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A Study of Public Finances in Thailand

(In Four Volumes)

Volume I: The Main Report

October 31, 1974

East Asia and Pacific Department

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CURRENCY EQUIVALENTS

Currency Unit - Baht

US $1.00	=	B20.00
฿ 1.00	=	US $0.05
฿ 1.00 million	=	US $50,000
฿ 1.00 billion	=	US $50 million

Note: The Baht was maintained at a parity of ฿ 20.8 = US$1.00 until July 1973 when it was revalued to ฿ 20.0 = US$1.00. An average exchange rate of ฿ 20.4 = US$1.00 has been used for 1973 in this report.

FOREWORD

This report is based on the finding of a Public Finance Study Mission that visited Thailand from January 10 to February 8, 1974. The Mission consisted of Oktay Yenal (Chief), Kazuko Artus (Fiscal Economist), Karl Stichenwirth (Public Enterprises), Kenneth Hubbell (Local Finance and Regional Development), James Theberge (Industrial Incentives), and was assisted by Lawrence Hinkle (Country Economist) and Bernard Schmutz (Resident Economist). Woo Sik Kee contributed to the analysis of taxation. Ubolwann Binmahmood was secretary to the Mission.

The report was updated and revised after discussions of the draft with the Government.

The Mission gratefully acknowledges the assistance of the Thai Working Group under the chairmanship of Dr. Amnuay Viravan and later Mr. Nukul Prachuabmoh. The members of the Working Group contributed substantially to the preparation of the report and commented on an earlier draft. Naturally, they bear no responsibility for the contents, interpretations and the conclusions of the report.

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I. INTRODUCTION

1. This report examines developments in public sector expenditures in Thailand and analyzes the problems that may arise in the management of the government's economic activities in the next five years. The study focuses on structural issues. Developments in the immediate future are included only where they throw light on the prospect for the medium term.

2. The issues for the public sector are discussed under three major topics: resource needs and availabilities, fiscal policy, and financial organization and management. Corresponding to these, the basic questions to which answers are sought are the following: what will the expenditure needs of the public sector be in the next five years, and how can these "best" be financed? How can the efficiency in this sector be improved? In what ways can the benefits of the public services and the burden of financing these be "more equitably" distributed?

3. These questions have not received explicit attention in the development plans or other government programs. The public finance section of the Third Five Year Development Plan (1972-1976) is concerned only with a loosely defined "developmental" component of the public sector activities. This concept includes most of capital expenditures and some of current expenditures, but is not clearly related to either, the actual classification of individual expenditures being determined on an ad hoc item by item basis. The government sector is treated in the framework of national accounting concepts which are not translatable to fiscal categories. Nor does the government - which is a transitory government until the elections - have a public sector expenditure program extending beyond the next year.

4. This review has not arisen out of any acute crisis either in the economy in general or in the sphere of public finance developments. Over the past decade, Thailand's economic performance has been credible in almost all respects. Growth achieved was respectable; until last year prices were extremely stable; and the distribution of benefits from growth, though far from satisfactory, has very recently improved. There are signs though that the situation may be deteriorating in the fiscal area. Cash deficit has expanded rapidly from the mid-1960's to FY1971/72. The ratio of public expenditure to GDP which had exceeded 21 percent in FY1970/71 and FY1971/72 is estimated to fall below 19 percent in FY1973/74. The decline in the ratio is attributable to real declines in capital expenditures. The present system of public finances does not seem to be elastic enough to respond to the increasing needs of the economy.

5. A summary description of the public sector structure in Thailand is followed by examination of future expenditure needs and financing prospects for the public sector. Since the Five Year Plan is outdated -and does not set targets for fiscal magnitudes in any case - and since no other public sector plans or programs covering the next five years exist, information for

this discussion had to be derived from historical trends and the partial programs of some public agencies. Probable public sector expenditure requirements are described and compared with future financing prospects. The discussion concludes with an overview of the financing requirements of the public sector in the medium term.

6. The three chapters following this survey are concerned with major issues in fiscal policy. The chapter on taxation reviews the three important types of taxes - income taxes, commodity taxes and property taxes - and offers recommendations for improving the structure of taxation in Thailand. The taxation of rice as it relates to the agriculture sector and the fiscal incentives for the promotion of industry and exports are discussed separately in this chapter. The chapter on state enterprises reviews their future financing needs and prospects and examines the pricing policies and taxation issues of the most important entities. The chapter on local finances concentrates on fiscal policies at the local government level and makes recommendations on intra-governmental financial arrangements.

7. The last chapter is devoted to a discussion of the organizational and administrative issues in Thai public finances. Topics stressed in this section are: planning and budgeting, budgeting at the local level, debt management and tax administration. Conclusions and recommendations are summarized at the end of the report.

Structure of the Public Sector

8. The public finance system in Thailand is highly centralized, reflecting the structure of public administration in the country. The central government accounts for a predominant share in the consolidated revenue and expenditure of the public sector, as shown by Tables 1 and 2. Over the last decade, the central government has consistently accounted for about 90 percent of the consolidated revenue and about 84 percent of the consolidated expenditure of the public sector. However, the impact of the central government on the allocation of expenditure is larger than this suggests since the forms of transfers to local governments and to state enterprises determine, to a large extent, the ultimate use of these funds.

9. The central government is the principal supplier of public services in the country. It is exclusively responsible for defense, police services, industrial promotion, irrigation and land settlement. It furnishes the bulk of social services, although local governments also participate in this area. In education, municipal governments are responsible for primary schools within their precincts, but the central government is responsible for all other services including the supervision of private and municipal schools. In health care also local government participation is limited, and most public health care services are provided by the central government hospitals and health centers.

TABLE 1: PERCENTAGE SHARE OF PUBLIC SECTOR REVENUE
FY1966/67 - FY1972/73 Average

Central Government	
Current Revenue	81.5
Extrabudgetary Treasury Receipts	3.5
Foreign Grant Receipts	4.9
Central Government Revenue	89.9
Local Government Revenue 1/	4.8
State Enterprise Operating Surpluses 2/	5.4
Consolidated Total	100.0

1/ Net of transfers from the central government.

2/ Net of contributions to central government budget.

Source: Tables B-1 and B-2 of Annex B.

TABLE 2: PERCENTAGE SHARE OF PUBLIC SECTOR EXPENDITURE
FY1965/66 - FY1972/73 Average

Central Government	
Total Expenditure	90.0
Less: Transfers to the Rest of Public Sector	-5.6
Central Government Direct Expenditure	84.4
Local Government Expenditure	5.5
State Enterprise Gross Fixed Capital Expenditure	10.1
Consolidated Total	100.0

Source: Tables B-1 and B-2 of Annex B.

10. The central government is directly responsible for the construction and maintenance of highways, water supply in non-metropolitan areas, postal service, and international telephone service. Other public utilities - electricity, metropolitan water supply, TV broadcasting, domestic telephone service, air transportation, port administration, railway services and housing - are provided by state enterprises, but the central government controls their pricing and investment policies. State enterprises are defined as establishments in which the government holds more than half of the equity. The legal forms range from enterprises established by specific act (e.g., Electricity Generating Authority of Thailand) or by Royal Decree (e.g., Express Transit Organization) or under the commercial (e.g., Thai Tobacco Monopoly). State enterprises are discussed more extensively in Annex D.

11. Local administration is conducted by two types of agency. There are, firstly, branches of the central government in the provinces referred to as the "provincial administration." The primary unit under this system is the province (changwat). At present there are 71 such territorial units, each under the administrative control of a governor who is appointed by the central government (by the Undersecretary of the Ministry of Interior in the case of non-metropolitan provinces, and by the Cabinet in the case of the Bangkok Metropolis). Secondly, there are the institutions of "local self-governments" which exist in four forms: the Bangkok Metropolitan Government, provincial government, municipal government and sanitary district government. These agencies are concerned more with the provision of social and community services than with general administration per se. The weight of local governments in the Thai public finance is very low. Their total current revenue accounts for only about 5 percent of the consolidated revenues of the public sector.

II. RESOURCE NEED AND AVAILABILITY

Public Expenditure

12. Details of the Thai public sector accounts are given in Annex B. According to these figures, the ratio of public expenditure to GDP increased from 16.7 percent in FY1965/66 to more than 21 percent in FY1970/71 and FY1971/72. 1/ The ratio declined in FY1972/73 to 19.6 percent, and the estimates for FY1973/74 show a further decline to less than 19 percent. The principal factor causing the steady rise in the ratio in the period from the mid-1960's to the early 1970's was a rapid increase in the expenditures of the central government. The decline in FY1972/73 and FY1973/74 reflects a slowdown in the rate of increase in central government current expenditure and real reductions in the capital expenditures of central and local governments.

13. The patern of public expenditure also showed deviations from the trend. Up to FY1970/71, the shares of expenditures were increasing for education, irrigation, security (defense and police) and interest payments. In FY1971/72, the expenditure share for education and interest payments continued to increase but that for irrigation declined and the share for security remained unchanged. In FY1972/73 and FY1973/74, the expenditure shares for most social services (including education) and economic services declined, while the increase in the share of interest payments continued.

1/ "Public expenditure" refers to the consolidated total of central and local government expenditures and state enterprise expenditure for gross investment in fixed assets. The definitions of terms used here are consistent with those in the public sector accounts of Annex B. They differ a little from the definitions used in the IBRD Economic Reports, which adopt the Bank of Thailand terminology. See Annex B for the differences.

TABLE 3: PUBLIC SECTOR ACCOUNTS 1/
(Millions of Baht)

	FY1966	FY1967	FY1968	FY1969	FY1970	FY1971	FY1972	FY1973	(Estimates) FY1974
Expenditure	16,222	19,331	22,743	26,059	26,923	30,580	33,290	37,106	44,804
Current	10,540	12,733	14,565	16,683	17,590	19,629	21,928	24,669	31,188
Capital	5,796/2	6,777/2	8,322	9,550	9,525	11,122	11,515	12,608	13,616
Unidentified Transfers	--	20	--	--	--	--	--	--	--
Adjustment	-114	- 199	-144	-173	-193	-171	-152	-170	--
Revenue	n.a.	18,552	19,913	22,144	22,727	24,146	25,195	29,660	39,585
Current	n.a.	16,558	18,251	20,107	20,888	21,411	23,795	28,045	37,978
Tax Revenue (Central & Local Govts.)	13.533	15,378	17,105	17,485	17,947	18,389	20,074	26,286	37,125
Non-Tax Revenue (Central & Local Govts.)				1,643	1,761	1,869	2,421		
State Enterprise Operating Surpluses	n.a.	1,180	1,146	979	1,180	1,153	1,300	1,759	853
Foreign Grants	891	1,016	1,274	1,464	1,022	1,165	892	857	807
Net Extrabudgetary Treasury Receipts	286	978	388	573	817	1,570	508	758	800
Deficit	n.a.	767	2,872	3,899	4,240	6,445	7,813	7,314	5,401
Expenditure less Revenue	n.a.	779	2,830	3,915	4,196	6,434	8,095	7,466	5,219
Adjustment for Time-Lags	25	-12	42	-16	44	11	-282	-132	182
Financed by:									
Net Foreign Borrowing	129	132	43	-165	-11	188	490	1,209	1,969
Net Domestic Borrowing (Non-Monetary Authority)	2,339	1,737	1,480	407	672	2,894	6,843	5,144	2,704
Non-Bank Public	49	-152	171	73	81	8	191	369	244
Government Savings Bank	871	1,108	611	496	435	766	1,455	2,212	2,079
Commercial Banks	1,419	781	698	-162	156	2,120	5,197	2,563	381
Other Sources	n.a.	-1,102	1,349	3,657	3,579	3,363	480	961	728
Bank of Thailand	161	-320	351	3,773	3,405	2,167	174	1,536	40
Exchange Equalization Fund	-40	5	77	-32	15	191	244	-370	---
Counterpart Fund	141	-78	-64	-14	-120	51	-94	-32	3
Coin Issue	80	54	101	61	55	138	17	121	151
Cash Balances	n.a.	-763	884	-131	224	816	139	-294	534
Memorandum: GDP in Current Market Prices 2/	97,100	106,560	114,650	125,620	134,100	142,990	156,460	189,300	239,600

1/ See Section II of Annex B for explanation of terms

2/ Revised GDP estimates of August 1974.

Source: Table B-1 of Annex B

TABLE 3a: EXPENDITURE AND REVENUE OF PUBLIC SECTOR AS PERCENT OF GDP 1/

	FY1966	FY1967	FY1968	FY1969	FY1970	FY1971	FY1972	FY1973	FY1974
Expenditure									
Current Expenditure	10.9	11.9	12.7	13.3	13.1	13.7	14.0	13.0	13.0
Capital Expenditure	6.0	6.4	7.3	7.6	7.1	7.8	7.4	6.7	5.7
Adjustments	-0.1	-0.2 2/	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-
Total	16.7	18.1	19.8	20.7	20.1	21.4	21.3	19.6	18.7
Revenue									
Current									
Central Government Tax Revenue	11.8	12.5	13.0	13.2	12.7	12.1	12.2	12.0	13.7
Central Government Non-Tax Revenue	1.3	1.1	1.2	1.1	1.2	1.2	1.4	1.3	1.0
Local Government Revenue	0.9	0.8	0.8	0.8	0.9	0.9	0.8	0.6	0.8
State Enterprise Operating Surpluses	n.a	1.1	1.0	0.8	0.9	0.8	0.8	0.9	0.4
Sub-Total	n.a	15.5	15.9	16.0	15.6	15.0	15.2	14.8	15.9
Foreign Grants	0.9	1.0	1.1	1.2	0.8	0.8	0.6	0.5	0.3
Net Extrabudgetary Treasury Receipts	0.3	0.9	0.3	0.5	0.6	1.1	0.3	0.4	0.3
Total	n.a.	17.4	17.4	17.6	16.9	16.9	16.1	15.7	16.5
Deficit 3/	n.a.	0.7	2.5	3.1	3.2	4.5	5.0	3.9	2.3

Source: Tables B-1 and B-2, Annex B

1/ Revised GDP estimates of August 1974 were used.

2/ Including unidentified transfer payment from the central government, which was 0.2 percent of GDP.

3/ Expenditure less revenue adjusted for time-lags in the payments and receipts of intra-public sector transfers.

TABLE 4: COMPOSITION OF PUBLIC EXPENDITURE
(As Percent of Total)

	FY1966	FY1967	FY1968	FY1969	FY1970	FY1971	FY1972	FY1973	FY1974
General Administration (Current)	11.1	13.6	13.1	12.8	10.2	10.2	8.3	10.7	13.3
Defense and Police (Current)	17.2	16.4	17.0	17.8	20.5	20.8	20.8	19.8	21.7
Education	14.2	13.7	15.1	14.8	15.0	16.5	17.6	16.4	15.4
Health Care	3.9	3.2	3.2	3.0	2.7	2.9	2.9	2.5	2.3
Water Supply	1.4	1.0	1.3	1.4	1.5	1.8	1.9	2.3 1/	2.1 1/
Power (Capital)	3.4	3.6	4.2	5.9	6.0	4.9	5.9	6.9	4.9
Communication and Transportation	14.6	15.7	16.4	17.0	16.5	14.6	13.6	13.5	12.8
Of which: Highways and Roads	(8.9)	(11.0)	(11.9)	(11.7)	(11.1)	(10.5)	(10.9)	(8.7)	(8.0)
Agriculture	8.8	9.1	10.1	8.7	10.0	9.8	7.4	6.4	6.1
Of which: Irrigation	(5.4)	(5.5)	(6.7)	(5.2)	(6.6)	(6.7)	(4.8)	(3.8)	(3.4)
Persons	2.8	2.4	2.1	2.1	2.2	1.9	2.3	2.1	1.9
Interest Payments	4.0	4.4	4.4	4.3	5.1	5.9	7.3	7.7	8.2
Other 2/	18.4	16.9	13.3	12.3	10.4	10.8	12.1	11.7 3/	11.4 3/
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Current	65.0	65.9	64.0	64.0	65.3	64.2	65.9	66.5	69.6
Capital	35.7	35.1	36.6	36.7	35.4	36.4	34.6	34.0	30.4
Adjustments etc. 4/	-0.7	-0.9 5/	-0.6	-0.7	-0.7	-0.6	-0.5	-0.5	-

Source: Table C-2b of Annex C

1/ Capital expenditure only. Current expenditure included in the figures for other years was about 0.2 percent of the consolidated public expenditure in the period from FY1969 to FY1972.

2/ Mainly the expenditures of which the purposes are not identifiable. "Adjustments etc." in the last row are also included.

3/ Current expenditure for water supply is included, as its magnitude is not identifiable.

4/ Adjustments for double counting and for "unspent balance" of the budgetary funds disbursed from the central government treasury (see Annex B).

5/ Unidentified transfer of ฿ 20 million (0.1 percent of consolidated total expenditure) is included.

14. Public services in Thailand, as in most developing countries, need to be improved. Elementary education is compulsory, and yet there are villages with no primary schools within a reasonable distance. Public health services reach only one-third of the total population. Most rural roads are in such primitive condition that villages are isolated in dry season when water transport cannot operate, and the Bangkok metropolitan area suffers from heavy traffic conges-tion. Increased expenditures for social services are needed to reduce income disparities among regions, to equalize opportunities among individuals, and to improve the living conditions of an increasing population. Larger expenditures for economic services and infrastructure are necessary to maintain the growth of productivity in the economy. The extent of public services to be provided, and the expenditure this would entail, depend on the objectives of the society and the costs of providing the necessary finance. A projection of public expenditure without taking account of financial constraints would not be realistic. On the other hand, the discussion of a feasible finance effort must be based on some ideas about the urgency of expenditure needs. These are topics which would be best analyzed in the context of national plans. Since the existing plan does not provide such a ready basis, the Mission attempted to piece together the relevant information to arrive at some meaningful scenarios for desirable cum feasible public sector expenditure levels and financing alternatives.

15. Examination of past public expenditure and the impressions gained in the course of interviews with the Thai government officials suggest that the recent decline in public expenditure relative to GDP reflected a tightening financial constraint imposed by the slow increase in revenue. The rising trend in the public sector's revenue relative to GDP had already come to an end by FY1968/ 69; after this there occurred a decline in the ratio of revenue to GDP. 1/ The public sector sustained rising level of expenditure for a while by drawing on cash balances and borrowing heavily from the banking system. In FY1971/72 the excess of public expenditure over revenue equalled 5 percent of GDP. It was the attempt to restrain the size of borrowing and hence the deficit that brought down the ratio of public expenditure to GDP in FY1972/73.

16. Looking at eht recent developments in public finances and public service supply, we consider that the ratio of public expenditure to GDP should not be less than 22 percent, which is slightly higher than the average ratio for FY1970/71 and FY1971/72. This minimum level will be referred to as the "floor target" for public expenditure in the period from FY1973/74 to FY1979/ 80.

1/ "Revenue of public sector" is also defined in this report a little differently from the definitions in the IBRD Economic Reports, which adopt the Bank of Thailand terminology. Here it consists of the tax and non-tax current revenues of central and local governments, operating surpluses of state enterprises, foreign grant receipts and the net extrabudgetary receipts of the central government treasury. Hence the deficit figures cited in this report differs from the deficit figures given in the IBRD Economic Reports.

TABLE 5: Financing of Public Expenditure
(as percent of expenditure)

	FY 1969/70	FY 1970/71	FY 1971/72	FY1972/73	FY1973/74
Current Revenue of Central and Local Governments					
Central Gov't. Tax Revenue	63.0	56.5	57.3	61.2	73.2
Central Gov't. Non-Tax Revenue	5.9	5.4	6.4	6.7	5.3
Local Gov't. Revenue	4.3	4.4	4.0	2.9	4.4
State Enterprise Operating Surplus	4.4	3.8	3.9	4.7	1.9
Total Current Revenue	77.6	70.0	71.5	75.6	84.8
Other	6.8	8.9	4.2	4.4	3.6
Total Revenue	84.4	79.0	75.7	79.9	88.4
Cash in Transit 1/	-0.2	....	0.8	0.4	-0.4
Net Borrowing					
Foreign Sources	....	0.6	1.5	3.3	4.4
Domestic Sources 2/	2.5	9.5	20.6	13.9	6.0
Monetary Authority 3/	12.7	7.7	1.3	3.1	0.1
Total Net Borrowing	15.2	17.8	23.3	20.3	10.5
Other Sources	0.6	3.3	0.2	-0.6	1.5
Total Deficit Financing	15.8	21.1	23.5	19.7	12.1
Total Financing	100.0	100.0	100.0	100.0	100.0

Source: Tables B-1 and B-2 of Table B.

1/ A part of central government transfers to local governments. Floating between the two due to the time lag in the payments and the receipts.

2/ Excluding monetary authority.

3/ Bank of Thailand and Exchange Equalization Fund.

17. In addition to the floor target, we attempted to estimate the magnitude of financial resources the public sector would need and could meaningfully utilize to improve the supply of public services qualitatively and quantitatively. 1/ This magnitude will be referred to as the "high target" for public expenditure. The estimates take as broad policy guideline the qualitative objectives of the Third Five-Year Plan (1972-1976): increase in the share of developmental expenditure for agriculture, education and other social services; and improved distribution of development gains for poorer regions and rural areas.

18. The results of the exercises are shown in Table 6. The ratio of the resource requirement to GDP is calculated from the figures expressed in assumed current prices. 2/ As the future need for borrowing is not known at this stage, the resource requirement for interest payments included here reflects only the interests payable on the debt outstanding at the end of FY1973/74. Additional requirement for interest payments on the debt to be incurred in the projection period will be considered later in conjunction with resource shortfall. The exercises assume that the real growth rates of GDP and agriculture value added will be 7 percent and 5.1 percent a year during the projection period, respectively, 3/ and that the rate of price inflation - in terms of GDP deflator - will taper off after FY1973/74. 4/ The rate of population growth is assumed at 3.1 percent as the basis for assessing the pace at which the supply of certain types of social services should expand. To estimate the cost of public services in current prices, it is assumed that the prices of goods and services the public sector would purchase will move at the same pace as the GDP deflator. 5/ The possible changes in the employment

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1/ See Section IV of Annex C for details.

2/ For the purpose of this exercise, we projected the future values of national account variables on the basis of the national account figures given to the mission in January 1974. The figures for 1973 were revised after the completion of our exercises.

3/ These are the target rates for the Third Five-Year Plan.

4/ We used the future rate of inflation estimated by the East Asia and Pacific Department of IBRD, i.e., 15 percent in FY1973/74; 8 percent in FY1974/75; 4% in FY1975/76 and FY1976/77; and 3% in FY1977/78 to FY1979/80.

5/ At the level of aggregation adopted in this analysis, refinements concerning the price elasticity of public expenditure would not be meaningful. An assumption of unit price elasticity was adopted for expenditure requirement for all purposes except for interest payments. Under this assumption, the ratio of public expenditure requirement to GDP would not be affected significantly by the rate of price inflation. To the extent the salary adjustments for central and local government employees lag behind price increase, a higher rate of inflation would lower the ratio of expenditure requirement to GDP. The magnitude of interest payments on debt outstanding at the end of FY1973/74 would be independent of inflation rate, and hence its ratio to GDP would tend to be lower under higher rate of inflation.

policy and the rates of remuneration in the central government are being considered by the Civil Service Commission. However, in this exercise the employment patterns of central and local governments are assumed to remain the same as in the past and the nominal rates of remuneration to be adjusted each year so that the average real rate of remuneration would remain at the FY1971/72 level.

19. The rate of remuneration for central and local government employees did not change significantly between 1967 and 1972. However, recently the central government has taken three legislative actions to raise the remuneration for its employees to restore their income, which had been eroded by the rises in consumer prices. These measures increased the cost of given personal services to the central government by about 26.5 percent in a little over a year.

20. The introduction of family support scheme at the beginning of FY1972/73 increased the remuneration expenditure by about 6 percent relative to that under the FY1971/72 remuneration structure. The effect of a minor salary adjustments for low-salary employees in June 1973 was negligible. However, an across-the-board salary increase of February 1974 (effective January 1974) increased the remuneration expenditure by about 24.5 percent relative to that of the FY1971/72 structure. A part of this was offset by the abolition of the "income tax subsidy," and the net effect is estimated as an increase by about 20.5 percent.

21. These adjustments covered only the salaries of central government civil servants. The mission was not able to obtain any figures on the remuneration for local government employees, but it is known that their remuneration is considerably lower than that for central government employees. And yet, there have been no salary adjustments for them that would match the increases in central government civil service salaries. It is necessary that the remuneration for local government employees be adjusted at least to restore the parity under the FY1971/72 remuneration structure to keep local governments functioning. Our estimates assume that this adjustment of remuneration for local government employees will be made by the end of FY1973/74.

22. Under the present arrangement the employees of central and local governments are not guaranteed cost-of-living adjustment in remuneration. 1/ However, with the expected rate of inflation it is almost certain that the government sector will be forced to make further adjustments of remuneration for the employees in order to secure sufficient personnel needed to maintain its activities. 2/ For this reason, the resource requirement estimates assume that the average nominal rate of remuneration for central and local governments employees will increase at the same rate as GDP deflator during the projection period, so that the average real rate of remuneration would remain the same at the FY1971/72 level. Hence in our exercise the prices of all goods and services move in parallel, without changing the relative price between personnel services and other input for the activities of the public sector.

1/ See Section III of Annex C.

2/ With 15 percent price increase in FY1973/74, any real increase that might have accrued from the recent adjustments will be eroded and the average real rate of remuneration in FY1973/74 will be lower than in FY1971/72.

TABLE 6: LOW AND HIGH SCENARIOS FOR PUBLIC EXPENDITURE REQUIREMENT
(As Percent of GDP)

	Actual Expenditure /1			Projected Requirement /2		
	FY1970/71 to FY1971/72 Average	FY1972/73 (Estimate)	FY1973/74 (Estimate)	FY1974/75	FY1976/77	FY1970/80
Low Scenario (Total)	21.3	19.6	18.7	22.0	22.0	22.0
High Scenario						
Education	3.6	3.2	2.9	4.5	4.5	4.6
Current	2.6	2.4	2.0	3.6	3.6	3.7
Capital	1.1	0.8	0.9	0.9	0.9	0.9
Health Care	0.6	0.5	0.4	0.7	0.9	1.3
Current	0.5	0.4	0.4	0.5	0.6	0.8
Capital	0.1	0.1	0.1	0.2	0.3	0.5
Water Works	0.4	n.a.	n.a.	0.9	0.9	0.9
Current	0.1	n.a.	n.a.	0.1	0.1	0.1
Capital	0.3	0.4	0.4	0.8	0.8	0.8
Power - Capital	1.1	1.4	0.9	1.5	1.6	1.7
Communication and Transportation	3.0	2.7	2.4	3.4	3.6	3.7
Current	0.5	0.5	0.4	0.5	0.5	0.5
Capital	2.5	2.2	2.0	2.9	3.1	3.2
Agriculture Services	1.8	1.3	1.1	2.0	2.3	2.7
Current	0.7	0.6	0.6	0.8	0.8	0.9
Capital	1.2	0.7	0.6	1.2	1.4	1.8
General Administration -- Current	2.0	2.1	2.5	2.0	2.0	2.0
Security -- Current	4.4	3.9	4.1	3.6	3.2	2.6
Interest Payments	1.4	1.5	1.5	1.4/3	1.0/3	0.6/3
Pensions	0.4	0.4	0.4	0.45	0.45	0.45
Other	2.4/4	2.3/4	2.1/4	3.0	3.3	3.9
Current	1.3	1.3/5	1.3/5	1.5	1.6	1.7
Capital	1.2	1.1	0.9	1.5	1.7	2.2
Total	21.3/4	19.6/4	18.7/4	23.5	23.6	24.5
Current	13.9	13.0	13.0	14.5	13.8	13.4
Capital	7.6	6.7	5.7	9.0	9.8	11.1

Source: Table C-4

/1 Ratios calculated with the revised GDP estimates of August 1974.

