STSR TAXBITS

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by

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The 10-member Association of South East Asian Nations (ASEAN) forged the ASEAN Economic Community (AEC) Blueprint which seeks to transform ASEAN into a single market and production base through five (5) core elements, namely (i) free flow of goods; (ii) free flow of services; (iii) free flow of investment; (iv) freer flow of capital; and (v) free flow of skilled labor. In the Declaration on the ASEAN Economic Community Blueprint, the heads of States committed to abide by and implement the AEC by December 2015.[1]

A reading of the AEC Blueprint shows that while there is a long list of things-to-do in the areas of legislation and policy, the Blueprint is relatively silent in the matter of individual and corporate tax regimes. This could be justified by the Declaration whereby the heads of States recognize that the "different levels of development within ASEAN require some flexibility as ASEAN moves towards a more integrated and interdependent future".

It bears stressing that aside from the existence of reasonable levels of taxation and the overall stability of the tax regime, the most frequently cited reasons for multinational investments are the market size and growth prospects of the host country, the availability of infrastructure, stable political environment, conditions that support

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[1] ASEAN (2008). ASEAN Economic Community Blueprint.

physical and personal security, legal framework, rule of law, corruption and governance concerns.

Moreover, the European Union which existed since 1993 has skirted the issue on a uniform tax system among member-States. The EU website publishes that “National governments are responsible for raising taxes and setting tax rates. The amount of tax you pay is therefore decided by your national government, not the EU”.[2]

However, since harmonization is both a model and requisite for regional integration, differences in the corporate and individual income taxation regimes would swing the pendulum as investors and professionals could shift from a high-tax jurisdiction to a low-tax jurisdiction. Considering also that the Philippines has a rich professional population, it is not far-fetched that migration to favorable tax havens would come as a result.

Despite the avowed principle to collectively “achieve higher levels of economic dynamism, sustained prosperity, inclusive growth and integrated development of ASEAN”, the pragmatism of country competition for foreign direct investment (FDI) exists and the manipulation of tax systems is one modality to achieve an edge.

This observation finds support at the track record of ASEAN member-States which dramatically lowered their corporate income tax rates following the signing of the ASEAN Blueprint in 2007. On the average, the corporate income tax rate is at the 23.1 percentage mark and convergence to this average rate was observed, except for the Philippines which holds the highest rate at 30%.[3] At present, the standard corporate income tax rates are as follows:

Member-State	Standard Corporate Income Tax Rate
Brunei	20%
Cambodia	20%
Indonesia	25%
Laos	24%
Malaysia	25% (will be reduced to 24% beginning 2016)
Myanmar	25% - Company; 35% Branch
Philippines	30%
Singapore	17%
Thailand	20%
Vietnam	25% (reduced to 22% beginning 2014 and to 20% beginning 2016)

Following this regional trend, calls are rife to reduce the 30% corporate income tax rate around the convergence rate. Some questions, however, arise. First, can we afford to lose revenue given that we have been in fact operating on budgetary deficit, which in 2013 was pegged at ₱238 billion? Second, how far more can we stretch government finances given that the post-typhoon Yolanda rehabilitation efforts require at least ₱361 billion?[4] This amount almost eclipses the ₱363 billion the BIR collected from corporate income tax in 2012.[5]

Using the modeling formula devised by the National Tax Research Center wherein for every 1% increase (decrease) in the corporate income tax rate, the corporate income tax revenue will increase (decrease) by 2.55%[6], and using the Bureau of Internal Revenue (BIR) corporate income tax collection for 2012 as base and the GDP growth projection of 6.8% [7], the revenue loss is estimated as follows:

Reduced Rate	Estimated Revenue Loss (Php Billion)
29%	7.37
28%	38.29
27%	69.12
26%	99.94
25%	130.86
24%	161.68
23%	192.50
22%	223.42
21%	254.25

From the point of view of fiscal responsibility, the above revenue loss estimates from a reduction in corporate income tax rate should be viewed with extreme caution. Should Congress race to the bottom in order to make the Philippines an investment destination of choice, it would be prudent to pass countervailing measures that would neutralize the expected revenue loss. This fiscal responsibility would ensure that inclusive growth will not remain elusive to the majority of Filipinos. As Finance Undersecretary Jeremias Paul puts it, a holistic approach could be the key to balance the interests of economy and government.

