

**TRANSFERRING WEALTH: A LOOK AT THE CURRENT INCOME TAX
POLICIES IN THE PHILIPPINES AND PROGRESSIVE TAXATION**

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ABSTRACT

The research aims to study the income tax policies in the Philippines. The Philippine Constitution authorizes a progressive system of taxation which implies that taxes are proportional to income. Specifically, the research will mainly shed light on the effectivity of current income tax laws using comparative analysis of Southeast Asian countries. Taxes, as significant fiscal policy instruments, are major sources of government revenues which are used to finance the provision of social services or lessen the effects of poverty through tax exemptions and subsidies.

Public Fiscal Administration deals with the effective management and administration of taxes. The end goal of which is to promote inclusive growth. There are recent legislations advocating for a decrease in income tax rates.

Among the Southeast Asian countries, the Philippines has the second highest income tax rate with 32%, second from Vietnam which imposes 35%. Yet, it seems to be growing economically but not inclusively.

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ACRONYMS

- Forex (Foreign Exchange)
HB (House Bill)
NIRC (National Internal Revenue Code)
NPM (New Public Management)
PFA (Public Fiscal Administration)
WB (World Bank)

CHAPTER 1 INTRODUCTION

1.1 Statement of the Problem

The research will study the effective personal income tax policy appropriate to the country's economic and political situation that could promote inclusive growth. Specifically, it will delve on specific problems such as the effectivity of current personal income tax policies, optimal income tax policies, determination of how can income tax policies promote inclusive growth, assessment of current income tax policies in relation to inclusive growth, tax burden, tax reforms, and corresponding stakeholder/s who are affected by changes in income tax policies.

1.2 Goals and Objectives

The research aims to discuss and assess the current personal income tax policies in the Philippines. It aspires to set a balanced perspective between the current system and proposed tax reforms while taking into consideration their common ground and advantages. It will provide a comparison between income tax policies of Southeast Asian countries.

Theories and skills acquired from PA299.2 lectures and discussions will be applied in order to contribute to the study of Public Administration. Similar literatures will be provided to guide the research and to have a comprehensive output. This is also a tool utilized by the researcher to develop her knowledge in the subfield of Public Fiscal Administration concentrating on tax management.

Lastly, the research is intended to improve the current system of fiscal administration. It is a work in progress project which the researcher wants to cultivate to be able to share it publicly and inspire further reflections on the subject matter.

1.3 Significance of the study

The study deals with the reality of paying taxes that are deducted in an individual's salary. It sheds light on serious macroeconomic and public administration concepts such as income tax management, poverty, inequality, inclusive growth, and policy reforms. It is timely at the same time in relation to recent initiatives that advocates to change the current

income tax rate. This is primarily due to perceived high taxes and the fact that National Internal Revenue Code has not been revisited since it was enacted in 1998.

It will assess the current Philippine personal income tax system and compare it to Southeast Asian countries. This could be a starting point for corresponding income tax policies reform only if proven necessary. It will highlight the importance of income taxes to finance government activities bearing in mind that the ultimate goals of tax management are to produce inclusive growth and to reduce taxpayers' burden.

1.4 Scope and limitations

It will be limited to the following concepts:

- (1) Focus on income tax administration in the Philippines
- (2) Limit the comparative analysis to neighboring South East Asian countries
- (3) Use as a model the political and economic demographics in the Philippines (i.e. high poverty rate, inequality and current income tax administration)
- (4) Discuss the relationship between income tax administration and inclusive growth

CHAPTER 2 METHODOLOGY

2.1 Hypothesis

The current tax policies in the Philippines follow the progressive system of taxation as stated in the Philippine Constitution. Taxation as an instrument in fiscal policy is the lifeblood of government revenues. When utilized efficiently, this could promote inclusive growth in terms of providing basic social services. The tax on personal income as mandated in the National Internal Revenue Code was enacted in 1998. In 2013, the Philippines has the second highest growth rate in Southeast Asia with a 7.2%* annual growth in gross domestic product yet it has the highest poverty rate in the region with 25.2%** . Income tax could be lowered in order to increase the purchasing power of low income salary workers. In this way, low income workers could be better off financially. Economic growth can be inclusive if growth is felt from until the bottom of the population¹. The Philippines also has one of the highest income tax rates in Southeast Asia leaving low income workers pay more taxes than

¹ Philippine Development Plan

their neighboring country counterparts. A critical analysis of this fiscal situation will be verified in the study in order to assess whether tax reforms are necessary.

2.2 Research design

The study is a qualitative research focused on the comparative analysis of income tax systems in Southeast Asian countries. In choosing the research design, justifications were carefully considered. After analyzing the income tax system in the Philippines and current initiatives to reform it, evidences are essential to ascertain whether income taxes in the country is indeed higher hence, burdensome.

The economic and political situations in the Philippines are also accounted for. It is a sad truth that the country has a very high poverty rate yet previous and current administration have been claiming that the economy is growing. With this, poverty and inequality variables are included to quantify the statement.

Both public administration and economic Indicators together with their measurements such as effective tax administration, progressive taxation, minimization of tax burden, promotion of social welfare, and lessened economic inequality are chosen to show how can effective income taxes promote inclusive growth.

2.3 Data Collection

Selected secondary literatures were gathered and analyzed in order to define the variables and indicators. These were very significant in data analysis particularly in comparing the different income tax policies. Various data from both financial and public institutions such as the Bureau of Internal Revenue, World Bank, International Monetary Fund, Organization for Economic Cooperation and Development and others were utilized.

Journals, academic papers, and books were helpful in the research process. In particular, these are the Philippine Journal for Public Administration, Harvard University Publications, National Economic Development Authority Researches, Oxford University Press, World Bank Handbook, Asian Development Bank Paper Series and the rest of the related literature. International income tax data from Southeast Asian countries were meticulously collated to guide the recommendations.

