Siep Società italiana di economia pubblica

WORKING PAPER
No 399
Gennaio 2005

TAX SYSTEMS AND TAX REFORMS IN SOUTH AND EAST ASIA: THAILAND

MARCO BARTOLICH

University of Trieste - Italy

JEL CLASSIFICATION: H20, H24, H25

KEYWORDS: Taxation, Tax Reforms, Thailand

società italiana di economia pubblica

dipartimento di economia pubblica e territoriale – università di Pavia

TAX SYSTEMS AND TAX REFORMS IN SOUTH AND EAST ASIA: THAILAND

by

Marco Bartolich

University of Trieste - Italy

Abstract
This paper is part of a wider research on South and East Asia countries' taxation, carried on at this Department, under the direction of L. Bernardi, A. Fraschini and P. Shome, and the supervision of. V. Tanzi. The aim of the paper is to describe and discuss the main features of Thailand's fiscal system and its recent and underway reforms. Firstly, the current structure of the system and its development from 1992 to 2002 is considered. The total fiscal pressure is relatively low (almost 17 percent) and is mainly constituted by tax revenue (social contributions are a marginal component). Indirect taxes are the main source of receipts (about 66 percent of the total), while direct taxation is still lowly developed, especially as to personal income tax. Then, the basic features of the main national and local taxes are depicted. The following section considers the distribution of the taxation charge among the main economic factors and its evolution during the last decade as to economic function and implicit tax rates. Consumption suffers from the highest fiscal burden, a common feature of developing countries. Finally, the paper examines the recent fiscal reforms enacted after the 1997 financial crisis, which was mainly faced with temporary fiscal stimulus' measures. However further reforms are still necessary, not only in the financial and fiscal sectors, to give more stability to Thailand's economy.

JEL Classification: H20 - H24 - H25
Keywords: Taxation, Tax reforms, Thailand
E-mail address: wili79@hotmail.com

Department of Public and Environmental Economics
University of Pavia – Italy
January 2005

1. Introduction, contents and main conclusions

The aim of this chapter is the discussion of the main features of Thai fiscal system, its development during the 1990s and the recent and underway reforms.

Paragraph 2 describes the structure of the tax system and its development during the last decade. Fiscal pressure is low if compared with industrialized countries and also with some less developed ones: it had an increasing trend until the financial crisis of 1997, when it fall by 2.2 percentage points on GDP. After the economic recovery, it started again to increase, but until now it has not reached the pre-crisis level yet.

Indirect taxation is the main source of receipts: it amounts to more than 60 percent of tax revenue, although recently the spread between direct and indirect taxes has somewhat decreased.

Personal income tax has a limited room as source of receipts, because of some structural weaknesses, while capital taxation does not go over a low value, which can explain the inflows of foreign investments during the last decades (together with the low cost of labor).

In paragraph three we examine the main taxes levied at central and local levels. Among direct taxes, personal income tax has many allowances and deductions which reduce the tax base. The brackets of income are eight, while the minimum and maximum rates are five and 37 percent respectively, and the first Baht 80,000 are exempt. Corporate income taxation is about at the same level as in the more developed countries. VAT is just the second main indirect taxes after the excises, also because its relatively low rate (7 percent).

Thailand has a highly centralized fiscal system: tax receipts of local governments are very low, despite the recent reforms, which are leading to a major fiscal decentralization. Hence central government's grants are the main financial resource for local authorities.

Paragraph 4 focuses the distribution of tax charge by analyzing the evolution of fiscal burden on the main components of national income (consumption, labor and capital & business) by economic function and implicit tax rates during the last decade. Consumption is the most heavily hit (at an average of 10.4 percent of GDP), while the taxation of labor and capital is comparatively low. This is usually considered as one of the explaining factors of the rapid economic growth of the last decades.

In the last paragraph we describe the fiscal measures taken as response to the financial crisis of 1997 and the main features of the 1999 Public Sector Management Reform Program, which had, among its objectives, the improvement of revenue collection and of tax burden's distribution as well as a progressive increase of fiscal decentralization. In the first phase of the crisis budget cuts were prevailing together with an increase of taxation, especially through indirect taxes, while in a second phase tax policy became more expansionary in order to reduce the social impact of the economic fall.

Among the aims of the Public Sector Management Reform Program there were the enforcement of tax collection, an increase in taxpayers' compliance, the improvement of information technology, a devolution of expenditure functions and a greater degree of tax autonomy at the benefit of local governments.

Many improvements should be taken, especially for the main taxes. VAT refunds should be redefined in order to reduce their costs, PIT's allowances and deductions must be simplified, while for corporate income tax the IMF suggests to avoid fiscal competition with other developing countries by lowering the tax rate and to reinforce the controls over corporations with international businesses, which try very often to repatriate dividends without paying taxes. Finally, some further improvements in fiscal decentralization should be taken in order to take advantage of all its benefits.

2. A broad view of tax system and its developments from the early 1990s

2.1 A short reminder of Thailand's economy and public sector outline

In 2002 general government's expenditure was 25.3 percent of GDP (without considering intergovernmental transfers), with an increase of 4.5 percentage points with respect to 2001. Central government's expenditure represents 90.3 percent of the total: this value indicates that Thai fiscal system is still highly centralized. Local governments' expenditure concerns mainly transport, housing and community amenities and general public services.

Central government's expenditure reflects Thailand's development priorities: public expense focuses on the sectors that are fundamental for country's development and growth. These sectors are agriculture, forestry, fishing and hunting (1.7 percent of GDP), transport (1.4 percent), health (1.8 percent, mainly for hospital services), education (4.2 percent, of which 2.8 for pre-primary and primary education), social protection (1.6 percent); less money is spent for social security and welfare and defense. Public debt transactions represent 1.3 percent of GDP.

