REVENUE PERFORMANCE OF REPUBLIC ACT (RA) NO. 9337, OTHERWISE KNOWN AS THE REFORMED VALUE-ADDED TAX (RVAT) LAW, 2004-2010*

I. INTRODUCTION

The Value-added tax (VAT) is a tax on consumption levied on the sale, barter, exchange or lease of goods or properties and services, and on importation of goods. Its key feature is to charge and collect tax throughout the production or distribution process, with provision for tax payable to be reduced by the tax paid in respect of purchases. The VAT addresses the cascading problem which is typical in sales or turn-over tax. Compared to other indirect taxes, it has more revenue potential due to its broader tax base and it entails a trail of invoices that helps improve tax administration.

It has been six years since RA No. 9337[1] or the Reformed VAT Law was implemented on November 1, 2005. Since then various revenue measures have been issued which greatly affected the effectiveness of VAT in generating the much needed revenues of the government. In this regard, this paper seeks to measure the efficiency of the RVAT Law with respect to its revenue performance and evaluate its impact on the economy and government's fiscal condition for the period 2004-2010.

II. SALIENT FEATURES OF THE RVAT LAW

The VAT was introduced in the Philippines in 1988 through Executive Order (EO) No. 273[2] to replace numerous taxes on goods and services. It aimed to simplify tax

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[1] Entitled, "An Act Amending Sections 27, 28, 34, 106, 107, 108, 109, 110, 111, 112, 113, 114, 116, 117, 119, 121, 148, 151, 236, 237, and 288 of the National Internal Revenue Code (NIRC) of 1997, As Amended, And For Other Purposes", Approved on May 24, 2005.

[2] Entitled "Adopting a VAT, Amending for this Purpose, Certain Provisions of the NIRC, and for Other Purposes", Approved on July 27, 1987 and Effective January 1, 1988.

administration and make the tax system more equitable. Since then, several major laws were enacted to amend and/or expand the coverage of the VAT. The most recent was RA No. 9337 or the RVAT Law, which expanded the coverage of VAT and authorized the President of the Philippines upon the recommendation of the Secretary of Finance to raise the VAT rate from 10% to 12% after meeting certain conditions. RA No. 9337 was implemented on November 1, 2005 while the VAT rate increase from 10% to 12% took effect only on February 1, 2006 via Bureau of Internal Revenue (BIR) Revenue Memorandum Circular (RMC) No. 7-2006[3].

RA No. 9337 was enacted to help the government balance its budget through the collection of more revenues to address the budgetary problem and to sustain the provision of basic social services. It was designed to effectively broaden the tax base which is in accordance with the well-settled principle that for the VAT to be effective, it should be broad-based and with limited exemptions.

RA No. 9337 incorporated other reform measures that were devised to plug the leaks in the existing VAT system. These include the 70% cap on input VAT[4], the spreading of the input VAT claim on capital goods which exceeds Php1 million (net of VAT component) to 5 years, the removal of the 1.5% presumptive input VAT on public works contractors, and the imposition of a uniform 5% final withholding VAT on government purchases of goods, services and public works contracts[5]. These reform measures were enacted to strengthen the government's cash flow and to simplify the VAT administration as well.

A number of mitigating measures were also included in the VAT reform package to cushion or minimize its impact on consumers of goods/services. In particular, the excise taxes on kerosene, diesel and bunker fuel oil were reduced to P0.00 per liter; the franchise tax on power distribution and domestic airlines, and common carriers tax on domestic shipping were removed; the presumptive input VAT on agro-processors[6] was increased from 1.5% to 4%; and the marginal threshold exempt from VAT was raised from Php750,000 to Php1.5 million[7] per annum, and sale of house and lot and other residential dwellings from Php1.5 million to Php2.5 million[8].

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[3] Entitled, "Publishing the Full Text of the Memorandum from Executive Secretary Eduardo R. Ermita dated January 31, 2006 Approving the Recommendation of the Secretary of Finance to Increase the Value Added Tax Rate from 10% to 12%, Effective February 1, 2006".

[4] Abolished under RA No. 9361, Entitled, "An Act Amending Section 110 (B) of the National Internal Revenue Code of 1997, as Amended, and for Other Purposes", Approved on November 21, 2006.

