REPLACEMENT OF SALE TAX BY COST TAX FOR EFFICIENT TAXATION IN VIETNAM AND OTHER DEVELOPING COUNTRIES

Loi, Ta Van, School of trade & international economics, National economics university of Hanoi, Tran Dai Nghia str., Hanoi, Vietnam, 84903434688, loitv@neu.edu.vn; taloiktqd@yahoo.com.vn.

I. INTRODUCTION

Almost every country in the world applies sale tax or VAT in their tax system. There are a many reasons why governments get fewer taxes than they should in this system. In USA the government applies "sale tax". Retailing companies collect sale tax from the client but the government is not sure to get the same tax amount collected from the customers. Each year the loss is estimated to be about a hundred billion dollars of sale tax on remote sale such as internet sale, mail order, telephone sale..., reported by Peter franchot (2011)-Maryland remote sale tax loss study. Europe uses Value Added Tax (VAT). In Europe, the VAT's avoidance is estimated to be about 107 Billion € in 2006.

In Vietnam, the situation of VAT implementation is really bad. In 2009, the VAT avoidance is about 442.3 Billion VN Dong. More than 607 companies in the nation involved in problems with VAT, 63 companies among them simply disappeared. Government tries to get tightly tax control the tax collection with a huge tax collection team. The expenditure for tax collection is so much but the results are not very good.

It is about time to think about new tax law. This paper recommends – Cost tax instead of sale tax in The USA or Value added tax in other countries. Author believes that Cost tax will do better job at tax collecting and other goals achieved by efficient tax collection system. Because the Cost tax will companies to control their cost in order to reduce tax burden. This will result in lower cost of doing business. Lower costs will make companies to become stronger competitors and increase their ability to effectively compete in the global market – With low cost countries like China.

In The USA, the Sale tax applied in 50 states instead of Value added tax. Sale Tax only pays an attention retail sale group in collecting sale tax. Under sales tax system, the situation of tax avoidance still happens when the company hides the profits in business. The tax rate of profit is about 35% while tax rate of sale is only 9% or little more. It quite easy to avoids income tax by declaring high production cost and avoid sale tax through remote sale. Tax loss seems to be an overlapping issue.

In others countries which use Value added tax (VAT) faces the same tax loss issues. It is not the remote sales but it is hidden revenue. Companies do not have to control the expenses very carefully. They would like to hide the profit by higher production cost declaration.

II. REVIEW EXISTING RESEARCH

In The USA, the issues of sale tax loss through remote sale especially digital goods are very serious. As the study of Peter Franchot (2011) about Maryland remote sale tax loss shows that estimated foregone sales tax loss of 219.3 Million USD in Maryland only. The forecast of foregone sales tax loss is under table:

Table 1: Estimated Foregone Sales tax revenue from remote Sales ($ in Millions)

CY	Electronic remote sales		Non-Electronic remote sales		Total
	B2C	B2B	B2C	B2B	
2010	79.1	18.1	85.4	15.7	198.4
2011	91.2	19.3	93.4	15.4	219.3
2012	100.9	20.5	98.2	15.1	234.8
2013	111.9	21.8	103.3	14.8	251.8
2014	120.2	23.0	105.4	14.5	263.1
2015	127.0	24.2	105.7	14.3	271.2
2016	133.6	25.4	105.6	14.1	278.7

Source: Maryland remote sales tax loss study by Peter franchot

Other is income tax losses also happened with tax asymmetries- reported by Rosanne Altshuler, Alan J. Auerbach, Micheal Cooper and Matthew Knittel (2008) in their study of Understanding US Corporate Tax losses from National Bureau of Economic research. Tax asymmetries is that the firms will be able to use carry- back and carry- forward provisions to get nearly full value from deduction of losses. Losses over income in three industrial categories accounting for the largest share of net assets in 2005: manufacturing, finance and information are growing from 6% to 10%, especially in financial from 21% to 41% in 2005. Income tax rate is from 15% to 39% and flat rate is 34% for income earning over 335.000$ and 35% for service companies.

In Vietnam, corporate income tax losses are serious. Companies, both private and state, use two accounting system, one for business administration one for tax declaration. The main purpose is raising the cost deductibility when paying taxes. Each one Dollar they hide they will save 0.25 dollar for not paying corporate income tax. There are so many research (like Booming in VAT avoidance by Laszlo Kovacs, VAT still have trouble during 13 years implementation by HoaiThuong and LePhuong …), focus on the tightening procedures such as control the form of Bill or invoice issued by the firms, enforcement of tax declaration by tax officers.

