise of inflowing investments to the country . We did not ask to the managers , the reasoning behind the policy set by the government on this subject specifically , as we had not studied a relevant theory for the details to analyze further . It would be out of our thesis's purpose. Therefore they did not add notable information either .

On the other hand , it is probable that the investors in China are in the type of efficiency-seeking investors trying to minimize costs of producing labor-intensive goods.
Moreover in China exists another appealing factor for investors strengthening ultra low labor costs , absence of the unions that is .

About other production costs ,China's improved infrastructure ensured lower transportation costs compared to the past time ,supporting the presented theory ; while no comment on raw material costs were made which must be due to the relatively more significance of other two production costs .

Here we witnessed that some other factors may have an effect on the low costs , like conditions of infrastructure or customs taxes as well as the significance of low labor costs.

7.1.4.Influence of a stable government policy

We moved on inquiring about the governmental policy.
We witnessed that stable policy with institutions and private enterprises are considered to be attractive in investment decisions like in the literature we reviewed .

Privatization has been more of a concern in the last years especially in developing countries. They have relatively less private institutions and multinationals have been paying attention to privatization due to the less governmental interferences it ensures in a liberal market economy with more private capital .

On the other hand institutionalized economy providing a stable government policy with clear regulations that is applied equally to both domestic and foreign enterprises without discriminatory purposes, just like we examined in the theory for investments seems to be verified in our empirical research .

Medical companies in China also acknowledge the stable governmental policy, within the concept of a constant progress and reform China has been undertaking in their economic policy ,regulations for a more free trade . In China the government was under socialist political and economic system since 1949 that has been responsible for managing national economy . Since 1978 ,when economic reforms were instituted , the government role in the economy has lessened to a great degree. [36] China is going on to open up business relations that foreign enterprises favor .

Here we come across with the approval of the literature which is about the increase in the incoming FDI s under a stable government policy .

7.1.5. Influence of Taxation

We moved on with the extent taxation matters for the investors.
We witness that tax systems matter for investors in their decisions, however there are other important factors such as ; access to suppliers, political stability, low costs, skilled labor etc… These concerns approve the literature we reviewed on the integration of the motives for attracting investments. We realize that neither any of the items pointed out, nor taxation can only be a motive for investment decision but rather the whole of them would establish the idea.

7.2. Implementation of Tax systems in Turkey &China

7.2.1.Incentives on corporate taxes

We later asked about the investors' satisfaction on the applied corporate taxes compared with Europe and the incentives they were receiving on corporate taxes to analyze the theories in chapter 4 & 5.

Both investors in Turkey agreed on lower corporate tax rate than in Europe combined with one incentive one of them, the Textile company ,receives : corporate tax exemption in free

[36] http://www.state.gov/r/pa/ei/bgn/18902.htm#econ

zones that is , just in the way we examined in "tax exemption for the gains made in free zone regions " under section 4.3.4 in chapter 4.

The Chemical company does not have an affiliate with a Turkish company and operates as 100% foreign enterprise with a taxable income subject to corporate tax , thus benefiting from no exemption . Alternatively same company does not operate in the four relatively less developed regions of Turkey as well as being no industry specific investment ,i.e. hi-tech or free zone investment , therefore benefits from no corporate tax reduction or exemption.

For both of the investors in Turkey one incentive they may benefit in the future , is the investment expenditure discounts on taxation in case they make investment on fixed assets related with their investment .

On the other hand investors in China are satisfied not only for the lower corporate tax rates than Europe but also for the preferential tax policy provided as " two free , three half" with a meaning of two years of tax holiday and the next three years of half tax payment .
This issue has been attractive for the investors that complies with the regulation we reviewed either for regional investments or for foreign entities in China .
Especially when we are informed that these medical companies have subsidiaries in various cities of China where per capita income lessens ,we realize that same tax holidays account for regional investments of these entities according to the regional investments we reviewed with Intel example in Chapter 5 of China tax system .

On the other hand both investors in China do not benefit from additional reduced rates after the half tax payment period as they do not operate within industry specific investments like dock, hi-tech or small investments with low profits to benefit from a reduced rate of 20%.

