An analysis of tax incentives in the FDI decision process from organisational structural perspectives: Evidence from UK multinationals

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Abstract

This paper investigates the role of tax incentives in the FDI decision making process in a sample of UK multinational companies. The paper considers the relative importance of stages and determinants in the FDI decision making process. The determining factors in FDI decision process are examined from the organisational structure perspectives – FDI ownership form and market entry mode. The paper specifically identifies the role of tax in the strategic decisions of FDI organisational structure, as well as the stages of FDI decision making process. Relatively few prior empirical studies have examined the interface between tax strategy and corporate strategy in the context of FDI organisational structure and decision making process. This paper therefore attempts to examine the tax incentives for FDI decision process from the perspectives of the organisational structure.

1. Introduction

Foreign direct investment (FDI) has attracted the attention of many researchers for several decades (Demirbag, Tatoglu and Glaister, 2008, 2010; Dunning, 1993; Mintzberg, Raisinghani and Thèorêt, 1976). The FDI decision making process, however, has received little attention from researchers. The existing literature generally treats tax issues as a single factor in a list of considerations underlying the choice of organisational structure of the FDI. The interaction between tax strategy and the strategic decisions of organisational structure in the FDI is ignored in the mainstream literature. Also, there is very little evidence in the current literature to demonstrate the FDI decision making process with respect to the choice of FDI organisational structure – market entry mode and ownership form. The importance of stages in the FDI decision making process and the role of tax in relations to the stages where tax incentive is taken into consideration is lacunae. As certain stages of the FDI decision process emphasised in the decision making process might lead to different strategic decisions. It is therefore important to examine the variation in importance of the stages of the FDI decision process with the choice of the ownership form and market entry mode of FDI.

In order to address these lacunae, this paper will serve the following main goals. It will:

(i) examine the relative importance of variables and stages in the FDI decision making process;

(ii) identify the determinants for the FDI organisational structure decisions;

(iii) provide a set of distinct non-overlapping determinants and influences of FDI decision process and organisational structure for the sample studied by means of factor analysis;

(iv) consider the variables of FDI decision process in the context of the sample characteristics: the ownership form and market entry mode; and

(v) evaluate the factors of organisational structure by stages of considering tax implications

The remainder of the paper is structured as follows. The next section briefly considers the prior literature relating to FDI decision process in respect of the FDI organisational structure, and sets out the research questions of the study. Research methods for the study are in the third section. This is followed by a presentation of the findings and discussion. A summary and conclusions are provided in the final section.

2. Literature Review and Research Questions

FDI decision process in respect of FDI organisational structure

When a UK firm decides to undertake FDI, the issue of whether to acquire an existing local firm (by merger or acquisition) or to establish a completely new subsidiary (‘greenfield’ investment) in the foreign market has to be decided (Dikova and Van Witteloostuijn, 2007; Harzing, 2002). A substantial number of studies has investigated the influences with respect to the choice between mergers or acquisitions (M&A) and ‘greenfield’ investment (Anderson and Svensson, 1994; Arslan and Larimo, 2011; Barkema and Vermeulen, 1998; Brouthers and Brouthers, 2000; Demirbag, Tatoglu and Glaister, 2008; Padmanabhan and Cho, 1995; Slangen and Hennart, 2007). Several researchers have found that an MNE favours the M&A over the ‘greenfield’ investment in terms of strategic market entry mode (e.g., Arslan and Larimo, 2011; Demirbag, Tatoglu and Glaister, 2008; Hennart and Park, 1993; Larimo, 2003). All these studies have in common that they examine the choice of market entry mode from strategic and non-tax specific characteristics. Glaister and Frecknall-Hughes (2008: 41) undertook a tax specific research and argued that the choice of market entry mode is typically driven by strategic or commercial objectives rather than tax incentives. Becker and Fuest (2011: 477) claimed that greenfield investment becomes more tax sensitive due to the existence of M&A investment. Desai and Hines Jr. (2004: 19) debated that the contractual arrangements of M&A in comparison with building up a new entity from scratch, can offer numerous possibilities for sophisticated tax strategy due to the acquisition of an existing firm located in countries with different tax rates. Furthermore, in many cases, however, tax strategy is considered to be a post-deal activity (PriceWaterhouseCoopers, 2006) and the deal structure with respect to tax implications is often not given enough attention in the decision process.

