TAX INCENTIVES IN THREE COMMON MARKETS

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ABSTRACT

There are three approaches to dealing with tax incentives within common markets: permit them, limit them, or harmonize them. Broadly speaking, the United States (U.S.) follows the first approach, the European Union (EU) adopts the second, and the Gulf Cooperation Council (GCC) pursues the third by harmonizing some tax incentives, particularly those offered to the industrial sector. Unlike the U.S. and EU common markets, where incentives have gained significant scholarly attention, no academic literature exists on the legal framework of tax incentives in GCC common market. This work attempts to compensate for this insufficiency in scholarship and compares the three approaches.

This work also explores the case against locational tax incentives and concludes that the conventional case against tax incentives is overall debatable, and further evidence considering the ongoing changes in international tax policy is needed to better evaluate the case. Furthermore, this work analyzes the advantages and disadvantages of the three approaches to dealing with tax incentives. In particular, this work explores how effective the approaches are in managing bidding wars, increasing tax law predictability, allowing flexibility to reform domestic tax policy as needed, and policing tax incentives. It concludes that each method has its limitations, advantages, and disadvantages. Thus, another contribution that this work offers is the inclusion of a holistic examination of the three approaches that merits focusing beyond the one consideration on which much of the existing literature focuses, that is, bidding wars between competitor states.

Although this work primarily aims to assist GCC policymakers in deciding the best policy option for managing tax incentives, this scholarship is helpful even beyond the GCC. Federal countries and regional blocks that see and experience incentives competition can benefit from this work since it analyzes the merits of different approaches to managing incentives in general.
Keywords: Tax Incentives, State Aid, Dormant Commerce Clause, Tax Competition, Gulf Cooperation Council, GCC.

I. INTRODUCTION

In an unprecedented shift in tax policy, most of the Gulf Cooperation Council (GCC) states (Kuwait, Bahrain, Kingdom of Saudi Arabia (KSA), Qatar, United Arab Emirates (UAE), and Oman) have introduced locational tax incentives.[1] These include tax holidays for up to fifty years or other forms of tax incentives granted at the authorities' discretion on a case by case basis to lure foreign businesses' investments in the last two decades.[2] Some GCC states have announced that they are planning to adopt generous tax incentives in their impending special economic zones. Their introduction across the GCC states at approximately the same time suggests the emergence of tax incentives competition in the GCC common market.[3] The rise of this competition evokes the following questions:

- What is the legal framework for locational tax incentives in GCC common market?
- How valid is the classic case against tax incentives?
- How are other common markets, in particular the United States (U.S.) and the European Union (EU) common markets, dealing with tax incentives?
- What lessons can be learned from the three common markets' experience in addressing tax incentives?

This paper examines these questions.

There are three approaches to deal with tax incentives within common markets: permit them, limit them, or harmonize them. Broadly speaking, the U.S. follows the first approach, the EU adopts the second, and the GCC pursues the third by harmonizing some tax incentives, particularly those offered to the industrial sector. Unlike the U.S. and EU common markets, where incentives have gained significant scholarly attention, to the best of this author's knowledge, no academic literature exists on the legal framework of tax incentives in the GCC common market. This work is the first to investigate the legal framework of tax incentives in the GCC common market and compare it to the legal framework of tax incentives in the U.S. and the EU common markets.

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[1] Common examples of tax incentives are a tax holiday, tax exemption, tax credits, investment allowance, accelerated depreciation, enhanced deduction, and reduced tax rate.

[2] Sarah Khalid Alsultan, *The Gulf Cooperation Council (GCC) States: New Players in the International Tax Competition Game*, 49 INTERTAX 361, 370 (2021).

[3] *Id.* (arguing the rise of corporate tax rates incentivizes competition in the GCC common market).

The paper also considers the conventional case against tax incentives, specifically that incentives:[4] should not be used to compensate for disadvantages, distort behavior, create harmful tax competition, are ineffective, undermine tax revenues, and transfer tax revenues from host countries to investors' home countries. This paper concludes that, overall, the arguments are open to debate. This paper exposes the fact that the recent ongoing changes in tax policies worldwide have impacted the conventional case against incentives.

Finally, this paper analyzes the advantages and disadvantages of the three approaches that deal with tax incentives. While much of the existing literature often focuses on just one consideration—tax competition or a so-called "bidding war" between states or local governments—to argue in favor or against regulating tax incentives, this article considers three other important aspects—how effective the approaches are in increasing tax law predictability, tolerating flexibility to reform domestic tax policy as needed, and policing tax incentives.

Although this work primarily aims to assist GCC policymakers on whether to permit, limit, or harmonize locational tax incentives within the GCC common market, this scholarship is helpful even beyond the GCC. Federal countries and regional blocks that witness incentives competition can benefit from this work since it analyzes the merits of different approaches to managing incentives in general.

This work is divided as follows: Part I briefly introduces GCC states' tax mix in order to provide a necessary background. Part II reassesses the arguments against foreign investment tax incentives. Part III discusses the legal framework of tax incentives in the United States, EU, and GCC. Part IV examines and compares the advantages and disadvantages of each approach to manage tax incentives.

II. THE TAX MIX IN GULF COOPERATION COUNCIL STATES

The GCC states are high-income developing countries where oil plays the central role in funding states' spending.[5] The region can be characterized as a low or no tax jurisdiction regarding indirect taxes, direct

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[4] Yoram Margalioth, *Tax Competition, Foreign Direct Investments and Growth: Using the Tax System to Promote Developing Countries*, 23 VA. TAX REV. 161, 181 (2003) (referring to the arguments mentioned in this work and noting that "[c]onventional wisdom weighs against using tax incentives to attract investment in general and foreign direct investment in particular").

[5] *See* UNITED NATIONS, WORLD ECONOMIC SITUATION AND PROSPECTS 127 (2021), https://www.un.org/development/desa/dpad/wp-content/uploads/sites/45/WESP2021_FullReport.pdf (characterizing the states as developing countries); *List of High Income Economies*, WORLD BANK, https://data.worldbank.org/income-level/high-income (last visited Feb. 2, 2022).

taxes on individuals, and corporate income tax (CIT) on domestic enterprises. For example, no personal income tax and no gift or inheritance tax exists in any GCC state.[6] There are limited property taxes and social security taxes that exist in all six states.[7] So far, four states have implemented value added tax (VAT) at a 5% rate with the other states soon adopting such a tax.[8] Sin taxes are also levied on a few items, such as tobacco products, alcohol, and energy drinks. The VAT and sin consumption taxes were harmonized in GCC agreements in late 2016.[9]

Regarding CIT, the normal domestic tax regime generally favors domestic companies. In Kuwait, the KSA, UAE, and Qatar, either the tax laws or the tax authorities provide such treatment. Kuwait applies different tax rates to national and foreign companies; the latter are taxed at a 15% rate, and national companies are either not taxed at all or taxed at a 1% to 2.5% rate depending on a company's form.[10] Similarly, KSA national companies are

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[6] For further details on the Kuwait tax system, see PWC, DOING BUSINESS IN KUWAIT 7 (2015), https://www.pwc.de/de/internationale-maerkte/assets/doing-business-in-kuwait-2015.pdf. On the Qatar tax system, see PWC, DOING BUSINESS IN QATAR 20–23 (2013), https://www.pwc.de/de/internationale-maerkte/assets/doing-business-in-qatar.pdf. On the Saudi Arabia tax system, see DELOITTE, UNDERSTANDING SAUDI ARABIA'S TAX POSITION 26 (2021), https://www2.deloitte.com/content/dam/Deloitte/xe/Documents/tax/me_doing-business-guide-ksa-2021.pdf. On the Oman tax system, see PWC, DOING BUSINESS IN OMAN 8 (2016), https://www.pwc.de/de/internationale-maerkte/assets/doing-business-in-oman-2017.pdf. On the Bahrain tax system, see PWC, DOING BUSINESS IN BAHRAIN 7 (2015), https://www.icricinternational.org/wp-content/uploads/countries/bahrain/investment%20laws.pdf. On the United Arab Emirates tax system, see PWC, DOING BUSINESS IN THE UAE 18–22 (2020), https://www.pwc.de/de/internationale-maerkte/assets/doing-business-in-the-uae.pdf.

[7] *See, e.g.*, DOING BUSINESS IN KUWAIT, *supra* note 6, at 7 (explaining further details on Kuwait property taxes and social security taxes); DOING BUSINESS IN QATAR, *supra* note 6, at 23 (highlighting the Qatar social security tax); DELOITTE, *supra* note 6, at 26 (touching on the Saudi Arabia's property tax system); DOING BUSINESS IN OMAN, *supra* note 6, at 8 (highlighting the property and social security tax system in Oman); DOING BUSINESS IN BAHRAIN, *supra* note 6, at 7; DOING BUSINESS IN UAE, *supra* note 6, at 18 (delineating the UAE tax system).

[8] KPMG, GULF COOPERATION COUNCIL STATES GEAR UP FOR VAT IN 2018 5 (2017), https://assets.kpmg/content/dam/kpmg/xx/pdf/2017/02/gits-article-vat-in-gcc-web-v4.pdf; DELOITTE, VAT IN THE GULF COUNTRIES THINKING AHEAD 1 (2017), https://www2.deloitte.com/content/dam/Deloitte/xe/Documents/tax/countriesvatimplementation/Deloitte-VAT-in-the-Gulf-countries-infographic.pdf.

[9] *See* COMMON VALUE ADDED TAX AND COMMON EXCISE TAX AGREEMENTS OF THE STATE OF THE GULF COOPERATION COUNCIL (GCC) art. 6 (2016), https://www.mof.gov.ae/en/lawsAndPolitics/govLaws/Documents/Common%20Excise%20Tax%20Agreement.pdf.

[10] Two laws govern CIT on Kuwaiti companies. *See* Law No. 19 of 2000, arts. 10–11 (Kuwaiti) (discussing subsidizing and encouraging national labor to work in the non-government sector); Law No. 46 of 2006, art. 1 (Kuwaiti) (regarding Zakat contribution of public and closed shareholding companies in the state's budget). Foreign companies are

subject to Islamic Zakat at 2.5%, while a 20% rate is applied to foreign companies.[11] Qatar tax law exempts national companies but taxes foreign firms at a 10% rate.[12] The practice in the Emirates of UAE is to only tax foreign banks and oil companies.[13] However, not all GCC states follow this trend. Oman applies the same regime to both national and foreign companies, taxing them all at a 15% rate.[14] Bahrain, on the other hand, does not tax non-oil national and foreign companies.[15] Since 1989, under the GCC tax anti-discrimination rule, GCC companies are treated as nationals for tax purposes.[16] Thus, tax incentives de facto target foreign enterprises because GCC states do not tax their domestic enterprises or impose a minimum rate.

III. THE CLASSIC ARGUMENTS AGAINST TAX INCENTIVES

Before exploring how the three common markets manage tax incentives and the merits of each, it is essential to first evaluate the case for and against locational incentives to determine whether eliminating incentives is the superior approach. This part reviews the most common arguments against tax incentives: they are used to compensate for disadvantages, they distort investment decisions, they create harmful tax competition, they are ineffective in attracting investments, they undermine tax revenues, and they transfer tax revenues from host countries to investors' home countries. The first two arguments are of little, or no, persuasive value. However, the recent and ongoing changes in tax policies in the capital exporting countries, the growth in the OECD Base Erosion and Profit Shifting project, the existence of mixed empirical evidence, and the lack of evidence from the GCC region

taxed according to Law No. 2 of 2008 (amending some provisions of Kuwait Income Tax Decree 3 of 1955).

[11] On Zakat, *see* Ministerial Resolution No. 2216, 7/7/1440H, art. 14 § 1 (Mar. 14, 2019) (Saudi Arabia). On tax laws that apply to foreign companies, *see* Royal Decree No. M/1, 15/1/1425H, art. 2 § a (Mar. 7, 2004) (Saudi Arabia).

[12] Law No. 24 of 2018, arts. 4 §§ 10–11, 9 (Qatar).

[13] DOING BUSINESS IN THE UAE, *supra* note 6, at 10; DELOITTE, INTERNATIONAL TAX UNITED ARAB EMIRATES HIGHLIGHTS 2019 1 (2019), http://www.iberglobal.com/files/2019-1/emirates_deloitte_ficha.pdf.

[14] Royal Decree No. 28/2009, Promulgating the Income Tax Law, arts. 1 §§ 21–24, 112 (Oman) (amended by Income Tax Decree 9 of 2017).

[15] Amiri Decree No. 22/1979 with Respect to Repealing Provisions of Amiri Decree No. 8 of 1955 and Amendments Thereof with Respect to Income Tax, art. 2 (Bahrain).

[16] Resolution of the Supreme Council in the Ninth Session (Dec. 1988) (Bahrain) (providing equal tax treatment of the GCC nationals in all Member States when engaged in economic activities, professions, and crafts); *Steps Have Been Taken to Achieve Economic Citizenship*, GCC, https://www.gcc-sg.org/en-us/CooperationAndAchievements/Achievements/EconomicCooperation/TheGCCCommonMarketandEconomicnationality/Stepshavebeentakentoachieveeconomiccitizenship/Pages/VIIITaxTreatment.aspx (last visited Feb. 2, 2022).

have made the rest of the arguments debatable. This author will discuss the arguments not in order of importance, but as they naturally build on one another as related concepts."

A. *Compensate for Countries' Disadvantages*

Some contend that developing countries should not utilize tax incentives to compensate for market imperfections or disadvantages; instead, the impediments must be eliminated and dealt with directly.[17] Depending on firms' activities, locational determinants can include non-institutional factors such as cost of labor, geographic location, market size, availability of natural resources, adequate infrastructure, cultural and social factors, population size, environmental risks (e.g., hurricanes, tornadoes, earthquakes), and institutional factors such as protection of private and intellectual property rights, corruption, legal and judicial systems, and bureaucracy.[18]

The argument above can be broken down into three assumptions: 1) incentives are merely used to compensate for disadvantages; 2) tax incentives are harmful because, when governments introduce incentives, governments come to a standstill and cease improving the non-tax negative factors; and 3) all disadvantages can be corrected, but governments choose the easier path and grant tax incentives instead. Each of these assumptions is questionable. First, tax incentives are not merely used to counter disadvantages; they are also used because governments are forced to grant them due to competition over similar investments.[19] An IMF study on developing countries noted that "[t]ax competition is often cited by policymakers as a key reason for providing tax incentives."[20] Thus, the underlying assumption is debatable at least in developing countries like the GCC states.

Second, even if countries use incentives to compensate for disadvantages, it does not follow that governments come to a standstill and do not deal with impediments. Governments attempt to enhance both non-tax and tax factors to reduce the cost of doing business. For instance, around the same time that the GCC states introduced tax incentives, they reformed institutional and non-institutional factors to improve investment climates in general. The states have adopted foreign investment laws to protect investors and anti-

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[17] *See, e.g.*, Avi Nov, *Tax Incentives to Entice Foreign Direct Investment: Should There Be A Distinction Between Developed Countries and Developing Countries?*, 23 VA. TAX REV. 685, 691 (2004) [hereinafter *Nov Tax Incentives to Entice FDI*].

[18] *See* Ewe-Ghee Lim, *Determinants of, and the Relation Between, Foreign Direct Investment and Growth: A Summary of the Recent Literature* 12–13 (Int'l Monetary Fund, Working Paper No. WP/01/175, 2001).

[19] Aleksandra Bal, *Tax Incentives: Ill-Advised Tax Policy or Growth Catalysts?*, 54 EUR. TAX'N 63, 64 (2014).

[20] Mario Mansour, *Tax Policy in MENA Countries: Looking Back and Forward* 27 (Int'l Monetary Fund, Working Paper No. WP/15/98, 2015).

corruption laws to increase transparency and trust in the legal system.[21] These states have civil law systems, but some have established courts that adopt English common law with the hope that investors who are used to a common law system will be encouraged by the predictability of the courts' judgements.[22] In 2019, Kuwait and the KSA were among the top ten most notable improvers in the World Bank's "Doing Business Report," a report that measures improvement in twelve areas such as starting a business, enforcing contracts, and protecting minority investors.[23] These areas test some of the above locational determinants.