/2 Ratios calculated with the GDP figures projected on the basis of GDP estimates for 1972 and 1973 which were given to the mission in January 1974. Expenditure requirement estimates were derived on the basis of pre-revision GDP estimates.

/3 Interest payable on the debt incurred before the end of FY1973/74 only.

/4 The total differs from the sum of "current" and "capital" figures due to adjustments.

/5 Including current expenditure for water supply.

23. This is a minimum plausible assumption and not a recommendation. Restricting of the rates of renumeration for central and local governments employees combined with changes in employment policies of the government sector will, probably, be necessary. It seems that the low level of salaries in the higher echelon of the civil service leads to difficulties in attracting efficient personnel, promotes the proliferation of side benefits, and tends to exclude the members of the families who do not have independent income. On the other hand, the very low salaries for low grade officers are likely to be causing excessive employment of non-technical staff in the central government. This is an area where studies of competitiveness with the private sector -- though making adequate allowance for the high prestige that is still attached to public service -- are urgently needed.

24. The functional composition of the projected resource requirement differs somewhat from that of the expenditure in the recent past. The goal of improved social services in rural areas implies increased expenditure for primary education, health services and rural public works. Expenditures for irrigation and other agriculture services will also have to increase to maintain the momentum of growth in agriculture.

25. The estimates of required expenditures for public school education assume that the enrollment at each level of schools will increase in the next six years at the rate envisaged in the Third Five-Year Plan. However, the number of students in primary and secondary schools will be higher than the Plan targets since in 1972 the actual enrollments have already surpassed the targets for the year. A large portion of the capital expenditure will be devoted for the construction of school buildings in villages where there are no primary schools. Current expenditure per student at primary, secondary and vocational schools has to increase to improve the quality of teachers and to provide students and teachers with adequate teaching materials.

26. Public expenditure on health has been small, amounting to only 0.6 percent of GDP in each year from FY1956/66 to FY1971/72. In FY1972/73 and FY1973/74 health service expenditure dropped in real terms and the ratio to GDP fell to 0.4 percent in FY1973/74. In most developing countries, the public expenditure for health services amount to 1 percent of GDP or more. Health service in Thailand has been concentrated in the metropolitan area despite the efforts of the government to improve rural services. 1/ The health statistics of 1971 - the latest available - show that among health service personnel employed by the public sector 64 percent of medical doctors, 70 percent of dentists and 55 percent of nurses and practical nurses were serving the metropolitan area, where only about 11 percent of the population resided. The Ministry of Public Health estimates that only about one-third of the population benefits from public health services. Large portion of the financial and human resources of the Ministry of Public Health has been devoted to curative services; environmental sanitation and disease control are largely left to local governments, which do not have

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1/ "Metropolitan area" refers to the present Bangkok Metropolis and its suburbs.

sufficient resources to execute these functions properly. The expenditure requirement for health services is estimated on the proposition that the public expenditure per capita in non-Central Regions be raised in real terms to the level currently prevailing in the Central Region by FY1979/80, while maintaining the same per capita level in real terms in the Central Region for the same period.

27. Public expenditure for water works has been about 0.2 to 0.4 percent of GDP excluding the operating expenses of the Metropolitan Water Works Authority (MWWA) -- a state enterprise that serves the Bangkok Metropolis and two adjacent provinces. Regional distribution of expenditure on water works is biased in favor of the metropolitan area. In the period from FY1967/68 to FY1971/72, the capital expenditure of MWWA (partly financed by grants and loans from the central government) accounted for about one-quarter of public expenditure for water works. Since MWWA serves less than 15 percent of the population, the per capita expenditure in the MWWA area is about twice that in the rest of the country. Provincial water works are not yet developed enough to supply piped water to a large majority of the population. Only about 40 percent of the population in the cities with water supplies are connected to the systems. About 10 percent of the population in villages and small towns have benefitted from an improved water supply. Additional capital expenditure is needed for the MWWA territory and in the rest of the country. The capital expenditure requirement is estimated on the basis of the MWWA investment project list and an assumption that provincial water work development will need about 1.5 time of financial resources required for the MWWA projects. From the equity view point the provincial water works should receive much larger resources. However, the existing man power for rural water works could not absorb increased financial resources immediately.

28. The responsibility for electricity generation and distribution rests largely with state enterprises, and the central government directly provides only supporting services such as fuel survey. Public expenditure for power supply and related services increased from about 0.6 percent of GDP in FY1965/66 to 1.4 percent of GDP in FY1972/73. However, in FY1973/74, the ratio to GDP is estimated to decline to 0.9 percent. Gross fixed investment of state enterprises accounted for more than 90 percent of this expenditure. Electricity consumption is expected to increase rapidly in urban areas, and rural electrification will bring about a small additional demand for electricity. Continuous expansion of electricity generating capacity is necessary for industrial development. The estimate assumes, on the basis of the investment projects of state enterprises, that the resource requirement for this purpose will increase from 1.5 percent of GDP in FY1974/75 by about 10 percent each year in real terms.

29. Public expenditure for communication and transportation have equalled about 3 percent of GDP since FY1966/67 absorbing 13 to 17 percent of the financial resources of the public sector. In the period from FY1966/67 to FY1971/72 about 11 percent of public expenditure was allocated for the construction and maintenance of major roads, and a basic highway structure

has been created. Emphasis of future transportation development should be placed on improving rural roads and expanding urban and suburban roads. Basic infrastructure for communication services needs expansion in urban areas and improvement in rural areas. Telecommunication facilities in rural areas are very limited. The capital expenditure requirement for transportation and communication services are estimated on the basis of the ratio of actual expenditure to GDP in the past but with some adjustments which seem needed for state enterprise project lists.

30. Public services to the agriculture sector were mainly geared to increasing land productivity, entailing major emphasis on irrigation. Up to FY1970/71 public expenditure for agriculture services was about 2 percent of GDP, and about two-thirds of the amount were used for construction and maintenance of irrigation facilities. However, because of the failure to focus on irrigation works between dams and farms, the large expenditure for dam construction has not yet brought about the expected effects on production. Considerable expenditure will be required in the near future to improve the existing irrigation facilities to ensure better utilization. Construction of new facilities is also necessary to expand irrigated area. Since FY1971/72 public expenditure for irrigation has been declining in real terms, but this trend should be reversed immediately. Also, the government will need to expand and intensify extension services to introduce to farmers the farming methods that would maximize the effect of irrigation. In addition, supporting services to rain-fed areas need be increased. The estimates of the future expenditure requirement are based on the Third Plan projects with such adjustments as the mission has felt necessary.

31. While public resources allocated for social and economic services have been generally inadequate to supply a desirable level of services, the expenditure for external and internal security seems to have been high. 1/ In the period from FY1965/66 to FY 1970/71, the current expenditure for defense and police increased from 3 percent of GDP to 4.5 percent of GDP, and in the early 1970s this accounted for one-fifth of the total public expenditure. Had defense and police expenditures remained at 3 percent of GDP, this would have provided budgetary savings in the order of about 5.5 billion baht in 1973. Current expenditure for general administration was about half this size. It increased toward the end of the 1960's, when it reached 2.7 percent of GDP, but in FY1969/70 to FY1972/73 its ratio to GDP remained at about 2 percent. The resource requirement for security and general administration will depend on political and security situation of the country. In the absence of detailed forecasts on these factors, the estimates assume that general administration expense will remain at 2 percent of GDP and that security expenditure can be kept at ฿7 billion in real terms (in constant FY1971/72 prices) in the hope that security situation does not deteriorate.

32. The "high target" expenditure scenario described above would suggest that the financial resource requirement of the public sector amounts to about 23.6 percent of GDP in FY1976/77 and 24.5 percent of GDP in FY1979/80. These ratios are considerably higher than the peak ratios of actual public expenditure to GDP achieved in FY1970/71 and FY1971/72, which was about 21.3 percent. The major force behind this development is the large

capital expenditure requirement, which is enviasaged to amount to 9.8 percent of GDP by FY1976/77 and to 11.1 percent of GDP by FY1979/80. The ratio of actual capital expenditure to GDP was less than 8 percent since mid-1960's, and in FY1972/73 and FY1973/74 it was below 7 percent. Since capital expenditure for social services in rural areas has been small in the past, large investments for this purpose is inevitable in the future.

33. The current expenditure requirement amounts to 14.5 percent of GDP in FY1974/75. The ratio to GDP declines during the projection period to about 13.4 percent in FY1979/80, but this is largely due to the exclusion of interest payments on debts to be incurred during the projection period. As noted above, the interest payment figures in Table 6 are calculated on the basis of the debts outstanding at the end of FY1973/74.

34. The broad picture that emerges from the "high scenario" above is that public expenditure requirement in Thailand during the next six years will be about 24 percent of GDP. To the extent economies can be effected in security expenditures and through improved efficiency in other sectors, the expenditure level may be below this ratio. On the other hand, additional upward adjustment of real wages and salaries for central and local government employees may become necessary, and this may raise the expenditure requirement relative to GDP. In the absence of solid basis for estimating the effects of these three unknowns, namely, the future development in security situation, possible improvements in the efficiency of public services, and the pay policy for central and local government employees, there is no point in speculating about the probable outcomes except for pointing out that the deviations are unlikely to exceed 1 percent of GDP on each side. In what follows, therefore, the high expenditure target will be taken as 24 percent of GDP, as against the floor target set at 22 percent of GDP.

35. In attempting to draw a perspective for the near future in which we can discuss the fiscal requirements, we have not said anything about the absorptive capacity of the public sector to utilize additional resources. This is not because we find this aspect of the problem unimportant. On the contrary, we would emphasize the need for major improvements in this area. To analyze this issue in any detail was, however, beyond the terms of reference and the expertise of our Mission. On the other hand, we want to emphasize that excessive scepticism about the absorptive capacity of the public administration should not constrain the fiscal effort since fiscal resources are usually a prerequisite for administrative improvements. Furthermore, since the fiscal effort issue in Thailand is related to the provision of infrastructure and social services and not to the public vs. private ownership controversy, the low level of efficiency in the public sector should not mitigate against the expansion of public services, since there is no other alternative.

Public Revenue

36. The ratio of public sector's revenue to GDP fluctuated between 16 percent and 18 percent in the period from the mid-1960's to FY1971/72. The ratio rose from about 16 percent in FY1965/66 to 18 percent in FY1968/69,

then declined to 16 percent in FY1971/72. It declined further to 15.7 percent in FY1972/73, but the estimates for FY1973/74 indicate an increase to 16.5 percent.

37. About 90 percent of the total revenue accrues to the central government, and remainder is divided about equally between local governments and state enterprises. 1/ Central government taxes have been the major revenue source, accounting for about three-quarters of the total public revenue. The weight of income taxes (personal and company income taxes) is still relatively small (10.7 percent of total public revenue in FY1972/73), but it has increased considerably from the mid-1960's. The weight of commodity taxes (business and excise taxes) has also increased, due to improvements in the system of taxation as well as administration, and in FY1972/73 these taxes accounted for about one-third of the total public revenue. The weight of import taxes tended to decline, mainly due to import substitution in petroleum products and other industrial goods, but they still accounted for over one-fifth of the total public revenue in FY1972/73. The most significant change in the revenue structure since the mid-1960's was a decline in the share of export taxes form more than 9 percent in FY1965/66 to less than 2 percent in FY1970/71 and FY1971/72, mainly caused by the policy to reduce rice export premium in the early 1970's.

38. The revenue from central government taxes increased faster than GDP in the latter half of the 1960's, and its ratio to GDP rose from less than 12 percent in FY1965/66 to over 13 percent in FY1968/69. However, in the early 1970's the receipts from this source tended to increase more slowly than GDP, resulting in a sluggish increase in the total public revenue. The non-tax current revenue of the central government increased at about the same pace as GDP, and its ratio to GDP remained stable at aroung 1.2 percent of GDP.

39. The stagnation in the ratio of central government tax revenue to GDP in the early 1970's was largely attributable to a slow increase in foreign-trade-related taxes, and particularly to the reductions in export taxes. In the mid-1960's revenue from rice export premium and the rice export duty combined amounted to over 1 percent of GDP, but in early 1970's the revenue from these taxes fell to about 0.2 percent of GDP when it was decided to reduce the rice export premium.

40. Local government revenue was about 0.9 percent of GDP without exhibiting any clear trend up to FY 1971/72, but the ratio to GDP fell to 0.6 percent in FY1972/73. Other revenues were between 2 percent to 3 percent of GDP. Extrabudgetary treasury receipts fluctuated between 0.3 percent of GDP to over 1 percent of GDP. The ratio of foreign grant receipts to GDP followed a minor upward trend in the latter half of the 1960's but began to decline after marking a peak at 1.2 percent in FY1968/69 and came down to 0.5 percent in FY1972/73. The state enterprises generated operating surpluses of about 1 percent of GDP each year up to FY1972/73.

1/ State enterprises' operating surpluses after remittances of required contributions to the central government.

41. The fact that the revenue from central government taxes tended to increase more slowly than GDP could be an indication of low revenue elasticity with respect to income, but it was also partially attributable to the changes in the structure of taxes. It is necessary to identify the revenue pattern not affected by discretionary changes in tax structure to evaluate the responsiveness of tax revenue to income growth and price movement. 1/ A set of time series regressions was conducted to estimate the tax revenue functions under the tax structure prevailing in FY1972/73. 2/

42. The results of this exercise indicate that the revenues from personal income tax, company income tax, tax on property transfers and stamp duty depend on the GDP of the year prior to the year of collection. In the case of income taxes this is obviously due to the mode of collection. The ratios of the revenues from these taxes to GDP at current prices tend to decline when the latter increases fast whether due to real growth or due to price inflation.

43. Revenues from certain other taxes have been found elastic with respect to real income but independent of price movements. Examples are excise tax on soft drink and taxes on petroleum products, which are levied at specific rates. The ratio of revenues from these taxes to GDP at current prices would tend to increase when real GDP growth is substantial, but would tend to decline when there is a substantial increase in the price level. On the other hand, revenues from business taxes and import duties on non-petroleum products seem to be fairly responsive to both real income growth and price increase.

44. Using the results of the regression analysis, we attempted to project the magnitude of the financial resources that the present revenue system will generate in the next six years. 3/ The results are summarized in Table 7. The projection adopted the same assumptions concerning the rates of economic growth and price inflation as used for the projection of "high expenditure target." 4/ The figures show that total revenue will increase from 16 percent of GDP to 18 percent of GDP over the six years. The ratio of the revenue from central government taxes is projected to be about 13 percent of GDP in FY1973/74 and to increase to about 15 by FY1979/80. Non-tax current revenue of the central government is assumed to remain at 1.2 percent of GDP. Local government current revenue is projected to increase slightly to 1 percent of GDP by FY1979/80. The revenues from other sources are envisaged to decline over the six year period to less than 1 percent of GDP. Foreign grants will remain about ฿ 600 million (in current prices) during the six year period, and the operating surpluses of state enterprises will diminish in the absence of tariff rate adjustment.

1/ See Section VI of Annex C.

2/ Results are presented in Section V of Annex C.

3/ I.e., the revenue that will accrue to the public sector if the present tax structure and state enterprise tariff rates remain effective during the projection period. See Annex C for the details of the exercise.

4/ As in the case of expenditure requirement projection, we projected the future values of national account variables on the basis of the national account figures given to the mission in January 1974. National account figures were revised after the completion of our exercises.

Table 7: Revenue Projection
(As Percent of GDP)

	Actual Revenue /1			Projected Revenue /2		
	FY1970/71 to FY1971/72 Average	FY1972/73	FY1973/74	FY1974/75	FY1976/77	FY1979/80
Central Govt. Tax Revenue	12.1	12.0	13.7	13.2	13.9	14.9
Central Govt. Non-tax Rv.	1.3	1.3	1.0	1.2	1.2	1.2
Local Govt. Revenue	0.9	0.6	0.8	0.9	0.9	1.0
Sub-total	14.3	13.9	15.5	15.3	16.0	17.1
Other Revenue /3	2.2	1.8	1.0	1.0	0.9	0.8
Total Revenue	16.5	15.7	16.5	16.2	16.9	17.9

/1 Calculated with the revised GDP estimate of August 1974.

/2 Calculated with GDP figures projected on the basis of national account figures given to the Mission in January 1974. The projection exercises also used the future values of national account variables projected on the basis of the national account figures available in January 1974.

/3 Operating surpluses of state enterprises (net of contributions to central government budget), foreign grant receipts, and net extrabudgetary receipts of central government treasury.

Source: Table C-5a and C-6 of Annex C.

Public Sector deficit and financing

45. The cash deficit of the public sector increased rapidly since the mid-1960's. While its ratio to GDP was less than 1 percent in the mid-1960's, the ratio rose to 3.2 percent in FY1969/70. The central government acted to restrain public expenditures since FY1971/72; but despite its attempts, the deficit of public sector in that year increased to 5 percent of GDP. However, in the following years, the deficit declined in absolute amount and the ratio to GDP fell to 3.9 percent in FY1972/73 and further to 2.3 percent in FY1973/74.

46. A very large part of the cash deficit of the public sector has been financed by domestic borrowing - about 90 percent of the total - during the past seven years. Borrowing from foreign sources was relatively insignificant in the total picture and made up the residual together with coin issuing, drawings on counterpart funds and cash balances. Almost all public debt was placed with the Bank of Thailand, commercial banks, and the Government Savings Bank. Very little public debt has been held by the non-bank public.

47. Compared to the financial resources created by the banking system, the share utilized by the public sector has been large. The ratio of public borrowing - net of repayments - to the increase in deposits and currency during the past ten years was never below 20 percent each year, and averaged at about 70 percent in more recent years. Almost all the resources of the Government Savings Bank has been used to finance public debt. In the case of public debt held by commercial banks, the volume has also increased but on a more fluctuating trend, mainly reflecting the liquidity situation of these banks.

TABLE 8: GOVERNMENT BORROWING FROM THE FINANCIAL SYSTEM
(millions of Baht)

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973
Government Borrowing/1 from:										
Bank of Thailand	205.5	53.1	91.0	-601.8	361.1	3,983.9	2,945.1	1,641.6	2,399.3	1,368.4/2
Government Savings Bank	428.1	654.1	1,052.8	832.2	569.7	600.9	448.7	862.8	1,666.7	1,643.9/2
Commercial Banks	486.6	368.2	1,579.3	739.2	695.7	-108.2	450.8	2,374.3	5,520.7	1,569.4
Total Borrowing from the Financial System/1	1,120.2	1,075.4	2,723.1	969.6	1,626.5	4,476.6	3,844.6	4,878.7	9,586.7	4,581.7
Total Government Borrowing/1 As Percentage of:										
GDP	1.50	1.28	2.69	0.90	1.39	3.48	2.83	3.36	5.99	2.30/3
Budget 4/	10.40	8.64	19.51	5.60	8.35	20.63	15.30	17.92	33.48	14.30
Increase in Currency and Deposits	40.02	45.67	54.95	23.97	30.67	88.82	158.83	80.79	103.00	33.81
Increase in Currency and Deposits as a Percentage of GDP	3.75	2.79	4.89	3.74	4.54	3.92	1.78	4.16	5.81	6.81 /3

/1 Annual increases.

/2 September 1973 figure.

/3 Revised GDP estimate of August 1974.

/4 Budgetary expenditure of the central government.

Source: Bank of Thailand, Monthly Bulletin, January 1974.

48. The size of future resource shortfall of the public sector may be estimated on the basis of the two sets of expenditure targets and the revenue projection obtained above.

	FY1976/77	
	Minimum (floor) Target (% of GDP)	High Target (% of GDP)
Public Expenditure	22.0	23.6
Public Revenue	16.9	16.9
Resource Shortfall	5.1	6.7

49. Unless an intensified effort is made to restructure the revenue system, the resource shortfall in FY1976/77 would amount to more than 5 percent of GDP even for the minimum expenditure target; for the high expenditure target the resource shortfall would amount to close to 7 percent of GDP. In the recent years the public sector financed deficits equal to more than 4 percent of GDP mainly by domestic borrowing. However, this was possible because of the slack demand for bank credits in the private sector. The scope of domestic borrowing in the future will depend on three factors: increase in the resources of the banking system; the share of the public sector in this increment; and the possibilities of selling public debt to the non-bank public. The last alternative may be due for some increase provided that attractive terms are offered, but it should not be expected to play a major role in public finances in the near future.

50. The financial resources of the banking system would grow faster than GDP. Although the rate of increase in currency supply and demand deposits would be only slightly higher than the nominal GDP growth rate, past trends indicate that time deposits and saving deposits could increase at a considerably faster pace. According to regression results, the annual increase in financial resources of the banking sector, which had reached a level equal to 7 percent of GDP by 1973, will reach at least 10 percent of GDP by FY1976/77.

51. However, the financial needs of the private sector are also likely to grow rapidly. Therefore, the share of the public sector will not remain as high as in the past. The large public borrowing in FY1971/72 was possible because the private sector's demand for funds was slack. The large borrowing in FY1972/73 has produced strains evidenced by large monetary expansion and significant inflows of foreign funds into the banking system. In view of this, it appears that public borrowing from the banking system should be lower than what has been in the recent past. For these considerations, the mission views that 3 to 4 percent of GDP, on the average, would be the maximum level of domestic public borrowing that could be tolerable. If public borrowing rises beyond this level, it is likely to put pressure on the monetary and credit system.

52. It is clear that the public sector could not finance the envisaged future resource shortfall entirely by domestic borrowing - even for attaining the "floor target" public expenditure. It is expected that the net foreign borrowing of the public sector can increase to more than 1 percent of GDP by FY1976/77 and to almost 1.5 percent of GDP by FY1979/80. However, even when the expected increase in foreign borrowing materializes, the net domestic borrowing required for attaining the "floor target" with additional resource requirement (for interest payments on the debt to be incurred during the projection period) would amount to 5 percent of GDP in FY1976/77. Therefore, it is necessary that the public sector make an intensified effort to obtain additional revenues.

53. The analyses of the tax system and state enterprise financial operations suggest that additional revenues equal to 1.5 percent and 0.5 percent of GDP respectively can be generated by restructuring the tax system and state enterprise tariff rates. 1/ These potentials should be fully exploited. With an additional revenue of this size, the resource shortfall to be financed by net domestic borrowing would be reduced to less than 2 percent of GDP for the "floor target" and, even with the additional resource requirement for interests payable on the new debts, the required net domestic borrowing would be less than 3 percent of GDP. For the "high target" the remaining resource shortfall to be financed by net domestic borrowing would amount to about 4 percent of GDP despite the envisaged additional revenues and increase in foreign borrowing. With the additional interests payable on the new debts, the net domestic borrowing required to attain the "high target" expenditure would amount to about 5 percent of GDP.

54. In the light of the considerations outlined above, the quantitative overview of public finances in Thailand for the next six years may be summarized as follows. The level of public expenditure should rise above the low level it has fallen to in FY1972/73 and FY1973/74 due to financial constraints. The level a little higher than what was attained in FY1970/71 and FY1971/72 should be regarded as the minimum level for this period. Public expenditure equal to 22 percent of GDP can be financed without difficulty provided that the existing potentials for raising public revenue is exploited. From the view point of public service supply, it is desirable that the level of public expenditure be raised to 24 percent of GDP. However, this scale of public expenditure in the near future would pose considerable financing problem. Too narrowly focussed concern with revenue aspect can frustrate efforts to improve the efficiency and the equity of the tax system. Excessive resort to domestic or foreign borrowing would have negative effects on the financing of the private sector, balance of payments, or demand management. It is therefore suggested that the target for public expenditure in FY1974/75 to FY1976/77 be set at a level equal to 23 percent of GDP. This would entail a higher level of public borrowing than the "minimum expenditure" scenario, but this scale of borrowing can be tolerated. Once the structural changes for this level of public sector activities are achieved, higher expenditure targets can be aimed at by making additional adjustments in the taxation system.

1/ See Section III of the main report and Annex D.

55. This overview is intended to serve not as a rigorous prediction, but to provide a framework in which important fiscal policy issues can be placed in perspective. The actual developments in the public finances will follow a route which may deviate from this simple outline, particularly in year-to-year changes in response to economic and political factors.

III. TAXATION POLICY

56. The previous chapter concluded that if a desirable program of public expenditure is to be financed, an increase in tax revenues will be necessary. The magnitude of the increase involved would be from a ratio of tax revenues to GDP of 14% that the present tax system would generate to a ratio of about 15.5%. This is not a big jump in relative terms. Over a three-year period and at a growth rate of 7 percent per annum, this is equivalent to a marginal tax ratio of 20.6%. A target tax ratio of 15.5% is not high by international comparisons either. The estimated average tax ratio for a group of 47 developing countries for the period 1969-72 is 15.1%. In comparison with some other Asian countries, while the target ratio will be above past levels attained in Pakistan and the Philippines, it will be about the same level as currently achieved in Korea and substantially below the level prevailing in Malaysia.

57. The objective of increasing the revenue yield of taxation in Thailand ought to be conceived in conjunction with changes in the tax structure aimed at improving the elasticity, efficiency and the equity of the system. As indicated, suggested revenue targets are modest enough to permit such a review. Although the structure of the tax system in Thailand is basically sound, there are areas where improvements are called for. Most of these topics have been analyzed in two previous unpublished reports, the first by Professor Neumark in 1959 1/ and the second by Messrs. Lent and Hirao in 1970. 2/ The latter report in particular detailed the basic structural defects in the Thai taxation system and suggested improvements, some of which have since been adopted. Our analysis below draws heavily on the analysis of this second report.

58. Of the 1973 central government revenue receipts, we find that taxes contributed 89.6% of the total and non-tax revenues contributed 10.4%. Of a total tax revenues of ฿22.7 billion, indirect taxes (including import duties, export taxes, business taxes, and excise taxes) contributed 78.1%, the income tax contributed 13.9% taxes on property and property transfers contributed 3.9% while the remainder of 4.0% is contributed by royalties and other taxes.

59. The average income buoyancies estimated over the 1964-1973 period (Table 11) indicate that Thailand obtained a 1.06% increase in total tax revenues for every 1% increase in GNP. Specifically, a 1% rise in GNP was associated on the average with a 1.79% increase in revenues from excises, 1.44% increase in income tax revenues, 1.24% increase in business revenues, and 0.92% increase in revenues from import duties. However, the low average

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1/ Fritz Neumark, Proposals to Create Additional Revenue for the Government of Thailand, mimeo., 1958.

2/ Gerge E. Lent and Teruo Hirao, A Survey of Thailand's Tax Structure, Fiscal Affairs Department, International Monetary Fund, 1970.

buoyancy for the aggregate is much attributed to the negative buoyancy of -2.1 for rice premium. It should be also recognized that the buoyancy of tax revenues over the period has been due in part to the discretionary changes both in tax rates and in the tax base. Despite the variations in income buoyancies of specific taxes, the revenue system as a whole in Thailand is not very elastic with respect to changes in GNP. This may be due, partly, to the ineffective taxation of business and professional incomes and the major revenue loss in rice export premium.

60. Ineffective taxation of business and capital incomes is a major weakness of the Thai tax system. The share of what may be considered taxes on capital and business incomes in total tax revenues is only about 12%. Taxation of personal income from business profits is very inefficient, the corporate taxation structure has many loopholes, interest income is exempt and taxation of income from property (movable or immovable) is negligible. Thus, whereas the trend in many countries has been for more progressive or discriminatory taxation of incomes from capital on the grounds of "ability to pay" principle, in Thailand income tax system is biased against the wage and salary earners.