These results can be explained by considering that after the 1997 crisis structural reforms became the priorities in order to create a solid ground for the economic recovery: education, health care and regional development have been considered the key sectors that would have led to an improvement of competitiveness, employment and economic growth. Current spending represents 60 percent and capital expenses 40 percent. Among the former, wages and salaries constitute 24.3 percent, a relative high value in international comparison, while in the second category capital transfers to public enterprises and households have strongly increased during last year and have caused the increase of expenditure and the deterioration of the general government overall balance.

In 2002 per capita GDP was 1,983 U.S. $ (not PPP corrected), while labor force was 54 percent of total population (IMF 2003). In the UN's 2004 Human Development Report, Thailand occupies the 76th place in the High Human Development rank, with a life expectancy at birth of 69.1 years, an adult literacy rate of 92.6 percent and a total fertility rate of 1.9 births for woman in the period 2000-2005. Infant mortality is still high (24 per 1,000 live births), despite a sharply decrease from 1970. For the period 2002-2015 the estimated annual population growth rate is 0.9 percent (it was 1.5 percent from 1975 to 2002). Aids is a serious problem in Thailand: the HIV prevalence is 1.5 percent of population between 15-49 years old.

2.2 The tax system

2.2.1 The current structure and its developments

In 2002 general government's revenues stay at 19.2 percent of GDP. Among them, direct taxes amount to 28.9 percent of total receipts, indirect taxes to 54.3 percent, other taxes to 0.4 percent, social contributions to 2.9 percent, non-tax revenues to 13.5 percent. In 2002, the fiscal pressure (*i.e.* tax revenues plus social contributions) was 16.6 percent of GDP: tax revenues were 16 percent, social contributions 0.6 percent. Direct taxes represent a lower fraction of tax revenues, 34.6 percent, while indirect taxes reach 65 percent.

Table 1 presents the fiscal pressure's evolution from 1992 to 2002 as percentage of GDP. During the past few years the quantitative spread between direct and indirect taxes has decreased, and the composition of the general revenues has slightly moved towards direct taxes, as the economy has passed from the early stages of modernization to a more sophisticated structure. Among direct taxes, corporation income tax constitutes 18.3 percent of tax revenues, while personal income tax represents only 12 percent, a low value in international comparison. This is mainly due to some structural weaknesses, like a narrow tax base (due to extensive exemptions, income deductions, allowances and tax relieves) and, more generally, to a non-transparent and unfair tax system (IMF 1998).

Social contributions amount to 0.6 percent of GDP: employees pay 46.2 percent of them, employers 52.6 percent, while self employed or non-employed contributions represent 1.2 percent.

Among indirect taxes, VAT plays an important role: it constitutes 18.5 percent of total tax revenue, despite the low VAT standard rate (7 percent). Excises are another important item of indirect taxes: in 2002 they totaled 27.2 percent of tax revenue. The most important were on petrol products, motor cars, tobacco and spirits. Finally, the third main category of indirect taxes is import duties (11.1 percent of tax revenues).

Thailand's fiscal system is highly centralized, despite recent reforms aimed to increase fiscal decentralization: central government collects 92 percent of tax revenues and pays 90.6 percent of general expenditure (including grants from central to local government units). Among central government's expenses, grants to local governments represent 7.4 percent (1.6 percent of GDP). These grants constitute 53.1 percent of local governments' total receipts; this high value emphasizes the important role of central government in the intergovernmental fiscal system.

2.2.2 The development of the system from 1992 to 2002

During the last decade, fiscal pressure shows an increasing path until 1996, the year before the financial crisis, when tax revenues and social contributions were 18.5 percent of GDP, and a deep fall until 1999 (15 percent). During the last three years fiscal pressure has grown again, but the 2002 level is lower then the average of the pre-crisis period.

Social contributions are increasing over all the period, while tax revenues, which have been strongly hit by the financial crisis, show the same path of the total fiscal pressure. Social contributions' weight in the fiscal pressure has constantly increased over this period: in 1992 it was 1.1 percent, in 2002 3.4 percent.

Among tax revenues, indirect taxes have always played the main role: they have totaled in the average the 66 percent of tax receipts, even during the crisis, albeit import duties decreased sharply because of the devaluation of the Baht and the consumption's shift from imports towards domestic goods. In fact, first fiscal measures of the central government during the financial crisis concerned indirect taxes (especially VAT) and caused a tax revenues' slight increase at the end of 1997 because of the growth of the indirect taxation's pressure, while direct taxation haven't been modified at that time. VAT had an increasing weight during the last decade: despite the low rate (actually 7 percent), its receipts amounted to an average of 20.7 percent of tax revenues during the 1990s, with a peak of 25.6 percent in 1998, after the 1997 VAT rate's increase from 7 to 10 percent, a fiscal measure which was introduced to accommodate the expected revenues' shortfall. Finally, excises are increasing during the decade (receipts have duplicated in ten years). They had a negative peak in 1998, when the central government implemented an expansionary policy (one of the measures was the reduction of some important excise duties).