Finally, and most importantly, this argument incorrectly assumes that all disadvantages can be corrected by government acts. It is true that, if any of the abovementioned disadvantages can be eliminated, it is best to do so. However, while some of the disadvantages, such as geographic location and environmental risks, are impossible to correct, others, such as population size, take a long time to improve.[24]

B. Create Harmful Tax Competition

Some argue that tax incentives cause "harmful" tax competition between countries.[25] The above cited IMF study indicates that competition is the main reason for offering incentives,[26] but the question remains whether competition is destructive or constructive. Competition's effects are widely debated. Between the theoretical arguments and the lack of good empirical

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[21] *See* Kennedy Prince Modugu & Juan Dempere, *Globalization and Foreign Direct Investment in the GCC Countries: A Recipe for Post COVID-19 Recovery*, 8 J. ASIAN FIN. ECON. & BUS. 11, 14 (2021) (describing some of FDI regulations reforms in the GCC).

[22] For instance, since the 2000s, at least two courts established in the region have been modeled on English common law: (1) The Dubai International Financial Centre Court (a judicial body within the Dubai International Financial Centre) and (2) the Abu Dhabi Global Market Courts (a judicial body within the Abu Dhabi Global Market). For more on some of these courts, see Jayanth K. Krishnan & Priya Purohit, *A Common Law Court in an Uncommon Environment: The DIFC Judiciary and Global Commercial Dispute Resolution*, 25 AM. REV. INT'L. ARB. 497 (2015).

[23] WORLD BANK GRP., DOING BUSINESS 2020 8 (2020), https://openknowledge.worldbank.org/bitstream/handle/10986/32436/9781464814402.pdf?sequence=24&isAllowed=y.

[24] *E.g.*, Ted G. Telford & Heather A. Ures, *The Role of Incentives in Foreign Direct Investment*, 23 LOY. L.A. INT'L & COMPAR. L. REV. 605, 607 (2001) ("Obviously, there are many elements outside a government's immediate control, such as higher labor costs or geographic location.").

[25] *See, e.g.*, Kim Brooks, *Tax Sparing: A Needed Incentive for Foreign Investment in Low-Income Countries or an Unnecessary Revenue Sacrifice*, 34 QUEEN'S L. J. 505, 545–46 (2009).

[26] *See* Mansour, *supra* note 20, at 27.

evidence, both in general and with specific regard to the GCC region, it is difficult to arrive at firm conclusions regarding competition.

Scholars credit tax competition for achieving optimal levels of expenditure on public goods,[27] reducing government sizes,[28] and stimulating further investments.[29] Competition also could arguably cause a free rider

[27] This argument is based on the Tiebout model created by Charles M. Tiebout. Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416 (1956). For an explanation of the Tiebout model, see John Douglas Wilson, *Theories of Tax Competition*, 52 NAT'L TAX J. 269, 271–73 (1999); Richard Vedder, *Tiebout, Taxes, and Economic Growth*, 10 CATO J. 91, 93–94 (1990). For a retort to this claim, see Lilian V. Faulhaber, *The Trouble with Tax Competition: From Practice to Theory*, 71 TAX L. REV. 311, 319 (2018) (arguing that Tiebout's model is originally formed to study local competition and it "relies on assumptions that are even less accurate in the context of international tax competition than in the context of competition between local jurisdictions").

[28] This argument first appeared in GEOFFREY BRENNAN & JAMES M. BUCHANAN, THE POWER TO TAX: ANALYTICAL FOUNDATIONS OF A FISCAL CONSTITUTION 1–33 (1980). *But see* INT'L MONETARY FUND, ISSUES IN INTERNATIONAL TAXATION AND THE ROLE OF THE IMF 8 (2013) (questioning the merit of this argument by stating "why this should be superior to other and more explicit fiscal constraints is unclear").

[29] Tax competition indirectly furthered investment since the untaxed money (due to tax exemption, for instance) in private hands will be reinvested. *See* James R. Rogers, *State Tax Competition and Congressional Commerce Power: The Original Prudence of Concurrent Taxing Authority,* 7 REGENT U. L. REV. 103, 113 (1996) ("After all, the money does not disappear if state governments do not collect it in the form of tax revenues; rather, it stays in private hands, potentially resulting in increased investment and higher incomes."). *But see* Reuven Avi-Yonah, *The WTO, Export Subsidies, and Tax Competition, in* MICHAEL LANG ET AL., WTO AND DIRECT TAXATION 124 (2005) (contending that, even if the argument that tax competition stimulates investments is accepted, the investments might be in different jurisdictions and the untaxed money will not benefit the host country).

problem,[30] distort economic activities,[31] reduce the supply of public goods,[32] reduce tax revenue,[33] reduce global welfare,[34] and push toward regressive tax systems.[35] Although international organizations such as the Organisation for

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[30] *See* OECD COMMITTEE ON FISCAL AFFAIRS, HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE ¶ 24 (1998). [hereinafter OECD HARMFUL TAX COMPETITION REPORT] (describing taxpayers who use tax havens as "free riders" in the host and home state). *But see* David C. Elkins, *The Merits of Tax Competition in a Globalized Economy*, 91 IND. L. J. 905, 938 (2016) (arguing that foreign firms are not free riders that enjoy public services without paying a fair share of taxes because firms pay "for many of those services indirectly when they purchase factors of production").

[31] *See* OECD HARMFUL TAX COMPETITION REPORT, *supra* note 30, ¶ 4; COMM'N OF THE EUR. CMTYS., REPORT OF THE COMMITTEE OF INDEPENDENT EXPERTS ON COMPANY TAXATION 11–12 (1992); Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573, 1625 (2000) [hereinafter *Avi-Yonah Globalization 2000*] (arguing that competition "can lead to an inefficient global allocation of capital"). *But see* Michael Littlewood, *Tax Competition: Harmful to Whom?*, 26 MICH. J. INT'L L. 411, 445 (2004) (admitting that, while tax competition does affect the location of a business, the author objects to labeling this effect as a distortion. As the author phrases his opinion, "[t]he OECD's use of the word seems to imply that the patterns of trade and investment which currently exist in the world are somehow optimal and that they should therefore be preserved").

[32] *See, e.g.*, Reuven S. Avi-Yonah, *Bridging the North/South Divide: International Redistribution and Tax Competition*, 26 MICH. J. INT'L L. 371, 375 (2004) ("[I]f government service programs are to be maintained in the face of globalization, and if developing countries are to raise the funds . . . . it is necessary to cut the intermediate link by limiting tax competition."). *But see* Peter Dietsch & Thomas Rixen, *Tax Competition and Global Background Justice*, 22 J. POL. PHIL. 150, 155 (2014) (noting whether tax competition causes under-provision of public goods cannot be empirically tested; however, the author emphasized that tax competition can impair the states "ability to effectively set the size of the budget and the extent of redistribution").

[33] *See, e.g.*, Mario Monti, *How State Aid Affects Tax Competition*, 8 EC TAX REV. 208, 209 (1999) (noting that unfair tax competition in the EU "represents a threat to tax revenue of the Member States"); OECD HARMFUL TAX COMPETITION REPORT, *supra* note 30, ¶ 85 ("Governments cannot stand back while their tax bases are eroded through the actions of countries which offer taxpayers ways to exploit tax havens and preferential regimes to *reduce the tax that would otherwise be payable to them.*" (emphasis added)); Rogers, *supra* note 29, at 107–08 ("State tax competition *almost certainly* means that states receive lower net tax revenues relative to a 'collusive' outcome" (emphasis added). However, the author notes that lower tax revenue does not mean lower welfare.). *But see Avi-Yonah Globalization 2000*, *supra* note 31, at 1597 (claiming that "there is no evidence that overall revenue . . . in OECD member countries has declined.").

[34] *See* OECD HARMFUL TAX COMPETITION REPORT, *supra* note 30, ¶ 37. *But see* Littlewood, *supra* note 31, at 442–43 (rejecting OCED's claim and describing it as "vague." In particular, the author claims that global welfare cannot be measured. Furthermore, assuming it can be measured, this will lead to a "problem of demonstrating causation" when it is uncertain what factor caused the reduction.).

[35] Mathias Risse & Marco Meyer, *Tax Competition and Global Interdependence*, 27 J. POL. PHIL. 480, 483 (2019).

Economic Cooperation and Development (OECD) and EU seem to view competition as harmful,[36] whether all forms of competition are harmful is still debatable. In a study conducted on tax competition by Michael Keen and Kai A. Konrad in 2013, the authors concluded that:

> the literature has not answered the basic question that has loomed over policy debates since OECD (1998): How can one distinguish tax competition that is "harmful" from that which is not? Progress has been made, but not yet enough to confidently determine whether, for instance, the presumption should be against or in favor of preferential regimes.[37]

One negative behavior that competition is said to promote is the so called "corporate blackmail."[38] Incentive-induced competition encourages this practice when firms shop around to pit countries against each other in order to obtain incentives that the company would not normally receive without such a maneuver.[39] These maneuvers occur when countries pass laws or when investment agencies have discretion to grant special incentives to a particular company. The story of Amazon described in Part III is an excellent example of this behavior. These custom-made deals might be particularly undesirable because they allow countries to pick winners, which is unfair to other competitors and wastes a country's resources. Another closely related issue is that incentives encourage rent seeking activities when special interest groups lobby governments to enact laws that provide incentives or extend their duration; rent seeking activities pressure governments to adopt incentives not based on economic costs and benefits.[40] Tax competition is viewed as a collective action problem for which unilateral action by

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[36] *See, e.g.*, OECD HARMFUL TAX COMPETITION REPORT, *supra* note 30.

[37] *See* MICHAEL KEEN & KAI A KONRAD, HANDBOOK OF PUBLIC ECONOMICS 321 (Alan J. Auerbach & Martin Feldstein, 5th ed. 2013).

[38] *See, e.g.*, Tracy Kaye, *Corporate Blackmail: State Tax Incentives in the United States, in* ALEXANDER RUST & CLAIRE MICHEAU, STATE AID AND TAX LAW 38 (2012); David Brunori, *Principles of Tax Policy and Targeted Tax Incentives*, 29 ST. & LOC. GOV'T REV. 50, 59 (1997) ("[T]ax incentives are perhaps most detrimental in that they compel firms to negotiate tax burdens by playing one jurisdiction against another."); Robert Louis Perkins, *The Need for A New Political Playbook Which Mitigates the Public Harm Caused by Tax Incentives*, 38 MISS. COLL. L. REV. 1, 14–16 (2019) (illustrating how BMW increased the tax incentives package offered from South Carolina from $35 million to $150 million by leveraging another bid from Nebraska while later "company documents revealed that Nebraska was not under consideration for the BMW").

[39] On incentive competition which operate in the same way country tax incentives can, *see* Kaye, *supra* note 38; Brunori, *supra* note 38; Perkins, *supra* note 38.

[40] Brooks, *supra* note 25, at 544–45.

individuals is probably insufficient.[41] *If* it is considered harmful overall, then the best way to deal with tax competition is at a regional or supranational level. Note that these two issues do not, by themselves, mean incentives should be eliminated since incentives can be harmonized to minimize their destructive effects, as explained in Part IV.

C. *Ineffective*

Tax incentives are frequently seen as ineffective for attracting business.[42] While it is true that incentives will not cause losses when businesses are not attracted to invest, incentives are a waste if granted to investors who will invest anyway.

Existing studies are inconclusive in both developed and developing countries about whether tax incentives are effective.[43] Some studies assert that

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[41] THOMAS RIXEN, THE POLITICAL ECONOMY OF INTERNATIONAL TAX GOVERNANCE 43–46 (2008).

[42] *E.g.*, *The Chamber Comments on 2013-2016 Strategic Plan to Develop Non-Oil Exports in the Gulf Countries*, KUWAIT CHAMBER OF COM. & INDUS., http://www.kuwaitchamber.org.kw/echamber/website/index.jsp?pageID=ws_cmsmenu.jsp&fromPublic=yes&language=en&rootMenu=572&menuID=572 (last visited Feb. 2, 2022) (Arabic) (indicating that investment incentives are "bad incentives", and it is more effective to enhance the investment environment. The Chamber view is based on investment literature rather than a study conducted on the GCC or Kuwait.); James R. Rogers, Symposium: *Daimlerchrysler v. Cuno and the Constitutionality of State Tax Incentives for Economic Development: The Law and Policy of State Tax Competition: Much Ado About Nothing?*, 4 GEO. J. L. & PUB. POL'Y 101, 105 (2006) (using a simple game-theoretic model to show that tax incentives are ineffective). For a counter argument, see *Avi-Yonah Globalization 2000*, *supra* note 31, at 1644–46; Margalioth, *supra* note 4, at 182–83.

[43] It has been asserted that this argument is not easy to conclusively support for two reasons. First, it is difficult to compare the empirical evidence. Eric M. Zolt, *Tax Incentives and Tax Base Protection Issues* 7–8 (United Nation, Draft Paper No. 3, 2013), https://www.un.org/esa/ffd/wp-content/uploads/2014/10/20140604_Paper3_Zolt.pdf [hereinafter *Zolt Tax Incentives*] (pointing to several studies on the relation between foreign investments and taxes that concluded that it is not easy to compare the results of different empirical studies "because the studies contain different data sources, methodologies, and limitations"); Carlos F. Liard-Muriente, *US and EU Experiences of Tax Incentives*, 39 AREA 186, 192 (2007) (attributing the mixed evidence even when studying the same program to differences in "methodological approaches and selection of an 'effectiveness' benchmark (job creation vs firm location)"). Second, when conducting surveys, companies have no motive to truly reveal whether incentives are effective. *See* Edward A. Zelinsky, *Tax Incentives for Economic Development: Personal (And Pessimistic) Reflections*, 58 CASE W. RES. L. REV. 1145, 1148–49 (2008) (pointing out that "corporations … know their locational choices and preferences and have no reason to disclose these to the officials with whom they are bargaining for tax benefits. Indeed, those negotiating for tax benefits from states and localities have every reason to hide their true choices and preferences."); UNITED NATION, DESIGN AND ASSESSMENT OF TAX INCENTIVES IN DEVELOPING COUNTRIES 4 (2018)

taxes are less important compared to non-tax considerations.[44] Other studies find that taxes are important factors in general and particularly for some types of businesses.[45] The orphan study found by the author that surveyed fifty EU companies investing in or seriously considering investing in the GCC region in 2017, asserts that, soon after the region cut tax rates and introduced tax incentives,

> free zones and low levels of taxation (both income and corporate tax) have the most positive effect on EU companies' decisions to invest in the region. The existence

[hereinafter UNITED NATION TAX INCENTIVES] (noting "[w]hile foreign investors often claim that tax incentives were necessary for the investment decision, it is not easy to determine the validity of the claim").

[44] *E.g.*, Mansour, *supra* note 20, at 27, 29 (acknowledging that the empirical evidence on the effectiveness of tax incentives and foreign direct investment is mixed; however, noting that, in the Middle East and North Africa, "non-tax policies affecting investment, such as barriers to entry, capital controls, public infrastructure, high statutory tariff rates, seem to be more important for investment than the CIT"); Howell H. Zee et al., *Tax Incentives for Business Investment: A Primer for Policy Makers in Developing Countries,* 30 WORLD DEV., 1497, 1508 (2002) (reviewing empirical studies in developing countries and concluding that "tax incentives can stimulate investment, but that a country's overall economic characteristics may be more important for the success or the failure of industries than any tax incentives package"); Haroldene Wunder, *The Effect of International Tax Policy on Business Location Decisions*, TAX NOTES INT'L, Dec. 2001, at 1331 (surveying 75 Fortune 500 companies and concluding that "non-tax factors dominate the location decisions of the firms represented in this research"). *But see* Sebastian James, *Effectiveness of Tax and Non-Tax Incentives and Investments: Evidence and Policy Implications* 11 (2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2401905 (surveying several studies in developing non-GCC countries and concluding that "[s]tudies have found that incentives did not affect investment in West and Central Africa" but, at the same time, asserting that "the opposite was true in the Eastern Caribbean").

