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Tax Reforms toward Fiscal Consolidation

Policy Options for the Government of the Philippines

Norio Usui

Asian Development Bank

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This note is prepared by Norio Usui, senior country economist, Philippines Country Office (PhCO), to elicit discussion and comments. The original paper was prepared in July 2010 as a PhCO policy note when the new administration came in. The findings, interpretations, and views expressed are entirely those of the author, and do not necessarily represent the views of the Asian Development Bank, its executive directors, or the countries they represent. Questions and comments can be addressed to the author (nusui@adb.org).

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Contents

Tables and Figures

Tables

Figures

Abbreviations

ADB	–	Asian Development Bank
CIT	–	corporate income tax
VAT	–	value-added tax
PIT	–	personal income tax
GDP	–	gross domestic product
BIR	–	Bureau of Internal Revenue
BOC	–	Bureau of Customs
RATS	–	Run after the Smugglers
RATE	–	Run after Tax Evaders

Summary

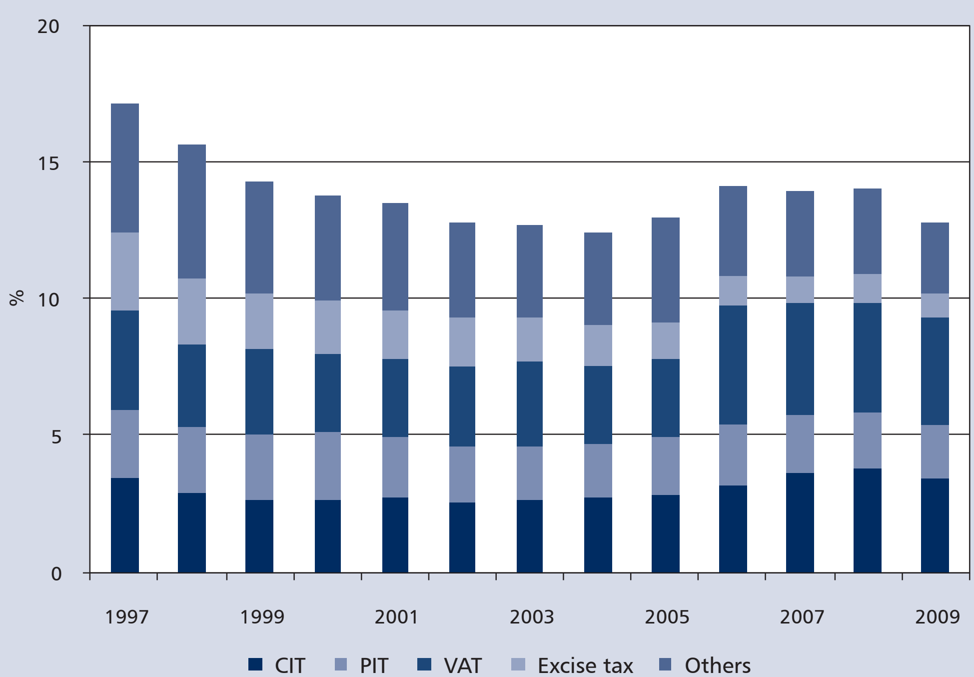
Over the decades, the Philippines has suffered from persistent fiscal imbalances, resulting in the consistently low delivery of basic public services such as infrastructure, education, and health. The gains of the 2005 tax reform were not sustained and the country once again faces difficult fiscal conditions. Two contrasting approaches to increasing the tax revenue have surfaced: one focuses on tax rate adjustments and the other on tax administration. This policy note assesses the two options in terms of their efficiency in mobilizing revenue and their impacts on tax equity or fairness. Key findings are as follows: (i) Given the relatively high dependence on indirect taxes, the policy mix of a higher value-added tax rate and a lower corporate income tax rate will make the overall tax system more regressive, even if its impact on tax revenue is neutral; (ii) The country's tax productivity is extremely low compared to that of the other countries in the Asia and Pacific region, which signals the presence of significant tax loopholes and weak tax administration; and (iii) There is ample room to increase excise taxes on tobacco, alcoholic products, and gasoline, without ruining the equity of the tax system. These results suggest that tax administration remains a key focus of efforts to mobilize revenue in the new administration. Enforcing anti-tax evasion campaigns, converting tax collection authorities to semiautonomous agencies, preparing a clear and updated tax database, and developing the capacity of tax officers are prioritized.

Where Are We?

Fiscal consolidation progressed well in the Philippines during the past 5 years before the global financial crisis in 2008. Fiscal deficits, as a percent of gross domestic product (GDP), declined from 5.3% in 2002 to 0.2% in 2007, and the national government's debt was down from 72.5% of GDP to 55.8% over the same period. The improved fiscal position gave room for the stimulus package, amounting 4.8% of GDP, for spending on infrastructure and social protection to mitigate the impacts of the crisis in 2008. The latest economic indicators show a rapid recovery of the economy due to the strong rebound in exports and accelerated growth in private consumption backed with surging remittance inflows.

Fiscal pressure, however, has been growing since 2009. While the stimulus spending and post-calamity restructuring cost contribute to the larger deficit, an aggravating factor is the country's weak capacity to mobilize revenue. The combination of accelerated spending and weak revenue collection drove the fiscal deficit to 3.9% of GDP, and the debt-to-GDP ratio to 57.3% in 2009. Tax revenues were eroded to 12.8% of GDP in 2009, the lowest since the 2005/2006 tax reforms in the country as well as in the neighboring countries (Figures 1 and 2). While the falling revenues can be partially traced to the economic slowdown and erosion in the tax base due to tax-reducing

