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The Relationship Between Corporate Income Tax and Foreign Direct Investment in Vietnam in the Context of the Global Minimum Tax Implementation

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Abstract
This study aims to analyze the structural shift in the relationship between corporate income tax (CIT) and foreign direct investment (FDI) in Vietnam, in the context of the official implementation of the Global Minimum Tax (GMT). Employing a qualitative research method, primarily through desk-based documentary analysis, the paper synthesizes and evaluates the rules of the Organisation for Economic Co-operation and Development, Vietnam's legal policies, and relevant scholarly works to clarify the multifaceted impacts of this new tax mechanism. The research findings indicate that the GMT has directly neutralized Vietnam's core competitive advantage, which was based on low CIT rate incentives. This mechanism causes the benefits from tax incentives to no longer accrue to the investor but instead risk being shifted to the parent company's home country, thereby posing a serious challenge to Vietnam's traditional FDI attraction model. Consequently, non-tax factors such as institutional quality, infrastructure, and human resources become the decisive factors in maintaining the nation's investment attractiveness. From these findings, the study affirms the urgent importance of Vietnam implementing a Qualified Domestic Minimum Top-up Tax (QDMTT) to protect its taxing rights and revenue base. Concurrently, a key policy implication is the necessity of a strategic shift from income-based incentives to cost-based support mechanisms and of focusing resources on substantively improving the overall investment environment. The novelty of the study lies in providing one of the first comprehensive and timely analyses of the GMT's impact in Vietnam, offering specific scientific arguments for policymakers in the process of reshaping the strategy for attracting high-quality FDI in the new era.

Keywords: Global Minimum Tax, Corporate Income Tax, FDI, Tax Incentives, Tax Policy, Vietnam

1. Introduction

For decades, corporate income tax competition has become a prominent feature of the global economy, as countries, especially developing ones, engage in a "race to the bottom" to attract foreign direct investment (FDI). Economic theory and empirical evidence have shown a significant inverse correlation between the tax burden and the investment decisions of multinational enterprises (MNEs), making tax incentives a popular policy tool (Devereux *et al*., 2008; Feld & Heckemeyer, 2011; Saptono *et al*., 2024) [6, 8, 20]. However, this competition has led to global tax base erosion and profit shifting, raising profound concerns about the fairness and sustainability of the international tax system (Kuhn, 2024) [12].

To address this challenge, the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting has introduced a landmark solution: the Global Minimum Tax (GMT), also known as Pillar Two. By imposing a minimum effective tax rate of 15% on MNEs with a consolidated global revenue exceeding 750 million euros, the GMT is designed to end the tax race and ensure that large corporations contribute a fair share of tax where they operate (BEPS, 2021; Beyer, 2024) [1, 2].

Vietnam, one of the most dynamic and successful economies in attracting FDI, has heavily relied on attractive CIT incentive policies. Many large-scale FDI projects, particularly in the high-tech sector, are enjoying effective tax rates significantly lower than the 15% threshold (REGION & UNIT, 2022) [19]. The introduction and implementation of the GMT from 2024 have created an exogenous policy shock, posing a direct and unprecedented challenge to Vietnam's investment attraction model. The core competitive tool based on low tax rates is at risk of being rendered ineffective, forcing the nation to comprehensively re-evaluate the relationship between its tax policy and FDI flows.

Against this backdrop, this study is conducted with the main objectives: (1) to systematize the theoretical basis of the relationship between CIT and FDI and the core principles of the GMT; (2) to analyze the current state of CIT incentive policies for attracting FDI in Vietnam; (3) to assess the impact of the GMT on the effectiveness of these policies and the change in the relationship between CIT and FDI; and (4) to propose policy implications for Vietnam to adapt to the new global investment environment.

To achieve these objectives, the paper employs a qualitative research method, with documentary analysis as the primary technique. The secondary data sources compiled and analyzed include the OECD's model rules and guidance on Pillar Two, Vietnamese legal documents such as the Law on Investment (National Assembly of Vietnam, 2020) [16] and tax laws, reports from the Government, international organizations like UNCTAD and the World Bank, and published scientific research.