While a number of studies has identified the choice of the ownership form of FDI (Brouthers, Brouthers and Werner, 2008; Buckley and Casson, 1998; Cui and Jiang, 2009; Erramilli and Rao, 1993; Kim and Hwang, 1992; Kwon and Konopa, 1993; Laufs and Schwens, 2014; Morschett, Schramm-Klein and Swoboda, 2010; Ripollés, Blesa and Monferrer, 2012), little attention has been paid to the FDI decision making process with respect to the choice of the ownership form. Harzing (2002: 211) claimed that equity-based entry modes of FDI are joint venture (JV) and wholly owned enterprises. Wholly owned enterprises may be either a wholly owned subsidiary (WOS) or a branch/division of an established enterprise. The WOS is considered as a separate legal entity of the parent firm whereas the branch/division of the established enterprise is not. Several international business scholars suggest that the WOS is more favourable than the other two entry modes due to extensive knowledge and experience in the host countries (Slangen and Tulder, 2009; Barkema and Vermeulen, 1997; Demirbag, Tatoglu and Glaister, 2009; Kim and Hwang, 1992; Padmanabhan and Cho, 1996; 1999; Yiu and Makino, 2002). While other researchers argue that high levels of external uncertainty lead MNEs to choose JVs over WOSs as such JVs enable enterprises to reduce external uncertainty (Hill, Hwang and Kim, 1990; Luo, 2001; Slangen and Tulder, 2009; Xu and Shenkar, 2002). These empirical studies, however, neglected the tax related determinants in the choice of FDI ownership form. Desai and Hines Jr. (1999: 380) suggest that the tax system often gives firms incentives to adopt certain forms. For instance, a UK firm is likely to have to choose between a subsidiary and branch in terms of launching a new firm in a foreign market. Given the nature of the two ownership forms, if a UK-based MNE sets up a subsidiary, the subsidiary will be taxed on its corporate earnings and the dividends, royalties, interest payments flowing from the subsidiary to the UK parent are subject to UK taxes. However, organising units as branches will result in the inclusion of all branch income in the worldwide income of the UK parent firm because a branch is not an independent legal entity, but merely an extension of the parent.

A review of the prior literature indicates that the FDI decision making process and stages at which the tax implications are considered in the investment decision process are lacunae. As little guidance is mentioned in the literature as to how the choice of the organisational structures - ownership form and market entry mode is associated with the FDI decision process. It is important to examine the role of tax in the choice of FDI organisational structure, as well as identify whether there are differences in the decisions of organisational structure with respect to the variables of the FDI decision making process. To address these issues in the current literature, it is therefore essential to investigate the following questions.

(i) Does the importance of the variables in the FDI decision making process vary according to the choice of the FDI ownership form?

(ii) Does the importance of the variables in the FDI decision making process vary with the choice of the market entry mode?

(iii) What is the relative importance of the stages of the FDI decision making process in practice?

(iv) Does the relative importance of the organisational structure-related factors vary with the stages at which tax implications are considered in the FDI decision making process?

3. Research Methods

Given the nature of this study, a self-administered questionnaire was deemed the most suitable means of collecting data. The questionnaire was developed according to procedures outlined by Gill and Johnson (2010: 141). Following Gill and Johnson (2010: 141), particular attention was paid to questionnaire focus, question phrasing, the form of response, question sequencing and overall presentation.

In order to confirm understanding of the main research issues on the part of potential respondents and to make sure that the content and format of the questionnaires were clear and unambiguous, a pilot test was undertaken in July 2009. A total of 30 companies was approached for this pilot test study. Feedback from the respondents indicated that the questionnaire was adequately designed, was comprehensive and would obtain detailed data on the role of tax in the FDI decision process.

The questions incorporated in the instrument were broadly of two types: categorical questions of a factual nature, and questions designed to measure the attitude and perceptions of the respondents. In line with prior research, these research questions were of an ordinal nature. Ordinal classification of attitude and perception was considered a more realistic task for respondents than the use of interval or ratio measures (Geringer, 1991: 51). Given that the time available to the target respondents – senior managers to complete the questionnaire would be limited, an easily understood Likert-type scale was adopted. Questions were restricted to a five-point scale, since it was felt that more numerous response categories would make it too onerous for respondents to discriminate, leading to ‘noise’ rather than more precise data (Geringer, 1991: 51; Glaister and Buckley, 1998: 100).

3.1 Respondent Selection

The FAME database for UK companies was used as a sampling frame. FAME is a comprehensive database of listed companies, which contains ten years of detailed information and includes summary data for subsidiaries, as well as information for liquidated companies. The Hemscott Company Guru database was also used to provide detailed information on directors, organisational management and the activity status of firms.

The sampling frame of UK companies selected from the FAME database was 4,068 companies. The initial selection criterion was a minimum turnover of £200,000 which aimed to filter out very small businesses. The 3,500 companies (out of the 4,068) for which the FAME database contained e-mail addresses were initially contacted by e-mail to request participation in the survey. Since the questionnaires were sent out by e-mails with a direct link to the on-line questionnaire, all the respondent companies were required to have e-mail addresses. The objective of sending such requests was to identify participants who would/could respond and also prepare for the distribution of the questionnaire.

Out of 3,500 companies contacted initially, 780 firms indicated that they did not wish to participate. A total of 2,720 on-line questionnaires was then distributed to the potential respondents. Feedback from the participating organisations indicated that the best person to complete the questionnaire were Chief Financial Officers (CFOs) or Group Directors of Taxation rather than tax specialists. This was because tax managers found it a struggle to answer several of the questions as they had not been involved in the FDI decision making process, hence they could only make a limited contribution to this survey.