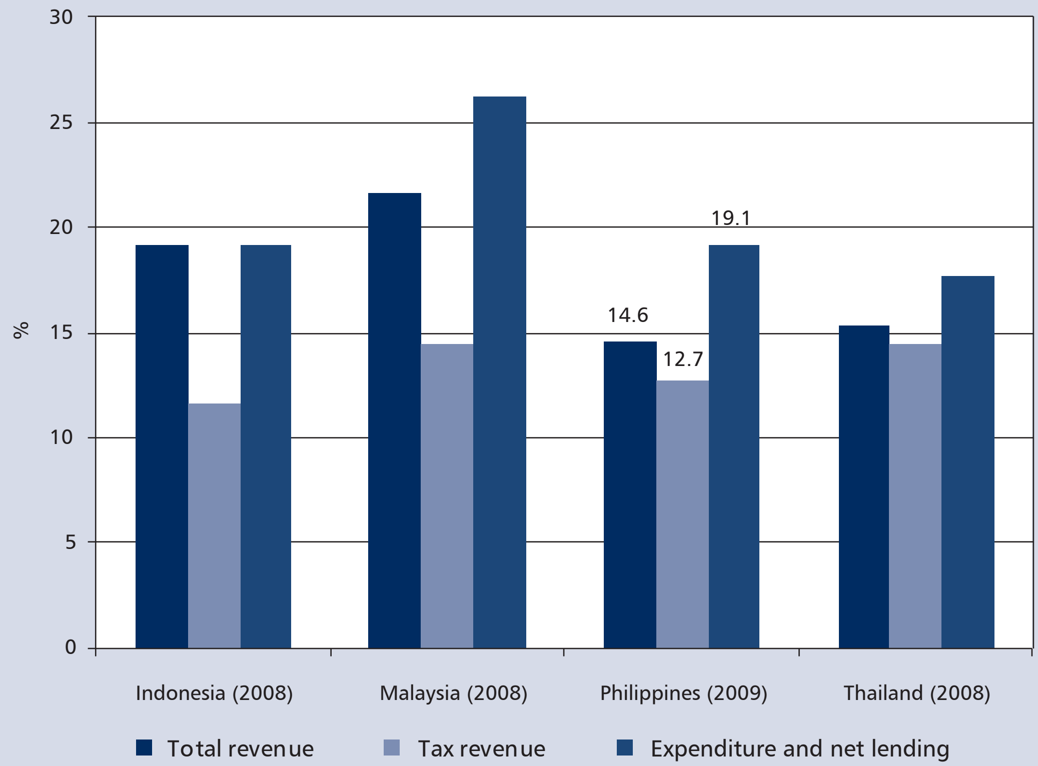
Figure 1 **Philippines: Tax Revenue Trends** (% of GDP)



CIT = corporate income tax, GDP = gross domestic product, PIT = personal income tax, VAT = value-added tax.

Source: International Monetary Fund Article IV consultation reports.

Figure 2 **ASEAN 4: Revenue and Expenditure** (% of GDP)



ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product.

Source: World Bank, World Development Indicators.

measures implemented in 2009, the overwhelming consensus is that the country's tax system has several structural weaknesses.

The country suffered from persistent fiscal imbalances for the past 3 decades. The limited fiscal space has led to the consistently low delivery of public services. Historically, the country's public spending on infrastructure, education, and health, has been underfunded relative to its neighboring countries, both as a percentage of GDP and as percentage of total public expenditure (Figures 3 and 4). Several business surveys and growth diagnostic studies identify the deteriorating infrastructure as one of the key binding constraints to the country's economic growth.[1] Underinvestment in the social sector has also prevented the country from addressing the relatively high inequalities and increasing poverty.

In the short term, the authorities need to find a right balance between the fiscal stimulus to ascertain economic recovery, and medium-term fiscal consolidation. However, with the strong economic recovery in the first half of 2010, the government is expected to prioritize fiscal consolidation. For the new administration, given the long-standing low delivery of public services, the only option is to increase tax revenues to reverse the compression of public expenditures for basic public services.