Corporate income tax constitutes the main direct tax, with an average value of 18.7 percent of tax revenue, despite the sharp fall in 1998 (only 12.9 percent), when receipts decreased because of the high buoyancy of corporate income tax with respect to

GDP (on average 1.5 from 1965 to 1996) and the devaluation of the Baht (many corporations had net, short foreign positions). In the 1997-98 period, GDP decreased by 12 percent, which had highly negative consequences on corporate income tax receipts. Personal income tax always had a secondary weight in the mix of total tax revenue (about 12.6 percent as average value) because of the already mentioned structural weaknesses. This tax hasn't been hit by 1997 crisis as much as corporate income tax, because of its low buoyancy with respect to GDP: in 1998, personal income tax receipts were 0.6 percentage points higher than corporate income tax revenues as fraction of GDP. After the fiscal stimulus package's measures, its weight relative to total revenues has decreased.

In the last decade Thailand's fiscal system has presented few changes in its taxes' mix. Tax receipts were always dominated by indirect taxation. The economic growth has slightly shifted the composition of fiscal receipts away from indirect towards direct taxes, but direct taxation, especially personal income tax, still represents a low fraction of tax revenues.

Finally, as to fiscal decentralization, central government's share of total tax receipts has been high in the 1990s (an average 93.3 percent), despite a slight but constant decrease (94.7 percent in 1992, 92 percent in 2002). We can see the same evolution on expenditure side, where central government's share of total expenses (including grants from central to local government units) has moved from 91.4 percent in 1992 (but 92.6 percent in 1993 and 92.7 percent in 1994) to 90.6 percent in 2002 (an average 91.5 percent).

2.2.3 An international comparison

In this paragraph we compare Thai distribution of fiscal revenues (as percentage on GDP) with that of some selected countries: Vietnam, Japan, Hungary, Germany,

Table 1 Structure and development of fiscal revenue in Thailand as % of GDP, 1992-2002

	1992	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Direct taxes, of which	*5.6*	*5.8*	*6.3*	*6.6*	*6.6*	*6.2*	*4.9*	*4.9*	*5.2*	*5.4*	*5.5*
Personal income	1.8	1.8	1.8	2.1	2.3	2.3	2.5	2.2	1.8	1.9	1.9
Corporation income	2.9	3.4	3.8	3.8	3.8	3.3	1.9	2.2	2.8	2.8	2.9
On property	0.3	0.6	0.6	0.6	0.5	0.4	0.3	0.3	0.3	0.3	0.3
Indirect taxes, of which	*11.2*	*11.4*	*11.4*	*11.4*	*11.5*	*10.7*	*10.2*	*9.6*	*9.5*	*9.8*	*10.4*
VAT	3.9	3.3	3.6	3.1	3.7	3.2	3.9	3.2	3.2	3.2	3.0
Excises	3.9	4.2	4.2	4.1	4.0	4.1	3.6	3.9	3.7	4.0	4.4
Import duties	3.0	3.3	3.2	3.1	2.8	2.2	1.4	1.4	1.8	1.8	1.8
Other taxes	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
TOTAL TAX REVENUE	17.0	17.3	17.8	18.1	18.2	17.2	15.1	14.6	14.8	15.2	16.0
Social contributions	*0.2*	*0.2*	*0.2*	*0.2*	*0.3*	*0.3*	*0.2*	*0.4*	*0.6*	*0.6*	*0.6*
Employees	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.3	0.3	0.3
Employers	0.1	0.1	0.1	0.1	0.2	0.2	0.1	0.2	0.3	0.3	0.3
TOTAL FISCAL REVENUE	17.2	17.5	18.0	18.3	18.5	17.5	15.3	15.0	15.4	15.8	16.6
Administrative level											
Central government	15.9	16.1	16.5	16.8	16.9	15.5	13.5	13.0	12.9	13.1	13.9
Local government	1.1	1.2	1.3	1.3	1.3	1.7	1.6	1.6	1.9	2.1	2.1
Social Security	*0.2*	*0.2*	*0.2*	*0.2*	*0.3*	*0.3*	*0.2*	*0.4*	*0.6*	*0.6*	*0.6*

Source: own elaboration on Thailand Ministry of Finance data

Mexico, United States (Table 2). These countries have been chosen in order to see if, and how, Thailand's fiscal system is similar to other economic realities with different levels of development: Vietnam, Mexico and Hungary can be considered as still developing countries and hence they can present an analogous situation with Thailand (although Hungary has an higher level of economic growth and a more consolidated fiscal structure also because of its recent entering UE), while, by analyzing the cases of Japan, Germany and United States, we can compare Thai fiscal system with those of some industrialized countries.

Fiscal revenues as percentage on GDP in Thailand are similar to Vietnam's and Mexico's ones, but very lower than in Hungary, besides than industrialized countries. These differences are due to both tax revenue and social contributions.

By considering tax revenue, developing countries have a similar situation: indirect taxation is the main source of receipts, at an average of two thirds of the total, although Hungary is moving towards an imposition mainly based on direct taxes.

Among direct taxes, individual taxation is very lower in Thailand than in industrialized realities: because its structural weaknesses Thai personal income tax is a marginal fiscal revenue, while it is the first source of receipts in Japan and United States and the second in Germany. Indeed, social contributions percentage on GDP indicate that security system in developing countries is still underdeveloped (Hungary excepted, where social contributions have a relevant weight). These two features lead to the low fiscal burden on labor in Thailand.

Finally, the value of the capital income's taxation can be considered as one the main causes of the considerable foreign investments which have come to Thailand during the last decades (together with the low cost of labor) and have promoted one of the fastest economic growth among developing countries, especially in East Asia.

