Fiscal Policy and Tax Reform in Taiwan – by Minister Mr. Shsh-Der Lee (2010/01/26)

1. Introduction

In this article I would like to illustrate the fiscal policy and tax reform in Taiwan, and I hope that this will enhance public understanding of the role that the Ministry of Finance plays in our economic system.

2. Fiscal Policy

First, I would like to give an overview of our government finance and fiscal policy, and then of our operations and major fiscal measures.

2.1 Overview of Government Finance

As Figure 1 shows, GDP in 2009 was about NT$12 trillion. About 61% was derived from private consumption, 17% from the government and private investment, 13% from current government expenditure, and 9% from net exports.
As the need for public services has grown, the scale of government expenditure and that of the fiscal deficit have increased, so the fiscal condition has become more difficult year by year and the improvement in the revenue structure has been required to counter this difficulty. As Figure 2 shows, the growth in tax revenues is related to economic growth.
Nevertheless, as the functions of government have expanded, the fiscal deficit has often been larger than the surplus and so the accumulated fiscal surplus has declined year by year.
Figure 3: Annual Fiscal Surplus or Deficits of the Central Government (Final Accounts)

-104.2, -201.8, -144.4, -72.3, -28.3, -8.1, -26.2, -118.6, -142.5, -247.2, -297.2, -196.6, -102.5, -26.2, 168.4, 64.7, 16.6, 83.5, 23.2

Figure 4: Yearly Changes in Fiscal Surplus of Central Government (Final Accounts)

NT$ billion

1997: 199.7, 107.4, 78.3, 69.5, 100.1, 93.5, 209.6, 208.3, 201.0, 129.2, 99.8, 97.2, 72.1, 35.7


*Estimate
But the balance is restricted by the Public Debt Act, whereby outstanding central government debt shall not exceed 40% of the average GNP of the last three fiscal years.

In order to finance insufficiencies in capital expenditure, the outstanding debt increased year by year, but the surplus from the special funds provided to the national treasury has contributed to a decrease in the deficit. And so, although the growth of annual revenues is closely related to changes in the economic situation, a modest growth in tax revenue was recorded in the long-term. However, as expenditure has grown at a more rapid pace, outstanding debt has continued to accumulate. And, to sum up, the fiscal condition is deteriorating somewhat and the fiscal structure needs to be improved.
2.2 Overall Framework of Fiscal Policy

The overall framework of our fiscal policy is to support the new blue print of our economy and to achieve the ideas of economic growth, social justice, and a sustainable environment.

Hence we have planned nine strategies for use in the corresponding aspects, such as expansion of domestic demand (12 construction projects), improvements in tax efficiency and equity, and energy saving & reductions in carbon emissions. The vision of the Ministry of Finance is to ‘support construction with public finance, raise public finance with construction,’ and thus
we are devoted to building a positive cycle among government finance, sources of finance, construction, and taxes, charges & fees. Our core tasks are financial, tax and national property management, and the ideas of our new economic blue print can be achieved through the creation of more sources of finance, higher efficiency, and the provision of better services. It is everyone’s responsibility to aid in the expansion of sources of finance, it requires the participation of all of the people to improve efficiency, and great efforts have to be exerted to produce a better quality of service. We have also set up three strategies to utilize in the accomplishment of these missions: the planning of overall government finance, the consolidation of social consensus, and the strengthening of public and private cooperation, and these strategies could be smoothly carried out through the use of ‘fast reaction, action, and growth’ and ‘change in concept, attitude, and approach.’ The vision will be successfully achieved if the functions of the work are well-divided, work is completed according to schedule, action is taken only after careful planning, and the staff is united.

2.3 Operation of Fiscal Policy

We have integrated the operation of our organization to market our core business to different target groups. And we are trying to reform the fiscal scale, structure, revenues and expenditures through the use of efficient financial operations and improvements in local finance. And under the four
principles of tax management, we are providing better tax administration services and a more competitive tax system. The major tasks of management on the state-owned real estate property are to improve the use and development of national property. And for government shareholdings, the object of our management is to create “shareholder-customer-staff” 3-wins investment.