However Novo –Nordisk must be benefiting from the incentive of fully deductable R&D costs due to the R&D center they have in Beijing.

7.2.2. Other Tax Incentives

Later we went on inquiring other tax incentives granted .
We realize that the Chemical company is not established as any of the region, zone , or facility specific investment (such as R&D investment) therefore does not benefit from either social security or employee income tax exemption or reductions.

The Textile company is exempt from employee income taxes because of operating in free zone area in Turkey , in line with the regulation we reviewed in chapter 4.

Companies in China are not benefiting from any of the social security or employee income tax exemptions even if they establish subsidies in poorer regions , in accordance with the regulation warranting no concession .

7.3. Impact of Taxation on NPV considerations and International competition

7.3.1. Effect of taxes in investment decisions

We moved ahead with the information the investors gathered about the tax systems in two countries before they made their decision .
The positive reply we received demonstrates us that taxes are subject to investigation for the incoming companies before they make a decision of investment .

We studied in the literature that FDI s would invest only for the purpose of profit and they make calculations for the period of return of investment.
Taxes are part of costs that decrease the profitability for being compulsory payments. Therefore there is a need for the investors to take tax payments into consideration in case of profitability (before they make their decision), that would lower their calculated net present values (NPV s).

This query for investors supported the theory we reviewed .It confirmed that taxation comes in first five motives of investment for the expectation of preserving higher NPV s by the usage of tax adjusted discount rates.

7.3.2. Tax policy of governments

Before we ended our survey on the applications of the corporate taxes through these investors we inquired about the stability of the rates during the period of these entities were activated .

We were informed that investors came across , not with an increase but with a decrease in the rates in China only and no change in the rates in Turkey recently .
However there has been a reduction in the rates in Turkey either (from 25% to 20%) ,although the investors did not encounter during the time of their activity .

Limitation was set within the presented literature therefore comments of the investors about the reasoning behind were not inquired and applying the propositions from the literature elicited a meaningful and an adequate understanding.
The issue supported our theory on taxation with the unprecedented changes the governments can undertake at any time of the implementation , such as in Turkey and China .The situation

referred to “capital levy problem” where firms are not likely aware of the tax changes as well as they might be aware of the possibility before they made their investment decision.

Moreover we studied in the literature another theory which was about the reduction in the tax rates due to the reduction in the cost of the investments .When we apply this theory to China , we can reach to an assumption of the decreasing rates in China entailing from the outflow of the investments from Chinese entities to other geographies due to low costs in investments.

Another proposition in the literature was about the decline of the tax rates causing from a volatility as a precautionary act of the governments in order to prevent the outflow of the FDI s. It is likely to apply to both of the developing countries lowering the tax rates in order to alleviate the adverse affects of volatility before they established a stable government policy.

Connected with this proposition, we have come across with another theory which is about the globalization process raising volatility and causing lower tax rates .When both Turkey and China are two developing countries ,this proposition seems to be highly possible with either the reform or the growth they have been undergoing from , due to a globalization process in all over the world.

Furthermore it should be noted that the reduced tax rates urge narrower aggregate tax base and that leads to lower tax revenues for these two developing countries.

7.3.3. Other Factors

We then queried about their expectations or the profitability the investors could enjoy from their investments .We expected to learn some factors affecting their profitability other than the specific motives mentioned .

Investors in China confirm that their business is profitable due to the economic development , the market growth , the nation has been going through. General economic development does have influence obviously on the industry they are operating in , the medicine/health care sector that is, via the increase in the intermediary distributors .Overall growth in the economy affects expansion of the market in general , by the business done more between the industries ,such as between the pharmacies and these medical companies as well as by business done with new opening channels .

For the textile company ,Delta Galil , in Turkey , it was not easy to reach their expectation of profitability however they managed it .It is due to the fact that textile industry is under a fierce competition in Turkey with lots of manufacturers , importers chasing low costs .

