



Fiscal Reform Social Implications

The World Bank
Philippines Development Forum
Fiscal Working Group Meeting
Shangri-La Hotel Makati
28 October 2005

Background

- August 2004 general acknowledgement of fiscal deterioration.
- MTPDP 2004-2010 proposes eight legislative revenue measures.
- Two measures with clear revenue impact were passed.
 - The sin tax
 - The EVAT
- Other measures remain difficult to quantify.

**Original Legislative
Revenue Measures**

Status**Yield**

| | | |
|--------------------------------------|---|---------------------|
| Excise tax on sin products | Passed in 2004; 2005 first half collection below target | 15 billion |
| EVAT | Passed in May 2005; Implementation expected in Nov 2005 | 83 billion |
| Excise tax on petroleum products | Combined with EVAT as mitigating measure | Subsumed in EVAT |
| Lateral attrition | Passed; not yet being Implemented | Hard to determine |
| Rationalization of fiscal incentives | Deferred | 5 billion |

Focus Shifts to Implementation

- Legislation of revenue measures are done.
- The Supreme Court has removed all impediments to the implementation of the EVAT.
- Implementation is the next step, especially for the VAT, whose performance has been disappointing over the last ten years. (From 1.3% of GDP in 1994 to 1.7% in 2004).

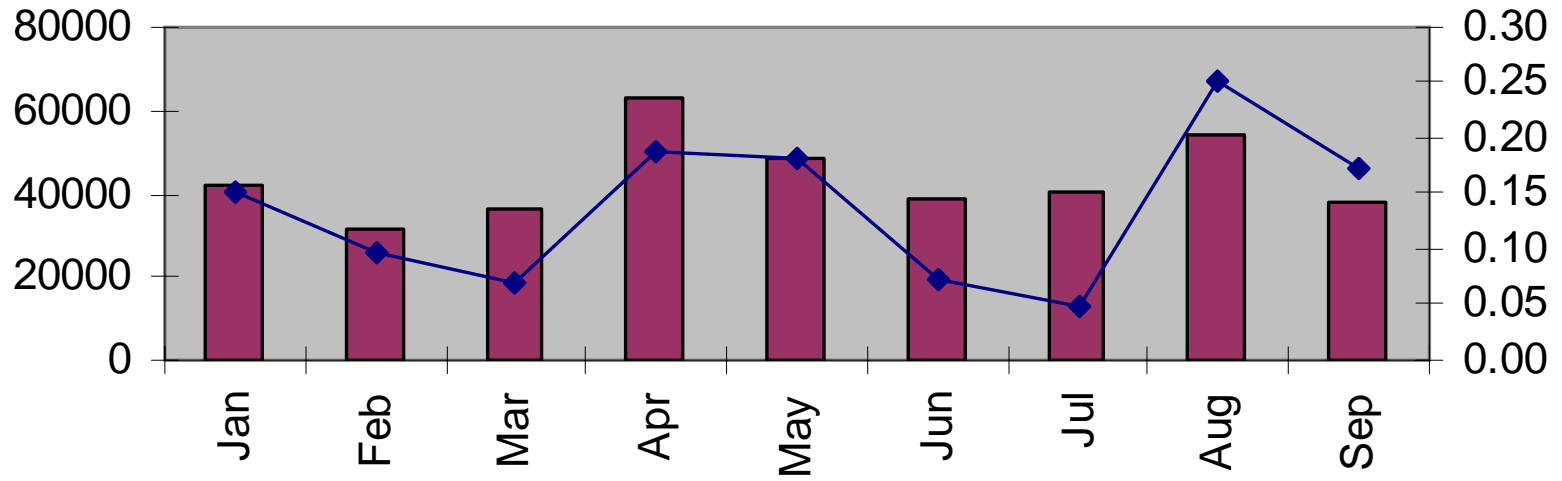
VAT efficiency ratio

| in billions of pesos | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 |
|----------------------|--------------|--------------|--------------|--------------|--------------|---------------|
| VAT collection | 22 | 30 | 41 | 47 | 48 | 55.15 |
| Nominal GDP | 1693 | 1906 | 2172 | 2427 | 2665 | 2977 |
| VAT/GDP | 1.3% | 1.6% | 1.9% | 1.9% | 1.8% | 1.85% |
| VAT rate | 10.0% | 10.0% | 10.0% | 10.0% | 10.0% | 10.00% |
| VAT efficiency ratio | 12.9% | 15.5% | 18.8% | 19.5% | 17.8% | 18.53% |
| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005/p |
| VAT collection | 54 | 59 | 66 | 83 | 80 | 98 |
| Nominal GDP | 3355 | 3631 | 3960 | 4211 | 4739 | 5354 |
| VAT/GDP | 1.6% | 1.6% | 1.7% | 2.0% | 1.7% | 1.8% |
| VAT rate | 10.0% | 10.0% | 10.0% | 10.0% | 10.0% | 10.0% |
| VAT efficiency ratio | 16.1% | 16.3% | 16.6% | 19.6% | 16.9% | 18.2% |

Recent Signs of Progress

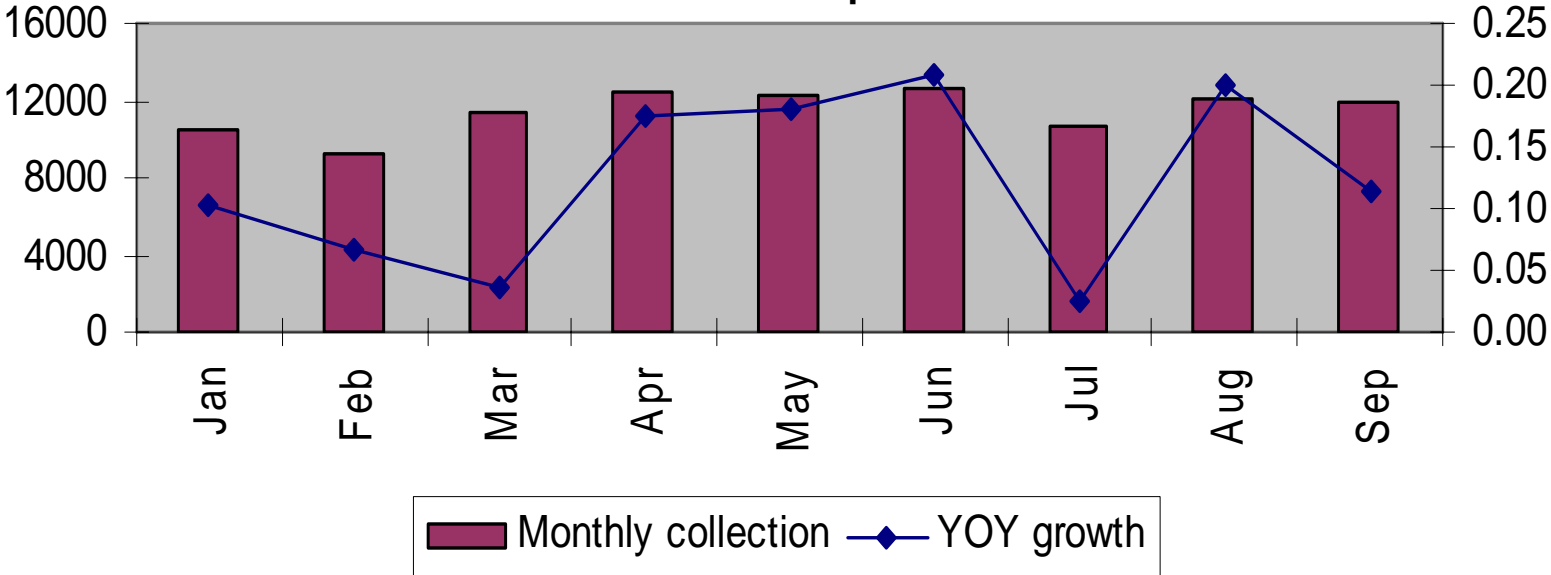
- Over the last nine months, corporate income tax and individual income tax have improved substantially.
- The sin tax collection appears to be catching up in the second half.
- However, progress on total revenue performance has not been sustained.
 - BIR collection significantly high in April and August
 - BOC collection significantly high in June and August

