I. INTRODUCTION:

This paper looks into the pros and cons of a proposed debit tax as a temporary revenue source for the government.

II. BACKGROUND INFORMATION:

A. Other Countries’ Experiences

The Financial Transaction Tax (FTT) is a tax levied on each instance of specified banking, equity, currency, securities, or other financial dealings. It first saw light in 1936 when Keynes suggested a tax on financial transactions to discourage speculative activities in the US stock market which were not in line with economic fundamentals. This idea was revived in the 1970s by James Tobin, who suggested that cross-border currency transaction be taxed to discourage speculative activities and a run on currencies.

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6 Prepared by Ms. Monica G. Rempillo, Supervising Tax Specialist, Economics Branch, NTRC.

1 Isaias Coelho, Liam Ebrill and Victoria Summers, Bank Debit Taxes in Latin America: An Analysis of Recent Trends, May 2001, p. 3.


3 Ibid.
The Bank Debit Tax (BDT) is a subset of the FTTs implemented in Latin America. Given the growing popularity of the BDT, several academic studies have been made on the subject. Some of these studies are presented as tax reform proposals while others analyze the performance of said tax in countries that have adopted it. Thus, the following may be noted:

1. Latin America

The BDT was introduced in half a dozen Latin American countries in the past 17 years in response to a general economic crisis as a means of raising government revenue. It is a tax levied on withdrawals from or other debits to bank accounts, and generally include the clearance of checks, cash withdrawals, payment of loan proceeds, withdrawals through ATMs and charges to bank issued credit cards. The countries’ bid to raise revenue from the BDT had been successful as revenues collected from said tax ranged from 0.29% of GDP (Argentina, 1992) to as much as 3.5% (Ecuador, 1997). The transactions subject to or exempt from BDT as well as the tax rates differ from country to country. The tax rates ranged from 0.2 percent to 2 percent.

In Brazil, the tax was approved at first on a temporary basis to secure revenues for socially-relevant government programs and later renewed to aid in fiscal adjustment efforts. Peru, on its part, has imposed the temporary tax of 0.08% on all banking operations in national or foreign currency (both debits and credits) but deductible for income tax purposes. Argentina and Ecuador also allowed the BDT to be creditable against the income tax or the VAT.

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4 The BDT has different terminologies: Bank Debit Taxes (BDTs) in Latin America; Cash Withdrawals from Banks for Pakistan; and Banking Cash Transaction Tax (BCTT) for India.

5 Argentina, Brazil, Colombia, Ecuador, Peru and Venezuela.

6 Coelho, Ebrill and Summers, p. 9.


9 The 2 percent tax rate was applicable in Peru during April-September 1990.

10 Schneider, Lledo and Moore.


12 Coelho, Ebrill and Summers, p. 10.
2. **India**

A Banking Cash Transaction Tax (BCTT) was introduced in India through the Finance Act 2005 and became effective on June 1 of the same year. For individuals and Hindu Undivided Families (HUF), the tax is at 0.1% on withdrawals of cash from banks in excess of Rs 25,000 on a single day from the same account (other than a savings bank account). On the other hand, for businesses (including State and Central governments), cash withdrawals in excess of Rs 1 lakh\(^\text{13}\) on a single day from the same account (other than a savings bank account) are the ones subject to the BCTT.\(^\text{14}\) The tax base for the BCTT is the value of the taxable banking transaction, which can be categorized as cash withdrawals or receipts of checks on encashment of term deposits. Cash withdrawals from savings bank accounts are not subject to the said levy.