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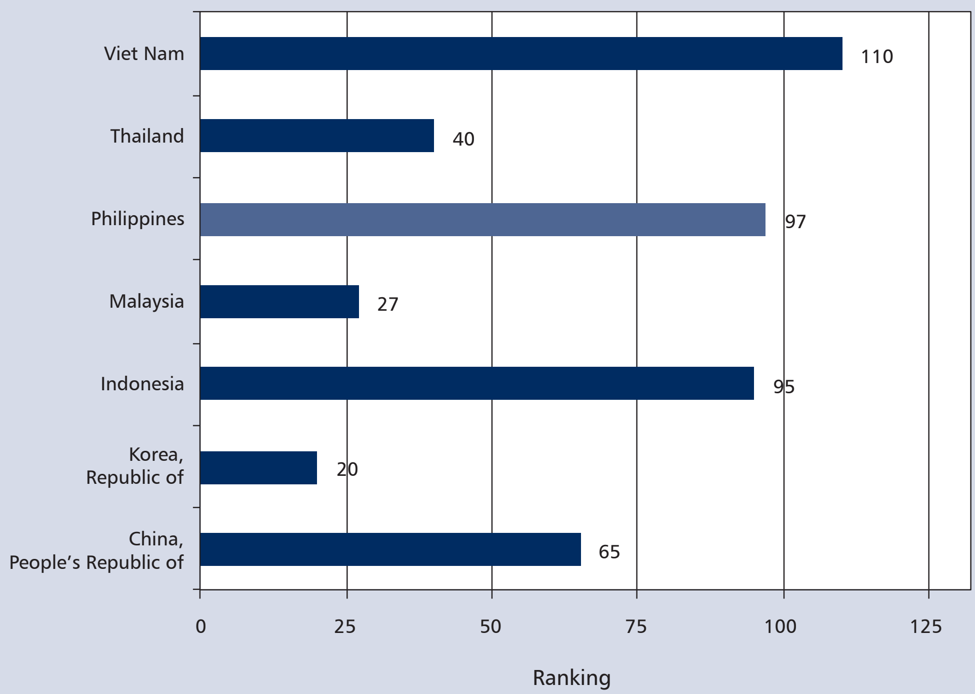
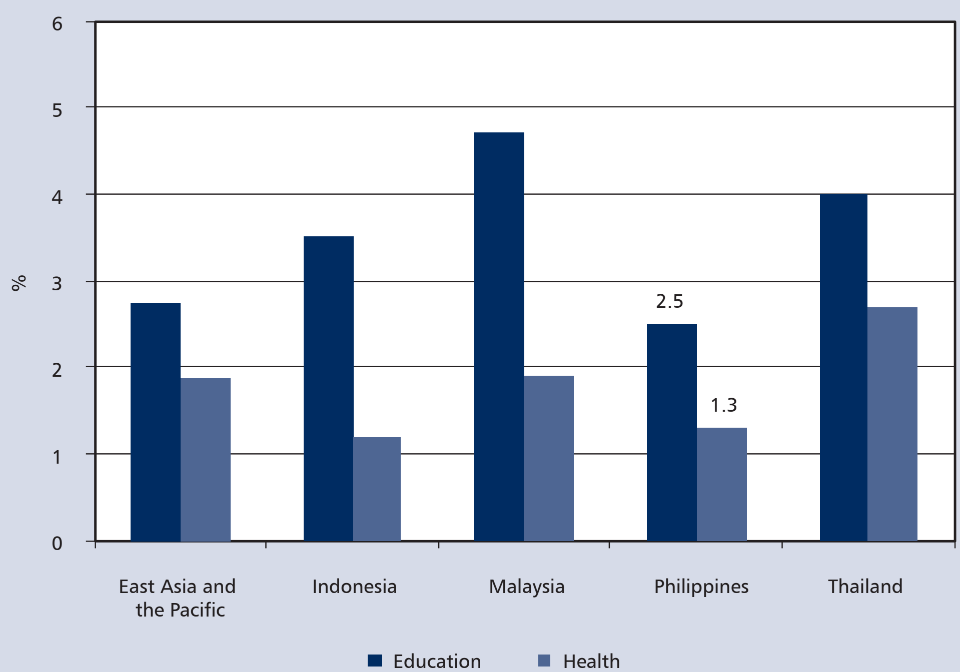
[1] For example, Asian Development Bank (ADB). 2007. *Philippines: Critical Development Constraints.* Manila: ADB, and Bocchi, M. A. 2008. Rising Growth, Declining Investment: The Puzzle of the Philippines. *Policy Research Working Paper* No. 4472. Washington, DC: World Bank.

Figure 3 **Infrastructure Quality Index** (ranking among 132 countries)



Source: Global Innovation Index Report 2009–2010.

Figure 4 **Public Spending on Education and Health** (2007, % of GDP)



GDP = gross domestic product.

Source: World Bank, World Development Indicators.

Two Policy Options

The Government of the Philippines had two views on how to increase its tax revenues.[2] One focuses on adjusting tax rates, and the other on implementing tax administration measures without changing tax rates.

(i) **Option 1: Tax rate adjustments.** This option proposes changes in tax rates in value-added tax (VAT), corporate income tax (CIT), and excise taxes on tobacco, alcoholic products, and gasoline and diesel. Proposed changes are: (a) increasing VAT rate from 12% to 15%; (b) cutting CIT rate from 30% to 25% (or 20%); and (c) increasing excise tax rates for tobacco and alcoholic products (through the implementation of RA 9334[3]) and excise tax on gasoline and diesel. Supporters of option 1, at the same time, acknowledge the importance of better tax administration.

(ii) **Option 2: Tax administration measures.** Key measures proposed under this option include (a) intensifying efforts for better compliance and stronger enforcement by the tax authorities, the Bureau of Internal Revenue (BIR) and Bureau of Customs (BOC); and (b) rationalizing tax incentive schemes. This option is based on the view that the eroding tax revenue is caused by the country's weak tax administration. Supporters of this option take the view that better tax administration can produce adequate revenues without raising tax rates.

This note reviews the country's current tax system and assesses these options in terms of their efficiency to mobilize revenue and their impacts on tax equity or fairness.

[2] This note was prepared in July 2010 when the new administration came in. At that time, there were the two different views to increase tax revenues within the government circle.

[3] Government of the Philippines. 2004. Republic Act 9334: An Act Increasing the Excise Tax Rates Imposed on Alcohol and Tobacco Products, Amending for the Purpose Sections 131, 141, 142, 143, 144, 145 and 288 of the National Internal Revenue Code of 1997, as Amended. 21 December. www.lawphil.net/statutes/repacts/ra2004/ra_9334_2004.html

The Current Tax System and Its Problems

In the Philippines, VAT, CIT, and personal income tax (PIT), make up over two thirds of total tax revenues. Although the statutory tax rates applied in the country are higher than those of its neighboring countries, the revenues generated as a share of GDP are not proportionally higher compared to those of its neighboring countries. Although the share of indirect taxes (VAT, excise taxes, customs duties, etc.) has been decreasing, indirect taxes still account for 58% of total tax revenues in 2009. This suggests that the country's overall tax system is relatively regressive compared to that in the other countries in the Asia and Pacific region. In theory, fairness of a tax system must be checked in the context of the progressivity of public spending. Even if revenues are raised in a regressive manner, the overall impacts of the tax system can be progressive if the authorities spend its resources more for the poor. However, given the limited spending on education and health and weak targeting of poverty programs[4] in the Philippines, the country's tax system cannot be progressive even after taking into account the expenditure pattern. The fiscal system has not helped distribute income more equitably.[5]

Several business surveys show that a high tax rate is one of the barriers to doing business in the country. However, the current CIT rate of 30%, having dropped from the previous 35% in 2009, is comparable with the rate of the neighboring countries (Table 1).[6] PIT rates, both the maximum (34%) and the minimum (5%), are also comparable with those of the other countries. In the Philippines, the VAT was introduced in 1998 with a single rate (10%) and a reasonable exemption threshold. The VAT base was then broadened to cover services in 2004 and petroleum products and electricity in 2005. With the VAT reform in 2005 (RA 9337,[7] known as the reformed VAT law), the VAT rate was increased to 12%, the highest in the Asia and Pacific region. With the rate increase, the VAT-to-GDP ratio rose from 1.65% in 2004 to 2.18% in 2007.