Table 2 Structure of fiscal revenues in selected countries as % on GDP in 2001

	Thailand	*Vietnam*	*Japan*	*Hungary*	*Germany*	*Mexico*	*United States*
Fiscal revenue	*15.8*	*n.a.*	*27.3*	*39.0*	*36.8*	*18.9*	*28.9*
Tax revenue	*15.2*	*16.6*	*17.0*	*27.5*	*22.2*	*15.7*	*21.8*
Social contributions	*0.6*	*n.a.*	*10.3*	*11.6*	*14.6*	*3.2*	*7.1*
Personal income	1.9	0.4	5.5	7.6	10.0	n.a.	12.2
Corporation income	2.8	5.6	3.5	2.4	0.6	n.a.	1.9
Tax on property	0.3	0.9	2.8	0.7	0.8	0.3	3.1
Tax on goods and services	9.8	9.7	5.2	15.1	10.6	9.7	4.6

Sources: own elaboration on Thailand Ministry of Finance data for Thailand, IMF 2003 for Vietnam, OECD 2001 for OECD Members.

3. Some quantitative and institutional features of the main taxes

3.1 Direct taxes

3.1.1 Personal Income Tax (PIT)

Personal income tax (PIT) is payable by resident and non-resident individuals. An individual is resident if s/he stays in Thailand for more than 180 days during the calendar year. Tax is levied on income from Thai sources and, for income from foreign sources, only on the portion that is brought in Thailand. A non-resident is subject to tax only on income from sources inside Thailand.

Taxable income (called "assessable income") is divided into the following eight categories: wages and salaries, income from jobs, positions or services rendered, income from liberal professions, income from construction and other contracts of work, dividends, interests, shares of profits, capital gains, income from leasing property, income from goodwill, copyright, franchise and other rights, other income from business, commerce, agriculture, industry, transport and other activities.

The main exemptions are: insurance policies, gifts and bequests, workers' compensation, insurance claims, medical benefits, proceeds from sales of immovable property acquired by bequest (these proceeds are included only if the sale is made for a commercial purpose).

For the income from employment is allowed a 40 percent deduction (but not exceeding Baht 60,000). Other deductions are applied for the different kinds of income.

The main tax allowances are: personal and spouse allowance (Baht 30,000), child allowance (Baht 15,000, a maximum of Baht 45,000 for family), education, life insurance premium, provident funds, estate, social insurance and charitable contributions.

Interest income and dividends can be excluded from the assessable income: in the first case, the taxpayer can choose for the withholding tax at a rate of 15 percent (certain forms of interest income are exempted from this tax, such as interest on bonds or debentures issued by a government organization). Dividends can be subject to a withholding tax at a rate of 10 percent; alternatively, the taxpayer can include them in her/his assessable income and claim for a tax credit, which is calculated according to the formula:

(Dividends)*(corporate income tax rate)/(1 – corporate income tax rate)

After the deductions and allowances, the income is subject to a progressive tax rate scale (the first Baht 80,000 are exempted) (Table 3).

For certain categories of income, the payer of income has to withhold tax at source, file tax return and submit the amount of tax withheld to the District Revenue Office. The tax withheld shall then be credited against tax liability of a taxpayer at the time of filing PIT return.

Table 3: Thailand PIT

Taxable income (Baht)	*Rate (%)*
0 to 80,000	0
from 80,000 to 100,000	5
from 100,000 to 500,000	10
from 500,000 to 1,000,000	20
from 1,000,000 to 4,000,000	30
over 4,000,001	37

Source: Thailand Ministry of Finance, Revenue Department

3.1.3 Corporate Income Tax (CIT)

Corporate income tax (CIT) is levied on Thai and foreign companies. In the first case, a company is incorporated under the law of Thailand and its net worldwide profits are subject to tax at the end of each accounting period. In the second case, a company is considered foreign if it is incorporated under foreign law and only its net profits arising from Thai source, or in consequence of business carried on in Thailand, are subject to CIT. A foreign company engaged in international transport is subject to tax on its gross receipts. Incomes received by foreign companies, such as service fees, interests, dividends, rents, professional fees, are subject to CIT on the gross amount received; the payer of the income pays a withholding tax which depends on the type of income and the status of the recipient. The withheld tax is credited against final tax liability of the taxpayer.

In the calculus of CIT, 50 percent of inter-corporate dividends is exempted; a fully exemption is applied if the recipient company is listed in the Stock Exchange of Thailand, but only if the shares are held three months prior to and after the receipts of dividends. The main deductions concern ordinary and necessary expenses (for Research&Development, job training and equipment for the disabled are allowed special deductions, 200 percent, 150 percent and 200 percent respectively), interests, taxes (except for CIT and Thai VAT), provident fund contributions, donations and depreciation (rates depend on the kind of assets). An initial depreciation of 40 percent is allowed for the purpose of encouraging investment. Net losses can be carried forward to five consecutive years.

The ordinary tax rate is 30 percent, but for small companies, with paid-up capital to less than Baht 5 million, a progressive tax rate scale is applied (Table 4).

For foreign companies many proportional tax rates are applied, which depend on the kind of business.

Table 4: Thailand CIT

Net profits (Baht)	*Rate (%)*
0 to 1,000,000	20
from 1,000,000 to 3,000,000	25
over 3,000,000	30

Source: Thailand Ministry of Finance, Revenue Department

3.2 Indirect taxes

3.2.1 The Value Added Tax (VAT)

Valued Added Tax (VAT) has been introduced since 1992 replacing Business Tax. It is charged on any person or entity that regularly supplies goods or services in Thailand and has an annual turnover exceeding Baht 1.2 million. Service has to be provided in Thailand if it is performed in Thailand regardless where it is utilized or, if it is performed in a foreign country, it is demanded to be utilized in Thailand.