BIR 2005 collection in millions of Pesos



Monthly collection — YOY growth

BOC 2005 collection in millions of pesos

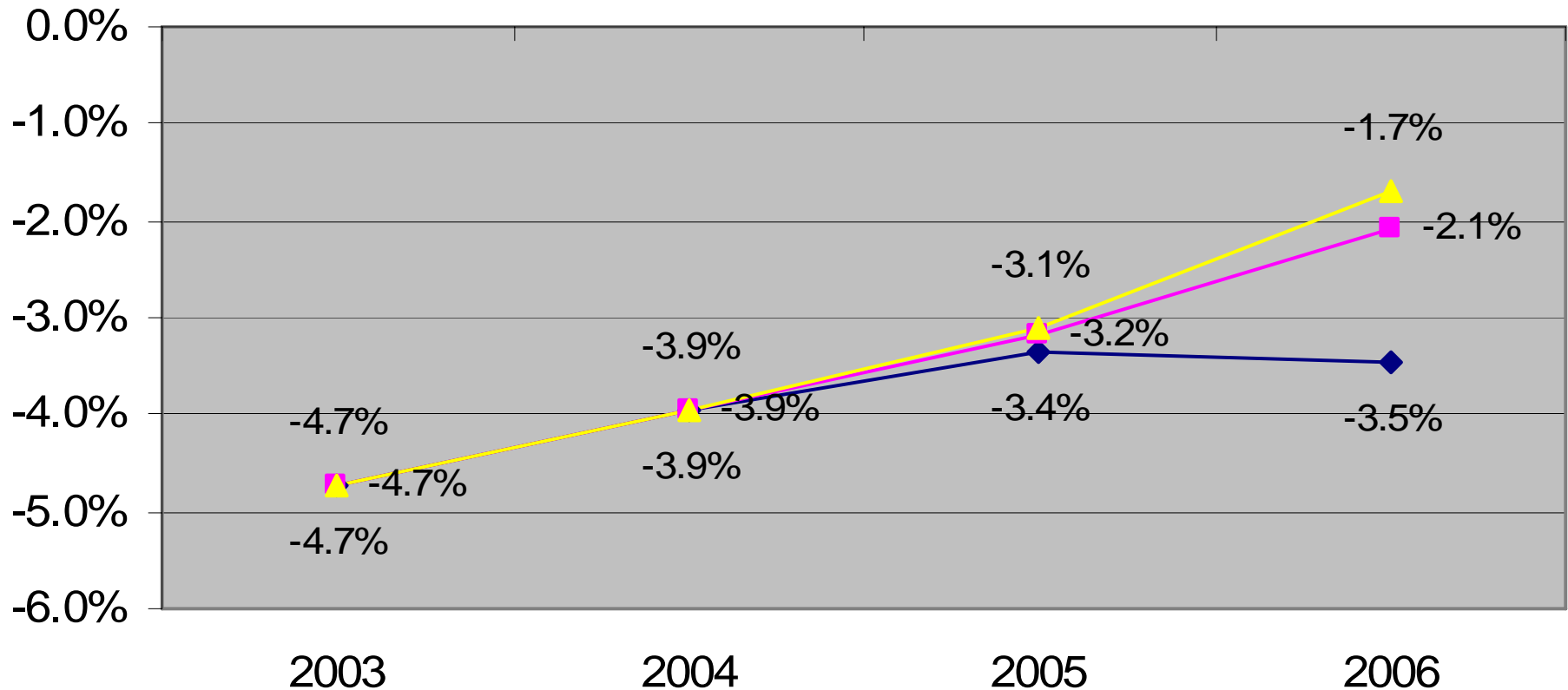




Sustained institutional reform crucial

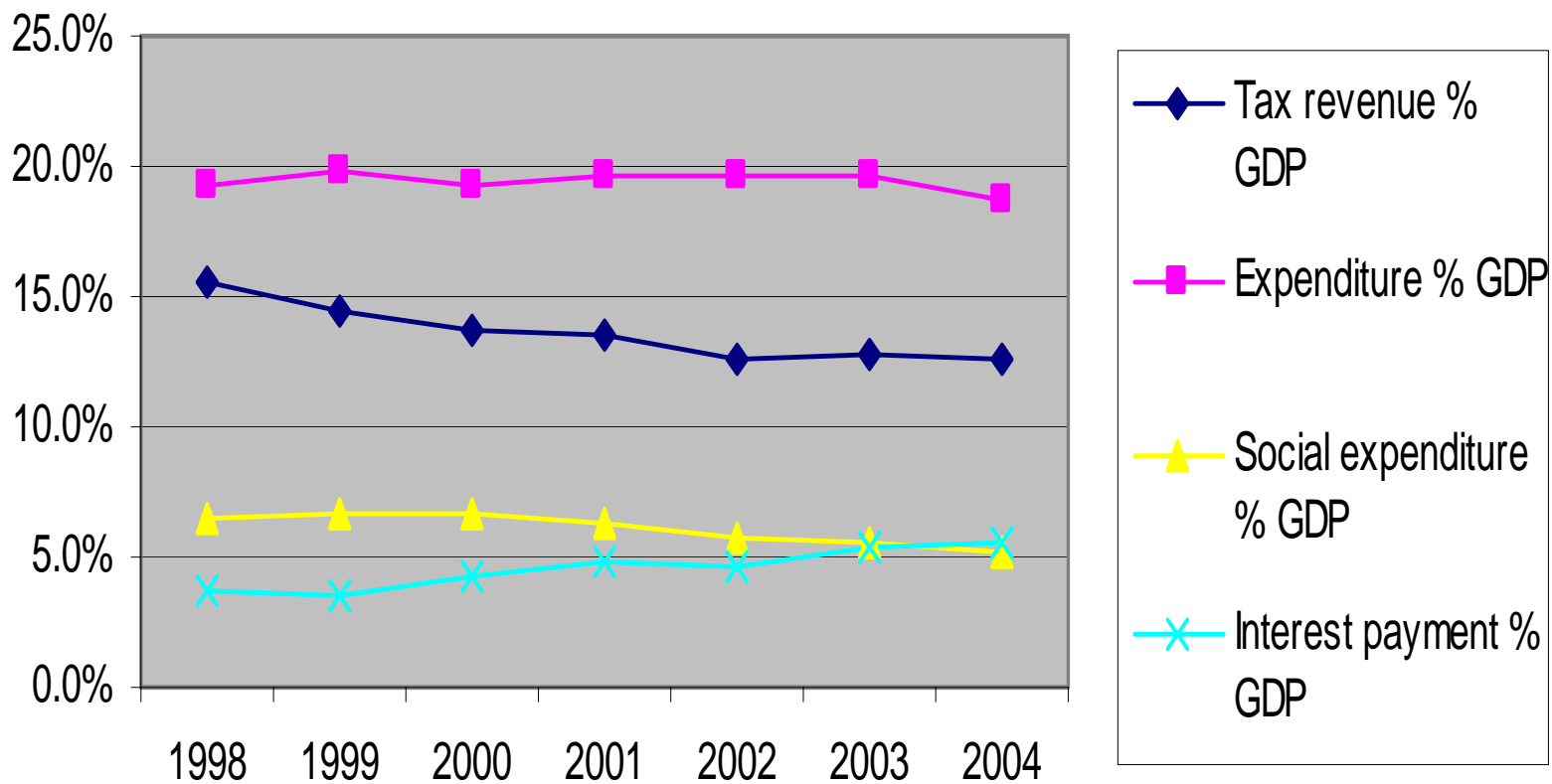
- Comprehensive upgrading of BIR and BOC roles and functions.
- Improve information systems for tax compliance
- Improve registration, tax processing, payments and standardize reporting systems.
- Simplify Procedures
- Strengthen Audit systems
- Improve client orientation of BIR and BOC
- Modern human resource management strategy