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4 Poor targeting in poverty programs leads to significant leakages and waste of resources on the non-poor. For example, Manasan, R. G. 2009. Reforming Social Protection Policy: Responding to the Global Financial Crisis and Beyond. *Discussion Paper Series* 2009-22. Manila: Philippine Institute for Development Studies, estimates that the leakage rate of the National Food Agency (NFA) rice subsidy program, which accounted for 29% and 69% of total government spending on social protection in 2007 and 2008, respectively, could reach as high as 71%.

5 The heavy reliance on indirect taxes, which are inherently regressive, and the limited income redistribution effect of the country's fiscal system are chronic problems of the country's fiscal system. Tan, E. A. 1975. Taxation, Government Spending and Income Distribution in the Philippines. *ILO Working Paper*. Geneva: International Labour Organization.

6 In the 2005 tax reform, the CIT rate was increased from 32% to 35% as a temporary measure (from November 2005 to the end of 2008) to raise tax revenues. While it is sometimes argued that a lower CIT rate can stimulate domestic investment and improve international competitiveness, it is not necessarily clear that a lower rate can induce more investment in the country. At least, the current 30% is comparable with those of the neighboring countries.

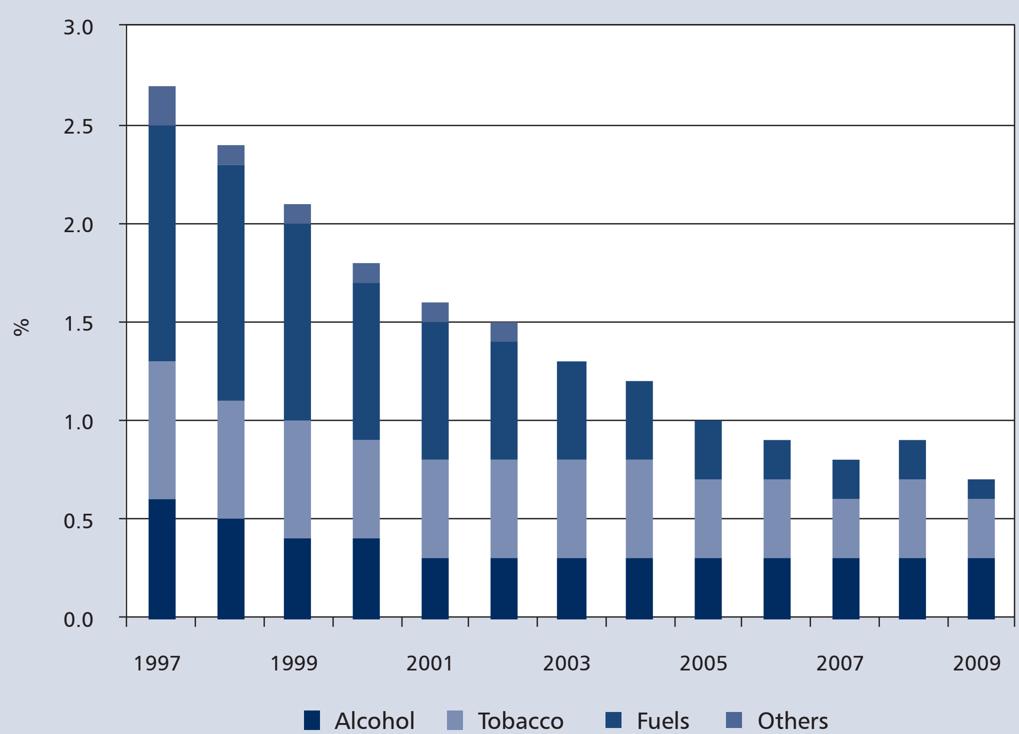
7 Government of the Philippines. 2005. Republic Act 9337: An Act Amending Sections 27, 28, 34, 106, 107, 108, 109, 110, 111, 112, 113, 114, 116, 117, 119, 121, 148, 151, 236, 237 and 288 of the National Internal Revenue Code of 1997, as Amended, and for Other Purposes. 24 May. www.lawphil.net/statutes/repacts/ra2005/ra_9337_2005.html

Table 1 **Tax Rates in Selected Countries**

Tax rate (%)	VAT	CIT	PIT Max.	PIT Min.
East Asia and the Pacific (2006)	10.7	27.6	29.4	9.4
PRC (2006)	17.0	33.0	35.0	5.0
Republic of Korea (2007)	10.0	27.5	35.0	8.0
Indonesia (2007)	10.0	30.0	35.0	5.0
Malaysia (2006)	10.0	27.0	27.0	1.0
Philippines (2009)	**12.0**	**30.0**	**34.0**	**5.0**
Thailand (2007)	7.0	30.0	37.0	10.0
Viet Nam (2007)	10.0	28.0	40.0	10.0

CIT = corporate income tax, PIT = personal income tax, PRC = People's Republic of China, VAT = value-added tax.
Source: World Bank, World Development Indicators.

Figure 5 **Philippines: Excise Tax Revenues** (% of GDP)



Source: International Monetary Fund, Article IV consultation reports.