This study is expected to make significant contributions. Academically, it provides an in-depth analysis of the transformation of the classic economic relationship between tax and investment under the impact of a new global policy mechanism. Practically, the analyses and recommendations of the paper offer timely, scientific arguments for policymakers in Vietnam in the process of formulating a new-era FDI attraction strategy, ensuring a balance between growth objectives and the protection of national revenue.

2. Theoretical Framework and Literature Review

2.1 Theory on the Relationship between Corporate Income Tax and FDI

The relationship between corporate income tax (CIT) and foreign direct investment (FDI) is explained through several foundational economic theories. Prominent among them is Dunning's (2015) [7] eclectic OLI paradigm, in which 'Location' advantages are one of the three pillars determining FDI flows, alongside 'Ownership' and 'Internalization' advantages. Factors constituting location advantages include the legal environment, infrastructure quality, market size, and particularly, the host country's tax policy. CIT rates and related incentives directly impact operating costs and expected profits, thereby influencing the relative attractiveness of an investment location.

Elaborating on this point, investment location choice models argue that rational MNEs seek to maximize their global post-tax profits. When faced with different investment options, MNEs will prioritize countries with lower effective tax rates, thereby increasing their competitiveness and profitability (Devereux & Griffith, 1998) [5]. This inverse correlation has been consistently demonstrated through numerous empirical studies worldwide. Large-scale meta-analyses all indicate that higher CIT rates have a negative and statistically significant impact on attracting FDI (De Mooij & Ederveen, 2003; Feld & Heckemeyer, 2011) [4, 8]. In Vietnam, studies have reached similar conclusions, affirming that CIT incentives have been a crucial factor in the investment decisions of foreign enterprises over the past decades (Nguyen *et al*., 2020) [17].

2.2 Overview of Tax Incentives and Non-Tax Factors in Attracting FDI

Besides competing with nominal CIT rates, countries also use a diverse portfolio of tax incentives to enhance their appeal. These forms are not limited to lower tax rates but also include measures such as time-bound tax exemptions and reductions, accelerated depreciation, and investment tax credits (James, 2009) [10]. However, the academic debate on the effectiveness and efficiency of these incentives is far from over. Many studies indicate that tax incentives are often redundant, meaning the FDI would have been invested even without them, leading to a waste of budget revenue (Klemm & Van Parys, 2012) [11]. Furthermore, these incentives can create complexity in the tax system and open up opportunities for tax avoidance behaviors.

Consequently, non-tax factors are increasingly recognized as having a more decisive and sustainable role in attracting high-quality FDI. An attractive investment environment is constituted by political stability, the quality of transparent and effective institutions, a strong rule of law, and low levels of corruption (Wei, 2000) [21]. In addition, fundamental factors such as infrastructure quality, market size, economic openness, and especially the quality of the labor force are also key elements that MNEs consider in their long-term investment decisions (Blonigen, 2005; Giroud, 2024) [3, 9]. These factors create genuine competitive advantages, unlike the temporary advantages derived from tax incentives.

2.3 Core Principles of the Global Minimum Tax (Pillar Two)

The Global Minimum Tax (GMT), or Pillar Two, is a system of rules designed to ensure that large MNEs with annual consolidated global revenue of 750 million euros or more are subject to a minimum effective tax rate of 15% on the profits generated in each jurisdiction where they operate (OECD, 2022) [18]. This mechanism operates based on three main interlocking and complementary rules.

First is the Income Inclusion Rule (IIR), which allows the home country of the ultimate parent entity to collect a top-up tax on the profits of its foreign subsidiaries that are taxed at an effective rate below 15%. Second is the Undertaxed Profits Rule (UTPR), which serves as a backstop mechanism. If the parent entity's jurisdiction does not apply the IIR, the UTPR allows other jurisdictions where the group has operations to collect the top-up tax by denying deductions or making equivalent adjustments.