[45] Jacques Morisset, *Tax Incentives: Using Tax Incentives to Attract Foreign Direct Investment* 3 (World Bank, Working Paper Note No. 253, 2003) https://openknowledge.worldbank.org/bitstream/handle/10986/11325/255210NEWS0RE P10Box345634B01PUBLIC1.pdf?sequence=1&isAllowed=y ("Growing evidence shows, for example, that tax incentives are a crucial factor for mobile firms and firms operating in multiple markets—such as banks, insurance companies, and Internet-related businesses—because these firms can better exploit different tax regimes across countries."). *See* Kimberly Clausing, *The Nature and Practice of Tax Competition, in* GLOBAL TAX GOVERNANCE WHAT IS WRONG WITH IT AND HOW TO FIX IT 35 (Peter Dietsch & Thomas Rixen eds., 2016) (concluding that there are "great deal of evidence that suggests that multinational firms are tax-sensitive in their economic decision"); A. J. Easson, *Tax Incentives for Foreign Direct Investment in Developing Countries*, 9 AUSTL. TAX F. 387, 394 (1992) (concluding that there is a mix of evidence but generally "taxation has an important effect upon some decisions to invest . . . once a decision to invest abroad has been reached, taxation plays an important role in determining where to locate that investment, both as between competing host countries").

> of free zones was mentioned by 18% of all survey participants as having a 'strongly positive' or 'positive' effect on investment decisions, followed closely by the levels of corporate and income taxes by 16%.[46]

The same study also concluded that "[t]he favourable tax regime in the GCC is an important factor of consideration for the EU companies in the region."[47] Notably, the rate drop from a 55% progressive rate to a flat 15% rate in Kuwait caused a "*major influx"* of foreign direct investments.[48] Although the dearth of empirical studies that evaluate the GCC region helped the study show the effectiveness of tax incentives in that region, the effectiveness of incentives cannot be concluded with confidence. Additionally, the introduction of incentives and tax cuts in the GCC region coincided with other reforms such as the liberalization of investment for foreigners.[49] Thus, it is difficult to attribute an influx of investment solely to tax incentives.

Nonetheless, the existing literature suggests that taxes have a greater impact on common markets and regional groupings since businesses freely move from high to low tax jurisdictions.[50] Globalization in general has changed the role of tax incentives.[51] A United Nations study attributed the role change to several factors:

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[46] EUROSUPPORT CONSORTIUM, 2017 EU – GULF COOPERATION COUNCIL INVESTMENT REPORT 29 (2017), https://trade.ec.europa.eu/doclib/docs/2018/april/tradoc_156661.pdf.

[47] *Id.* at 34.

[48] *Id.* at 55.

[49] *See, e.g.*, Modugu & Dempere, *supra* note 21, at 12.

[50] *E.g.*, Jacques Morisset & Neda Pirnia, *How Tax Policy and Incentives Affect Foreign Direct Investment: A Review, in* LOUIS T. WELLS ET AL., USING TAX INCENTIVES TO COMPETE FOR FOREIGN INVESTMENT: ARE THEY WORTH THE COSTS? 91–93 (2001); Philipp Genschel et al., *Accelerating Downhill: How the EU Shapes Corporate Tax Competition in the Single Market*, 49 J. COMMON MKT. STUD. 585 (2011) (providing qualitative and quantitative evidence arguing that the competition is "stronger in the EU than in the rest of the world" partly due to market integration); Alex Easson, *Tax Incentives for Foreign Direct Investment Part I: Recent Trends and Countertrends*, 55 BULL. INT'L TAX'N 266, 267–68 (2001) (providing examples of intra-regional competition).

[51] *E.g.*, OECD, CORPORATE TAX INCENTIVES FOR FOREIGN DIRECT INVESTMENT 58 (2001) [hereinafter OECD FDI INCENTIVES] (summarizing recent empirical evidence and concluding that there is "convincing evidence" that taxation influences firms' decisions and attributing this change in part to globalization); Margalioth, *supra* note 4, at 183 ("Until ten years ago, a consensus existed in the literature that tax considerations have only a minor effect on FDI decisions. Determinants like consumer market size, labor skills, infrastructure, trade policies and political and macroeconomic stability dominated decisions regarding investment location. Globalization has dramatically reduced the importance of these factors, and elevated the role tax incentives play. Former FDI barriers

> First, tax incentives may be more generous now than in past years. The effective reduction in tax burden for investment projects may be greater than in the past, as tax holiday periods increase from 2 years to 10 years or the tax relief provided in certain enterprise zones comes to include trade taxes as well as income taxes. Second, over the past several decades there has been substantial trade liberalization and greater capital mobility. As non-tax barriers decline, the significance of taxes as an important factor in investment decisions increases. Third, businesses have changed in many ways. Firms have made major changes in organizational structure, production and distribution methods and the types of products being manufactured and sold. Highly mobile services and intangibles are a much higher portion of cross-border transactions than in past years.[52]

The internet has also contributed to that effect.[53] Additionally, an empirical study implies that the recent trend in developed countries to move to a territorial system has contributed to their tax sensitivity.[54] Finally, some predict that the ongoing global efforts to avoid profit shifting and tax eroding will increase the attractiveness of tax incentives in developing countries.[55]

Against this, in 2019, the OECD announced that it is considering a proposal to impose a global minimum tax rate on multinational companies' global income.[56] This proposal is in its early stages and, depending on how it is designed, it might reduce the effectiveness of incentives if it claws back tax reductions. In conclusion, mixed evidence and ongoing changes in global tax policy have made the effectiveness of incentives unclear.

D. Transfer Revenue to Investors' Home Countries

Some contend that incentives result in a transfer of tax revenues from host to home countries.[57] This happens when the home country taxes its

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like tariffs and currency exchange controls are reduced or gone, making taxes a more decisive factor.").

[52] UNITED NATION TAX INCENTIVES, *supra* note 43, at 6.

[53] Morisset, *supra* note 45, at 4.

[54] Thornton Matheson et al., *Territorial vs. Worldwide Corporate Taxation: Implications for Developing Countries* 18 (Int'l Monetary Fund, Working Paper No. WP/13/205, 2013).

[55] *Zolt Tax Incentives*, *supra* note 43, at 31–32.

[56] *See* OECD, GLOBAL ANTI-BASE EROSION PROPOSAL ("GLOBE") - PILLAR TWO 29–30 (2019), https://www.oecd.org/tax/beps/public-consultation-document-global-anti-base-erosion-proposal-pillar-two.pdf.pdf.

[57] *E.g.*, *Avi-Yonah Globalization 2000*, *supra* note 31, at 1642 (restricting this argument to direct foreign investments); Vito Tanzi & Howell H. Zee, *Tax Policy for Emerging*

domestic companies on their worldwide income, so any money that is untaxed by the host country will be taxed by the home country instead.[58] Aside from revenue losses, tax incentive effects will be eliminated since the investors will be taxed either way. The existence of tax credit systems, which reduce tax liabilities in the home country by any tax paid in the host country, tips the scale in favor of not offering tax incentives.[59] Thus, unless a tax sparing clause, which allows taxpayers to credit taxes not actually paid, is included in a bilateral agreement between the home and host states, the incentives are merely subsidizing the home country.[60]

This argument is currently far from straightforward and, while it carries weight, it also has limitations. There is a growing trend to abandon worldwide taxation systems and move to territorial structures, especially between OECD Member States that are the home countries of 85% of multinational enterprises.[61] In 2013, only eight countries of the OECD members (the United States, Greece, Chile, Poland, Korea, Israel, Ireland, and Mexico) adopted worldwide taxation, while 28 countries, including EU countries, adopted a territorial system.[62] In late 2017, the United States shifted to a form of a territorial tax system.[63]

This movement tips the scale back to granting tax incentives since, at least in theory, foreign income is not taxed under a territorial system. Thus, multinationals hailing from resident states with territorial systems, in theory, should be able to keep the benefit of any tax incentives offered by source countries. However, the reality is much more complex as there is no pure territorial system, and each country's regime differs substantially. The OECD countries, which are considerably dissimilar, tax some forms of foreign income, but each also has limitations:

Markets: Developing Countries 24–25 (Int'l Monetary Fund, Working Paper No. WP/00/35, 2000).

[58] Thornton Matheson et al., *supra* note 54, at 3.

[59] *See Avi-Yonah Globalization 2000*, *supra* note 31, at 1642 ("If a foreign tax credit is available in the investor's home country, the investor is unaffected by the host-country tax (since she would have to pay the tax to either the home or the host jurisdiction).").

[60] *See, e.g.*, OECD FDI INCENTIVES, *supra* note 51, at 43–46 (describing tax sparing); Jinyan Li, *Improving Inter-nation Equity Through Territorial Taxation & Tax Sparing, in* GLOBALIZATION AND ITS TAX DISCONTENTS: TAX POLICY AND INT'L INVESTMENTS 128–29 (Arthur J. Cockfield ed., 2010).

[61] Reuven S. Avi-Yonah, *Globalization and Tax Competition: Implications for Developing Countries*, 44 L. QUADRANGLE NOTES 60, 65 (2001).

[62] Matheson et al., *supra* note 54, at. 4.

[63] *See* Daniel N. Shaviro, *The New Non-Territorial U.S. International Tax System*, TAX NOTES, July 2, 2018, at 57–58 (discussing some aspects of the new hybrid non-territorial system post-Tax Cuts and Jobs Act).

> Whether and to what extent foreign income is taxed depends on various considerations: the type of income (active or passive) and its percentage of the overall foreign profit, the type of business, the shareholding percentage requirement of controlled foreign corporations (CFC), the foreign country's CIT rate, and whether the foreign country is listed by the home country as a tax haven or low tax jurisdiction, whether it has a tax treaty with the home country, and whether the host country is an EU member.[64]

Even with these rules that enable countries to tax foreign income under territorial systems, there is still opportunity for exemption and deferral of income earned abroad.[65]

Some predict that the shift to a territorial system has resulted in "probably very little" revenue transfer to the home countries.[66] Beyond prediction, the exact impact of the recent trend on tax incentives is still unknown. The elimination of tax incentives also does not ensure that there is no transfer of revenues. The abovementioned description of the hybrid territorial systems does not directly concern tax incentives, but rather the host state's general tax regime and whether companies use the regime abroad to shift profits. Thus, even if tax incentives are eliminated, adopting a "low" tax rate (for which there is *currently* no global standard that determines what is considered low) might still result in a transfer of revenue. Again, adopting the OECD minimum global tax proposal might change the effectiveness of tax incentives and whether they result in a transfer of revenue.

The value of tax sparing clauses is questionable today. Tax sparing is a tool often used by developed countries to aid low-income countries and to preserve the competitive advantages of their firms abroad.[67] Currently, for different reasons, OECD countries are unenthusiastic about granting tax

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[64] Kyle Pomerleau & Kari Jahnsen, *Designing a Territorial Tax System: A Review of OECD Systems*, TAX FOUND. FISCAL FACT, Aug. 1, 2017, at 4–6, 15–21.

[65] *Cf.* Reuven S. Avi-Yonah, *Globalization, Tax Competition and the Fiscal Crisis of the Welfare State: A Twentieth Anniversary Retrospective* 9 (L. & Econ. Working Paper, Paper No. 159, 2019) (recommending that G20 countries "to further strengthen CFC rules to eliminate exemption or deferral" of active income which implies these countries still do not currently fully tax foreign income).

[66] Eric Zolt, *Tax Incentives: Protecting the Tax Base* 36, 39 (2015), https://www.un.org/esa/ffd/wp-content/uploads/2015/04/2015TIBP_PaperZolt.pdf. However, the author notes that the ongoing changes in how foreign income is taxed might amend this conclusion. In particular, he states that "[d]epending on the form of minimum tax adopted, it may be that the desirability of tax incentives to foreign investors will be reduced." *Id.* at 39.

[67] *See* OECD, *Tax Sparing: A Reconsideration, in* MODEL TAX CONVENTION ON INCOME AND ON CAPITAL 13 (2019).

sparing when they (re)negotiate tax treaties and these countries tend to limit the scope of tax sparing clauses.[68] The United States has similarly been unenthusiastic and has never utilized tax sparing.[69] After reviewing tax treaties in the four GCC states that have broad-based CIT, only approximately 10% of their treaties with OECD countries include a tax sparing clause.[70] Regardless, as countries become more territorial, the tax sparing clause may be of less concern.[71]

E. Undermine Tax Revenues

Critics view incentives as detrimental to the states offering them due to the forgone tax revenue which, in the absence of the incentives, is due.[72] As a consequence, incentives jeopardize the ability to provide public goods and services, and shift the tax burden from CIT to a less mobile tax-base, such as consumption.[73] Incentives could also shift the burden from foreign investors to local firms when incentives are only granted to foreign investments.[74] This argument has merits because tax incentives inherently

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[68] *See id.* at 19–20 (stating that tax sparing provides an opportunity for tax avoidance, is difficult to administer, and benefits the investors rather than the host country); United Nations, *Tax Incentives and Foreign Direct Investment* 29 (ASIT Advisory Studies No. 16, 2000), https://unctad.org/system/files/official-document/iteipcmisc3_en.pdf (asserting that tax sparing may have the unintended effect of encouraging investors "to repatriate profits rather than to reinvest them in the host country where they would further promote economic development"); Brooks, *supra* note 25, at 547–58 (analyzing the case for and against tax incentives and concluding that developed countries should not grant tax sparing).

[69] Tanzi & Zee, *supra* note 57, at 14 n.25.

[70] This author reviewed the English version of 96 bilateral treaties available at the International Bureau of Fiscal Documentation (IBFD) website with Oman, Kuwait, Qatar, and the KSA. Only ten of these treaties have tax sparing.

[71] *But see* Céline Azémar & Dhammika Dharmapala*, Tax Sparing Agreements, Territorial Tax Reforms, and Foreign Direct Investment,* 169 J. PUB. ECON. 89, 91 (2019).

[72] *E.g.*, Brunori, *supra* note 39, at 53 (arguing that countries "fail to collect as much revenue as would be collected without the incentive program").

[73] *E.g.*, Peter Calcagno & Frank Hefner, *Economic Development Tax Incentives: A Review of the Perverse, Ineffective, and Unintended Consequences*, *in* FOR YOUR OWN GOOD: TAXES, PATERNALISM, AND FISCAL DISCRIMINATION IN THE TWENTY-FIRST CENTURY 225–27 (Adam J. Hoffer & Todd Nesbit eds., 2018).

[74] *See, e.g.*, Avi Nov, *Tax Incentives for Foreign Direct Investment: The Drawbacks*, 38 TAX NOTES INT'L 263, 267 (2005) [hereinafter *Nov Incentives Drawbacks*]; *but see* Addy Mazz, *Constitutional Framework of Tax Free Zones*, *in* SPECIAL TAX ZONES IN THE ERA OF INTERNATIONAL TAX COORDINATION 57 (Antti Laukkanen et al. eds., 2019) (arguing that incentives do not conflict with the ability to pay or represent unequal treatment of persons with similar economic abilities because "if their purpose is the development of the country and in this way they increase employment, tax incentives are compatible with those principles").

result in lost CIT revenues from incentives' recipients. However, a few notes complicate this argument.