Excise taxes are levied on tobacco, alcoholic products, and petroleum products. Currently, a grave concern is the dramatic decline of the excise taxes. From 1997 to 2009, excise taxes as a share of GDP decreased by 1.8 percentage points (Figure 5). In 1996, the authorities shifted the excise tax from an ad-valorem to a complicated multitiered unit tax rate, and did not allow for inflation adjustment. The authorities, with the RA 9334 approved in 2004, planned discrete increases in the tax rate on tobacco and alcoholic products beginning 2005 and every other

Table 2 **Philippines: Excise Taxes on Petroleum Products** (Peso/liter)

Item	Before the 2005 reform	After the 2005 reform
Gasoline (regular)	4.80	4.35
Kerosene	0.60	0.00
Diesel	1.63	0.00
Bunker fuel	0.30	0.00

Source: The Philippine Government.

year until 2011.[8] The reformed VAT law in 2005 incorporated a number of mitigating measures, including reducing the selected petroleum excises (Table 2) and import tariff of petroleum products from 5% to 3%.

Currently, three different taxes are levied on gasoline: excise tax of P4.35/liter (fixed in nominal term in 1996), import tariff of 3%, and VAT of 12%. While excise taxes were levied on diesel and bunker oil before the 2005 VAT reform, they were excluded from the excise tax to mitigate the impacts of the higher VAT rate on public transportation cost. The excise tax-to-GDP ratio went down from 0.37% in 2004 to 0.15% in 2007. More than half of this drop is attributable to the decrease in excise taxes on petroleum products.

Overall, the country's tax productivities, or revenue efforts, of these major taxes are significantly lower compared to those of the other countries in the region (Figure 6). Tax productivity is a conventional index to measure how effectively the tax system produces revenues.[9] The country's tax productivities, in particular VAT (0.18) and CIT (0.11), are far below the region's averages (average in East Asia and the Pacific is 0.49 for VAT and 0.20 for CIT). The productivity of PIT (0.06) is also lower than the region's average (0.16), while it is comparable with neighboring countries. The low productivities of major taxes signal the presence of significant tax loopholes and weak tax administration in the country.

The CIT is complex and characterized by a variety of tax incentives for investment, export, job creation, and regional development. Investment promotion agencies[10] have provided a wide range of incentives for registered firms such as income tax holidays, exemptions from VAT and import duties, and deduction of wage bills from taxable income. However, some studies, including a technical assistance from ADB,[11] find that tax incentives are redundant for over 50% of firms, meaning that those firms that were granted the tax incentives would have invested irrespective of receiving the tax incentives. The government's revenue loss from redundant incentives was estimated to be as large as 1% of GDP, providing a windfall gain to receiving firms.[12] The authorities thus need to examine how the current tax incentive schemes can be consolidated.

Erosion of the VAT base is serious. In the past tax reforms, authorities have always broadened the VAT base by increasing its coverage. However, several policy measures reversed the initial

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8 Under the amendment, the tax rates will be higher than those in 2003 for tobacco (34%–143% higher) and alcoholic products (22% higher). For details on the excise tax rates, see BIR website: www.bir.gov.ph/lumangweb/tax_excise.html

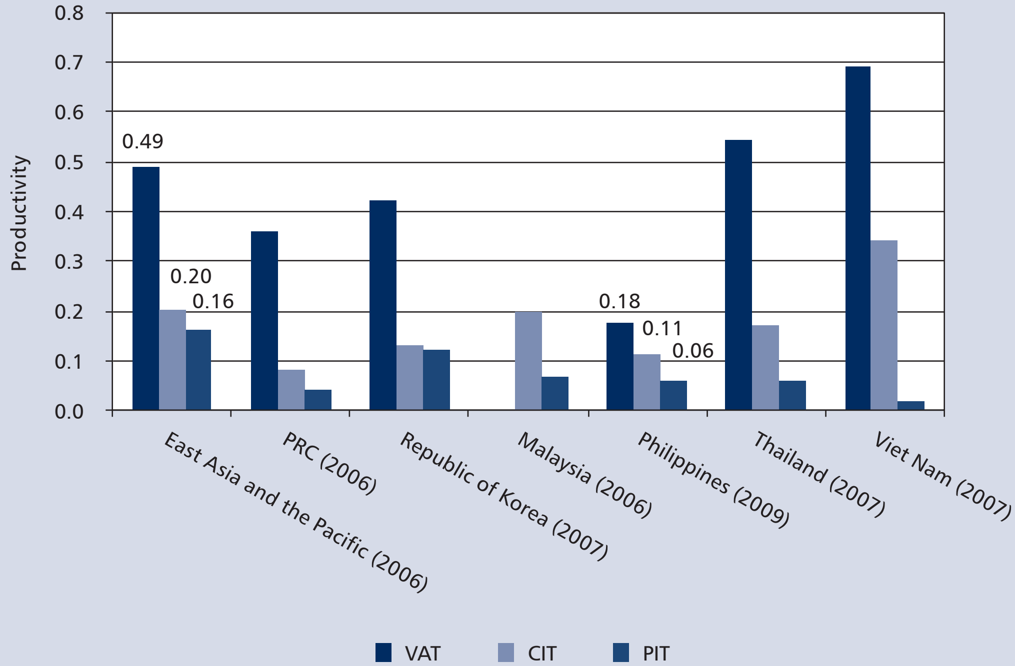
9 For each tax, the productivity is measured as the ratio of the tax revenues to GDP divided by the standard tax rate, i.e., (tax revenue/GDP)/(tax rate). It can thus be regarded as a ratio of actual tax revenue to the hypothetical tax revenue (GDP*tax rate), which reflects the extent to which the revenue-generating capacity of a country has been exploited by the government.

10 These include the Board of Investments, Philippines Economic Zone Authority, Base Conversion and Development Authority, and Subic Bay Metropolitan Area.

11 ADB. 2010. *Technical Assistance to the Philippines for Strengthening Investment Climate and Competitiveness*. Manila.

12 Reside, R. E. 2006. Towards Rational Fiscal Incentives (Good Investments or Wasted Gifts?). *Economic Policy Reform Advocacy Fiscal Sector Report.* No. 1. United States Agency for International Development.

Figure 6 **Tax Productivities in Selected Countries**



CIT = corporate income tax, PIT = personal income tax, PRC = People's Republic of China, VAT = value-added tax.