For example, a company sells the wooden table at price of 1.000$. He has to pay 600$ for input and 200$ for added value. He will get 200$ of profit. Sale tax rate is 9% (In the USA) or Value added tax is 10% (in Vietnam) and the income tax rate is 35% in USA and 25% in Vietnam. The counted table for tax declaration as bellows: *(See table2)*

Actually, Companies seldom make an attempt to reduce his cost or declare exact profit amount. The company can declare the cost at 900 or more for avoiding the income tax. In countries which use VAT, the same situation happens. The input tax amount will be deducted by output tax amount. The government collects in each stage of making the goods or service. But the tax avoidance and tax base is used twice in calculating VAT and income tax.

Each dollar of cost the firm carry-forward to the selling price they will save 0.35$ in USA (or 0.25$ in Vietnam). However, the firm tries to hide the revenue when they sell the digital goods or remote sales in order to avoid both Sale tax and corporate income tax.

TABLE 2: EFFECT OF SALE TAX AND VALUE ADDED TAX

	Items	Sale Tax (IN USA)			VAT (In Vietnam)		
		Tax base (USD)	Tax law	Tax amount		Tax amount	Disadvantage
1	**Input value**	600			VAT tax 10%	-60	Return 60$, complex procedures
2	**Cost**	800					May be declare untruth
3	**Selling Price**	1.000	Sale Tax 9%	+90	VAT tax 10%	+100	+ Double taxation because 1.000$ including 200$ of profit.
4	**Profit**	200	Income Tax 35%	+70	Income tax 25%	+50	
	Total			**+160**		**+90**	

III. COST TAX – NEW IDEA FOR AN EFFICIENT TAXATION

In the truth, the revenue and profit have been controlled by sale tax, VAT and corporate income tax but the cost is not controlled by any law. Thus, firms try to get more profit under tax asymmetries. Thus, How to control the cost officially? The cost control should be considered in this case.

Supposed the above-example but the wooden table will be imposed by cost tax or the cost added tax at rate of 16% and 22.5%. These tax rates are the same applied for corporate income. It is clear on the table 3 bellow:

TABLE 3: EFFECT OF COST TAX (COST ADDED TAX)

	Items		Cost tax in USA		Cost added tax in Vietnam		Advantage
			Tax law		Tax law		
1	**Input**	600					
2	**Added Cost**	200			CAT 22.5%	+45	*Encourage to declare the truth*
3	**Total cost**	800	Cost Tax 16%	128			
4	**Price**	1.000	-	-	Nil		*No double taxation*
5	**Profit**	200	Income tax 16%	32	Income Tax	+45	To declare freely
	Total			+160		**+90**	

The US government still collects the same tax amount at 150$ for this case but firms could avoid

corporate income tax. If they declare their cost is not right. It may be over 800$ they will avoid 0.16$ per 1 dollars of income tax but they will pay 0.15 $/1 dollar of cost tax. The firm gets nothing for his trick so that company will declare the true cost. The government doesn't need to check them every time.

The company will take care of their added cost in business administration. They attempt to reduce cost to get more advantage and focus on "low cost strategy" than that of rivals. The government will collect tax by two ways:

Firstly, we can apply cost added tax as other countries have done like France, Belgium…

Secondly, we can collect one time when selling the goods like sale tax. Now we can apply cost tax as the whole-sale or retailer declares. We can save the time of checking and monitoring their activities and their contribution.

The most advantage of Cost added tax law is ***Optimization*** of gross product in society.

Supposed that there are two furniture companies in society. They produce the same goods (for example: wooden table) but their cost is different. The first company (company A) has to pay 600$ for making a wooden table but the second company (company B) has to pay 800$ for making the same wooden table. The company B use old technology, machine or/and lack of management skills. If both of them exist in society and share natural material allocation, the inefficiency will occurs. The company B makes wooden table inefficiently because they use much more raw material. The company B still exists if he has profit although it is very little. When we apply the cost added tax law the situation will be changed as the following table 4:

TABLE 4: OUTCOME AFTER APPLYING COST TAX LAW

No.	Items	Company A	Company B
		Use 0,6 m3 wood for making 1 wooden table set	*use 0,8m3 wood for making the same 1 wooden table set*
1	Cost tax basic	600 USD	800 USD
2	Cost tax rate	16%	16%
3	Cost tax amount	96USD	128USD
	Envisaged Action	Can cut down selling price if necessary (rivalry is strong, leading price…)	***Firstly:*** Try to reduce the cost, If not choose the 2nd way ***Secondly:*** Withdraw out of this production field.

