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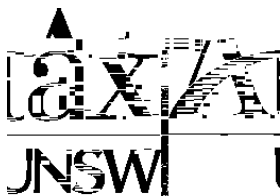
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South East Asian tax administration issues in the drive to attract foreign direct investment: Is a regional tax authority the way forward?

Timothy Brand¹, Alistair Hodson² and Adrian Sawyer³

Abstract

1. INTRODUCTION

1.1 Overview

Over recent decades, developing South East (SE) Asian nations have been the subject of monumental political, cultural and economic change. Association of South East Asian Nations (ASEAN) members such as the Philippines, Vietnam, Laos, Cambodia and Myanmar, are at varying points on the journey to development, yet the combined economic significance of the region is undisputable.⁴ In relation to Vietnam, Tran-Nam considers economic growth to be the most important determinant of economic development, with good tax policy a cause rather than a result of such progress.⁵

It has been argued that promoting economic growth is almost synonymous with attracting inbound foreign direct investment (FDI).⁶ The United Nations Conference on Trade and Development (UNCTAD) recognised that deciding whether to invest in a nation is a vexed decision, with a nation's 'policy framework' being one factor considered by potential investors, along with economic considerations (market size, infrastructure etc.) and the ease of doing business in the chosen nation.⁷ There is a plethora of research pertaining to the inverse relationship between corporate income taxes (CIT) and Gross Domestic Product (GDP), including Hartman's quantitative study.⁸ However, the majority of this literature is United States (US) centric in nature with a focus on inbound US investment, and thus fails to consider the tax administration challenges unique to developing countries. Despite this limitation, Hines' survey of multiple quantitative studies found an elasticity of -0.5 to -0.6 between CIT rates and FDI, which, due to being less than perfect, supports the view of the UNCTAD that the decision to invest in a nation is multifaceted and not solely dependent on corporate tax rates.⁹ Instead, an effectim151(no)11(t)-4(108(t30x9(i)6(n5(i)-4(ni)-4(s

facilitation' head due to the intrinsic link between tax administration and the ease of doing business. It is thus conceivable that tax administration issues can play a significant role in attracting FDI, giving a basis for the present study to test this relationship in addition to identifying current SE Asian tax administration issues relevant to foreign investors, and also investigating whether a Regional Tax Authority (RTA) may be an appropriate solution.

While some researchers have argued that 'externally imposed initiatives in tax administration are likely to be resisted, if not rejected, by local interests', they fail to explore the potential acceptability of a less radical proposal aimed at 'foreign interests' as opposed to 'local interests'.¹² Vehorn appositely observes that administrative

domestic compliance problems rather than the subcategory of administration issues which are of relevance to foreign investors. Despite this general trend, several papers contain analysis of issues relevant to the present study, including Chaikin and Dyball's study¹⁸ of the Philippines tax compliance and administration issues. Chaikin and Dyball's study surveys various compliance and administrative challenges in the Philippines, seemingly on the basis of pre-existing literature and empirical data. It is noted that corruption is rampant and so deeply entrenched in the Bureau of Internal Revenue (BIR) that the Philippines Congress has considered the BIR's complete disestablishment 'in favour of starting out fresh'.¹⁹

Additionally, Chaikin and Dyball refer to a 2008 Social Weather Station (SWS) survey gauging the extent that businesses encountered corruption in the revenue authorities. An alarming 71 percent of respondents reported having been asked for a bribe, 31 percent when paying import duties and 46 percent when paying income taxes. More telling, 79 percent of respondents did not report the solicitation accompanying these bribes as they believed that 'nothing would be done'.²⁰

Perhaps of greater relevance to potential investors, the corruption perceptions index (Transparency International) shows markedly high levels of perceived corruption in the Philippines.²¹ This index is calculated by country analysts through extensive surveying of business people, with unbiased hard data being inherently difficult to obtain on such a politically 'sensitive' issue.²²

As with Chaikin and Dyball, Tran-Nam's case study of Vietnam does not focus directly on tax administration issues relevant to foreign investors, yet it still notes several systematic administration issues relevant to the present study.²³ After critiquing the gradual lowering of CIT rates, Tran-Nam claims that 'administrative reform is

Another solution to many of the unique challenges faced by developing countries is the establishment of an autonomous or Semi-Autonomous Revenue Authority (SARA) operating under an organisational structure with many features in common with private sector organisations.³⁵ Devas, Delay and Hubbard, for example, note in this regard that the role of the government is to ‘steer, not to row’.³⁶ The authors state that the rationale behind a SARA is that independence from the government can yield greater efficiencies as a result of lower levels of corruption than is found in the public sector and being able to invest in sophisticated staff training. Mann adds that SARAs are typically introduced as a measure to remedy the lack of transparency in revenue authorities which can be indicative of corruption.³⁷