61. The very low share of income taxes in total tax revenue and heavy dependence on indirect taxation are other shortcomings of the Thai taxation system. In Table 12 a comparison is drawn between the tax structure of various Asian countries. Thailand's heavy reliance on the taxation of international trade is shared by Malaysia. For the Philippines and Pakistan, the weight of such taxes in the total is much less, and a minor factor in the revenue structure of Korea. Pakistan is similar to Thailand in that only a small share of total tax revenues are provided by income taxation. The income tax share is substantially higher, however, in Malaysia and the Philippines, and very much higher in Korea. The share of taxes on property in the total is much the lowest in Malaysia, and relatively low in Pakistan, Thailand and the Philippines. This share is the highest in Korea. In aggregate, the share of indirect tax is the highest in Thailand.

62. In the light of these general considerations a review of the Thai taxation system is presented below, which is predicated on the following objectives: (a) to make the system more sensitive to price and income changes and to achieve an increase in revenues; (b) to rely more on broadening the tax base rather than on increasing tax rates; (c) to aim at a higher degree of equity in the comparative treatment of incomes from employment, business, and property; (d) to develop an integrated commodity tax system; (e) to remove the fiscal impediments to efficient allocation of resources; and (f) to take a pragmatic view of what structural changes can be made given the economic and administrative setting in which the present tax system operates.

TABLE 9: SUMMARY OF THAILAND'S REVENUE STRUCTURE

(in millions of Thai baht)

	1968	1969	1970	1971	1972	1973 1/
Central Government Revenue 1/	16,285	18,150	18,721	19,098	21,339	25,347
Tax Revenue	14,863	16,625	16,968	17,274	19,058	22,720
Taxes on Income	1,726	1,973	2,169	2,363	2,550	3,168
Personal Income Tax	973	1,122	1,272	1,407	1,556	1,700
Corporate Income Tax	753	851	897	956	994	1,468
Taxes on Domestic Consumption	5,758	6,468	7,029	7,965	8,703	10,562
Business Taxes	3,068	3,345	3,577	3,927	4,307	5,096
Excise Taxes	2,064	2,436	2,686	3,192	3,413	4,341
Beverages	544	617	647	717	874	1,449
Petroleum Products	787	1,000	1,066	1,399	1,382	1,626
Tobacco	660	738	883	989	1,064	1,181
Snuff	10	11	13	13	18	
Others	63	70	77	74	75	85
Entertainment Tax	79	86	94	98	119	132
Profits of Fiscal Monopolies	547	601	672	748	864	993
Tobacco	400	450	500	579	650	771
Lottery and Playing Card	147	151	172	169	214	220
Taxes on International Trade	6,183	6,980	6,440	5,617	6,213	7,186
Import Duties	4,811	5,305	5,393	5,186	5,804	6,366
Petroleum Products	550	514	544	274	286	n.a.
Foodstuffs	344	369	380			
Textiles, Yarns and Threads	592	625	634			
Others	3,325	3,397	3,835			
Rice Premium	1,116	1,236	654	262	163	276
Export Duties	256	439	393	169	246	545
Rice	151	157	135	117	192	n.a.
Rubber, etc.	105	282	258	52	54	n.a.
Taxes on Properties and Property Transfers	453	513	564	556	744	890
Stamp Duties	110	123	124	122	140	151
Tax on Transfers of Immovable Properties	151	175	201	172	188	271
Automobile Registration Fee	192	215	239	262	416	468
Royalties	373	354	398	411	433	445
Other Taxes	370	337	368	362	415	468
Nontax Revenue 1/	1,422	1,525	1,753	1,824	2,281	2,627

1/ Including the unspent balance of the previous fiscal year's budget.

Source: Bank of Thailand

TABLE 10: COMPOSITION OF THAILAND REVENUE STRUCTURE

(composition percentage of total)

	1968	1969	1970	1971	1972	1973 1/
Central Government Revenue	100.00	100.00	100.00	100.00	100.00	100.00
Tax Revenue	91.27	91.60	90.64	90.45	89.31	89.63
Taxes on Income	10.60	10.87	11.59	12.37	11.95	12.50
Personal Income Tax	5.97	6.18	6.79	7.37	7.29	6.71
Corporate Income Tax	4.62	4.69	4.79	5.01	4.66	5.79
Taxes on Domestic Consumption	35.36	35.64	37.55	41.71	40.78	41.67
Business Taxes	18.84	18.43	19.11	20.56	20.18	20.10
Excise Taxes	12.67	13.42	14.35	16.71	15.99	17.13
Beverages	3.34	3.40	3.46	3.75	4.10	5.71
Petroleum Products	4.83	5.51	5.69	7.33	6.48	6.41
Tobacco	4.05	4.07	4.72	5.18	4.99	4.66
Snuff	0.06	0.06	0.07	0.07	0.08	
Others	0.39	0.39	0.41	0.39	0.35	0.34
Entertainment Tax	0.49	0.47	0.50	0.51	0.56	0.52
Profits of Fiscal Monopolies	3.36	3.31	3.59	3.92	4.05	3.92
Tobacco	2.46	2.48	2.67	3.03	3.05	3.04
Lottery and Playing Card	0.90	0.83	0.92	0.88	1.00	0.87
Taxes on International Trade	37.97	38.46	34.40	29.41	29.12	28.35
Import Duties	29.54	29.23	28.81	27.15	27.20	25.12
Petroleum Products	3.38	2.83	2.91	1.43	1.34	n.a.
Foodstuffs	2.11	2.03	2.03			
Textiles, Yarns and Threads	3.64	3.44	3.39			
Others	20.42	18.72	20.49			
Rice Premium	6.85	6.81	3.49	1.37	0.76	1.09
Export Duties	1.57	2.42	2.10	0.88	1.15	2.15
Rice	0.93	0.87	0.72	0.61	0.90	n.a.
Rubber, etc.	0.64	1.55	1.38	0.27	0.25	n.a.
Taxes on Properties and Property Transfers	2.78	2.83	3.01	2.91	3.49	3.51
Stamp Duties	0.68	0.68	0.66	0.64	0.66	0.60
Tax on Transfers of Immovable Properties	0.93	0.96	1.07	0.90	0.88	1.07
Automobile Registration Fee	1.18	1.18	1.28	1.37	1.95	1.85
Royalties	2.29	1.95	2.13	2.15	2.03	1.76
Other Taxes	2.27	1.86	1.97	1.90	1.94	1.85
Nontax Revenue	8.73	8.40	9.36	9.55	10.69	10.37

1/ Including the unspent balance of previous fiscal year's budget.

Source: Bank of Thailand

TABLE 11: INCOME BUOYANCIES OF THAILAND'S REVENUES

	Average Buoyancy (1968-1973)	1968	1969	1970	1971	1972	1973
Central Government Revenue	1.06	1.52	1.19	0.47	0.34	1.42	0.89
Tax Revenue	1.06	1.50	1.23	0.31	0.31	1.26	0.92
Taxes on Income	1.44	1.36	1.47	1.43	1.47	0.98	1.15
Personal Income Tax	1.44	2.22	1.56	1.90	1.73	1.29	0.44
Corporate Income Tax	1.44	1.39	1.34	0.80	1.09	0.50	2.27
Taxes on Domestic Consumption	1.41	1.24	1.28	1.26	2.14	1.14	1.02
Business Taxes	1.24	0.90	0.95	1.01	1.60	1.19	0.87
Excise Taxes	1.79	1.89	1.82	1.48	2.95	0.86	1.30
Beverages	1.58	0.98	1.38	0.72	1.76	2.53	3.13
Petroleum Products	5.17	2.95	2.62	0.97	4.63	-0.16	0.84
Tobacco	1.16	1.51	1.23	2.71	1.94	0.94	0.44
Snuff		1.42	1.05	2.52	0.00	4.14	
Others	0.76	1.59	1.16	1.44	-0.68	0.17	0.64
Entertainment Tax	1.12	1.82	0.93	1.35	0.71	2.49	0.52
Profits of Fiscal Monopolies	1.04	0.68	1.03	1.69	1.83	1.85	0.71
Tobacco	0.93	1.42	1.29	1.59	2.51	1.48	0.89
Lottery and Playing Card	1.72	-1.14	0.30	1.97	-0.30	3.02	0.13
Taxes on International Trade	0.55	1.61	1.33	-1.22	-2.34	1.29	0.75
Import Duties	0.92	1.73	1.07	0.25	-0.67	1.44	0.46
Petroleum Products	-1.03/1	4.43	-0.74	0.86	-11.31	0.55	n.a.
Foodstuffs	0.82/2	0.56	0.77	0.44	--	--	--
Textiles, Yarns and Threads	0.66/2	0.92	0.60	0.22	--	--	--
Others	1.59/2	1.60	0.24	1.83	--	--	--
Rice Premium	-2.07	2.47	1.12	-9.32	-14.67	-5.98	3.30
Export Duties	-0.26	-3.29	5.79	-1.67	-13.66	4.76	5.79
Rice	n.a.	-3.43	0.43	-2.28	-2.45	6.23	n.a.
Rubber, etc.	n.a.	-3.07	10.06	-1.35	-22.78	0.48	n.a.
Taxes on Properties and Property Transfers	1.55	2.40	1.37	1.43	-0.24	3.71	0.94
Stamp Duties	1.08	2.70	1.23	0.12	-0.28	1.76	0.37
Tax on Transfers of Immovable Properties	1.38	3.09	1.62	2.09	-2.67	1.14	2.10
Automobile Registration Fee	1.85	1.80	1.24	1.60	1.57	5.83	0.60
Royalties	0.95	0.48	-0.57	1.77	0.55	0.67	0.13
Other Taxes	0.63	1.91	-1.03	1.33	-0.28	1.75	0.61
Nontax Revenue	1.13	1.81	0.77	2.11	0.68	2.86	0.72

/1 Average elasticity for 1964-1972.

/2 Average Elasticities for 1964-1970.

Source: Table 26.

TABLE 12: COMPARISON OF TAX STRUCTURE IN SELECTED COUNTRIES, 1969-1971

(a) As Percentage of Total Tax Revenue

	Income Taxes	Taxes on Property	Total Direct Taxes	Taxes on International Trade	Taxes on Production & Domestic Transactions	Total Indirect Taxes
Pakistan	15.2	3.8	19.0	25.7	55.2	80.9
Thailand	12.8	3.0	15.8	37.4	44.4	81.8
Philippines	28.6	4.4	33.0	24.4	41.3	65.6
Korea	33.7	3.8	37.5	12.3	49.8	62.0
Malaysia	28.6	0.5	29.0	36.3	19.5	55.8

(b) As Percentage of GNP

	Income Taxes	Taxes on Property	Total Direct Taxes	Taxes on International Trade	Taxes on Production & Domestic Transactions	Total Indirect Taxes
Pakistan	1.3	0.3	1.6	2.3	4.8	7.1
Thailand	1.9	0.4	2.3	4.6	5.5	10.1
Philippines	2.6	0.4	3.0	2.2	3.8	6.0
Korea	5.2	0.6	5.8	1.9	7.7	9.6
Malaysia	5.5	0.1	5.6	7.0	3.8	10.8

Source: R.G. Chelliah, H.J. Baas and M.R. Kelly, "Tax Ratios and Tax Effort in Developing Countries, 1969-1971", IMF Working Paper (DM/74/47), May 2, 1974.

Personal Income Tax

63. The personal income tax contributed 7.6% of total tax revenue in fiscal 1973. The average income buoyancy of the tax from 1964 to 1973 was about 1.4. In most countries this tax is the source of the greatest revenue elasticity in the tax system. Generally speaking this tax contains the most income elastic and productive elements in the modern tax system, but in Thailand it covers a limited fraction of income in general and of professional income in particular. There is ample room for improvements in the structure of the income tax and for additional revenue from this source. Eventually the income tax (personal and corporate) should become the backbone of Thai revenue system.

64. Incomes subject to the personal income tax may be broadly grouped into two categories, employment income and income from businesses and professions. Although agricultural income is legally subject to tax in Thailand, only a small fraction of it is taxed, because a major fraction of agricultural income is exempt from taxation under Section 42 (15) of the Revenue Code. Even if it were otherwise, it is probable that, in many cases, farmers' incomes would fall below the exemption limit.

65. Individuals must file income tax returns if their incomes are ฿5,000 or more. There is no reduced tax rate for joint returns, and a taxpayer's and spouse's income are taxed as if the income were all the taxpayer's. The taxpayer is allowed a concessional deduction of ฿5,000 for himself and his spouse and ฿2,000 for each of his children. In addition, 20% of earned income with a maximum amount of ฿20,000 each may be deducted by both husband and wife. Dividends of up to ฿5,000 each for husband and wife, and, if each income exceeds ฿5,000, 20% of the amount in excess of ฿5,000 are tax exempt. Under the present income tax law, a taxpayer is allowed a standard deduction. However, if he establishes that his actual expenses were greater than the standard deduction, he may claim a larger deduction. Standard deductions are set according to the source of income as shown in Table 13. The tax rate rises from 7% on net income not exceeding ฿10,000 to a maximum of 60% on taxable income in excess of ฿1 million. Taxpayers having earned income amounting to ฿30,000 or more are subject to a minimum tax of 0.5% of total earned income. Income taxes on wages and salaries are withheld at source and the employer is liable jointly with the taxpayer for such source withholding.

66. Employment Income. Taxation on income from employment, i.e., wages and salaries, generates about 80% of total personal income tax receipts, although no definite figures are available. The tax base is comprehensive and includes various fringe benefits provided by employers. But the current level of standard deductions for employment income plus liberal personal allowances are excessive. The present 20% deduction with a ฿30,000 ceiling should be reduced by one half. The adjustment would increase the income tax base and increase tax revenues. The coninuation of the minimum tax could be justified -- even then only temporarily -- if the revenue yield was significant. Unfortunately no data is available on this except for an estimate for the Bangkok/Thonburi area for 1964 when the yield was about ฿15 million.

TABLE 13: PRESENT AND PROPOSED STANDARD DEDUCTION RATES AS PERCENT 1/ OF GROSS RECEIPTS

	Type of Income	Present Rate 1/	Proposed Rate 2/
1.	Income from employment and service	20% but not exceeding ₱30,000	10% but not exceeding ₱15,000
2.	Income in the nature of royalty, interest, dividends, etc.	No deduction is allowed	No deduction is allowed
3.	Income from leasing property		
	a. house and other buildings	30%	20%
	b. land for agricultural use	20%	10%
	c. land for other purposes	15%	10%
	d. vehicles	30%	20%
	e. other property	10%	10%
4.	Income from liberal professionals	30%	20%
5.	Income of contractors	80%	60%
6.	Income from business, industry, any other occupation	75%-95%	60%-85%

1/ In the cases of (3), (4), (5) and (6) above, taxpayers may select to itemize their ordinary and necessary expenses incurred for the purpose of earning income in lieu of the standard deduction.

2/ In the cases of (5) and (6), the standard deductions are allowed for income below ₱250,000.

The revenue yield from this tax from all Kingdom should be ascertained. This tax should be abolished if the yield is insignificant. If the yield is sizable, then measures should be taken to abolish this tax as administration of the income tax improves. The revenue gain which can be obtained by lower standard deductions will probably compensate the loss that will result from the termination of the minimum tax.

67. The 1972 amendments to the Revenue Code have achieved a smooth progression in rates by raising marginal rates for taxable incomes in excess of ฿700,000. Relatively few persons are affected by these amendments however and the additional revenue expected from this change would be only ฿4 million in fiscal 1974. Future tax reform should not be in the direction of raising the nominal rate, but should concentrate on broadening the tax base. One might suggest that lowering the maximum rate, to say 50%, would reduce the incentive for evasion and the opposition to effective enforcement and result in a tax system that is in effect more equitable and productive. The Revenue Code amendments of 1972 also alleviated an undue burden placed on marriage by the joint income tax requirement. After the amendment the level of family allowances seems appropriate.

68. Personal Income from Businesses and Professions. The excessive deductions allowed for expenses in the taxation of business income constitute the major deficiencies in the income tax. At present, the standard deductions are differentiated by source of income and the deduction rates often do not adequately reflect the actual expense ratios of business and this feature violates the equity principles. Eventually the standard deduction system should be replaced by itemization of actual expenses by the taxpayer. Immediate and drastic change in this direction would be premature because present accounting practices in Thailand do not meet the requisite standard. Until the accounting system is improved a case can be made for retaining the current system of deductions. Even so, the allowable deductions in Categories 5 and 6 in Table 13 could become unreasonably large as the size of income increases. To cope with this, if a taxpayer's income exceeds a certain level, say, ฿250,000, he should be allowed to deduct only actual expenses incurred in earning his income without having the alternative privilege of using the standard deduction.

69. In Table 14, the allowed rates of standard deduction are compared with the actual expenses of different branches of business and industry. Although there were shortcomings in the data, the evidence clearly indicates a substantial difference between the present standard deduction allowed and the actual expense ratio for some industries. For example, manufacture of non-alcoholic beverages, pottery, ceramics, ice, glass products, and rice milling are allowed unduly large expense deductions. To a lesser degree deduction rates set by Section (8) of the Revenue Code for other businesses are also generous in relation to their net value added and gross receipts. On the basis of this a reduction in the allowable rate of standard deduction is recommended. A suggested schedule of revised rates is shown in Tables 13 and 15. The revised schedule would reduce the present 20% deduction

TABLE 15: PRESENT AND PROPOSED STANDARD DEDUCTION RATES AS PERCENT OF GROSS RECEIPTS

		Present Rates	Proposed Rates
1.	Business of organizing gambling, contest, or game in respect of which a percentage of the winnings or charges are collected.	75	60
2.	Business of taking, developing, printing or enlarging of photographs or cinematographic films, including sale of accessories.	75	60
3.	Business of dry docking, dockyard or ship-repair not including repair of machinery and mechanical contrivances	75	70
4.	Business of manufacturing shoes and real or imitation leather wares, including sale of accessories.	75	70
5.	Business of tailoring, sewing, knitting and embroidering cloth and other materials, including sale of accessories.	75	70
6.	Business of manufacturing, remodelling or repairing furniture, including sale of accessories.	75	70
7.	Business of operating a hotel or restaurant or preparing food and drink for sale.	75	70
8.	Business of curling, cutting, dressing hair or of a beauty parlor.	75	60
9.	Business of manufacturing soap, shampoo or cosmetics	75	70
10.	Business of producing literary subjects	80	65
11.	Receiving price of redemption of or acquiring absolute ownership in a property through a sale with the right of redemption	85	50
12.	Business of operating a clinic including healing, nursing and sale of medicine.	85	60
13.	Business of dealing in wares made of silver, gold, red-gold, diamond, gem or any other precious stone, including sale of accessories.	85	70
14.	Business of forestry, operating a rubber plantation or an orchard	85	70
15.	Business of transport or rendering services by means of vehicles	85	70
16.	Business of making blocks, seals, publishing or binding books and documents, including sale of accessories.	85	70
17.	Business of mining.	85	70
18.	Business of masonry.	85	70
19.	Business of manufacturing beverage within the meaning of Section 3 of the Beverage Tax Act, B.E. 2495.	85	60
20.	Business of manufacturing ceramics, procelain, cement or earthen wares.	85	60
21.	Business of producing or distributing electric currents	85	70
22.	Business of manufacturing ice	85	60
23.	Business of making flour and powder, not being cosmetics	85	70
24.	Business of making balloons, glass wares, plastic or rubber finished products	85	70
25.	Business of laundry or dyeing	85	70
26.	Business of smoking rubber, producing rubber sheets or other types of rubber not being rubber finished products	90	80
27.	Business of tanning	90	70
28.	Business of manufacturing sugar or molass.	90	80
29.	Business of fishery	90	80
30.	Business of saw-milling.	90	80
31.	Business of extracting or pressing oil.	90	80
32.	Business of selling any articles other than those specified under other headings, which are not manufactured by the seller.	90	80
33.	Business of letting out properties on hire-purchase not coming under the description given in Section 40 (5) of the Revenue Code as amended by the Revenue Code Amendment Act (No. 16) B.E. 2502	90	80
34.	Business of rice-milling	90	80
35.	Business of cultivating seasonal and cereal crops	90	80
36.	Business of drying or curing tobacco leaves	90	80
37.	Business of raising livestock of all kinds, including sale of by-products	90	80
38.	Business of slaughtering animals for sale, including sale of by-products	90	80
39.	Prices received by horse owners from the racing of their horses	95	85

TABLE 14: STANDARD DEDUCTION RATE AND EXPENSE RATIO BY INDUSTRY

(Amounts in million baht)

Type of Industries	No. of Establishments (1)	Net Value Added 1/ (2)	Gross Receipts (3)	Expense Ratio 100 [(2)/(3)]	Standard Deduction Rate (%)
Footwear apparel, except plastic ones	34	22.9	111.9	79.6	75
Manufacture of wearing apparel, except footwear.	33	19.7	71.0	72.3	75
Furniture and fixtures	30	25.6	119.1	78.5	75
Manufacture of soaps, cosmetics and toilet preparations.	18	26.5	108.3	75.5	75
Printing, publishing and allied industries	150	182.4	490.7	66.7	85
Manufacture of non-alcoholic beverages	11	180.2	443.8	59.4	85
Manufacture of pottery, earthenware, and ceramics	5	112.2	265.0	57.6	85
Ice factories	29	244.1	55.4	56.0	85
Manufacture of glass, glass products, plastic products and rubber products	76	226.7	491.5	53.9	85
Rubber and rubber sheet	58	27.2	134.1	79.7	90
Leather tanning and finishing	23	9.2	33.7	72.8	90
Sugar mills and refineries	6	61.3	253.8	78.8	90
Sawmills and plywood factories	53	50.8	282.1	82.0	90
Rice Mills	51	116.2	531.8	78.2	90

1/ Value added minus wages and salaries paid.

Source: The Thai National Statistical Office, The 1969 Industrial Census, Tables 1 and 2.

allowed for employment income by one-half, that on professional income from 30% to 20%, that on income of contractors from 80% to 60%, and provide for rate reductions on various income from leasing property. The revised standard deduction rates allowed for incomes from various types of business and industry are fixed to reflect the expenses of different businesses. Additional revenue of about ฿300 million could be expected from these changes in fiscal 1974.

70. Dividends and Interest. Under the present income tax system the first ฿5,000 of income from dividends and 20% of receipts in excess of this amount are tax exempt. Since there is no developed capital market in Thailand, retention of a limited exemption on dividends seems reasonable because of the effects of such an exemption on encouraging saving and investment by the small investors. While it may be argued that further extension of the exemptions would increase the rate of saving in the private sector, this would run counter to the basic need of broadening the income tax base. As a general rule, dividend incomes should not be allowed for tax exemption under the imputation system as proposed in the following section, but the dividends on registered stocks quoted on the new stock exchange may be considered for a special tax exemption.

71. By the provisions of the pending capital market act, the first ฿10,000 and 30% of the rest of dividends received from corporations registered in the stock market will be exempt from personal income tax. The exemptions for non-registered corporations will be the first ฿5,000 and 20% of the remainder of net profits. The Mission finds these provisions unnecessarily generous and grossly unrequitable, and recommends that all dividends received during a year exceeding the first 2,000 baht should be subject to personal income tax.

72. Income tax legislation exempts interest payments on government bonds and on bank deposits from the personal income tax. 1/ The exemption of interest on savings accounts seems justified as an encouragement to saving by lower and middle income groups and should be continued. The exemption should, however, be subject to a ceiling. Accordingly a maximum of ฿500 in interest income is recommended to be exempt from income tax. The amount of interest exceeding ฿500 should be subject to withholding at source (bank) at a flat rate of 20% and be integrated with the personal income tax.

73. The exemption of interest on government bonds from taxation, on the other hand, is an inefficient means of supporting government finance, because high nominal interest rates in lieu of exemptions would secure financing at a lower cost to the government. Furthermore, this exemption is inequitable since it is equivalent to paying higher rates of interest to high income investors. Such exemptions should be discontinued, unless the nature of

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1/ The exemption provision for interest on Thai government bonds applicable to juristic companies and partnerships was repealed in 1969 by Royal Decree No. 30.

certain outstanding securities is such that exemption cannot be avoided. Future issuance of government bonds should be encouraged by raising interest rate payable rather than by exempting the interest paid from income tax.

Capital Gains Tax

74. At present there is no capital gains tax on the sale of real estate in Thailand. The tax treatment of real estate transactions included in Section 42(9) of the Revenue Code exempts from the income tax profits derived from the sale of property obtained which is not "for the purpose of trade or obtaining profit." Since it is difficult to establish that the transaction was "for the purpose of obtaining profit" virtually all the gains realized on the sale of real estate escape taxation, except those realized by official dealers in real estate.

75. The absence of a tax on profits earned from the sale of real estate has undoubtedly contributed to increases in property values generally and in urban land values particularly, and has encouraged speculation in land. The rise in land value is an unearned increment to the income of the owner and should be taxed when realized, regardless of the motive underlying the transaction. A capital gains tax on urban real estate is recommended. Such a tax will discourage speculative investment, and more generally contribute to increased equity. The tax should be administered as a national tax, even though its application will be limited to major urban areas. Administration of the tax may be well integrated with that of the property tax as discussed in the subsequent section. Individual taxpayers should be made responsible for self-assessment of capital gains realized from the sale of real estate. A capital gains tax rate of 25% on occupied land and buildings, and of 50% on unimproved land is suggested. The tax should exempt gains below a stated minimum amount, say, ฿2,000, and should be on profits adjusted by the cost of living index for Bangkok or the wholesale price index to allow for the effect of general inflation.

76. For example, if one purchased a given property in Bangkok in 1965 for ฿500,000, and sold in 1970 for ฿1 million, the "gain" subject to tax would be determined as follows. At the time of sale, let us assume the Bangkok cost of living index was 130 (1965 = 100). At 1970 prices the acquisition price of the property is computed at ฿650,000 (฿500,000 x 1.30). The amount taxable under the proposed capital gains tax would be ฿350,000 (฿1,000,000 - ฿650,000). As an alternative, the wholesale price index might be used as the deflator.

77. One of the provisions which must accompany the proposal for the capital gains tax is the extent of retroactivity. The issue of how far a capital gains tax is to apply retroactively to gains that accrued in the past is often encountered by serious opposition from taxpayers. In general, the greater the extent of retroactivity, the stronger the popular opposition. In order to ensure the adoption of a strong and effective tax on capital gains, it is recommended that the tax would be applied only prospectively to gains that accrue after the date of enactment. Regardless of the question of the

taxpayer's opposition, the extent of retroactivity would certainly depend on the availability of property values as of the base year. In Thailand, urban property values in the past are not easy to obtain, and thus the application of the capital gains tax retroactively may be very difficult.

Corporation Income Tax

78. The corporation income tax is based on net profits of limited partnerships, registered partnerships, and limited companies (or corporations). However, there is one significant exception to this coverage. Any partnership or corporation is treated as a personal entity for income tax purposes if one of the shareholders owns more than half of the capital.

79. Corporate taxation yielded 1.5 billion baht or 6.5 percent of total central government revenues in FY1973. Revenue growth from this source of income has been steady. From 1964 to 1973 the average income buoyancy of tax was 1.3. Rapid increase in proceeds of this tax was mainly due to the rapid growth of industrial and commercial activities. The three step graduation in the rates - 20 percent on taxable income through 500,000 baht, 25 percent on 500,001 through 1 million baht, and 30 percent on 1 million and above - may also have contributed to this increase.

80. The corporation tax is paid by about 11 thousand firms. As shown in Table 16, corporation is by far the most important legal form of business as far as their contribution to taxes are concerned. In FY1968, corporations accounted for 66 percent of the total taxable income or 85 percent of the total income reported by domestic companies, although they constitute only 25.4 percent of the total number of companies. On the other hand, limited partnerships, which are more numerous - 62.8 percent of the returns - account for only 9.2 percent of the taxable income. In FY1968, 217 foreign companies (1.2 percent of the total return) accounted for 22.8 percent of the total taxable income and paid company tax of 120.5 million baht.