2.4 Major Fiscal Measures under Implementation

The major fiscal measures under implementation have helped greatly in dealing with the financial problems that we have faced since 2007. ‘The Program for Strengthening Local Construction to Expand Domestic Demand’ allows for the raising of financial resources and for the provision of subsidies to local governments during periods of construction. We have also stabilized current prices through the lowering & freezing of administrative fees, the lowering of import tariffs, and by allowing for reductions in commodity & business taxes. The benefits of this action plan have been significant. Measures of the ‘Economic Vitalization Package’ for financial tsunami of 2008, such as the reduction of commodity tax for new motor vehicles, the granting of a five-year tax exemption for certain types of investment, and the lowering of business, individual, estate and gift tax, have all contributed to the revitalization of our economy and to the enhancement of the fairness of the tax system. Other measures such as the release of consumer
vouchers, and the expansion of investment in public construction have greatly benefited employment, urban regeneration and economic prosperity. The deregulation of certain laws has allowed for the relaxation of certain limitations and for the streamlining of procedures has brought convenience and saving in costs to the public. There are still many other important reform measures such as simplification of customs clearance procedures, review of customs control measures on goods imported from Mainland China, etc. And these strong policy responses have not only helped us in combating the global recession but also in reinforcing the foundations of the economic system.

2.5 Current Major Fiscal Works

Following is the introduction of our current major fiscal work. ‘The Program for Improving the Efficiency of Government Finance’ is mainly for saving, looking for, and making money in order to improve our fiscal situation. ‘The Program for Strengthening the Management of Government Shareholdings’ provides for fairer and more market-oriented governance and management for government shareholdings. Through ‘The Program for Assisting Local Government Finance’ and by amending the related laws, local governments will improve their finances and get assistance in raising their efficiency in the handling of financial matters. ‘The Program of Customs Innovation’ concerns security and efficiency at the same time. In
‘The Program for Strengthening the Management of National Property’, measures such as complete registration of ownership, the handling of illegally occupied national property, and enlivening the utilization of property will improve the management efficiency. And the development of large-sized national land may bring numerous investment and job opportunities through BOT, BTO, ROT, BOO or OT.

3. Tax Reform

Now we turn to a continuing task: tax reform. Firstly, I will provide a briefing on the current status and problems of our tax system, and then show our progress and the major tasks of current tax reform.

Currently, there are 17 tax items in Taiwan, including national and local taxes. And an annual total of about 110 million tax cases are handled in Taiwan. But while total tax revenues have been growing in recent years from NT$ 1,257.8 billion of 2001 to NT$ 1,518.9 billion of 2009, and the ratio of direct tax has also been rising from 40% of 1980s to over 60% of 2009, total tax revenues as a percentage of GDP (usually known as the ‘tax burden’) first declined from 17.0% in 1990s to bottom of 11.7% in 2003 and then have only slowly increased to 13.9% of 2008. Unfortunately, it might reduce to below 13% in 2009 due to tax revenue shortage from international economic recession of financial tsunami.
Figure 7: Total Tax Revenues in Recent Years

Figure 8: Comparison Between the Ratio of Direct Taxes and Indirect Taxes in Recent Years
However, the tax burden is still quite low in Taiwan compared with other key countries.