First, tax revenues are not the only value that foreign investors bring to the table; the argument ignores non-monetized benefits.[75] These benefits include increased employment, transfers in technology, enhanced international competitiveness, accelerated regional development within one country, increasing or even initiating local goods production, as well as opening up new sectors and access to foreign markets, all of which ultimately induce further investments.[76] These benefits are of a particular interest to developing and capital-importing countries like the GCC states; for instance, the KSA "remains primarily a capital-importing country, where equipment, skills and technology are purchased from foreign suppliers, mainly from industrialized nations."[77] In fact, GCC states have been unequivocally vocal about their need to transfer knowledge.[78] They are also facing enormous employment challenges, and the cost of their public sector employment is unsustainable; in 2018, approximately 65% of the nationals in the GCC region were employed by the government.[79] This dependence on government employment comes at a high cost; between 40% and 60% of public budgets are spent on salaries.[80] Thus, bringing foreign capital to the GCC region is important. However, some note that these benefits do not automatically result from foreign investments and depend on other elements, such as the ability of the local firms to learn from and adopt foreign technologies and skills.[81]

Second, people have claimed that since tax incentives are to some extent effective in attracting investment, incentives might increase tax

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[75] *E.g.*, Telford & Ures*, supra* note 24, at 608 ("Increased education, improvements in standards of living, and a location's image in the global economy as favorable are all benefits of FDI that are difficult, if not impossible, to quantify.").

[76] *E.g.*, Elkins, *supra* note 30, at 918; Louis Brennan & Frances Ruane, *A Holistic Approach to Investment Incentives*, *in* RETHINKING INVESTMENT INCENTIVES: TRENDS AND POLICY OPTIONS 189–91 (Ana Teresa Tavares-Lehmann et al. eds., 2016); OECD FDI INCENTIVES, *supra* note 51, at 19–20.

[77] Vladimir A. Gidirim, *Taxation of Foreign Multinational Enterprises Conducting Business in and with Saudi Arabia*, 70 BULL. INT'L TAX'N 230, 230 (2016).

[78] *See* Law Decree No. 8 of 2001 Regarding Organization of Direct Investment of Foreign Capital in the State of Kuwait (listing the need for transfer of technology as one of the goals behind adopting the law).

[79] OLIVER WYMAN, MAXIMIZING EMPLOYMENT OF NATIONALS ON THE GCC 5 (2018), https://www.oliverwyman.com/content/dam/oliver-wyman/v2/publications/2018/october/maximizing-employment-of-nationals-in-the-gcc.pdf.

[80] *Id.* at 3.

[81] *See* Magnus Blomström & Ari Kokko, *The Economics of International Investment Incentives* 8 (Ctr. Econ. Pol. Rsch., Discussion Paper No. 3775, 2003), https://www.researchgate.net/publication/5094506_The_Economics_of_Foreign_Direct_Investment_Incentives.

revenues.[82] To explain, if a company, lured to a place because of tax incentives, is granted any form of tax incentives apart from a tax holiday, this company will pay taxes that were otherwise not due. For instance, if this company would have $100,000 in taxes but its tax liability was reduced to $80,000 due to tax incentives, this $80,000 is more than the zero in tax revenues that would have resulted if this company did not operate at all. Also, since investments will bring well-paid employees who pay taxes on their consumption and properties, this *might* result in an increase of revenues from other types of taxes. Although this theoretical counter argument is sensible, empirical evidence is lacking regarding the impact on overall tax revenues of tax incentives in the GCC region.

Third, the argument to shift the burden from mobile to less mobile bases has weight in countries where the burden is shifted to taxpayers who will be viewed as paying taxes for the public goods they and foreigners consume.[83] This is problematic from an equity perspective. However, just because this consequence is undesirable in the rest of the world does not mean it is unacceptable in the GCC region; shifting the burden from foreign investors to individuals and domestic companies is not necessarily a bad outcome. As described in Part I, the GCC states impose no or minimal tax on individuals and local firms, while foreign firms bear almost the entire tax burden. This practice is unjust, limits the states' ability to employ taxes as an instrument to achieve policy objectives, has undesirable political effects, and is inconsistent with World Trade Organization (WTO) agreements, among other issues.

To explain, in terms of individual taxation, the states recently introduced consumption taxes in the region. This introduction came after unprecedented cuts in CIT rates and the introduction of tax incentives; thus, the burden might have indeed shifted.[84] Aside from raising revenues, taxes are governments' tool to redistribute wealth, encourage individuals to save money, and decrease the use of goods that endanger environments or health.[85] Thus, levying VAT and sin taxes provides a policy lever for the states. A study has found that levying sin taxes on cigarettes in the KSA has resulted in a "statistically significant reduction in smoking."[86] Additionally, the absence of individual taxes has a political impact; a study linked the absence of taxes

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[82] *See* James, *supra* note 44, at iv.

[83] *E.g.*, *Avi-Yonah Globalization 2000*, *supra* note 31, at 1624.

[84] Alsultan, *supra* note 2, at 366–73.

[85] *See* OECD FDI INCENTIVES, *supra* note 51, at 13–14 (stressing that taxes on individuals play a vital role in the redistribution of wealth, allocate resources, and raise revenues).

[86] Abdulrahman Alghamdi et al., *Smoking Behaviour After Enforcement of a 100% Tax on Tobacco Products in Saudi Arabia: A Cross-sectional Study*, 26 E. MEDITERRANEAN HEALTH J. 39, 39 (2020).

prior to 2016 to the lack of political transparency and accountability in the region.[87]

Likewise, regarding the shift of burden to domestic firms, CIT is considered as a price for public goods and services and could be used to influence companies' economic decisions.[88] First, discriminatory taxes have been widely criticized for reducing foreign companies' competitive advantages over domestic ones. In particular, an IMF study pointed out that the discriminatory practice in the GCC region undermined the states' efforts to encourage foreign investment.[89] Thus, eliminating those comparative advantages would be a major reason for foreign companies to enter a GCC state. Second, current discriminatory practices have raised questions within the WTO since this practice likely violates the WTO anti-discrimination obligation.[90] Third, the shift of burden can rebalance equity in the region since it is not fair for foreign companies to bear all of the tax burdens while GCC companies enjoy public goods and services tax-free in most cases. Thus, shifting the burden will eliminate any suspicion about the states' practices. In conclusion, moving the tax burden to GCC individuals and companies might be a situation that results in an unforeseen positive outcome.

However, it could be argued that nothing guarantees that the states will shift, or further shift in the case of individuals, the burden. Instead, the government might decide to cut spending on public goods. The concern is not that governments might not shift the burden— UAE and Kuwait have announced their intention to impose corporate tax on nationals, and GCC states are considering increasing VAT rates and taxing more goods with the sin tax.[91] The genuine concern is that governments might choose to do both; shifting the burden and cutting spending. Cutting spending on public goods

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[87] Donald L. Losman, *The Rentier State and National Oil Companies: An Economic and Political Perspective,* 64 MIDDLE E. J. 427, 435 (2010).

[88] *See* OECD FDI INCENTIVES, *supra* note 51, at 15.

[89] IMF, *Tax Policy Reforms in the GCC Countries: Now and How?*, Annual Meeting of Ministers of Finance and Central Bank Governors 10 (Nov. 2015).

[90] In regards to the WTO, Kuwait and the KSA tax policies were questioned during a WTO session—while Kuwait asserted that a law is being drafted to eliminate differentiation between foreign and national companies, the KSA made no such promise. *See* WTO, *Report of the Working Party on the Accession of the Kingdom of Saudi Arabia to the World Trade Organization*, at 9, WTO Doc. WT/ACC/SAU/61/Add.2 (Nov. 1, 2005); WTO, *Trade Policy Review the State of Kuwait*, at 60, WTO Doc. WT/TPR/M/258/Add.1 (Mar. 26, 2012).

[91] *See, e.g.*, Resolution of the Ministerial Council at the 141st preparatory session (Nov. 2016). GCC O.J Y. 5 no. 17 (Jan. 15, 2017) at 16. (the GCC Supreme Council has authorized the GCC Financial and Economic Cooperation Committee to determine a timeline to increase the VAT rate from 5% to 10% at the GCC level).

could negatively reduce investments.[92] Thus, the merits of this counterargument depends on how the GCC states choose to react.

It could be claimed, however, that the loss of tax revenues is not the only cost that comes with tax incentives. Corruption, tax avoidance, and erosion are other costs to consider.[93] While it is true that tax incentives could incur these significantly important costs, they are commonly associated with discretionary incentives and tax holidays. For instance, investors might attempt to bribe officials to adopt or grant incentives if they are conferred based on the authorities' discretion.[94] Another opportunity for corruption might arise when tax authorities do not require filing a tax return during tax holidays since taxpayers are being exempted. In the absence of tax returns, incentives facilitate corruption since tax returns help uncover corruption crimes when tax audits review suspected transactions.[95] However, these costs are associated with discretionary incentives, and tax holidays and not inherited in tax incentives; thus, these costs can be avoided by adopting other forms of tax incentives and non-discretionary incentives.

As for tax evasion, when incentives are only granted to foreign investors, taxpayers might attempt to shift the tax burden from domestic firms to foreign ones causing revenue loss and increasing the administrative cost.[96] However, the fear of shifting the tax burden to foreign enterprises is currently unlikely in the GCC, as described in Part I; except for Oman, the states do not tax domestic businesses or tax them at a rate ranging between 1% and 2.5%.With this low rate, the domestic business has almost no incentive to shift

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[92] *See* Perkins, *supra* note 38, at 16 (pointing out that tax incentives result in less revenues which might result in less public goods and accordingly reduce investments).

[93] *E.g.*, Brooks, *supra* note 25, at 542–44.

[94] *E.g.*, *Zolt Tax Incentives*, *supra* note 43, at 12 ("The opportunity for corruption is much greater for tax incentives regimes where officials have much discretion in determining which investors or projects receive favorable treatment. The potential for abuse is also greater where no clear guidelines exist for qualification."); *Nov Tax Incentives to Entice FDI*, *supra* note 17, at 692 (pointing out that "foreign investors may easily bribe and conspire with government officials, thereby influencing domestic politics of the host country to secure tax incentives for their investments"); Calcagno & Hefner, *supra* note 73, at 227–28.

[95] *See* OECD, MONEY LAUNDERING AND TERRORIST FINANCING AWARENESS HANDBOOK FOR TAX EXAMINERS AND TAX AUDITORS (2019) http://www.oecd.org/tax/crime/money-laundering-and-terrorist-financing-awareness-handbook-for-tax-examiners-and-tax-auditors.pdf (offering guidance in recognizing corruption during the conduct of tax audits).

[96] *E.g.*, *Zolt Tax Incentives*, *supra* note 43, at 21 (noting that transfer pricing issues might occur in one country); *Nov Tax Incentives to Entice FDI*, *supra* note 17, at 692; Zee et al., *supra* note 44, at 1501 (noting that tax incentives "can often absorb a substantial amount of quality administrative resources[,] a scarce commodity in most developing countries"); Brooks, *supra* note 25, at 542 (noting that foreign firms might shift income to domestic firms); Charles Mclure, *Tax Holidays and Investment Incentives a Comparative Analysis*, 53 BULL. INT'L FISCAL DOC. 326, 334 (1999).

the burden to foreign investors. If anything, granting incentives will do just the opposite; it will decrease the motive for foreign firms to shift the tax burden to local ones.

F. *Distort Investment Decisions*

Commentators claim that incentives have international consequences—incentives distort economic activities that affect global welfare.[97] In particular, incentives "will cause allocation of resources that may result in too much investment in certain activities or too little investment in other non-tax favored areas."[98] It is worth noting that this claim implicitly acknowledges that incentives are, in fact, effective because, if incentives do not work, they do not distort behavior. This argument is flawed because it ultimately criticizes incentives for fulfilling their goal; incentives are meant to attract investors and alter locational decisions. This argument is not convincing when the distortion is intended.

IV. TAX INCENTIVES' LEGAL FRAMEWORK IN THREE COMMON MARKETS

Thus far, this paper has concluded that, overall, when considering the arguments against incentives, it is impossible to arrive at a firm conclusion regarding tax incentives in the GCC region due to the lack of empirical evidence that considers the ongoing changes in tax policies worldwide. This part explores the legal framework of tax incentives in the U.S., EU, and GCC common markets to compare the advantages and disadvantages of each approach in Part IV and inform policy makers when they are considering which approach to adopt.

While there is vast scholarship analyzing and comparing the U.S. and EU common markets' legal framework of tax incentives,[99] this work is the

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[97] *Nov Incentives Drawbacks*, *supra* note 74, at 268; Melvin L. Burstein & Arthur J. Rolnick, *Congress Should End the Economic War Among the States*, 9 THE REGION 2 (1995) https://www.minneapolisfed.org/article/1995/congress-should-end-the-economic-war-among-the-states. *But see* Elkins, *supra* note 30, at 925–30 (rejecting this argument in the context of tax competition in general).

[98] *Zolt Tax Incentives*, *supra* note 43, at 11.

[99] On comparison between the EU and United States regarding tax incentives, see, for example, Ruth Mason, *Common Markets, Common Tax Problems*, 8 FLA. TAX REV. 599, 624–28 (2007) [hereinafter *Mason Common Markets*]; Janet E. Milne, *Energy Tax Incentives in the United States: A Comparative Perspective on State Aid*, 16 EUR. ST. AID L. Q. 34, 42–45 (2017); Alan O. Sykes, *The Questionable Case for Subsidies Regulation: A Comparative Perspective*, 2 J. LEGAL ANALYSIS 473, 477–80, 486–90 (2010); Marcos André Vinhas Catão, *Current Scenario of the Tax Incentives in Brazil: A Comparison*

first scholarly attempt to extend the comparison to the GCC. The attitudes toward tax incentives in the United States and the EU can be summarized as follows: while states in the United States are permitted to offer incentives, the EU State Aid Rule limits the ability of the member states to offer targeted tax incentives.[100] The GCC states have harmonized tax incentives that are offered to industrial enterprises by adopting a binding law and have harmonized incentives granted to foreign investments by adopting a soft law.[101] However, in the absence of a GCC binding agreement forbidding further incentives, the GCC states are free to offer tax incentives since there is no GCC rule similar to EU State Aid that limits targeted tax incentives. Since the GCC states harmonized locational incentives with a soft law that is not binding, the states are free to offer incentives to entice foreign investment.

A. *United States*

Locational tax incentive competition between states is very aggressive in the United States and has been frequently called a bidding war and a new civil war.[102] Congress has vast authority to curb competition between the states under the Commerce Clause of the Constitution but has chosen not to regulate tax incentives. The U.S. Supreme Court has interpreted the Commerce Clause to allow states to use their tax systems to maintain and entice new business investment provided they do not discriminate between residents and non-residents.[103] However, the constitutionality of tax incentives and subsidies under the Commerce Clause is still an open question.

This section first describes Congress's reluctance to regulate incentives and the Supreme Court's jurisprudence on incentives. Next, it explores how companies have managed to manipulate states to pressure them to offer generous incentive packages to successful businesses to expand their operations within the state's border.

i. *The Commerce Clause: Between the Congress and the Court*

The Commerce Clause of the U.S. Constitution states that "Congress shall have Power ... To regulate Commerce … among the several States."[104] It has been understood to afford Congress the authority to regulate

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Based on the Concepts of State Aid in Europe and of the Commerce Clause in the United States, 35 INTERTAX 638 (2007).

[100] For an examination on the US system, see *infra* Part III(1). For an examination on the EU system, see *infra* Part III(2).

[101] For an examination on the GCC system, see *infra* Part III(3).

[102] *E.g.*, Robert Guskind, *The New Civil War*, 25 NAT'L J. 817, 821 (1993).

[103] *See infra* Part (III)(1)(i).

[104] U.S. CONST. art. I, § 8, cl. 3.

competition, including tax incentive competition.[105] Despite this congressional power, Congress does not interfere in competition between the states,[106] with a few exceptions.[107] Some attribute Congress's reluctance to the "uphill battle" it would face from states and businesses.[108] Thus, scholars note that "[t]ax competition among the states, whether harmful or not, is simply not generally regarded as an object of federal concern."[109]

While the Commerce Clause grants Congress the affirmative power to regulate interstate commerce, the same clause—commonly referred to as the Dormant Commerce Clause—has been understood by the Supreme Court as imposing a negative obligation on the states that restricts their ability to burden or regulate interstate commerce.[110] The goal of the Dormant Commerce Clause is to maintain the U.S. common market where individuals, capital, and services can move freely.[111] Under the Court's jurisprudence, although the states can "structure[e] their tax systems to encourage the growth and development of intrastate commerce and industry… [and] compete with

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[105] *E.g.*, Peter D. Enrich, *Saving the States from Themselves: Commerce Clause Constraints on State Tax Incentives for Business*, 110 HARV. L. REV. 377, 405 (1996) (indicating "[t]here is little question that Congress has the authority under the Commerce Clause to adopt . . . a statutory restriction.").