Such revenue-raising measures could include the fast-tracking of the Fiscal Incentives Rationalization

[2] http://europa.eu/pol/tax/index_en.htm
[3] KMPG International (2013). ASEAN Tax Guide.
[4] Alegado, S.O. (2013). Post-Yolanda rehab to cost P361B over three years, says NEDA. GMA News. Accessed at http://www.gmanetwork.com on March 5, 2014.
[5] BIR Annual Report.
[6] Tibubos, J.P. (2012). Developing Models in Estimating the Revenue Impact of Proposed Reforms on Income Tax. NTRC Tax Research Journal: Vol. XXIV.4 (July-August 2012).
[7] Revenue Memorandum Order No. 4-2014. Bureau of Internal Revenue.

bill and the abolition of the income tax holiday (ITH) and other tax breaks. According to a World Bank study[8], the ITH translates to revenue loss equivalent to 1-percent of the GDP. Using the 2012 GDP of ₱ 10,564.887 billion, we save ₱105.65 million per year with the ITH abolition alone.

The STSRO shares the sentiment that our present tax regime is a stumbling block to regional competitiveness. On the other hand, as we recognize the oft-repeated principle that taxes are the lifeblood of our society, we strongly urge that such opposing interests be addressed by other tax measures that would at least be revenue neutral.

by

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As part of the ASEAN Community, the Philippines is among those who are gearing up for the upcoming regional integration in 2015 or more popularly known as the **ASEAN Economic Community (AEC) 2015.** The AEC 2015 resulted from the adoption of the ASEAN Vision 2020 in December 1997. In essence, the AEC 2015 was seen as the culmination of the economic integration set forth in the ASEAN Vision 2020. To further ensure the success of AEC, the member states adopted the **AEC Blueprint** on 20 November 2007. This Blueprint is designed to "transform ASEAN into a single market and production base, a highly competitive economic region, a region of equitable economic development, and a region fully integrated into the global economy." [9]

Although there is only a year to go before the said integration takes place, it seems that there are still a lot of questions left unanswered insofar as our country's preparedness is concerned. In line with this, there are currently three (3) resolutions pending before the Senate that focuses on the forthcoming ASEAN integration in 2015, to wit:

1. P.S. Res. No. 191 (*Sen. Angara & Sen. Aquino*) – Resolution Directing the Committee on Trade and Commerce to Conduct an Inquiry, in Aid of Legislation, on the ASEAN Economic Community Integration, to Assess Risks and Opportunities for the Filipino Workforce and the Domestic Industries, and to Inform the Public of These Accordingly;

2. P.S. Res. No. 403 (*Sen. Poe*) – Resolution Urging the Senate Committees on Trade and Commerce, Economic Affairs and Foreign Relations to Look Into Approaches and Strategies on how the Philippines can Maximize its Potential with Regard to the Association of Southeast Asian Nations (ASEAN) Economic Integration in 2015, taking into consideration Recent Economic Developments and the Philippine Business Sector that can be More Competitive with the Economic Blueprint's Full Implementation; and

3. P.S. Res. No. 429 (*Sen. Trillanes*) – Resolution Directing the Senate Committee on Trade, Commerce and Entrepreneurship, the Senate

[8] Cited in "DOF mulls 5-yr limit to income tax holidays". The Philippine Star online, October 12, 2013.
[9] Declaration on the ASEAN Economic Community Blueprint, AEC Blueprint (Indonesia: ASEAN Secretariat, 2008).

Committee on Economic Affairs, and Other Relevant Committees of the Senate to Conduct an Inquiry, in Aid of Legislation, on the Preparedness of our Local Industries and Business Sectors and the Government's Industrial Masterplan Governing the Same, in Lieu of the Impending ASEAN Economic Community (AEC) by 2015, with the End in View of Enacting Necessary Policy Measures to Provide Safety Nets Therefor and to Boost the Growth, Competitiveness and Flexibility of Said Sectors.

4. P.S. Res. No. 484 *(Sen. Santiago)* - Resolution Directing the Proper Senate Committee to conduct an inquiry, in Aid of Legislation, on protecting the Filipino labor force for the opening of the ASEAN Labor Market on 2015, considering the reported presence of Illegal Chinese Migrant Workers in the Philippine.

The three resolutions zero in on how the Philippines is preparing for the said regional economic integration. The authors also expressed the following concerns relative to this matter:

- Questions the supposed benefits the country will actually derive out of this economic integration particularly since most of our trade partners are non-ASEAN nations, i.e. Japan, USA, China, Hong Kong, and South Korea;
- Our domestic businesses, manufacturing industry and labor sector are not prepared to compete against other ASEAN nations and the influx of foreign businesses;
- The need to prepare the country's micro, small and medium enterprise sector for the possible effects of this economic integration;
- The need to inform the people about AEC 2015 – what to expect and how to adequately prepare for the same; and
- Enactment of a regulatory legislation before the full implementation of the AEC 2015.

While these resolutions all raised valid points, it is unfortunate that possible taxation concerns were not considered. The envisioned economic integration will undoubtedly raise potential tax issues and as such, reforms in the individual tax policies of these member States must be addressed.