The said tax was imposed in India in order to unearth black money and assets. The government is concerned about large cash transactions, especially withdrawals of cash, when there is no ostensible purpose for withdrawing such large amounts of cash. Thus, it was presumed that said withdrawals become part of the black economy.\(^\text{15}\) The Finance Minister of India further stressed that the new BCTT is imposed not on the event of withdrawals of cash from banks but rather on the unknown trail that the cash withdrawals may not leave.\(^\text{16}\)

3. **Australia**

A Bank Account Debits Tax (BADT or BAD) was introduced by the Commonwealth in 1982 and the power to levy the tax was transferred to the States and Territories in 1990.\(^\text{17}\) The tax, together with the Financial Institutions Duty (FID), was abolished by the States and Territories between 1 July 2002 and 1 July 2005 as part of the package of reforms for the introduction of the Goods and Services Tax.\(^\text{18}\)

The BADT or BAD was levied on customer withdrawals from all banking accounts and financial institutions with a check facility (both

\(^{13}\) Rs.1 lakh (Rs. 100,000) is equivalent to US$2,242 (1 Rupee:$44.6100) as of 31 March 2006, [http://www.rbi.org.in/home.aspx](http://www.rbi.org.in/home.aspx), 01 April 2006.


\(^{17}\) The Commonwealth levied the BAD tax under the Debits Tax Act 1982 and the Debits Tax Administration Act 1982 until 1 January 1991. From that date, the Commonwealth transferred BAD tax to the States and Territories under the Debits Tax Termination Act 1990.

withdrawals made by check or by other means, such as Electronic Fund Transfer at Point of Sale (EFTPOS)). When the tax is cleared, it is instantly deposited through the Electronic Funds Transfer (EFT) system into the National Treasury.

The tax was levied according to the State and Territories where the bank account was domiciled, not where the account holder lived. The schedule of the Debits Tax ranged from a low of $0.15 to a high of $4.00 (Table 1):19

<table>
<thead>
<tr>
<th>Amount of Withdrawal ($)</th>
<th>NSW, Vic, Qld, SA, WA, ACT, NT*</th>
<th>Tasmania</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 - 99</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>1 - 99.99</td>
<td>0.30 (0.15 – NT)</td>
<td>0.15</td>
</tr>
<tr>
<td>100 - 499.99</td>
<td>0.70</td>
<td>0.35</td>
</tr>
<tr>
<td>500 - 4,999.99</td>
<td>1.50</td>
<td>0.75</td>
</tr>
<tr>
<td>5,000 - 9,999.99</td>
<td>3.00</td>
<td>1.50</td>
</tr>
<tr>
<td>10,000 and above</td>
<td>4.00</td>
<td>2.00</td>
</tr>
</tbody>
</table>

* NSW – New South Wales; Vic – Victoria; Qld – Queensland; SA – South Australia; WA – Western Australia; ACT – Australian Capital Territory; NT – Northern Territory

The Debit Tax offered no exemption since according to policymakers this would only allow “clever” legal minds to find “legal” ways for tax evasion. Revenue raised by the FID and BAD tax increased from $468 million in 1984-1985 to $2.24 billion in 1999-2000.

4. Pakistan

Through the Finance Act, 2005, the government of Pakistan has imposed a 0.1% withholding tax on cash withdrawals from banks exceeding Rs 25,000 effective July 1, 2005. The following transactions are exempted from the withholding tax:20

a. Encashment of Pay Order or other similar banking instruments;

b. Cash withdrawal from ATM in Pakistan against credit cards issued outside Pakistan;

c. Withdrawals on credit cards issued by non-banking companies, e.g., Diners Club;


d. Cash withdrawals by banks from accounts maintained with sub-treasury for their day-to-day cash requirements; and

e. Withdrawal from ATMs not exceeding Rs 25,000

5. Papua New Guinea

The government of Papua New Guinea has introduced a Debits Tax effective in the early part of 2004. The tax was aimed to “pluck out” extra money from peoples’ bank accounts.\(^\text{21}\) It was applied to all withdrawals (whether savings or current accounts, loan withdrawals), including withdrawals using the electronic banking services, such as ATMs and EFTPOS and branch withdrawals or over the counter. Papua New Guinea’s Debits Tax ranges as follows:\(^\text{22}\)

<table>
<thead>
<tr>
<th>Amount Withdrawn</th>
<th>Amount of Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>K50</td>
<td>NIL</td>
</tr>
<tr>
<td>K50 – K100</td>
<td>K0.01</td>
</tr>
<tr>
<td>K100 – K124,999.99</td>
<td>0.01% of the debit amount</td>
</tr>
<tr>
<td>K125,000 or more</td>
<td>K12.50</td>
</tr>
</tbody>
</table>

Under the new Debits Tax Act, the Government exempted foreign currency accounts and term deposit rollovers. Accounts held by governments of other countries other than Papua New Guinea, charities and non-profit organizations were also exempted, subject to the bank holding an exemption certificate issued by the Internal Revenue Commission.\(^\text{23}\)

In the same vein, stamp duties on checking accounts are no longer payable.\(^\text{24}\)

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\(^{22}\) Ibid.