Legislations and laws were also incorporated namely the Philippine Constitution, National Internal Revenue Code, and current income tax bills. In defining the variables especially the concepts of tax burden, optimal taxation, and inclusive growth, both public administration theories focusing on fiscal administration and public economics were combined. The current administration's development plans as manifested in the Philippine Development Plan served as the basis on how the country is faring.

2.4 Data Analysis

Since the research is focused on personal income tax policies in the Philippines, the available data were analyzed and compared to similar information from Southeast Asian countries. Concepts involved include current tax systems, optimal tax policies, public fiscal administration, and inclusive growth were all incorporated in the analysis.

The following tables are the income tax rates of selected Southeast Asian countries specifically the Philippines, Indonesia, Cambodia, Laos, Malaysia, Singapore, Thailand, and Vietnam. In other to have a common ground of comparison, the exchange rates prevailing on May 05, 2015 were computed and the point of comparison set was the highest personal income tax bracket in the Philippines which is over five hundred thousand (P500,000). The amount after the exchange rate has been computed is matched in the appropriate tax bracket in the respective neighboring country.

For instance, the exchange rate of a Philippine Peso to an Indonesian Rupiah is 1:294.1176. This implies that an income of P500,00 is equivalent to 147, 058, 800 Rupiah. Under the Indonesian income tax law, this converted income amount falls in the second bracket equal to a 15% tax.

Comparative Analysis of Current Personal Income Tax Rate of Selected Southeast Asian Countries

***Per P500,000 personal income (since this is the highest personal income tax cap in the Philippines)**

PHILIPPINES

| | |
|------------------------------------|---------------------------------------|
| Not over P10,000 | 5% |
| Over P10,000 but not over P30,000 | P500+10% of the excess over P10,000 |
| Over P30,000 but not over P70,000 | P2,500+15% of the excess over P30,000 |
| Over P70,000 but not over P140,000 | P8,500+20% of the excess over P70,000 |

| | |
|-------------------------------------|--|
| Over P140,000 but not over P250,000 | P22,500+25% of the excess over P140,000 |
| Over P250,000 but not over P500,000 | P50,000+30% of the excess over P250,000 |
| Over P500,000 | P125,000+34% of the excess over P500,000 |

Table 1 Income tax rate in the Philippines

Source: National Internal Revenue Code

INDONESIA

FOREX: 1 Peso = 294. 1176 Rupiah as of 05 May 2015 (P500, 000 = 147, 058, 800 Rp)

| Taxable Income Tax Brackets | Tax Rate |
|---|-----------------|
| Over Rp 500.000.000,00 (five hundred million rupiah) | 25% |
| Rp 50.000.000,00 (fifty million rupiah) or less | 5% |
| Over Rp 50.000.000,00 (fifty million rupiah) – Rp 250.000.000,00 (two hundred fifty million rupiah) | 15% |
| Over Rp 250.000.000,00 (two hundred fifty million rupiah) - Rp 500.000.000,00 (five hundred million rupiah) | 30% |

Table 2 Income tax rate of Indonesia

Source: Indonesian Income Tax Law of 2008 <<http://www.expat.or.id/info/2008-IncomeTaxSDSN.pdf>>

Same computations were applied to other Southeast Asian Countries. The exchange rates were obtained and the amount of comparison is converted. From this, the income tax rate equivalent to the case country at hand can be ascertained.

CAMBODIA

FOREX: 1 Peso = 91.27 Cambodian Riel as of 05 May 2015 (P500, 000 = 45, 635, 000 KHR)

| Taxable Income (KHR) | Tax rate |
|---------------------------------|-----------------|
| KHR 0 – 500,000 | 0% |
| KHR 500,001 – 1,250,000 | 5% |
| KHR 1,250,001 – 8,500,000 | 10% |
| KHR 8,500,001 – 12,500,000 | 15% |
| KHR 12,500,001 and above | 20% |

Table 3 Income tax rate of Cambodia

Source: **Cambodia Income Tax** <http://www.rd.go.th/publish/fileadmin/user_upload/AEC/AseanTax-Cambodia.pdf>

LAOS

FOREX: 1 Peso = 180.950 Lao Kip as of 05 May 2015 (P500, 000 = 90, 475, 000 Kip)

| Taxable Income per year (Kip) | Tax rate |
|--------------------------------------|-----------------|
| Kip 1 – 1,500,000 | 5% |
| Kip 1,500,001 – 4,000,000 | 10% |
| Kip 4,000,001 – 8,000,000 | 15% |
| Kip 8,000,001 – 15,000,000 | 20% |
| Above 15,000,000 | 25% |

Table 4 Income tax rate of Laos

Source: **Laos Income Tax** <http://www.rd.go.th/publish/fileadmin/user_upload/AEC/AseanTax-Lao.pdf>

MALAYSIA

FOREX: 1 Peso = 0.081 Malaysian Ringgit as of 05 May 2015 (P500,000 = 40, 500 MYR)

| Taxable Income | Tax Calculation | Tax Rate (%) | Tax Amount |
|----------------------------|--|---------------------|----------------------------|
| RM 0 to 2500 | On the First 2,500 | 0 | RM 0 |
| RM 2,501 to 5,000 | Next 2,500 | 0 | RM 0 |
| RM 5,001 to 10,000 | On the First 5,000 Next 5,000 | 1 | RM 0 RM 50 |
| RM 10,001 to 20,000 | On the First 10,000 Next 10,000 | 1 | RM 50 RM 100 |
| RM 20,001 to 35,000 | On the First 20,000 Next 15,000 | 5 | RM 150 RM 750 |
| RM 35,001 to 50,000 | On the First 35,000 Next 15,000 | 10 | RM 900 RM 1,500 |
| RM 50,001 to 70,000 | On the First 50,000 Next 20,000 | 16 | RM 2,400 RM 3,200 |
| RM 70,001 to 100,000 | On the First 70,000 Next 30,000 | 21 | RM 5,600 RM 6,300 |
| RM 100,001 to RM 250,000 | On the First 100,000 Next RM 150,000 | 24 | RM 11,900 RM 36,000 |
| RM 250,001 to RM 400,000 | On the First 250,000 Next 150,000 | 24.5 | RM 47,900 RM 36,750 |
| Exceeding RM 400,000 | On the First 400,000 Next RM | 25 | RM 84,650 |