In addition , in the theory we studied about the greater demand uncertainty adversely affecting the expected income under both production modes; vertical and horizontal FDI s. The issue suggests that in times of internal less demand compared to the supply in the market , the income of inward-FDI s' will also be adversely affected as the income of local suppliers which is another factor on Delta Galil's concern of their market share .In other words volatility in demand would affect profitability adversely. However operating in the free zone and getting its benefits seems to have assisted to reach their goal of profitability.

For the Lord Chemicals , they received more than they expected .
This must be due to the profitable industry they are already operating in with the advantage of working with a lot of customers ;customers of other companies or distributors .Chemical companies benefit from possession of highly regarded products that are needed and purchased by many different industries .

Therefore it shows us ,sometimes some other realities like the industry a company is making business in or the situation of that industry in the new investment location shall also be notable in the reachable expectation of profitability other than the general economic growth.

7.3.4. Competition on macro base through tax revenues

We moved with competition in the market whether investors found challenging or not .

Companies in China find the market more competitive each year with the entrance of the new players that inserted pressure in taking up more market share . First of all this remark supports the favorable conditions China has provided beginning from 1980s such as ; duty free imports, low cost power , absence of unions as well as helpful regulatory procedures , an ultra low-wage , upgraded infrastructure and reduced tax rates with deferred taxes for several years.

Secondly these determinant factors ensure the investments by multinationals.
In other words it complies with the proposition of lower investment costs leading to more profitability thus leading to more incoming FDIs that we reviewed in section 3.2.1 , which would then cause more competition .

In addition we can apply the following proposition which is; "more FDI s widening tax base and if it is high enough leading to more tax revenues ." This link of theories appears to have been confirmed in China example especially when we look at the table of corporate tax revenue figures by years and the proportion of them in the total tax revenues in chapter 5.

Corporation tax revenues increase substantially in the last years almost with a 40% rise in 2007 compared to one previous year .This of course includes the tax collection from the local entities either. However foreign corporation tax revenues increase by 33% in 2007 as well, compared to 2006 .

For the chemical company in Turkey , they have not encountered with harsh competition , not too challenging rivals have entered to the market yet that would force them a decline in their market share compared to their business in other countries .
This can be due to the less local competitors mainly .
FDI s may also be relatively less in number in chemical sector although this is less probable due to the lower corporate tax rate FDI s are getting advantage of ,in Turkey . However it seems more is needed for more players in the market like investment location assignment or exemption from import duties especially for the incoming FDI s choosing importation instead of manufacturing .

For the textile company it was a competitive market as Turkey possessed competitive local textile companies manufacturing with low raw material costs .

Thus by this query we witnessed that local rivals as well as the existence of more FDIs can determine the intensity of competition .

Alternatively if we apply the same proposition of rising tax revenues because of an enlargement of tax bases due to more incoming FDI s ; in Turkey we witness to slight increases in collected corporate tax figures in the last two years and a 13% rise in 2007 compared to one previous year ,2006.Therefore the statistics in comparison with China demonstrates us more increase in China's corporate tax collections , thus lower tax bases in Turkey arising from lower incoming FDI s ,compared to China .

7.4. Developing Countries

Our last question was about the attributes of these two markets and how they contributed to the experience of these investors in relation with the suggestion they would make to other entities whether to invest or not in these markets.

Replies given were already broad enough to highlight the important specifications either in Chinese or Turkish market.
Both countries are the developing countries; China with a huge population over 1 billion people that could not maybe survive without the existence of the FDI s and Turkey with its larger population than European countries with 70 million people with a majority of the

young dynamic generation ; seems to have taken steps to boost their economy for their own people through attracting local and foreign enterprises in order take a position in the competitive markets ,the world is filling more with. These steps in terms of various concessions obviously have attracted FDIs to initiate in investment projects in these territories which stimulates economic revival and higher growth (causality running from FDI to GDP).

Then , more FDI s begin to enter to these markets as they are informed about the growth and the existing favorable conditions which complies with the theory : multinationals tend to locate in enhancing economies where favorable economic conditions with higher growth rates convince foreign-based companies to establish subsidiaries in a developing country (causality running from GDP to FDI).
Therefore the reply of "growth" from companies implies the positive consequence of profitability returning back to them at the end of this chain of happenings.