[106] *E.g.*, Thomas F. Field, *Tax Competition in Europe and America*, 98 TAX NOTES 2045, 2047-48 (2003); Daniel Shaviro, *An Economic and Political Look at Federalism in Taxation*, 90 MICH. L. REV. 895, 952 (1992) [hereinafter *Shaviro Federalism*] (noting that generally, and not merely with regards to tax incentives, "Congress has almost never barred or restrained state and local taxes that created burden — even though judicial review of state and local taxation under the negative Commerce Clause does not make its role wholly redundant.").

[107] *See* Tracy A. Kaye, *The Gentle Art of Corporate Seduction: Tax Incentives in the United States and the European Union*, 57 U. KAN. L. REV. 93, 147–48 (2008) (listing a few examples where Congress interferes to regulate interstate commerce).

[108] Enrich, *supra* note 105, at 406 ("Business advocates would vigorously oppose such a proposal, because it would deprive businesses of the benefits of state tax competition. Even the states might view such a measure as a threat to their relative competitive positions and as a restriction on their freedom of action."); *See Shaviro Federalism*, *supra* note 106, at 954 (summarizing legal and economic scholarship and concluding that Congress "usually tries to avoid conflictual issues altogether or defer their resolution to agencies and courts").

[109] Field, *supra* note 106, at 2047.

[110] *See* Freeman v. Hewit, 329 U.S. 249, 252 (1946) ("[T]he Commerce Clause was not merely an authorization to Congress to enact laws for the protection and encouragement of commerce among the States, but by its own force created an area of trade free from interference by the States. In short, the Commerce Clause, even without implementing legislation by Congress, is a limitation upon the power of the States."); Deborah H. Schenk, *The Cuno Case: A Comparison of U.S. Subsidies and European State Aid*, 2006 EUR. ST. AID L. Q. 3, 3 (2006); Kevin Thompson & Diann L. Smith, *The Commerce Clause and the Constitutionality of State Business Tax Incentives*, 10 ST. & LOC. TAX LAW. 1, 3 (2005).

[111] *See, e.g.*, Great Atl. & Pac. Tea Co. v. Cottrell, 424 U.S. 366, 380 (1976); Hunt v. Washington State Apple Advert. Comm'n, 432 U.S. 333, 350 (1977).

other States for a share of interstate commerce," they cannot, by their own act, jeopardize the common market by imposing discriminatory taxes.[112] The basic concept is that states cannot impose higher taxes on non-residents than the states do on residents, or treat residents of other states more unfavorably than in-state residents. The Court has struck down discriminatory tax advantages, indicating that the Dormant Commerce Clause functions as the main constitutional limit on the states' taxing power.[113]

The Court has not determined the constitutionality of locational investment incentives which causes ongoing debate. In 2004, the Sixth Circuit Court of Appeals, in *Cuno v. Daimler Chrysler Inc.*, invalidated Ohio's investment tax credits, which were designed to attract investments into economically depressed areas, as violating the Commerce Clause because the incentive granted preferential treatment to in-state investments.[114] This treatment was viewed as coercing businesses to expand locally rather than out-of-state.[115] However, the case was later vacated in part by the Supreme Court because the taxpayers lacked standing, meaning the Court did not review the merits of the case.[116]

Direct subsidies are a different story. Although tax incentives and subsidies are considered economically equivalent—meaning the grant of a subsidy and forgiving taxes produce the same result[117]—the Supreme Court

[112] Bos. Stock Exch. v. State Tax Comm'n, 429 U.S. 318, 336–37 (1977). However, if "discrimination is . . . justified by a valid factor unrelated to economic protectionism," then it can be tolerated. New Energy Co. of Indiana v. Limbach, 486 U.S. 269, 274 (1988).

[113] *See, e.g.*, *Bos. Stock Exch.*, 429 U.S. at 336 (invalidating the New York transfer tax on security transactions because it reduces the rate only for in-state sales made by non-residents of New York); Westinghouse Elec. Corp. v. Tully, 466 U.S. 388, 407 (1984) (invalidating New York tax credit designed to benefit state's exports and discriminates against export shipping from other states); *Limbach*, 486 U.S. at 269 (striking down Ohio "tax credit against … motor vehicle fuel sales tax for each gallon of ethanol sold (as a component of gasohol) by fuel dealers, but only if the ethanol is produced in Ohio or, if produced in another state, to the extent that State grants similar tax advantages to ethanol produced in Ohio").

[114] Cuno v. Daimler Chrysler, Inc., 386 F.3d 738 (6th Cir. 2004), *vacated in part sub nom.* Daimler Chrysler Corp. v. Cuno, 547 U.S. 332 (2006).

[115] *Cuno v. Daimler Chrysler, Inc.*, 386 F.3d at 746.

[116] *Daimler Chrysler Corp. v. Cuno*, 547 U.S. at 354. An element that contributes to the limited instances where the Court settles the merits of a tax incentive dispute is that the Court often finds the parties lack standing. Some have argued that the states themselves have standing. Enrich, *supra* note 105, at 418–23. However, it has been noted that the states are not interested in suing since over half of the states supported Ohio in *Cuno*. Kaye, *supra* note 107, at 132.

[117] *See, e.g.*, Comment, *Tax Incentives As State Action*, 122 U. PA. L. REV. 414, 420–21 (1973) (arguing that the direct government subsidies and tax benefit incentives are economically equivalent); Lilian V. Faulhaber, *Charitable Giving, Tax Expenditures, and Direct Spending in the United States and the European Union*, 39 YALE J. INT'L L. 87, 101 (2014) [hereinafter *Faulhaber 2014*] ("Although direct spending and tax expenditures are

seems to view them differently. Unlike the EU State Aid Rule, in which both direct subsidies and targeted tax incentives are prohibited unless authorized by the EU Commission, in 1988, the Supreme Court appears to favor subsidies.[118] As it stated,

> [t]he Commerce Clause does not prohibit all state action designed to give its residents an advantage in the marketplace, but only action of that description *in connection with the State's regulation of interstate commerce*. Direct subsidization of domestic industry does not ordinarily run afoul of that prohibition; discriminatory taxation . . . does.[119]

The closest the Court has come to examining subsidies was in *West Lynn Creamery v. Healy*, a 1994 case involving a tax on milk dealers in Massachusetts.[120] The Court held that designing a non-discriminatory tax imposed on all businesses but later distributing the collected funds as subsidies to only local businesses constituting "conjoining a tax and a subsidy" and violated the Commerce Clause.[121] However, the Court asserted that a "pure subsidy funded out of general revenue *ordinarily* imposes no burden on interstate commerce, but merely assists local business."[122] In *Cuno*, the Sixth Circuit Court rationalized the difference, indicating "the distinction between a subsidy and a tax credit, in the constitutional sense, results from the fact that the tax credit involves state regulation of interstate commerce through its power to tax."[123] No further explanation for differentiation from the Court has been provided. Although it "never squarely confronted the constitutionality of subsidies,"[124] the above discussion suggests that direct subsidies are compatible with the Commerce Clause.[125]

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often approved through different political processes, they are generally accepted in the tax and economics literature as being economically equivalent.").

[118] *See Mason Common Markets*, *supra* note 99, at 627–28; *Faulhaber 2014*, *supra* note 117, at 125.

[119] New Energy Co. of Indiana v. Limbach, 486 U.S. 269, 278 (1988).

[120] W. Lynn Creamery, Inc. v. Healy, 512 U.S. 186 (1994).

[121] *Id.* at 187.

[122] *Id.* at 199 (emphasis added).

[123] Cuno v. Daimler Chrysler, Inc., 386 F.3d 738, 746 (6th Cir. 2004*), vacated in part sub nom.* Daimler Chrysler Corp. v. Cuno, 547 U.S. 332 (2006).

[124] *W. Lynn Creamery*, 512 U.S. at 199 n.15.

[125] *Mason Common Markets*, *supra* note 99, at 627 ("[T]he Circuit Court distinguished the investment tax credit from direct subsidies, suggesting, as has the Supreme Court, that direct subsidies do not violate the Commerce Clause.").

ii. *How Companies Manipulate States; Amazon HQ2 as an Example.*

Amazon's process for establishing its second headquarters was an excellent illustration of how companies, in the absence of congressional action and with minimal judicial review, manipulate the states to "one-up" each other's tax incentive bids. To provide some background, in 2017, Amazon drafted a seven-page Request-For-Proposals (RFPs) to publicly invite states and communities in North America to submit proposals within a six-week deadline to host its second headquarters.[126] To initiate a frantic bidding war, Amazon estimated the new campus would create 50,000 jobs with an average salary of $100,000 per year and $5 billion in investments over fifteen to seventeen years.[127]

The Amazon RFPs gained significant attention because it was the first public call for bidding when the process is usually conducted covertly.[128] Holly Sullivan, Amazon's Global Head of Economic Development, justified the public RFPs, claiming that the project "will have an impact on a community. So we wanted to make sure we were having open dialogue and receiving invitations from locations that wanted to partner with us for the long term."[129] Ms. Sullivan indicated the RFPs were intentionally designed to create wide competition.[130] Any site in North America could qualify if it was within thirty miles of a population center, within forty-five minutes to and from an international airport, no more than two miles to a major highway, and had on-site access to mass transits.[131]

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[126] AMAZON, AMAZON HQ2 REQUEST FOR PROPOSAL 1 (Sep. 7, 2017), https://images-na.ssl-images-amazon.com/images/G/01/Anything/test/images/usa/RFP_3._V516043504_.pdf [hereinafter AMAZON HQ2 RFP].

[127] *Id.*

[128] *Episode 55: After the HQ2 Reversal: 25 Minutes with Mike Grella, Amazon's Former Director of Economic Development*, DCI (Feb. 20, 2019), https://aboutdci.com/2019/02/episode-55-hq2-reversal-25-minutes-mike-grella-amazons-former-director-economic-development/ (transcribing an interview with Mr. Michael Grella, Amazon's first director of economic development and an experienced tax-incentive consultant).

[129] Ethan Rothstein & Jon Banister, *Exclusive: Amazon Real Estate Head Holly Sullivan Has No Regrets About The HQ2 Search*, BISNOW (Feb. 21, 2019), https://www.bisnow.com/washington-dc/news/economic-development/exclusive-amazon-real-estate-head-holly-sullivan-has-no-regrets-about-the-hq2-search-97628?utm_source=CopyShare&utm_medium=Browser.

[130] When asked whether Amazon was looking for an urban or suburban site, Ms. Sullivan responded, "We really wanted to keep it open. We learned a lot about ourselves in this process too, and I think that's sometimes been lost in the conversation." *Id.*

[131] AMAZON HQ2 RFP, *supra* note 126, at 2.

Amazon cited eight factors that impacted the selection process, and any proposal had to illuminate how the proposed location would be the perfect fit to host the new Amazon headquarters. These factors—which the RFPs indicated were not ranked according to their importance—were site, capital and operation costs, incentives, labor force, logistics, cultural community fit, and community quality of life.[132] As for incentives, the RFPs explained that the proposal needed to "[i]dentify incentive programs available for the Project at the state/province and local levels[, o]utline the type of incentive (i.e. land, site preparation, tax credits/exemptions, relocation grants, workforce grants, utility incentives/grants, permitting, and fee reductions) and the amount."[133] The RFPs emphasized that the "incentives offered … will be significant factors in the decision-making process."[134]

In response, Amazon received 238 bids before narrowing the list to twenty.[135] Contrary to the "open dialogue" policy Amazon had claimed to embrace, the company asked the finalists to sign non-disclosure agreements (NDAs) before further negotiations could take place.[136] The tax incentives included serious ten-digit numbers; the available data indicates that packages ranged from $1 billion offered by Atlanta to $8.5 billion by Maryland.[137] To make these offers, some cities had to pass laws to approve the incentive packages.[138]

Fourteen months after announcing the RFPs, conducting various visits, and negotiating with state and local officials, Amazon revealed its pick for its two new headquarters—New York (which Amazon later decided to cancel after political backlash)[139] and Northern Virginia.[140] Picking two headquarters was unexpected since the RFPs did not indicate that Amazon

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[132] *Id.* at 5.
[133] *Id.*
[134] *Id.*
[135] Billy Hamilton, *Amazon HQ2: Infinity War*, 90 ST. TAX NOTES 877, 877 (2018).
[136] Karen Weise, *What We Don't Know About Amazon's Split HQ2*, N.Y. TIMES (Nov. 7, 2018), https://www.nytimes.com/2018/11/07/technology/amazon-hq2-know.html.
[137] On offers submitted by communities, see Alfred Ng, *Here's What the Final 20 Cities Offered Amazon for HQ2*, CNET (Jan. 18, 2018, 1:45 PM), https://www.cnet.com/news/heres-what-the-20-finalist-cities-offered-amazon-for-hq2/.
[138] For instance, Newark City Council passed an act to authorize an incentives package. *Newark City Council Approves Amazon HQ2 Incentives Creating at Least 30,000 Jobs*, CITY OF NEWARK (July 11, 2018), https://www.newarknj.gov/news/newark-city-council-approves-amazon-hq2-incentives.
[139] *Update on Plans for New York City Headquarters*, AMAZON: BLOG (Feb. 14, 2019), https://blog.aboutamazon.com/company-news/update-on-plans-for-new-york-city-headquarters.
[140] *Amazon Selects New York City and Northern Virginia for New Headquarters*, AMAZON: BLOG (Nov. 13, 2018), https://blog.aboutamazon.com/company-news/amazon-selects-new-york-city-and-northern-virginia-for-new-headquarters.

was looking for two locations.[141] Amazon announced that its original estimate of jobs and investments was to be divided between the two locations but after terminating the New York plan, Amazon decided it would still only assign half of the jobs (25,000) to Virginia despite the New York cancelation.[142]

Although the Amazon RFPs specified that incentives would play a significant role, the Amazon senior vice president indicated that incentives "did not drive this process" for Amazon.[143] Amazon's blog also emphasized that "[e]conomic incentives were one factor in [the] decision—but attracting top talent was the leading driver."[144] However, Amazon did not rank the factors in the RFPs, and both of these comments came after the conclusion of the process.

The furious competition between cities gained unprecedented attention and was accurately described as a "14-month circus,"[145] "lottery,"[146] "public auction."[147] It was even compared to the movie *Avengers: Infinity War*.[148] Amazon *possibly* orchestrated a show to entice states to sign NDAs, offer billions of dollars' worth of incentives - although it claimed incentives "did not drive this process"- and exhaust states' resources.