[5] The 5% final withholding VAT represents the net payable of the seller. Prior to RA No. 9337, withholding VAT on government payments is creditable. The rates were 3%, 6% and 8.5% on gross payments for the purchase of goods, services rendered, and payments made to government public works contractors, respectively.

[6] Persons or firms enaged in the processing of sardines, mackerel and milk, and in manufacturing refined sugar, cooking oil and packed noodle-based instant meals.

[7] Adjusted to Php1.92 million under RR No. 16-2011, Effective January 1, 2012.

[8] Adjusted to Php3.20 million under RR No. 16-2011, Effective January 1, 2012.

Under RA No. 9337, the following previously exempt goods and services were made subject to the VAT, viz.:

a) Domestic transport of passenger by air and sea;
b) Generation, transmission[9] and distribution of electricity;
c) Coal and natural gas;
d) Petroleum products and their raw materials;
e) Electric cooperatives[10];
f) Non-food agricultural products;
g) Marine and forest products;
h) Cotton and cotton seeds;
i) Importation of passenger/cargo vessels more than 5,000 tons;
j) Works of art, literary works, musical compositions and similar creations;
k) Doctors of medicine duly registered with the Professional Regulation Commission (PRC); and
l) Lawyers registered with the Integrated Bar of the Philippines (IBP).

On the other hand, the following goods and services were made subject to zero percent (0%) VAT, viz.:

a) Transport of passengers and cargoes by domestic air or sea carriers to a foreign country;
b) Services rendered to international air transport operations[11] including lease of property for use thereof;[12]
c) Sale of goods, supplies, equipment and fuel to aircrafts and vessels engaged exclusively in international transport; and
d) Sale of power or fuel generated through renewable sources of energy such as, but not limited to, biomass, solar, wind, hydropower, geothermal, ocean energy, and other emerging energy sources using technologies such as fuel cells and hydrogen cells.

[9] Exempted from VAT beginning December 20, 2008 under Section 9 of RA No. 9511, Entitled, "An Act Granting the National Grid Corporation of the Philippines a Franchise to Engage in the Business of Conveying or Transmitting Electricity through High Voltage Back-Bone System of Interconnected Transmission Lines, Substations and Related Facilities, And For Other Purposes, Approved on December 1, 2008.

[10] Electric Cooperatives duly registered with the Cooperative Development Authority were exempted from VAT under Section 61 (2) (b) of RA No. 9520, Entitled, "An Act Amending The Cooperative Code of the Philippines to be Known as the Philippine Cooperative Code of 2008", beginning February 17, 2009.

[11] Under BIR Ruling 099-11, services provided by the hotel in its premises to international air transport operations pertaining to room accommodations and food and beverages services are not directly attributable to the transport of goods and passengers from Philippines ports to a foreign port. Hence, they are not subject to zero-rating but to 12% VAT.

[12] Prior to the RVAT Law, only services rendered to vessels engaged exclusively in international shipping are subject to the 0% VAT under Section 108 (B) (4) of RA No. 8424.

In addition, RA No. 9337 introduced non-VAT reforms. For instance, it increased the corporate income tax rate from 32% to 35% but to be later on reduced to 30% effective January 1, 2009. It also removed the income tax exemption of government-owned or controlled corporations (GOCCs) and instrumentalities except the Government Service and Insurance System (GSIS), Social Security System (SSS), Philippine Health Insurance Corporation (PHIC) and the Philippine Charity Sweepstakes Office (PCSO). Furthermore, the gross receipt tax on royalties, rentals of property, real or personal, profits from exchange and all other items treated as gross income of banks and non-bank financial intermediaries was increased from 5% to 7%. The rationale for these provisions is to share the tax burden between individuals and corporations considering that the VAT is ultimately shouldered by the consumers.

III. VAT REVENUE PERFORMANCE, 2004-2010

Aggregate VAT revenues more than doubled from Php156.67 billion in 2005 (pre-RA No. 9337 regime) to Php330.78 billion in 2010. There was a sharp increase in VAT collection of both the BIR (60.42%) and the BOC (72.74%) in 2006, which was attributable to the first full year implementation of RA No. 9337, and the increase from 10% to 12% of the VAT rate.