Source: Author's calculation.

broadening of the base. In 2009, for example, the VAT on electricity transmission was replaced with a lower-yielding franchise tax to reduce the domestic price of electricity, and senior citizens' spending on medical goods and services was excluded from the VAT base (Table 3).

Compliance with the PIT has been low and thus its progressivity has been falling over the years (Figure 7). The relative share of tax paid in total spending of relatively high-income households has been declining compared to that of lower-income households. The bulk of the problem arises with poor tax administration, particularly for self-employed professionals. Although a bill on the simplified net income taxation scheme was approved to increase tax collections from self-employed professionals in 2008, the tax authorities' capacity in detecting and enforcing tax liabilities is limited.

The country's overall capacity for tax administration is low. The Philippines has the lowest ratio of tax staff to overall population (0.13) in the region (0.49), and the highest ratio of taxpayers (609) per tax staff in the region (579).[13] Although the indexes suggest that the country's tax authorities work in a relatively efficient manner, they also imply lack of tax mobilization efforts by authorities. In 2004, the government offered the tax administrators a system of rewards and punishments, depending on whether they exceed their annual revenue targets or fail to meet them (RA 9335[14]). However, the tax authorities continued to fail to meet the targets in the following years, and no concrete actions were taken for tax officials who failed to meet the targets.

[13] These mean that the country has only 0.13 tax staff member for every 1,000 population, and 1 tax staff member serves 609 taxpayers.

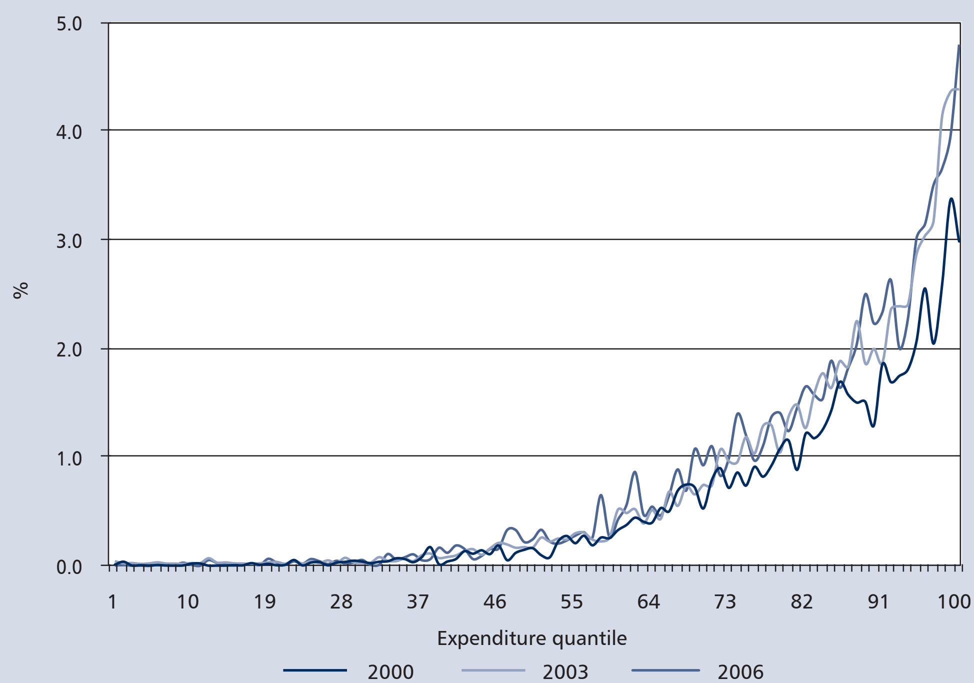
[14] Government of the Philippines. 2005. Republic Act 9335: An Act to Improve the Revenue Collection Performance of the Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC) through the Creation of a Rewards and Incentives Fund and of a Revenue Performance Evaluation Board and for Other Purposes. 25 January. www.lawphil.net/statutes/repacts/ra2005/ra_9335_2005.html

Table 3 Negative Revenue Impact Laws

Law	Year	After the 2005 reform
RA9337	2005	Corporate Income Tax Reduction
RA9504	2008	Individual Income Tax Relief
RA9505	2008	Personal Equity and Retirement Account
RA9511	2008	Imposition of Franchise Tax on Power Transmission in lieu of all taxes
RA9593	2009	Tourism Incentives
RA9648	2009	Abolition of Documentary Stamp Tax (DST) on Secondary Trading of Stocks
RA9679	2009	Incentives under the Home Development Mutual Fund Charter
RA9728	2009	Bataan Freeport
RA9856	2009	Real Estate Investment Trust Incentives
RA9994	2010	VAT Exemptions of Selected Goods and Services Purchased by Senior Citizens
RA9999	2010	Tax Deductibility of Actual Free Legal Services Rendered by the Poor
RA10001	2010	Restructuring of DST on Life Insurance Policies and Reduction of Premium Tax on Life Insurance Policies from 5% to 2%
RA10020	2010	Migrant Workers and Overseas Filipino Act (Abolition of DST on OFW Remittances)
RA10026	2010	Income Tax Exemption and Condonation of Unpaid Taxes for Local Water Districts
RA10083	2010	Creation of Special Economic and Freeport Zone in Aurora

Source: Manasan, R. G. 2010. Financing the MDGs and Inclusive Growth in the Time of Fiscal Consolidation. *Discussion Paper Series* 2010-34. Manila: Philippine Institute for Development Studies.

Figure 7 Progressivity of Personal Income Tax
(tax paid as a share of total household expenditure by expenditure quantile, %)



Source: Author's calculation based on Family Income and Expenditure Survey 2000, 2003, and 2006.