81. As shown in Table 17, the corporate income tax was mostly derived from trade and manufacturing activities. In fiscal 1968 these two sectors accounted for 67.5% of tax returns, 73% of gross income, 69.7% of taxable income, and 70.4% of corporate tax payments. However, the share of these sectors in GDP is only 25.1%. This large difference is partially explained by the extent to which the corporate form of business is concentrated in these sectors. The mining and banking, insurance, and real estate sectors are also characterized by a relatively greater tendency to corporate forms while the services sector shows a lesser degree of incorporation and in agriculture corporate forms are almost nonexistent. The low ratio of company income profit to GDP in the public utilities sector reflects the high concentration of government enterprises in this sector, which perhaps are not very profit oriented and some of which are tax exempt.

82. Since those sectors of the economy which are relatively more characterized by incorporation are expanding their share in total GDP, total

TABLE 16: NUMBER OF COMPANY TAX RETURNS, TAXABLE INCOME AND TAX PAYMENTS BY FORM OF BUSINESS, 1968
(Amounts in Million Baht)

Form of Business	Number of Returns		Taxable Income		Income Tax	
	Number	Percent	Amount	Percent	Amount	Percent
Corporations	4560	25.4	1802.1	66.0	417.5	69.5
Limited Partnerships	11267	62.8	250.8	9.2	42.3	7.0
Registered Partnerships	1666	9.3	54.8	2.0	8.6	1.4
Foreign Companies	217	1.2	624.2	22.8	120.5	20.1
Transport Companies	224	1.2	--	--	11.9	2.0
TOTAL	17934	100.0	2731.9	100.0	600.7	100.0

Source: The Thailand Revenue Department.

TABLE 17: COMPOSITION OF TOTAL NUMBER OF COMPANY TAX RETURNS, GDP INCOME AND INCOME TAX OF COMPANIES BY TYPE OF BUSINESS, FY1968
(In Percent of Total)

Type of Business	Number of Tax Returns	Contribution to GDP 1964	1972	Gross Income	Taxable Income	Income Tax
Agriculture, Forestry and Fishing	0.4	37.8	33.8	0.2	0.3	0.3
Mining	1.6	1.6	1.8	3.1	2.1	2.0
Construction	9.0	6.3	5.7	5.4	2.9	2.4
Manufacturing	17.4	12.7	14.2	22.6	33.1	34.3
Public Utilities	5.6	8.9	8.3	3.6	2.9	4.6
Trade	50.1	12.0	13.3	50.4	36.6	36.1
Banking, Insurance and Real Estate	3.0	2.7	4.7	3.6	6.6	9.4
Services	11.0	10.4	11.1	5.6	4.5	3.9
Others[1/]	1.9	7.7	7.0	5.5	10.7	7.1
	100.0	100.0	100.0	100.0	100.0	100.0

1/ Includes ownership of dwellings and public administration.

Source: Data from the Revenue Department and the Bank of Thailand.

corporate activity in the economy will increase at a rapid rate. Data relating to the industrial origin of GDP are presented in Table 17. Between 1964 and 1972, the most important changes in the composition of output were the increase of manufacturing production from 12.7% to 14.2% of GDP and the decline of agriculture's share from 37.8% to 33.8%. The proportion of GDP contributed by the banking, insurance, and real estate sectors also increased substantially from 2.7% to 4.7%. In view of the fact that industries with a high degree of incorporation tend to contribute a growing share of GDP, the corporation income tax, if well administered, could become one of the most productive revenue sources for the government.

83. In fiscal 1968 a total of 17,934 corporate tax returns were filed, of which only 10,846 returns had taxable income. Of these, only 269 companies were subject to the maximum rate of 25%, 1/ but they accounted for 83% of the total corporation tax. At the other extreme, 82% of the total tax returns were subject to a tax rate of 15% and in aggregate contributed only 11% of the total revenue from corporation tax. It is interesting to note the unusually large amount of net loss claimed by the company tax returns. The claims for net loss in proportion to taxable income tend to concentrate on small companies with a gross income of ฿500,000 or less. They are more frequent in the construction and the banking, insurance and real estate business. They represent an estimated amount of ฿00 million revenue loss in fiscal 1968.

84. Corporation tax rates in Thailand are low in relation to the existing personal income tax rates and are also relatively low in comparison with rates in other countries. Income tax rates for an ordinary company in selected Asian countries are as follows: a flat rate of 45% in Malaysia and Singapore; a 30% rate in Pakistan; a graduated schedule of 20%-30%-40% in Korea, and a two-step schedule of 25% and 35% in Philippines. Some justification may exist for a low tax rate on the argument that entrepreneurial risk needs to be rewarded, but the present differentials between personal and corporate tax rates are too great to be warranted. The rate disparities between the personal income tax and the corporation income tax for undistributed profits clearly indicate the advantage of the latter, especially at high income levels. As shown in Table 18 the break-even point is at the level of income just below ฿250,000. At higher income levels, however, profits face more advantageous tax treatment if accumulated in the business.

85. In Thailand the profits of firms subject to the corporation tax are taxed twice: firstly, through the corporation tax, and secondly, through the personal income tax if and when dividends are distributed. The effect is to have a differential tax on business profits. However, if profits are

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1/ The corporation tax rates which were progressive at rates of 15%, 20% and 25% applying to portions of net profits below 0.5 million baht, 0.5 - 1.0 million baht and over 1 million baht respectively in 1968 are at present 20%, 25% and 30% for the same profit slices.

TABLE 18: AVERAGE OF PRESENT AND PROPOSED CORPORATION TAX AND PERSONAL INCOME TAX

(Amount in Thousand Baht)

Taxable Income	Corporation Tax		Personal Income Tax
	Present Tax	Proposed	
10.0	2.0	4.0	1.0
100.0	20.0	40.0	14.2
250.0	50.0	100.0	52.3
500.0	100.0	200.0	161.5
1,000.0	225.0	400.0	427.0
5,000.0	1,425.0	2,000.0	2,835.0
10,000.0	2,930.0	4,000.0	5,830.0

retained in the business, then they go with the first stage corporation tax rate only. Clearly, the present rate structure favors the accumulation of profits in these forms of corporations rather than in personal business or ordinary partnership, after exceeding a break-even level. This level is approximately 250,000 baht under present rate structure (see Table 18). Furthermore, distributed profits are not likely to be accurately reported as part of personal income of recipients, particularly in corporations that are owned mostly through bearer shares.

86. To prevent the corporation form to serve as a shield for avoiding the progressive rates of the personal income tax for strictly personal business all the profits of a shareholder owning more than 50 percent of the capital are subject to personal income tax rates. But this stipulation is quite ineffective in most cases; a person can have a controlling share in a company without reaching the legal 50 plus percent ceiling. Moreover, it is easy to find fictitious shareholders in order to keep the main share below 50 percent. The concept of controlling share, somewhat more general and well developed in the practice of corporation tax, can be a more useful device to prevent a personal (or family) business to take the cover form of corporation for avoidance of progressive income tax rates. The concept of registered partnerships needs to be examined to see whether there is any justification for subjecting them to the corporation tax rather than to the personal income tax as ordinary partnerships.

87. One important issue in the reform of the present corporate income tax is to decide whether or not the present progressive rate structure on company profits should be maintained. This practice, which is not very common, has important drawbacks. Firstly, progression should be with respect to owners' incomes rather than with respect to the company's profit level since large firms may be owned by small shareholders. Secondly, this sort of progression induces companies with growing profits to split their business to avoid climbing to higher tax brackets. One alleged advantage, namely the progressive taxation of family corporations, can, to a certain extent, be achieved by subjecting the controlling shareholders to personal income tax. Progressive rates would give favorable tax treatment to small firms. However, for small firms with a few partners, complete abandonment of the corporate form and opting for taxation under personal income tax is a possibility.

88. A second important issue is the method of linking the corporation tax to the personal income tax. At present, dividend receipts must be reported by personal income tax payers. This procedure provides no incentive for reporting of dividends, nor does it penalize non-reporting.

89. It is recommended that a uniform rate of 50 percent tax on corporate profits be adopted with a 50 percent credit to be written against the personal tax liabilities of the shareholders who receive dividends. This imputation system, sometimes also known as the credit or set-off system, would reduce the differential tax upon the profits of corporate form of enterprises to an effective 25 percent. 1/ This remaining differential tax burden is justified as a counterpart of corporate form of enterprise, namely, easier access to capital market and limited liability in case of risky ventures.

1/ If the possibility of shifting corporate income tax in the long run is taken into consideration, which is very likely in the dominantly corporate sectors, the differential burden is even less.

90. An imputation system of corporate tax would close the present loophole of evading personal income tax by not declaring dividends -- which may lead to a significant tax revenue loss particularly in the case of family corporations. 1/ The distribution of dividends would be encouraged when the shareholders are at low tax brackets and discouraged when they are at high tax brackets. However, this method would induce small shareholders to report the dividends they receive in order to get a refund, and more generally, tax credit would reduce the temptation to avoid reporting the dividends for personal income tax. Finally, since this form of corporate taxation would be in the nature of advance payment of taxes on dividends, the lag between the time of income generation and tax collection would be shortened.

91. Foreign companies conducting business in Thailand are subject to corporation taxation provisions same as domestic corporations. However, in addition to the ordinary income tax on net profit, a remittance tax of 25 percent is applied to any transfer of profits from a branch office of a foreign corporation to its head office abroad. This remittance tax is not levied on foreign unregistered partnerships or foreign-owned personal businesses. If our proposal of corporation tax at a uniform rate of 50 percent of net profits were adopted, the present 25 percent remittance tax on the profit remaining after payment of corporate tax would result in a combined tax rate of 62.5 percent of net profits on all funds transferred. Given prevailing rates of corporation tax in most developed countries which have provisions against double taxation, this resulting rate seems high. Therefore, if the 50/50 system is adopted, the remittance tax should be reduced to 10% so that the combined burden on foreign profits would come to 55%. (The present rate of 25% should be kept if a corporation tax rate of 40/40 is adopted.)

Taxes on Goods and Services

92. In this section we turn to various types of indirect taxes on goods and services. In Thailand, these taxes are classified under two categories - business and excise taxes - and administered separately by the Revenue Department and the Excise Department of the Ministry of Finance. Both taxes are essentially single stage rate taxes at the manufacturers' level. Although the business tax has more of the attributes of a general sales tax at uniform rates - although in some categories the rate is highly differentiated - the present distinction from the excise tax is based, as in many other countries, mainly on administrative expediency. Excise taxes are enforced by methods which are different - such as the continuous surveillance of liquor distilleries and oil refineries - from the procedures based more on self assessment and accounting controls that typifies the administration of business taxes.

93. A move towards either a general sales tax at retail level or a value added tax is premature. Existence of too many businesses would make

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1/ Although this tax loss can, is principle, be recorded by taxations of capital gains at the time of stock sales, the chances of this happening in an underdeveloped capital market are low.

the implementation of a general sales tax very difficult, as was experienced in Thailand before the present system was adopted. Given the underdeveloped state of business practices and record keeping in the country, a change to a value added tax system should not be aimed at in the near future either. The discussion below, therefore, is predicated on the objective of developing and simplifying the present system of business and excise taxes on goods and services, with emphasis on increasing its revenue yield, improving its progressivity, and eliminating the distortionary effects, particularly in regard to cascading.

94. Business Tax. At present, the business tax is the second most productive source of revenue to central government revenues and yields nearly twice as much revenue as all income taxes combined. In fiscal 1973 the business tax produced ฿5.1 billion or 22.4% of the total tax revenue, as against ฿3.2 billion or 13.9% for income tax.

95. The business tax is basically a sales tax imposed on gross receipts of traders including importers, exporters, manufacturers, contractors of hired works, financial institutions, and operators of hotels and restaurants. There is a problem of tax pyramiding caused by the tax falling both on raw materials and semifinished goods and on the finished goods produced from them. This "cascade" or cumulative nature of the tax is most inequitable among producers. But it must be credited with providing the basis for most of the individual income tax assessment on business income, and even for much of the company income tax. The individual income tax on business income may be considered nothing more than a surcharge to the business tax. The assessment of gross receipts under the business tax is extremely deficient, and this deficiency is in turn carried over into the individual income tax.

TABLE 19: BUSINESS TAX COLLECTION, FY-1970

Business Category	Tax Rate (% of gross receipts)	Amount /1 (million baht)	Percent of Total
Distribution & processing of goods	1.5 up to 30.0	1,375.6	68.8
Rice mills and saw mills	2.5 and 4.0	102.7	5.1
Made to order goods	2.0	220.0	11.0
Letting of proporty	2.5	8.4	0.4
Warehousing	2.5	2.1	0.1
Nightclubs, hotels and restaurants	2.0, 7.5 and 10.0	80.2	4.0
Transport business	0.5	25.8	1.3
Pawnbrokers	2.5	5.1	0.3
Commission agents	5.5	23.7	1.2
Sales of land and buildings	3.5	16.7	0.8
Banking	2.5 and 10.5	97.2	4.9
Life and general insurance	2.5 and 3.0	25.0	1.3
Other		15.9	0.8
Total		1,998.4	100.0

/1 The amount does not include business tax collections at the Customs Department.

Source: The Thailand Revenue Department

96. A schedule of tax rates and a breakdown of estimated tax receipts are shown in Table 19. By far the most important single group of business taxes are those on the distribution and processing of goods, amounting to ฿1.4 billion or 69% of total business tax receipts in fiscal 1970. Of the total tax collected from the sale of goods, about 43% was paid by importers and the remainder by producers and others. Other important items are taxes on

TABLE 20: BUSINESS TAX SCHEDULE

Description of Business	Trader Liable to Business Tax	Tax Rate as a Percentage of Gross Receipts
Type 1 Goods and by-products not specified under types 2 through 8, or under any other category	Importer or Manufacturer	7.0
Type 2 (a) Refrigerator, cooling cabinet, airconditioning machine, humidity controlling machine, air purifier or any other goods under a different name but of similar nature.	Importer or Manufacturer	30.0
(b) Massaging, blowing, grinding, or drying machine, washing machine, vacuum cleaner, floor polishing or scrubbing machine, cooking, boiling or toasting machine, stove or oven or other appliances operated by electricity, fuel, oil, or gas.	Importer of Manufacturer	20.0
(c) Watch or clock.	Importer or Manufacturer	20.0
(d) Television receiving set, radio receiving set, phonograph record playing machine, sound recording machine, sound amplifier or modulator, phonograph record, sound recording tape, or any other article under a different name but of similar nature, excluding radio receiving sets with not more than 4 tubes or transistors which are taxable under type 1.	Importer of Manufacturer	20.0
(e) Musical instruments excluding native instruments which are taxable under type 1.	Importer or Manufacturer	15.0
(f) Cinematographic camera or still picture camera, apparatus used for taking or reproducing pictures or documents, projector or cinematographic projector, film winding or editing machine, machine for	Importer or Manufacturer	15.0

(Table 20 Contd.)

Description of Business	Trader Liable to Business Tax	Tax Rate as a Percentage of Gross Receipts
developing, copying, enlarging or printing pictures, documents or cinematographic films, unused films or other objects for use in printing or taking pictures, document or motion picture, excluding X-ray machines and X-ray films which are taxable under type 1.		
(g) Accessories, components, or parts of goods in (a), (b), (c) and (f). Goods under (a) through (g) which are used as medical equipment and approved by the Minister shall be taxed under type 1.	Importer or Manufacturer	15.0
Type 3	Importer or Manufacturer	15.0
(a) Electric lamp shade or globe, electric fan or iron.		
(b) Motor cycle or motor units for bicycles.	Importer of Manufacturer	12.0
Type 4	Importer or Manufacturer	40.0
(a) Passenger car.		
(b) Buses with not more than 10 passengers capacity.		
Type 5 1/	Importer or Manufacturer	30.0
Whisky, brandy, gin, rum, wine, and other potable spirits, excluding local white wine (surarong) and beer which are taxable under type 1		
Type 6	First seller	1.5
Books, documents or printed materials.		
Type 7	Sellers at every level	3.0
(a) Gold, platinum, white gold, silver, red gold or alloy of		

1/ Now exempt from business tax by N.E.C.D. No. 175 dd. 14 July B.E. 2515

(Table 20 Contd.)

Description of Business	Trader Liable to Business Tax	Tax Rate as a Percentage of Gross Receipts
such materials, goods made of such materials, and imitation of such materials or goods.		
(b) Diamond gem, ruby, emerald, topaz, amethyst, opal, sapphire, zircon, lapiz lazuli, jade, pearl or any other precious stone of similar nature, any goods made of such materials, and imitation of such materials or goods.		
(c) Secondhand articles under the law on dealing in secondhand articles, only if such articles are antiques or objects of arts		
Type 8	Exporter	4.0
(a) All kinds of metallic minerals or ores except manganese, but not including articles made of metallic minerals or ores which are taxable under type 1.		
(b) Sheet rubber or other kinds of rubber which are produced or derived from any part of rubber trees, manganese mineral or ore, whether metallic or non-metallic, but not including articles made of rubber or such mineral or ore which are taxable under type 1.	Exporter	1.5

services (11.0%), and rice and saw milling (5.1%). A substantial amount of revenue was also collected from nightclubs, hotels and restaurants, and from financial institutions.

97. The rate of business tax on the sale of goods was originally differentiated into 9 different commodity subgroups but these have been reduced to 7 after the exclusion of industrial raw materials and alcoholic beverages from the tax. Commodities grouped under Type 1 (Table 20) which include food and beverages, clothing, furniture, machine tools and applicances, bicycles, petroleum and petroleum products, etc. are assessed at a rate of 7%. The tax rates on commodities under Type 6 (books and printed materials) and Type 7 (gold, silver, jewelery, etc.) are 1.5% and 3%, respectively. Less essential commodities grouped under Type 2, 3, and 4 are taxed at much higher rates, e.g., passenger cars and small size buses, at 40%; refrigerators, air conditioning, electrical applicances, televisions, etc., at 30%; and electric lamps and electric fan and iron, at 15%.

98. The amounts estimated from the monthly business tax receipts which were available for the Bangkok metropolitan area show that taxes received from the sale of Type 1 commodities contributed ฿ 1.7 billion, 36% of total business tax, and taxes realized from the sale of passenger cars and buses, (Type 4) was about $185 million in fiscal 1973. For other commodities revenue information was scanty. The disaggregation of taxes on Type 1 commodities for the Bangkok/Thonburi metropolitan area is shown with that of Thailand in 1966 as follows:

	Bangkok 1973	Thailand 1966
	(in Millions of Thai Baht)	
Food and beverage	242	197
Clothing and leather goods	209	100
Cosmetics and pharmaceutical products	151	59
Construction materials and furniture	215	91
Machine tools and appliances	43	60
Bicycles, boats and lift vehicles	49	56
Petroleum and petroleum products	523	84
Miscellaneous goods (tires, batteries, paper, etc.)	127	118
Other clay, wood, plastic, stone metal, etc. products	100	69
TOTAL	1,661	832

The amounts shown for 1973 are tax receipts estimated for Bangkok and Thonburi only, and thus they are not directly comparable with those for the entire Kingdom. The figures do indicate the increasing importance of taxes on petroleum products as a component of business tax revenues.

99. The business tax rate is too highly differentiated, much more so than any discrimination between luxuries and essentials would warrant, particularly so in the tax rates based on services. It is suggested that the rate structure of business taxes be consolidated under three classes separately for goods and for services as follows:

	Goods	Services
Basic rate	10%	5%
Reduced rate-essentials	5%	3%
Increased rate - luxuries	40%	10%

Further differentiation in rates should be confined to few exceptional cases. A suggested list of business tax rates incorporating the suggestion above is given in Table 21. The standardization of rates on services at this level would produce an estimated ฿1.0 billion additional revenue in fiscal 1974. The major portion of the increase is expected from hired labor and transport business.

100. The scope of the business tax should be extended to cover tax on electricity consumption -- which was abolished in 1965 -- and on telephone services. Sale of professional services should also be subjected to the business tax. Both the revenue and the equity aspects of the business tax are vitiated by the fact that the so-called "liberal professions" are exempt from the tax. It is widely acknowledged in Thailand that under-reporting of taxable income and tax evasion are prevalent among doctors, lawyers, accountants, architects, and other professions. This loophole could be plugged by making professional income subject to the ordinary business tax. Practical measures to strengthen the business taxation of professional activities would include obligatory registration of all professionals with stiff registration fees.

101. Ideally, the business tax should be designed so as to avoid discriminatory effects on consumer choice and methods of doing business. This objective would be best served by a uniform rate applied to consumer goods and services at the retail level. However, social as well as economic considerations make it difficult if not impossible to apply such a uniform rate to all of the consumer goods and services. Therefore, the distortionary effect of business taxes should be minimized by instituting a system of tax credits where cascading is evident.

102. A group of commodities, the production of which can be audited through physical monitoring, should be included under the excise system and be administered by the Excise Department. Recent changes in Thai tax system have already moved in this direction. In 1973, business taxes on non-alcoholic beverages, tobacco, and liquor were integrated into the excise tax. It is suggested that commodities now subject to both business and excise taxes should be combined into a single tax, e.g., tax on cement and petroleum products. A further integration can be made through an expansion of excise tax coverage to some other commodities that are now subject to

TABLE 21: PROPOSED NEW EXCISES AND TAX RATES

Commodity Group	Proposed Rate (Ad Valorem %)
1. Electrical goods, including those using fuel oil and gas.	
(a) Type 2(a): Refrigerator, air-conditioner, cooling cabinets, etc.	30
(b) Type 2(b): Massaging, blowing, grinding or drying and washing machine, vacuum cleaners, etc.	20
(c) Type 2(d) and (e): Television, radio, phonograph record playing machine, etc.	30
(d) Type 3(a): Electric lamp shade or globe, electric fan or iron.	15
2. Motor cars and Motor cycles.	
(a) Type 4(a) and (b): Passenger cars and small size buses.	40
(b) Type 3(b): Motor cycle or motor units for bicycles.	15
3. Watches, precious metal and jewelery.	
(a) Type 2(c): Watches and clocks.	15
(b) Type 7(a), (b) and (c): Gold, platinum, diamond, ruby and goods made of such materials, imitation of such materials or goods.	15
4. Petroleum and petroleum products (a portion now included under Type 1 and Schedule 1)	
(a) Gasoline	50
(b) Kerosene	30
(c) Diesel	30
(d) Jet Fuel	30
(e) Bunker oil	20
(f) Lubrication oil	20
(g) Petroleum gas	15
(h) Petroleum bitumen	15
5. Cosmetic products (a portion now included under Type 1 and Schedule 1)	20
6. Photographic equipment: Type 2(f)	20

the business tax. Commodities suggested to be included in new excises are most of those falling under Type 2, 3, 4 and selected items of Type 1 specified in Section (93) of the Revenue Code. This transfer should be gradual depending on the development of the administrative preparation in the Excise Department.

103. Various measures to improve the administration of the business tax are essential, and they are similar to those required to strengthen the administration of income tax on business income. Heavy penalties for failure to declare and for under-reporting especially for corporations and the large individual taxpayers are called for. Substantial improvement in assessing the larger taxpayers should be possible. But for the large number of small taxpayers, the task is much more difficult. Progress can be made through strict licensing and by establishing presumptive standards for sales.

104. Excise Tax. The growth of excise tax revenue has been steady, and produced ฿ 4.1 billion or 20.5% of total tax revenue in 1973. Of these, taxes on two major items, petroleum products and cigarettes, accounted for 65.3% and the balance was mainly generated by taxes on liquor, non-alcoholic beverages, and beer. The ratio of total excise revenue to GDP has been maintained at a level ranging from 2.13% to 2.19% from 1968 to 1973 (Table 22). On the basis of preliminary estimates this ratio is expected to rise to a level of 2.97% in 1974, the three items (petroleum products, liquor, and tobacco) accounting for 85.6% of the total. The substantial increase in revenue expected in 1974 is mainly due to recent rate increases. Major changes in excises in 1973 include a 50% increase in the cigarette tax, a 25% increase in the excise on whisky, a rise in the tax on beer from ฿ 8.7 to ฿ 10.0 per litre, and increases in gasoline and diesel taxes from 1 baht to 1.3 baht per litre and from 0.12 baht to 0.3 baht per litre, respectively.

105. While yields from these major categories have kept in step with the rising revenue needs of the Government, taxes on other commodities have not fared well. Additional revenue sources that the government might tap include increases in the taxation of non-alcoholic beverages since current level of this tax is still quite low and consumption of these drinks is rising rapidly. In particular, the tax on non-alcoholic beverages is light, and prices of soft drinks are lower than those found in neighboring countries. In view of the rapidly rising trend in consumption, there would be a substantial opportunity for greater revenue. Higher taxes are recommended for soft drinks which cost more than 3 baht a bottle at present. Additional scope also exists for increasing tax yields from petroleum products, particularly through additional taxation of gasoline and diesel fuel. Even after the 1973 increases in excise rates, the taxation of gasoline and diesel still appears below the level warranted by the costs of providing the infrastructure, as well as the social costs of congestion and pollution that road transport imposes.

106. At present the excise tax rate on diesel fuel (20% of the retail price) is far below that on gasoline (40% of the retail price). As a result, the present fuel tax distorts the choice between diesel using and gasoline

TABLE 22: Excise Tax Revenue as a Percent of Gross Domestic Product, 1968-1974
(in million baht)

	Petroleum Products		Tobacco Products		Liquor		Beer		Nonalcoholic Beverages		All Others 2/		Total	
	Amount	Percent of GDP	Amount	Percent of GDP	Amount	Percent of GDP	Amount	Percent of GDP	Amount	Percent of GDP	Amount	Percent of GDP	Amount	Percent of GDP
1968	1170.0	1.00	665.0	0.57	276.4	0.24	175.0	0.15	86.0	0.07	118.6	0.10	2491.0	2.13
1969	1390.0	1.08	790.0	0.61	276.4	0.22	195.0	0.15	96.0	0.08	131.7	0.10	2879.1	2.24
1970	1555.0	1.14	840.0	0.62	296.6	0.22	215.0	0.16	123.0	0.09	134.4	0.10	3164.0	2.33
1971	1712.0	1.18	968.0	0.67	350.0	0.24	282.0	0.19	271.0	0.19	140.8	0.10	3723.8	2.56
1972	1385.0	0.87	1120.0	0.70	382.0	0.24	230.0	0.14	240.0	0.15	136.5	0.09	3493.5	2.18
1973	1560.0	0.83	1120.0	0.60	655.0	0.35	290.0	0.16	340.0	0.18	137.8	0.07	4103.8	2.19
1974 1/	2500.0	1.20	1700.0	0.82	1087.0	0.52	367.0	0.18	378.0	0.18	143.0	0.07	6175.0	2.97

1/ Preliminary estimates

2/ Includes cement, matches, lighters, playing cards and snuff.

Source: The Thailand Excise Department

using motors. Of course gasoline and diesel are not used exclusively in road transport. Since diesel-using agricultural and industrial machinery does not produce any road costs, such fuel users may be providied by periodic rebates rather than a low tax. However, in view of maintaining low fares for the use of mass transportation, it is suggested that the rate differential in tax be eliminated in steps so that it would not disrupt the urban bus services especially in Bangkok. To maintain low bus fares, it would be more preferable to reduce taxes on bus transport by reducing import duties, excises, or license fees rather than keeping a low tax on diesel fuel.

107. Since most excises in Thailand are assessed on a unit basis rather than as an ad valorem rate, the tax base does not respond automatically to price rises thus warranting frequent rate increases. To introduce an element of automaticity in this adjustment it is recommended that excises on petroleum products, liquor, beer, and non-alcoholic beverages be placed on ad valorem rate wherever administratively possible. In cases where this is not possible,, an automatic adjustment system of specific rates to costs should be established. To conclude, the excise system in Thailand can be improved through: (a) integration of excises with business taxes on selected commodities; (b) extension of a progressive rate system on different types of commodities; (c) assessment on an ad valorem rate rather than a unit basis; and (d) consolidating nine separate Excise Codes into a single one to improve the administration.