Michael Grella, Amazon's first director of economic development and an experienced tax-incentive consultant, claims that Amazon was a unique case and unlikely to be replicated by other companies.[149] However, there is nothing unique about Amazon except that the RFPs were public, and now it is known what often occurs behind closed doors. Even in terms of incentive packages, Amazon is not unique. Boeing, a fortune-500 company, landed an $8.7 billion tax deal, notably larger than Amazon's Virginia $2.5 billion offer, with Washington state in 2013.[150] Foxconn, Apple, Google,

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[141] AMAZON HQ2 RFP, *supra* note 126, at 1.
[142] Eugene Kim, *New York Will Lose the Bulk of the 25,000 Jobs That Were Promised by Amazon HQ2*, CNBC (Feb. 14, 2019), https://www.cnbc.com/2019/02/14/new-york-will-lose-the-bulk-of-the-25000-jobs-that-were-promised-by-amazon-hq2.html.
[143] *Amazon's Carney Says Tax Breaks Did Not Decide Where They Put HQ2*, CNBC, at 00:50 (Nov. 13, 2018), https://www.cnbc.com/video/2018/11/13/amazons-carney-says-tax-breaks-did-not-decide-where-they-put-hq2.html.
[144] *Amazon Selects New York City and Northern Virginia*, *supra* note 140.
[145] Hamilton, *supra* note 135, at 881.
[146] Daniel G. Mudd, *Jungle Warfare—Amazon HQ2 Disclosure Fights and Battle Over Tax Transparency*, 29 J. MULTISTATE TAX'N 36, 37 (2019).
[147] Greg LeRoy & Kenneth Thomas, *Lessons for the U.S.: How the EU Controls Bidding Wars for Jobs and Investment*, SHELTERFORCE (Jun. 17, 2019), https://shelterforce.org/2019/06/17/lessons-for-the-u-s-how-the-eu-controls-bidding-wars-for-jobs-and-investment/.
[148] Hamilton, *supra* note 135, at 882.
[149] *Episode 55: After the HQ2 Reversal*, *supra* note 128.
[150] *See* Niraj Chokshi, *The United States of Subsidies: The Biggest Corporate Winners in Each State*, WASH. POST (Mar. 18, 2015),

Mercedes-Benz, Honda, Hyundai, ThyssenKrupp, Nissan, and Toyota are among many other successful companies that have made deals with U.S. states.[151] The lesson to be learned from the Amazon chaos is that the failure to regulate subsidies leads directly to a bidding war during which companies manipulate states or countries to offer incentives and, which, as explained in the next section, is unlikely to happen in the EU where the state aid rule bans individual aid.

B. *European Union*

The treatment of tax incentives in the EU is unique among the common markets—targeted tax incentives are strictly limited under the state aid rule.[152] To ensure this binding rule is followed, the EU Commission monitors any suspected incentives, and the EU Courts hear disputes on non-compliance.[153]

Under the state aid rule, not all tax incentives are forbidden.[154] In order for an incentive to constitute illegal aid, three conditions must be met. The aid must (1) provide an unjustified selective advantage, (2) be granted by the state or through state resources to companies, and (3) affect competition or trade between EU members.[155] As noted, tax incentives inherently consume state resources and affect competition.[156] Thus, the actual challenge that the

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https://www.washingtonpost.com/blogs/govbeat/wp/2015/03/17/the-united-states-of-subsidies-the-biggest-corporate-winners-in-each-state/.

[151] *See id.* (ranking the top 30 tax incentives deals in the history of the United States); Perkins, *supra* note 38, at 4–12 (describing mega deals with some U.S. states).

[152] Andreas Bartosch, *State Aid Control in Europe and Elsewhere*, 5 EUR. ST. AID L. Q. 1, 1 (2006) ("One of these uniquely European things is State aid control."); Claus-Dieter Ehlermann, *State Aid Control in the European Union: Success or Failure?*, 18 FORDHAM INT'L L. J. 1212, 1213 (1995) (indicating that "[s]tate aid control is a unique feature" of the EU).

[153] *See infra* text accompanying notes 196–201.

[154] For a discussion of the impact of recent case law on state aid and taxation in the EU, see, for example, Ruth Mason, *Special Report on EU State Aid* (pts. 1–6), 154 TAX NOTES 451, 615, 735 (2017); 155 TAX NOTES 947 (2017); 157 TAX NOTES 645 (2017); 158 TAX NOTES 771 (2018). *See also* CLAIRE MICHEAU, STATE AID, SUBSIDY AND TAX INCENTIVES UNDER E.U AND WTO LAW *passim* (Richard Doernberg et al. eds., 2014) (addressing the relationship between subsidies and State aid within the context of taxation) [hereinafter MICHEAU 2014 BOOK]; STATE AID LAW AND BUSINESS TAXATION *passim* (Isabelle Richelle et al. eds., 2016) (compiling a series of essays on the current state of the relationship between "business taxation and state aid law"); CONOR QUIGLEY, EUROPEAN STATE AID LAW AND POLICY 97–152 (3d ed. 2015).

[155] Consolidated Version of the Treaty on the Functioning of the European Union, art. 107(1), Oct. 26, 2012, 2012 O.J. (C 326) 47 [hereinafter TFEU] (forbidding State Aid).

[156] Ruth Mason, *Tax Rulings as State Aid FAQ*, 154 TAX NOTES 451, 452 (2017) [hereinafter *Mason State Aid FAQ*]. *See Commission Notice on Application of the State Aid Rules to Measures Concerning Direct Business Taxation*, 1998 O.J. (C384) 3 ¶¶ 10–11

EU Commission faces in tax cases before the EU Courts is to substantiate that the incentive represents an unjustified selective advantage.[157] This has proven to be burdensome, and both bodies have been widely criticized.[158]

The concept of an advantage is "[t]he basic idea … that if the state forgoes tax that otherwise would be due under its regular tax regime, that forgone tax is an advantage conferred on the taxpayer."[159] The commission provides examples of tax measures that constitute unlawful aid including:

- a reduction in the tax base (such as special deductions, special or accelerated depreciation arrangements, or the entering of reserves on the balance sheet);
- a total or partial reduction in the amount of tax (such as an exemption or a tax credit); and
- deferment, cancellation, or even special rescheduling of tax debt.[160]

To determine whether there is an advantage, the baseline or "system of reference must be identified."[161] The purpose of the baseline is to help identify if an incentive is an advantage. Traditionally, the system of reference is the investigated state's domestic law such as the corporate income tax.[162] However, in recent cases involving advanced transfer pricing rulings (like Apple, Fiat, and Amazon), the commission opted to use its own novel rule.[163]

[hereinafter *Commission Notice on State Aid 1998*] (explaining the second and third conditions in tax measures. It is worth noting that this notice was repealed and superseded by the subsequently mentioned Commission Notice on State Aid 2016).

[157] *See* TFEU, *supra* note 155, at art. 108.

[158] *See, e.g.*, Emily Forrester, *Is the State Aid Regime a Suitable Instrument to Be Used in the Fight Against Harmful Tax Competition*?, 27 EC TAX REV. 19, 28 (2018) (discussing both the Advocate General and scholar's concerns with the unjustified selective advantage requirement); Claire Micheau, *State Aid and Taxation in EU law*, *in* RESEARCH HANDBOOK ON EUROPEAN STATE AID LAW 210 (Erika Szyszczak ed., 2011) (noting that the EU's position could be open to criticism); Phedon Nicolaides, *Fiscal State Aid in the EU: The Limits of Tax Autonomy*, 27 WORLD COMPETITION 365, 365 (2004) (noting that the commission has stretched the nation of regional selectivity "too far").

[159] *Mason State Aid FAQ*, *supra* note 156, at 453. On tax advantage, see, for example, MICHEAU 2014 BOOK, *supra* note 154, at 190–99.

[160] *Commission Notice on State Aid 1998*, *supra* note 156, ¶ 9.

[161] *Commission Notice on the Notion of State Aid as Referred to in Article 107(1) of the Treaty on the Functioning of the European Union*, 2016 O.J. (C262) 1, ¶ 128 [hereinafter *Commission Notice on State Aid 2016*].

[162] *Id.* ¶ 134.

[163] On the new EU commission approach, see, for example, Ruth Mason, *Identifying Illegal Subsidies*, 69 AM. UNIV. L. REV. 479, 505–09 (2019) [hereinafter *Mason Identifying Illegal Subsidies*]; Christopher Bobby, *A Method inside the Madness: Understanding the*

Under this rule, it "concluded that the state-aid rules themselves require all states to allocate income according to the arm's-length standard, *regardless of domestic law*."[164] To add greater uncertainty, the commission explicitly stated that applying the globally used OECD Transfer Pricing Guidelines does not necessarily protect rulings from being suspicious.[165] In late 2019, the EU Court confirmed the validity of the commission's novel rule in the Fiat case.[166] This uncertainty of state aid has effectuated wide criticism, as discussed in Part IV.

Turning to the second prong, the commission must establish that the tax advantage is selective by testing whether the advantage deviates from that baseline.[167] For a tax incentive to be selective, it must be granted only to certain companies or for the production of certain goods;[168] it does not matter whether an incentive is permanent or temporary.[169] This step tests for discrimination by comparing the recipient of the incentive in question to other companies in a similar legal and factual situation.[170] An incentive is considered materially selective if it is available depending on a firm's size or granted to some operators but not to others that are similarly situated.[171] For example, the Court of Justice of the European Union has held that an aid exclusively available for the textile industry was selective and therefore illegal.[172] Alternatively, incentives can be "regionally selective" if the central

European Union State Aid and Taxation Rulings, 18 CHI. J. INT'L L. 186 (2017) (discussing transfer pricing cases).

[164] *Mason Identifying Illegal Subsidies*, *supra* note 163, at 519.

[165] *Commission Notice on State Aid 2016*, *supra* note 161, ¶ 173 (stressing that a "transfer pricing arrangement compl[ying] with the guidance provided by the OECD Transfer Pricing Guidelines . . . is *unlikely* to give rise to State aid" (emphasis added)).

[166] *See* Case T-755/15, Grand Duchy of Luxembourg & Fiat Chrysler Fin. Eur. vs. Comm'n, ECLI:EU:T:2019:670, ¶ 151 (Sept. 24, 2019). *See also* Ruth Mason, *Implications of the Rulings in Starbucks and Fiat for the Apple State Aid Case,* 165 TAX NOTES FED. 93 (2019).

[167] *Commission Notice on State Aid 2016*, *supra* note 161, ¶ 128. On tax selectivity, see, for example, *Commission Notice on State Aid 1998*, *supra* note 156, ¶ 13–20; Michael Sánchez Rydelski, *Distinction Between State Aid and General Tax Measures*, 19 EC TAX REV. 149 (2010); Humbert Drabbe, *The Test of Selectivity in State Aid Litigation*, *in* STATE AID AND TAX LAW 87–105 (Alexander Rust & Claire Micheau eds., 2013); QUIGLEY, *supra* note 154, at 109–27.

[168] *Commission Notice on State Aid 2016*, *supra* note 161, ¶ 117.

[169] Case C-83/98, French Republic v. Ladbroke Racing Ltd & Comm'n of the Eur. Cmtys., ECLI:EU:C:2000:248, ¶ 8 (May 16, 2000).

[170] *Commission Notice on State Aid 2016*, *supra* note 161, ¶ 135; Case C-143/99, Adria-Wien Pipeline v. Comm'n, ECLI:EU:C:2001:598, ¶ 41 (Nov. 8, 2001).

[171] *Commission Notice on State Aid 2016*, *supra* note 161, ¶ 121; Rydelski, *supra* note 167, at 151–52.

[172] *See* Case 173-73, Italian Republic v. Comm'n, ECLI:EU:C:1974:71, ¶¶ 18–20 (July 2, 1974).

government unilaterally offers them only in certain regions or special economic zones.[173]

Measures available to all companies are not deemed to be selective. However, those disguised as being available to all companies when, in fact, they are only granted to some companies are deemed selective as applied.[174] Thus, if the criteria for incentives are vague or stipulate a margin of discretion to determine the recipient of incentives, then the incentives could be deemed selective.[175] The same result could happen if incentives are granted based on "criteria unrelated to the tax system."[176] Otherwise, if incentives are granted automatically once satisfying certain objective criteria, the measures will not be considered selective as long as the criteria leave no discretion for the authorities.[177]

Aside from the law, selectivity could result from favorable treatment by tax authorities. For example, an advanced tax ruling for an individual taxpayer is considered selective if it provides a lower tax burden than the ordinary rules of a CIT regime.[178] Recent cases, such as Apple, Starbucks, and Amazon, resulted in administrative tax rulings that the commission deemed favorable.[179] Similarly, a tax settlement with a particular taxpayer does not mean the treatment is selective as long as the settlement does not result in an unreasonably lower tax liability.[180]

The third step is to determine "whether the derogation is justified by the nature or the general scheme of the (reference) system."[181] The commission has listed adequate justifications for derogation. That list includes reasons relating to the proper functioning of the tax system, such as "the need to fight fraud or tax evasion, . . . the principle of tax neutrality, the progressive nature of income tax and its redistributive purposes, [and] the need to avoid double taxation."[182] On the other hand, a justification that relies on external

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[173] *See Commission Notice on State Aid 2016*, *supra* note 161, ¶¶ 142–44; Claudio Cipollini, *Special Tax Zones in the European Union: Implementing Models Under State Aid Rules,* 60 EUR. TAX'N 17, 18–19 (2020) (discussing conditions where tax advantages available only in free zones or special economic zones can avoid State Aid characterization); Pasquale Pistone, *Tax Policy and Special Tax Zones*, *in* SPECIAL TAX ZONES IN THE ERA OF INTERNATIONAL TAX COORDINATION 86–89 (Antti Laukkanen et al. eds., 2019).

[174] *Commission Notice on State Aid 2016*, *supra* note 161, ¶ 118.

[175] *Id.* ¶ 124.

[176] *Id.*

[177] *Id.* ¶ 125.

[178] *Id.* ¶ 174; *Commission Notice on State Aid 1998*, *supra* note 156, ¶¶ 21–22.

[179] On these cases, see Ruth Mason, *Tax Rulings as State Aid — Part 4: Whose Arm's-Length Standard?*, 155 TAX NOTES 947 (2017).

[180] *Commission Notice on State Aid 2016*, *supra* note 161, ¶ 176.

[181] *Id.* ¶ 128.

[182] *Id.* ¶ 139.

policies, such as environmental, industrial, or regional policy objectives, is impermissible.[183]

Since incentives are sometimes necessary to achieve policy objectives or correct market failures,[184] the EU Treaty provides exceptions to the rule. Some of these exceptions depend on the discretion of the commission, while others do not.[185] For instance, incentives to overcome national or exceptional disasters, such as floods, earthquakes, war, or terrorist attacks, are considered acceptable without the EU Commission's discretion.[186] However, EU Commission approval is required when aid is granted for causes such as the promotion of economic development or the facilitation of economic activities.[187] In order to acquire the commission's approval, the incentive must be proportional and targeted toward accomplishing the goals.[188]

The burden of proof is on the EU Commission to show whether a tax incentive is an unjustified selective advantage, but the Commission has significant powers to investigate any suspected violations.[189] EU members must notify the Commission about any tax incentives they plan to introduce,[190] and it can initiate an investigation of any existing incentives.[191] Once an investigation leads the Commission to believe an incentive is unlawful, it refers the matter to the court.[192] Two consequences will result if the court finds an incentive illegal: (1) the state must abolish or amend the incentive, and (2) the incentives must retroactively be repaid from the previous ten years with additional interest.[193] For instance, the EU Commission has estimated that without favorable tax rulings, Apple's tax

[183] *Id.* ¶ 135; Case C-143/99, Adria-Wien Pipeline v. Comm'n, ECLI:EU:C:2001:598, ¶ 52 (Nov. 8, 2001) (holding that pure ecological considerations do not justify granting tax only to manufacturing companies).
[184] *See* Diheng Xu, *Rationale Behind State Aid Control over Tax Incentives*, 41 WORLD COMPETITION 255 (2018) (explaining the rationale behind granting tax incentives).
[185] *See* TFEU, *supra* note 155, at art. 107(2)–(3). On the exceptions, see MICHEAU 2014 BOOK, *supra* note 154, at 92–102.
[186] TFEU, *supra* note 155, at art. 107(2).
[187] *Id.* at art. 107(3).
[188] *Commission Notice on State Aid 1998*, *supra* note 156, ¶ 33.
[189] On the Commission powers, see TFEU, *supra* note 155, at art. 108; EU Council Regulation 2015/1589 of 13 July 2015, Laying Down Detailed Rules for the Application of Article 108 of the Treaty on the Functioning of the European Union, 2015 O.J. (L 248) 9 [hereinafter EU Council Regulation 2015/1589]; Lilian V. Faulhaber, *Beyond Apple: State Aid as a Model of a Robust Anti-Subsidy Rule*, 48 GEO. J. INT'L L. 381, 387–88 (2017).
[190] EU Council Regulation 2015/1589, *supra* note 189, at art. 2.
[191] *Id.* at art. 12.
[192] *Id.* at art. 14.
[193] *Id.* at arts. 16, 17(1). On the recovery, see, for example, Margarida Afonso, *Recovery of Fiscal Aid*, *in* STATE AID AND TAX LAW, 57–68 (Alexander Rust ed., 2013); MICHEAU 2014 BOOK, *supra* note 154, at 377–98.

