

Research on the Effect of Tax Incentives on the Development of Western China

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Abstract: China is in a period of economic transformation, but the phenomenon of unbalanced regional economic development is prominent, to alleviate this phenomenon, China implemented the strategy of Western development at the beginning of this century. Tax policy development is closely related to the macroeconomic situation, so western tax incentives play an important role in the revitalization process of western China. This paper analyzes and combs through the classification of the relevant literature on the effect of the Western development tax preferential policy and explores the research results of the policy in terms of the macro effect and micro effects of the policy. Finally, this paper comprehensively analyzes the implementation effect of the policy and the shortcomings of the existing research and puts forward the corresponding recommendations for subsequent scholars to study the implementation effect and impact of the tax incentives to provide help.

1 INTRODUCTION

Tax policy is the core tool of national macro-control, and a reasonable tax policy plays a crucial role in optimizing resource allocation, narrowing the gap between the rich and the poor, achieving smooth economic operation, stimulating enterprise innovation, and coping with economic crises. Since the reform and opening up, China's economic level has been rising, and people's lives have become increasingly happy, but due to the constraints of natural conditions and other factors, the economic growth of the Western region has been slow. This has led to the aggravation of China's regional economic development imbalance, which is not conducive to social stability and long-term peace and security. To alleviate the problem of unbalanced regional development and promote the development of the West, China fully implemented the Western Development Strategy in 2001 to support and develop the Western economy. 2011, the Ministry of Finance, the General Administration of Customs, and the State Administration of Taxation jointly issued the Circular on Issues Concerning Tax Policies for the In-depth Implementation of the Strategy for the Development of the West, which stipulates that enterprises of encouraged industries located in the Western region shall be subject to a reduced tax rate of 15%. The enterprise income tax rate is reduced by 15%. Tax incentives not only mobilize local governments to

develop their economies but also play an important role in supporting local characteristics and key industries and promoting enterprise development.

It has been more than twenty years since the implementation of the strategic tax incentives for the development of the Western region, and when the second round of tax incentives expired, China optimized the policy and extended it for ten years, which shows that the policy still plays an important role in coordinating regional development. Therefore, it is of great significance to summarize the literature on this policy. Based on reading the literature related to the Western development strategy tax incentives, this paper introduces the background and policy content of the Western development strategy tax incentives, screens the articles with high relevance to the topic of this paper and sorts out the related literature, and summarizes the existing research in the academic field according to the results of the articles. To explore whether the Western development strategy tax policy can promote Western economic growth, narrow the regional development gap plays a positive role.

2 BACKGROUND AND CONTENT OF THE IMPLEMENTATION OF TAX INCENTIVES FOR THE WESTERN DEVELOPMENT STRATEGY

The Western Development Strategy is an important national strategy implemented by the Chinese government to promote coordinated regional development and narrow the development gap between the Eastern and Western regions. The strategy aims to promote the economic and social development of the Western region and to incentivize the development of characteristic advantageous industries and emerging industries in the Western region through preferential tax policies in order to promote industrial transformation and upgrading. The policy stipulates that enterprises in the encouraged industries in the Western region can enjoy a reduced enterprise income tax rate of 15%, which has a significant advantage over the national standard enterprise income tax rate of 25%. In addition, the policy also relaxes the requirement for the proportion of enterprises' income from the main business, from 70% to 60%, enabling more enterprises to enjoy tax incentives. The Western region includes 12 provinces (autonomous regions and municipalities) such as Inner Mongolia, Guangxi, Chongqing and the Xinjiang Production and Construction Corps, and some autonomous regions and Ganzhou City can also be implemented *mutatis mutandis*. The Catalogue of Encouraged Industries in the Western Region, led by the Development and Reform Commission, is the main basis for enterprises to enjoy preferential tax policies. Through the implementation of these tax incentives, the Western region has reduced or exempted enterprises' taxes by more than RMB 400 billion, effectively promoting industrial transformation and upgrading as well as economic development. In the follow-up management, the tax authorities may, in respect of the main business of an enterprise that is difficult to define, request the relevant departments such as development and reform to issue opinions to ensure the precise implementation of the policies. Together, these measures constitute the framework of the tax incentive policy of the Western Development Strategy, which aims to promote high-quality economic and social development in the Western region through tax incentives.

3 MACRO EFFECTS OF TAX INCENTIVES FOR WESTERN DEVELOPMENT

American scholar Arthur B Laffer (2004) put forward the "Laffer Curve" in the 1970s, which depicts the impact of different tax rates on tax revenue and the economy, i.e. in general, raising tax rates can increase government tax revenue. However, when the tax rate is increased beyond a certain limit, the operating cost of enterprises will be increased, investment will be reduced and income will be decreased, i.e., the tax base will be reduced, which in turn will lead to a decrease of tax revenue of the government. The impact of tax incentives for Western development on China's macroeconomy has been a topic of intense debate in the academic community, and there are two main points of view.