To encourage responses, two UK professional organisations, the Chartered Institute of Taxation (CIOT) and the Institute of Chartered Accountants of Scotland (ICAS) provided support for this research by assisting in the distribution of the questionnaires to their industry and company members. To ensure the likelihood of good quality responses, the e-mails with covering letters were sent out to the CFOs and Group Directors of Taxation in UK multinational companies. The covering letter identified the researcher, explained the research objective, assured confidentiality and created a direct link to the on-line questionnaire. An offer of a summary of the study's results (with anonymity maintained), was given to respondents to try to influence positively the likelihood of response. Following two rounds of reminder e-mails and follow-up phone calls, a total of 273 firms indicated either that they had not engaged in FDI or had not undertaken FDI in the previous five years and hence were not eligible to complete the questionnaire. A total of 326 questionnaire responses were obtained, of which 134 were not fully complete, leaving 192 usable responses - a usable response rate of 7.9%.

Given that the focus of this study was taxation, this is a relatively good response rate, especially in terms of obtaining on-line questionnaire responses from a commercial and industrial population. According to Saunders, Lewis and Thornhill (2012: 235), organisations are less likely to cooperate where the topic of the research is relatively sensitive. Further, for regular mail surveys without a telephone follow-up or pre-contact, response rates vary between 6 and 16 per cent (Harzing, 1997). Cycyota and Harrison (2006: 140) have indicated a low rate of response from executives. Other academic studies, which obtained data from company executives, demonstrated a similar response rate. For example, Graham and Harvey (2001) achieved a response rate of nearly 9 per cent from CFOs. Some studies have reported lower response rates than that reported in this study. For instance, Koch and McGrath's (1996) study had a 6.5 per cent response rate as did that by Lepak, Takeuchi and Snell (2003). The 192 usable responses returned in this research could be expected to provide fairly representative and generalisable results.

3.2 Characteristics of the Sample

The characteristics of the sample used in this chapter are summarised in Table 1.

[Insert Table 1 here]

The distribution of the sample of FDI by equity ownership forms can be categorised into three sub-groups, namely JV, WOS and branch/division. The market entry mode of FDI can be partitioned into 'greenfield' investment and M&A. The size of parent firm is classified by reference to the number of employees. The data, however, shows that the outliers positively skewed the distribution. According to Field (2009: 98), outliers can affect the measure of the mean. The median was therefore considered as the best representation of the size of parent firm in the study. Hence, four outliers were removed from the sample in order to reduce the effects of the outliers skewing the statistical results. The range of the minimum and maximum of the size of parent firm extends from 3 to 10,000 employees. The median value was thus adjusted to 1,000 employees, hence the number of employees from 3 to 1,000 is categorised as small sized firm whereas from 1,001 to 10,000 employees is classified as large sized firm.

3.3 Determinants and stages of FDI decision making process

The questionnaire presented a list of nine determinants affecting the FDI decision making process. The nine determinants in the order they appeared on the questionnaire are shown in Appendix (Table A1). Respondents were asked: 'How important were the following factors in affecting the FDI decision making process?' Responses were assessed using a five point Likert scale (where 1 = 'not important' and 5 = 'very important').

A list of eight stages in the FDI decision making process was presented in Appendix (Table A2). The eight stages in the order they appeared on the questionnaire are shown in Table 6.3. Respondents were asked 'How important were the following stages in the FDI strategic decision process?' Further, the same eight stages were used to identify the relative importance of the tax consideration at each stage of the FDI decision making process. The respondents were asked: 'How important were tax considerations at each stage of the FDI decision process?' Responses were again assessed using five point Likert scales (where 1 = 'not important' and 5 = 'very important').

3.4 Stages of tax implications considered in the FDI decision process

Three stages determine the stages of tax implications to be considered in the FDI decision making process. The stages in the order they appeared on the questionnaire are shown in Table 2. Respondents were asked: 'At what stage were tax implications considered in the FDI decision making process?' Respondents were assessed by giving three options to select the particular stage at which the tax implications are taken into consideration.

[Insert Table 2 here]

4. Findings and Discussion

4.1 FDI decision making process

4.1.1 The relative importance of stages in the FDI decision process with tax consideration

The rank order of the variables of the FDI decision process in the condition of taking tax issues into consideration is shown in Table 3.

[Insert Table 3]

For the full set of eight stages in the FDI decision making process with tax considerations, the scale measure of 3 is exceeded by three stages of which ‘identifying the legal structure’ (3.52), ‘identifying the ways of financing the FDI’ (3.22) and ‘identifying the organisational form’ (3.11) comprise the first three stages with the highest degree of importance. Other relatively less important stages in the FDI decision process when tax issues are taken into consideration include ‘reviewing the choice of decision’ (2.59) and ‘investigation of investment opportunity’ (2.47). By contrast, neither the stage of ‘recognition of investment opportunity’ (2.21), ‘investigation of target market’ (2.18) nor ‘identifying the management structure’ (2.03) are perceived as an important stage for the FDI decision process when tax issues are taken into consideration.