VAT is imposed on the value added at each stage of the production and distribution: the tax liability is the difference between the "output tax" (i.e. the tax collected when goods or services are supplied) and the "input tax" (the tax collected on any purchase of goods or services; it includes any tax charged on imported goods).

The main exemptions are: unprocessed agricultural products and related goods, base services, such as transportation, healthcare, educational and professional services, renting of immovable properties, services in the nature of employment of labor, research and technical services and services of public entertainers, sales and import of newspapers, magazines and textbooks. Certain businesses are excluded and are subject to Specific Business Tax.

Tax base includes, for import goods, the C.I.F. price, import duties and any other taxes, if any, such excise tax and fees; for exported goods, it includes the F.OB. price and the eventual taxes (excise tax and fees).

Tax rates are:

- 0 percent rate: export of goods, services rendered in Thailand and utilized in a foreign country, goods and services supplied under international programs and agreements;
- 7 percent: any other goods and services subject to VAT.

Initially the ordinary tax rate was 10 percent; then it has been reduced to 7 percent to reduce the fiscal burden during the 1997 financial crisis.

Local governments receive 10 percent of total VAT revenues; the VAT receipts are collected for the Revenue Department by the Customs Department and allocated to all levels of local government.

3.2.2 Excise Taxes

Excise duties are collected by Excise Department: the collection is mainly made by means of excise stamps. Tax is imposed on specific goods and services: among them, we can mention liquors, tobacco, petroleum products, playing cards, non-alcoholic beverages, telephone and other services (entertainment places, golf, horse racing). In some cases, exemptions are allowed: for example, goods which are exported, deteriorated or damaged, donated to charitable organizations and services which donates the receipts to public charities. Tax rates may be: ad valorem (entertainment and telephone services, motor vehicles), specific (some petroleum products, playing cards) or whichever is greater (spirits, tobacco, non-alcoholic beverages

3.2.3. Customs Duties

Customs duties are collected by the Customs Department, which collects excise tax for the Excise Department and the VAT for the Revenue Department too. Tariff duties are levied on ad valorem or a specific rate base; in some cases, however, the tariff, which gives the most revenue, is applied.

Tax rates change frequently: the majority of goods imported by businesses is subject to rates ranging from 0 percent to 80 percent on the C.I.F. price. Specific duties are levied on certain commodities in the form of ad valorem (on the import duty) or specific tax rate.

Because of exporting promotion, most exported goods are exempted: only few items are subject to duty, including rice, rubber, raw hides and wood. Exemption is granted for goods covered by privileges according to international agreements, laws or treaties, for goods imported for personal use and for re-export.

The current tariff structure is undergoing to a reform, which includes lower tariff barriers and a reduced number of tax rates, as follows (Table 5):

Table5: Tax rates of the Customs Duties' undergoing reform

goods	*tax rate (percent)*
raw materials	1
intermediate goods	10
finished goods	10
protected goods	20
input cannot be produced in Thailand	1

Source: IMF 2003

3.3 Local taxes

Shared taxes are the most important tax receipts for local governments in Thailand. They include the VAT and selected excises. The surcharge is collected by the Revenue Department for the VAT and by the Excise Department for the selected excises and allocated to local governments. The surcharge is 10 percent of the total VAT and of the excise taxes.

The two most important taxes levied by local governments are the Land and Building Tax and the Local Development Tax. The central government determines the rate and the base of these taxes, while the local authorities collect them.

The Land and Building Tax is levied annually on buildings rented or used for other commercial purposes. Owner-occupied dwellings and buildings used by government, agencies, public hospitals, religious and educational institutions and buildings unoccupied for 12 months or longer are exempted. The tax rate is 12.5 percent of the annual rent received during the previous year. Inadequate databases, underreporting and evasion cause a low tax collection. Indeed the tax is disproportionately paid by low income households (unable to buy an own home) because often the owners of the rented dwellings pass along the tax to their tenants by increasing the rent or charging an annual payment in addition to the rent. There's a horizontal equity' violation too, because owner-occupied property is not taxed, while property occupied by the owner's immediate family is taxed.

The Local Development Tax is levied annually on the value of unimproved land not subject to the Land and Building Tax. Land occupied by owner or used for annual crops or owned by government agencies, public hospitals, schools, public utilities and religious organizations are exempted. 34 different rates are applied, ranging from Baht 0.50 per rai with an assessed value of under Baht 200 to Baht 70 per rai with an assessed value of over Baht 30,000 and Baht 25 per rai for each additional Baht 10,000 (one rai is equivalent to 0.16 hectare).

This tax presents some equity problems. First, public enterprises and owner-occupiers receive many local services, but they don't pay for them because they are exempted from the Local and Development Tax. Second, the tax is regressive because the rates decrease as the value of the property increases.

Another important local tax is the Real Estate Transfer Tax. Transfer of real estate (by sale, gift or succession at death) is taxed on the base of the assessed value of the property at the tax rate of 2 percent (0.5 percent if the transfer is made to parents, spouses or children). The same tax is applied by the central government (in this case some exemptions and deductions are allowed).

4. The distribution of taxation charge

The analysis of the distribution of tax charge by economic function can be used in order to see how the main direct and indirect taxes are levied on productive factors and main employment of the economic system and, hence, to analyze the impact of taxation on resources' allocation, because the tax burden has to be considered as part of the relative factor prices. Usually, the study is focused on three main items: consumption, labor and capital & business. The three indicators are obtained by using, as numerator, indirect taxes (general and specific), social contributions and direct taxes paid by employees, taxes on capital (corporation income tax included) respectively, and, as denominator, GDP. By this way one can understand the weight of taxation on the three main economic components of national income as percentage of the gross domestic product.