Most important for investment-receiving countries like Vietnam is the Qualified Domestic Minimum Top-up Tax (QDMTT) mechanism. This rule allows the host jurisdiction the priority right to apply and collect the top-up tax arising within its territory before the IIR and UTPR rules are triggered (BEPS, 2021) [1]. The application of a QDMTT not only helps protect national revenue but is also a crucial policy tool for host countries to maintain their taxing rights in the new context.

3. Analysis of the Current Situation and Impacts of Gmt in Vietnam

3.1 The pre-GMT era: CIT incentive policies and FDI attraction in Vietnam

Before the implementation of the Global Minimum Tax, Vietnam's FDI attraction strategy for decades relied significantly on a system of CIT incentives as a key competitive tool. Alongside the standard tax rate of 20%, Vietnam established a multi-layered incentive policy framework, including attractive rates such as 17%, 15%, and especially the 10% rate applicable for long periods (up to 15 years) for qualifying projects (National Assembly of

Vietnam, 2008) [15]. More importantly, the appeal of the tax policy lay not only in the tax rates but also in the mechanisms for time-bound tax exemptions and reductions. Popular incentive packages such as "a four-year tax exemption, followed by a 50% reduction for the next nine years" or "a two-year exemption, followed by a 50% reduction for the next four years" became a distinctive advantage. These incentives were primarily aimed at projects in high-tech sectors, large-scale capital projects, projects with spillover effects, or those located in areas with difficult socio-economic conditions and in economic zones or high-tech parks.

This strategy proved to be exceptionally effective, turning Vietnam into one of the most successful and attractive investment destinations in the region and the world. Registered and disbursed FDI flows consistently recorded impressive figures over the years, with the presence of many leading multinational corporations, often referred to as FDI "eagles" like Samsung, Intel, LG, Foxconn, and many other major investors (Ministry of Planning and Investment, 2023) [14]. However, the downside of this policy was the significant reduction in the effective tax rates paid by large FDI enterprises. The combination of preferential tax rates and extended periods of tax exemption and reduction caused the effective tax rates of many large-scale projects, especially in their initial phases, to drop to very low levels. Analyses by authorities and consulting firms show that in many cases, the effective tax rate ranged from only 2% to 5%, far below the 15% GMT threshold (Ministry of Finance, 2023) [13]. This indicates that the income-based tax incentive tool, which is the core of Vietnam's FDI attraction policy, faces the risk of being directly neutralized by the GMT mechanism.

3.2 Impact of GMT on the CIT-FDI relationship in Vietnam

The emergence of the Global Minimum Tax (GMT) creates a transformative change, profoundly reshaping the classic relationship between CIT policy and foreign direct investment decisions in Vietnam. This impact is not uniform but manifests in various complex aspects, from diminishing the effectiveness of traditional policy tools to altering the structure of investment decision factors for multinational corporations.

3.2.1 Neutralizing the competitive advantage from low tax rate incentives

The operational mechanism of the GMT directly impacts and nullifies the effectiveness of the income-based CIT incentives that Vietnam has been applying. In essence, when a subsidiary of an MNE within the scope of the GMT enjoys an effective tax rate in Vietnam below 15%, the Income Inclusion Rule (IIR) will be triggered in the ultimate parent entity's jurisdiction. This allows the tax authority of that country to collect a top-up tax, which is the difference between the 15% rate and the effective tax rate the subsidiary paid in Vietnam. For example, if a large FDI project in Vietnam is enjoying an effective tax rate of 5%, the parent company in a country that has adopted the IIR will have to pay an additional tax equivalent to 10% of that project's profit to its home tax authority.