Table 5 Income tax rate in Malaysia

Source: Malaysia Salary. <<http://www1.malaysiasalary.com/income-tax/income-tax-rate-for-2015-in-malaysia.html>>

SINGAPORE

FOREX: 1 Peso = 0.30 Singaporean Dollars as of 05 May 2015 (P500, 000 = 150,000 SD)

| Personal Income Tax Rates Applicable for YA 2012 to YA 2016 | |
|--|---------------------|
| Chargeable Income (S\$) | Tax Rate (%) |
| Less than 20,000 | 0 |
| 20,001-30,000 | 2 |
| 30,001 to 40,000 | 3.5 |
| 40,001- 80,000 | 7 |
| 80,001- 120,000 | 11.5 |

| | |
|------------------------|-----------|
| 120,001-160,000 | 15 |
| 160,001-200,000 | 17 |
| 200,001-320,000 | 18 |
| Above 320,000 | 20 |

Table 6 Income tax rate of Singapore

Source: Singapore Taxation <<http://www.taxationservices.com.sg/singapore-tax/personal-tax/>>

THAILAND

FOREX: 1 Peso = 0.7377 Baht as of 05 MAY 2015 (P500, 000 = 368, 840 THB)

| Taxable Income (baht) | Tax Rate (%) |
|--|--------------------|
| 0-150,000 | Exempt |
| more than 150,000 but less than 300,000 | 5 |
| more than 300,000 but less than 500,000 | 10 |
| more than 500,000 but less than 750,000 | 15 |
| more than 750,000 but less than 1,000,000 | 20 |
| more than 1,000,000 but less than 2,000,000 | 25 |
| more than 2,000,000 but less than 4,000,000 | 30 |
| Over 4,000,000 | 35 |

Table 7 Income tax rate in Thailand

Source: Thailand Revenue Department <<http://www.rd.go.th/publish/6045.0.html>>

VIET NAM

FOREX: 1 Peso = 484.72 Dong as of 05 May 2015 (P500, 000 = 242, 360, 000 VND)

| | |
|-------------------------|------------|
| 0 – 5,000,000 | 5% |
| 5,000,001 – 10,000,000 | 10% |
| 10,000,001 – 18,000,000 | 15% |
| 18,000,001 – 32,000,000 | 20% |
| 32,000,001 – 52,000,000 | 25% |
| 52,000,001 – 80,000,000 | 30% |
| 80,000,001 + | 35% |

Table 8 Income tax rate in Vietnam

Source: HSBC Worldwide Personal Tax Guide

<https://www.expat.hsbc.com/1/PA_ES_Content_Mgmt/content/hsbc_expatriate/pdf/en/global_tax_navnaviga/vietnam.pdf>

Using the computed data, the highest tax bracket in the Philippines can be easily compared to neighboring countries. It could be evaluated either as lower, at par, or higher than counterparts. The next table illustrates the obtained personal income tax rates:

| PERSONAL INCOME TAX RATE PER P500,000 OF SELECTED SOUTHEAST ASIAN COUNTRIES | |
|--|-----|
| VIETNAM | 35% |
| PHILIPPINES | 32% |
| LAOS | 25% |
| CAMBODIA | 20% |
| INDONESIA | 15% |
| SINGAPORE | 15% |
| THAILAND | 10% |
| MALAYSIA | 10% |

Table 9 Income tax rates of Southeast Asian countries

2.5 Literature Review

These literatures guided the research and served as basis for analysis. From these, definitions of the variables were made:

- (1) Systems of taxation – the prevailing tax system in the Philippines as mandated in the National Internal Revenue Code specifically on income tax (see income tax rate)
- (2) Current tax policies – present income tax bills as legislated in Congress
- (3) Tax burden – the economic effect of current tax
- (4) Optimal taxation – the most appropriate system of taxation relative to the country’s economic and social objectives
- (5) Inclusive growth – economic growth that is felt by all the population and that which promotes development

Comparative Tax Analysis

Brixi, Hana Polackovaet. al. (2004). Tax Expenditures – Shedding Light on Government Spending through the Tax System. The World Bank. Washington D.C.

The **purpose of the study** is to discuss the different system of tax expenditures policies across regions. In-depth discussions about tax expenditures and measurements were provided. Practices in ten (10) OECD countries such as Australia, Austria, Belgium, Canada, France, Germany, Italy, Netherlands, United Kingdom, and United States were illustrated.

The **methodology** used in the study is an inclusion of both quantitative and qualitative tax expenditure data analysis in the case countries. From these data, appropriate tax policies were recommended and reforms were crafted.

The author **concluded** that each country has a distinct tax expenditure program yet all tax expenditures should be managed critically and carefully.

The literature is very significant to the study as it sheds light on the effective tax practices across the globe. This will be utilized in tax policy analysis and ascertaining the feasibility of tax reforms.

Comparative Tax Systems

National Economic Development Authority. (1975). A Comparison of the Individual and Corporate Income Tax Systems in Some Countries in the Asia Pacific Region. National Tax Research Center.