Land and Property Tax

108. The current house and rent tax is a tax imposed annually on owners of houses and buildings which are either rented or are used for commercial purposes. Every year the owner of such property is required to submit a statement of annual rental value of the property in tax return. For the intervening three years the tax liability on that property remains the same as in the year when the rental value was filed. Rental value assessments of most structures are usually outdated and fall far below realized values. Since the tax does not extend to owner-occupied houses and buildings, there is no discouragement to the building of large houses by the wealthy.

109. At present, the house and rent tax is levied at 12.5% of the assessed annual rent. While the revenue composition of Bangkok differs from other units of local government, Table 23 shows that in Bangkok the house and rent tax is expected to account for 20.4% of total local revenue and 60.8% of all revenue from locally administered taxes in fiscal 1974. This tax currently imposes an extremely low burden both in relation to property owners' income and to the capital value of property. It could easily yield much more revenue than it does at present.

110. Despite a rapid rise in urban property values in Thailand, the house and rent tax has not generated corresponding increases. This is partly because of the limited coverage and the low rates of the tax, partly because of the obsolete assessment system and inefficient administration of the tax. It is strongly recommended that the present house and rent tax should be

Table 23: REVENUE ESTIMATE OF METROPOLITAN BANGKOK, FY-1974

Revenue	Amount in Millions of Baht		Percent of Total
Total Revenue	720.5		100.0
Taxes	589.2		81.8
Business Tax /1	321.9	(44.7)	
House and Rent Tax	146.7	(20.4)	
Gambling Tax	33.2	(4.6)	
Land Development Tax	27.8	(3.9)	
Signboard Tax	26.5	(3.7)	
Entertainment Tax /1	10.1	(1.4)	
Liquor and Beverage Tax /1	9.0	(1.2)	
Slaughtering Tax	7.0	(1.0)	
Rice Export Tax /1	6.9	(1.0)	
Property Income	47.4		6.6
Fees and Charges	45.7		6.3
Public Utilities	1.0		0.1
Others	37.3		5.2

/1 A 10% surcharge levied on the central government taxes.

replaced by a property tax both on land and on improvements to the land. This tax reform would involve the repeal of the various concessions now given to the present house and rent taxpayers, and the adoption of a single standard of value (capital or market value) applied uniformly to rental as well as to owner-occupied property. This capital value tax may be levied separately at different rates on land and on improvements to make possible specific and substantial taxation of land values.

111. If actual and imputed rental income from buildings could be taxed effectively through the income tax system, the ideal tax on real estate would be a tax on site value. In the conditions likely to prevail in Thailand, the taxation of land value alone cannot be justified for several reasons. First, a tax on site value alone would not only fail to tap the wealth created by investment in buildings but would entail insufficient payments for municipal services provided. Second, there are problems of equity that arise if ostentatious construction is left untaxed. Third, it is difficult to assess the value of the land alone if transactions in vacant lots are not frequent enough to furnish adequate estimates of unimproved land value.

112. The tax on property is strongly recommended in countries where ownership of land is sought as a refugee from inflation. The diversion of capital to non-productive land speculation tends to accentuate the rise in land prices. The land value tax has not only a large revenue potential but would also alleviate speculative increases in land value and provide incentives for more economic use of land. The replacement of the house and rent tax with an annual tax on capital value of property and a capital gains tax on increments in property value would strengthen Thailand revenue system.

113. With regard to the taxation on rural land, the land development tax is imposed on the assessed value of unimproved land not subject to the house and rent tax. As a general rule, the tax base is the average land value assessed once in every four years. If, however, the prices of land in a taxing district (tambol) change rapidly, the tax base can be revised more frequently by a committee appointed by the provincial governor. The responsibility for its administration is assigned to the provinces, municipalities, and sanitary districts for lands lying within their jurisdiction.

114. Under the present Revenue Code, land that is used for owner residence or devoted for annual crops is either partially or fully exempt from the tax. This concessional exemption together with the perverse rate structure cripples the potential yield of the tax. Furthermore, the effect of providing excessive deductions and exemptions creates a tendency for landowners to break up their holdings into small pieces to take the tax advantage. In case of a person owning land in several provinces, the allowable deductions or exemptions are limited to land in only one province, but the land holdings are taxed separately, not combined for each landowner. Thus, if the future assessment of tax is made on the basis of the aggregate holding by any one individual, it would undoubtedly broaden the tax base and increase the revenue to local governments.

115. As to the tax rate, there are 43 different rates specified for the same number of land value brackets (for detail see Annex E). The rate ranges from 0.25% for land valued at ฿ 200 per Rai to 0.50% for land valued at ฿ 10,000 per Rai, and declines to less than 0.10% for land value exceeding ฿ 300,000 per Rai. The land development tax, as exemplified by its rate structure is not only regressive but the tax burden is extremely light in relation to the value of land and income of the landowners. In FY1971, the tax produced only ฿ 213.0 million. This amount on a per capita basis equals to a mere 6 baht per person. A much larger revenue can be raised by improving the present tax through the adoption of (a) a 1% uniform rate on the value of land, (b) the repeal of the preferential treatment on farm land devoted to annual crops, and (c) the limitation of the household area exemption to only 0.50 Rai per family or household in rural areas.

116. The success of property taxation will depend greatly on practical details regarding the assessment of property values, availability of the administrative facilities, the existence of a fiscal cadastre, and the availability of real estate market information. The present practice of self-assessment of a tax base (annual rental value) by individual taxpayers once in every four years is inadequate in urban areas where property values rise very rapidly, and assessment of property values and taxes made every other years would be more suitable. With respect to taxes on residential properties, serious consideration should be given to an annual tax levied at progressive rates on both land and house in excess of a stated minimum value. This provision seems to have been useful in Korea not only to keep private savings away from unproductive uses in luxury homes but also to make the revenue system more equitable. Properties other than those used for residential purposes should be taxed at a flat rate.

117. Although revenue from the property tax is now used to finance local expenditures, in the future the tax should be an integral part of the national tax structure. Therefore, serious consideration should be given to the possibility of transferring the administration of the tax on property to the Revenue Department since the national government is better equipped to handle technical problems of property assessment and administration.

Taxation of Rice Export

118. Rice exports are subject to three explicit taxes: the rice premium, an export duty on rice and municipal taxes on rice exports. The revenues from the rice export premium and from export duty accrue to the central government, and the revenue from the municipal tax on rice export accrues to municipal and sanitary district governments. In addition the central government earns profits on its trading in rice with other governments. These profits are termed a "rice premium." 1/

1/ The rice export premium as a tax and the profit on inter-governmental trade derived from the same historical origin. See Annex F (paragraphs 4 and 5). The profit on official trading derives from the fact that the government purchases rice at prices below the market level by using a statutory force similar in form to its powers of taxation.

119. The public sector, particularly the central government, obtained substantial revenue through these channels. Prior to the 1960's the rice premium in these two forms (including their predecessors) and the export duty on rice accounted for over 15 percent of central government current revenue. The share began to decline in the early 1960's, but the revenue from these sources remained higher than the revenue from all income taxes in Thailand through FY1965/66. A rapid decline in the share occurred after FY1968/69, when the rice premium revenue fell in absolute amount. In FY1971/72, the rice premium and export duty on rice accounted for less than 2% of central government current revenue. In FY1973/74 the revenue from these sources are expected to more than double from the FY1972/73 level to ฿ 2,500 million, but the share in the central government current revenue will be less than that in the early 1960's. As for the municipal tax, very few statistics are available but existing data show that these revenues were very small compared to central government revenues from the taxation of rice exports.

120. The rice exports have been taxed primarily for the revenue they yield and for isolating the domestic market from world price fluctuations as will be pointed out below. However, these taxes, together with policies on rice marketing, have had an effect on income distribution and resource allocation in agriculture which cannot be ignored.

121. Rice Premium. Up to 1950 the Ministry of Economic Affairs operated a Rice Bureau (later reorganized as the Rice Division), which purchased all surplus rice from domestic wholesalers at local prices for export on a government-to-government basis at world prices, the difference being absorbed by the Government. In 1950 rice exporting began to be devolved by the Rice Bureau to designated private firms in return for license fees, the conversion of export earnings into baht at the official (overvalued) exchange rate, and individually negotiated profit-sharing arrangements. This export "premium" system was regularized in 1952 with the fixing of profit-sharing arrangements for all rice exports and was further elaborated in 1954 with the standardization of license-granting procedures and the differentiation of "premium" rates by variety and grade of rice.

122. The official liberalization of the Thai economy in 1955 involved among other things the end of multiple exchange rates and direct public participation in a variety of private sector activities including rice exporting. These changes required a thorough-going reorganization of the Government's fiscal system, particularly the replacement of the exchange-conversion, profit-sharing, and license-fee arrangements that had constituted the government's chief means of tapping the resources of agricultural sector. The replacement of the former taxes, a tax levy on rice exports--known as the Rice Export Premium in cognizance of its patrimony--has remained in effect since 1955 with only minor modifications and interruptions.

Table 24 : Revenue from Rice Export Taxes
(Millions of Baht)

	Rice Export Premium /1	Export Duty on Rice	Sub-total	Sub-Total as % of Central Govt. Current Revenue	Municipal Tax on Rice Exports
FY 1956	842		842	16.5/2	n.a.
FY 1960	745		745	11.0/2	n.a.
FY 1962/63	800	153	953		n.a.
FY 1963/64	1090	197	1287		n.a.
FY 1964/65	1250	197	1447		n.a.
FY 1965/66	1067	218	1285	10.1	n.a.
FY 1966/67	929	195	1124	7.8	n.a.
FY 1967/68	1116	151	1312	7.8	n.a.
FY 1968/69	1236	157	1393	7.7	9.0/3
FY 1969/70	654	135	789	4.3	8.6/3
FY 1970/71	262	117	379	2.0	8.4
FY 1971/72	163	192	355	1.7	16.1/3
FY 1972/73	276	n.a.	n.a.	n.a.	n.a.
FY 1973/74 /4	1470	n.a.	n.a.	n.a.	n.a.

/1 Including profits from government-to-government rice trade.

/2 As percent of central government "ordinary" revenue.

/3 Estimate based on partial data.

/4 Budget estimate as of August 1974.

Sources: FY 1956 and FY 1960: J.C. Ingram, Economic Change in Thailand 1850-1970, 1971.
FY 1962/63-FY 1973/74: Bank of Thailand.

Table 25: Rice Export Premium Rates 1/
(Baht per metric ton)

	Oct. 27, 1972- Aug. 8, 1973	Aug. 9, 1973- Sept.17, 1973	Sept. 18, 1973- Dec. 5, 1973	Dec. 6, 1973- Jan. 31, 1974	Feb. 1, 1974 Mar. 21,1974	Mar. 22, 1974 to date
White rice, 100%	750	750	5,000	3,000	4,500	5,100
White rice, 5%	750	750	1,400	3,000	4,500	5,100
White rice, 10%	500	500	1,300	2,700	4,000	4,600
White rice, 15%	500	500	1,300 2/	2,700	4,000	4,600
White rice, 20%	-	-	1,300	2,700	4,000	4,600
White rice, lower than 20%	-	-	1,100	2,300	3,500	-
White broken rice, A1 Super Special	-	900	900	1,800	2,800	3,400
White broken rice, A1 Super and Special	-	650	650	1,300	2,000	2,350
White broken rice, A1 Ordinary	-	650	650	1,300	2.000	2,350
White broken rice, C1 Super Special and	-	500	500	1,000	1,700	2,050
Ordinary	-	500	500	1,000	1,700	2,050
White broken rice, C3	-	500	500	1,000	1,700	2,050
White broken rice, others	-	-	-	-	-	-
Glutinous rice, long grain 10%	500	1,100	1,100	2,200	3,500	4,100
Glutinous rice, long grain 15%	500	500	500	-	-	-
Glutinous rice, short grain 10%	500	1,100	1,100	2,200	3,500	4,100
Glutinous rice, short grain 15%	500	500	500	-	-	-
Broken glutinous rice, A1 Special	-	600	600	1,200	2,200	2,250
Broken glutinous rice, C1 Special	-	600	600	1,200	2,200	2,250
Cargo rice, 100%	675	675	1,200	2,200	3,500	4,100
Cargo rice, 5%	675	675	1,200	2,200	3,500	4,100
Cargo rice, 10% and 15%	500	500	1,100	2,000	3,200	3,800
Cargo rice, 20%	-	-	-	-	3,200	-
Cargo rice, 25%	-	-	1,100	2,000	3,200	3,800
Cargo rice, lower than 25%	-	-	-	-	-	-
Broken cargo rice of all grades	-	-	500	1,000	1,700	2,050
Parboiled rice, 100% and 5%	350	1,000	1,000	2,000	3,000	3,600
Parboiled rice, 10% and 15%	250	900	900	1,800	2,800	3,400
Parboiled rice, 25%	-	900	900	1,800	2,800	3,400
Parboiled rice, lower than 25%	-	-	-	-	-	-
Broken parboiled rice of all grades	-	500	-	1,000	1,700	2,050
White rice flour	-	-	300	600	800	1,150
Glutinous rice flour:						
Fine	-	-	300	600	800	1,150
Ordinary	-	-	300	600	800	1,150
Vermicelli made from rice	-	-	150	300	400	600

1/ The following rate schedules do not refer to export quotas, reserve requirements, and other controls of the rice export trade. Premium rates on glutinous rice to Laos have deviated from the following rate schedules.

2/ Premium on white rice, short grain 15% set at ฿1,400 per metric ton.

123. The tax base for assessment of the Rice Premium presently consists of 5 major trade classifications of rice subdivided as follows: 14 categories of white rice, 6 categories of glutinous rice, 7 categories of cargo rice, 5 categories of parboiled rice, and 4 categories of rice flour and vermicelli (see Table 24). This breakdown is a slightly modified version of the tax base as it was first instituted in 1955 and is now rarely amended. The premium rate is specific (per metric ton) and varies by commodity classification. In recent years the rate structure has been adjusted so frequently that some have called the premium a "sliding scale" tax. Because export prices fluctuate from sale to sale and the premium rate structure is adjusted from time to time, it is not possible to calculate the premium rate structure in ad valorem rate equivalents, but the implicit ad valorem rate structure would appear to be slightly progressive, 1/ especially type of rice, as lower-priced export categories are frequently exempted from payment of the premium. 2/

124. While the premium's rate structure has been adjusted a number of times since 1955, there has been a dramatic increase in the frequency and magnitude of rate changes and a noticeable shift from across-the-board adjustments to more detailed compositional alterations since 1967-68. From 1955 to 1967 the rate structure was changed only 22 times, and a number of these changes consisted of nothing more than elaborations of the base. On the other hand, the rate structure was changed seven times during the recent 16-month period, October 1972-March 1974, and as Table 26 indicates, these adjustments differ substantially from category to category. 3/ Table 26 illustrates the major break in the premium-rate adjustment trend that occurred between 1966 and 1967, reflecting a shift in the Government's attitude to the premium as a fiscal policy instrument.

1/ With respect to the price of rice.

2/ Between 1967 and November 1969, the premium was actually set at ad valorem rates.

3/ Premium rate adjustments during the months immediately preceding this period. In April 1971 the premium was eliminated on all grades but 100% and 5% white rice, cargo rice and parboiled rice. In September 1972 this unprecedentedly rate structure was discarded and the former rates were reimposed on most grades.

Table 26: Year-to-Year Premium Rate Adjustments, White Rice, 5% and 10% Broken* (Baht per metric ton)

	White Rice, 5% broken	White Rice, 10% broken
1959	0	-32
1960	-45	-63
1961	0	25
1962	30	55
1963	30	30
1964	0	0
1965	0	0
1966	0	0
1967	368	322
1968	351	306
1969	-373	-378
1970	-338	-338
1971	-208	-637
1972	0	-100

*Expressed as change in mid-year premium rate from previous mid-year rate.

Source: Board of Trade

125. Other Taxes and Controls on Rice Marketing. Aside from the rice export premium (in tax form), most rice exports are liable to export duty and municipal tax. The export duty is levied and administered by the Customs Department (Ministry of Finance). This is an ad valorem tax the rate of which varies depending on the grade of rice. Prior to November 1973, the rates ranged from 3.2 percent to 7 percent. On November 23, 1973, all rates were raised to 10 percent. The municipal tax is also collected by the Customs Department, but the revenue (net of specified commissions for the Customs Department) is remitted to the Department of Local Administration (DOLA, Ministry of Interior), which in turn allocates the receipts to municipal and sanitary district governments. This tax is levied at specific rates on all rice liable to export duty. The rate is 1 baht per 100 kg for white rice and cargo rice, and 0.5 baht per 100 kg for broken rice, paddy and bran.

126. Rice export taxes function not only as revenue instruments of the public sector but also as indirect price control instruments. The government has also intermittently adopted various direct quantity controls over rice exports. Direct market interventions have been facilitated by the standing rule that rice exporters must obtain licenses to clear their shipments throug customs. A rice export license can be obtained only upon submission of a promissory note to the Ministry of Commerce in the amount of the anticipated premium liability. Although licenses are ordinarily available in unlimited

amount, restrictions on their availability have been the means of enforcing export quotas (and outright bans) during the rice shortages of 1957/58, 1962/63, 1966/67 and 1972/73.

127. During the most recent increase in rice prices several unprecedented measures were taken in an effort to stabilize domestic and export markets. Instead of relying on premium rate adjustments and limited quota restrictions, the "standard" means of adapting to speculative rice market conditions, the Government decided on massive direct intervention. Starting in November 1972, a rice reserve-requirement system was introduced. 1/ For every 100 tons of rice exported, exporters were required to sell a specific percentage-equivalent to the government at a fixed price. The reserve requirement has been altered a number of times since its inception, with the reserve rate ranging from a low of 5 percent of export volume to a high of 200 percent (see Table 27).2/

Table 27: Rice Reserve Requirement

November 10, 1973 - January 28, 1973		5%
January 29 - March 4, 1973		10%
March 5 - March 31, 1973		25%
April 1 - May 31, 1973		50%
June 1 - July 30, 1973		100%
July 31 - October 3, 1973		200%
October 4 - December 5, 1973:	white rice	100%
	other types	200%
December 6, 1973 - to date		100%

Source: Bank of Thailand

128. Government Policy. The Thai Government's fiscal policy objectives with respect to the place of the agricultural sector and rural populace within the overall economic context are nowhere clearly defined. The several Development Plan documents issued since 1961 might be expected to present the most detailed statements of objectives. Though these documents contain a

1/ A precedent for this scheme was the Government's earlier (1961) establishment of a Rice Reserve Plan, a buffer stock system organized as a public enterprise within the Ministry of Economic Affairs.

2/ As the crisis continued to deepen, the Government resorted to an export quota system, and in June of 1973 placed a total ban on nonglutinous rice exports. At the end of July the ban was lifted from parboiled and broken rice, and certain other rice categories were also permitted to re-enter the export market under close supervision.

series of rather gradiloquent pronouncements concerning long-term agricultural targets, Plan implementation has deviated considerably from these expressed goals, and short-term fiscal policy appears to work to quite different ends.

129. In the past, Government's policy objectives have traditionally stressed revenue collection, subsidization of the urban population's cost of living, and administrative expediency. The growing complexity of the Thai economy and the rising pressures on the Thai Government to stimulate national development have forced increasing consideration of a variety of other aims, the most important of which are maintenance of adequate international reserves, economic diversification, and domestic price stability. It now appears that in future revenue considerations will move to a secondary place and price stability, foreign trade and agricultural productivity considerations will gain in primacy.

130. An agricultural tax policy which relies almost exclusively on the rice premium remains uncertain in its impact and probably produces unplanned redistributive and reallocative effects. Given the variety of agricultural fiscal policy instruments that can be used, the most reasonable alternative to the present situation is heightened recognition of the potential usefulness of the spectrum of available instruments, followed by their effective application.

131. As far as revenue considerations are concerned, the objective should be to reduce dependence on the rice export taxes and substitute income and land taxes as a means of taxing agriculture. For the medium term, it will probably not be feasible to apply income taxation effectively in agriculture except in the case of large units. This function must, therefore, rest for some years to come on improved land taxation as discussed above. Under the system of land taxation proposed above, the land tax being a fixed cost in production would serve as a reallocative instrument in providing an incentive to land owners to use their holdings more efficiently. In particular, such a tax revision would stimulate commercial rice production as against subsistence farming; it would also stimulate the improvement of rice yields through the application of fertilizer and other intensive cultivation methods.

132. The rice premium and the rice export duty should be merged into one tax and its rate schedule reduced. Considerable public debate has already been vented over this particular issue. A surprisingly high degree of consensus has been reached among economists in favor of such a reduction, with many going so far as to call for the premium's outright abolition. Retention of the premium at a much diminished rate can permit it to serve as an effective stabilization instrument while greatly diminishing the anti-rice and anti-egalitarian biases that have characterized it in the past. The peak which rice prices have reached in the world market and the expected downward trend of prices during coming years may provide a good opportunity for reducing the rice export taxes to a low level--as occurred from 1968 to 1971.

133. In its new rate, then, the premium would serve primarily as a means of stabilizing domestic income levels and for maximizing foreign exchange earnings. This function can be reinforced by or coordinated with marketing arrangements for price support. However, the economic and administrative implications of such price stabilization or marketing schemes needs careful study.

134. In mid 1974, legislation was under consideration to create a Farmers' Aid Fund for which the revenues of the Rice Premium would be earmarked. The funds would be managed by the Ministers of Commerce, Finance, and Agriculture, and its resources could be used to stabilize prices, to subsidize agricultural inputs such as fertilizers and pesticides, and to finance land reform. Another draft law would create a Farmers' Marketing Organization which would be financed by the Aid Fund. From a fiscal point of view, these schemes would lead to further fragmentation of the central government budget -- similar to the use of land development tax proceeds now by the Ministry of Interior -- and, therefore, creation of a separate budget should be eschewed.

Fiscal Incentives for Industrial and Export Promotion

135. The major impact of fiscal policy--particularly taxation--on domestic productive activities especially the promotion of industry is through the protective effect of import duties. Tariff policies are so closely linked with the industrialization process that they cannot be evaluated in isolation from a thorough study. This report is not in a position to offer specific recommendations concerning the protective impact of the import tax system. A separate study is underway on this topic in the context of an industrial sector mission. This section is, therefore, confined to a discussion of industrial promotion and export promotion measures through specific and selective fiscal incentives.

136. Industrial Promotion. By the provisions of the Investment Promotion Act of 1972, selected enterprises are granted the following fiscal incentives: full exemption from the corporate income tax on net profits for three to eight fiscal years, beginning when the business starts operations; exemption from the payment of customs duties and business taxes on imported machinery and equipment, provided that similar machinery and equipment, approximately equal in price and quality, are not being manufactured in Thailand in sufficient quantity; exemption from export duties and business taxes of manufactured export product. The Board of Investment (BOI) is empowered to decide whether a corporation will be granted tax exemption and for how long. Once the corporation is granted this exemption, the other priviledges follow. In addition, increases in import duties on foreign competitive product and levy of surcharges on foreign competitive products can be introduced with the approval of the Cabinet and the Parliament. BOI can also recommend prohibition of certain imports for Cabinet approval.

137. In addition to these, under the 1972 Promotion legislation, the BOI was empowered, to grant one or more special rights and benefits to promoted firms that locate in one of the industrial promotion areas to be designated by the Cabinet. These special regional location incentives include:

(a) exemption of one half of corporate income tax for a period of five years (in addition to the basic 3-8 year period authorized for all promoted investments);

(b) an investment allowance comprising deduction from taxable corporate income of up to 25 percent of the cost of installation and construction of industrial infrastructure, which may be taken on any one of the first 10 years of trading and in addition to normal depreciation;

(c) deduction from taxable corporate income of twice the cost of transport, electricity and water supply;

(d) exemptions of up to 90 percent of business taxes on sales and up to 50 percent of import duties and business taxes on imported raw or essential materials up to five years from the start of trading and operations, respectively.

138. Composition and Regional Distribution of Promoted Firms. From October 1960 to December 1973, some 831 firms were issued promotion certificates by the BOI in all economic sectors, as can be observed in Table 28 below. Some 696 or about 90 percent of the firms receiving certificates actually undertook their planned investments, involving an estimated total of 34.7 billion baht over the 13-year period. By the end of 1973, 508 promoted firms or about 60 percent of those receiving promotion certificates were actually in operation.

139. In 1972 and particularly in 1973 there has been a pronounced increase in the number of firms receiving BOI promotion certificates, with 1973 being the peak year (with 115 certificates issued and 97 firms undertaking planned investments) since the introduction of the investment promotion legislation. Although the rise in investment demand was mainly responsible for this increase, this may also reflect more flexible and expeditious BOI administrative procedures in recent years.

140. About 60 percent of the firms in operation are manufacturers of textiles (20.3 percent), mineral, metal and ceramic products (17.9 percent), machine tools and electrical machinery (13.5 percent), and chemicals and chemical products (9.1 percent). The textile industry has been the single most important beneficiary of the promotion legislation followed by mineral, metal and ceramic products. The promoted firms are roughly divided between Thai-owned (318) firms and joint ventures (359), with completely foreign-owned firms (19) accounting for an insignificant share of the total number of firms promoted since 1960. 1/

1/ The statistics on promoted firms issued by the BOI are often contradictory and ambiguous. The figures cited above must be treated with caution and considered as only rough approximations.

TABLE 28: BASIC STATISTICS OF PROMOTED INVESTMENTS FROM 1960 - 1973[1/]

	1960-1962	1963-1965	1966	1967	1968	1969	1970	1971	1972	1973	Total
Total Number of Certificates	77.0	154.0	31.0	85.0	93.0	68.0	79.0	59.0	70.0	115.0	831.0
Total Number of Promoted Firms	64.0	131.0	29.0	77.0	82.0	51.0	54.0	50.0	61.0	97.0	696.0
Thai Firms	29.0	47.0	12.0	36.0	38.0	24.0	22.0	30.0	33.0	47.0	318.0
Foreign Firms	1.0	1.0	2.0	3.0	8.0	1.0	2.0	--	--	1.0	19.0
Joint Ventures	34.0	83.0	15.0	38.0	36.0	26.0	30.0	20.0	28.0	49.0	359.0
Total Registered Capital	994.3	1,274.4	512.4	953.7	615.2	1,250.7	902.1	457.0	1,007.9	1,284.0	9,251.6
Thai (฿ 000,000)	746.3	773.9	322.1	707.0	336.4	805.7	615.0	320.9	772.3	988.4	6,387.9
Foreign (฿ 000,000)	248.0	500.5	190.3	246.7	278.8	445.0	287.1	136.1	235.6	295.6	2,863.7
Total Investment (฿ 000,000)	2,593.3	3,846.7	1,714.7	4,444.1	2,561.8	4,162.2	2,726.1	779.1	4,078.7	7,764.8	34,671.4
Machinery and Equipment (฿ 000,000)	1,459.7	2,150.5	1,034.3	2,512.0	1,305.8	2,556.5	1,511.6	449.4	2,444.4	2,486.6	17,910.8
Estimated Number of Thai Employees	30,590.0	26,380.0	4,447.0	10,840.0	10,605.0	8,092.0	16,590.0.	12.079.0	19,719.0	21,640.0	160,982.0
Promoted Firms in Operation	.....180.....				73.0	80.0	56.0	43.0	36.0	40.0	508.0

1/ October 26, 1960 - December 31, 1973.

Source: Office of the Board of Investment, Research Division.

141. The regional distribution of promoted firms is given in the table below:

Table 29: Location of Promoted Firms in Operation, 1960-73.