Fiscal scenarios - VAT and Improved Admin



- ◆ Deficit without EVAT and admin/GDP
- Deficit with EVAT/GDP
- ▲ Deficit with EVAT and admin/GDP

Fiscal ratios 1998-2004





Impact of E-VAT on the Poor

Minimal Impact on Poor

- For the bottom 50% of the population, the EVAT will increase their expenditure by about 2.3% or about P1.00 per day.
- The richest 10 percent of households would contribute 39% of VAT revenue
- The poorest 50 percent of families will contribute 17% of VAT revenue. The non-poor will account for about 83 percent of the VAT
- Most items in the poor's consumption basket are VAT-free.
- Cooking gas and commuting costs are perhaps the only significant commodities subject to EVAT.

Average Percentage Increase on Bottom 50% of Population

| Commodity group | Weights | Percent increase due to VAT | Average percent Increase |
|--------------------------|---------------|-----------------------------|--------------------------|
| All Items | 100.0% | 0.0% | 2.3% |
| Food, Beverage & Tobacco | 65.0% | 0.6% | 0.4% |
| Clothing | 3.5% | 5.0% | 0.2% |
| Housing & repairs | 10.0% | 5.0% | 0.5% |
| Fuel, light & water | 5.7% | 6.6% | 0.4% |
| Services | 8.7% | 5.0% | 0.4% |
| Miscellaneous items | 7.2% | 5.0% | 0.4% |

Note: Assumes 5% increase in prices of poor's purchases of other commodities.

Minimal Impact on Food Items

| Food item | Price per kilo before VAT | Official Price per kilo after VAT | Percent increase in price |
|---|---------------------------|-----------------------------------|---------------------------|
| Rice | 20.76 | 20.77 | 0.05% |
| Corn | 10.60 | 10.30 | 0.03% |
| Bangus | 83.03 | 83.05 | 0.04% |
| Tilapia | 67.93 | 68.04 | 0.02% |
| Cabbage | 24.03 | 24.01 | 0.00% |
| Eggplant | 43.37 | 43.40 | 0.05% |
| Chicken | 97.33 | 97.41 | 0.09% |
| Pork | 141.67 | 141.94 | 0.19% |
| Other food items (include some semi-processed) | | | 4.00% |
| Average increase for poor | | | 0.64% |

Source: DOF, DA, DOE, NTRC, WB staff estimates

Minimal Impact on Power Consumption

| Electricity (monthly) | Peso increase per kwh |
|--------------------------------------|--------------------------------------|
| Residential | |
| <i>Below 200 kwh</i> | 0.00/kwh |
| <i>Between 200 and 999 kwh</i> | 0.73/kwh |
| <i>Above 999 kwh</i> | 0.85/kwh |
| Commercial | 0.85/kwh |
| Average increase for poor | 0.00/kwh |

Source: DOF, DA, DOE, NTRC, WB staff estimates
Note: figures above for MERALCO clients only.

Mitigating Measures on Petroleum

| | Price per liter before VAT | Mitiga- ting mea- sure | Price per liter at 10% VAT | Percent increase at 10% | Price per liter at 12% VAT | Percent increase at 12% |
|---|-------------------------------------|------------------------------|----------------------------------|-------------------------------|----------------------------------|-------------------------------|
| Unleaded | 34.07 | 0.85 | 36.54 | 6.80% | 37.21 | 9.21% |
| Premium | 35.55 | 0.40 | 38.67 | 8.10% | 39.37 | 10.74% |
| Diesel | 32.45 | 2.13 | 33.35 | 2.70% | 33.96 | 4.65% |
| Kerosene | 33.01 | 1.10 | 35.10 | 6.00% | 35.74 | 8.27% |
| Liquefied petroleum gas by cylinder | 461.50 | 8.03 | 498.82 | 7.50% | 507.89 | 10.05% |
| Average increase for poor (Kerosene and LPG) | | | | 6.60% | | 8.98% |



Thank you!