

## “MAPping the Future” Column in the INQUIRER – 9 November 2015



### **Tax reform—When is the proper time?**

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We need tax reform. There is no debate about that.

Our tax system is antiquated, overtaken by time. It is uncompetitive compared to that in our counterparts in the Association of Southeast Asian Nations.

It has many antibusiness provisions, which largely contributed to the growth of the underground economy, and many more.

But when is the best time for tax reform?

Should it be now when we have a government nearing the end of its term? Or should we wait seven more months for a new administration?

Economists say that ideally, tax reform is best pursued during the first six months of a new administration.

This would give the new administration a fresh start, fiscally, that is.

Proponents of ‘tax reform now’ insist that the time is now and time is of the essence. People had long been overtaxed and suffering. So true.

But to my mind, how much difference does it really make if we push for limited tax reform now (I say limited because the reform being pushed now is only for lowering the rates and widening the bracket for income tax) vis-à-vis wait for seven months, use

this time to pool resources and prepare for a well-thought and comprehensive reform package in time for the new administration?

In short, the choice is between a 'tax reform now' but with limited scope (income tax only) vis-a-vis a tax reform after seven months but comprehensive in coverage. If we talk in terms of cost of money, a seven-month lag may not mean much considering the low inflation rates.

If we talk in terms of opportunity being open now, will this opportunity be lost in seven months?

If we talk in terms of coverage, are we satisfied with a limited victory now compared to a bigger victory in seven months?

There are cries urging this current administration for the immediate passage of partial tax reforms, particularly, lowering of the tax rate both for personal and corporate taxes, and widening the income bracket. Such demand is not without basis.

Over time, there was a "bracket creep" which means even our rank-and file employees are slapped with the highest rate of 32 percent.

A table comparison of our effective tax rate with that of Asean countries will show that the Philippines is an outlier—with the highest tax imposed on both personal income and corporate income.

But the defect in our tax system is not only related to high income tax rates and narrow income brackets. It is the whole structure itself. Is our tax system still in line with the times? Is it responsive to the prevailing circumstances in the country?

Even within the income tax structure itself, there are many other things to be fixed other than the tax rates and brackets. For example, many countries which shifted away from being heavily income tax dependent have not only reduced their tax rates but have also discarded the imposition of second-level income taxes, such as dividend tax and estate tax, these being already taxed when earned.

In the case of dividend, these income are already taxed at the corporate level, and in the case of estate tax, these assets are already taxed when the decedent earned the income.

These are just examples of how income tax reforms are shaping up in other parts of the world.

The biggest fear of the government is that reforming the income tax alone without any accompanying counterpart measure to recoup the revenue losses will put our fiscal position in danger.

Understandably, income tax is the bread and butter of revenue collection.

A comprehensive review of the tax structure will address this fear by putting in place a tax system that is appropriate to our situation and fiscally adequate to meet the needs of the government.

Based on estimates, the reform will result in a revenue loss of a whopping P50 billion. Many believe that this can be recovered through administrative measures by improving the collection and administration of taxes.

But to my thinking, even if we have a Commissioner ten times the likes of Commissioner Kim Henares, nowhere will the improvement from collection near this figure, unless there are drastic reforms in the structure of the tax administration itself such as perhaps the long-pushed autonomy of the Bureau of Internal Revenue (BIR).

There are many other unfair provisions in the Tax Code that need to be reviewed and changed for being unfair to taxpayers.

Among these are the: (1) Defective procedure in claiming VAT refunds which resulted in billions of refund claims being trapped in the hands of the government; (2) Excessive penalties as high as 40 percent annually, with the simultaneous imposition of delinquency and deficiency penalty interest on unpaid taxes; (3) Disallowance of deductible expenses simply for failure to subject it to withholding tax notwithstanding the payment of the withholding tax and penalties for failure to withhold.

If we do an income tax reform now, there would be less chances of adopting a more comprehensive reform during the new administration.

It may not look good to undertake a tax reform every so often.

This means that there will be a smaller chance of having all these defects in the tax system fixed.

Looking at the platform of the presidential aspirants, tax reform is common to all except for Secretary Mar Roxas.

Both leading candidates Senator Grace Poe and Vice President Jojo Binay declared that they are for tax reform.

As to what kind of tax reform that is, we do not know. I think it is our role to provide them with inputs and help shape the tax reform they will soon champion.

As for Secretary Mar Roxas, he is towing the line of the President against tax reform.

What is not clear though is whether his statement is good for now—no tax reform now—but not “no tax reform later”.

It is possible that he may change his position later on when he assumes the Presidency considering that many of those pushing for these reforms are from his own party.

With Asean regionalization, one thing is clear—tax reform is inevitable. This is one thing we have to face head-on.

But when is the proper time? And in what form?

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