Table 1. VAT REVENUES AND GROWTH RATES: 2004-2010
(Amounts in Billion Pesos)

Year	VAT Revenues			Growth Rate (%)		
	BIR	BOC	Total	BIR	BOC	Total
2004	80.22	58.88	139.10	-2.92	11.81	2.81
2005	87.86	68.81	156.67	9.52	16.86	12.63
2006	140.93	118.87	259.80	60.40	72.75	65.83
2007	145.01	129.02	274.03	2.90	8.54	5.48
2008	140.32	156.33	296.65	-3.23	21.17	8.25
2009	168.29	133.90	302.19	19.93	-14.35	1.87
2010	173.28	157.50	330.78	2.97	17.63	9.46

Sources of basic data: BIR and BOC.

Specifically, the BIR VAT revenue showed an upward trend from Php80.22 billion in 2004 to Php173.28 billion in 2010 except for 2008 when collection dropped by 3.23% from the previous year's collection. The decline was traced by the BIR to the increased input tax claims by importers and taxpayers with capital expenditures of more than Php1 million in

2007, and other non-recurring transactions such as privatization, audit/assessment, closures, etc., of about 8% of the total VAT collected.[13]

Likewise, the Bureau of Customs' (BOC) VAT revenue steadily grew from Php58.88 billion in 2004 to Php157.50 billion in 2010 except for the 14.35% drop in collection in 2009. The decline was due to the reduction in the value of imports by 20.04% specifically the lower crude oil imports; the stronger peso and lower tax payment by the government through the tax expenditure fund (TEF).[14]

It is noted that since the full implementation of RA No. 9337 in 2006, the share of VAT to total tax revenue significantly increased from a 22% - 23% level to a range of 28% to 30%. Hence, the passage of RA No. 9337 (i.e. broadened tax base, increased rate and the 70% cap on input VAT in 2005) has proven to be an effective revenue generating measure.

Table 2. SHARE OF VAT REVENUE TO TOTAL TAX REVENUES: 2004-2010
(Amounts in Billion Pesos)

Year	Total VAT Revenues	Total Tax Revenues	% Share to Total
2004	139.01	598.01	23.25
2005	156.67	705.62	22.20
2006	259.80	859.87	30.21
2007	274.03	932.93	29.37
2008	296.65	1,049.19	28.27
2009	302.19	981.62	30.78
2010	330.78	1,093.64	30.25

Sources of Basic Data: BIR, BOC and BTr.

Another way of assessing VAT performance is through the determination of its efficiency ratio or the ratio of VAT revenue to the VAT base divided by the standard VAT rate. For this purpose, the VAT base was represented by GDP and aggregate consumption expenditures. The use of these VAT tax bases are justified by the fact that the level of economic activities or GDP influences VAT revenue while consumption expenditures reflect the consumption type nature of VAT. Using the GDP as the VAT base, the ratio is known as VAT efficiency ratio or sometimes called VAT productivity. On the other hand, using the aggregate consumption expenditures as the VAT base, the ratio is known as Consumption Efficiency Ratio or simply C-Efficiency. An efficiency ratio of 100% is an indicator of a

[13] BIR Annual Report 2008, Value Added Tax, BIR Collection Performance, p.18.

[14] BOC Annual Report, 2009, pp. 6, 8-9.

very good VAT system while a low ratio is typically taken as *prima facie* evidence of erosion either by exemption and zero-rating or by imperfect enforcement.[15]

In 2004 and 2005, the ratio of VAT to GDP was 2.86% and 2.88% respectively. Starting 2006, it went up to 4.31%; however, declining rates were noted in the succeeding years. Moreover, prior to RA No. 9337, the VAT efficiency ratio was about 29% using GDP as the VAT base. Since its full implementation in 2006, the VAT efficiency ratio improved to almost 36% although it continuously declined over the years until it reached about 32% in 2010. In the case of VAT efficiency with respect to aggregate consumption or C-efficiency ratio, a similar pattern is observed during the period under review.

The possible reasons for the decline can be attributed to the complicated tax administration of the VAT and the broken VAT chain brought about by the passage of certain measures which have negatively affected the flow of potential revenue from the VAT such as the abolition of the 70% cap and the passage of the National Grid Corporation of the Philippines Franchise, the Cooperative Code of 2008, and the Expanded Senior Citizens Act of 2010, as well as the effects of the global financial crisis.