A more recent IMF survey of various SARAs found that they operate with varying degrees of autonomy, yet they share common features.³⁸ A later Organisation for Economic Co-operation and Development (OECD) analysis found that indicators of autonomy, or rather, the SARA’s ability to operate independently of government, include its independence in organisational planning and budget management, whether it sets its own performance measurement standards, and whether it has control over its human resource policies.³⁹ Through comparative analysis of SARAs in existence, Crandall found that 75 percent have empowered management boards, 70 percent operate outside the public service and 30 percent are funded independently by retaining a percentage of their tax collection.⁴⁰

With extensive use of the SARA model in Africa, Devas et al.’s study of the Ugandan experience exposes several weaknesses with this reform option.⁴¹ Uganda introduced a SARA to combat extensive corruption and staff training deficiencies that were thought to be the reason for its poor tax share.⁴² Devas et al. observe that ‘while the desired results were initially obtained with dramatic increases in tax share’, problems of corruption have re-emerged highlighting that SARAs ‘do not guarantee isolation from political interference, incompetence or malpractice’.⁴³ There is no discussion in the literature on whether the effectiveness of the SARA model in developing nations may differ if it were fully autonomous and operating at an international (or regional) level.

2.3 Reform proposal: A World Tax Organisation

While SARAs and LTUs are currently in existence, Sawyer proposed the forward looking and normative establishment of a World Tax Organisation (WTO) as a

³⁵ William Crandall, ‘Revenue Administration: Autonomy in Tax Administration and the Revenue Authority Model’, *IMF Technical Notes and Manual 10/12* (2010) <<http://www.imf.org/external/pubs/ft/tnm/2010/tnm1012.pdf>>.

³⁶ Nick Devas, Simon Delay and Michael Hubbard, ‘Revenue Authorities: Are they the Right Vehicle for Improved Tax Administration?’ (2001) 21(3) *Public Administration and Development*, 211–222.

³⁷ Arthur J Mann (2004), ‘Are Semi-Autonomous Revenue Authorities the Answer to Tax Administration Problems in Developing countries? A Practical Guide’ *Research paper for the project: Fiscal Reform in Support of Trade Liberalization* <http://pdf.usaid.gov/pdf_docs/PNADC978.pdf>.

³⁸ International Monetary Fund (2006), *Revenue Authorities: Issues and Problems in Evaluating Their Success* WP/ 06/240 <<http://www.imf.org/external/pubs/ft/wp/2006/wp06240.pdf>>.

³⁹ Organisation for Economic Co-operation and Development (OECD) (2009), *Tax Administration in OECD and Selected Non-OECD Countries: Comparative Information Series* (2009), (OECD, 2009).

⁴⁰ Crandall, above n 35.

⁴¹ Devas et al., above n 36.

⁴² Crandall, above n 35.

⁴³ Devas et al., above n 36, 213 and 221.

solution to certain tax challenges in ‘an increasingly integrated and globalised world with many cross-border transactions and companies operating across many jurisdictions’.⁴⁴ Sawyer proposes that the initial jurisdiction of such a body be limited to binding (advance) rulings and advance pricing agreements (APAs) accompanied by a dispute resolution function giving standing to private parties. Sawyer argues that over time, ‘through gradualism, an international organisation should assume ever greater authority for coordinating administrative tax policy and processes for cross-border business transactions’, although Sawyer adds the caveat that he is not a proponent of ‘complete harmonisation’.⁴⁵

Pinto and Sawyer reason that a WTO could have the subsidiary benefit of being a global ‘relationship bridge’ to share research and best practices in tax administration.⁴⁶ Usefully, their study examines the limited roles of a wide range of international organisations that may constitute ‘associations of tax organisations’, ultimately concluding that the proposed WTO would be an appropriate body for such a function. Sawyer acknowledges that his research ‘is certainly not the final work on the topic [of a WTO]’ with several aspects unexplored including the potential ‘expansion of its jurisdiction’.⁴⁷ The possibility of a regional tax authority with the independence and jurisdiction of the proposed WTO is also not examined by these studies.

2.4 Proposed regional tax organisations

was also examined, indicating that such ‘solutions’ have failed in practice due, primarily, to a failure to prevent the re-emergence of corruption. However, aspects of the LTU and SARA ‘solutions’, such as increased staff training, will be considered in the present study as possible features of the proposed RTA.