3.1 Favorable for Economic Growth

Keith (1983) examines panel data on tax incentives in several countries and finds that low tax burdens resulting from tax cuts can promote macroeconomic growth. It can be seen that tax policy, as a powerful means of regulating the macroeconomy, plays an important role in the Western economy. Zeng Zhiyong and Li Junjie (2011) concluded by analyzing the panel data of Enshi, Hubei, that the tax revenue preference policy promotes economic development and industrial structure optimization. Dong Guanghui (2018) demonstrated a series of economic growth data based on the Sichuan national tax perspective and found that the comprehensive implementation of tax incentives for Western development has strongly cooperated with the implementation of the overall strategy of China's Western development. Based on the survey data of nearly 5,000 enterprises in Chongqing Municipality, Zhang Bo and Li Jing (2009) studied the implementation of the tax preferential policies for the development of Western China, the implementation effects and problems, and found that the tax preferential policies play an important role in promoting the economic growth of Chongqing Municipality through the comprehensive effect, and have a positive impact on the development of enterprises and the formation of advantageous industries. The study shows that tax preferential policies play an important role in promoting macroeconomic growth and optimizing industrial structure. Through tax cuts and fee reductions, it not only stimulates market vitality, but also promotes scientific and technological innovation and industrial

upgrading, and provides strong support for the implementation of the strategy of Western development.

3.2 Unfavorable for Economic Growth

Some scholars have questioned the effectiveness of tax incentives on economic growth in the Western region. Ma Shuanyou and Yu Hongxia (2003) empirical study found that the tax burden in the Western region is obviously characterized by a high tax burden when compared with the central region, which has a relatively comparable level of economic development, suggesting that the tax policy in the Western region does not play a significant role in actually promoting economic development. Luo Mingling, Fan Ziying and Chen Chen (2019) believe that taxes can change the enterprise and factor flows to a large extent, and regional tax incentives, as a kind of guiding very clear policy, have a double impact on the regional economy, on the one hand, low-tax regions can attract capital inflow, effectively expand the tax base, and promote economic development; on the other hand, high-tax regions, due to the increase in the relative tax burden, lead to the loss of resources, economic development is affected, and economic development is affected. On the other hand, high-tax-rate regions are affected by the loss of resources due to the increase in relative tax burden, which indicates that the design and implementation of tax incentives need to take into account the balance and coordination between regions. Liu Ruiming and Zhao Renjie (2015) studied the impact of the Western development policy on economic development, using the PSM-DID method to further identify the mechanism found that the Western development had a hindering effect on industrial restructuring, and also failed to effectively attract private investment and foreign investment. Yu Jingyuan (2021), in his analysis of tax data in the Western region, concluded that the Western development policy increased local government transfer dependence and fiscal imbalance. The effectiveness of tax incentives on economic growth in the Western region is controversial, which requires policymakers to fully consider regional differences, market mechanisms and the long-term effects of policies when formulating and implementing policies in order to achieve coordinated regional economic development. At the same time, the evaluation and monitoring of the effectiveness of the policies should be strengthened to ensure that the tax incentives can truly promote economic growth and social progress in the Western region.

4 MICRO EFFECTS OF TAX INCENTIVES FOR WESTERN DEVELOPMENT

Tax policy not only affects the regional macroeconomy but also influences the development of enterprises. Liu Jun and Qiu Changsol (2006) conducted an empirical study from the three perspectives of the impact of tax policy on economic growth, production and business activities of companies, and local revenue, and concluded that tax incentives have significantly advanced the economic growth in the west, and the capital profitability of enterprises has significantly increased, but the driving effect of tax incentives on economic growth has been diminishing with the passage of time. Raffaello Bronzini and Paolo Piselli (2016) study the impact of tax incentives on firms' innovation and find that a lower tax rate on patent income boosts the number of patent applications and innovation capacity, a phenomenon that is particularly pronounced among small firms. Ernst C., Richter K. and Riedel N. (2013) examined the impact of tax incentives on firms' R&D activities and found that all three forms of tax incentives - special tax breaks, tax credits, and lower tax rates - are effective in increasing the amount of R&D-related activities. Eric (2019) estimated the impact of the adoption of tax incentives on the manufacturing sector in the US states and found that tax incentives reduce the cost of new investment by firms and can stimulate firms to invest and improve firm performance. This illustrates the positive role of tax incentives as an effective economic regulatory tool in increasing firms' profits, incentivizing firms' innovation and R&D activities, and enhancing firms' performance.