Table 3. VAT EFFICIENCY RATIO: 2004-2010
(Amounts in Billion Pesos)

Year	VAT Revenues (BIR + BOC)	GDP at Current Prices	Consumption Expenditure	Ratio of VAT Revenue to		VAT Efficiency with Respect to	
				GDP	Consumption Expenditure	GDP	Consumption Expenditure
2004	139.10	4,871.55	3,838.83	2.86%	3.62%	28.55%	36.23%
2005	156.67	5,444.04	4,299.29	2.88%	3.64%	28.78%	36.44%
2006	259.80	6,031.16	4,819.43	4.31%	4.31%	35.90%	44.92%
2007	274.04	6,648.62	5,265.64	4.12%	5.20%	34.35%	43.37%
2008	296.65	7,409.37	5,978.73	4.00%	4.96%	33.36%	41.35%
2009	302.19	7,678.92	6,484.65	3.94%	4.66%	32.79%	38.83%
2010	330.78	8,513.04	7.077.14	3.89%	4.67%	32.38%	38.95%

Source of basic data: BIR, BOC, BTr and NSCB.

It is worth noting that the average VAT efficiency and C-efficiency ratios in Asia and the Pacific region are 35% and 58%[16] respectively while Keen (2011)[17] pointed out that the average C-efficiency ratio on advanced and emerging markets is 50% although big variations

[15] Ebrill. L, Keen, M, Bodin, J-P, and Summers, V 2001, The Modern VAT, International Monetary Fund, Washington D.C., p.40.

[16] Ibid. p.41.

[17] Michael Keen, Tax Policy Options for Fiscal Sustainability, International Monetary Fund, 2011. http://www.imf.org/external/np/fad/news/2011/docs/Keen2.pdf, (February 1, 2012).

were noted. On the other hand, the New Zealand Goods and Services Tax (GST), which is often held as a model VAT, has efficiency ratio of 65%. Hence, the Philippines' VAT efficiency and C-efficiency ratios are still below the Asia and the Pacific average and far from New Zealand's ratios.

Meanwhile, Ebrill, et al (2001) pointed out that securing the VAT collections on imports is generally a crucial part of ensuring the effective collection of the VAT throughout the chain of production or distribution. In this regard, the BOC plays an important role in the overall efficiency of the VAT regime.

The BOC VAT on imports steadily grew from 2004 to 2010 except for 2009, which fell by 14.35%. The ratio of VAT on imports to total value of imports was higher after RA No. 9337 i.e. from 3.59% in 2004 to 6.50% and 6.67% in 2006 and 2007. The VAT efficiency ratio similarly increased from 35.94% in 2004 to 54.20% in 2006 and 55.62% in 2007. However, declining efficiency ratios were recorded beginning 2008 except for a slight increase in 2009.

The improvement in BOC VAT collections can be attributed to the various programs that the BOC has implemented. In addition, a presumption may be made that collecting VAT on imports is easier than on domestic transactions.[18] There are also no input tax claims at the time of importations. The claims start to kick in only when the imported item is used to produce an output subject to the VAT.

Table 4. VAT ON IMPORTS EFFICIENCY RATIO: 2004-2010
(Amounts in Billion Pesos)

Year	VAT on Imports	Total Imports	Ratio of VAT on Imports to Total Imports (%)	VAT Efficiency Ratio (%)
2004	58.88	1,638.35	3.59	35.94
2005	68.81	1,726.41	3.99	39.86
2006	118.87	1,827.65	6.50	54.20
2007	129.02	1,933.00	6.67	55.62
2008	156.33	2,985.65	5.24	43.63
2009	133.90	2,387.38	5.61	46.74
2010	157.50	2,920.46	5.39	44.94

Sources of Basic Data: BOC and NSCB.

[18] Ebrill. L, Keen, M, Bodin, J-P, and Summers, V 2001, The Allure of the Value-Added Tax, Finance and Development: A Quarterly Magazine of the IMF, Vol. 39, No. 2, (June 2002), http://www.imf.org/external/pubs/ft/fandd/2002/06/ebrill.htm, (July 22, 2010).