Likewise, the proposed WTO is radical in its conception and, although not directly concerned with the SE Asian region, contains several attractive features such as an accessible disputes settlement function and the issuance of binding rulings.⁵⁷ Sharkey’s proposed RTO is radical and extreme and could potentially be viewed as an ‘end point’ rather than a ‘starting point’ for reform.⁵⁸ Thus, it is clear that there have been no proposals in the literature exploring the feasibility of a less radical RTA acting as an intermediary between foreign investors and SE Asian States.

3. RESEARCH APPROACH

This study focuses on Vietnam, although some of the data collected relates to the wider ASEAN region as opposed to being Vietnam specific. This case study utilises mixed research methods, which primarily consisted of semi-structured interviews, but also includes phenomenological observations. Interviewees were asked questions pertaining to their perceptions of a potential RTA, both in relation to the identified administration issues, and whether it would likely prove attractive to foreign investors in their capital investment decisions.

3.1 Interviews

The interview subjects included three academics with knowledge of ASEAN tax administration, senior executives or tax managers of NZ companies that have invested or are considering investing in Vietnam, one who has worked for New Zealand Trade and Enterprise (NZTE) in SE Asia, and a NZ tax adviser, who provides advice to NZ companies on SE Asia market entry. For practical and ethical reasons, individuals currently residing in Vietnam were not interviewed. While this may appear to be a limitation, it was largely to improve the validity of the study, as individuals living in Vietnam may not feel that they are in a position to be ‘open’ to discussing challenges in the tax administration, and may subsequently provide opaque, misleading or false information.

With this study being explorative, there is no intention to seek to generalise the findings from the interviews. Nevertheless, it was our intention to interview a sufficient number of subjects so as to ensure any emerging themes had qualified support. Eight interviews were undertaken with the subjects selected on the basis of their expertise and experience concerning FDI and Vietnam. In the case of the academic subjects, these were selected from a very small pool of established Australasian researchers examining SEA tax administration issues. The senior executives, tax managers, and advisors were either key personnel in businesses that one of the authors had established prior contact with or were known to be actively involved in undertaking or advising on FDI in Vietnam.

⁵⁷ Sawyer, above n 44.

⁵⁸ Sharkey, above n 50.

The phenomenological observations were collected by one of the authors while living and working in Vietnam for three months from late 2012 through to early 2013. Unlike ethnography, the observations do not pertain to internal phenomena within the

NZ companies can get involved with infrastructure development in the region. The time is now. We will see more in the next 10 years in the way of demand for investment than the 5 years after that.

so it can be in a position to bid for projects with immediate start dates. However, Vietnam's political stability, relative to neighbouring ASEAN nations (which is inextricably linked to many tax administration functions), was also a fundamental investment consideration.

4.4 Vietnam/ASEAN tax administration issues

The present section of this paper identifies the tax administration issues that are currently of concern to foreign investors. Most of the findings were made in relation to Vietnam; however, several interviewees commented on issues encountered in other

I'm very risk averse. I don't want to be escorted off to a small room next time I land in Vietnam. I like to pay per the letter of the law, so I need to know what the law says I must pay or what I must do ... Also, to me, if you want to do long term business in a country, you need to do what is right, not what is perceived to be right.

The difficulty of ascertaining the correct legal position is also symptomatic of the broader administration issue of the difficulty of attaining binding rulings from tax authorities, as noted by 'Adviser B':

for NZ companies considering SE Asia market entry, as they will be able to clearly identify the tax ramifications flowing from the commercial decision of entering an Asian market. These themes are evident in the following comment by 'Company A':

If you got all [ASEAN] countries to buy into it, it would be attractive, it would be fantastic. It would add a lot of value. While we invest on the basis of commercial reasons, it would create certainty and predictability which is

There needs to be a cost sharing agreement between countries and users. The formula for cost sharing would have to take into account that some countries receive more FDI than others.

Moreover, 'Company C' warned:

Cost would be an issue, how much we would use it depends on how much it would cost.

'Adviser A' suggested:

Cost wise, it may be best to sit under ASEAN so that all countries can help pay for it, perhaps as a proportion of its tax take. Myanmar and other developing countries may go to the World Bank to pay for their share of it- this fits within their [the World Bank's] objectives.

4.5.7 *Political acceptability*

Interviewees were sceptical of whether culturally, politically and economically diverse ASEAN States would be willing to cede certain sovereign rights of taxing and cooperate as members of an RTA. 'Company A' observed:

Inter ASEAN rivalries are potentially a massive barrier. The underlying general hate of countries in Asia [pause] ... you'd be amazed, and it goes back hundreds of years. These countries are incredibly nationalistic and don't easily cede sovereignty.