The **purpose of the study** is to provide a comparison of individual and corporate tax systems in fifteen (15) countries namely Australia, Cambodia, China, India, Indonesia, Japan, Korea, Malaysia, New Zealand, Pakistan, Philippines, Singapore, Sri Lanka, Thailand, and Vietnam. It is a good manual that serves as a basis of quantitative tax data across these case countries.

The **methodology** used in the study is an illustration of the different tax systems particularly income and corporate taxes in the said countries. It focused on the following factors: tax bases, tax rates, and tax exemptions.

The author **concluded** that the Philippines has the most number of income brackets with 37 and it is the only country from the list at hand to exclude life insurance proceeds from being taxed.

The book is a reliable reference of tax bases not only across the Asia-Pacific region but most especially in the Philippines. A comparison can likewise be made and it can be added to the annexes supporting the study.

Development

Mendigorin, Abdon M. (1973). Taxation Under The New Society: A Developmental Approach. Philippine Journal of Public Administration. 17(1):80-94, January 1973.

The **purpose of the study** is to discuss the modern role of taxation in development. The legal mandate mentioned in the study is the Presidential Decree No. 69 (November 24, 1972) which modified the Philippine tax system making it suitable in the “New Society” through a responsive restructuring of all institutions and reforms implementation. It focuses on the role of taxation as a tool for capital formation, redistribution of income and wealth, and as a device for incentives and disincentives.

The **methodology** used is an analysis of these roles and means to improve the administration of tax. Factors which hamper tax administration are poverty, negative tax consciousness, undesirable behavior of tax administrators and defective tax policies.

The author **concluded** that the agricultural sector including idle lands must be taxed, Republic Act 1405 (September 9, 1955) which classifies bank deposits and bond investments issued by the Philippine government as confidential is recommended to be repealed in order to increase the reach of tax, and personal income on those exempt from taxed must also pay a minimal amount of tax.

The study is interesting in terms of its objective which is to explain the modern role of taxation in development. On the other hand, I do not agree with the other recommendation which is to tax employees who are exempt from paying taxes due to their low income since there is no need to burden the workers who receive meager salaries.

Development Tools

Bird, Richard M. (1970). Taxation and Development. Harvard University Press. Cambridge, Massachusetts.

The **purpose of the study** is to analyze fiscal problems and economic development. This covers development finance, tax policies and reforms.

The **methodology** used is the Columbian experience particularly the analysis of its public finance. In the latter part of the book, other fiscal administration concepts were added such as local government finance and taxing for development.

The author **concluded** that tax policy is a development tool. Hence, tax reforms are necessary to be institutionalized in order to be effective.

Even if the case study is in Columbia, this piece of literature is valuable as it contains detailed information on how tax reforms can be achieved. The strategies can be incorporated in the paper.

Inclusive Growth

Ali, Ifzal and Zhuang, Juzhong. (2007). Inclusive Growth Toward A Prosperous Asia: Policy Implications. Economics and Research Department Working Paper No. 97. Asian Development Bank.

The **purpose of the study** is to discuss inclusive growth in Asia particularly its significance in lessening inequality and promoting sustainable economic growth. It listed the factors associated with inclusive growth. Strategies to achieve it are also included.

The **methodology** used is an outlining of conceptual issues and the policies necessary to achieve inclusive growth. An analysis of economic variables namely income per capita, poverty incidence, inequality as measured by the Gini coefficient, expenditures, and progress in achieving the Millenium Development Goals are highlighted.

The author **concluded** that the policy necessary to achieve inclusive growth is centered on sustainable growth through employment opportunities and social inclusion. The components of the latter are expansion of human capacities, good policies and sound institutions, and social safety nets.

The literature defined the elements of inclusive growth. Means to achieve them are included. It is a significant work about the subject.

Income Distributions

Maertens, Peter R. (1984). Income Distribution and the Role of Taxation in Philippine Development: An Analysis of Two Decades. Philippine Journal of Public Administration. 28(4):321-374, October 1984.

The **purpose of the study** is to explain the *role of tax in distributing income*. Historical data from 1960-1972 and 1973-1980 were included to illustrate the changes in total household income and *tax burden* of different groups.

The **methodology** used is a *comparative analysis of the tax revenue* of different groups from 1972-1980 and the 1960 study. The *tax instruments* determine the increase or the decrease in the total tax revenue of different groups.

The author **concluded** that the government must be mindful of the *historical economic trends* in order to craft effective taxation policies. This will only be possible through long-term political wisdom, strong political commitment, and administrative capability.

The study clearly pointed out the significant role of tax in distributing income. The historical economic data can be incorporated in the paper as a basis.

Growth and Development

Commission in Growth and Development. (2008). The Growth Report: Strategies for Sustained Growth and Inclusive Development. The International Bank for Reconstruction and Development/The World Bank.

The **purpose of the study** is to give details on the strategies for sustained growth which could foster inclusive development. It discussed growth and the “13 Success Stories”.

The **methodology** used in analyzing the system is the *macroeconomic view* which includes income redistribution, persistence of poverty, and how tax reform could be a tool to increase the economic capacity of the poor.

The author **concluded** that there is an *inequitable income distribution* and *higher poverty rate* in the Philippines than in other neighboring countries which are caused by a *sluggish economic growth* and *ineffective policies*.

Direct taxes were found to be progressive while *indirect taxes* were said to be regressive. The poor spend more of their income on food than the wealthy thereby making the latter type of tax regressive.

Tax reforms may result in both positive and negative effects. As such, not all tax reforms may produce an equal distribution of income or reduce poverty. Nevertheless, the study has valuable insights on tax systems and reforms in the Philippines. It is a good basis for the current paper the researcher is conducting particularly in mitigating the tax discrepancy between salaried workers and other professionals.