liability is $14.4 billion plus interest.[194] Once an incentive is deemed illegal, there is little margin of freedom to not recover the aid.[195] This can be problematic and impact the legal certainty of domestic laws. If a company chooses to operate in an EU state after evaluating the cost of doing business, including tax incentives, it might end up paying back all of its tax savings for the last ten years that the company legally (according to national law) obtained, because *the state* violated EU state aid rule. The recovery has been labeled a "drastic consequence,"[196] a "doozy,"[197] and an award to the EU states for their own faulty actions.[198]

C. *Gulf Cooperation Council*

The GCC common market was established in 2008.[199] However, what is the legal framework for tax incentives in the GCC common market? This question has never been addressed to the author's best knowledge. As discussed in this part, there are two projects that aim to harmonize tax incentives: a binding law adopted by the GCC that harmonized incentives offered to industrial sectors and a soft law (or non-binding commitment) that harmonized incentives offered to foreign investments. Not all incentives are harmonized; for example, the GCC States have not harmonized tax incentives offered to small and midsize enterprises.[200] Since there is no binding rule that constrains granting incentives for those entities, GCC states are free to offer any incentives that the states did not commit themselves to by a binding law to harmonize. Since GCC states have harmonized *some* incentives, this author views the GCC as taking a middle ground between the U.S. and EU approaches. This portrayal is useful since harmonizing has its inadequacies and virtues just like the other approaches; a topic that is further explained in Part IV. This section explores the GCC's lack of focus on tax incentives at the

[194] EU Commission Press Release IP/16/2923, State Aid: Ireland Gave Illegal Tax Benefits to Apple Worth up to €13 Billion (Aug. 30, 2016).
[195] The aid must be recovered by the EU States that granted the incentives, unless in exceptional circumstances such as companies' liquidations or if the commission's own acts created legitimate expectations that the aid is legal. On these exceptions, see *Mason State Aid FAQ*, *supra* note 156, at 456–57; Afonso, *supra* note 193, at 66–67.
[196] MICHEAU 2014 BOOK, *supra* note 154, at 91.
[197] *Mason State Aid FAQ*, *supra* note 156, at 455.
[198] Saturnina Moreno Gonzalez, *State Aid and Tax Competition: Comments on the European Commission's Decisions on Transfer Pricing Rulings*, 2016 EUR. ST. AID L. Q. 556, 571 (2016) ("[T]he same Member State that passed the tax ruling considered illegal and incompatible State Aid is 'awarded' with the reimbursement of the outstanding amounts plus late-payment interest.").
[199] Resolution of the Supreme Council in the Twenty-Eighth Session (Dec. 4, 2007) (Qatar) (establishing the GCC common market).
[200] *Id.*

GCC level and what is permissible or impermissible within the GCC common market.

Chiefly because of the accumulated state-owned oil revenues, GCC states widely neglected taxes and did not use tax incentives to influence economic activities until the 2000s.[201] Since the states did not utilize tax incentives to draw investment, the GCC as an organization also did not pay attention to tax incentives.[202] The new millennium was a turning point for GCC tax policies. Due to unstable oil prices, the states found they needed non-oil revenues to fund public spending and at the same realized the importance of tax policies in attracting foreign investors and influencing local ones.[203] Consequently, the states introduced tax incentives in laws regarding foreign investment, special economic zones, small and medium-sized enterprises, and the industrial sector.[204] Despite the sharp increase in tax incentives, the GCC's attitude toward tax incentives has not changed; the organization has largely overlooked them. From reviewing GCC agreements, laws, strategies, policies and plans, there is no publication that principally focuses on them; nor is there any EU State Aid-style Rule that restricts targeted tax incentives.[205]

Nevertheless, in accordance with the GCC goal to harmonize GCC states' laws,[206] two projects *indirectly* attempt to approximate tax incentives: a binding law that harmonized industrial sector incentives and a soft law that harmonized foreign investment incentives.[207] The primary goal for these laws was not to harmonize tax incentives but to harmonize GCC laws. However, tax incentives were harmonized as a result of harmonizing laws that included such incentives.

The GCC's First Economic Agreement, adopted in 1981, articulated the group's plans to reach advanced stages of economic integration by harmonizing the states' laws, including GCC investment laws.[208] Accordingly, the GCC adopted a soft law entitled *The Uniform Law for the Investment of Foreign Capital in the GCC States* in 1998.[209] The goal behind

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[201] Alsultan, *supra* note 2, at 370.
[202] *Id.* at 373–75.
[203] *See id.* at 369.
[204] *Id.* at 370–73.
[205] *See id.* at 373–75.
[206] The Charter Establishing the Gulf Council, art. 4, May 25, 1981, 21244, 1288 U.N.T.S. 13, 26 I.L.M 1131, http://www.gcc-sg.org/en-us/AboutGCC/Pages/Primarylaw.aspx.
[207] *See infra* text accompanying 221–39.
[208] The Unified Economic Agreement between the Countries of the Gulf Cooperation Council, art. 21, Nov. 11, 1981, 26 I.L.M 1131. This agreement has been superseded by article 32, ¶ 2 of the Economic Agreement between the Gulf Cooperation Council States in 2001.
[209] On this project, see GCC, FOREIGN CAPITAL IN THE GULF COOPERATION COUNCIL MEMBER STATES: THE ROLE OF LEGISLATION AND LEGAL FRAMEWORK IN ATTRACTING

harmonizing the law was to encourage foreign investment since, at that time, only three GCC states (Oman, the KSA, and Qatar) had foreign investment laws; these laws seemed like they were invented to discourage investments.[210] This non-binding commitment was adopted by the GCC Ministerial Council and aims to harmonize rules governing investments, like rules governing applications for investment licenses, investors' rights and obligations, and incentives.

Article 11 of the soft law listed incentives that foreign investments may be granted according to the discretion of the investment agency of each state; exemptions include eligibility for (1) CIT exemptions according to periods selected by the individual states, (2) full or partial custom duty exemptions, and (3) exemptions for allotted properties and lands, among others.[211] It must be emphasized that the law does not provide objective criteria to award these incentives, which affords the local authorities a great margin of discretion. Additionally, the article does not articulate whether these incentives are mere examples or whether the states are forbidden to grant other types of incentives.

Although the GCC evaluated this soft law and its amended proposal, the 146-page study stated very little about tax incentives A study from the College of Business and Economics at United Arab Emirates University in 2007 stated that, while the underlying idea of having a uniform law is to have identical rules that govern foreign investment across the GCC region, Article 11 does not achieve that goal since each state will have the option to select CIT exemption periods.[212] Further, the discretion used by investment authorities will create confusion for investors because there is no clear guidance on eligibility.[213] These were the only two comments from the study regarding incentives.

Under the GCC legal framework, the states do not have to adopt the soft law domestically.[214] A soft law, or as the GCC refers to it, "قانون استرشادي" or "qānwn īstrshādy" literally translated to "guiding law," is meant to help or inspire the states when designing their domestic laws. Stated differently, soft laws can be used as a source while drafting domestic laws.[215] Sometimes, soft

INVESTMENT AND PROMOTING ECONOMIC GROWTH 103–07 (2008) (Arabic) [hereinafter THE GCC INVESTMENT STUDY].

[210] For instance, the domestic laws capped the foreign ownership percentage to 49%, included limited incentives, and required approval from high domestic authorities like an order from the Council of Minister in some GCC States. *See id.* at 4–5.

[211] *Id.* at 107.

[212] *Id.* at 108.

[213] *Id.*

[214] This reminds EU readers of the EU's Code of Conduct since both the EU Code and GCC soft laws are not binding.

[215] *See Al-Hujailan: Guiding Laws are an Essential Stage for Harmonizing and Developing Legislation in the Gulf Countrie*s, KUWAIT NEWS AGENCY (Jan. 14, 2001) (Arabic),

laws are later reviewed and adopted as a binding law on the GCC level,[216] but the above-described soft law on foreign investments has not been adopted.

In 2001, the GCC replaced the First Economic Agreement with the Second Economic Agreement; the latter agreement reaffirms the aim to synchronize GCC investment laws as a tool to boost investments.[217] As the agreement stated, the goal behind harmonizing investment law is to "enhance[] local, external, and intra-GCC investment levels, and provide an investment climate characterized by transparency and stability."[218] Correspondingly, the GCC drafted a proposal to harmonize foreign investments; however, the proposal did not amend the tax incentives under Article 11.[219]

In the latest GCC foreign investments unpublished proposal, which this author recently acquired from a GCC official, a 5-year CIT holiday is cited as a tax incentive.[220] However, the proposal does not forbid the states to further extend the period beyond five years,[221] meaning the states can offer a long holiday. The proposal has not yet come into existence. This author was not able to locate any statements explaining why GCC states did not adopt the foreign investment law as a binding law or why other amended proposals did not go through,[222] but the GCC has asserted that it is still considering harmonizing investment laws.[223] Thus, foreign investment tax incentives might be harmonized *if* this project is accomplished and adopted as a binding law.

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https://www.kuna.net.kw/ArticlePrintPage.aspx?id=1137253&language=ar (reciting a press release by Jamil Hejailan, GCC former Secretary General from 1996 to 2002).

[216] *Id.*

[217] *See* THE ECONOMIC AGREEMENT BETWEEN GCC STATES art. 5 (Dec. 31, 2001), http://www.gcc-sg.org/en-us/CognitiveSources/DigitalLibrary/Lists/DigitalLibrary/Economy/1274258747.pdf [hereinafter THE SECOND ECONOMIC AGREEMENT].

[218] *Id.*

[219] On one of the GCC amended proposals, see THE GCC INVESTMENT STUDY, *supra* note 209.

[220] GCC, A Proposal: The Unified Law for the Investment of Foreign Capital in the GCC States art. 13(1) (unpublished) (on file with author).

[221] *Id.*

[222] As pointed out by other GCC scholars, "excessive confidentiality" imposed on GCC documents and the lack of transparency are obstacles scholars have to deal with when conducting a GCC related study. *See* A. A. Al-Muslemani, The Legal Aspects of the Gulf Cooperation Council 30 (1989) (Ph.D. thesis, London School of Economics and Political Science). The GCC does not publish legislative history or members' discussions on any project.

[223] *See* GCC SECRETARIAT-GEN., GCC: THE PROCESS AND ACHIEVEMENT 134 (8th ed., 2014); GCC SECRETARIAL GEN.: ECON. AFF., COM. & INDUS. DEP'T, THE REVISED LONG-TERM COMPREHENSIVE DEVELOPMENT STRATEGY FOR THE GCC STATES FOR THE YEARS 2010-2025 25 (2011).

As for the second project, the second economic agreement states a goal of harmonizing industrial legislation to develop and enhance the participation of the industrial sector in the economy.[224] Based on the agreement, the GCC adopted a binding law to harmonize industrial laws entitled *Common Industrial Regulatory Law of the GCC Countries* in 2004 to encourage the industrial sector.[225] This law was later adopted in GCC states. Under this law, industrial enterprises are defined as:

> every establishment [that] mainly aims at transformation of raw materials to fully- or-semi- manufactured products, or transformation of semi- manufactured products to fully-manufactured products including mixing, separating, forming, assembling and packing works provided that all or most of such works are mechanically operated. It also aims to operate cognitive, environmental and other industries.[226]

The law regulates enterprises' licenses, industrial records, incentives, inspections, and sanctions, among other things. Two articles in the law discuss tax incentives. Article 17 states:

> The minister or the authorized representative may take the appropriate formalities required to give the industrial enterprise all or some of the following exemptions: 1. [Complete] or partial exemption from customs duties imposed on the enterprise imports according to industry input exemption's regulations agreed on by GCC. 2. [Complete] or partial exemption from all taxes, including income tax, per law applied in each state. 3. Exemption of industrial enterprise's exports from export taxes and duties. 4. *Any other exemptions agreed upon by GCC*.[227]

The law includes other types of incentives. Article 18 states that the industrial enterprise can be granted all or some of the following advantages:

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[224] THE SECOND ECONOMIC AGREEMENT, *supra* note 217, art. 8.

[225] Common Industrial Regulatory Law of the GCC Countries (April. 4, 2006), https://www.customs.gov.sa/themes/custom/customs/files/agreements/GCC/en.pdf: The Unified Industrial Organization System for the Cooperation Council for the Arab States of the Gulf, Resolution of the Supreme Council in the Twenty-Fifth Session, (Dec. 2004) (Bahrain).

[226] *Id.* at art. 1(5).

[227] *Id.* at art. 17 (emphasis added).

> 1. Allocation of an appropriate plot. 2. Rental of industrial premises required for the industrial enterprise upon encouraging terms in the industrial zones established by the government. 3. Provision of electricity, water, fuel and other facilities required for the industrial enterprise at encouraging prices. 4. *Any other advantages agreed upon by GCC*.[228]

Unlike the GCC foreign investment soft law, this binding law mandates that further incentives can be granted as agreed at the GCC level.[229] Article 18 seems to suggest that GCC states cannot offer other forms of incentives unless allowed by the GCC to level the playing field between states. In contrast to this reading, the Kuwaiti law added a section that provided eligibility to exempt industrial enterprises from duties and fees in general, on top of what is already mentioned in Article 17.[230] There did not appear to be a GCC agreement that added such incentives in accordance with Article 17 section 4. *If* there is no such agreement at the GCC level and this interpretation is correct, then Kuwait law might violate Article 17 of the GCC industrial act.

In conclusion, apart from the incentives offered to industrial sectors, GCC states are free to offer tax incentives like those in the United States. As in the United States, there is an explicit tax anti-discrimination rule that prohibits discriminating against GCC nationals in any GCC host countries. However, the scope of this rule is limited to nationals who are identified by their nationality; thus, foreign investors—the focus of this paper—are outside the rule's scope.

V. THE MERITS AND DEMERITS OF THE THREE APPROACHES TO MANAGE INCENTIVES

Part III explored the three ways to deal with tax incentives in three common markets. This part compares how well the approaches achieve four things: 1) controlling bidding wars; 2) making tax laws predictable; 3) allowing flexibility to reform domestic tax policy as needed; and 4) monitoring tax incentives. These four considerations are of significant importance to policymakers and investors. Here, this author intentionally disregards the details of what form of tax incentives is better, because existing literature already addresses the matter and the purpose of this article is to conduct an overall comparison of the three approaches.

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[228] *Id.* at art. 18 (emphasis added).
[229] *Id.* at art. 17(4).
[230] Industrial Law 22 of 2009 (amending Law No. 56 of 1996), art. 14 § 2 (Arabic), https://www.pai.gov.kw/documents/10179/39797/قانون+الصناعة+المعدل.pdf/9dd83b1d-3383-4794-ae71-e98ffbb68fe0.

A. *Bidding War*

Bidding wars between U.S. states has been a source of wide criticism.[231] As discussed in Part II, tax competition, corporate blackmail, and rent seeking activities are associated with each other. When there is no agreement between countries to limit competition, corporate blackmail and rent seeking activities emerge. While the merits of competition are debatable, Amazon-style corporate blackmail and rent seeking activities are undesirable. Some scholars use the game theory model of the prisoners' dilemma to explain how countries choose their tax policies in a competitive setting.[232] Applying this theory to tax incentives indicates that countries look to their neighbors when considering what form of tax incentives to offer. A study on the fifty states of the United States, for example, has concluded that "[o]ver the last forty years, state investment tax incentives have become increasingly large and increasingly common among states. . . . States that enact investment tax credits tend to do so around the same time as their neighboring states."[233] In the GCC region, a report revealed that the KSA is planning to introduce tax holidays in its special economic zones because it is the standard incentive in the region,[234] although tax holidays receive the most criticism relative to other forms of incentives.[235] In that sense, competition is undesirable because it drives countries to adopt poorly designed incentives.