On the taxation aspect, a reading of the AEC Blueprint would reveal that the plans and programs of AEC did not involve a detailed reform tackling possible taxation issues that might arise from the integration of the ASEAN into one community. In fact, the Blueprint only makes mention of taxation in two action statements, to wit:

1. Enhance withholding tax structure, where possible, to promote the broadening of investor base in ASEAN debt issuance (Item 31, Action iv); and
2. Complete the network of bilateral agreements on avoidance of double taxation among all Member Countries by 2010, to the extent possible (Item 58).[10]

However, it can be inferred from the other suggested action plans contained in the Blueprint that necessary reforms must also be had in the tax policies of the member states such as but not limited to the following:

1. The recognition that intellectual property as a major determinant of local value added and external competitiveness (Item 44);
2. A call to harmonize the policy and legal infrastructure for e-commerce (Item 59); and
3. An objective to realize a more comprehensive investment agreement which would increase investor confidence in ASEAN (Item 26) and provide enhanced protection to all investors and investments (Item 27).[11]

Aside from the above, there is also a need to achieve what is referred to as "**harmonization of taxation**[12]". This is when member states in a region agree to adopt the same tax treatment, thus eliminating the incentive for taxpayers to shift from one high-tax jurisdiction to a low-tax jurisdiction.

Although this serves as a good model for regional integration, its downside is that the respective countries must necessarily surrender a part of their sovereignty insofar as it limits their ability to fix their own tax rates.[13] As a consequence of this harmonization, there are other recommended amendments needed to be made in the tax legislation of the member countries insofar as the following types of taxes are concerned:

1. *Corporate Taxes* – given the fast approaching deadline for the integration, member states have steadily worked towards decreasing their corporate income tax rates.

[10] Warrick Cleine and Brahma Sharma. "The ASEAN Economic Community," ASEAN Tax Guide, November 2013: 3. KPMG Asia Pacific Tax Centre. 14 January 2014 < https://www.kpmg.com/Global/en/IssuesAndInsights/ArticlesPublications/Documents/asean-tax-guide-v2.pdf>
[11] Id.
[12] Id.
[13] Id.

As it now stands, the average corporate income tax rate in ASEAN member countries is around 23.1%[14]. It should be noted, however, that the Philippines' own rate at 30% ranks considerably higher than most, and is almost double that of Singapore's 17% corporate income tax rate[15]. Given the current trends, it is predicted that there might be a possible convergence of rates at 20%, except for Singapore whose rate is already lower[16].

2. *Indirect Tax: VAT/GST* – due to the steady decline of corporate income tax rates among member nations, the tendency of some member states is to push the rates of indirect taxes up so as to make up for lost revenues. The global trend being seen is that indirect taxes have increased by 0.17% to a 15.5% average since January 2012[17]. However, in Asia, the average rates moved by 0.4% to 12.24%[18].

3. *Withholding Tax & Double Tax* – as earlier pointed out, the Blueprint expressly emphasized the need to fast track the completion of double taxation treaties among the different member nations. Although the 2010 deadline has long passed, there is still a long way to go before the entire region complies with this treaty requirement. In fact, Cambodia has yet to enforce a treaty of this nature up to this time[19]. Aside from the issue of tariffs and duties, free flow of trade and capital also requires the elimination of withholding taxes[20]. It should be pointed out that withholding taxes within the region are considerably higher than the withholding taxes found in bilateral agreements with nations outside of ASEAN, thus giving an advantage to external trade rather than boosting trade within the region.

4. *Customs* – the aim is to reduce and eventually remove all forms of customs tariffs and duties in preparation for the ASEAN integration. This is a necessary consequence given that one of the proclaimed pillars of the AEC is the free flow of goods or freedom of trade[21]. As per the Blueprint, the plan is to remove all import duties by 2015 for all the member States. At present, tariffs are down to zero on 99.65% of the traded lines for the ASEAN-6 (Brunei, Indonesia, Malaysia, Philippines, Singapore, and Thailand), and range from 0 to 5% on 98.86% of lines for CLMV (Cambodia, Laos, Myanmar, and Vietnam).

With only a year left before the projected economic integration of the region, there are still a lot of tax concerns that have to be addressed in order to ensure a smooth transition among the different member States. The tax legislation of these countries must be adjusted in order to accommodate the changes laid down in the AEC Blueprint. Unfortunately, doing so will prove to be difficult considering the glaring disparities existing among the countries concerned. And these changes are not only in terms of economic conditions, but there are also political and ethnical factors that have to be evaluated.