The direct consequence of this mechanism is that the financial benefits from Vietnam's tax incentive policy are no longer retained by the investor. Instead of increasing the enterprise's post-tax profit, the amount saved from Vietnam's tax incentives is effectively shifted and becomes budget revenue for another country. Therefore, Vietnam's low tax rate and tax exemption/reduction incentives, designed to create a competitive edge, are now economically neutralized for investors subject to the GMT. Vietnam finds itself in a dual disadvantage: losing its core competitive tool for attracting large-scale investment projects, while also risking the loss of potential budget revenue if it does not proactively exercise its taxing rights through a Qualified Domestic Minimum Top-up Tax (QDMTT).

3.2.2 A shift in MNEs' investment decision factors

As the tax factor is gradually neutralized and no longer a major differentiator between investment locations, MNEs will adjust their decision-making matrix. The weight of non-tax factors in the investment location choice model will be significantly increased. In this context, Vietnam's attractiveness will be assessed based on a combination of more fundamental and sustainable factors.

Vietnam possesses many inherent strengths, including political and social stability, a factor highly valued by long-term investors; labor costs that remain competitive compared to many countries in the region; a strategic geo-economic location at the heart of a dynamic supply chain; and an extensive network of free trade agreements (FTAs) that open doors to major global markets.

However, the competition in the GMT era also more clearly exposes the challenges and weaknesses that Vietnam needs to overcome. The quality of the labor force, especially the shortage of high-skilled labor, engineers, and mid-level management, is a major barrier to attracting FDI projects with high technology content and value-added. The infrastructure system, although improved, still has shortcomings, particularly in logistics, multimodal connectivity, and high transportation costs. Furthermore, administrative procedures can sometimes be complex, lacking predictability and transparency, coupled with the limited development of supporting industries, which increases costs and risks for investors seeking to build a localized supply chain.

3.2.3 Impact on different investor groups and industries

The impact of the GMT is not uniform but is clearly differentiated among investor groups. The group most directly and heavily affected is MNEs with global revenues over 750 million euros, especially those operating in high-tech, electronics, and large-scale manufacturing sectors that are enjoying deep tax incentives in high-tech parks and economic zones. These are the target subjects of both Vietnam's incentive policies and the GMT rules.

Conversely, the less affected group includes small and medium-sized FDI enterprises not subject to the GMT, or investment projects that do not receive significant tax incentives, resulting in effective tax rates already above 15%. For this group, factors such as market size, operating costs, and the general business environment remain the primary drivers. This change could lead to a potential restructuring of FDI flows into Vietnam in the medium and long term. There may be a relative shift from racing to attract mega-projects at all costs to focusing more on improving the investment environment to attract quality projects of suitable scale with better connectivity and spillover effects on the domestic economy.

4. Discussion and Policy Implications

4.1 Discussion on Challenges and Opportunities for Vietnam

First and foremost, the biggest challenge for Vietnam is the risk of diminished competitiveness in the short term. As income-based tax incentives are neutralized, the advantages that Vietnam has painstakingly built over decades may no longer be sufficiently attractive to large MNEs, which were the main targets of these incentives. Without sufficiently strong and timely alternative policies, Vietnam could lose its edge over competing countries in the region. This is coupled with the risk of a "bleeding" of budget revenue. If Vietnam does not apply a top-up tax, the tax difference will be transferred and paid in the parent company's home country, meaning Vietnam voluntarily relinquishes its legitimate taxing rights. Finally, this change creates immense pressure, forcing Vietnam to comprehensively and substantively reform its business investment environment, addressing long-standing bottlenecks in infrastructure, human resources, and institutions.

However, within challenges lie opportunities. The most apparent opportunity is that Vietnam can reclaim its taxing rights and significantly increase budget revenue by implementing a Qualified Domestic Minimum Top-up Tax (QDMTT). This is a crucial resource that can be reinvested for socio-economic development. More importantly, the GMT provides a necessary impetus for Vietnam to transition its FDI attraction model from "quantity" to "quality." As the tax playing field becomes more level, competition will shift towards fundamental factors. This is an opportunity for Vietnam to attract projects with high value-added, advanced technology, environmental friendliness, and strong spillover and linkage capabilities with the domestic economic sector. The new context also helps reduce dependence on tax incentives, avoiding resource wastage and the negative consequences of a race to the bottom on taxes.