Another important ratio that may show the efficiency of the VAT is the so called VAT gross compliance ratio (VATGCR) which is a measure of how well the VAT produces revenue for the government by taking into account the fact that the VAT is mostly applied to final consumption of households and individuals.[19] In this regard, the VATGCR is the ratio of VAT revenue to private consumption in the economy divided by the standard VAT rate.

As shown below, VATGCR went up to 51% in 2006 or after the full implementation of the RVAT as compared to 41.5% level in 2004 and 2005 or prior to RVAT. However, VATGCR deteriorated beginning 2007 until it settled to 44.5% in 2010.

Table 5. VAT GROSS COMPLIANCE RATIO: 2004-2010
(Amounts in Billion Pesos)

Year	VAT Revenue (BIR + BOC)	Private Consumption	VAT Gross Compliance Ratio
2004	139.10	3,346.72	41.56%
2005	156.67	3,772.25	41.53%
2006	259.80	4,229.50	51.19%
2007	274.04	4,611.88	49.52%
2008	296.65	5,281.07	46.81%
2009	302.19	5,674.97	44.37%
2010	330.78	6,192.86	44.51%

Overall, the RVAT regime in general is more efficient than pre-RVAT regime although it is still below the recorded average in Asia and the Pacific region. The highest efficiency ratio recorded in 2006 is due to the fact that the VAT coverage is at its broadest. VAT-registered taxpayers are limited to 70% input VAT credit and the rate increased from 10% to 12%. In 2007 onwards, the declining efficiency can be explained by the enactment of several measures exempting certain transactions from the coverage of VAT and the scrapping of the 70% cap on input VAT.

IV. IMPACT OF THE RVAT LAW TO THE ECONOMY

It is noted that the VAT reform in 2005 was primarily introduced as part of the fiscal measures aimed at putting the public sector deficit and debt on a sustainable path in order to revive the fiscal condition of the government, foster economic growth and alleviate poverty.

[19] Fiscal Reform, VAT Gross Compliance Ratio, http://www.fiscalreform.net/index2.php?option=com_content&do_pdf=1&id=734, (July 21, 2010).

Hence, the RVAT performance can also be evaluated by measuring its impact on the national government (NG) deficit and debt prior to and after its implementation.

The NG debt continuously dropped from Php4.65 trillion in 2004 to Php4.20 trillion in 2007 before it shot up to Php5.01 trillion in 2009 and Php5.27 trillion in 2010. As a percent of GDP, it went down from 95.36% in 2004 to 63.12% in 2007. It then slightly went up in 2008 and 2009 and settled at 61.88% in 2010, which is almost a one-third cut from the 2004 level.

Likewise, the budget deficit to GDP ratio dropped from 3.84% in 2004 to an almost a balanced budget in 2007 before it gradually went up to 0.92% in 2008. In 2009, the budget deficit skyrocketed to 3.89% of GDP, which is higher than the 2004 level although in 2010 it slightly fell to 3.69%. The upsurge in the budget deficit in 2009 was attributed to the lower over all tax collection and the higher spending policy of the government in order to mitigate or cushion the impact of the global financial crisis.

Table 6. NG DEBT, EXPENDITURE AND SURPLUS/(DEFICIT): 2004-2010
(Amounts in Billion Pesos)

Year	NG Debt	Surplus/ (Deficit)	NG debt to GDP	Surplus/(Deficit) to GDP
2004	4,645.66	-187,057	95.36%	-3.84%
2005	4,474.58	-146,778	82.19%	-2.70%
2006	4,421.43	-64,791	73.31%	-1.07%
2007	4,196.67	-12,441	63.12%	-0.19%
2008	4,766.48	-68,117	64.33%	-0.92%
2009	5,010.77	-298,532	65.25%	-3.89%
2010	5,267.97	-314,458	61.88%	-3.69%

Source of Basic Data: BTr.

It is noted that the incremental revenue from RVAT is channeled to finance various social programs and infrastructure projects of the government. In particular, RA No. 9337 expressly provided that the local government unit's 50% share from the incremental revenue from VAT be allocated and used exclusively for the following purposes, viz.:

a) 15% for public elementary and secondary education, to finance the construction of buildings, purchases of school furniture and in-service teacher trainings;

b) 10% for health insurance premiums of enrolled indigents as a counterpart contribution of the local government to sustain the universal coverage of the national health insurance program;

c) 15% for environmental conservation to fully implement a comprehensive national reforestation program; and

d) 10% for agricultural modernization to finance the construction of farm-to-market roads and irrigation facilities.