\(^{23}\) Papua New Guinea’s currency is called Kina (K) with an exchange rate of K0.3240:US$1 (as of 30 March 2006, http://www.bankpng.gov.pg/exchangerate/index.htm).

\(^{24}\) Ibid.

6. Vanuatu

The government of Vanuatu imposes a Debit Tax on all withdrawals from a taxable account in a commercial bank. The debit tax applies to all withdrawals of VT1,000 or more. The bank is responsible for collecting the tax by taking it out of the customer’s account and paying it to the Vanuatu Government within 14 days after the end of the month in which the withdrawal was made. The amount of debit tax to be paid on every withdrawal is as follows:

<table>
<thead>
<tr>
<th>Amount of Withdrawal</th>
<th>Amount of Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>VT1,000-VT9,999</td>
<td>VT10</td>
</tr>
<tr>
<td>VT10,000-VT49,999</td>
<td>VT20</td>
</tr>
<tr>
<td>VT50,000-VT99,999</td>
<td>VT30</td>
</tr>
<tr>
<td>VT100,000-VT499,999</td>
<td>VT100</td>
</tr>
<tr>
<td>VT500,000-VT999,999</td>
<td>VT200</td>
</tr>
<tr>
<td>VT1,000,000-VT4,999,999</td>
<td>VT300</td>
</tr>
<tr>
<td>VT5,000,000 or more</td>
<td>VT400</td>
</tr>
</tbody>
</table>

B. Proposed Debit Tax for the Philippines

As proposed, the debit tax is to be applied on withdrawals from checking, savings and term accounts at a rate of 0.2% of the amount withdrawn. The proposed tax is programmed to operate only under an automatic trigger mechanism based on a national government deficit to GDP ratio. When the government deficit hits 3.5% of GDP, the tax would be automatically imposed for a period of at least six months. After the six-month period, the tax will be discontinued when the deficit-to-GDP ratio goes below 3.5%. The following transactions may be exempted from the proposed debit tax based on the lessons learned from the experience of the Latin American countries:

1. Withdrawals from the same account amounting to P5,000 and below in a given day;

26 A long Y shaped archipelago, Vanuatu lies in the South West Pacific, near Australia and Papua New Guinea, comprising of 12 islands.

27 Vanuatu’s currency is called Vatu (VT) with an exchange rate of VT116:US$1 as of 31 March 2006 (http://www.crinmill.com/USD_vuv.html).

28 University of the South Pacific, “Debit Tax”.

29 Vicerra and Singson, p. 5.
2. Long term loans;

3. Transfers between accounts of the same person in the same financial institution;

4. Transactions with the central bank;

5. Inter-bank clearing and inter-bank transfers to ATM operations;

6. Stock market and government bonds transactions; and

7. Foreign exchange market transactions

The proposed debit tax is seen as a temporary solution to a serious fiscal problem. However, its reliability as a steady source of revenue for the government cannot be depended upon since its imposition is discontinued when the deficit-to-GDP ratio goes below the trigger point of 3.5%. But once the proposed tax is in force, it is assumed to bring in a hefty amount of revenue for the government. Based on the study conducted by the CPBO, the expected revenue from the proposed debit tax would be P28.40 billion based on the value of cleared checks of P14,200.72 billion from January to October 2005. The estimate is said to be conservative because it does not include withdrawals from savings and term accounts.