We supposed that our country exploits 4.8 million m3 of wood material per year only. If these resources will be allocated by two companies, the output of wooden table is never reaches at 8 million sets. If the company B only reacts by two ways bellows:

The first way: If the company B try to reduce cost by improving management skills, upgrading machine and changing new technology, the cost should be reduced at/or lower than 600USD. At that time, material will be used efficiency and then total output will be at/or more than 8 *million sets*.

The second way: If the company B withdraws out this production field, the raw material will be allocated to company a (more effective). The total output of wooden table will be at 8 *million sets.*

IV. SUMMARY AND CONCLUSIONS

Generally, tax is contribution to government for public commodities. Any government needs funds for their operation. But the tax system must have been fair and independent. The normal formula is:

Total revenue = total cost + total profit (1)

If we impose tax on revenue by sale tax or value added tax that will guide the consumers choosing the necessary goods but the revenue amount consists of cost and profit. Once again, the profit will be imposed by corporation income tax that it is double while the cost will be controlled by firms freely.

The cost tax will force all firms to pay more attention to operation of business and controlling the costs. The more firms make the goods with lower price the more jobs they create in domestically and be more competitive without moving to other lows cost labor countries. We can see most consumer goods sold America are from China. May be the trade balance will be changed if Americans can make more goods domestically with the same price with China or others.

Although the above example the economic benefits of Cost tax is illustrated, show how to make the tax contribution fair? The tax rate is very important for tax system to promote efficiency and fairness in economy. Study suggests the following chart of setting tax rate and fitting fiscal budget:

- Step 1: calculating the tax burden in the economy as bellows:

Absolute tax burden:

$$K_a = \frac{\sum_{i=1}^{n} Ti}{\sum_{i=1}^{n} Pi} \qquad (2)$$

Ka: Absolute tax burden Index.

Ti: Tax contribution on i product; i: object pay tax

Pi: Profit of i product; n: times of tax payable.

And Relative tax burden:

$$K_b = \frac{\sum_{i=1}^{n} Ti}{\sum_{j=1}^{m} Tj} \qquad (3)$$

Kb: Relative tax burden Index; i, j: Objects pay tax.

Ti: tax contribution of i product; n: times of tax payable on i product.

Tj: tax contribution of j product; m: times of tax payable on j product.

- Step 2: balance tax contribution on general formula

Tax-to-GDP ratio on national budget. $= \sum_{,j=1}^{m} Tj1+Tj2+...+Tjn = \sum_{i=1,\, j=1}^{n,m} Tij$ *(4)*

Consist of:

Tj1...Tjn: *Tax contribution from first time to n times of i product.*

i: *Object pay tax*, n: times payable tax of i *product.*

j: *type of j industry, m number of different type of industries in economy.*

- Step 3: To determine the product and type of industry that get more tax incentive and tax burden in entire economy

When we balance economy we will eliminate the free adjustment of local authority. In some case, the local authority will be providing too much tax incentive to investor but they never consider about the budget deficits. The conflict between tax incentives will be compensated by other tax burden. The government will balance in general without unduly interfering into economy.

Other impact of cost tax pushes the monopoly status stronger. When the raw material is shared by a few strong companies, it will make them monopoly in their field. The government should have more anti-monopoly acts and methods to accompany Cost Tax Laws.

REFERENCES

[1] Nhµ xuÊt b¶n tµi chÝnh, *HÖ thèng ho¸ c¸c v¨n b¶n ph¸p luËt vÒ thuÕ gi¸ trÞ gia t¨ng ®· ®-îc söa ®æi bæ sung*, Hµ Néi, 2005.

[2] Hoµi Th-¬ng-Lª Ph-¬ng, *Thuế VAT sau 13 năm vẫn nhiều bất cập*, www.dantri.com.vn, 2010.

[3] Laszlo Kovacs-Cao uû EU vÒ thuÕ quan, *Bïng ph¸t gian lËn thuÕ VAT*, www.vnexpress, 2006.

[4] Ben Terra & Peter wattel, *European Tax Law*, Kluwer law international, third edition, 2001.

[5] E. Verwaal & S. Cnossen, *Europe's new border taxes*, Erasmus University research Memorandum 008, 2009.

[6] Peter franchot – comptroller of Maryland, *Maryland remote sale tax loss study*, 2011.

[7] Rosanne Altshuler (Rutgers University), Alan J.Auerbach (University of California, Berkeley), Micheal Cooper (U.S Department of Treasury), Matthew Knittel (U.S Department of Treasury), *Understanding U.S. Corporate tax Losses*, Presented at NBER Tax Policy and economy conference Washington DC, October 6, 2008.