During the last decade, consumption's taxation shows an increasing trend until 1997, when the fall of tax receipts began because of the overall crisis. Indeed, consumption's taxation has registered a decrease due to the reduction of the VAT rate in 1999 (from 10 to 7 percent), one of the temporary measures taken in order to stimulate the economic recovery. Only in 2001 the weight of consumption's taxation started to raise again.

Labor's taxation is just a small percentage on GDP because of two main factors: the structural weaknesses of the personal income tax and the poor development of the social security system, which causes the low weight of social contributions on GDP (on average 0.35 percent).

Capital & business' taxation was strongly hit by the 1997 crisis, which exploded in the financial sector. Because of its high buoyancy with respect to GDP, corporate income tax fall from 1997 to 1998 by 43 percent, but taxation on financial and capital transactions had a deep decrease too (-46 percent).

Another important indicator of the distribution of tax charge is the implicit tax rates. There are many definitions and methods of computation of these rates, which can lead to different values. As a rule, the three main indicators (implicit tax rates on consumption, labor and capital & business) use, as numerator, the same values for the distribution of tax charge by economic function, and, as denominator, three economic aggregates taken from the national account statistics: private consumption, compensation of employees, gross (or net) operating surplus.[1] These rates can be considered as macroeconomic indicators of factor tax loads.

Consumption's tax burden is very high in comparison with that levied on labor, despite a gradual reduction from 1992 to 2002 (-2.1 percent) due exclusively to the decrease of tax receipts (private consumption has yearly increased in this period, 1997-98 biennium excepted). This result indicates that Thai economy is still mainly based on indirect taxation (a common feature of developing countries).

The implicit tax rate for labor is relatively higher during the crisis then before and after it. This result is due to the PIT, which reaches a peak in 1998, while social contributions have a slightly increasing trend. Table 6 shows the two groups of indicators for the period 1992-2002.

[1] Because of the lack of detailed data, the computed indicators have to be considered as approximated measures of tax distribution by implicit tax rate. Indeed, due to the lack of data on the operating surplus the implicit tax rate for capital & business could not be created.

Table 6 - Structure and development of taxation by function and by implicit tax rate in Thailand, 1992-2002

	1992	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Economic functions											
Consumption	10.7	11.1	11	11	11.2	10.8	10.2	9.4	9.3	9.7	10.2
Labor	2.0	1.9	2.0	2.2	2.5	2.6	2.8	2.5	2.3	2.4	2.5
Capital & Business	3.5	3.7	4.1	4.2	4.0	3.7	2.2	2.5	3.2	3.2	3.4
Implicit tax rate											
Consumption	20.2	20.3	20.2	20.5	20.8	19.7	18.6	16.7	16.6	17.0	18.1
Labor	5.8	5.4	5.9	6.2	7.1	7.2	7.2	6.7	6.2	6.5	6.7

Source: own elaboration on Thailand Ministry of Finance data

5. Tax reforms

5.1 A quick glance at macro economic and budget outlook

In 2002 the GDP growth rate of Thailand was 5.2 percent, the best performance after the 1997 crisis. Private consumption and investment gave the major contribution to this result: thanks to growing consumers' confidence and credits, high increase of farm income, low interest rates and a supportive government policy, private consumption grew by 4.5 percent, especially in the sectors of automobiles, mobile phones, telecommunication services, televisions, while private investment rose by 8.6 percent, with a decreasing inflow of foreign direct investments, although their level was still high. Residential construction, purchase of commercial vehicles and office equipment registered the highest inflow of new investments (IMF 2003).

Exports of goods and non-factor services grew by 2.1 percent, with China and ASEAN (Association of Southeast Asian Nations) countries as main trade partners. Manufactured products (semi-conductors, radio and television receivers and parts, video recording, automobiles and parts, steel, plastic and chemical products) have been the first source of the export volume's growth, while natural rubber was the main agricultural export product (IMF 2003).

Inflation decreased from 1.7 percent in 2001 to 0.6 percent in 2002 and unemployment rate continued to fall, from 3.3 to 2.4 percent, following the trend begun in 1998. Agriculture's share in GDP was 9.9 percent, while manufacturing (including construction) and services (commerce, transport and communication, financial and other services) were 39.6 and 50.5 percent of GDP respectively. In 2002 labor force by occupation presented the following composition: agriculture 41.6 percent, manufacturing 23.1 percent and services 35.3 percent (IMF 2003).

In 2002 Thailand's fiscal system registered a general government overall balance in deficit for an amount equal to 6.6 percent of GDP, a value in line with the negative trend that began in 1997, the financial crisis' year. This negative result is mainly due to the sharp increase of expenditures (+30.6 percent); the ratio between general revenues and GDP decreased because GDP grew more than total revenues. In comparison with 2001, the expenditure as a proportion of GDP has increased by 5.1 percent: while the main expense categories have slightly increased (salaries and wages, goods and services, interest payment, grants) or have decreased (social benefits), capital transfers to public enterprises and households have signed a strong increase, which has caused the 5.1 percent increment of the incidence of expenditure on GDP (Thailand Ministry of Finance).

Public debt was equal to 55.1 percent of GDP, the lowest value after the 1997 crisis; by comparison with 2001, it has decreased by 2.8 percent (as a proportion of GDP), and this reduction is mainly due to the decrease of non-financial public enterprises' debt (-2.2 percent as fraction of GDP)(IMF 2003).