The reason why the proposed debit tax is pegged at a single rate of 0.2% is to promote administrative simplicity. Once the bank deducts the 0.2% on the amount withdrawn, it then remits the collection to the government after deducting a service fee as compensation for their work. Hence, the costs of collecting and administering the tax may be minimal.

III. COMMENTS AND OBSERVATIONS:

1. In a situation where the government is facing financial woes, it becomes imperative for those managing the country to look for ways to augment the government’s dwindling financial position. Thus, the proposal to impose a debit tax has surfaced.

2. Just like the other countries that impose a tax on bank withdrawals, the proponents of the debit tax are looking at the measure as a tool to raise substantial revenue in the short term when the existing tax policies have proven to be incapable of providing the needed increases in government’s revenues.

30 Ibid.

31 Ibid, p. 4.
3. There is no denying that the proposed tax has the potential to raise quick and easy revenue for the government. However, there is a great possibility that the estimated revenue to be generated from the proposed debit tax may be illusory because of the possible financial disintermediation\textsuperscript{32} effects that may result as a reaction to the tax. Based on the experience of Latin American countries, the introduction of the BDT led individuals and businesses to substitute bank-intermediated transactions into cash and conducted a greater proportion of their bank transactions offshore. The increase in “offshore banking” or the possibility of depositors/investors shifting their transactions to countries where their savings would not be covered by taxation is not remote. Hence, the imposition of the proposed debit tax may be enough reason to drive away capital to places outside the country.

4. Further, the imposition of the proposed tax would jeopardize the role of banks in savings mobilization because depositors may favor other products outside the banking system; for example, stock market, bond transactions, investment funds, etc., where the yield is much higher.

5. The proponents of the tax claim that exempting withdrawals below P5,000 would shield those belonging to the low income bracket from the burden of the tax and that only those in the affluent sector of the economy who are capable of shouldering the tax burden shall be liable to the tax. It is worth mentioning, however, that there are users of the banking system whose objective is not to accumulate funds and/or earn interest from their savings but only to use the system as a method to transfer funds (payment of utilities, credit cards, etc.). Hence, those who will be most affected by the proposed tax will be those who are heavy users of the banking system, such as corporations, whose volume/magnitude of banking transactions is not an indicator of capacity to pay but is only dictated by business requirements.

6. Also, there is the fear that the proposed tax may only serve to push people to place their money in the black economy that would result in greater tax evasion. This possibility cannot be ignored as taxation is always considered a major factor that hinders any economic activity. In fact, once economic activities are driven underground as a result of the introduction of the debit tax, this will have an adverse impact on the yield of other major taxes\textsuperscript{33} like the income tax, VAT and documentary stamp tax.

7. Moreover, from an economic standpoint, the proposed tax would further discourage savings in a country that already has one of the lowest savings rate in Southeast Asia. (Table 4) Presently, low savings holds back the country’s development due to lack of capital formation and investments. The proposed tax would be viewed as a disincentive to save in banks aggravating further the country’s low savings rate.

\textsuperscript{32} Broadly speaking, by disintermediation is meant the withdrawal of funds from financial intermediaries, with the payments being made in some other way (e.g., in cash, by barter through accounts not subject to tax, etc.), Andrei Kirilenko and Victoria Summers, “Bank Debit Taxes: Yield vs. Disintermediation”.

Table 4. % OF GROSS DOMESTIC SAVINGS TO GDP

<table>
<thead>
<tr>
<th>Country</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Philippines</td>
<td>18.6</td>
<td>23.1</td>
<td>17.5</td>
<td>18.8</td>
<td>16</td>
</tr>
<tr>
<td>Singapore</td>
<td>50.1</td>
<td>48.1</td>
<td>43.9</td>
<td>44.8</td>
<td>47</td>
</tr>
<tr>
<td>Malaysia</td>
<td>47.4</td>
<td>47.2</td>
<td>42.3</td>
<td>41.9</td>
<td>-</td>
</tr>
<tr>
<td>Thailand</td>
<td>33.1</td>
<td>31.4</td>
<td>30.6</td>
<td>31.1</td>
<td>32</td>
</tr>
<tr>
<td>Indonesia</td>
<td>19.5</td>
<td>25.6</td>
<td>24.9</td>
<td>21.1</td>
<td>22</td>
</tr>
</tbody>
</table>


