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Simplified taxation for MSMEs

Large businesses operating in the Philippines are insignificant compared to micro, small and medium enterprises (MSMEs) in terms of numbers. This is based on a 2013 Department of Trade and Industry report which shows that, out of a total of 941,174 business establishments, there are only 3,847 (.4 percent) large enterprises. The rest, which comprise the 99.6 percent, or 937,327 enterprises, are MSMEs. Of the total MSMEs, 90 percent are microenterprises.

The classification is based on asset value following the definition of MSME under Republic Act 9178, the Barangay Micro Business Enterprise law of 2002. Microenterprises are those with assets of not more than P3 million, small enterprises from P3 million to P15 million and medium enterprises from P15 million to P100 million.

Of significant mention are the microenterprises of more than 900,000 and described in a report as pertaining to those operating in the informal economy, not registered, not keeping books of accounts and not paying their taxes. These are the home-based businesses, small start-ups, single proprietors, individual service providers and the like. I must emphasize, there are more than 900,000 MSMEs out there operating beyond the borders of our tax laws.

This information is alarming but expected, considering the high tax rate and complicated tax system we have in the country. We hear of many stories where small and micro businesses would want to pay their taxes but ends up not doing so because of two reasons—first, the tax cost is too high to cause the closure of the business, and second, there is fear of inability to comply or sustain compliance because of the difficult and costly processes and requirements.

There are two models of a tax system—that which is complicated but fair and the other is simple but practical. Complexity in tax rules results from a desire to remove inequity and provide a fair system of taxation. Thus, the choice is between fair but complicated vis-à-vis simple but practical. The Philippine tax laws are patterned after US, which follows the first model. Other countries have chosen to sacrifice a bit of fairness in favor of practicality and simplicity. One good example is Singapore.

But in an economy where 90 percent of businesses are small and micro enterprises, a complicated tax structure exacerbated by a high tax rate, like ours, simply does not work. It does not and it will not work. Considering the profile of our taxpayers, 90 percent of which are micro and small, a complicated tax structure will only spur the growth of the underground economy and encourage noncompliance, especially in an environment where the chances of being caught is low, and even if caught, may still go unpunished or infractions fixed.

The taxation of MSMEs deserves a second look. MSMEs are a distinct segment of the taxpaying population that deserves a special tax regime. After all, they are the principal drivers of inclusive growth and while their contribution to government revenue may be small, they employ around 65 percent to 70 percent of the total work force.

What MSMEs need is a simplified form of taxation to encourage them to comply, help them grow, until they are ready to join the mainstream. Simplification should include simplified bookkeeping, simplified forms, simplified tax base (i.e., use of presumptive income bases, or final withholding taxes), reduced frequency of tax filing, file and pay anywhere, reduced compliance requirements, dedicated fast lanes and assistance at Bureau of Internal Revenue Centers, among others.

In addition, a lower tax rate for MSMEs should be considered. Malaysia, Thailand and Vietnam have adopted a two-tiered corporate-tax rate, where a lower rate of tax is applied to MSMEs. In Malaysia, for example, the tax rate imposed on MSMEs is 19 percent, which is 5 percent lower than the regular rate of 24 percent. Thailand, on the other hand, imposes a 10-percent tax on MSMEs, compared to the 20-percent regular rate, while Vietnam passed a law reducing the tax rate to 20 percent and which was applied retroactively for MSMEs. In the Philippines the same rate of 30 percent applies to all uniformly.

In this period of Asean regionalization, should we not do something to help ease the tax burden of our MSMEs, too?

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