Thanks to increasing export growth and relatively weak US dollar, Thailand registered a current account surplus, in line with the post-crisis trend, and the external debt stock continued to decrease, as consequence of the government's efforts to reduce its multilateral loans (World Bank, IMF, Asian Development Bank).

5.2 Tax reforms of last years, underway and planned

In order to face the financial crisis, after the Baht devaluation Thai authorities implemented fiscal measures necessary to reduce the effects of the economic decrease and to promote the recovery.

From July 1997 to February 1998 budget cuts and revenues measures have been taken to accommodate an expected revenues' shortfall, to reduce current account deficit and to produce a budget surplus of 1 percent of GDP. FY98 budget was cut from Baht 982 to 800 billion, while VAT rate was raised from 7 to 10 percent and selected excise taxes and import duties were increased, primarily on luxury consumption goods.

In a second phase, fiscal measures were taken to reduce the social impact of the crisis and to stimulate the economy. Because of some difficulties and constraints on expenditure side, the government began an expansionary policy on revenues side. VAT rate passed from 10 to 7 percent and the 1.5 percent VAT on gross revenues for small enterprises with sales between Baht 600,000 to 1,200,000 was eliminated. Personal income tax relief was provided to all taxpayers, but particularly low-income earners, by exempting from tax the first Baht 50,000 of net income (Baht 80,000 since 2003).

Further measures to reduce the tax burden were introduced in August 1999 through selected excise taxes' and import tariffs' reductions and accelerated depreciation of fixed assets, targeted to provide investment incentives, and the postponement of corporate income tax payments and remittances from State-Owned Enterprises, in order to alleviate liquidity constraints in private and public sectors.

Under the influence of the 1997 new Constitution, promulgated after the financial crisis, in May 1999 the government launched the three-year Public Sector Management Reform Program. Among the main objectives of this reform there were an improvement of revenues' collection, a more equitable distribution of the tax burden and an increasing fiscal decentralization.

To achieve the first two objectives, the tools of the Revenue Department were: a strengthening collection enforcement, an increasing taxpayer compliance and an improvement in information technology. During the crisis, tax debts increased strongly (from 0.7 percent of GDP in

1996 to 2 percent in 1999): as consequence, in 1999 collectible debt was 9.3 percent of total tax collections, but thanks to the Public Sector Reform Loan program (a US $ 400 Million loan from the IMF) this percentage was reduced to 6 percent in 2001. A Debt Collection Management Division has been created with the following functions: preparing a 3-year debt reduction plan, setting collection targets for each office of the Revenue Department, developing new enforcement procedures and monitoring debt collection performance. Indeed, more resources have to be allocated by the Revenue Department for debt collection activities.

Another consequence of the crisis was an increase in non-compliance, both in formal sectors, where registered taxpayers have many incentives to understate their income and over-claim expenses, and in informal sectors, where a weak business registration permits to many street vendors to evade. The main actions underway to improve taxpayer compliance are: a tightening of the rules regarding VAT refunds, the development of automated systems for the VAT refund and for the audit case selection, the reduction of taxpayer compliance costs, the simplification of excises taxes' and VAT's forms, a support to the Large Business Tax Administration Office in managing the largest taxpayers, tighter control over marketplaces and street vendors, a strengthening of requirement for business registration and an increase of registered VAT taxpayers.

Finally, the 1997 crisis evidenced the difficulties of the institutions in formulating and implementing tax policy. These difficulties were due especially to the lack of information, revenues' data and other statistics that were necessary for the Revenue Department to formulate forecasting models and predictions of the impact of tax changes. Recently, the responsibility for determining tax policy has been transferred from the Revenue, Customs and Excise Departments to the Fiscal Policy Office. The main tasks underway are the creation of a functional and integrated computer system for the Revenue Department, the implementation of on-line taxpayer registration and automated audit case selection systems, the development of modules for debt management and the creation of data entry, processing and reporting schedules for all taxes.

Increasing fiscal decentralization was another main scope of the 1999 reform. The 1999 National Decentralization Act introduced changes in the local and central governments' roles and in their fiscal and administrative relations. First, it specified a gradual four-year devolution of administrative competences in order to define the expenditure functions of local and central governments and to avoid overlapping functions. Second, it aimed to increase local authorities' revenues to 20 percent of total government revenues by 2001 and to 35 percent by 2006. Some national tax bases have been shifted to local governments, such as mineral resource tax, land registration fees, gambling tax, underground water fees, bird net tax, but the receipts have registered just a little increase. With the introduction of two local shared taxes, VAT and excise taxes, local tax revenues have increased sharply in the period 2001-2002. Indeed, local grants have increased in the same period (+75 percent in 2001 and +170 percent in 2002 from 2000). Most of these grants were specific grants allocated through national government departments, in contrast with the principles of fiscal decentralization: in fact local authorities don't have full discretion in using these funds. An objective of the reform was a redefinition of intergovernmental transfers, by passing from specific to general-purpose grants allocated through a more transparent system. Finally, underway reforms concern the promotion of responsible local borrowing (the Regional Urban Development Fund has been recently created in order to channel credit to projects of creditworthy local governments) and the enhancement of local accountability.

5.3 Suggestions for further improvements

Since 1997 The IMF has suggested some measures necessary to improve Thailand fiscal policy and tax administration. These measures concern particularly revenues' collection and fiscal decentralization.

An increase of tax receipts is indispensable to reduce budget deficit, especially because a raising proportion of the budget will go towards mandated expenses, such as wages and salaries, payment on public debt and specific grants allocated to local governments.