4.1.2 Variables for FDI decision making process

The rank order of the variables for the FDI decision making process based on the mean measure of the importance of the eight components is shown in Table 4.

[Insert Table 4 here]

For the full set of variables for the FDI decision making process, the variable of ‘strategic plan of the firm’ (4.71) obtains the highest degree of importance in the rank order, with a mean being significantly above the median point on the scale. It is clear from Table 4 that the most important element in the FDI decision process is primarily concerned with the corporate strategic point of view which is in line with the findings of Wilson (1990: 29) where the actual initiation of foreign investment proposals was mainly via the corporate strategy group.

The second group of variables of the FDI decision process (those ranked 2 to 4) are mainly concerned with cost, location and available partners: ‘size of the investment’ (2.85), ‘potential target country’ (2.81) and ‘available acquisition candidate’ (2.44). However, their means are below the median of the scale. Such results indicate that investigating the potential market situation and gathering relevant information are perceived as the second most important components in the FDI decision making process.

The third and lowest ranked group (5 to 8) consist of a number of distinct variables. The variable ‘prior international operational experience’ (2.28) is not perceived as an important driving force. Similarly, the variables of ‘effective management’ (1.99) and ‘competition situation’ (1.98) do not feature as being important. The variable of ‘available joint venture partner’ (1.96) is ranked lowest for the FDI decision process.

In order to reduce the number of observed variables and make the analysis more meaningful, factor analysis was used to extract the underlying factors, shown in Table 5.

[Insert Table 5 here]

The eight variables of the FDI decision making process represent a number of overlapping perspectives, which is confirmed partly by the existence of a number of low to moderate inter-correlations between the components. Owing to potential conceptual and statistical overlap, an attempt was made to identify a set of variables to determine the underlying primary dimensions of the components in the FDI decision process for the sample data. Exploratory factor analysis using varimax rotation was used to extract the underlying constructs. The factor analysis produced three underlying factors which make good conceptual sense and explained a total of 58.4 per cent of the observed variance, as shown in Table 5. It is important to note that a negative value for Cronbach alphas was obtained in the results. Thus, an internal reliability test showed that Cronbach alphas for the underlying factors range from 0.05 to 0.61. The negative Cronbach alpha apparent in the study is mainly due to the negative relationship between the two variables of ‘available acquisition candidate’ and ‘available joint venture partner’. The covariance between the two components is subsequently negative, which directly causes the negative Cronbach alpha in the result (Field, 2009: 676). It suggests that if UK companies choose available acquisition candidate, then joint venture partners are unlikely to be selected. The three underlying factors may be summarised as: *corporate strategic considerations*, *evaluation of management and competition situation*, and *availability of foreign partners*.

4.2 Determinant factors in FDI decision process and organisational structure

To investigate further the underlying nature and pattern of the FDI decision making process associated with the FDI strategic decisions in terms of organisational structure - ownership form and foreign market entry mode, the analysis was developed by undertaking multinomial logistic regressions and binomial logistic regressions. In this case, the three underlying factors of the FDI decision making process were assumed to be a set of independent factors, while the ownership form and foreign market entry mode were considered as dependent variables, and the size of parent firm was regarded as a control variable in the statistical test. The overseas ownership forms consist of joint venture (JV), wholly owned subsidiary (WOS) and branch/division in this study. As the dependent variable can be categorised into more than two non-ordinal categories, a multinomial logistic regression was employed in the statistical test.

Before the analysis, the assumptions of the model were checked, including the collinearity within the data. The Durbin-Watson test was used to check whether the residuals in the model are independent. The correlation matrix is shown in Table 6.

[Insert Table 6 here]

Table 6 reports the descriptive statistics and correlation matrix of the variables in the FDI decision making process. The pair-wise correlations do not seem to present serious collinearity[1] problems for the multivariate statistical analysis, as none of the variables has a correlation coefficient above 0.50. According to Wetherill (1986: 105), the correlations between relevant pairs of variables should not be large because it might restrict the generality and applicability of the estimated model.

[1] The effect of collinearity is to inflate the variance of the least squares estimator and possibly any predictions made, and also to restrict the generality and applicability of the estimated model (Wetherill, 1986, p. 82).

4.2.1 Determinant factors in FDI decision process and ownership form

The results of multinomial logistic regression of the determinant factors in the FDI decision process associated with the FDI ownership form are presented in Table 7 below.

[Insert Table 7 here]

In Table 7, the significant model chi-square values of 40.95 ($p < 0.01$) and log likelihood measures suggest that the three models have high overall explanatory power. Pseudo R-square measures also confirm that all the models have adequate explanatory power. Further, the models have a good fit with a classification rate of 73 per cent of the observations. Rates that are higher than that would be expected by chance. The primary interpretation is based on the estimated odds ratios (exponentiated β), which relate independent variables of the three determinant factors of the FDI decision process for the ownership form categories to their impact on a reference category (Feeney and Bozeman, 2010: 1665). The results shown above suggest that there is a relatively weak support for the view that the relative importance of the variables of the FDI decision process will vary with the choice of the FDI ownership form because only one factor of *availability of foreign partners* ($p < 0.01$) shows statistically significant coefficients.