Table 1: Total Tax Revenues as Percentage of GDP of Key Countries

<table>
<thead>
<tr>
<th>Year</th>
<th>ROC</th>
<th>USA</th>
<th>Japan</th>
<th>Korea</th>
<th>U.K.</th>
<th>Singapore</th>
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<tbody>
<tr>
<td>2002</td>
<td>11.8</td>
<td>19.6</td>
<td>16.2</td>
<td>19.8</td>
<td>29.4</td>
<td>13.6</td>
</tr>
<tr>
<td>2003</td>
<td>11.7</td>
<td>18.9</td>
<td>15.8</td>
<td>20.4</td>
<td>28.9</td>
<td>12.8</td>
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<tr>
<td>2004</td>
<td>12.2</td>
<td>19.2</td>
<td>16.4</td>
<td>19.5</td>
<td>28.9</td>
<td>12.2</td>
</tr>
<tr>
<td>2005</td>
<td>13.4</td>
<td>20.6</td>
<td>17.3</td>
<td>20.2</td>
<td>29.5</td>
<td>12.5</td>
</tr>
<tr>
<td>2006</td>
<td>13.1</td>
<td>21.3</td>
<td>17.7</td>
<td>21.1</td>
<td>30.3</td>
<td>13.0</td>
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<tr>
<td>2007</td>
<td>13.4</td>
<td>…</td>
<td>…</td>
<td>…</td>
<td>…</td>
<td>14.3</td>
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<tr>
<td>2008</td>
<td>13.9</td>
<td>…</td>
<td>…</td>
<td>…</td>
<td>…</td>
<td>14.6</td>
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<tr>
<td>2009</td>
<td>12.2</td>
<td>…</td>
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</tr>
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Notes: The tax burden ratios in this table exclude social security contributions.
3.2 Current Taxation Problems

Current taxation problems are viewed with respect to adequacy, efficiency, tax administration, and equity. Tax revenues are inadequate to meet expenditure because the tax burden is too low and the increasing number of tax deductions and exemptions has eroded the tax base. Different tax treatments for salaried and non-salaried income, or for high-tech and traditional industries have also led to problems of equity. Tax deductions and exemptions have caused distortion in the allocation of resources and also a loss of efficiency. The problems of tax administration such as complicated procedures of tax declaration are still in existence. Difficulties in the computation of exempt income, sharing of costs and expenses, identification of income category, and disputes in taxation have all made the operation of the tax system more complex.

3.3 Aims in Tax Reform

The current directions of tax reform are to promote economic development, pursue social justice, improve international competitiveness and maintain a sustainable environment. We established a commission and an advisory council to promote tax reform. Different viewpoints are fully exchanged during numerous meetings, seminars and sessions. And the current tax reform project is set to achieve the objectives of enhancing efficiency, widening the tax base, and streamlining tax
administration. First, we firmly established the goal and visions of tax reform to lead the direction of the follow-up work. As for income tax, issues like earned income tax credits, implementation of tonnage tax, and the anti-avoidance system etc., had been carefully reviewed. The estate & gift tax system, and exemptions or reductions of land and house tax also had been studied. We are researching the introduction of a green tax and necessary modification of the business tax for a sustainable environment. There are also studies on tax problems of special economic zones and capital gains so as to increase our taxation competitiveness. Tax administration is being streamlined in order to provide the public with more convenience. And we also pay great attention to the protection of taxpayers’ rights.

3.4 Progress in Tax Reform

We have completed 20 study items and the results have been fruitful. Certain articles in income, estate and gift laws have been amended and some are still in progress. For instance, the rates of individual income tax have been reduced from 6%, 13% and 21% to 5%, 12% and 20% since 2009, and the estate tax rate has been reduced and simplified to a flat tax rate of 10% from a multiple tax rate schedule which the highest tax rate is 50% since 2009. Many measures have been taken to streamline tax administration and reduce tax litigation.
3.5 Major Tasks of Current Tax Reform

By reforming the tax system and administration, the tax environment has become fairer, more reasonable and competitive. And the modernization of our taxation information system is making our service faster, more efficient and professional.

4. Conclusions

The operation of the business cycle easily brings about fiscal imbalance. It is hard to achieve an annual balance at a time when the government is responsible for providing counter-cyclical measures to stabilize economic shocks, but we also try our best to maintain long-term fiscal responsibility. The responsibility of the Ministry of Finance is to manage overall fiscal affairs to promote national development. By setting up a complete system and cultivating our manpower, and handling our core business through systematic and organizational operation, we seek for excellence and higher quality, and make our fruitful results known to the public. Last but not least, The Ministry of Finance is always dedicated to the service of the people. Our job is like a relay race; our elders did their best and passed the responsibility on to us, we will try our best in turn and then pass our task on to the next generation in an unending process, like a wheel that never stops.