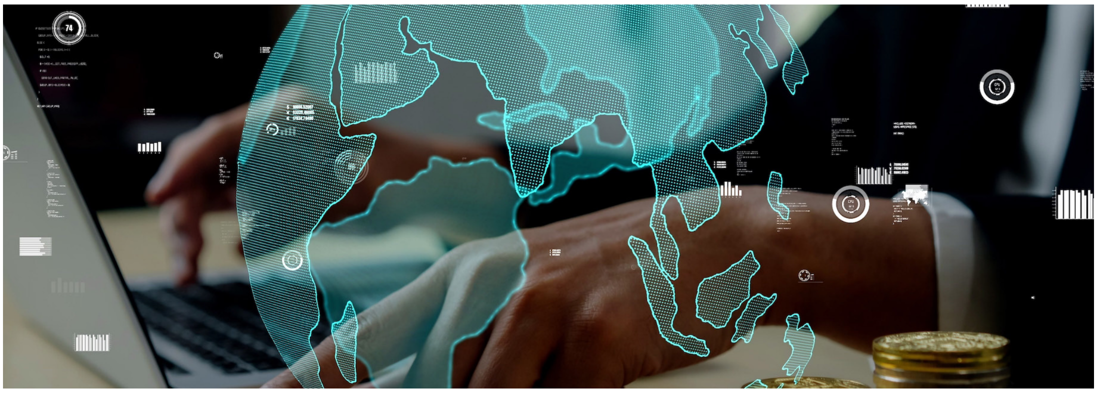
P R A K A R S A *Policy Brief*

October 2023

Wealth Tax to Fight Asymmetrical Distribution of Tax Burden



Key Points:

- Tax payment asymmetry refers to the unequal distribution of the tax burden among different economic groups, namely the working class, especially those in the formal sector, who are subject to high tax rates. At the same time, HNWI's passive sources of revenue are taxed at lower rates.
- Taxing wealth can distribute income equality and supplement existing tax types, mainly for high-net-worth individuals who may have significant passive income sources. Wealth tax potential revenue is estimated at US$ 8.18 billion (Indonesia), US$ 2.28 billion (the Philippines), and US$ 3.09 billion (Vietnam).
- The government and parliament of Southeast East Asian countries should draw up a policy on wealth tax and increase the tax rate on passive income sources, and impose a tax on untaxable sources of income such as inheritance.

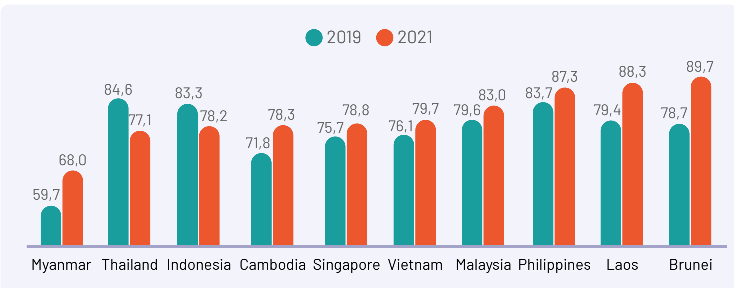
Income and wealth inequality have been a growing concern

Income and wealth inequality have risen in many countries over the last three decades. About 71% of the global population lives in countries with increased income inequality (UN, 2020). Despite progress in some regions, income and wealth are increasingly concentrated at the top ladder of the income group. Since the 2008 financial crisis, the number of billionaires worldwide has nearly doubled. In 2018, the 26 wealthiest people in the world had as much wealth as half of the world's population.

There are shreds of evidence that there is a global trend towards the accumulation of wealth and income and, as a result, increasing inequality. In Southeast Asian countries, the bottom half of the population only possess 10-15% of income shares. At the same time, 10% of the population earns 55% of the shares (Chancel et al., 2022).

The COVID-19 pandemic has worsened inequality in Southeast Asian countries. Wealth inequality, which is much more unequal than income, has increased after the pandemic (Chancel et al., 2022). This condition is illustrated by the value of the Gini index in 2021, which is trending upwards (Credit Suisse Research Institute, 2022).