In this regard, the share of LGUs from VAT is 20% of the 50% VAT collections in excess of the increase in collections for the immediately preceding year per Section 283 of the NIRC of 1997, as amended. Consequently, total BIR VAT collection in 2006 or the full implementation of RVAT is higher by 60.4% as compared to 2005. This resulted to P380 million share of LGUs from VAT or higher by almost 476% as compared to their previous year's share.

Table 7. SHARE OF LGUs FROM VAT, 2004-2010
(Amounts in Million Pesos)

Year	Share from VAT	Growth
2004	12	0.00%
2005	38	216.67%
2006	66	73.68%
2007	380	476.76%
2008	110	-71.05%
2009	183	66.36%
2010	64	-65.03%

Source of Basic Data: Local Government Audit Office Annual Report.

It should be noted however that the share of LGUs from the incremental VAT collections only accrues to the city or municipality where such taxes are collected and is allocated in accordance with the rule on the situs of the local business tax per Section 150 of the Local Government Code. Thus, the share may not be consistent and there are instances when some LGUs failed to avail of the said share because of complicated procedures involved in adopting the rule of situs of the local business tax, not to mention the absence of computer linkages in the VAT payment stations that makes it difficult for the BIR to monitor and verify the accuracy of the LGU's share from the gross receipts of business taxpayers maintaining branches, plants/plantations or factories in different localities.[20] Hence, only LGUs with incremental collection, with less complicated procedures in determining the situs of the local business tax and with computer linkages in the VAT payment system benefit from the said provision.

[20] Caro, R 2008, Shares of Local Government Units from National Taxes, NTRC Tax Research Journal, January-February 2008, Vol. XX.1.

Meanwhile, the national government instituted various poverty reduction programs out of the tax revenue, a major source of which is the VAT. One such program is *Pantawid Pamilyang Pilipino* Program (4Ps) being implemented by the Department of Social Welfare and Development (DSWD).

In addition to the 4Ps, the DSWD also implemented other social programs as part of the "*Katas ng* VAT" such as a one-time Php500 subsidy to qualified senior citizens and lifeline users of electricity.[21] Other programs funded by the "*Katas ng* VAT" include scholarships and loans to students, wives and relatives of transport workers, rehabilitation of areas damaged by typhoons and upgrading of public hospitals, among others.

V. CONCLUSIONS AND RECOMMENDATIONS

The passage of RA No. 9337 in 2005 significantly improved the VAT revenue in 2006 by almost two-thirds and registered moderate increases in succeeding years. Hence, R-VAT proved to have the ability to deliver the needed revenue to the government coffers and helped reduce its public debt and deficit. In addition, RA No. 9337 improved the efficiency of the VAT system although short-lived due to the passage of certain measures exempting certain transactions from the VAT.

VAT revenues were used to finance government's programs on education, health, environmental conservation and agricultural modernization. Furthermore, a fund called "*Katas ng* VAT" was used to provide a one-time subsidy to qualified senior citizens and lifeline users of electricity which directly benefited the poor. It also funded scholarships and loans to students, wives and relatives of transport workers, rehabilitation of areas damaged by typhoons and upgrading of provincial hospitals, among others. Moreover, VAT revenue shares of LGUs augmented their resources to finance basic social services.

In terms of sustaining the revenue productivity of the VAT, the government should avoid proposals, which seek to expand the coverage of VAT exempt transactions because these break the VAT chain which lead to higher costs and prices, and revenue losses to the government. It is worth noting that one of the features of the VAT is its ability to prevent the cascading of tax burden as it occurs along the VAT chain. Likewise, the VAT has a self-policing mechanism in the sense that it provides an audit trail for the government tax auditors to verify the accuracy of the output tax payments versus the input tax payments that may reduce the incidence of tax evasion. It is a well-agreed principle that for VAT to remain effective, it should be broad-based and with limited exemptions.

[21] DSWD 2008 Annual Report, p.10.