Assessment of the Two Options

Our calculation, based on assumptions (Table 4), shows that if the authorities raise the VAT rate to 15% and cut the CIT rate to 25% with the current tax productivities, its overall impact on the tax revenue-to-GDP ratio is neutral (scenario 1 in Figure 8). However, if the CIT rate is cut further to 20%, the total tax revenue-to-GDP ratio decreases by 0.6 percentage points (scenario 2). Without making a serious effort to mobilize taxes, this option thus cannot create adequate fiscal space for higher public spending on basic public services. On the other hand, our results show that the country can dramatically improve the tax-to-GDP ratio by increasing tax productivities for VAT, CIT, and PIT. If the authorities can raise the tax productivity of these taxes to 70% of the regional averages, the tax-to-GDP ratio increases by 4.6 percentage point (option 2).

Although our estimate does not include the possible impacts of tax rate changes in excise taxes, there is ample room to increase excise taxes. The authorities need to implement the planned upward revisions of tax rates on tobacco and alcoholic products with indexation to price changes. Although these taxes can be regressive due to higher spending by the poorer households, they have a significant positive externality effect on public health. In addition, we think it reasonable to charge a higher excise tax on gasoline, given the country's low taxation on gasoline by international standards.[15] This tax has several merits:

(i) it is relatively easier to administer;
(ii) highly progressive (since the richer households spend more on gasoline) to offset the regressive effect of the higher taxation on tobacco and alcoholic products (Figure 9); and
(iii) impacts on negative externalities of gasoline consumption (will potentially reduce traffic congestion, accidents, pollution, etc.).

Possible impacts on the poor can be reduced by limiting increases in kerosene and liquefied petroleum gas.

Our assessment suggests that given the relatively high regressivity of the overall tax system, the best policy option for the new administration is to improve tax administration and rationalize taxes without changing major tax rates, and charge higher excise taxes on tobacco, alcoholic products, and gasoline with inflation adjustment.

[15] World Bank. 2010. *Philippine Quarterly Update: Laying Out the Exit Strategy*. Washington, DC: World Bank.

Table 4 **Policy Options: Assumptions**

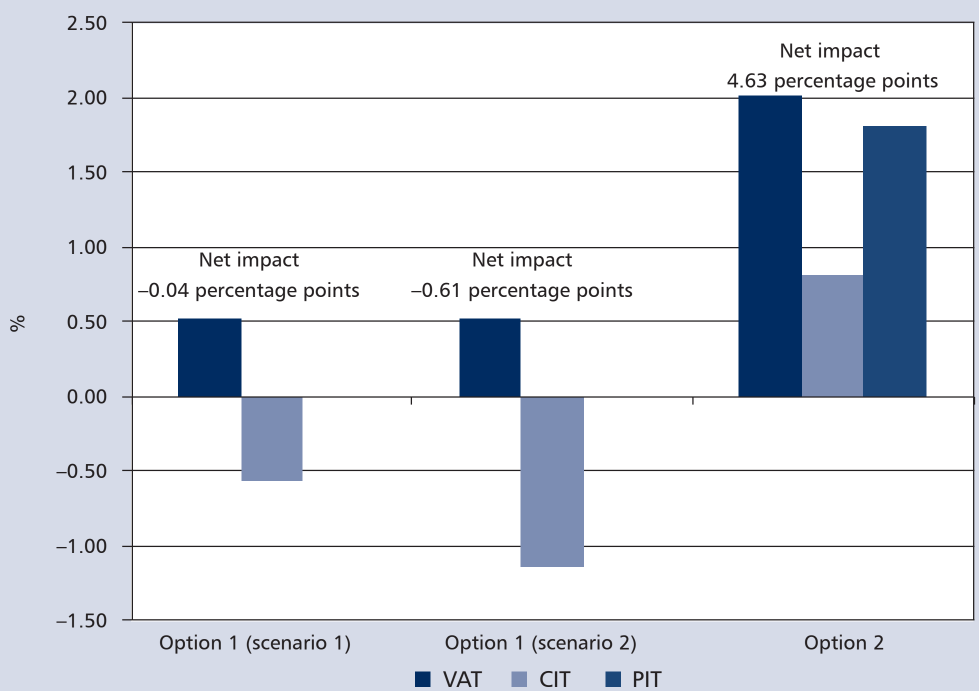
Item	2009 (baseline)	Option 1 Scenario 1	Option 1 Scenario 2	Option 2
Tax rates (%)				
VAT	12	15		12
CIT	30	25	20	30
PIT	34–5	34–5		34–5
Tax productivity				
VAT	0.18	0.18		0.34[a]
CIT	0.11	0.11		0.14[a]
PIT	0.06	0.06		0.11[a]

CIT = corporate income tax, PIT = personal income tax, VAT = value-added tax.

[a] Seventy percent of the average of East Asia and the Pacific.

Source: Author.

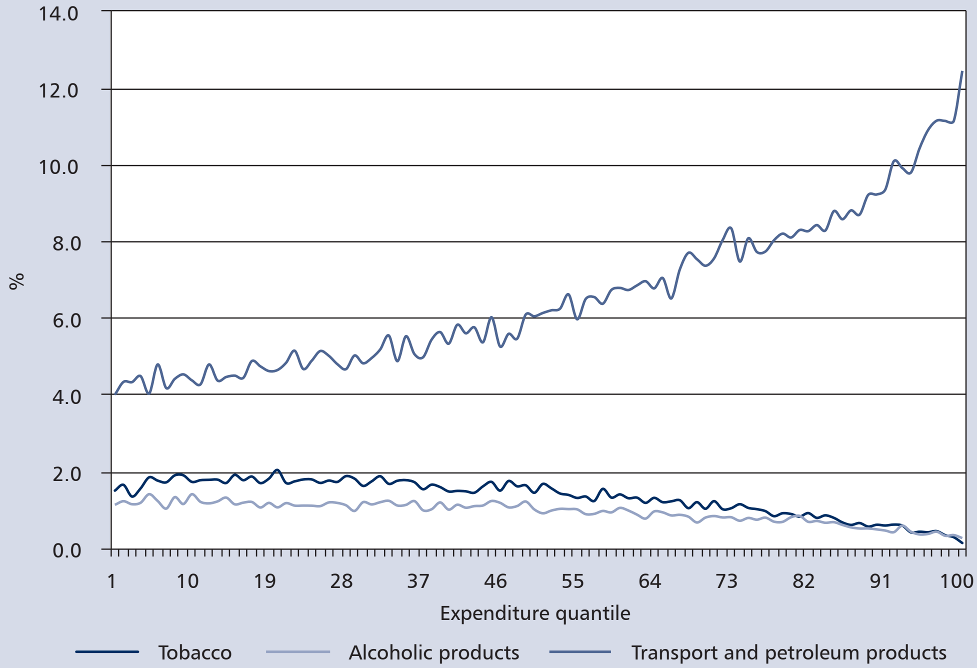
Figure 8 **Estimated Impacts on Revenues** (percentage point of GDP)