The findings indicate that although all the three determinant factors of the FDI decision process affect the general strategic decision making in the FDI, the choice of the ownership form is not highly associated with the underlying factors, except for *availability of foreign partners*. The factor of *availability of foreign partners* ($p < 0.01$) was the only factor found to be statistically important to the ownership form decisions. When UK firms select the ownership forms between JV and WOS, the factor of *availability of foreign partners* obtains a positive coefficient in model 1 and a negative coefficient in model 2, which suggests that the particular factor is more important to the ownership form of JV than the WOS. Similarly, when the choice is made between branch and JV, the factor of *availability of foreign partners* obtains statistically significant coefficients. The negative coefficient in model 2 and positive coefficient in model 3 indicates that this factor is predicted as a more important determinant to the ownership form of JV than the branch/division.

Such results might be mainly due to the fact that a JV is a form of partnership. Thus, the UK firms are more likely to choose the ownership form of JV when the choice of the ownership form is made between JV and any other forms because of partner availability, whereby foreign firms are ready for the UK firms to select and co-operate with. The finding implies that if foreign partners are available, UK companies tend to choose an easy option in terms of ownership form decisions as it makes investment relatively easier by going for partnership rather than building up from scratch. It is important to note that when the ownership form decisions are made between branch and WOS, the factor of *availability of foreign partners* is no longer significant because none of the forms can take partnership form.

4.2.2 Determinant factors in FDI decision process and market entry mode

In order to examine the relationship between the variables of the FDI decision process and the FDI strategic decisions in terms of the foreign market entry mode, a binomial logistic regression was undertaken to identify the main predictors. This is because the dependent variable is a binary and dichotomous variable which can be coded as Yes/No or 0/1. A binomial logistic regression was therefore used to implement the data analysis (Pallant, 2007: 169). The results of binomial logistic regression are shown in Table 8.

[Insert Table 8 here]

Table 8 shows weak support for the view that the relative importance of the underlying factors of the FDI decision making process will vary with the choice of the market entry mode of FDI. Only one of the three factors, that is, *availability of foreign partners*, shows a statistically significant coefficient ($p < 0.01$). In order to examine whether the variables of the FDI decision process will vary with the choice of the foreign market entry mode, the entry mode of 'greenfield' investment was used as the base mode and assigned a value of zero. The model has a highly significant explanatory power with a model chi-square of 27.04 ($p < 0.01$) and correctly classifies 79 per cent of the observations. In line with the examination, the coefficient of *availability of foreign partners* is positive, indicating that, regarding the availability of partners in the host market, the entry mode of 'greenfield' investment is relatively more important than cross-border M&A.

The findings suggest again that not surprisingly, firms might prefer to choose a comparatively easier option instead of a difficult one in terms of the choice of market entry mode. A firm can establish a subsidiary from scratch, that is so-called 'greenfield' investment, or by acquiring an enterprise in the target market, that is an M&A. From its definition it is clear that an international M&A involves multinationals in taking over firms in a foreign market. With respect to the availability of acquisition candidates in the host market, it was expected that the M&A would be preferred to 'greenfield' investment. However, the results were surprising, which suggest that UK firms are more likely to select 'greenfield' investment than M&A. This might be because M&A is relatively more challenging than 'greenfield' from the perspective of the effects of external factors and risks associated with acquisition partners (Wang, 2009: 242). According to Wang (2009: 240), M&A is an investment model which expands the internal organisation of firms through the external market trading, whereas in a 'greenfield' model, external market trading has been replaced by trading in the enterprises' internal organisation. By making a comparison between the two modes, therefore, it is apparent that 'greenfield' investment is likely to be preferred more than M&A ever where foreign partners are available in the host country. In other words, if foreign partners are available, the M&A will not necessarily be preferred to 'greenfield' in investment.

4.3 Tax incentive in FDI decisions from organisational structure perspective

Table 9 indicates that the three organisational structure-related influences are perceived as the most important determinants for the organisational form decisions: 'effective management structure' (3.24), 'company preferred this organisational form' (3.21), and 'how the organisational form was financed' (3.15), with means being above the median point on the scale (1 to 5). The results show that the highest ranked influences for the organisational form of the FDI are principally concerned with the effectiveness of the structure, company preferences, as well as the way of financing the FDI.

[Insert Table 9 here]

The second group of influences (those ranked 4 to 8) are mainly concerned with cost, risk sharing, nature of location, and regulatory requirements of the formation to achieve a sound organisational structure in a foreign market. These determinants are: 'taxation factors' (3.08), 'ease of profit extraction' (3.08), 'nature of location of investment' (2.69), 'regulatory requirements. (2.55) and 'risk sharing' (2.52), with the mean values being slightly above or fairly below the median of the scale.