Progressive Income Taxation

Colm, Gerhard. (1955). *Essays in Public Finance and Fiscal Policy*. Oxford University Press.

The **purpose of the study** is to discuss the characteristics of an ideal tax system which are justice-based, fiscal productivity, and serviceability. He defined fiscal justice as the enduring right of citizens against the state.

The **methodology** used is a descriptive analysis of justice as the heart of an ideal tax system. This was related to capitalism and issues regarding the components of an ideal tax policy were included.

The author **concluded** that justice requires equality and universality yet it is a changing theory depending on one's political and economic situation. Progressive income taxation is an example of an ideal tax system.

The essays are relevant since they offer different perspectives most of which in economics about tax policies and administration. This could assist the study at hand in terms of effective tax administration policies.

Roles of Taxation

Bloch, H.S. *The Relation of Tax Policy to Economic Growth* in Smith, Dan et. al. (1953). *The Limits of Taxable Capacity*. Tax Institute Incorporated. Princeton.

The **purpose of the study** is to understand the relationship of tax policy particularly the increase in the ratio of tax burden to national income during the growth of the economy.

The **methodology** used in the study is an analysis of the capacity to pay taxes in relation to government expenditures. It dealt with issues as tax compliance, effects of taxation, and the relationship of tax policy to economic growth.

The author **concluded** that tax policy must be related to expenditure policies and the economic framework it operates. Additional government revenue is needed to facilitate development.

The discussion about the roles of tax policies is essential in understanding their effects. From this perspective, more effective tax policies can be recommended. Also, this literature gives a clear view about the role of taxation in economic growth.

Tax Burden

Shah, Anwar & Khalil-Shirazi. (1991). Tax Policy in Developing Countries. The International Bank for Reconstruction and Development/The World Bank.

The **purpose of the study** is to present the tax policies in developing countries. In this light, it analyzed tax reforms and different systems of taxations particularly indirect taxes, tax on foreign investment, tax on agricultural land and financial institutions. It enlightened the readers on tax incidence and its redistributive impact on developing countries, tax burden, institutional distribution and tax benefit model.

The **methodology** used in the study is a comparative analysis of tax policies in developing countries. Lessons learned on tax were given as examples for tax reforms and tax incidence analysis.

The author **concluded** that taxation is a component of development through the provision of basic social services. Tax reforms are deemed necessary if it will foster growth, address unemployment and alleviate poverty.

This literature is complete in terms of taxation policies and link to development. It is very useful for the research. The topic on tax incidence is timely.

Tax Policy

Gerson, Philip. (1998). *Poverty, Income Distribution, and Economic Policy in the Philippines*. International Monetary Fund.
<<http://www.imf.org/external/pubs/ft/wp/wp9820.pdf>>

The **purpose of the study** is to examine the system of taxation in the Philippines. The instrument utilized is the *Comprehensive Tax Reform Program (CTRP)* which was implemented in 1994. This policy advocated *tax reform* particularly for oil, cigarettes, alcohols, personal and corporate income.

The **methodology** used in analyzing the system is the *macroeconomic view* which includes income redistribution, persistence of poverty, and how tax reform could be a tool to increase the economic capacity of the poor.

The author **concluded** that there is an *inequitable income distribution* and *higher poverty rate* in the Philippines than in other neighboring countries which are caused by a *sluggish economic growth* and *ineffective policies*.

Direct taxes were found to be progressive while *indirect taxes* were said to be regressive. The poor spend more of their income on food than the wealthy thereby making the latter type of tax regressive.

There are many loopholes in the tax system such as the high incidence of tax avoidance by the wealthy and other professionals who are the ones who declare their own income. As such, tax reform in the form of a lower income tax is recommended.

Tax reforms may result in both positive and negative effects. As such, not all tax reforms may produce an equal distribution of income or reduce poverty. Nevertheless, the study has valuable insights on tax systems and reforms in the Philippines. It is a good basis

for the current paper the researcher is conducting particularly in mitigating the tax discrepancy between salaried workers and other professionals.

Tax Reforms

Gloria, et. al. (2014). *An Analysis of Philippine Income Tax Reforms*. Asian Institute of Management. <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2466989>

The **purpose of the study** is to examine the possibility of income tax reforms in the Philippines. It is advocating *inclusive growth* and *development* through redistribution of income.

The **methodology** used in analyzing tax reforms is the analysis of previous proposals to change the system of taxation and their significance. These proposals namely *Senate Bill 2149*, *Senate Bill 1942*, and *Senate Bill 716* were sponsored by Senator Edgardo Angara, Senator Benigno Aquino IV, and Senator Ralph Recto respectively.

The authors **concluded** that each of the tax reform proposals has its own *tradeoff* in terms of *equity and efficiency*. Each proposal could be effective depending on the desired taxation or income objectives.

The study is very useful in terms of the current movements in tax reform. From these initiatives, the paper could include the significant contributions of each proposal to the betterment of the system of taxation in the Philippines.

Tax Revisions

Lim, Avelino B. The Case of Tax Revision. (1962). *Philippine Journal of Public Administration*. 6(3):192-199 July 1962.

The **purpose of the study** is to highlight the need to revise the current tax policies in the country due to its obsolence and ineffectiveness. By doing so, more government revenues can be generated and *corrupt practices* could be mitigated.

The **methodology** used in showing the archaism of the tax policies prevalent at that time and the need to reconstruct it is an illustration of the perceived defects and their resulting effects.

The author **concluded** that the following are the perceived defects in the tax code namely: (1) *ambivalent tax provisions*, (2) *flaws in codal amendments*, and (3) *non-integration of tax mandates embodied in special laws*. These result in numerous interpretations of tax laws, errors in implementation, and confusion in the tax exemptions.