Figure 1. Gini Index in Southeast Asian Countries



Source: Credit Suisse Research Institute (2019, 2022a)

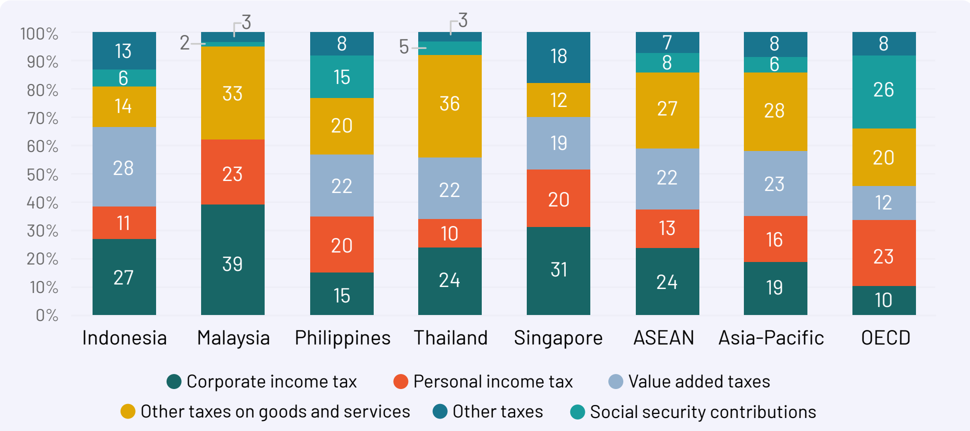
While billionaires' wealth soared rapidly during the pandemic -as businesses in food, pharmaceuticals, energy, and tech sectors have cashed in, millions of people worldwide faced a cost-of-living crisis due to the continuing effects of the pandemic and the soaring costs of essentials, including food and energy. Therefore, inequality, which was already extreme before COVID-19, reached a new level. So far, no measures truly tackle this kind of increase in inequality (Oxfam, 2022).

Taxation policies are still unfair

Oxfam, in its report, explains that decades of neoliberal economic policies have ripped away public services into private ownership and have encouraged the move toward massive concentration of corporate power and tax avoidance on a vast scale. These policies have contributed to a deliberate undermining of labor rights and a reduction in corporate and wealthy tax rates. These policies have also enabled the environment to have much higher levels of exploitation than our planet can sustain (Oxfam, 2022). The State of Tax Justice 2021 report also found that annual tax losses of US$ 483 billion worldwide are lost to tax havens.

At the same time, the world is losing US$ 171 billion in tax annually to offshore wealth tax evasion related to financial wealth alone, and US$ 312 billion is lost to cross-border corporate tax abuse by multinational corporations (Tax Justice Network, 2021). Furthermore, the ASEAN countries still depend much on regressive taxes for their tax revenues. Contributions from Value Added Tax (VAT) and Sales Tax in ASEAN countries are dominant, although these taxes tend to be regressive and unfair to low-income households.

Figure 2. Tax structures as a percentage of total tax revenue 2020 (%)



Source: "Revenue Statistics - Asian and Pacific Economies: Comparative tables", OECD Tax Statistics (database)

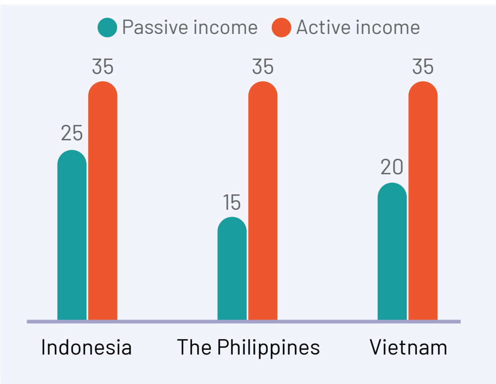
Moreover, ASEAN countries are competing in a race to the bottom by reducing corporate income tax (CIT) rates and offering aggressive tax incentives to foreign multinationals. Across the region, the average CIT rate has fallen over the past decade, from 25.1% in 2010 to 21.7% in 2020 (Oxfam et al., 2020).

Tax asymmetry in Indonesia, The Philippines, and Vietnam

Asymmetrical tax payment refers to the unequal distribution of tax burdens among different economic groups. The working class, especially those in the formal sector, are subject to high-income tax rates, while the HNWIs' passive income sources are subject to low tax rates. Addressing this issue will require significant reforms to tax laws and wealth taxation is considered one prominent mechanism to ensure a more equitable tax system for all.

The asymmetrical tax burden is happening in Indonesia, The Philippines, and Vietnam. In Indonesia, the working class is subject to high tax rates, 0 to 35%, while the HNWIs' passive income sources are subject to low tax rates, 0 to 25%. In the Philippines, the working class is subject to rates on income taxes ranging from 0 to 35%, while the income tax rate for various passive income sources ranges from 0 to 15%. Meanwhile, in Vietnam, the tax rate for active income is 0 to 35%, while passive income sources are subject to a lower tax rate of 0 to 20%.