Before further reasoning:

However, they have committed to the joint ASEAN vision of closer integration, and the AEC (ASEAN Economic Community) 2015.

As a result of these findings, it is clear that the bounds of the taxing rights signed over to the RTA by members would have to be well defined and narrowly drafted to cover only tax administration. Additionally, the RTA stands a greater chance of attracting developed nations such as Singapore if it is established under the ASEAN umbrella.

4.5.8 *Location of headquarters*

Interrelated to the aforementioned issue of the inter-ASEAN tensions and rivalries is the issue of where to domicile the RTA. It was suggested by 'Company A' that Indonesia's nationalism as a potential barrier can only be overcome with it being located in Jakarta:

Indonesia is problematic as they have announced that they wish to be self-sufficient by 2022. ... In saying that, the ASEAN secretariat is in Jakarta, so locating it there could be quite strategic.

However, the majority of interviewees thought that Singapore was the best location, both for investors and as an inducement to encourage Singapore to join the RTA. 'Academic B' stated:

With Singapore it would have to be 'tit for tat', you would have to give them some benefit such as locating it in Singapore. I think this is not acceptable to Vietnam as Vietnam has a good relationship with Singapore,

The RTA differs as it is at the international level, so is much more transparent, much more robust. It would be self-policing as each member could check each other.

4.7 Practical considerations

Certain practical considerations are inextricably linked to the feasibility of a potential RTA. A common theme to emerge was that an RTA should be representative of all member nations. In order to achieve this end, multiple interviewees suggested the establishment of a 'rotating' chair or secretariat, whereby each Member State would provide a secretariat to the RTA for a stipulated time period. Likewise, the dispute settlement function would retain judges and mediators from every state, but such personnel would not preside over disputes involving their home states. Therefore, a Vietnamese tax law being disputed by an NZ investor may be heard before a Thai judge. Interviewees thematically noted that certain functions of the RTA would have to be carried out by ASEAN nationals in order to maintain political 'palatability'. However, all academic interviewees identified the importance of employing expatriates for certain functions, such as TP data production, which require a high level of both independence and technical skill.

It became apparent from the interviews that a RTA is only feasible if it includes

5. A MORE RADICAL APPROACH?

An important aspect of this study was to assess the bounds of a potential RTA, including whether it could, through gradualism, morph into the more radical RTO proposed by Sharkey.⁶⁴ A common theme to emerge from those interviewed was that there would be crippling political resistance to Sharkey's RTO proposal. Interviewees viewed it as highly unlikely that nationalistic ASEAN States would be willing to surrender the high degree of sovereignty called for by the RTO. Instead, an RTA was viewed as far more feasible than an RTO.

A commonly identified reason for resistance was the differing levels of economic development and political mandate across ASEAN members. This is manifested in drastically different tax structures, as noted by 'Adviser B':

There are huge differences in the structure of tax systems across Asia. You have socialist regimes through to extremely free market regimes and tax is an important part of how they want to redistribute wealth. Many ASEAN nations have youthful populations; if you don't have a fair distribution of wealth, you would have riots and civil disobedience.

Similarly, 'Adviser A' added:

It would be impossible, but it [a RTO] would be a utopia, as it would make it so much more transparent and simple. It just wouldn't happen as these countries need to use tax as a tool to manage their economies.

'Academic B' emphasised the historical political tensions between ASEAN nations and how this may prohibit a convergence of tax policy:

For countries that have been fighting for independence for so long, I don't think they are ready to hand over such sovereignty. ASEAN countries have surprisingly little in common ... and are not that united. The RTA is just about right [in terms of feasibility] but they [ASEAN members] would never accept a RTO, as the differences are just too great to find a common ground.

All interviewees reasoned that a RTA was far more realistic. For example:

Pipedream! It [a RTO] has merits from an idealistic point of view, but has no chance politically or even practically.

'Company A'

The RTA proposed is much more realistic, each country involved will still want to have their own rights and set their own tax rates ...

'Company C'

⁶⁴ Sharkey, above n 50.

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In addition to the theme suggesting that an RTO would be unfeasible due to varying

The research also confirmed the findings of the UNCTAD⁶⁷ that foreign investment decisions are multifaceted, with investors taking into account a wide range of factors. Nonetheless, it was found that tax administration is a factor in such decisions. Therefore,

proposed RTA. However, this research also found that resistance to an RTO could come from investors who have a 'social conscience' towards the societies in which

with increased ease and certainty. Ultimately, this increased FDI and trade will benefit the economies of investors' 'home' nations which receive the benefits of the after tax profits from the increased offshore capital investments. It is hoped that the RTA proposed by this research will be further developed to contribute towards a 'win-win-win' solution for foreign investors, ASEAN nations and non-ASEAN investor 'home' economies.