Competition is considered a collective action problem,[236] and is better dealt with at a regional, federal, or supranational level. If legislators want to avoid the U.S. competitive scene and view it as destructive, then regulating tax incentives by limiting or harmonizing them are superior approaches. Both approaches will largely shield individual states and localities against lobbying by special interest groups and corporate blackmail since decisions to revise the agreement or grant exceptions must be taken at the supranational or regional level. However, while state aid in direct taxation is used to curb "harmful tax competition" between EU States,[237] even the

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[231] *See*, *e.g.*, Enrich, *supra* note 105; Kaye, *supra* note 107.

[232] Avi Nov, *The 'Bidding War' to Attract Foreign Direct Investment: The Need for a Global Solution*, 25 VA. TAX REV. 835, 845–46 (2006).

[233] Robert S. Chirinko & Daniel J. Wilson, *State Investment Tax Incentives: What Are the Facts?* 4 (Federal Reserve Bank of San Francisco, Working Paper No. 2006-49, 2006) http://www.frbsf.org/publications/economics/papers/2006/wp06-49bk.pdf.

[234] *See Saudi Arabia Publishes Special Tax Rules for Integrated Logistics Bonded Zone*, EY (Mar. 20, 2021), https://taxnews.ey.com/news/2021-0663-saudi-arabia-publishes-special-tax-rules-for-integrated-logistics-bonded-zone?uAlertID=Sd%2fG8rua1oj6%2fl58EZ2AiA%3d%3d.

[235] *See*, *e.g.*, Mclure, *supra* note 96, at 330–32.

[236] RIXEN, *supra* note 41, at 43–46.

[237] COMM'N OF THE EUR. CMTYS., TOWARDS TAX CO-ORDINATION IN THE EUROPEAN UNION: A PACKAGE TO TACKLE HARMFUL TAX COMPETITION ¶ 17 (1997) (emphasizing the role of

commission admits that state aid is unsuitable and incoherent to tackle different harmful tax competition when general incentives in any state member are introduced.[238] On the other hand, harmonizing locational incentives could level the playing field between the states.

As for competition with the rest of the world, harmonization also allows the region to compete with the rest of the world and maintain international competitiveness since competition does not stop at the GCC market frontier. Until there is a global agreement to restrict incentives, other regions and countries will still offer them. In the alternative, banning tax incentives will limit competition between the states and restrict their ability to compete with other jurisdictions. Note that regulating incentives might push the competing regions and countries to tax rate competition, relax enforcement of tax laws, and offer other non-typical incentives such as sweetheart tax rulings that are favorable to the taxpayer.

B. *Predictability*

Predictability of the tax system is an important aspect that potential investors consider before investing in any country.[239] Predictability regarding tax incentives could include two elements: 1) what incentives are offered for investors, and 2) their competitors and whether these incentives maybe taken away from them.

The U.S. approach provides little predictability. Although nearly absent congressional and judicial interference allows firms to project their tax deals before establishing a business in a state, firms cannot predict what the

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state aid in compacting harmful tax competition); Edoardo Traversa & Pierre M. Sabbadini, *State-Aid Policy and the Fight Against Harmful Tax Competition in the Internal Market: Tax Policy in Disguise?*, *in* EU TAX LAW AND POLICY IN THE 21ST CENTURY 107 (Werner Haslehner et al. eds., 2017).

[238] The commission stated that state aid does not capture "some general tax measures [that] impede the proper functioning of the internal market." *Commission Notice on State Aid 1998*, *supra* note 156, ¶ 6; Monti, *supra* note 33, at 208–09; *See also* Edoardo Traversa & Alessandra Flamini, *Fighting Harmful Tax Competition through EU State Aid Law: Will the Hardening of Soft Law Suffice?*, 2015 EUR. ST. AID L. Q. 323, 331 (2015) (concluding that the State Aid Rule cannot be "indefinitely starched" to capture harmful tax competition); Patricia Lampreave, *Harmful Tax Competition and Fiscal State Aid: Two Sides of the Same Coin?*, 59 EUR. TAX'N 197, 208 (2019) (noting that "tax measure might be reprehensible and harmful, while not being considered selective. This would occur where the measure is applied generally to all taxpayers and without exception. Or, a tax measure could be selective and not harmful. Therefore, the aims of each tool are different and do not overlap."); Luis Miguel Perdiago Borrego, *State Aid Law and Taxation*, 7 BOCCONI LEGAL PAPERS 97, 153–54 (2016) (noting that if tax competition is the goal, then state aid is not the tool but rather harmonization).

[239] Brooks, *supra* note 25, at 543.

states are going to offer their competitors. In fact, because of non-disclosure agreements, they might never know what their competitors are granted.

In the EU, the initial reaction might be that there is a great deal of predictability because incentives are granted to every company within a similar legal and factual situation in order to avoid the issue of selectivity. It might also be assumed that whoever receives incentives will keep them. This initial reaction is not always true. The merit of state aid as a negative obligation cannot be ignored; the rule can be developed to face future actions by Member States since taxation is tricky.[240] However, this feature has caused the rule to sometimes be vague or uncreditable. Recent cases regarding the commission's novel transfer pricing rule have effectuated wide criticism attacking the predictability of the rule. The United States and scholars generally have criticized this novel approach; Professor Ruth Mason, a noted EU state aid scholar, has argued in a series of articles that this approach is "unpredictable," "invades reserved Member State tax authority,"[241] is not supported by precedent, and "leads to absurd results."[242] The U.S. Treasury has accused the commission's new approach of increasing legal uncertainty and stated that it "may lead to a growing chilling effect on U.S.-EU cross-border investment," "undermine the international consensus on transfer pricing standards, call into question Member States' ability to comply with existing bilateral tax treaties, and undermine the progress made under the OECD/G20 BEPS project."[243] Apple, which created more than 1.5 million jobs across Europe, called out the uncertainty of the law in Europe, stating

[240] *See* Theodoros G. Iliopoulos, *The State Aid Cases of Starbucks and Fiat: New Routes for the Concept of Selectivity*, 16 EUR. ST. AID L. Q. 263, 271 (2017) (arguing that the commission did not widen the scope of state aid in transfer pricing cases since "no new conceptual elements were introduced," and that the commission's "analysis was adapted to the novel issues that the tax rulings have brought into play").
[241] *Mason Identifying Illegal Subsidies*, *supra* note 163, at 138.
[242] Mason, *supra* note 179, at 951. *See also* Spencer A. Lee, *Cutting Ties: Examining the Social, Economic, and Political Implications of Inconsistent European Union State Aid Interpretations on Multinational Businesses*, 52 WAKE FOREST L. REV. 713, 725–27 (2017) (criticizing the commission as being inconsistent in applying the State Aid Rule in the tax rulings of Starbucks, Fiat, and Apple); Dimitrios A. Kyriazis, *From Soft Law to Soft Law through Hard Law: The Commission's Approach to the State Aid Assessment of Tax Rulings*, 15 EUR. ST. AID L. Q. 428, 431 (2016) (arguing that the novel approach is not supported by case law). *But see* Richard Lyal, *Transfer Pricing Rules and State Aid*, 38 FORDHAM INT'L L. J. 1017, 1043 (2015) (arguing that the commission's approach is "firmly in line with previous practice and follow[s] well established principles in the identification of fiscal State aid, notably in the determination of a selective advantage"). It is worth noting that the author of this article is the principal legal adviser in the EU Commission.
[243] U.S. DEP'T OF THE TREASURY, THE EUROPEAN COMMISSION'S RECENT STATE AID INVESTIGATIONS OF TRANSFER PRICING RULINGS 3–4 (2016). *But see* Daniel Shaviro, *Friends Without Benefits? Treasury and EU State Aid*, 83 TAX NOTES INT'L 1067 (2016) (criticizing the treasury paper).

that "[u]sing the Commission's theory, every company in Ireland and across Europe is suddenly at risk of being subjected to taxes under laws that never existed," which will ultimately deter foreign investments and lead to an economic downturn.[244] Some have even speculated that the devolvement of the rule in an inconsistent manner might push EU members to leave the union.[245] The issue of predictability is not only linked to the EU Commission's new approach; how to distinguish legal from illegal aid and what is considered aid will arise generally in any regime that controls incentives.

As for harmonization, predictability depends on the details of eligibilities and incentives. For instance, if the harmonized incentives are uniform across a region and their eligibility does not depend on discretion, then investors will be able to predict their tax liability and the incentives offered to their competitors. If, on the other hand, the authorities have discretion to grant the incentives in the first place, or incentives are capped at a certain amount, there is little predictably. Whether incentives may be taken away from investors is predictable to a great extent. For instance, as described in Part III, the GCC harmonized industrial incentives, and these incentives do not seem to be mere examples. The GCC states cannot offer any other incentives unless those additional incentives are agreed upon by the GCC. Therefore, if there is no further agreement at the GCC level, the additional incentives granted under Kuwaiti law are actually invalid. Such a conclusion is straightforward when comparing GCC and Kuwaiti law, and investors can predict that these additional incentives contradict GCC law and may consequently not hold.

C. *Policing*

Monitoring and enforcing any agreement to regulate incentives by a capable body is another important aspect to consider. The EU Commission and court play undeniable roles to ensure the state aid rule is followed, as seen in Part III. This is an important consideration, particularly to the GCC, since the organization lacks a powerful supranational body equivalent to the EU

[244] *See, e.g.*, *A Message to the Apple Community in Europe*, APPLE (Aug. 30, 2016) https://www.apple.com/ie/customer-letter (asserting that "the most profound and harmful effect of this ruling will be on investment and job creation in Europe. Using the commission's theory, every company in Ireland and across Europe is suddenly at risk of being subjected to taxes under laws that never existed"); Lee, *supra* note 242, at 727–31; Nina Hrushko, *Tax in the World of Antitrust Enforcement: European Commission's State Aid Investigations into EU Member States' Tax Rulings*, 43 BROOK. J. INT'L L. 327, 343–55 (2017).

[245] Lee, *supra* note 242, at 731–32.

Commission.[246] Although establishing powerful bodies to investigate any violation is necessary to ensure participants' commitment, it involves costs that must be taken into consideration. First, there is a monetary cost to establish a body, hire qualified staff, rent a building, and provide necessary resources when adopting an agreement between regional groupings. Another cost is the risk that policing the agreement might spark tension between the enforcing body and participants, participants themselves, or with non-participants. One example of tension with third parties is the U.S. Treasury's reaction to the targeting of U.S. multinationals in the transfer pricing cases that might cause diplomatic and trade problems for the EU.[247] The full political consequences of this are still unclear.

A U.S.-like approach of allowing incentives requires minimum supervision at the federal level of government and no supervision regionally since no agreement is adopted. In the United States, the Economic Development Act of 2005 was introduced by some members to Congress to allow certain tax incentives that might otherwise be unconstitutional under the Commerce Clause and eliminate judicial enforcement as a consideration.[248] In contrast, an agreement to regulate incentives like those in the GCC or the EU always requires policing.

D. Flexibility

The idea of flexibility is one for which countries have the ability to reform incentives to adopt a better practice based on international experience, introduce different packages of tax incentives to suit the unique need of different investments (e.g. industrial, agricultural), or even abolish incentives if proven ineffective. Flexibility is important when adopting up-to-date tax policies and avoiding unnecessary waste of revenue.

Among the three approaches, permitting tax incentives without a regional agreement to regulate incentives—like the United States—grants

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[246] In 2016, the GCC agreed to establish a commission titled the Economic Judiciary Commission. As the Commission's Charter mandates the Charter becomes enforceable three months after domestically ratification by all Member States. At the time this work was written, there is no further information on whether Qatar and UAE ratified the Commission Charter. Once the Commission convenes, the bylaws should be issued within six months after selecting the judges. Gulf Cooperation Council Economic Judiciary Commission Charter, art. 2, ¶ 1 (adopted by GCC Resolution of the Supreme Council in the Sixteenth Session Regarding Common Actions (May 2016)) GCC O.J Y. 4 no. 15 (July 1, 2016) at 13-16. The legal basis to establish the Commission is THE SECOND ECONOMIC AGREEMENT, *supra* note 217, at art. 27.

[247] *See supra* text accompanying notes 167–78.

[248] On the proposal, see Walter Hellerstein, *Cuno and Congress: An Analysis of Proposed Federal Legislation Authorizing State Economic Development Incentives*, 4 GEO. J. L. & PUB. POL'Y 73, 75–78 (2006).

great freedom and enables countries to be flexible. Harmonization, on the other hand, provides little to no flexibility depending on the agreement to regulate incentives. For instance, if the regional agreement provides for one uniform incentive structure (such as tax credits, investment allowances, or enhanced deductions) for a certain duration, countries will not have flexibility. If the agreement imposes ceilings on subsidies or floor rates, there is more flexibility, but countries still will not be able to replace the required incentives form. In both cases, any proposals to reform the harmonized law will have to go through a long process; a new agreement between all participant countries at the regional level will need to be created and then approved by national parliaments, which is a time-consuming process. The last approach, limiting incentives, provides minimal to no flexibility as well. If the agreement bans locational incentives unless they are authorized by a superior regional authority, then there is no flexibility since countries are not allowed to offer tax incentives in the first place. However, if the agreement is like that in the EU, where countries can still offer incentives as long as they are not targeted to certain sectors or regions, then there is some room for flexibility since countries are still able to provide general incentives.

VI. CONCLUSION

The purpose of this essay is to revisit the classic case against tax incentives, explore and compare the legal framework for locational tax incentives in the United States, EU, and GCC common markets, and examine the merits of each of the three approaches to deal with incentives enlightened by the experience in the three common markets.

The paper first revisited the case against tax incentives which includes that incentives: create "harmful tax competition," are ineffective in attracting businesses, cause loss of tax revenues, transfer tax revenues to investors' home countries, should not be used to compensate for disadvantages, and distort investment decisions. This paper concludes that, while the last two arguments have almost no merits, the other arguments are debatable when considering the recent and ongoing changes in tax policies in capital-exporting countries, the impact of the OECD forthcoming tax projects, and the existence of mixed empirical evidence in developed countries and the dearth of empirical studies in the GCC common market.

The United States, EU, and GCC common markets' approach toward tax incentives are dissimilar. Under the state aid rule, EU members are prohibited to offer targeted tax incentives – when some conditions are met – unless authorized by the EU Commissioner. On the other hand, due to the almost absent congressional action and judicial review by the U.S. Supreme Court, the U.S. states are allowed to grant locational incentives. The GCC seems to be taking middle ground between the U.S. and EU approaches; the

GCC states have harmonized tax incentives offered to industrial enterprises by adopting a binding law. However, aside from industrial enterprises tax incentives, the states are free to offer locational incentives since there is no binding GCC law that restricts the states' abilities to offer incentives.

Finally, this work explored the merits of the three approaches – to allow, prohibit, or harmonize tax incentives – by assessing four considerations: 1) controlling competition; 2) the predictability of tax regime; 3) policing tax incentives regulations; and 4) the flexibility of the system to reform the tax policy. In terms of controlling a bidding war, allowing tax incentives will permit the states to compete with each other and the rest of the world. On the contrary, forbidding incentives will restrict the states' ability to compete among themselves and with the rest of the world. Harmonizing tax incentives within a common market will constrain competing within the market but, at the same time, allow the states to compete with the rest of the world. Whether one approach is superior to the others depends on whether competition is destructive. As for the predictability of tax incentives granted to foreign investors and their competitors, and whether incentives can be stripped away after granting them, the harmonization approach will provide the most predictability depending on the tax incentives design. The other two approaches provide little predictability; in the U.S. the investors are unable to predict their competitors' incentives packages, and in the EU investors' ability to keep national incentives may be jeopardized such as in the tax ruling investigation cases. Either harmonizing or banning tax incentives approaches, unlike allowing incentives, will entail monetary and other costs to enforce and police them. Similarly, the two approaches limit countries' ability to reform tax incentives to adopt up-to-date tax policies. Thus, this paper concludes that these methods have limitations, advantages, and disadvantages.