The third and lowest ranked group (9 to 10) consists of two distinct organisational structure-related influences. The influence of 'ease of cooperation between two partners' (2.44) does not feature as being important. Similarly, the influence of 'compliance with legal requirement' (2.32) is the lowest ranked organisational structure-specific influence for the FDI undertaken by UK firms.

The factor analysis of the organisational structure-related influences is shown in Table 10.

[Insert Table 10 here]

The correlation matrix of ten organisational structure specific influences revealed a number of low to moderate inter-correlations between the influences. Owing to potential conceptual and statistical overlap, an attempt was made to identify a set of variables to determine the underlying primary dimensions governing the full set of ten organisational structure-related determinants in the FDI. Exploratory factor analysis using varimax rotation was used to extract the underlying constructs. Factor analysis produced four underlying factors which make good conceptual sense and explained a total of 75.1 per cent of the observed variance. Also, an internal reliability test showed strong Cronbach alphas for the underlying factors ranging from 0.57 to 0.88. The four determinant factors may be summarised as: *financial strategies*, *corporate strategic behaviours*, *legal concerns*, and *management and organisational structure*.

4.4 Interaction of the organisational structure-related factors with the stages at which tax implications are considered in the FDI decision process

To examine whether the relative importance of the organisational structure-related factors varies with the stages at which tax implications are considered in the FDI decision process, an one-way ANOVA was employed.

[Insert Table 11 here]

Table 11 shows that there is little support for the view that the relative importance of the organisational structure-related factors varies with the stages at which tax implications are considered in the FDI decision making process. This is because only one factor, *financial strategies* ($p < 0.1$) shows a statistically significant difference in means between the various stages at which tax issues are considered, being relatively more important for the stage at which tax issues are considered after FDI decisions are made. Such results suggest that tax issues are indeed considered after the FDI strategic decisions have been made. It provides evidence to support the argument in the previous section that tax issues usually come as secondary after the corporate strategic decisions are made. A conclusion drawn from the findings is that tax decisions appear to be a second order consideration rather than a dominant influence, because the corporate strategy is the driving force of the FDI strategic decisions, which is in line with the findings of Glaister and Frecknall-Hughes (2008: 41).

Summary and Conclusion

The strategic decisions in terms of capital investment in the foreign market, the process by which the FDI decisions are made, is a neglected research area. Little is known about the way tax issues are treated in the FDI decision process and also the specific stages at which tax implications are brought into the FDI decision making process. In an attempt to bridge the gap in the literature, this paper has examined several research questions by using factor analysis, multinomial and binomial logistic regressions, together with one-way ANOVA and a paired-sample *t*-test.

Tests of the variables of the FDI decision process provided evidence that the relative importance of the variables hardly varies with the FDI strategic decisions in terms of the ownership form and market entry mode. If a JV partner is available in the foreign market, firms are more likely to select the JV formation as an ownership form compared with the forms of WOS and branch. From the perspective of available foreign partners, 'greenfield' investment is preferred more than M&A in terms of foreign market entry mode due to lack of availability of partners or external factors such as high risk involved.

Furthermore, tests of the relative importance of the stages of the FDI decision making process with tax considerations provided evidence to argue that the relative importance of the stages of the FDI decision process will vary with the situation where tax issues are taken into consideration in the decision process. Importantly, it was found that tax implications were usually considered after the corporate strategy had been made in the FDI decision process. Also, the findings suggest that tax can play an important role at the stages of reviewing the choice of decisions and identifying the operation structures in terms of legal structure, organisational form and financial structure.

Overall, a conclusion from the findings is that tax strategy is usually put as secondary after corporate strategy has been made in the FDI decision process.

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Table 1. Characteristics of the sample

	Total		%	
FDI equity ownership form				
Joint venture (JV)	39		20.3	
Wholly owned subsidiary (WOS)	132		68.8	
Branch/division	21		10.9	
		192		100
Market entry mode of FDI				
'Greenfield' investment	66		34.4	
Merger or acquisition (M&A)	126		65.6	
		192		100
Size of parent firm (no. of employees)				
3 – 1,000	97		51.6	
1,001 – 10,000	91		48.4	
188[a]		100		

Notes:
[a]Missing values = 4

Table 2. Stages of tax implications considered in FDI decision process

(1)	At the stage when investment proposal is raised
(2)	At the stage after the investment proposal is decided
(3)	Both before and after the investment proposal is made

Table 3. The importance of stages in the FDI decision making process: with tax considerations

Stages	Rank	Mean	SD
Identifying the legal structure	1	3.52	1.38
Identifying the ways of financing the FDI	2	3.22	1.24
Identifying the organisational form	3	3.11	1.23
Reviewing the choice of decision	4	2.59	1.12
Investigation of investment opportunity	5	2.47	1.30
Recognition of investment opportunity	6	2.21	1.24
Investigation of target market	7	2.18	1.24
Identifying the management structure	8	2.03	1.15