As for the Philippines, the most significant achievement in terms of AEC has been the creation of the National Single Window (NSW) in 2005. Sadly, the inability of the Bureau of Customs (BoC) to fully implement the NSW has also been pointed out as one of the reasons why our customs service is still perceived as the "most inefficient, corrupt, and costly (by middle-income country standards)" in East Asia[22]. Aside from this, other problems identified in the Philippines' AEC Scorecard that will hinder the country from achieving regional goals are as follows:

1. Inadequate government policies to facilitate free flow of investments and freer flow of capital;

2. Lack of an effective competition policy that is aligned with regional guidelines;

3. The need for better policies to protect intellectual property rights;

4. The need to improve tax regulation policies;

5. The need to strengthen small-medium enterprises (SMEs) to make it at par with the best practices in East Asia;

6. No strategy for external economic relations;

7. Low investments in infrastructure;

8. Lack of political will;

9. High transaction costs; and,

10. Lack of coherent industrial policy[23].

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14 Id. at 4.
15 Id.
16 Id.
17 Id. citing "Corporate and Indirect Tax Survey 2012," KPMG International, January 2013 at p. 2.
18 Id.
19 Id. at 5.
20 Id.
21 Id
22 Jenny Balboa, Fatima Lourdes Del Prado & Josef Yap, "Achieving the AEC 2015: Challenges for the Philippines", in *Achieving the ASEAN Economic Community 2015*, ed. Sanchita Basu Das (Singapore: ISEAS Publishing, 2012), at 113. For the executive summary of this book, please refer to ***Annex D***.
23 *Id.* at 113-118.

In the other areas of taxation, the country still has a long way to go especially in terms of lowering our very high corporate income tax rate. Moreover, another matter that should be looked into are the business taxes being imposed by the government that undeniably increase the cost of doing business in the country. Putting these two problem areas together definitely puts our country in a disadvantageous position in terms of attracting new investors.

As for the trend of hiking up the rates of indirect taxes such as VAT, it is submitted that this might prove to be a more tumultuous task considering the expected opposition that this will surely generate from the various sectors of our economy and in general. It is hoped that the government will look into other areas of possible revenue generation instead of increasing the existing VAT rates. In fact, there are currently two pending bills before the Senate Committee on Ways and Means proposing the reduction of the VAT rate, to wit:

- **SBN 461** (*Sen. Recto*) – An Act Increasing The Threshold For Certain Non-Vat Taxpayers, Amending For The Purpose Sections 109 And 236 Of The National Internal Revenue Code Of 1997, As Amended; and,

- **SBN 462** (*Sen. Recto*) – An Act Authorizing The President Of The Philippines To Lower The Rate Of Value Added Tax To Ten Percent (10%), Amending For The Purpose Sections 106 (A), 107 (A), And 108 (A) Of The National Internal Revenue Code Of 1997, As Amended By Republic Act (R.A.) No. 9337.

Without necessarily surrendering our need to raise possible tax revenues, it is imperative that our current tax policies be assessed in light of the impending AEC 2015. Necessary policy changes must be made not only to ensure our smooth transition into AEC but also to enable the government to maximize the benefits envisioned by this regional integration.

SENATE INITIATIVES ON ASEAN 2015

by

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Preparatory to the ASEAN Integration, Senator Sonny M. Angara felt the need to introduce SB No. 2149 and SB No. 2163, twin measures that aim to reduce the rates of individual income tax and corporate income tax. These measures are in line with the Philippine commitment to the 10-member ASEAN Economic Community (AEC) Blueprint which seeks to transform ASEAN into a single market and production base by 2015. While member countries are not mandated to amend their income tax schedules, Senator Angara noted that it is highly expected that financial and human capital would flow to where these could earn best.

SBN 2149 (Individual Income Tax)

Taxable Income	Beginning January 1, 2015	Beginning January 1, 2016	Beginning January 1, 2017
P20,000 but not over P70,000	15%	13%	10%
Over P70,000 but not over P200,000	P10,500 + 20% of the excess over P70,000	P9,100 + 18% of the excess over P70,000	P7,000 + 15% of the excess over P70,000
Over P200,000 but not over P1,000,000	P111,500 + 30% of the excess over P500,000	P101,500 + 25% of the excess over P500,000	P86,500 + 22% of the excess over P500,000
Over P1,000,000	P261,500 + 32% of the excess over P1,000,000	P226,500 + 28% of the excess over P1,000,000	P196,500 + 25% of the excess over P1,000,000

SBN 2163 (Corporate Income Tax)

From	To (Beginning January 1)		
	2015	2016	2017
32%	29%	27%	25%

In the same vein, several Senate Resolutions were filed directing appropriate Senate Committees to conduct inquiries in aid of legislation on the effects of the ASEAN Economic Community on the various dimensions of Philippine development. These Resolutions are:

SRN 191 by Senator Sonny M. Angara & Sen. Paolo Benigno “Bam” Aquino IV
SRN 403 by Senator Grace L. Poe
SRN 429 by Senator Antonio “Sonny” F. Trillanes IV
SRN 484 by Senator Miriam Defensor Santiago

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