5 SUGGESTIONS FOR THE CONTINUATION OF TAX INCENTIVES FOR WESTERN DEVELOPMENT

5.1 Implementation of Graded Tax Incentives

The support of tax incentives is indispensable in the process of striving to realize the industrialization of the Western region (Zhang & Li, 2009). The most important viewpoint of the gradient tax preference policy lies in its ability to reduce the tax burden on enterprises, especially to support small, medium and

micro enterprises and key industries, and to enhance their capital strength and internal development power. At the same time, the gradient tax preference policy gives full play to the regional adjustment effect of the tax preference policy by implementing different tax preferences for enterprises in different regions and industries, plays the redistributive role of the government by setting up different tax policies for different regions, realizes the flow of resources between regions, promotes the optimization of the industrial structure and the coordinated development of the region, and realizes the principle of "the first to be rich will bring the later to be rich" so as to promote economic growth and the development of the economy. "The first to get rich will lead the second to get richer", thus promoting economic growth and social development.

5.2 Expanding the Target Beneficiaries of Tax Incentives

Refining and improving the Catalogue of Encouraged Industries in the Western Region, promotes the cultivation of advantageous industries and characteristic industries in the Western region. By reducing the tax burden of enterprises in specific industries and trades, the Western region has been incentivized to develop characteristic advantageous industries and emerging industries, which is conducive to the formation of strategic emerging industry clusters and advanced manufacturing clusters in the Western region. In addition, business tax concessions have been implemented for a few special industries in Western provinces and municipalities (Zhang & Li, 2009). In 2008, the local tax structure of Gansu Province was 813 million yuan in corporate income tax and 16.280 billion yuan in business tax. It can be seen that the implementation of business tax concessions for some industries in the Western region in urgent need of development support is conducive to increasing support and strengthening the effectiveness of policy implementation.

5.3 Appropriate Enhancement of the Flexibility of Tax Systems

The Western region is a vast area involving many provinces, with varying levels of development in each region and changing development dynamics. In view of the vast territory and diversified development needs of the Western region, it is necessary to give the Western regional government the right to propose tax relief industries. Provincial governments should

be allowed to make moderate adjustments to the catalog of tax-preferential industries within the prescribed framework according to the industrial characteristics, resource conditions, and ecological protection needs of the region, so as to better adapt to and promote the economic and social development of the region. The preferential tax policy for the development of the Western region will better play a regulatory role in fully stimulating the vitality of the local economy, effectively promoting coordinated regional development, and realizing the goal of coordinated regional development.

6 GAPS IN THE EXISTING LITERATURE AND PERSPECTIVES FOR FUTURE RESEARCH

In the research on tax incentives for Western development, a large number of valuable research results have emerged in the past two decades. The academic research on the preferential tax policy for the development of the Western region has focused on policy effects and policy improvement, etc. Rich research results have been achieved in these areas, and the question of whether the preferential tax policy for the development of the Western region can promote the long-term development of the national economy from the perspectives of the industrial structure, foreign investment, and the total amount of the local economy has been investigated, which has provided China with a rich theoretical basis for the development of its tax policy and practical experience.

Although these studies provide valuable insights for researchers, research still face many challenges. The current study is deficient in terms of the policy formulation process and lacks sufficient theoretical support and validation in terms of recommendations for policy improvement. In addition, most of the studies only focus on specific regions for data collection and analysis, but this may lead to problems such as under-representation of samples and data bias, thus limiting the generalizability and reliability of the conclusions. Currently, most studies in the academic community use the double-difference method as well as the case study method, and in future studies, interdisciplinary cooperation should be encouraged to integrate the cross-study method into the study of tax incentives for the development of Western China, in order to form a more comprehensive and holistic perspective of the study.

In addition, the research results should be applied to the updating and improvement of tax incentives for Western development in order to test their effectiveness and practicality and to promote the development of the field.

7 CONCLUSION

Summarizing the above summarization and analysis of domestic and foreign research literature, the research of domestic scholars mainly presents two distinct views. The research results show that although there is still controversy on the impact of tax incentives on the macroeconomy, tax incentives have a significant role in promoting the growth of enterprises, improving profitability and enhancing market competitiveness, thus favoring the healthy development of the microeconomy. Although scholars at home and abroad have studied from different perspectives, presenting a diversified situation, in general, the research focuses on both macroeconomics and microeconomics and in terms of practical research, it also focuses on the general state of the economy and the cases of enterprises. The research on tax incentives by scholars at home and abroad has provided a rich theoretical foundation for economic development and has also played an important role in promoting the government's tax policy and regional development policy formulation. This study helps scholars identify the gaps and shortcomings in the research by sorting out and evaluating the existing research results, and also promotes the construction and validation of the theoretical framework. In addition, comparing and contrasting the theories and models of different researchers deepens the understanding of the effects of tax incentives on Western development. It is found that the current academic research on the effect of tax incentives for Western development has a single method, mostly using case analysis or double-difference methods, and future research can be conducted through interdisciplinary cross-study methods, thus providing a multi-dimensional solution to the research problem of the effect of tax incentives for Western development. There are still some limitations in this study, which may lack timeliness due to the influence of literature publication and the research process in this field.

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