8. In the same vein, the proposed tax on bank withdrawals would cause another heavy burden on depositors. At the moment, there is already a 20% final withholding tax (FWT) on interest income and a DST of P1.50 per check. The proposed 0.2% tax on bank withdrawals would further diminish the value of the money placed in banks. Moreover, there is also a bank fee ranging from P7.00-P10.00 for every transaction made on withdrawals using other bank’s ATM cards. Further, the amount of maintaining balance for both savings and checking accounts is already high, ranging from P3,000-P5,000 (depending on which bank the depositor will put his/her money) for savings account while checking account requires P10,000 for individual accounts and P25,000 for corporate accounts. In order to earn interest from said accounts the deposit should be around three folds that of the maintaining balance.

9. It may also be worth mentioning that a study conducted by the International Monetary Fund (IMF) on the effectiveness of the bank debit taxes in Latin American countries proved that these taxes are not to be considered as an efficient source of revenue in the long-term due to significant domestic disintermediation which could be difficult to reverse even if, and when the bank debit tax is revoked. Hence, the overall policy conclusion of the IMF is that the use of these taxes should be avoided.34

10. It is also noted that the proposed tax may be futile due to the envisioned balanced budget by 2008 or 2010. For 2006-2010, the highest projected ratio of deficit to GDP is only 2.9% in 2006 (Table 5) which is below the trigger ratio of 3.5%.

Table 5. PROJECTED DEFICIT AS PERCENT TO GDP

<table>
<thead>
<tr>
<th>Year</th>
<th>MTPDP 2004-2010</th>
<th>20-Sept-05 Emerging Estimates</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>-2.9</td>
<td>-2.2</td>
</tr>
<tr>
<td>2007</td>
<td>-2.0</td>
<td>-1.0</td>
</tr>
<tr>
<td>2008</td>
<td>-1.1</td>
<td>0.0</td>
</tr>
<tr>
<td>2009</td>
<td>-0.2</td>
<td>0.2</td>
</tr>
<tr>
<td>2010</td>
<td>0.0</td>
<td>0.2</td>
</tr>
</tbody>
</table>

MTPDP – Medium-Term Philippine Development Plan
Source: Development Budget Coordination Committee

34 Coelho, Ebrill, Summers, p. 24.
11. Lastly, if and when the proposed debit tax is pushed through, the following transactions have to be carefully taken into consideration in order to strike a balance between the achievement of the objective of the proposed debit tax and avoidance of tax distortions:

a. Distributions from trusts in cash;

b. Withdrawals of dividends earned from government security systems – dividends granted by government security systems are exempted from interest income. Thus, any form of taxation thereon is unjustifiable; and

c. Salaries withdrawn through the banking system - the move would cause double taxation since the same has already been subjected to income tax. The usage of bank as a medium to obtain salaries of employees is only meant for administrative purposes and not for wealth accumulation.

III. CONCLUSION:

Different studies on the tax on bank withdrawals offer information on the experiences and lessons of countries that have already implemented this type of tax. And based on these experiences, we know that while the main purpose for the adoption of the bank debit tax (quick and easy revenue for the government) was achieved, it has numerous negative consequences. While in some countries the quick way to generate revenues and ease of collecting the bank debit tax received a very heavy weight at the expense of efficiency and equity considerations, the Philippines cannot afford to disregard the last two considerations due to the country’s low savings rate. At present, there are efforts being done by the government to align the tax treatment of both banks and non-bank financial institutions so that said institutions can help facilitate savings mobilization and to develop the country’s capital market. At the moment, savings and checking accounts are already saddled with existing taxes and bank fees. Thus, the proposed tax would only lead people to shy away from using banks especially since the use of bank services may easily be substituted or voluntarily reduced.

In conclusion, it is submitted that at this point when the country’s fiscal situation is beginning to improve, the proposed debit tax will only bring on negative consequences that will far outweigh whatever positive revenue impact it may have.