Some changes have been suggested for VAT, excise taxes, Personal Income Tax and Corporate Income Tax. For the indirect taxes, VAT rate could be raised to 10 percent, while the excise taxes should be increased, especially on beer and tobacco, petroleum products and motor cars. Indeed, VAT refund represents a strong inefficiency in the VAT collection. The monthly refunds require significant resources spent on this task and a proportional number of staff. In 1998 and 1999, 60 percent and 42 percent of audits were for VAT refunds. Legal procedures and measures that reduce these administrative actions and the risk of fake invoicing should be taken: among the options, VAT refund rights could be limited or the tax administration could shift the VAT subject from the seller to the buyer, by forcing a partial or total withholding pre- payment in certain transactions where tax evaders are involved, or VAT pre-payment could be applied for sales of certain goods to risky retailers in order to shift the VAT subject and prevent tax evasion. Finally, a minimum amount for tax refund could be introduced.

A general redefinition of allowances and deductions should be introduced in order to improve PIT's horizontal equity and to simplify the withholding tax rate's computation. Targeted exemptions, specific sector-based allowances and the lack of automatic adjustments of brackets and monetary allowances necessary to avoid inflation's effects are the cause of the low progressivity of the rate structure. Some deductions, such as that of 40 percent for income from employment against that of only 30 percent for income from professional income, appear illogical, while the many tax allowances should be simplified and redefined for appropriateness. Finally, the need for employees in many cases to file tax returns should be eliminated, in order to make the PIT a withholding system.

The two major problems concerning corporations are the tax rate and the possibility for corporations having international business to avoid taxes on dividends. In the first case, the IMF suggests that the tax rates should not be too low in order to attract foreign investments, because there could be a net transfer of capitals from poor countries to rich ones. For the second problem, it suggests a reinforcement of the controls over the corporations with international business, because they try very often to repatriate dividends without paying taxes. The mechanisms used are thin capitalization, overpayments of royalties and intangible assets and over-invoicing of imports. Against them, a reduction of options for hidden equity capitalization, anti-avoidance rules and high penalties associated to a strong coordination between Revenue and Customs offices should be applied.

In order to increase tax administration's efficiency, some improvements have been recently introduced, such as the "Large Taxpayers Office" and the computerization of tax-paying system, but others are still necessary. The priorities concern a more effective coordination between the different departments of the Ministry of Finance and the third-party obligations for providing information and collection of taxes.

The other field where the IMF has made some suggestions is fiscal decentralization. According to the 1999 National Decentralization Act, in 2006 local authorities' revenues will raise up to 35 percent of the total revenues. In order to take advantage of all the benefits of fiscal decentralization, local governments have to increase their financial management, to improve the technical skills indispensable to decentralized functions, to strength accounting and financial reporting and to plan efficient programs for the use of the resources. Collaboration between local governments in providing some public services should be supported when a single small-size government cannot do it efficiently. Finally, an increasing cooperation between central and local governments is necessary to minimize and avoid duplication of functions.

References

International Monetary Fund (2000). *Thailand: Selected Issues*, IMF Staff Country Report, 00/21, Washington, D.C., The International Monetary Fund, March.

International Monetary Fund (2001). *Thailand: Selected Issues*, IMF Country Report, 01/147, Washington, D.C., The International Monetary Fund, August.

International Monetary Fund (2004). *Thailand: Selected Issues*, IMF Country Report, 04/1, Washington, D.C., The International Monetary Fund, January.

International Monetary Fund (2002). *Thailand: Selected Issues and Statistical Appendix*, IMF Country Report, 02/195, Washington, D.C., The International Monetary Fund, September.

International Monetary Fund (1998). *Thailand: Statistical Appendix*, IMF Staff Country Report, 98/119, Washington, D.C., The International Monetary Fund, November.

International Monetary Fund (2000). *Thailand: Statistical Appendix*, IMF Staff Country Report, 00/20, Washington, D.C., The International Monetary Fund, February.

International Monetary Fund (2001). *Thailand: Statistical Appendix*, IMF Country Report, 01/155, Washington, D.C., The International Monetary Fund, September.

International Monetary Fund (2003). *Thailand: Statistical Appendix*, IMF Country Report, 03/388, Washington, D.C., The International Monetary Fund, December.

Mukul G. Asher, Ramkishen S. Rajan (1999). *Globalization and Tax systems: Implications for Developing Countries with Particular Reference to Southeast Asia*, No. 99/23 Centre for International Economic Studies.

OECD (2002), *Revenue Statistics 1965-2001*, Paris, OECD, October.

The World Bank Group (1999). *Thailand Economic Monitor*, Bangkok, The World Bank Thailand Office, October.

The World Bank Group (2000). *Thailand Economic Monitor*, Bangkok, The World Bank Thailand Office, February.

The World Bank Group (2000). *Thailand Economic Monitor*, Bangkok, The World Bank Thailand Office, December.

The World Bank Group (2001). *Thailand Economic Monitor*, Bangkok, The World Bank Thailand Office, July.

The World Bank Group (2004). *Thailand Economic Monitor*, Bangkok, The World Bank Thailand Office, April.

United Nations (2004). *Human Development Report 2004*, New York, United Nations.

Web Sites

Asian Development Bank. http://www.adb.org

Bank of Thailand. http://www.bot.or.th

International Monetary Fund. http://www.imf.org

Ministry of Finance Thailand. http://www2.mof.go.th

National Economic and Social Development Board (NESDB).http:// www.nesdb.go.th

National Statistical Office Thailand. http://www.nso.go.th

OECD. http://www.oecd.org

The World Bank Group. http//www.worldbank.org

United Nations. http://www.un.org