Afterwards , with increasing number of FDI s, the higher growth in the economy results in higher GDP ,more per capita income, more consumption , therefore more profitability for the investing companies leading them to provide more employment (start of the cycle again, with FDIs leading to GDP).

It is also notable that by the remarks of the two companies in China , China is going through the second phase (from growth to FDIs) much more while Turkey is more likely going through the first stage (FDIs to growth), as we understand from textile company's comment.

They would suggest to FDI s to invest in these two markets .This confirms ; FDI s would invest for the sake of profits.

It seems companies will go on entering to new markets with the aim of making more profits while the society especially in the developing countries with larger populations in need of more job and pay will go on seeking more employment opportunities and products in order to advance their living standards.

8. CONCLUSION

8.1.Conclusion and Reflection on Results

Four private enterprises in Turkey and China considered convenient circumstances they should have for the right investment decision .

They favored some identical motives for investment such as ; big markets with more consumers , low costs , stable government policy and taxation benefits .
The reason for large number of population is due to the potential the markets contain for more consumptions especially if accompanied by young generations.
In addition they were concerned about feasible geographical locations , as much as other top motives and also for the purpose of their business objective .Significance of geographical location lied within the direct and indirect linkage between an other motive ; low transportation costs that is, for the companies investing in China , as well as it was related with other markets to be close to such as ; Europe, Asia , Middle East and beneficial incentives to receive ,for the companies in Turkey .

Low costs maintained it's rank in top three for an investment decision for these companies . Low costs involved low labor, low raw material , low transportation and other costs related to manufacturing however low labor costs for manufacturing remained more substantial. Both Turkey and China were believed to possess lower labor costs than Europe by these companies . Especially both companies in China agreed on the irresistible advantage the country has with it's low labor costs. Moreover , it must be more effective with the absence of unions . On the other hand China's improved infrastructure ensured lower transportation costs while customs taxes made transportation costly for companies making importation in Turkey. Besides, textile company mentioned about the low raw material costs in Turkey .

These companies supported stable governments with a free and liberal economic policy ensuring more private enterprises in the market subject to less governmental interferences and institutions with clear regulations applied equally to both domestic and foreign entities. For investors in China , a stable government policy with constant progress in the economic policy that would open up the country more to trade , was considerable.

They considered the tax system as one of the stimulating top factor for investment however did not make their investment decision, even if the tax incentives provided were very attractive compared to their other businesses. All the factors constituted the components of the whole of an investment decision .

Corporate tax rates were lower in Turkey and China compared to Europe for investors. Both companies in China benefited from the preferential tax policy (which granted several years of tax exemption and several years of half tax payment) and from R&D incentive (one of them) and from no other incentives , while in Turkey only textile company received a corporate tax and employee income tax exemption due to a special zone (free zone) treatment they got .The applications complied with the presented literature of laws .During the presentation of the laws , various tax incentives ;i.e. tax discounts for regional investments , exemptions for foreign affiliates and zone based investments and general accounting applications granting deductions from tax bases ,are disclosed and companies interviewed benefited from the incentives according to their investment class.

All the four companies approved their examination of the tax system in these countries before they made their investment decision . Taxes constituted part of costs that decrease companies' profitability , therefore companies took tax rates of these countries into consideration in their NPV calculations with tax adjusted discount rates to ensure a better return figure .

Investors encountered with reduction in the corporate tax rates during the period they have been staying in these countries which indicated three signs ; governments' act as a response to a volatility arising from globalization , an unprecedented change governments could undertake at any time and a reduction in the cost of shifting investments to other geographies..

All the four companies operated with profits despite the fierce competition in the market , one company in Turkey faced as well as a volatility in demand in the market. Another company possessed the advantage of the industry they were making business in by working with more customers. Companies in China benefited from the general economic growth resulted in expansion in the market and more business done , helping their goal of profitability.

Three out of four investors found the market competitive ,confirming favorable conditions the countries are offering to multinational and local investments as well as larger tax bases and more tax revenues happening for the countries. However the inflow of the FDI s to Turkey occurred relatively less compared to the inflow of the FDI s to China ,by the figures of collected tax revenues in two countries. Alternatively for one company, existence of local or foreign rivals less in number ,affected competition negatively.