The criticisms on the timeliness and appropriateness of tax policies are worthy to take note of. Likewise, historical tax issues were included and can be incorporated in the paper as points of consideration.

CHAPTER 3 REVIEW OF RELATED LITERATURE

3.1 Indicators and measurements

The **concepts or variables** the research will analyze are namely: (1) systems of taxation, (2) current tax policies in the Philippines, (3) the notion of tax burden, (4) optimal taxation, and (5) inclusive growth. Each of these will be defined in this section.

The **indicators** for each variable are (1) effective tax administration, (2) progressive taxation, (3) minimization of tax burden, (4) promotion of social welfare, and (5) lessening economic inequality respectively.

The **measurements** for each indicator are (1) proper tax administration in the form of accounting, collection, and evaluation; (2) neighboring Southeast Asian countries' personal income tax rates and present bills advocating reforms in personal income tax rates; (3) lessened effect of tax burden evident in greater purchasing power of individuals; (4) decrease in poverty rate; and (5) lower economic inequality.

3.2 Frameworks

Public fiscal administration in the Philippines will serve as the core foundation of the study. As such, the Public Administration Theories that will be discussed are income tax policies, income tax reforms, and development.

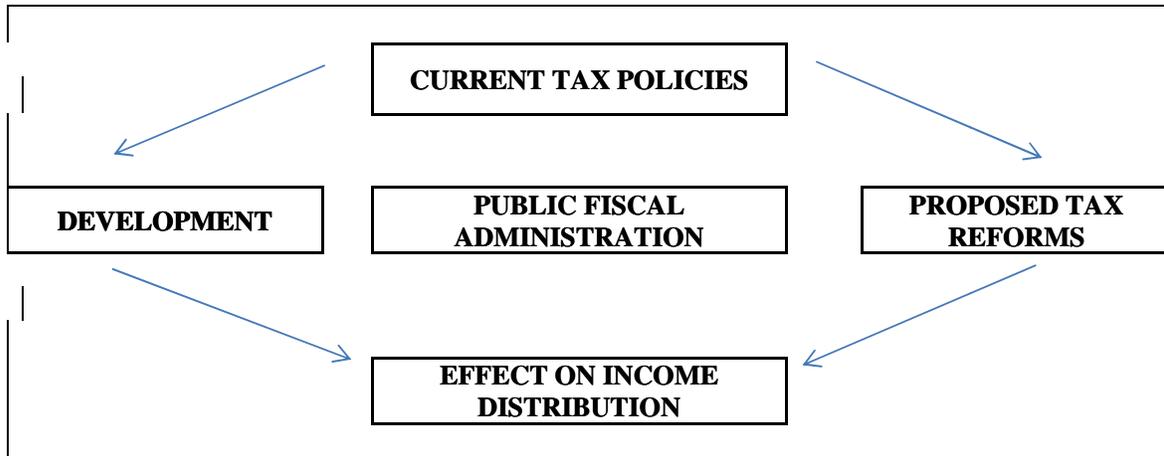


FIGURE 1: THEORETICAL FRAMEWORK

The study aims to shed light about the current systems of taxation in the country and the current proposed tax reforms. In this process, optimal taxation policies can be recommended which are based on inclusive growth and development.

Taxation policies have a direct relationship with government revenues and development. Aside from a discussion of the tax systems in the Philippines, the study aims to relate the significance of tax policies to development.

The study focuses on the systems of taxation in the Philippines and development. It will recommend measures to improve current tax policies.

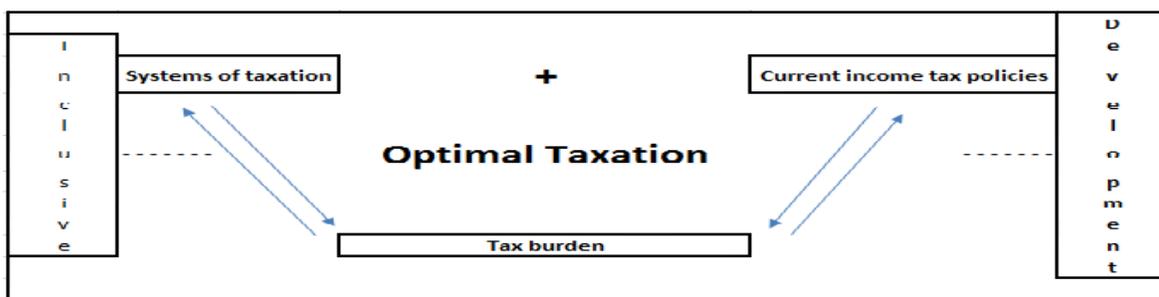


FIGURE 2 CONCEPTUAL FRAMEWORK

SYSTEMS OF TAXATION

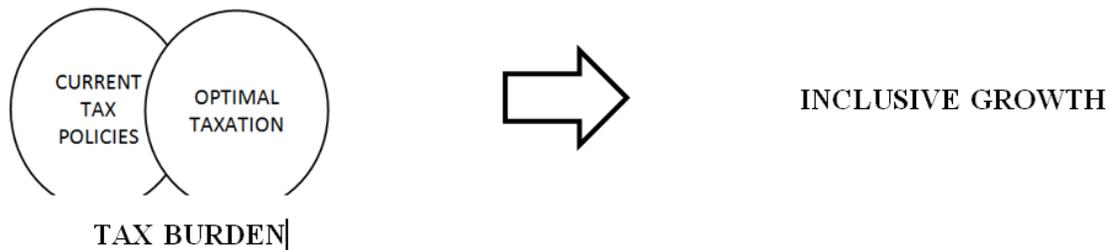


FIGURE 3 OPERATIONAL FRAMEWORK

The diagram above illustrates the relationship of all the research variables. Indicators need to be incorporated in order to understand the model. For instance, effective tax administration will be utilized in analyzing the system of taxation, so are progressive taxation for current tax policies, minimization of tax burden, promotion of social welfare for optimal taxation, and lessening economic inequality for inclusive growth.