4.2 Policy implication recommendations

To overcome challenges and seize opportunities, Vietnam needs to implement a comprehensive package of policy solutions, including both rapid short-term responses and long-term strategies.

4.2.1 Regarding tax policy (Short- and medium-term response)

The foremost and most urgent priority is the promulgation and effective implementation of a qualified domestic minimum top-up tax rule. Resolution No. 107/2023/QH15 of the National Assembly is the first legal step, but subsequent implementation steps, such as developing detailed guiding decrees, are crucial. These regulations must ensure strict compliance with OECD model rules and guidance to be recognized by other countries, thereby successfully protecting the nation's taxing rights and revenue.

In parallel, Vietnam needs to review and restructure its entire investment incentive system. The focus should be on shifting from incentives based on tax rates and income to forms of cost-based incentives or direct support mechanisms. These tools, such as partially subsidizing the cost of high-quality labor training, supporting R&D expenses, assisting with site clearance costs and essential project infrastructure, or cash grants for strategic projects, will directly reduce the initial investment cost for businesses without affecting the effective tax rate, thus retaining their effectiveness in the GMT context.

4.2.2 Regarding investment attraction policy (Long-term strategy)

In the long term, Vietnam's competitive advantage must be built on non-tax factors. This requires political determination to push for administrative procedure reforms towards streamlining, transparency, and reducing compliance costs. Enhancing the stability, consistency, and predictability of the legal and policy system is a key factor in strengthening investor confidence.

Furthermore, a strong and targeted public investment strategy in both hard and soft infrastructure is necessary. The synchronous development of transportation, logistics, and clean energy infrastructure will help reduce costs and improve business operational efficiency. At the same time, investing in digital infrastructure, building innovation centers, and perfecting the startup ecosystem will be the foundation for attracting high-tech projects.

Improving the quality of the labor force is a strategic task. A fundamental reform of the education and vocational training system is needed, strengthening the linkage mechanism between training institutions and businesses to ensure the labor supply meets market demands. Finally, developing breakthrough policies to foster supporting industries is a vital requirement, helping Vietnamese enterprises to participate more deeply in the supply chains of MNEs, increasing domestic value-added, and promoting technology spillovers.

5. Conclusion

The advent and implementation of the Global Minimum Tax have marked a historic turning point, fundamentally reshaping the decades-old economic relationship between corporate income tax and foreign direct investment. This study indicates that for a country like Vietnam, which has heavily relied on low tax rate incentives as its primary competitive tool, the impact is particularly profound. The traditional inverse correlation between tax and FDI is severely challenged as tax rate incentives are economically neutralized for MNEs subject to the rules. This forces Vietnam's competitive advantage in the new era to shift, no longer depending mainly on tax incentives but having to be built on the foundation of a comprehensive, transparent, stable, and high-quality investment environment.

Against this backdrop, the policy implications proposed in this paper emphasize the need for a dual strategy, one that is both timely in its response and formative in its long-term vision. In the short term, the urgent and effective application of a Qualified Domestic Minimum Top-up Tax is an imperative to protect national revenue. Concurrently, restructuring the incentive system towards cost-based support is a key solution to maintain investment attractiveness. In the long run, Vietnam's success will be determined by its relentless efforts to improve non-tax factors, from institutional reform and infrastructure development to enhancing the quality of its human resources.

This paper, using a qualitative research method, has systematized and analyzed the initial theoretical and practical aspects. However, for more comprehensive assessments, future research directions are necessary. First, quantitative studies should be conducted once sufficient statistical data is available to accurately measure the impact of the GMT on the structure and scale of FDI flows into

Vietnam. Second, comparative studies of Vietnam's policy responses with those of competing countries in the region, such as Malaysia, Thailand, or Indonesia, will provide valuable lessons. Finally, more in-depth analyses are needed on the effectiveness and design of new-generation non-tax incentives to optimize investment attraction policies in the new context.

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