Region	No. of Factories	Percentage
Central	432	86.4
- Bangkok/Samutprakarn	(289)	(57.8)
- Other Provinces	(143)	(18.6)
North	22	4.4
Northeast	17	3.4
South	39	5.8
	500	100.0

Source: Board of Investment, Research Division

142. Bangkok and surrounding provinces in the Central Region of Thailand accounted for nearly 90 percent of factory locations and most of the total investment undertaken under the investment promotion legislation. Most of the Thai investment in promoted firms has been attracted into metals and metal products, textiles, food processing (and cold storage), wood products, construction materials, machine tools, spare parts and engines. These are mainly small-scale, quick-yielding investments of the packaging, finishing, processing and assembly-type. They tend to have a relatively high import content and mainly supply the local market.

143. Export Incentives. Since the end of the sixties, the Thai government has given greater incentives to the export of manufactured products than before, and more attention to providing effective measures to foster industrial exports. At present (1974), the BOI offers special incentives for all investments in export-oriented manufacturing industry. In addition to this, the two most important fiscal incentives for exports are the tax rebate or "credit" scheme, and the drawback or refund of customs duties and business taxes on raw material imports used in export production. Some export firms also benefit from reduced electricity rates.

144. Tax Rebate Scheme. The purpose of the tax rebate or "credit" scheme introduced in 1971 is to promote Thai exports by making them more competitive through the "refund" of indirect taxes: excise taxes, business taxes, import duties, local municipal tax, and other levies and fees on raw materials, equipment, parts, machinery, fuels and energy used in manufacturing the exported products. These taxes embodied in the cost of the export commodities are "refunded" upon application of the exporter, government approval of the amount of rebated taxes, and after export. The refund is paid to the exporter in the form of a tax credit in lieu of cash. The exporter receives a tax certificate for the amount of the rebated taxes which can be applied

to the payment of the exporters tax liabilities (such as excise taxes, company income taxes, business taxes, excluding those levied on imports, and export duties).

145. The manufacturer must submit production cost data to the Ministry of Finance (Tax Rebate Committee) where it is reviewed and the indirect tax content of the exported commodity is determined. A refund formula is established so that the tax rebate can be set forth in terms of baht per unit of weight or measure (such as ton or yard). Once the formula is established, the value of the tax rebate can be determined by multiplying the volume or weight of the exported good by the rebate formula. Each year the Ministry of Finance establishes a baht budgetary ceiling for the amount of tax rebate that can be made available to exporters. In 1972, the allocation was 50 million baht, and in 1973 it was 100 million baht.

146. The tax rebate scheme applies only to exports of manufactured goods. It specifically excludes the export of minerals, mineral ores, agricultural and livestock products, gold, silver, precious and semi-precious stones. The tax certificates issued to approved exporters are valid for a period of three years from the effective date of issue and renewable under certain conditions for one or two additional three-year periods. 1/

147. Drawback Scheme. The present customs duty and business tax drawback scheme has its origin in the 1939 Thai Custom Legislation which permitted a rebate equal to 7/8ths of the custom duty paid on identifiable raw material imports used in exported manufactured products. 2/ In September 1971 duties paid on raw material imports used in industrial exports were reduced to 10 percent, making the effective duty paid by exporters of manufactured goods equal to 8.7 percent of the raw material import value 3/(i.e., 7/8ths of 10 percent). This duty drawback applies to both promoted and non-promoted exporting firms.

148. According to the present customs regulations (1974) a cash deposit or bank guarantee must be made upon import of the raw materials. These amounts are refunded upon export of the industrial goods that embody the equivalent of the imported raw materials. Manufacturers may also receive refund from the business tax on imported raw materials. 4/ The cumbersome administrative procedures of the drawback scheme considerably reduces its value to industrial exporters, particularly smaller firms who cannot bear the administrative costs involved. However, the administration of the scheme has been improved ssomewhat in the past few years.

1/ See Ministry of Finance Notice No. CP 1/2514 issued on December 19, 1971 for details.

2/ Customs Act No. 9 of B.E. 2482 (1939).

3/ Customs Notice No. 5/2514.

4/ Customs Notice No. 4/2514 announced April 1971.

149. Financial Incentives. The Bank of Thailand provides incentives to exporters through its special credit schemes which lowers the cost of borrowing for exporters of manufactured goods. Under the rediscount facility commercial banks which lend to manufacturers of export goods are able to rediscount promissory notes from these manufacturers at the Bank of Thailand at an interest rate of 5%. This enables commercial banks to lend to exporting firms at about 7% (189 days) which is considerably below the prevailing market rate of interest (8.5% for 180 day notes in January 1974).

150. Commercial banks wishing to use the Bank of Thailand's export credit rediscounting facility must apply for prior approval and assure the Bank of Thailand that the issuers of each type of promissory note are credit-worthy customers. Each bank is then assigned a line of credit based upon its liquidity position while its customers are provided credit lines based mainly on their financial status and their need for revolving export funds. Depending on the type of promissory note that is discounted in export transactions, the commercial banks do not accept requests for the total face value of the letters of credit, sales contract, purchase orders or warehouse receipts but cover 70-90 percent of the promissory notes.

151. The Bank of Thailand's export credit rediscount facility finances the export of agricultural, industrial, mineral and other goods. In the past four years, Bank of Thailand export credits for the manufacturing sector rose rapidly from 195.3 million baht in 1970 to 1.5 billion baht in 1973, so that they now account for about half of the total export credits under the Bank's rediscounting facilities. Nevertheless, export credits rediscounted by the Bank of Thailand comprise only a small proportion of the value of industrial exports and a very small fraction of total commercial bank credits.

152. Export Promotion Budget. A recent review of the organization and procedures of the Thai government in the field of export promotion concluded that the numerous ministries and agencies (Ministries of Industry and Commerce, the Board of Investment and the Ministry of Finance) that play an important role in export development are poorly coordinated, understaffed, under-budgeted and cumbersome. 1/ The Thai government has no export development policy or program of the kind that exists in other developing countries. Moreover, as presently organized, staffed and budgeted, the government administration is unable to provide the effective and sustained support required to implement an export promotion policy. In 1972, the total budget devoted to export promotion and development by the government (Ministry of Commerce and the relevant departments of the Ministry of Industry) amounted to 29 million baht or about 1.5 million dollars.

1/ An Export Development Plan for Thailand, Phase I and II. A report prepared for the Thai government by USOM, Bangkok (Arthur H. Luse, Jr.), March 28, 1973.

Conclusions

153. Without careful study, it is not possible to know to what extent the creditable performance of manufactured exports since 1970 is due to the Thai government's export incentives or ought to be attributed to other favorable factors affecting various manufactured goods such as strong world demand and rising prices for many processed raw materials and foodstuffs, increased domestic competition and excess capacity at home, and the rapid installation of foreign manufacturing firms and trading companies.

154. The evidence seems to indicate, however, that the Thai government's fiscal and financial incentives have contributed to the industrial export performance by increasing the profitability of manufacturing for export, offsetting somewhat the bias against exports inherent in the system of industrial protection. The ready availability of commercial export credits (particularly the access to subsidized credit through the rediscount facility for industrial exports with the Bank of Thailand) on comparatively reasonable terms has facilitated the expansion of Thailand's manufactured exports.

155. It is even more difficult to evaluate the effect of the industrial promotion schemes on the industrialization process of Thailand. Unfortunately, not only the benefits, but the costs of incentives are not clear either. Estimation of the real cost of the fiscal incentives to the government budget is beset with difficulties: Statistics on the main fiscal incentives have never been regularly or systematically collected or tabulated. Existing statistics themselves are of varying degrees of reliability and ambiguity. It is not always clear what coverage is included in the figures that are collected and conflicting estimates of tax exemptions and rebates are produced by the public administration. It is also difficult to obtain reasonably accurate estimates of how many of the firms that receive fiscal incentives would have invested and exported in the absence of the incentives and would be eligible, therefore, for the payment of the relevant duties and taxes. Fourth, further complicating the analysis is the unknown extent of corporate income and other tax evasion in the event the firms went ahead with their industrial investments and exports without the incentives; that is, to what extent investors and exporters would have paid corporate income and other taxes if they had proceeded without the incentives. Furthermore, since tax exemptions are granted for projects and not for firms, the administration of the corporation is complicated by the difficulties of apportioning the profits of a firm between the various components of its physical plant.

156. However, since the available qualitative evidence indicates that the cost of the incentives to the government budget may be substantial and is growing rapidly, it is becoming of increasing importance that the pertinent data on fiscal incentives be collected and analyzed in a systematic and comprehensive fashion by the Thai government. There is a need for a special unit to be established within the Ministry of Finance or the Board of Investment which would be charged with the responsibility of bringing together statistical information on monetary benefits conferred by the Industrial

investment and export promotion schemes, to reconcile conflicting data and establish improved data retrieval systems, and to prepare annual, or semi-annual, reports for use by the Minister of Finance and the Board of Investment. The fiscal incentives system should be kept under continuous review so that excessive benefits are scaled down over time.

157. For reasons of efficiency and fairness, the fiscal incentives system should be based on more objective criteria and procedures. There appears to be some scope for reducing fiscal incentives for promoted firms and to obtain a corresponding increase in revenues for the government budget without adversely affecting the inducement to invest. The exemption from the corporation tax seems excessive and not warranted since the businesses which would face financial difficulty in the initial years would not be taxed if they do not make profits. A limited tax allowance for investments from corporation tax liabilities might provide a better inducement for investment. It is therefore recommended that the corporate tax exemption be reviewed with a view to abolishing it or limiting its scope.

158. In view of the very rapid growth of Thailand's industrial exports, there may be little pressure on the government in the short run to strengthen the export incentive system. Such strengthening probably will be required over the next several years, particularly if there is a significant slackening in the rate of growth of manufactured exports. Any modification of the export incentive system (including tariff, tax, financial and institutional changes) should be based on a careful analysis of the manufacturing sector, its strengths and weaknesses, and the specific incentives affecting exports.

159. In order to sustain the recent rapid export expansion, Thailand's manufactured products must not only be competitive in foreign markets but also benefit from a far more serious marketing and after-sales servicing effort, particularly as the exports shift towards finished consumer goods and simple machinery and equipment. The Thai government will have to formulate a coherent export development plan supported by major changes in export procedures and reorganization of the public administration.

160. At present the greatest benefits from export incentives seem to be derived by the larger Thai firms (often joint ventures with foreign capital) which are best equipped to export their manufactured output and to take advantage of the fiscal incentives. The export incentives are not powerful enough, and easy enough, however, to overcome or offset the lack of an export capability and knowledge on the part of smaller Thai firms (usually Thai-owned). In short, the export incentive benefits are going to the foreign or partly foreign-owned firms which need them least and not to the Thai firms which need them most.

IV. STATE ENTERPRISES

161. Taken together, state enterprises in Thailand constitute a rather heterogeneous "sector" of some 80 entities engaged in all kinds of activities. It was therefore not possible to deal with each one of the firms separately in the comparatively limited time available for this report. Consequently, the most important enterprises in the transportation, fuel supply and public entities sectors have been singled out and dealt with in greater detail. The focus seems particularly warranted since these sectors include those companies which are directly concerned with provision of public services of various sorts and consequently are the prime focus among state enterprises as far as tariff policies, taxation policy and budgetary procedures are concerned. The state enterprises reviewed represent about 80 percent of the capital investment, 80 percent of revenues and 90 percent of gross fixed assets of all state enterprises in Thailand.

162. In the past, major state enterprises have not been a drain on the Government's budget; on the contrary, the total balance of fund flows has actually been in favor of the government treasury over the period 1969-1972. On the basis of 1973 results - partly estimated - the financial status of all state enterprises is as follows:

	FY1972/73 (Millions of Baht)
Current Revenues	12,816
Operating Expenses	-9,614
Debt Service	-786
Cash Surplus	2,416
Remittance to Government	-358
Government Loans	477
Government Grants	111
Borrowing	1,711
Investments	4,357

163. Enterprises in public utilities and transportation account for 92 percent of the annual investments. Their large share in the total capital formation of the state enterprise sector is further illustrated by the fact that they absorb 100 percent of the borrowing from source other than the Government and 78 percent of all such borrowing from the Government. The net internal cash generation expressed as a percentage of investments was as follows in 1973:

		Net Internal Cash Generation	Investment	Percentage
		Millions of Baht		
I.	Public Utilities	1,440	3,324	43
II.	Transportation	432	702	62
III.	Other Sectors	186	331	56
		2,058	4,357	47

The average percentage of internal cash generation is rather high because of a relative drop in the investment program in 1973; over the past four-year period (1970-1973), however, it never dropped below about 30 percent for the state enterprise sector as a whole. This is a reasonable figure quite within the range of comparable enterprises in other countries.

164. As discussed in detail in Annex D, the anticipated annual investment needs of all state enterprises are expected to triple over the next 4 years (from about 2.5 billion baht in 1972 to 7.6 billion in 1976), with investments in the power sector leading the way. In addition, serious increases in operating costs, in particular, fuel (estimated at 60 percent in 1974 and another 40 percent in 1975) are presently being experienced and are likely to occur in the future as well to a certain extent. Consequently, the prevailing favorable overall financial situation of the state enterprises is bound to deteriorate quickly in the absence of adequate remedies on the revenue side.

165. The impact of the finances of state enterprise on the government budget in future will depend on the decisions to be made in the field of tariffs. The projections of future finance needs of the enterprise sector, discussed in detail in Annex D, are made considering two variations. All expected increases in expenditure, particularly for fuel costs - have been included in both variations. In order to highlight the importance of timely tariff adjustments, however, one set of projections quantifies the revenues at tariff levels prevailing at the end of 1973; the other set incorporates the suggested tariff adjustments. Over the 1974-78 period the finance deficits of the enterprises are projected to be around ฿ 6.6 billion if tariffs are not adjusted. This would mean that net internal cash generation for the major enterprises would drop to an estimated level of about 10 percent of investments if tariffs stay at the 1973 levels.

166. With the suggested tariff adjustments, internal cash generation by these enterprises would remain at a minimum desirable level of around 25 percent to 30 percent of the investment outlays. Even with adequate tariffs, however, some state enterprises will have to raise local funds to supplement

foreign loans and credits. This applies in particular to the more capital-intensive sectors where financing of the total local component through internal cash generation would entail an increase in tariffs to unnecessary high levels. In the absence of a working domestic capital market, these funds have in the past been mainly contributed by the government through grants and, in rare cases, loans. Whether borrowing from non-government sources will be feasible in future will depend on the development of the financial market.

Pricing Policies

167. Until about two years ago Thailand was able to sustain growth with practically no attendant inflationary pressures. As a consequence frequent tariff increases were not necessary, and led to widespread expectation of stable tariff level.

168. In framing tariffs little consideration has been given in the past to the discrepancies in income between the urban (metropolitan) area and the country-side. Indeed one can say that in a number of instances the rural areas have, at least to a certain extent, subsidized the Bangkok area. For instance, until very recently, the railroad passenger tariffs on all lines within a 150 km radius of Bangkok were only 60% of the normal fare applicable in the first tariff zone. In power supply, Provincial Electricity Authority's (PEA) average tariff level is about 50% higher than the one of Metropolitan Electricity Authority (MEA), a spread which appears to be wider than is justified by the higher cost of rural electricity supply. Even within the MEA service area, Bangkok and Thonburi enjoy lowew tariffs than the more rural Nonthaburi and Jamut Prakan areas.

169. In the more recent past, some rate increases have been adopted in spite of the general reluctance to do so. Among these were increases in the water rates for the Bangkok area and very recent increases in the railroad tariffs and electricity rates. These increases, although made on an ad hoc basis rather than on the grounds of overall economic strategy, nevertheless will condition the Thai populace to the necessity of more tariff adjustments to come and thus to prepare the climate for future reasonable tariff policies.

170. In general, the boards of directors of state enterprises decide internally on the magnitude and structure of the new tariffs, if adjustments are required. The proposal is then submitted to NESDB which, after hearing various groups concerned, either rejects the proposal or recommends it to the Council of Ministers, which makes the final decision.

171. The government does not have a stated policy on what the "right" tariff level should be or what criteria should be used to determine the tariffs. Some of the Acts under which the state enterprises are chartered include the requirement that tariffs should be set at levels which cover all

cost (as defined in the Act) and permit a reasonable internal contribution to investment. This still leaves a wide range of possibilities for defining the appropriateness of tariffs.

172. The following discussion of tariffs and taxation deals mainly with public utilities, telecommunication and railroads. This is because the other state enterprises are either negligibly small or comprise "businesses" which are exposed to competition with the private sector; also by the very nature of their activities the scope for tariff adjustments for public policy is very limited. Furthermore the public utilities/telecommunication/railroad sectors provide the most important services for the public, directly affecting a large segment of the population. Their relative capital intensity also causes them to have the heaviest impact on the public finances. Accordingly, all enterprises not specifically dealt with in the following paragraphs should be treated as other business units in their respective sectors. They should be liable to corporate income taxation and should declare dividends in line with a sound financial policy.

173. State Railway of Thailand (RSR). In order to reach a modest return on investment of about 2%, which would keep the entity viable, selected tariff adjustments resulting in an overall 20% tariff increase will have to be made. Only very recently, some of the tariffs were raised and, as far as the mission understands from a newspaper clipping, the anomaly of the highly subsidized Bangkok area passenger tariffs was rescinded. The mission regards these actions as a step in the right direction.

174. Metropolitan Water Works Authority (MWWA). Among all state enterprises reviewed, MWWA is possibly in the worst financial situation. This, however, appears not only to be a tariff problem, but is at least due to an equal extent to managerial and technical difficulties (for instance a meter calibrating and replacement program which has to be carried out to decrease water losses). A comprehensive recovery program is underway with the help of consultants, and the mission has therefore no particular recommendations.

175. There is still a large discrepancy between the MWWA tariffs, which are lower, and the water tariffs in rural areas charged by various agencies. The mission did not have an opportunity to examine this question in detail, in particular since the rural water supply is carried out by Government departments from which useful cost data are not available. This problem, however, seems to open a wide field of activity and ensuing corrective measures, in particular as far as regional income distribution is concerned.

176. Power Sector. The power sector in Thailand is served by three companies, the Electricity Generating Authority of Thailand (EGAT), the Metropolitan Electricity Authority (MEA) and the Provincial Electricity Authority (PEA). EGAT is responsible for all generation and high voltage transmission throughout the country. It sells energy to MEA and to PEA for distribution and also sells directly to a few selected large industries. MEA is the distribution agency for the Bangkok area; it purchases all energy from EGAT and does not generate power. PEA is responsible for energy distribution throughout the rest of the country; in some isolated areas not interconnected with the main grid it generates its own energy.

177. In the past tariffs have been set separately for each of the three companies without much regard for the sector as a whole. Both MEA and PEA in trying to keep their tariffs as low as possible attempted to purchase the energy from EGAT at the lowest possible price. With the steep increase in demand that has prevailed, EGAT's investment program has been very heavy, about three to four times the combined investments of MEA and PEA. As a consequence, EGAT's internal cash generation fell to levels below 30% which, under the circumstances in Thailand, is below the desirable minimum.

178. PEA, whose market is much more difficult to serve than that of MEA, has barely been able to sustain a reasonable investment program despite the fact that its tariffs are on an average about 50% above MEA's level. MEA with its compact market on the other hand has been able to finance a substantial portion (about 80%) from its internal cash generation with revenues earned at very reasonable tariff levels.

179. Summarizing the power sector analysis, the following conclusions can be drawn:

(a) EGAT's tariffs appear somewhat low;

(b) PEA, despite its comparatively high tariffs, is barely in a position to meet its commitments; and

(c) MEA, in spite of reasonable tariffs, is making large profits and is able to remit substantial sums to the Government.

180. It is the mission's opinion that the relative tariff levels between the three enterprises should be modified so as to distribute the revenues from power sales more evenly, permitting each company to meet its financial requirements in a balanced manner. At the same time, consideration could be given to introducing a mechanism which permits a certain subsidization of the rural tariffs at the expense of the urban (Bangkok) tariffs. This is desirable in the light of creating better development opportunities in the rural areas and the income differential between Bangkok and the rest of the country.

181. One way of implementing these policies would be to merge the relevant authorities under one administration. This is worth studying. As an alternative, the Mission has developed a system which provides a way of rescheduling the electricity tariffs along the lines mentioned above while at the same time making the power sector as self-sufficient as possible, i.e. in the ideal case no government contribution to the sector should be needed. The detailed calculations are included in Annex D. The system is based on the following criteria:

(a) The assets of the total power sector (EGAT, MEA and PEA together) should earn a certain rate of return (in our example, 10%);

(b) EGAT's tariffs for sales to MEA and PEA should be the same and together with its revenues to other customers, should provide the pre-determined return; and

(c) MEA and PEA should sell their energy at equal tariffs which should be set at levels to earn the pre-determined rate of return on the combined assets of MEA and PEA (in our example, 10%).

These suggestions would assure that the tariffs are at the "right" level and that the rural population enjoys an "equalizing" tariff subsidy. They would not yet assure, however, that each of the companies is able to finance an equal percentage of its annual investments through internal cash generation, a necessary feature if the concept of balanced financing in the sector is to be maintained. Consequently, the internal funds in the sector have to be re-allocated in a way that the sector-internal cash generation expressed as percentage of annual investments is equal for each enterprise. Consequently, the following additional actions have to be taken:

(a) Calculation of the percentage of investment financing through internal cash generation for the whole sector;

(b) Application of this percentage for each enterprise separately; and

(c) Re-arrangement of the sector-internally generated funds through "equalization payments" in a way that each enterprise receives the equal share.

182. The system as outlined above and in more detail in Annex D would require a strong supervising agency which would be charged with supervising the tariff making and revenue rescheduling process. A good candidate for these functions would be NESDB which already at present exerts decisive power in the important economic decisions of the sector (tariffs, investment budget, etc.).

183. The mission has no strong views as to how the equalization payments should be administered. One possibility could be to treat them similar to the remittance-to-Government transfers, with the only exception that they

would constitute funds earmarked for the power sector. Another way could conceivably be to add appropriate, clearly identifiable surcharges to EGAT's tariffs which would be higher in the case of sales to MEA than to PEA.

Taxation of State Enterprises

184. Concerning income taxation, the original idea in Thailand was to treat the state enterprise sector as such no different than the private sector, i.e. income tax exemption for state enterprises on principle was not contemplated. This did not apply to those entities which serve the public with, what are considered, basic necessities (water, power).

185. In the course of time a number of enterprises were created by special act or royal decree. They were either newly established for particular purposes, such as the rubber plantation organization, or they consisted of part of certain government departments for which it was considered desirable to endow them with greater independence (for instance EGAT, TOT, etc.). Both kinds of enterprises, particularly the former government departments, were exempt from paying corporate income tax. This, in effect, only for the simple reason that as a government department they were not liable to taxes either. As a consequence, today's situation is such that enterprises created by special act or decree are income tax exempt whereas those established by civil code or cabinet resolution are generally tax liable.

186. The facts as described above led to the strange situation that the legal instrument rather than the activity determines whether a state enterprise is liable to income taxation. This is an undesirable situation. In principle, all state enterprises should be subject to the corporation tax. The implications of this on the financial structure of the enterprises should be studied in conjunction with the problem of transfers between the central government budget and the enterprise accounts.

Remittances to the Government

187. Each state enterprise created by special act or royal decree is required by law (normally included in the decree) to transfer its total annual net profit to the Government treasury; the Government in turn is obliged to cover any operational deficit which might occur. This requirement is equivalent to a 100% dividend payment with a built-in obligation on the part of the government to cover cash deficits (not business deficits since depreciation and allocations to reserves are excluded).

188. In effect, this stipulation has never been applied in the past because it was recognized that it would deprive the companies even of a minimum of financial independence. The practice which was gradually adopted is that the Government (Budget Bureau) assesses the financial capability of a company and determines the percentage of remittance. Very often it uses as a guideline the corporate income tax schedule for assessing the level of remittance. This procedure has led in some quarters to the erroneous opinion that the Government remittance is a substitute for the corporate income tax.

189. The level of the remittance percentage appears in some cases to be negotiated between the Government and the management of a company whereby the outcome is to a certain extent influenced by the relative strength of the negotiating partners. Furthermore fiscal consideration as more or less "dictated" by the Budget Bureau seems to be more relevant for determining the remittance level than business and financial necessities of the various state enterprises. This is an undesiable situation since it does not pay sufficient attention to the requirements of the various companies and sectors and should be corrected by instituting a coordination system whereby the needs and the financing sources of the enterprises are determined within the context of annual finarcial programs for the total public sector.

V. REGIONAL DEVELOPMENT AND LOCAL FINANCE

190. The trends and patterns of development at the regional level have not been satisfactory. Disparities in growth and development among the regions have persisted and have, if anything, become even more pronounced. In 1960, the year before the beginning of the First National Economic Development Plan, Northeast Thailand, with over a third of total land area and population, accounted for less than 20 percent of GDP, while the Central Plain, with 20 percent of total land area and less than a third of total population, generated almost half (49%) of the total GDP. In spite of government planning efforts, the share in income and production of the Northeast dropped to 15 percent, while that of the Central Plain increased to over 58 percent. A similar decline also took place in the Northern and Southern planning areas, where the share in GDP fell from 15 percent and 16 percent, respectively, to 14 percent and 12 percent respectively.

Local Government Expenditure

191. Allocation of public development outlays in recent years has not helped significantly to close the regional income differences. Available fiscal data does not permit one to estimate the regional distribution of public expenditures. However, the regional product estimates - in which the value added figures for social services and public utilities can be taken as a proxy for public expenditures in these categories - the regional disbursement figures compiled by the treasury, and the partial indicators of physical outputs in the public sector indicate that per capita use of public resources in the Central region has been significantly higher than in the other regions (for details, see Annex E).

192. The regional planning efforts of the National Economic Social Development Board (NESDB) have met with very limited success. The failure of these plans is primarily rooted in the institutional arrangements which circumscribe their implementation. In particular, NESDB has been unsuccessful in channelling the investment expenditures of the departments of the central ministries into scheduled regional projects or regional allocations. Each department tends to operate independently of the agency and makes unilateral regional investment decisions. This independent action by the departments is possible because the planning function carried out by NESDB is not integrated into the actual budgeting procedure of the government.

193. Local governments and local finances have not played significant role in the geographical distribution of the public services. Both from an administrative and a fiscal standpoint the local governments have remained tied to the central government. Dominance by the national government has been ensured, first because the Ministry of Interior, through the Department of Local Administration (DOLA) directly controls the administration of local government jurisdictions in the Kingdom. Provincial governors, appointed

by the Ministry of Interior, are delegated broad supervisory powers over local jurisdiction in the provinces. Second, the revenue sources reserved for the local government sector are inadequate to finance minimal functional expenditures; hence, local units are dependent upon the central government for grants and subsidies to narrow the gap between tax revenues and the demand for public services. Funds are provided by several departments of the central ministries, but the bulk of the assistance is channelled through DOLA. In recent years, these subsidies and grants have annually accounted for about one-third of total local government revenues, the lion's share of which has gone for needed local infrastructure.

194. The subordinate role of the local government sector is illustrated by the fact that of total public outlays of ฿ 33.6 billion in 1972, local government expenditures were just over 1.5 billion. This represents a mere 4.5 percent of total outlays. According to the law, local governments are required to perform certain duties; however, the range of services actually provided by them is much less than called for in the legislation. Municipalities, for example, are required to maintain roads; to collect refuse; to provide medical services, local elementary education, clean water, electrical works, and child and maternal welfare. In addition, they are also empowered to provide hospitals, public utilities, vocational schools, parks, sports facilities, trade centers, and cemeteries and crematories. But in practice most of the public activities listed are either wholly or substantially supported by the central government.

195. The departments of the twelve central ministries incur expenditures and extend services directly through their network of provincial and district sub-units; grants and subsidies are also given to the local governments by DOLA to finance local projects. Generally, road and highway construction, law enforcement and police security, public transportation and communication, and electricity generation are the responsibility of the departments or established state enterprises. Subsidies, grants and technical assistance are given to local governments for the provision of education, water supply, and health care. 1/ Structural rigidities imposed by the central government through DOLA collectively act as a significant restraint on the development of the local government sector.