3.3 Operational definitions

(1) Systems of taxation

The main functions of taxation are to generate government revenues, redistribute wealth or income, and control societal activities (Woodon, 2005). The research will focus on the current income taxation in the Philippines but will also include general income taxation types. The personal income tax rate for self-employed and practicing professionals is mandated under the *Republic Act 7496 or the Act Adopting the Simplified Net Income Taxation Scheme for the Self-employed and Professionals Engaged in the Practice of their Profession*:

| | |
|-------------------------------------|---------------------------------------|
| Not over P10,000 | 3% |
| Over P10,000 but not over P30,000 | P300 + 9% of excess over P10,000 |
| Over P30,000 but not over P120,000 | P2,100 + 15% of excess over P30,000 |
| Over P120,000 but not over P350,000 | P15,600 + 20% of excess over P120,000 |
| Over P350,000 | P61,600 + 30% of excess over P350,000 |

Table 10 Income tax rate in the Philippines for self-employed

Also known as the Tax Reform Act of 1997, the National Internal Revenue Code is the main basis for the taxation system in the Philippines. The national policy in terms of taxation is to promote sustainable economic growth through equitable tax administration.

(2) Current tax policies in the Philippines

The Constitution of the Philippines mandates a uniform and equitable rule on taxation as the Congress promotes a progressive tax system. Currently tax bills and resolutions in the

Congress include the: House Bill No. 210 that proposes a new and lower income tax rate, House Bill No. 4992 which seeks to amend the income tax rate of low salaried employees, and House Bill No. 5401 that aims to restructure the income tax brackets in the country.

House Bill No. 210 (July 01, 2013)

This is introduced by Honorable Salvacion S. Ponce Enrile and advocates a boost in the purchasing power of consumers through an increase in net salary. The proposed new income tax rate is exactly lower by a half as illustrated below:

| | |
|-------------------------------------|--|
| Not over P10,000 | 2.5% |
| Over P10,000 but not over P30,000 | P250+5% of the excess over P10,000 |
| Over P30,000 but not over P70,000 | P1,250+7.5% of the excess over P30,000 |
| Over P70,000 but not over P140,000 | P4,250+10% of the excess over P70,000 |
| Over P140,000 but not over P250,000 | P11,250+12.5% of the excess over P140,000 |
| Over P250,000 but not over P500,000 | P25,000+15% of the excess over P250,000 |
| Over P500,000 | P62,500+17.5% of the excess over P500,000 in 1998. |

Table 11 House Bill No. 210 Proposed Income Tax Rate

House Bill No. 4992 (September 11, 2014)

Representative Raul Del Mar initiated this bill in order to alleviate the plight of low income salaried employees. It seeks to improve the Republic Act 9504 which exempts minimum wage earners from paying taxes by proposing to tax only the income in excess of P100,000 using the existing tax rates.

House Bill No. 5401 (February 03, 2015)

Several lawmakers such as the Bayan Muna Partylist, Representative Neri Colmenares, and Representative Carlos Zarate introduced this timely bill aiming to restructure the income tax brackets. It clarifies that the Philippines imposes the highest personal income tax in the ASEAN Region with a 32% annual income tax for a P500,000 salary compared to 20% in Vietnam, 20% in Cambodia, 12% in Laos, 11% in Malaysia, 10% in Thailand, 2% in Singapore, and 0% in Brunei. The highest daily minimum wage in the country is given to workers in Metro Manila at P466 while the lowest is P213 in Ilocos. The suggested income tax rate is:

| | |
|---------------------------------------|---|
| Not over P396,000 | Exempt |
| Over P396,000 but not over P640,000 | 10% of the excess of P396,000 |
| Over P640,000 but not over P1,000,000 | P24,400+15% of the excess over P640,000 |

| | | |
|-----------------|---------|---|
| Over P1,000,000 | but not | over P78,400+20% of the excess over P1,000,000 |
| P1,650,000 | | |
| Over P1,650,000 | but not | over P208,400+25% of the excess over P1,650,000 |
| P2,700,000 | | |
| Over P2,700,000 | | P470,900+30% of the excess over P2,700,000 |

Table 12 House Bill No. 5401 Proposed Income Tax Rate

(3) Concept of tax burden

Tax payment is a civic duty of all Filipino citizens. Tax as a major government revenue is used to finance government activities and provision of social services. For consumers, they pay value-added taxes for every product or service they purchase aside from the fact that the country also imposes the highest income tax in the ASEAN region. The notion of tax burden is the amount of tax an individual pays so for an increase or decrease in the tax rate, there is a corresponding effect in the tax burden.

(4) Optimal taxation

This is the most effective system of taxation that makes both the government and taxpayers better off and that which promotes inclusive growth and development. It can also be one that fulfills the set tax objectives. Woodon (2005) stated that the assumptions in optimal tax approach are that the government needs revenues, it taxes income and products, individuals and corporations’ optimization is considered, and it maximizes social welfare.

(5) Inclusive growth

Economic growth as measured by gross national product is seldom inclusive as in the Philippines which has a poverty rate of more than 20% in 2012. An increase in government revenues through tax does not guarantee economic growth that is felt by all its citizens. A wide gap between the rich and the poor in the country remains and hinders the attainment of inclusive growth. Tax can be utilized as an instrument to promote growth that is inclusive through a lower income tax for low salary employees taking into consideration the effects of inflation.