Figure 3. Maximum tax rates on passive and active income in three countries (%)



Source: PRAKARSA (2022)

Furthermore, there is a tax payments asymmetry between the lower middle class and the rich. The lower middle class pays a more significant value-added tax (VAT) on their income than the wealthy for their VAT consumption tax. In Indonesia, the VAT rate is 11%, while the Philippines and Vietnam implement 10% VAT, respectively.

The effective tax rate for the lower-middle class is higher than for HNWIs. The ratio of taxes paid by the poor relative to their income is more significant than those paid to the income of the HNWI class. People living in poverty typically earn money only to meet their basic needs. A portion of the expenditure of people with low incomes contributes to VAT, tax on sales, and even corporate income tax. This is because, to purchase goods and services, consumers must spend money on distribution costs and logistics such as transport, fuel and so on, -which are the components of VAT.

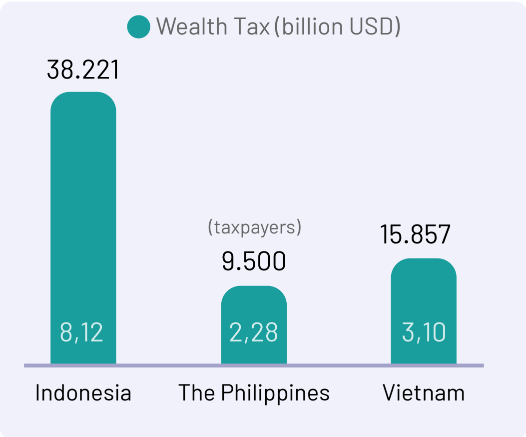
Wealth tax revenue estimation in Indonesia, The Philippines, and Vietnam

If these three ASEAN countries implement wealth tax, they would gain adequate revenues as the number of potential taxpayers is relatively high. Indonesia has around 173.7 thousand individual billionaires who recorded a total wealth of over one million US dollar in 2021 (Credit Suisse Research Institute, 2022). Using the assumption of an inverted pyramid, we estimate that around 38.2 thousand people have a total wealth above US$ 10 million or are classified as High Net Worth Individuals (HNWI). These HNWIs are potential taxpayers of wealth tax instruments with potential state revenues of US$ 8.12 billion for Indonesia (figure 4).

More than half of the potential revenue in Vietnam can be contributed by taxpayers from categories above US$ 250 million, subject to a two percent tax rate. Meanwhile, 26 people with wealth above US$ 1.6 billion accounted for 37% of the total potential receipts with a revenue value of 3.10 billion USD. This estimation is relatively moderate revenue since it is slightly higher than personal income tax, income articles 22 and 26, and income tax amnesty realisation in 2021.

In the Philippines case, the country has around 19 thousand individual billionaires who recorded a total wealth of over US$ 1 million in 2021 (Credit Suisse Research Institute, 2022). We estimate that half of them are people with a total wealth above US$ 6 million and are classified as HNWI. These individuals are potential taxpayers of wealth tax instruments with potential state revenues is around US$ 2.28 billion. This WT estimation constitutes only about 3.6% of total tax revenues collected in 2021. During this year, the government collected US$ 55.7 billion in taxes.

Figure 4. Wealth tax potential revenue in Indonesia, the Philippines, and Vietnam, 2021 (taxpayers and amount)



Source: PRAKARSA (2022)

We used a slightly different tariff and bracket since the Philippines has already designed and rolled out a wealth tax implementation plan into a tax bill, which is more progressive than other countries. Tax is applied to an individual with more than US$ 6 million net worth, with a 0.5 to 2% tariff variation. The highest category (above US$ 1,600 million) contributed 45% of the total potential receipts, with only 14 people. With a two percent tariff imposition, this highest category potentially accounts for US$ 1.03 billion of total likely revenues from wealth tax implementation.

In Vietnam, around 72.1 thousand individual billionaires recorded a total wealth of over US$ 1 million in 2021 (Credit Suisse Research Institute, 2022). We estimate that almost 15.9 thousand people have wealth above 10 million USD or are classified as HNWI. These HNWIs are potential taxpayers of wealth tax instruments with a possible state revenue is US$ 3.1 billion, using the same scheme as Indonesia. Compared to Indonesia and the Philippines' revenue, the distribution of potential revenue in each Vietnam bracket looks more evenly distributed. Taxpayers with wealth above US$ 250 million, estimated at 55 people, account for US$ 913 million or equivalent to almost 30% of the total potential wealth tax revenues.