N = 192

Notes:
1. The mean is the average on a scale of 1 (= 'of no importance') to 5 (= 'of great importance').
2. SD = standard deviation

Table 4. Variables for FDI decision making process: determinants ranked by mean measure of importance

Variables	Rank	Mean	SD
Strategic plan of the firm	1	4.71	0.72
Size of the investment	2	2.85	1.45
Potential target country	3	2.81	1.44
Available acquisition candidate	4	2.44	1.42
Prior international operation experience	5	2.28	1.30
Effective management	6	1.99	1.21
Competition situation	7	1.98	1.21
Available joint venture partner	8	1.96	1.31
N = 192			

Notes:
1. The mean is the average on a scale of 1 (= 'of no importance') to 5 (= 'of great importance').
2. SD = standard deviation

Table 5. Factors of FDI decision making process

Factors	Factor loads	Eigen-value	% Variance explained	Cumulative %	Cronbach alpha
Factor 1: Corporate strategic considerations		2.30	28.8	28.8	0.61
Size of the investment	0.745				
Potential target country	0.698				
Prior international operation experience	0.695				
Strategic plan of the firm	0.436				
Factor 2: Evaluation of management and competition situation		1.23	15.4	44.2	0.55
Effective management	0.835				
Competition situation	0.767				
Factor 3: Availability of foreign partners		1.14	14.2	58.4	-0.05
Available acquisition candidate	0.763				
Available joint venture partner	-0.551				

Notes:
Principal components factor analysis with varimax rotation.
K-M-O Measure of Sampling Adequacy = 0.620.
Bartlett Test of Sphericity = 183.204; $p < 0.000$.

Table 6. Descriptive statistics and correlation of determinant factors for FDI decision making process

Variables	Mean	SD	1	2	3	4	5	6
1. FDI ownership form	2.48[2]	0.81	1.00					
2. Foreign market entry mode	0.66[3]	0.48	0.14	1.00				
3. Size of parent firm[a]	1.48[4]	0.50	-0.20**	0.15*	1.00			
4. Corporate strategic considerations	4.04	0.67	-0.04	0.07	0.07	1.00		
5. Evaluation of management and competition situation	3.17	0.96	-0.04	0.02	0.02	0.27**	1.00	
6. Availability of foreign partners	2.81	1.03	-0.36**	0.33**	0.17*	0.34**	0.23**	1.00

Notes:
N = 192
SD = standard deviation
[a] Number of employees
*p< 0.05; **p< 0.01 (two-tailed).

[2] The FDI ownership form was categorised into three sub-groups: joint venture (JV), wholly owned subsidiary (WOS) and branch/division. JV was coded as 1, WOS was coded as 2, and branch/division was coded as 3. The mean value (2.48) is higher than the median point (2) on the scale, which suggests that UK firms prefer WOS to JV and branch when they select the FDI ownership form.

[3] The foreign market entry mode consists of two modes: 'greenfield' investment and merger or acquisition (M&A). The entry mode of 'greenfield' investment was coded as 0 and M&A was coded as 1. The mean value (0.66) shows that there are more firms entering the foreign market by M&A than 'greenfield' investment.

[4] The size of parent firm was measured by the number of employees in the parent firms. It was partitioned into two sub-groups: small (3 – 1,000) and large (1,001 – 10,000). The small parent firm was coded as 1 and the large parent firm was coded as 2. The value of 1.48 is slightly lower than the median point of 1.5 on the scale. This indicates that there are more small sized parent firms than large sized parent firms in the study.

Table 7. Multinomial logistic regression of the factors of FDI decision making process on overseas ownership form

Variables	Model 1[a]				Model 2[b]				Model 3[c]			
	JV vs WOS		Branch vs WOS		Branch vs JV		WOS vs JV		JV vs Branch		WOS vs Branch	
	Coeffi-cient	Odds Ratio	Coeffi -cient	Odds Ratio	Coeffi-cient	Odds Ratio	Coeffi-cient	Odds Ratio	Coeffi-cient	Odds Ratio	Coeffi -cient	Odds Ratio
Intercept	-3.14		-1.06		2.09		3.14		-2.09		1.06	
Factor 1: Corporate strategic considerations	-0.38	0.69	-0.21	0.81	0.17	1.18	0.38	1.46	-0.17	0.85	0.21	1.23
Factor 2: Evaluation of management and competition situation	-0.08	0.93	-0.19	0.83	-0.11	0.89	0.08	1.08	0.11	1.12	0.19	1.21
Factor 3: Availability of foreign partners	1.35	3.85***	0.10	1.11	-1.25	0.29***	-1.35	0.26***	1.25	3.47***	-0.10	0.90
Control variable:												
Size of parent firm	-1.18	0.31*	0.57	1.76	1.75	5.74***	1.18	3.26*	-1.75	0.17***	-0.57	0.57
Model chi-square $X^2(8)$	40.95***				40.95***				40.95***			
2 Log likelihood	220.96				220.96				220.96			
Correct classificaiton	0.73				0.73				0.73			
Pseudo *R*-square: Cox & Snell	0.21				0.21				0.21			
Nagelkerke	0.26				0.26				0.26			
McFadden	0.14				0.14				0.14			
N	181				181				181			

Note:
[a] Ownership form of wholly owned subsidiary (WOS) as a reference category
[b] Ownership form of joint venture (JV) as a reference category
[c] Ownership form of branch as a reference category
**p*< 0.1; ****P* < 0.01 (two-tailed test of significance).