7.2 Limitations

The present research contains several limitations and assumptions that warrant acknowledgement. First, it may be susceptible to criticism on the basis that it is fundamentally normative in nature. A further limitation of generalizability arises due to the methodology of a single country case study being used as a basis for the proposed RTA which will involve numerous SE Asian nations.

However, many of the interviewees commented not only on their tax administration issues in Vietnam, but also on many issues that they had encountered in other developing ASEAN countries. As discussed in the findings section, similar issues were found to exist in Vietnam, Cambodia, Indonesia and the Philippines. Comments made by interviewees suggested that Singapore, Malaysia and Thailand do not suffer from the same degree of tax administration issues as Vietnam, so certain findings may not be as generalisable to these ASEAN members. However, it should be noted that Vietnam can be viewed as at a 'mid-point' of development relative to other ASEAN members which acts to improve generalisability, illustrating the suitability of using Vietnam as a case study subject.

Additionally, it is arguable that the data collected with regards to Vietnam may not, in itself, be generalisable to the Vietnamese situation due to the small number of interviewees. Given the small potential pool of interview subjects, the interviews undertaken, together with the observations of one of the author's (phenomenology), collectively provide a justifiable means of collecting data pertaining to foreign investor administration issues, and enabling triangulation of the findings.

It is also assumed as a foundation of the present research that FDI leads to economic development, which leads to growth, which in turn, leads to improvements in living standards. This view is 'mainstream' and is not challenged by the present research in its discussion of why SE Asian nations should support the establishment of an RTA. Indeed, the existence of CIT competition in the region indicates that SE Asian nations hold a belief that increased FDI is in their economic interests. The present proposal does not address the issue of tax rate competition, and instead focuses on the significant benefits that can accrue from improving the region's tax administration.

7.3 Future research

The present research leaves many 'avenues' open for future research to explore. First, there is scope for the Vietnam case study to be replicated by future stu3(st)-4(r)219(s)-56351<0055>

- 2.3 Do you think that frequency of the tax administration issues discussed earlier in the interview would decrease with the establishment of such a body? Why/why not?
- 2.4 What are the potential challenges of establishing such a RTA?
- 2.5 Do you currently use a tax adviser in SE Asia? If so, would your use of such an adviser decrease or increase with the introduction of such an RTA? Why?
- 2.6 What resistance do you think such a proposal is likely to encounter? From whom? Why?
- 2.7 What features do you think should be included in the formation of such a RTA at the time of formation? Why?
- 2.8 What features do you consider to be the most important in order to maximise FDI? Why?
- 2.9 What features do you consider to be the least important to attaining the goal of maximising FDI? Why?
- 2.10 Do you consider it desirable for the jurisdiction of such an RTA to expand over time beyond the administration of taxes for foreign investors?
- 2.11 What features do you think should be added over time to expand the jurisdiction of the RTA?
- 2.12** (7KH LQWHUYLHZHU UHLWHUDWHV 1RODQ 6KDUNH\¶V UHFH
Review in 2013, for a South East (SE) Asian Regional Tax Organisation (RTO) which includes such features as the setting of a common tax rate among SE Asian nations through
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 UHVLGHQW¶ IRU WD[SXUSRHHV
- 2.12.1 What are your thoughts on this more radical approach compared to the less radical RTA proposal outlined above?
- 2.12.2 Would a single SE Asia tax rate administered by such an organisation be attractive to you when looking to increase its investment in the region?

3. Additional questions for the interview subjects who are academics:

- 3.1 Could such an RTA be effective in countering transfer pricing uncertainty? If so, how?
- 3.2 How do you think such an organisation be structured/formed? By treaty? By any other method?
- 3.3 Who do you believe should be employed by the RTA to maximise effectiveness? SE Asian nationals? Expats? Why/why not?
- 3.4 What accountability mechanisms do you consider it important to include in such a body?
- 3.5 What are the advantages/disadvantages of establishing such an organisation as an extension of ASEAN as opposed to under an independent treaty or any other method?

3.6 Do you consider such an RTA to be a better solution than the OECD Semi-Autonomous Revenue Authority (SARA) model (*interviewer explains if required*) in countering the tax administration issues faced by foreign investors? Why/why not?

4. For all interview subjects:

4.1 Are there any other comments that you wish to make?