According to the investors ,China and Turkey's governments have taken steps to attract more FDI s for a more prosperous country for their citizens and FDI s contribute to the growth of the economy in their country ,as the countries continue to accomplish their mission. Then with more GDP being available , more FDI s come to these countries with a profit share expected to be received more and the cycle starts from the beginning again, with more and more FDI s leading to higher and higher GDP. All companies would suggest to other firms to invest in these two developing countries for the purpose of profitability.

8.2. Suggestions for further research

All investment motives are suggested to be queried one by one in a list ,according to a rank of their significance for the investors instead of being questioned generally, because there must be other motives than what they counted which they might have been not remembering only at that time of inquiry.

Purpose of the government policy for the substantially lower labor costs in China is suggested to be evaluated more with the intended queries to investors with a relevant theoretical framework disclosed initially ,assuring an analogy.

Significance of low raw material costs for the investors can be investigated more.

Interviews are suggested to be held with more than two companies in each of the country which could add additional dimensions.

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APPENDICES

Appendix 1- Related Laws (in their original language)

1- Corporate Income Tax Law 5520 ; (5520 Sayılı Kurumlar Vergisi Kanunu); http://www.mevzuat.gov.tr/Metin.Aspx?MevzuatKod=1.5.5520&MevzuatIliski=0&sourceXmlSearch=

2-Income Tax Law 193 ;(193 Sayılı Gelir Vergisi Kanunu); http://www.gib.gov.tr/index.php?id=1028

3-Extraordinary state regions Law 4325 ; (4325 Sayılı Olağanüstü Hal Bölgesinde Ve Kalkınmada Öncelikli Yörelerde İstihdam Yaratılması Ve Yatırımların Teşvik edilmesi hakkında Kanun); http://www.alomaliye.com/4325_sayili_kanun.htm

4-Technology Development Regions Law 4691 ; (4691 Sayılı Teknoloji Geliştirme Bölgeleri Kanunu) ; http://www.gib.gov.tr/index.php?id=579

5-Free Zone Law 3218 ; (3218 Sayılı Serbest Bölgeler Kanunu) ; http://www.alomaliye.com/3218_sayili_kanun_serbest_bolgeler.htm

6-Modified Free Zone Law 5810 ; (5810 Sayılı Serbest Bölgeler Kanunu ile Gümrük Kanununda Değişiklik Yapılmasına Dair Kanun); http://www.mevzuat.gov.tr/Metin.Aspx?MevzuatKod=1.5.3218&MevzuatIliski=0&sourceXmlSearch=

7-R&D discount Law 5746 ;(5746 Sayılı Araştırma ve Geliştirme Faaliyetlerinin Desteklenmesi Hakkında Kanun); http://www.muhasebetr.com/yazarlarimiz/celal/001/

8-Tax Benefits Under China's New Corporate Income Tax Law (CIT): http://www.chinalawblog.com/2008/06/tax_benefits_under_chinas_new.html

Appendix 2 – Interview Questions

Motives for investment

1-What made you invest in Turkey /China?

2-Are you satisfied with your geographic location and to what extent do you think location is important in your investment decisions ?

3-Low costs are important in manufacturing . What do you think about the costs in Turkey /China ,in particular about labor costs?

4-What do you think about the government policy in Turkey /China ? Do you think it is stable or volatile ?

5-To what extent does taxation affect your investment decisions ?

Tax systems of Turkey &China

6-How do you find the corporate tax rates in Turkey/China when you compare it with Europe and is there any special treatments that you get ?

7- What are the other investment incentives that you obtain from Turkish/Chinese government in terms of social security , employee taxes ?

Npv & International competition

8- Did you know about the tax rates before you made the decision of investment ?

9-Has there been any change in the corporate income tax rate during your stay in Turkey /China ?

10-Did you find what you expected in Turkey/China in terms of profitability?

11-Was the competition in the market challenging for you or not ?

Developing Countries

12-What did you learn from Turkey/China market?

13-Would you suggest other firms to invest in Turkey /China?