CIT = corporate income tax, GDP = gross domestic product, PIT = personal income tax, VAT = value-added tax.

Source: Author's calculation.

Figure 9 **Equity Impacts of Excise Taxes**
(% of total household expenditure by expenditure quantile)



Source: Author's calculation based on Family Income and Expenditure Survey 2000, 2003, and 2006.

Tax Administration Reforms

The general guiding principles of tax administration reforms are that they (i) reduce the complexity of the tax system, (ii) encourage taxpayers' voluntary compliance, (iii) differentiate taxpayers by their revenue potential (or large taxpayers' services), and (iv) effectively manage reforms.[16] The authorities have taken concrete measures in these areas to improve tax administration. The BIR focuses on registration, audit, and collection, and the BOC on smuggling. Actions taken by the BIR include consolidating data with local government units to identify nonregistrants and suspected tax evaders, tightening controls over tax exemption removals, intensifying audit of taxpayers, and implementing the Run after Tax Evaders (RATE) Program. The BOC conducts media campaigns to avoid collusion between customs officials and importers through the Run after the Smugglers (RATS) Program.

Major development partners have set tax administration reforms as one of key priorities in their operations and have provided significant support for decades.[17] All reform options have been shown to past authorities through several projects and programs, but the expected results have not been achieved. A key problem was not the interventions themselves, but inadequate implementation of the agreed reforms. A top priority for the new administration is thus to review all past reform initiatives and to identify the root causes of the inadequate implementation. The assessment needs to include political economy factors such as internal resistance within the tax authorities, and lobbying activities against the reforms.

The new administration can focus on evaluating the Lateral Attrition Law (RA 9335) approved in 2005. The law intends to create semi-autonomous revenue authorities to address chronic problems in tax administration—rigid civil services, corruption, and low voluntary compliance.[18] It allows the BIR and BOC to create a reward and incentive fund, equal to at least 15% of the difference between the actual tax collection and revenue targets, for higher remuneration for officials, contingent on their collection performance. The law grants autonomy for human resource management of the BIR and BOC to recruit competent personnel with competitive salary. It also enables the authorities to dismiss corrupt officials and those who fall short of the collection targets.[19] The new administration needs to strengthen the implementation of this initiative.

Another area to be focused on is the BIR's registration database. The weak coverage of the taxable population renders tax processes such as audit, collection, and enforcement ineffective in the country. The BIR can expand the database further by using available information from various government agencies and private organizations. A clean and updated database is essential for an

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[16] Silvani, C., and K. Baer. 1997. Designing a Tax Administration Reform Strategy: Experiences and Guidelines. *IMF Working Paper* WP/97/30. Washington, DC: International Monetary Fund.

[17] ADB supports tax revenue mobilization and tax administration through development policy support programs. Key donors that support tax reforms include the World Bank, Millennium Challenge Corporation, United States Agency for International Development, Australian Agency for International Development, and Swedish International Development Agency. The International Monetary Fund also provides advisory services.

[18] World Bank. 1999. An Anticorruption Strategy for Revenue Administration. *PREM Notes* 33. Washington, DC: World Bank.

[19] Manasan, R. G. 2008. Are Recent Gains in BIR Tax Effort Sustainable? *Policy Notes* 07. Manila: Philippine Institute for Development Studies.

effective tax administration. With the reliable database, the authorities can further intensify the effort for anti-tax evasion program (the RATE) to improve taxpayers' voluntary compliance.

It is also important to allocate adequate resources for strengthening tax administration capacity. As mentioned, the numbers of tax officers both per population and per taxpayer in the Philippines are among the lowest in the region. Given the tight fiscal condition, it would not be easy to increase tax officers. However, it is an indispensable requisite for better tax administration. With further efforts in developing staff capacity, authorities need to consider allocating more human resources to tax collection authorities in the medium term.

Tax reform measures generally face serious challenges, particularly from the public. In particular, taxpayers oppose reforms when they do not realize the possible benefits of increased public services funded by their tax payments. Given the long-standing low delivery of key public services and the widespread corruption, the public in the country are skeptical about the link between costs (tax payments) and benefits (public service provisions). The new administration thus needs to show its strong political commitment to better public expenditure management to produce visible benefits of tax payments to the public.

Tax Reforms toward Fiscal Consolidation
Policy Options for the Government of the Philippines

This policy note assesses tax administration measures and tax rate adjustments, two options for the Philippines' fiscal consolidation in terms of their efficiency for revenue mobilization and impacts on tax equity. Its key findings are: 1) a policy mix of a higher value-added tax and a lower corporate income tax will make the overall tax system more regressive, even if its impact on tax revenue is neutral; 2) the country's tax productivity is much lower than those of its peers in the region, which signals the presence of significant tax loopholes and weak tax administration; and, 3) there is ample room to increase excise taxes on tobacco, alcoholic products, and gasoline, without ruining the equity of the tax system. These suggest that tax administration remains a key focus of efforts for the new administration.

About the Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to two-thirds of the world's poor: 1.8 billion people who live on less than $2 a day, with 903 million struggling on less than $1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

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