The Philippine Development Plan describes inclusive growth as one which is appropriate to the size of the population, geography, and social structures. Economic growth is inclusive if it creates jobs and reduces poverty. Inclusive growth translates into economic equality. The

Gini coefficient is used to measure inequality using two (2) variables which are income and population. A higher Gini implies that there is a high inequality in the country.

Below is a table illustrating the inequality ratios of selected Southeast Asian countries. The Philippines ranks second in terms of high income inequality.

| GINI COEFFICIENT OF SELECTED SOUTHEAST ASIAN COUNTRIES | |
|---|-------|
| QUANDL.COM SCALE: 50- HIGH >30-MEDIUM <30- LOW | |
| MALAYSIA (2009) | 46.21 |
| PHILIPPINES (2012) | 43.03 |
| SINGAPORE (1998) | 42.48 |
| THAILAND (2010) | 39.37 |
| INDONESIA (2011) | 38.14 |
| LAOS (2012) | 36.22 |
| VIETNAM (2012) | 35.62 |
| CAMBODIA (2011) | 31.82 |

Table 13: Gini Coefficient of Selected Southeast Asian Countries
Source: Quandl.com

The next table shows the poverty rates in these countries. Notably, the Philippines has the highest percent of population living at national poverty lines.

| POVERTY RATE (2013) Percent of Population at National Poverty Lines | |
|--|---------|
| Philippines | 25.2 |
| Laos | 23.2 |
| Cambodia | 17.7 |
| Vietnam | 17.2 |
| Thailand | 12.6 |
| Indonesia | 11.4 |
| Malaysia | 1.7 |
| Singapore | No data |

**Table 14: Poverty Rates of Selected Southeast Asian
Countries**

Source: World Bank

Poverty in the country remains high despite the remarkable growth in its annual gross domestic product.

| ANNUAL GROWTH OF GROSS DOMESTIC PRODUCT (2013) | |
|--|------|
| CAMBODIA | 7.4% |
| PHILIPPINES | 7.2% |
| INDONESIA | 5.8% |
| LAOS | 5.4% |
| VIETNAM | 5.4% |
| MALAYSIA | 4.7% |
| SINGAPORE | 3.9% |
| THAILAND | 1.8% |

Table 15: Annual Growth in Gross Domestic Product

Source: World Bank

Tax as a fiscal policy instrument can be a tool for promoting inclusive growth such is exempting low income workers. Other known method includes progressive taxation which is also mandated in the Philippine Constitution.

In order to study further the personal income tax rate in the Philippines, the current tax policy is compared with selected Southeast Asian countries namely Cambodia, Indonesia, Laos, Malaysia, Singapore, Thailand, and Vietnam. Since the highest personal income tax cap in the country is P500,000 or greater, this is used as the base in comparing each country's rate.

The next figure depicts the key indicators for inclusive growth which are (1) sustainable growth, (2) social inclusion, and (3) social safety nets that government institutions can employ.



FIGURE 4: INCLUSIVE GROWTH INDICATORS

Source: Asian Development Bank

Tax can be an instrument in achieving these indicators through effective tax administration from collection to accounting. By doing so, sustainable growth in terms of government revenues can be possible. Also, social inclusion can be targeted by imposing less tax on low salary employees so they could invest in education, health, and other activities for their human development. Tax if administered properly, is also a good social safety net that could protect the poor from paying too much.

Inclusive growth through effective and progressive taxation can be measured through a decrease in poverty rate after such tax policy reform has been enacted. Comparative data show that the Philippines has one of the highest personal income tax rates in Southeast Asia and it has the highest poverty rate. There are current clamors to reduce this rate in order to “unburden” low salary workers.

CHAPTER 4 RESULTS AND DISCUSSIONS

After gathering and analyzing the data, the following results were obtained: first, the Philippines indeed has a high income tax rate compared to other Southeast Asian countries. Second, a high government revenue in the form of taxes did not contribute to reduce poverty and inequality in the country. Third, with this, clamors to reduce income taxes can be considered in order to increase the net pay of salaried workers hence, their consumption and reduce inequality.

Perceived tax burden then is higher with a high tax rate. The stakeholders bearing this burden are employees and workers. Therefore, the most effective personal income tax policy appropriate in the political and economic context of the Philippines is a lower one which advocates the welfare of the poor.

Current income taxes cannot be considered effective in terms of alleviating poverty and promoting inclusive growth. Optimal income taxes aspire to help citizens and build a sustainable economy thereby unburdening taxpayers. It is important to note that other factors not included in the research such as inflation, corruption, and change of administrations can also affect growth and development.

CHAPTER 5 CONCLUSIONS

The research studied the current system of income taxation in the Philippines in terms of its effectivity. It was compared to other Southeast Asian countries and results show that it is higher so are poverty and inequality in the country. Initiatives to reform and lower current rates seem to be attractive as they envision to ease poverty levels.

If utilized properly, taxes are powerful public fiscal administration tools that can make or break people out of poverty zones and unburden taxpayers. Under the current income tax system, inclusive growth can hardly be seen with the data gathered. Tax incidence remains burdensome to stakeholders affected.

The three (3) pending bills in Congress are worthy to be reflected upon and better yet, implemented.

CHAPTER 6 IMPLICATIONS TO PUBLIC FISCAL ADMINISTRATION

Studies on taxation are very relevant since it affects citizens in countless means. Though very serious and most of the time difficult to predict, these researches add to the development of the field. There are limited works regarding these but it is always worth the time to ponder on what ways can academicians contribute to the greater reality outside the university which are that of poverty and governance.

This research can contribute to further studies regarding income taxation and its link to the promotion of inclusive growth. Through this, current systems were critically analyzed and assessed. It also provided a comparison between different tax systems.

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