Local Government Revenues

196. Another important constraint retarding the growth of the local government sector is the limited taxation power at the disposal of local units. The municipalities and the sanitary districts have almost identical tax sources. They are authorized to levy a house and rent tax, land development tax, signboard tax, and an animal slaughter tax for revenues. In addition, local jurisdictions are legally authorized to add a surcharge of up to 10 percent to certain national taxes. These taxes are the business tax, the liquor tax, the non-alcoholic beverage tax, and the entertainment duty; they are collected by local representatives of the Revenue and Excise Departments of the Ministry of Finance. Normally, the full 10 percent

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1/ In some cities, a state enterprise offers the water service.

surcharge is applied. Receipts from the 10 percent surcharge (as well as the basic tax) are forwarded to Bangkok, which they returns to the local government bodies the surcharge proceeds minus a 5 percent fee for administrative costs. Certain other taxes, classified as shared taxes, are levied by the Royal Thai Government, and all or a portion of the receipts are distributed to local jurisdictions. For municipalities and the sanitary districts, the shared taxes are the rice export duty and the road vehicle tax. The changwat administration organization, whose budget encomposses all territory not in the jurisdiction of municipalities and sanitary districts in the province, has access to the same taxes as the former urban government types, except for the house and rent tax, and the rice export duty.

197. For the data contained in Table 30 on the primary revenue sources of the local governments, it is noted that the locally levied taxes constitute only about one-fifth of local government income. The relatively low yield of these taxes is attributable to basic defects in the two major taxes, the land development tax and the house rent tax. The former suffers from an inordinate number of exceptions and deductions while the latter appears to be effectively evaded by city and town residents. These have already been discussed above under the taxation policy.

Table 30: TOTAL REVENUES FOR LOCAL GOVERNMENTS BY REVENUES SOURCE FOR FISCAL YEAR 1971

Revenue Sources	Municip-alities	Sanitary Districts	Changwat Admin. Organi-zations	Total for all local Governments
Total Local Revenues in millions of Baht	฿ 917.9	฿ 178.6	฿ 734.9	฿ 1831.4
Percentage Total Local Revenues	100.0	100.0	100.0	100.0
Total Tax Revenues	79.5	80.1	34.3	61.4
Local Levied	21.4	27.7	19.3	21.2
Surcharge Taxes	43.0	10.8	5.3	24.7
Shared Taxes	15.1	41.6	9.7	15.5
Other Revenue Sources	20.5	19.9	65.7	38.6
RTG Transfers	3.7	6.5	62.7	27.6

Source: Figures obtained from unpublished data supplied by the Bank of Thailand. Figures for RTG subsidies are low compared to information contained in the public sector account tables in Annex B.

198. Surcharge taxes, which were recorded as being ฿ 452.4 million in 1971, are the local governments' most lucrative revenue source. The preponderant share in this total, over 78 percent, came from business tax surcharges. Shared taxes contributed a little over 15 percent to total revenues; all but three percent of the total came from the vehicle tax. Subsidies from the RTG amounted to almost 28 percent of local governments' total revenues in fiscal year 1971. Data obtained by the Bank of Thailand from questionnaires furnished by the local units were found to be incomplete. In fact, the central government directly contributes more on the order of 30 percent to 35 percent of total local revenues.

199. A review of the revenue sources given in Table 30 taken together with a review of the specific revenue codes that affect local governments, suggest that the current local tax structure is unduly rigid and wholly inadequate to meet the obligations of the local governments. The inadequacy of revenues arises from the limited taxation powers of local governments and their limited ability to generate non-tax revenues from local sources. The system is an inflexible one, as all local governments must adhere to the revenue codes imposed by the central government, and are prohibited from cultivating new tax sources or exceeding the taxing perimeters established in law. The result is that local governments are starved for new revenues to meet the growing demands of urban as well as rural residents and are forced to turn to the central government for these funds. If the central departments do not respond, in many cases, the local services suffer.

200. While the local government sector as a whole has insufficient resources to fulfill its statutory obligations, within the sector itself, there are wide disparities in the fiscal capacity of local jurisdictions. Municipalities, for example, had total tax revenues of 129 baht per capita in 1972, in contrast to an estimated 40 baht for sanitary districts and 8 baht for changwat administrative organizations (CAOs). The wide range in these figures results directly from the differences in the tax bases of the three units, i.e., the greater property wealth and commerce of urban centers compared with the semi-rural and rural areas. Although central government grants and subsidies favor non-urban areas in absolute terms, this assistance did little to narrow the variation (see Table E-4, Annex E). In 1972, after taking government transfers into account, total revenues per capita were 233 baht for municipalities, 52 baht for sanitary districts, and 16 baht for CAOs.

201. Serious disparities also emerge if local government revenues are contrasted regionally rather than by administrative unit. Estimates of total tax collections of all local jurisdictions situated in the depressed Northern and Northeastern regions show that they each have approximately one-seventh the revenue per capita of the Central region. Moreover, the gap remains sizeable after government assistance; total revenue per capita for the Central region was three times that of the Northeastern sector and four times that of the Northern area. As stated earlier, improverishment of the local government units of the regions is to be expected in light of the extremely low GDP of these areas. This impoverishment is also reflected in the provision of

public services as evidenced by statistics on outlays per capita for education, health and water. This evidence suggests that in much of the country, local governments are economically unable to provide from their resources a reasonable range of local public services. If the national objective is to provide minimum levels of health, education and other services to all citizens and local authorities are to be used to provide some of these services, the central government must extend massive grants to the local governments located in the poorer regions to offset differences in their economic capacities.

Local Government Taxes

202. Additional insight into the local government sector is gained by a more detailed examination of the local tax sources identified in Table 30. As noted, combined total tax revenues constitute a little over 60 percent of the total revenue of the local government sector. For convenience the individual taxes are discussed under three classifications -- local levies, surcharges, and shared taxes.

203. Local Levied Taxes. The House and Rent Tax (HRT) is the largest revenue source amongst the taxes levied by the municipalities and the sanitary districts. Its share of total municipal tax revenues has been a stable 18 percent or 19 percent over the last five years. In the case of the sanitary districts the percentage has been less constant, fluctuating between 15 percent (1971) and 21 percent (1972) in recent years, but averaging about 19 percent. Revenue growth from the HRT has evidently kept pace or slightly exceeded the rate of growth of the overall economy. During the period 1969 to 1972, income from the HRT rose 50 percent for the sanitary districts, reaching ฿ 28.5 million in the latter year. Data are not available for 1972 in the case of municipalities, but between 1968 and 1971, revenue jumped by ฿ 35 million, or 36 percent. Incremental growth of the Thai economy, in comparison, averaged around 9.5 percent over the years covered.

204. The contribution of the land development tax (LDT) to the total revenues of the three forms of local government varies between units, but in general it is not large. In relative terms, the LDT is more important to the CAOs as a revenue source than to the municipalities and sanitary districts. In 1971 it accounted for approximately 19 percent of the total income of the CAO's, but only 3 percent and 11 percent of total municipal and sanitary district revenues, respectively. This is to be expected though, since most of the rural and agricultural area lies within the jurisdictional boundaries of the CAOs. For the kingdom as a whole, the LDT made up 11 percent of all local government revenues. These percentages are representative of the yield of this tax to local governments in recent years, but year-to-year changes can be expected, principally because the distribution is so heavily influenced by government subsidies.

205. Regardless of its relative importance to local governments, tax revenue yields from the LDT are extremely low, totalling ฿ 213.0 million in 1971. For the country as a whole, this corresponds to an average tax per household of 32 baht (US$1.62). When considered on a per capita basis, the amount falls to a mere 6 baht (US$0.28) per person. These figures correctly demonstrate the point that on a household or percapita basis only a minimal burden is born by landowners in relation to their money income. While data are not available to measure the burden of land taxes in relation to their money income an estimate was made using gross domestic product per capita. According to this measure, the average tax burden per capita for the country was 0.012 percent in 1971.

206. To complete the discussion of locally controlled tax revenues, brief consideration is given to the two relatively minor income sources, the slaughter and signboard tax. Combined revenue receipts for all local governments in 1971 totalled ฿ 51.7 million, signboard revenues were ฿ 31.2 million, and slaughter taxes amounted to ฿ 20.5 million. These comprises roughly 3 percent of total tax revenues collected by local governments. Municipalities and sanitary districts received the bulk of these funds. In 1971, proceeds from the signboard tax constituted 3.5 percent, 2.2 percent and 0.4 percent of total revenue of the municipalities, sanitary districts, and CAOs, respectively. For the same year the revenue yield of the animal slaughter tax represented 1.8 percent, 4.2 percent, and 0.6 percent for the municipalities, sanitary districts, and CAOs respectively. The low tax yield of the two taxes can be attributed to the narrow tax bases.

207. Surcharge Taxes. In 1961 the Royal Thai Government switched from a business tax levied at the retail level to a business tax placed primarily at the import and manufacturing levels. Since local governments were levying a 10 percent surcharge on business tax proceeds the shift in tax policy meant a loss of local revenues. To offset this income loss, the central government imposed a corresponding 10 percent surcharge at the import and production points. The Revenue Department of the MOF actually collects the surcharge and forwards the receipts to DOLA for distribution to the three sets of local government units. Payments to the local public authorities were based upon the proportion of business tax received by each type in 1960.

208. The surcharge on the business tax is the largest single source of tax revenue for local governments. According to 1971 data, the most recent available, 31.5 percent of the total tax revenues of the local government sector came from this source. Due to the allocation system of the 10 percent surtax, municipalities were the major recipients of the revenues, receiving ฿ 315.3

million of the total of ฿ 354.3 million, or nearly 89 percent of the total. 1/ In 1969 a little over 48 percent of the budgets of municipalities came from this source, but in the past two years the percentage has fallen slightly to 41 percent. For the larger municipalities such as Bangkok and Thonburi, however, this remains the chief revenue source, accounting for almost one-half of total tax revenues. In contrast, the surcharge contributed only 9 percent and 11 percent respectively to the total revenues of the sanitary districts and CAOs.

209. Local government revenues from the liquor tax and license arise from a 10 percent surcharge placed on the excise payments and duty the license fees of these distilleries. The surcharge is collected directly from the distilleries by the Excise Department of the MOF, and then turned over to DOLA for distribution to the local governments. Prior to October 1972, only jurisdictions where plants were located received surcharge income. According to DOLA officials, all local governments (municipalities, CAOs and sanitary districts) now receive income from the surcharge fund in relation to the jurisdiction's share of the Kingdom's population.

210. Data available from the Bank of Thailand combines the revenue collections of the liquor tax and the non-alcoholic beverage tax. Surcharge receipts have risen gradually with the increased consumption of beverages of all types, but their share of total taxes has remained relatively unchanged, in spite of the absolute increases. In 1969 the two taxes yielded ฿ 58 million for local governments, or 7 percent of total tax revenues; while in 1971 the yield had growth to ฿ 88 million, the percentage rose only slightly, to 7.8 percent. Since plant location determined the distribution of tax receipts in this period, the lion's share of the revenues accrued to the municipalities. In 1971 approximately two-thirds of the receipts flowed to these governmental units.

211. A 10 percent surcharge on the entertainment duty is collected by the Revenue Department on behalf of the local governments. The earmarked revenues are allocated on the basis of the share of the duty received from each of the local jurisdictions. Total income is extremely small from this tax, amounting to less than ฿ 10 million in 1971. Moreover, its contribution to total tax revenues is negligible, less than 1% for all local governments taken together.

1/ Officials of DOLA report that, starting in 1974, business surcharge tax (BST) revenues are to be allocated to the local governments on the basic of population. This change will bankrupt the municipalities of the kingdom. Based on the population figures contained in Table 6.1 of the Annex, municipal BST revenues would plumme from ฿ 315.5 million to ฿ 54.9 million in 1971, if the stated per capita measure were followed in that year. CAOs, on the other hand, would experience an extraordinary 692 percent increase. It is difficult to believe DOLA would strictly adhere to such a per capita allocation formula.

212. Shared Taxes. The export tax on rice is levied by the Customs Department of the national government on export of white rice and parboiled rice at a rate of 1.00 baht per 100 kilograms. For paddy rice, broken rice and bran, the tax rate is 0.50 baht per 100 kilograms. The proceeds are transferred to DOLA in the Ministry of Interior for distribution to the municipalities and sanitary districts in the kingdom. One-half of the total receipts from this levy is allocated among the CAOs and the sanitary governments, on the basis of population; the other half to municipalities, to be distributed in a like manner. Income from this tax fluctuates with the level of rice exports. In general, the shared revenues represent less than 1% of total tax revenues of local governments and can be considered insignificant as a tax resource.

213. The vehicle tax is administered by the central government's Police Department through offices located in each provincial capital. In October 1973, the police department at the changwat level was given the responsibility for the collection and distribution of this tax. Prior to that time, all receipts were forwarded to DOLA for allocation. Currently the revenues from the vehicle tax is divided among the three sets of local government units within the province as follows: 50% of the total proceeds go to the municipalities and are divided equally amongst all the municipalities within the province, 25% of the total receipts are split evenly among the sanitary districts of the area, and 25% are given over to the CAOs.

214. Next to the business surcharge tax, the vehicle tax is the largest revenue source of local governments. Based on 1971 income figures it provided ฿ 274.7 million to the consolidated tax revenues of the local government sector. This corresponds to nearly one-fourth of all such revenues. In 1974 the share is forecast to jump abruptly, owing to the sharp increase in rates which went into effect in February of that year.

215. Municipalities are heavily dependent upon this budget item since it represented nearly one-half of all their tax revenues in 1971. CAOs, while less dependent, receive 28% of their tax income from the vehicle tax, and municipalities receive a sizeable portion, 18.4%. Given this distributional formula, the municipalities will gain the most from the new rates.

Suggestions for Improving Local Finance

216. The foregoing discussion has identified two major deficiencies in the area of local government finance. Firstly, it is clear that the local government revenue is presently virtually incensequential, contributing a mere 6% to national tax revenues. Second, the present patchwork of local revenue sources provided to the local jurisdictions is inadequate to finance the obligatory functions required of them in the enabling acts. Major changes are indicated in the financing of local governments; the following broad recommendations are offered, predicated on the assumption that the establishment of a viable local government sector is a primary objective of the Thai Government.

217. There is no simple way of determining the degree of desirable budget decentralization in the Thai economy. As indicated above and described in more detail in Annex E, the system of allocating the proceeds of surcharge taxes and share taxes has lost its earlier rationale - of questionable merit - which was based primarily locality in which the taxed transactions took place. A review of the present allocation formulae clearly indicates that they are not consistent with any recognizable public finance objective. With the bulk of revenues for revenue-sharing emanating from commodity taxes at the manufacturing, import and export levels, there is no easy way of estimating the incidence of these taxes among the areas of local government jurisdiction. Even if this were feasible, it would not provide a necessarily desirable system of allocating public funds. Any system of allocation has to be based on normative judgements. However, it can be agreed that the system of allocation should look at the total tax revenue structure of the local governments and take into consideration (a) the needs of the regional units, (b) the objective of securing a minimum level of funds to promote local self-government, and (c) the need to leave room for flexibility in central government action. It is suggested that the essentials of the present system - local taxes, earmarked taxes and transfers - in inter-governmental transactions be kept with the modifications outlined below.

218. The need to reform the land development tax and the house rent tax under a general property tax system was discussed above as part of the total taxation policy of the country. Given the present state of local development in Thailand, it was recommended that the administration of the property tax be centralized. This move should be coupled with plowing the whole or a very high percent of the proceeds of these taxes back to the local jurisdictions from which they were collected. With the improvements suggested in the previous section, this may provide local governments with increased revenues, which will also bear a correlation to the demand for urban and rural public services linked to real properties.

219. The three locally levied taxes - the slaughter tax, signboard tax and gambling tax - should remain under the jurisdiction of local governments. It is recommended that the local units be given more discretionary authority in the setting of rates on these taxes. It is also recommended that the adminstration of business taxes on a selected list of services be transferred to local administration gradually over time.

220. The broad principle concerning the allocation of the surtaxes and share taxes among the regions should be based on some simple and objective formulae which would attach a heavy weight to the population distribution. The allocation among the various types of local administration - provincial governments, municipalities and sanitary districts - should be determined after study of the relative needs and capacities of these units, again giving weight to the population factor.

221. The expected outturn from taxes collected by or on behalf of the local governments plus revenue sharing from national taxes will provide the local administration with at least a minimum tax revenue package on the basis

of which they can plan their activities. However, depending on the characteristics of the regions or areas, additional funds will be needed for local expenditures. The question of whether these additional expenditures should be undertaken directly out of the central government outlays or through transfers to the local administration budgets will depend on the nature of the particular case. The programming of these transfers or expenditures to augment local government outlays will be the function of the central government's budgeting exercise.

VI. ORGANIZATION AND ADMINISTRATION

222. The public sector of Thailand consists of the Royal Thai Government (RTG), four types of local government, a number of agencies called "state enterprises" and decentralized agencies established to deliver specific public services in accordance with the policies of the government. An important characteristic of the public sector of Thailand is the strong concentration of power in the RTG. All other public sector agencies are, to a large degree, the instruments of the central government for implementing its policies. This, as will be argued below, has hindered the development of local initiative and the evolution of decentralized poles of regional growth.

223. On the other hand, while the public sector is highly centralized around the RTG, the latter itself is a rather diffuse organizational unit, particularly as regards fiscal administration. The major responsibilities for fiscal management are dispersed among a number of ministries and agencies, and, even within the ministries, individual departments possess significant autonomy in their activities. This state of affairs aggravates the problems of coordination, programming, and even implementation of public expenditures and finances. In this section, the issues relating to planning and budgeting functions are first reviewed, then the problems of tax adminsitration are discussed, and finally, the question of debt management is examined.

Planning and Budgeting

224. Major responsibilities for fiscal management are distributed mainly among the offices of the Ministry of Finance, the NESDB and the Budget Bureau in Prime Minister's Office and the Bank of Thailand. The chief function of the Ministry of Finance consists of determining taxation policy and administering the collection of revenues. The Finance Ministry also plays an important role in the management of the public debt, sharing this responsibility with the Bank of Thailand in the case of domestic borrowing and with the Foreign Loan Contracting Sub-Committee of the NESDB in the case of borroing from foreign sources, although the ultimate authority rests in the cabinet.

225. The responsibility of resource allocation is spread over the Budget Bureau, the Department of Technical and Economic Cooperation, the Foreign Loan Sub-Committee of the National Economic and Social Development Board and the Civil Service Commission. All three agencies are in the Prime Minister's Office, but there seems to be little coordination of work among them. The structure of the central government budget is also a factor which makes the resource allocation inefficient, given the fact that the three related agencies do not coordinate their work. The Budget Bureau is only responsible for the allocation of budgetary resources, and this provenance excludes various funds available to the central government, particularly foreign grants and foreign loans. The allocation of foreign grants is the responsibility of the Department of Technical and Economic Cooperation. The administration and

control of foreign borrowings by all public sector agencies, including local governments and state enterprises, are the responsibilities of the Foreign Loan Contracting Sub-Committee of the NESDB and the Fiscal Policy Office of the Ministry of Finance.

226. The "budget" of the Royal Thai Government consists of the receipt budget and the payment budget. The receipt budget consists of the estimates of the size of budgetary resources available comprising current revenue, domestic borrowing, new coin issue, and drawings on cash balances available. The ceiling on domestic borrowings is determined through discussions among the Ministry of Finance, Bank of Thailand and the Budget Bureau. 1/ The receipt budget sets the ceiling on the global size of "payment budget." Therefore, the Budget Bureau submits the receipt budget to the Cabinet for approval before it undertakes budget appropriation works.

227. The "budgetary payments" are the payments to be financed by budgetary sources. This budget includes repayment of foreign debt and domestic debt, and certain types of tax refunds. Since it does not include expenditures financed by foreign grants/loans, 2/ actual central government expenditure can differ considerably from budgetary expenditure adjusted for debt repayments and tax refunds. Figures in recent fiscal years compare as follows:

1/ The present Budget Procedure Act limits net domestic borrowing to 20% of the total budgetary payments net of debt repayments. The annual ceiling is determined within this limit through discussions among the Bank of Thailand, the Ministry of Finance, and the Budget Bureau.

2/ Except for the temporary financing of foreign-financed expenditures out of budgetary funds, which would be later reimbursed as a budgetary revenues.

Central Government Budgetary Expenditure and Actual Expenditure /1
(Billions of Baht)

	(1) Actual Expenditure Including Expenditure Foreign Sources /2	(2) Total Budgetary Payments	(3) Debt Repayments	(4) Budgetary Expenditure (2) - (3)	(5) (1) - (4)	(6) (4) as % Of (1)
FY1965/66	14.6	13.5	0.1	13.3	1.2	92
FY1966/67	17.7	17.5	1.0	16.5	1.1	93
FY1967/68	20.8	19.5	0.1	19.4	1.5	93
FY1968/69	23.2	22.1	0.6	21.5	1.7	93
FY1969/70	24.9	23.8	0.2	23.6	1.3	95
FY1970/71	28.4	27.7	0.6	27.0	1.4	95
FY1971/72	30.4	30.4	1.0	29.4	1.0	97

/1 All figures in this table are on a cash basis. Therefore, the "budgetary payments" figures in column (2) differ from those published by the Budget Bureau, which are on a closed account basis.

/2 Net of debt repayments and tax refunds.

Source: Bank of Thailand.

Budgetary requests start with the smallest spending units of the central government and the agencies outside the Royal Thai Government. Decentralized agencies such as government schools and hospitals submit their budget requests to the central government agencies which supervise them; these are departments or divisions of the central government. Local governments which desire financial assistance from the central government submit their requests either to the DOLA or other agencies related to the projects/programs in question. State enterprises which ask for central government assistance may submit their budget requests to the Budget Bureau directly or to other central government agencies which supervise the respective state enterprises. Within the central government, budget requests are prepared at the divisional level or at lower levels.

228. All requests are consolidated into departmental requests by the Finance Divisions in individual departments, which submit them to the Office of the Under-Secretary. Departmental requests are consolidated into ministerial requests for submission to the Budget Bureau. The Budget Bureau then determines the allocation of the budgetary resources on the basis of:

(i) the global ceiling on payments, which is the size of the "receipt budget"; and

(ii) the relative priorities of the projects or programs in the ministerial budget requests.

229. In principle, the allocation of resources for development projects or programs should be based on the relative priorities spelled out in the Annual Plan, which the National Economic and Social Development Board prepares in line with the Five-Year Development Plan; hence, the budget appropriation ought to be a joint responsibility of the Budget Bureau and the National Economic and Social Development Board. However, in practice the relative priorities of projects or programs are determined by the Budget Bureau alone owing to the lack of coordination between the two agencies.

230. Although expenditures financed with foreign grants/foreign loans are outside the budget, the programs or projects to be financed by these resources could be affected by the budget. In most cases such programs or projects require local counterpart funds, which have to come from the budget. Inadequate appropriations of counterpart funds could lead to delays in foreign financial programs or projects.

231. State enterprises are subject to specific budget regulations. These regulations ensure that the government has the sole power of approving or rejecting the enterprises' investment budgets and also provide the government with a direct influence on the financing plans for such budgets. The annual investment budget proposals of the state enterprises are submitted, through the ministries to which they are related, to NESDB's executive committee. The budget is accompanied by the estimated expenditures of the full investment program, and by the operational budget for information. A few of the state enterprises submit their budgets to the cabinet directly. In these cases, copies are sent to NESDB and the Budget Bureau for evaluation and comment. In NESDB, the subcommittee on state enterprises (which consists of the representatives of NESDB, the Budget Bureau, the Ministry of Finance, the Audit Council, and the Ministry concerned) evaluates these budgets and submits them to the executive committee of the NESDB, which in turn passes them on to the cabinet for approval after adding its own evaluation.

232. The logic of the arrangements outlined above provides the NESDB with a pivotal role in coordinating the planning, programming, and the budgeting activities of the public sector. Particularly in recent years, however, the NESDB has failed to perform this function, mainly because of the erosion of its effectiveness, but also partly due to the estrangement of the planning exercise from fiscally meaningful categories. This situation has arisen out of an approach to planning which, on the one hand excludes the planning for public expenditures that are not "developmental," (so that the planned expenditures have recently accounted for little more than one third of the total government budget) and, on the other hand, does not provide a macro-framework for public sector activities except in the very

general terms of national accounting concepts. Hence, no formal mechanism exists for explicit consideration of the total resources and their use in the public sector, nor for the consideration of the allocation of these resources amongst functional or geographical areas.

233. Improvements in the planning and budgeting practices will depend, fundamentally, on devising processes for decision-making that will facilitate the implementation of the necessary functions, that is the policy function which is concerned mainly with the level of expenditures and their financing, and the programming function - determining the allocation of funds and the development and coordination of expenditure projects. As things are, the Budget Bureau seems to be dominating matters with annual budgets, sharing the first function mainly with the Ministry of Finance and the Bank of Thailand and the second function with the NESDB. This has resulted in reducing the effectiveness of a longer-term perspective in programming. Nor is the allocation of responsibilities for demand management and short-term fiscal policy clearly defined.

234. So long as efficient modes of coordination, are achieved, the organizational questions would be secondary - and would vary from one country to another. The important improvements needed in Thailand can be summed up as follows:

(a) Planning should include the analysis of public sector finances in terms which would relate explicitly to budgetary fiscal concepts;

(b) Comprehensive annual programs should be prepared by the NESDB with the participation of concerned agencies covering all the activities of the central government, the local government and the state enterprises and submitted to the cabinet for approval;

(c) The unity of the central government budget should not be violated by earmarking separate funds for the Ministry of Interior or the Ministry of Commerce;

(d) Foreign grants and loans should be included in the budget so that the budgeting agency would consider an overall allocation of financial resources for the government;

(e) The supplementary budget should be explicitly used as an instrument for adjusting the government's fiscal demand management, and expenditure procedures should be reviewed and adapted to the inflationary environment;

(f) The link between planning and budgeting should be reinforced by strengthening the public finance capability of the NESDB and improving its cooperation with other agencies of the public sector.

235. Although these functions are not necessarily best performed under only one pattern organizational structure, there seems to be a case for a

reorganization of current administrative arrangements. The signs are that Thailand will, under the new constitution being drafted, move towards a parliamentary system. This may increase the problems of coordination between the revenue and the expenditure functions of budgeting. In view of this, one possible alternative to the present organization would be to enlarge the powers of the Ministry of Finance by bringing the Budget Bureau under it and thus centralizing the formulation of annual fiscal policy and coordinating it with demand management. On the other hand, strengthening the Planning Board under the Prime Minister can provide the necessary long-term perspective for the programming function.

Budgeting for Local Development

236. There are three budgets in Thailand which can be called "local government budgets." By this is meant that the budgets are prepared and passed by locally constituted bodies which have the powers under laws to levy taxes and to expend funds. There are the CAO budget, the municipal and the sanitary district budget. 1/ Usually the budget is for a one year period, beginning October 1 and ending on September 30 the next year. The budgetary process for local governments involves three successive stages: budgetary preparation, legislative approval, and execution of the budget. Unmistakably the entire budget process from formation to execution is under the direct supervision and tutelage of the Ministry of Interior through its agent, the Department of Local Administration.

237. Every budget is prepared by its executive officer. In the case of the CAO this would be the governor, for municipalities it is the municipal council. The actual framing of local budgets must comply with the directives and rules laid down by DOLA, and in general, the regulations are standardized for the CAO, municipality and the sanitary district. Principally they require the local governments to: (i) frame the budget expenditure appropriations on a line-item basis, specifying in detail the objects for which the money is to be spent; (ii) to divide the local budget into regular or current expenditures and special or capital expenditures; (iii) to draft a current budget that is within the specified 95% rule.