Table 8. Binomial logistic regressions of the factors of the FDI decision making process on foreign market entry mode

Variables	Greenfield vs Merger or Acquisition (M&A = 1)	
	Coefficient	Wald statistics
Intercept	-1.25	0.29
Factor 1:Corporate strategic considerations	-0.13	0.88
Factor 2: Evaluation of management and competition situation	-0.10	0.91
Factor 3: Availability of foreign partners	0.81	2.25***
Control variable:		
Size of parent firm	0.42	1.53
Model chi-square $X^2(8)$	27.04***	
Sensitivity	0.94	
Specificity	0.48	
Correct ratio	0.79	
Pseudo *R*-square: Cox & Snell	0.13	
Nagelkerke	0.18	
N	181	

Note:
****p* < 0.01 (two-tailed).

Table 9. Organisational structure influences for FDI decisions: determinants ranked by mean measure of importance

Organisational structure influences	Rank	Mean	SD
Effective management structure	1	3.24	1.20
Company preferred this organisational form	2	3.21	1.38
How the organisational form was financed	3	3.15	1.30
Taxation factors	=4	3.08	1.22
Ease of profit extraction	=4	3.08	1.13
Nature of location of investment	6	2.69	1.51
Regulatory requirements	7	2.55	1.44
Risk sharing	8	2.52	1.46
Ease of cooperation between two partners	9	2.44	1.42
Compliance with legal requirement	10	2.32	1.40
N= 192			

Notes:
1. The mean is the average on a scale of 1 (= ‘of no importance’) to 5 (= ‘of great importance’).
2. SD = standard deviation

Table 10. Factors of organisational structure influences in FDI

Factors	Factor loads	Eigen-value	% Variance explained	Cumulative %	Cronbach alpha
Factor 1: Financial strategies		3.23	32.3	32.3	0.75
How the organisational form was financed	0.727				
Taxation factors	0.869				
Ease of profit extraction	0.809				
Factor 2: Corporate strategic behaviours		1.82	18.2	50.5	0.76
Risk sharing	0.844				
Nature of location of investment	0.654				
Ease of cooperation between two partners	0.835				
Factor 3: Legal concerns		1.43	14.3	64.8	0.88
Regulatory requirements	0.925				
Compliance with legal requirement	0.929				
Factor 4: Management and organisational structure		1.03	10.3	75.1	0.57
Effective management structure	0.767				
Company preferred this organisational form	0.867				

Notes:
Principal components factor analysis with varimax rotation.
K-M-O Measure of Sampling Adequacy = 0.677
Bartlett Test of Sphericity = 613.443; $p < 0.000$.

Table 11. Factors of organisational structure by stages of considering tax implications

	Stages of considering tax implications			
Factors of organisational structure	Group	Mean	SD	*F*-ratio
Financial strategies	Before FDI decisions made	2.80	1.10	
	After FDI decisions made	3.53	0.75	
	Both before and after FDI decision made	3.05	1.02	2.30*
Corporate strategic behaviours	Before FDI decisions made	2.21	0.97	
	After FDI decisions made	2.78	1.45	
	Both before and after FDI decisions made	2.57	1.20	1.71
Legal concerns	Before FDI decisions made	2.35	1.15	
	After FDI decisions made	2.76	1.34	
	Both before and after FDI decisions made	2.48	1.42	0.41
Management and organisational structure	Before FDI decisions made	3.21	1.08	
	After FDI decisions made	3.32	1.04	
	Both before and after FDI decisions made	3.20	1.04	0.08
N = 187[a]	*Before FDI = 53; After FDI s = 20; Both before and after = 114*			

Notes:

The mean for the factors is the mean of the factor scores.

[a] 5 companies stated no consideration of tax implications in the decision process, so were excluded from the analysis.

*$p < 0.1$ (two-tailed).

Appendix

A1

Determinants affecting FDI decision making process: item listed by order of appearance on the questionnaire

(1)	Strategic plan of the firm
(2)	Prior international operation experience
(3)	Size of the investment
(4)	Potential target country
(5)	Available acquisition candidate
(6)	Available joint venture partner
(7)	Competition situation
(8)	Effective management
(9)	Others

A2

Stages in FDI decision process: items listed by order of appearance on the questionnaire

(1)	Recognition of investment opportunity
(2)	Investigation of investment opportunity
(3)	Investigation of target market
(4)	Identifying the appropriate organisational form
(5)	Identifying the ways of financing the FDI
(6)	Identifying the appropriate legal structure
(7)	Identifying the appropriate management structure
(8)	Reviewing the choice of decision