Gender inequality in the tax system

Moreover, the asymmetrical tax burden between the working class and HNWIs can disadvantage women, mainly female workers, in several forms. The first disadvantage is unfavorable VAT consequences. As prominent actors who play a significant role in providing basic household needs, women are often associated with domestic activities and care that meet daily logistical and reproductive needs, especially at the household level. They will bear the most tax burden when VAT charges increase, whether the percentage or the nominal rise by inflation. Since women, on average, also tend to earn less than men due to the gender pay gap, they may be disproportionately affected because, with lower income and wealth, they are not eligible to receive tax deductions, exemptions and loopholes in the tax system as HNWIs.

Second, widening wealth and income inequality. HNWIs benefit from preferential tax treatment on income and have more opportunities to accumulate and grow their wealth through investments, capital gains, and inheritance. However, the working class, including many female workers, often struggle to get significant wealth due to lower incomes, limited access to financial resources, and systemic barriers. As a result, they are disproportionately affected by a tax system that places a heavier burden on income taxes rather than wealth or capital gains taxes.

Third, weakening tax support system. High-net-worth individuals often have access to various resources and financial tools to mitigate their tax liabilities, such as tax planning services and offshore accounts. On the other hand, the working class, including female workers, have limited access to such tax support systems.

According to UN Women Indonesia (2020), women make 23% less than men on average. There is inequality for women and inequality of opportunities for women. At the same time, women are also burdened with products that are higher than men. At this moment, In Indonesia, no tax supports gender justice.

Women's Budget Group has argued that tax is a gendered issue for three main reasons: 1) different forms of tax have different distributional and behavioral effects; 2) tax policy influences the economy in a way that can affect gender equality; 3) tax provides revenue to support public services and social security, which women rely on more than men (Palmer, 2020).

VAT can lead to gender bias because of the different consumption patterns of women. Generally, for women's lower incomes, tax policies that focus solely on increasing indirect taxes such as VAT rather than also increasing direct taxes (income tax) have the potential to be more burdensome for women. This seems simple, but it can significantly impact society and become a form of inclusive economic policy.

Applying gender equality in the taxation system is critical in supporting individuals, and MSMEs can eventually increase tax revenues. However, when viewed from the previous discussion above, taxes are one of the contributing factors to gender inequality or discrimination. Kronfol et. al. (2019) writes that the forms of gender equality policies for women workers include: (1) a reduction of gross income as a basis for imposing taxes (Tax Deduction), (2) a delay in paying taxes within a certain period (Tax Deferrals), and (3) tax deduction on the total tax paid (Tax Credit).

Recommendations

In conclusion, governments in Southeast East Asia countries must implement fairer and symmetry progressive tax measures to invest in effective and proven steps to reduce inequality, with the following recommendations:

- **The Governments and the Parliaments of the Republic of Indonesia, the Republic of the Philippines, and the Socialist Republic of Vietnam** must increase the tax rate on passive income sources as well as impose a tax on untaxable sources of income such as inheritance with a value above US$ 1 million in Indonesia and Vietnam. This would mean that HNWIs' passive income sources would be subject to higher tax rates.
- **The Governments and the Parliaments of the Republic of Indonesia, the Republic of the Philippines, and the Socialist Republic of Vietnam** must regulate trust to register and report their ultimate beneficial owner(s). Trust must make this beneficial ownership registration and report compulsory to enhance transparency, combat financial crimes, and prevent money laundering and illicit activities.
- **The Government of the Republic of Indonesia, the Republic of the Philippines, and the Socialist Republic of Vietnam** shall accelerate multilateral cooperation on automatic exchange of information systems in international fora for international taxation purposes. Through multilateral fora, the state or government leaders shall propose a global approach to implementing a global wealth tax by preparing an initiative on global wealth tax standards.
- **The Governments of the Republic of Indonesia, the Republic of the Philippines, and the Socialist Republic of Vietnam, altogether with other ASEAN Leaders,** must propose a comprehensive global asset register in the international fora to register all wealth and assets in order to give policymakers and the public the data needed to tackle multinational tax abuse and redress inequality. A global asset register is a proposal to create a comprehensive international registry of all wealth and assets to give policymakers and the public the data needed to tackle multinational tax abuse and redress inequality.
- **The Governments of the Republic of Indonesia, the Republic of the Philippines, and the Socialist Republic of Vietnam, altogether with other ASEAN Leaders,** must increase oversight of taxpayer compliance through regulations regarding the obligation to register and report ultimate beneficial owners by Trusts as well as formulating a regulatory framework for Beneficial Owners and Trusts for tax purposes in rules at the level of Tax Law.
- **The Government and Parliament of the Republic of Indonesia, the Republic of the Philippines, and the Socialist Republic of Vietnam, altogether with other ASEAN Leaders,** must draft a policy regarding gender-based taxation, which can provide a stimulus for Tax Deduction or Tax Reduction to women who work and have dependent children.

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