238. The ceiling on the current year's budget is 95% of a three-year average of previous revenues plus ordinary RTG grants (it excludes special and specific grants). Under normal economic conditions, current revenue can be expected to exceed the three-year average, which means a surplus larger than the programmed 5% tends to occur. Such a practice is extremely conservative and retards the development of social programs and projects of the faster growing cities. A further penalty is imposed since the cities must transfer any surplus in the current year to DOLA. These monies are retained in a reserve fund (one for each form of local government) from which local government jurisdictions can borrow. Local governments have

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1/ Since the discussion of local public finance in Thailand boils down to an examination of the fiscal affairs of the self-governments, CAOs, municipalities and sanitary districts, the term "local governments" is used in the text to denote the sum of activities of these three jurisdictions.

not turned to these funds for loans in recent years, however, because of the bureaucratic procedures and the terms of repayment. From DOLA's standpoint, the budget process is simplified and facilitated by the 95% rule, but overall, its employemtn has a deleterious effect on the local government sector, and alternatives need to be explored.

239. The completed draft budget is transmitted to the appropriate elected legislative body by the executive office for their consideration and passage. The elected assembly has two alternatives: to affirm the draft budget as presented, or to reject the budget as submitted. If the latter course is taken, the assembly can request that the executive office reconsider specific items in the draft budget. In the case of the municipalities, if the municipal council refuses to yield on the issues raised in the review, the council is normally obliged to resign. But under the Ministry of Interior's August 1973 Directive, the governor of the province can order the adoption of the budget over the veto of the assembly without the resignation of the council. For the CAOs and sanitary districts, when the governor elects not to alter the proposed budget as requested, he can override the particular assembly's veto by obtaining the MOI's approval of the budget. Hence, ultimately the Ministry of Interior controls the adoption of local budgets either directly, or indirectly through its appointed representatives and governors. Approved budgets are adopted in the form of a local ordinance.

240. Besides annual budgeted expenditures from their own resources, local governments also receive budgeted funds from the central government. The RTG budgeted funds fall into two general categories, regular grants and special grants. Regular grants are for current expenditures and special grants are for capital outlays. The process by which local governments are allocated grant funds from the central government follows a different sequence of budgetary stages than those just traced for the local budget. It involves the administrative structures of the local government and the representative departments of the national government. Preparation of the special grant portion of the local jurisdiction's budget is also the responsibility of the executive office.

241. Grants come chiefly from the Ministry of Interior through its departments and divisions, the bulk of which are provided by the Department of Local Administration, the division of Rural Elementary Education of DOLA, Office of Accelerated Rural Development, the Community Development Department, and Public Works Department. In 1973 DOLA accounted for almost 55% of the MOI's total budget. Of DOLA's revenues of nearly ฿4.5 million, approximately two-thirds were budgeted for specific purposes, that is, they were earmarked for designated activities. The total of the four departments listed above represented 65% of the Ministry of Interior's budget.

242. Two central government agencies play key roles in the budgetary process; they are the DOLA and the Bureau of the Budget (BOB). As one would expect from DOLA's share of the MOI budget, it is the major source of local grant monies. Jurisdictions channel most of their grant request through that department, and decisions on which of the numerous projects

should be forwarded for possible funding rests with the management of that department. The BOB is significant, on the other hand, because it determines the total funds available for grants to local governments and because their review process actually involves a detailed appraisal of the special grant proposals submitted by the departments.

243. The lengthy and complicated procedure required for approval of activities funded from the central government, coupled with the 95% rule previously outlined renders the budget process useless as a fiscal planning device for local governments. First, it is difficult if not impossible for them to plan long-term capital expenditures when virtually all their funds are obtained externally, i.e. from the central government. Second, focusing on current outlays, it is fruitless for local jurisdictions to concern themselves with fiscal conditions beyond the current year in light of the inflexible 95% rule. Last, the provincial governors' delegated authority over budget matters allows the officer to override assembly's vetoes, thereby diminishing the public's indirect participation and influence over budgetary affairs.

244. The local budget procedure is in need of extensive overhauling. The lengthy, and often proforma planning, budgeting and implementation cycle for local government activities takes from 12 to 20 months. One way of streamlining the process is to enlarge the amount of discretionary grants and subsidies to local governments while also reducing central government control over budgetary matters. The latter would require that local assemblies be given more authority over budgetary affairs.

245. As already stated, the regional planning efforts of the National Economic Social Development Board (NESDB), the planning agency for the central government, have met with limited success. The failure of these plans is substantially rooted in the institutional arrangements which circumscribe their implementation. In particular, NESDB has been unsuccessful in chanelling the investment expenditures of the departments of the central ministries into scheduled regional projects. Each department tends to operate independently of the agency and makes unilateral regional investment decisions. The independent action of the departments is possible because the planning function carried out by NESDB is not integrated into the actual budget procedure of the Government. Therefore, a better linkage of these two processes is required if the regional plans are to become realities and the cited inequities in income and public service levels among the regions are to be effectively reduced.

246. Nor has the regional distribution of total public expenditures been a focus of planning. The outlays out of the central government budget are not detailed with respect to the geographical areas they are destined for, and the outlays out of the local budgets are not classified into functional categories. Hence, it is not possible to get a reasonably precise idea about the geographical distribution pattern of various public services. Cooperation among the NESDB, the Budget Bureau and the Ministry of Interior is needed

for progress in this direction to lay the basis for meaningful regional planning. Better data on the distribution of expenditures will, in itself, be useful as a basis for planning and contribute to political consciousness. For a more direct attack at the problem of regional development, however, planning procedures need to be established in the key ministries, perhaps on the lines of what is now being attempted in the new Office of Policy and Planning of the Ministry of Interior.

Tax Administration

247. Tax administration in Thailand suffers from a number of deficiencies: Tax offices are badly organized and understaffed; authority and responsibility for tax enforcement are fragmented; inspection divisions are poorly staffed; audit procedures are inadequate, most auditing and inspection activities consisting of pro forma checks on the arithmetic accuracy in tax returns; coordination between tax departments is lacking; taxation procedures are cumbersome; and systematization of tax administration, particularly making use of data processing techniques is almost non-existent.

248. The mission did not have the time or the expertise to examine tax administration in detail and offer extensive recommendations. Instead, some observations are offered below on what the approach to restructuring tax administration should be and what ingredients are essential for establishing an efficient tax collection system in Thailand.

249. The first major problem concerns staffing of the tax offices. Staff in tax offices and, in particular, in the inspection and auditing units at the headquarters do not have the high caliber either to perform their functions or to set standards for the field offices. Each tax department in the Ministry of Finance has its own inspectors and auditors who are further decentralized into each tax division. Most of the staff serving in these inspection offices are second or third grade civil servants with little or no training in tax auditing. Piecemeal efforts of diligent managers will, from time to time, improve efficiency, reflected in higher volume of tax collections, but this will not lead to a continued improvement in the long run. In order to improve the efficiency of tax administration, upgrading the levels of the civil servants in the tax offices is necessary. But this would not yield much improvement unless parallel measures are taken in staff training and tax collection systematization.

250. There appears to be a need for centralizing tax inspection so that strong units are established reporting directly to department directors. These units, with a comprehensive training program can play a major role in tax inspection, while the routine matters can be delegated to the divisional units. In addition to strengthened departmental units of inspection, a high level finance inspectors' unit reporting to the Finance Minister would be useful as coordinator of the total tax collection program and as the policy making organ in matters concerning tax administration. In fact, it may be

best to start the tax administration reform by establishing such a high powered unit reporting to the Minister or the Undersecretary of Finance first, and having this unit analyze, program and supervise the necessary measures for improving tax administration system.

251. Whether it be a high level tax administration unit under the Minister or not, a staff of full time specialists is needed to study and recommend measures to upgrade and train the staff of tax offices, to simplify tax procedures and to introduce data processing methods. One specific measure which should be adopted in any case without delay is the registration of all taxpayers in a general roster.

Public Borrowing

252. The legal constraint to government deficit financing through borrowing is specified in the Budget Procedure Act which authorizes the Ministry of Finance to borrow in any fiscal year an amount not exceeding 20 percent of total appropriated expenditures for that year. Since September 1972, the scope for borrowing by the Ministry of Finance has been somewhat broadened on two counts. Firstly, the Ministry is authorized to borrow an additional amount up to 80 percent of its refinancing requirements. Thus, the annual debt limit is set more or less in terms of net borrowing. Secondly, in case there is a delay in passing the annual Budget Appropriation Act and the current year's budget, the Ministry is authorized to borrow accordingly. Previously the Ministry of Finance accumulated cash balances at the end of the fiscal year for use during the next fiscal year if it anticipated a delay in enacting the Budget Appropriation Act. This new legal provision now eliminates the necessity to hold such excess balances.

253. Aside from the legal constraint, the Council of Ministers has established an additional limit on debt service payments. Under this administrative limit which, in fact, amounts to an implicit regulation on terms of borrowing, debt service payments in any one year must be kept within 13% of revenue. This provision concerning the debt service ceiling, coupled with the relative ease of administering bond issues, has resulted in the minimal use of treasury bills even for the seasonal needs of the Treasury. Since interest rates on government bonds are usually higher than the interest that would be paid on treasury bills, the interest burden on the government debt has been higher than what it could be if more use was made of the treasury bills.

254. The neglect of the treasury bill market--and the absence of a short-term line of credit to the treasury at the Bank of Thailand--has added to the already high liquidity of the public sector. In 1973 (September) currency held by the public sector amounted to 2.4 billion baht and demand deposits (almost all at BOT) to 5.6 billion baht. Since interest is not paid on government deposits, the high liquidity of the public sector has also been a factor in the high interest burden of the public debt. Hence, although the interest on domestic debt has averaged about 5-6.5% in the

past ten years, if the interest cost is related to the amount of borrowed funds actually utilized, that is, net of liquid balances, cost of these funds would vary between 6.5% and 11.5%. Of course, the public sector could not manage without a minimum level of liquidity and not all of the interest differential should be considered excess cost. According to a rough estimate by the BOT, the burden from excess borrowing may have been in the order of 170 million baht in 1967 rising to 632 million in 1972. 1/

255. Prior to 1972, an important reason for high government liquidity particularly towards the end of the fiscal year was the concern to maintain sufficient funds to meet the committed outlays at the beginning of the following fiscal year, as mentioned above. Other factors were also responsible for accumulation of cash balances, however, such as overborrowing to accommodate excess liquidities of the banks as during the mid-1960s.

256. There is room for reducing the liquid balances held by the treasury through improved cash management among the treasury agencies and by increasing the access of the treasury to short-term borrowing. Treasury bills can be used more extensively, thus helping to reduce needed balances as well as providing funds when needed at cheaper rates than long-term bonds. The possibility of an establishing short-term lending window to the government at the BOT--"short-term advances to the treasury"--which had existed some years ago, is worth giving serious consideration. Moreover, given the large volume of government enterprise deposits with commercial banks, particularly of enterprises whose operating expenses are dependent on the government budget, controls on their use of funds and their deposit accumulation may help reduce the public sector cash requirements and therefore the burden of domestic debt.

257. Overall, Thailand has been successful in coordinating its public debt policy with the management of aggregate demand in the economy over the past decade. Looking to the future, three likely trends will make debt management and its coordination with monetary policy more complicated. Firstly, as discussed in Chapter II, the borrowing needs of the public sector will increase relative to the GDP and to the budget. Apart from the implications of this trend on the statutory ceilings for public debt and on the fiduciary issues of the BOT, the level of interest payments from the budget, already an issue, will become a more serious problem. Secondly, in view of the much faster trend in the increase of quasi-money (saving and time deposits), the relations among the treasury, the BOT, and the commercial banks are likely to become more complicated. Thirdly, the flow of foreign funds into and out of the commercial banking system will also have to be taken into account in reconciling public debt management with monetary policy.

1/ It should be pointed out, however, that some of the benefits to the BOT resulting from high government liquidity--in currency or in deposits at the BOT--flows back to the treasury in the form of remittances of BOT profits to the government.

258. These developments together with the increasing sophistication in the financing of the private business and industry call for more active debt management and central bank policies. One way of providing flexibility for monetary policy and, at the same time, reducing the cost of funds to the treasury can be through more extensive use of reserve requirements of the commercial banks. Reserve requirements in Thailand are low compared to many other countries--only recently increased to 8 percent from 7 percent. Given the wide margin between the lending and borrowing rates of the commercial banks--estimated at 5.5 percentage points net of business taxes--and in view of the expected rapid rise in deposits, there is considerable room for diverting more funds from the commercial banks to the government by raising the reserve requirements to be kept at the BOT which can, in turn be lent to the government by the BOT at lower than the market rates of interest. There appears to be no reason why foreign funds borrowed by the commercial banks should not be subjected to the same reserve requirements as domestic deposits. Furthermore, reserve requirements can be used as an effective tool for purposes of demand management provided the monetary authorities stand ready to adjust reserve ratios in response to the changes in the economy.

VII. CONCLUSION AND RECOMMENDATIONS

Public Expenditures and Revenues

259. Public expenditures in Thailand, especially capital outlays, have suffered in recent years despite rising levels of public borrowing. Public expenditures which had reached a level exceeding 21 percent of GDP in FY1970/71 and FY1971/72 declined steadily to an estimated 18.7 percent in FY1973/74. Capital expenditures which have not increased in real terms since 1971 have borne the brunt of this adjustment. In spite of the planned increase, expenditures for agriculture, education and other social services have actually declined in FY1972/73 and FY1973/74 both in real terms and as a percentage of GDP.

260. It is estimated that in the near future public expenditures equal to at least 22 percent of GDP will be needed to maintain public services at a level comparable to the level of 1969/72. To accomplish improvements in public services needed for efficiency and equity reasons, the mission estimates that the public expenditure target for 1980 should be set at 24 percent of GDP. Within this perspective, given the expected revenue trends and the prospects for increasing the fiscal and financial sources of funds for the public sector in the medium term, it is recommended that a target level for public expenditures be adopted to reach a level of about 23 percent of GDP by FY1976/77 (Exclusive of interest payments due to increase in public debt in future).

261. Stressing that this increase has to accompany efforts to improve the efficiency and the absorptive capacity of the public sector management, and recognizing that the actual level of public spending can deviate from the target due to the trend of activity in the economy, the recommendations of the Mission are based on the following target financing plan for 1976/77.

As % of GDP	
17.0	Expected revenue under present structure
00.5	Additional revenue from adjustment of public utility tariffs
1.0	Net foreign borrowing /1
3.0	Net domestic borrowing /1
1.5	Total public expenditure
23.0	

/1 Net of all amortization payments and of interest payments on new debt.

Taxation Policy

262. The revenue objective of tax policy should be to increase tax level from 14 percent of GDP that the existing structure would generate to 15.5 percent over the next three years. In addition to this revenue target which implies an increase of about 3 billion baht in 1974 prices, the revision of the tax system should aim at broadening the tax base; achieving a higher degree of equity in the comparative treatment of incomes from employment, business and property; developing an integrated commodity tax system; and removing the fiscal impediments to efficient allocation of resources.

263. In taxing personal income, the emphasis should be on increasing the efficiency in taxing business incomes and reducing the exemptions. To this end:

(a) Those paying tax on business and professional incomes above a specified level - e.g., 250,000 baht - should be required to itemize actual deductible expenses incurred in business and not be allowed to use standard deductions;

(b) The standard deductions should be revised and reduced. A suggested rate schedule based on a preliminary study is given in the Report;

(c) The present 20 percent standard deduction for employment income with 30,000 baht ceiling should be reduced by one half;

(d) Dividends exceeding the first 2,000 baht should be subject to personal income tax; the mission finds the provisions of the pending capital market act - exemption from personal income tax of the first 10,000 baht and 30 percent of the rest of dividends received from corporations open to the public - unnecessarily generous and grossly inequitable;

(e) A maximum of 500 baht in interest income should be exempted from income tax. The amount of interest exceeding 500 baht should be subject to withholding at source (bank) at a flat rate of 20 percent and be integrated with the personal income tax;

(f) Exemptions of interest on government bonds from taxation should be discontinued;

(g) The revenue yield from the minimum tax from all Kingdom should be ascertained. This tax should be abolished if the yield is insignificant. If the yield is sizable, then measures should be taken to abolish this tax as administration of the income tax improves;

(h) A capital gains taxes on the sale of urban real estate and of corporate shares should be instituted. The tax rate should be higher for gains on sale of unimproved land. The tax should exempt gains below a stated minimum and should be on profits adjusted by an appropriate price index.

264. The revision of the corporation income tax should aim at establishing a balance between the taxation of corporate and unincorporated business, eliminate loopholes, reduce exemptions and facilitate tax administration. It is recommended that:

(a) Instead of the present separate entity system with progressive corporation tax rates, an imputation system should be adopted consisting of uniform rate of 50 percent corporation tax with a 50 percent credit to be written against the personal tax liabilities of the shareholders who receive dividends;

(b) The concept of registered partnerships should be examined to see whether there is any justification for subjecting them to the corporation tax rather than to the personal income tax as ordinary partnerships.

265. For taxation of goods and services, a move towards either a general sales tax at retail level or a value added tax is premature. The objective in the medium term should be to simplify the present system of single stage taxation at the manufacturing and import level, with emphasis on increasing its revenue yield, improving its progressivity and eliminating the distortionary effects. To achieve these objectives, it is recommended that:

(a) The rate structure of business taxes be consolidated under three classes separately for goods and for services as shown below:

	Goods	Services
Basic rate	10%	5%
Reduced rate - essentials	5%	3%
Increased rate - luxuries	40%	10%

Further differentiation in rates should be confined to few exceptional cases;

(b) In rearranging the rate structure, general rate level should be raised to increase revenue yield and improve progression;

(c) The scope of business tax should be extended to cover tax on electricity consumption which was abolished in 1965 and telephone services. Sale of professional services should also be subject to the general business tax;

(d) A group of commodities the production of which can be audited through physical monitoring should be included under the excise tax system and be administered by the Excise Department. This transfer should be gradual depending on the development of the administrative preparation in the Excise Department;

(e) Excise tax rates on non-alcoholic beverages which cost more than 3 baht a bottle at present and excises on gasoline and perhaps diesel fuel should be increased;

(f) Methods of increasing the taxation on the ownership and use of private motor cars should be reviewed;

(g) Business and excise taxes on cement and petroleum products should be consolidated under the excise tax system;

(h) Measures should be instituted to increased responsiveness of specific excise duties to inflation by changing the system to ad valorem wherever possible or establishing an automatic adjustment system of specific rates to costs.

A suggested list of business and excise tax rates incorporating the suggestions above is given in Table 31.

266. The present house and rent tax in urban areas and the land development tax in rural areas should be replaced by a property tax, at a uniform rate, on the value of the property - land and improvements on land. This should apply both to rental and the owner-occupied property. With respect to taxes on residential properties the possibilities of having a progressive rate in excess of a stated minimum value should be investigated. The property tax should be administered by the central government, but its proceeds should be earmarked for local government budgets. The property tax system should also include provisions for betterment levies to be implemented in cases of rapid appreciation of property due to public outlays.

267. An agricultural tax policy which relies almost exclusively on the rice premium remains uncertain in its impact and probably produces unplanned redistributive and reallocative effects. Given the variety of agricultural fiscal policy instruments that can be used, the most reasonable alternative to the present situation is heightened recognition of the potential usefulness of available instruments, followed by their effective application. Taxation of agriculture should be done by taxation of land under the property tax system proposed above. The rice premium and the rice export duty should be merged into one tax and its rate schedule reduced, though kept flexible to

TABLE 31: PRESENT AND PROPOSED BUSINESS TAX SCHEDULE

	Present Rates (%)	Proposed Rates(%)
1. Sale of Goods		
Type 1	7	10
Type 2	15, 20 and 30	40
Type 3	12 and 15	40
Type 4	40	40
Type 5 Exempted by N.E.C.D.	(No.175) BE 2515	--
Type 6	1.5	5
Type 7	3.0	10
Type 8	1.5 and 4.0	5
2. Rice and sawmilling	2.5 and 4.0	5
3. Deleted by R.C.A.A.	(No.19) BE 2508	--
4. Hire of Work		
Type 1	2.0	5
Type 2	5.0	10
5. Letting of property	2.5	5
6. Warehousing	2.5	5
7. Hotel and restaurant		
(a) Nightclubs or Cabaret	10.0	10
(b) Hotel	7.5	10
(c) Restaurant	2.0 - 5.0	5 - 10
8. Transport	0.5	3
9. Pawn Brokerage	2.5	5
10. Commission agents	5.5	5
11. Sales of land and buildings	3.5	5
12. Banking		
Type 1	2.5	5
Type 2	10.5	10
13. Insurance	2.5 and 3.0	5

serve primarily as a tool of domestic price stabilization. The desire to channell export tax proceeds back to agriculture should not lead to further fragmentation of the government budget as seems to be implicit in the proposed agriculture aid fund.

Fiscal Incentives

268. Both the industrial promotion provisions and the export promotion schemes suffer from being too discretionary and not based on an industrial policy. For reasons of efficiency and fairness, the fiscal incentives systems should be based on more objective criteria and procedures:

(a) Exemption from corporation tax as an industrial incentive should be abolished, and replaced by a limited tax allowance for investments from corporate tax liabilities;

(b) Import duties on capital equipment and raw materials should be reviewed and revised to provide incentives for industrial development; discretionary exemptions from import duties should be minimized.

State Enterprises

269. In the past, major state enterprises have not been a drain on the Government's budget; however, the prevailing favorable overall financial situation of the state enterprises is bound to deteriorate quickly in the absence of adequate remedies on the revenue side. It is therefore recommended that tariff adjustments be made in the following directions:

(a) In State Railways, in order to reach a modest return on investment of about 2 percent which would keep the entire entity viable, selected tariff adjustments resulting in an overall 20 percent tariff increase (in 1974 prices) will have to be made;

(b) EGAT's tariffs appear somewhat low; Provincial Electricity Authority, despite its comparatively high tariffs, is barely in a position to meet its commitments; Metropolitan Electricity Authority, in spite of reasonable tariffs, is making large profits and is able to remit substantial sums to the Government. The relative tariffs level between the three enterprises should be modified so as to distribute the revenues from power sales more evenly, permitting each company to meet its financial requirements in a balanced manner and enabling subsidization of the rural tariffs at the expense of urban (Bangkok) tariffs. The alternative of merging the relevant authorities under one administration should also be investigated.

270. All state enterprises should be subject to the corporation tax. Dividend payments to the Government should be made by individual enterprises

in the light of their financial position and investment requirements in the framework of annual public sector financial plans.

Local Finance

271. The fiscal system at present is not capable of making a significant contribution to regional development. Revenue sources provided to the local jurisdictions in inadequate to finance the obligatory functions required of them in the enabling acts. And the budgetary procedures are not integrated with planning for regional development. Following recommendations are offered, predicated on the assumption that the establishment of a viable local government sector is a major objective of the Thai Government:

(a) The administration of the property tax (land and urban property) suggested in the Report should be centralized in the Revenue Department coupled with ploughing the proceeds of these taxes back to the local jurisdictions from which they were collected;

(b) The three locally-levied taxes - the slaughter tax, signboard tax and gambling tax - should remain under the jurisdiction of local government, with enlarged discretionary authority given to them in the setting of rates on these taxes;

(c) The principle concerning the allocation of the surtaxes and share taxes among the regions should be based on some simple and objective formula which would attach a heavy weight to the population distribution. The business taxes on some services could be transferred to the local administration gradually over time;

(d) Cooperation among the NESDB, the Budget Bureau and the Ministry of Interior is needed for meaningful regional planning. Better data on the distribution of expenditures will, in itself, be useful as a basis for planning and contribute to political consciousness;;

(e) For a more direct attack at the problem of regional development, project oriented planning procedures need to be established in the key ministries.

Policy Management

272. Because of the shortcomings in formal planning activities and the unsatisfactory coordination between the planning, programming, budgeting and treasury functions of the government, economic decision-making in the public sector is not as efficient as it should be. The important improvements needed in Thailand can be summed up as follows:

(a) Planning should include the analysis of public sector finances in terms which would relate explicitly to budgetary fiscal concepts;

(b) Comprehensive annual programs should be prepared by the NESDB with the participation of concerned agencies covering all the activities of the central government, the local government and the state enterprises and submitted to the cabinet for approval;

(c) The unity of the central government budget should not be violated by earmarking separate funds for the Ministry of Interior or the Ministry of Commerce;

(d) Foreign grants and loans should be included in the budget so that the budgeting agency could consider an overall allocation of financial resources for the government;

(e) The supplementary budget should be explicitly used as an instrument for adjusting the government's fiscal demand management, and expenditure procedures should be reviewed and adapted to the inflationary environment;

(f) The link between planning and budgeting should be reinforced by strengthening the public finance capability of the NESDB and improving its cooperation with other agencies of the public sector;

(g) Budgeting function and the treasury function should be coordinated. This can be done under various organizational arrangements. One possible alternative to the present organization worth exploring would be to enlarge the scope of the Ministry of Finance by bringing the Budget Bureau under it, thus centralizing the formulation of annual fiscal policy and coordinating it with demand management.

Tax Administration

273. Tax administration needs to be improved in order to raise the revenue yield of taxation and to reduce inequities in the treatment of taxpayers.

(a) Data base concerning tax collections and taxpayers is very poor;

(b) Data processing is carried out mostly manually with almost no possibilities of cross-checking;

(c) A general taxpayers' register does not exist;

(d) Tax audit is usually confined to arithmetic checks on tax returns;

(e) Tax returns are not designed in a way to facilitate jobs of taxpayers as well as tax auditors;

(f) Tax offices are understaffed and the staff does not have needed qualifications.

274. Measures should be taken in all these areas to raise the efficiency in tax administration. However, the mission is in favor of a systematic approach and strongly recommends the establishment of a high level Finance Inspectors Unit reporting directly to the Finance Minister as the first step. With careful recruitment, good training and adequate incentives, this unit can perform the function of tax administration policy formulation and act as the high authority for selective taxpayer auditing and tax administration inspection. This unit should study the tax administration problems and recommend measures to upgrade and train staff of tax offices, to simplify tax procedures and to introduce data processing methods.

Public Borrowing

275. There is room for alleviating the cost of public borrowing by more flexible public debt practices and more efficient cash management:

(a) Treasury bills can be used more extensively, thus helping to reduce needed liquid balances as well as providing funds when needed at cheaper rates than long-term bonds;

(b) The possibility of establishing a short-term lending window to the government at the Bank of Thailand - i.e., short advances to the treasury - which had existed some years ago, is worth giving serious consideration;

(c) Given the large volume of government enterprise deposits with commercial banks, particularly of enterprises whose operating expenses are dependent on the government budget, controls on their use of funds and their deposit accumulation may help reduce the public sector cash requirements and therefore the burden of domestic debt;

(d) There is considerable room for diverting more funds from the commercial banks to the government through raising the legal reserve requirements to be kept at the Bank of Thailand which can be lent to the government at lower than the market rates of interest. However, caution must be exercised in recounting the objectives of funding public sector at reasonable cost, providing enough resources for private sector needs and prudent demand management.

Suggested Approach for Follow-Up

276. The report contains three types of recommendations:

(a) Those relating to revision or drafting of tax codes;

(b) Those relating to improving tax administration; and

(c) Those relating to institutional or policy changes.

The last category of issues dealt with in the report can best be evaluated in discussions in appropriate forums of the government leading to policy or legislative decisions. For the suggestions concerning tax structure and tax administration, however, the evaluation and follow-up work needs the development and formulation of new proposals for the government by teams of specialists. The Mission, therefore, recommends the establishment of two units:

(a) Tax Reform Commission whose main responsibility will be to revise the Revenue Code, finalize the Excise Code and draft the Property Tax Code within a specified period;

(b) Finance Inspectors Unit whose continuing responsibility will be to study and recommend measures to improve tax administration in coordination with the work of the Tax Reform Commission.