Forging Ahead

Restoring Stability & Boosting Prosperity

2. Revenue Mobilization

Lao PDR 2023

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2. Revenue Mobilization

Improving domestic revenue collection is fundamental to restoring macroeconomic stability and boosting growth-enhancing spending. Revenue performance was a concern even before COVID-19, as total revenue declined from 22 to 16 percent of GDP during 2014–2019, owing to declines in tax collection and foreign grants. Tax revenue fell from 14 to 11 percent of GDP in that period. Low tax rates, a narrow tax base, and weak compliance and enforcement have undermined tax collection. In particular, generous tax exemptions have deprived the budget of vital fiscal revenues and even foreign exchange. Revenue collection has heavily relied on indirect (consumption) taxes and is very low by international standards. In 2019, revenue-to-GDP and tax-to-GDP ratios ranked in the bottom 15 percent of the world, and these have deteriorated further since then. At 11 percent in 2022, the tax-to-GDP ratio is significantly below the recommended minimum international benchmark of 15 percent. Tax rates are among the lowest in the region, while tax administration inefficiencies also undermine performance. Tax collection is only reaching about 60 percent of its potential (due to suboptimal tax policy and administration), implying that there is vast scope for revenue-enhancing reforms that need not undermine economic growth or living standards. However, recent measures have further hampered revenue mobilization (e.g., tax rate cuts and growing fragmentation in the management of large taxpayers). Poor revenue performance jeopardizes fiscal and debt sustainability, as well as broader macroeconomic stability. Improving tax policy and tax administration is critical for boosting revenue mobilization, which would help increase fiscal space for growth-enhancing spending and meet growing debt service obligations.

Main recommendations: (i) restore the value-added tax rate to 10 percent; (ii) revise the Law on Investment Promotion to curb tax incentives; (iii) reform excise tax structures and increase rates, particularly on beverages, tobacco, and fuel; (iv) reform the land tax and prepare for the introduction of a property tax; and (v) strengthen compliance risk management by focusing on the administration of large taxpayers.

Chapter structure: The chapter starts by providing a brief overview of the tax system, after which it assesses key revenue trends and performance. It then presents a more in-depth assessment of major taxes, supported by key metrics and benchmarking to regional and income peers. The chapter also covers tax administration issues before concluding with recommendations for enhancing tax policy (including widening the tax base) and strengthening tax administration.

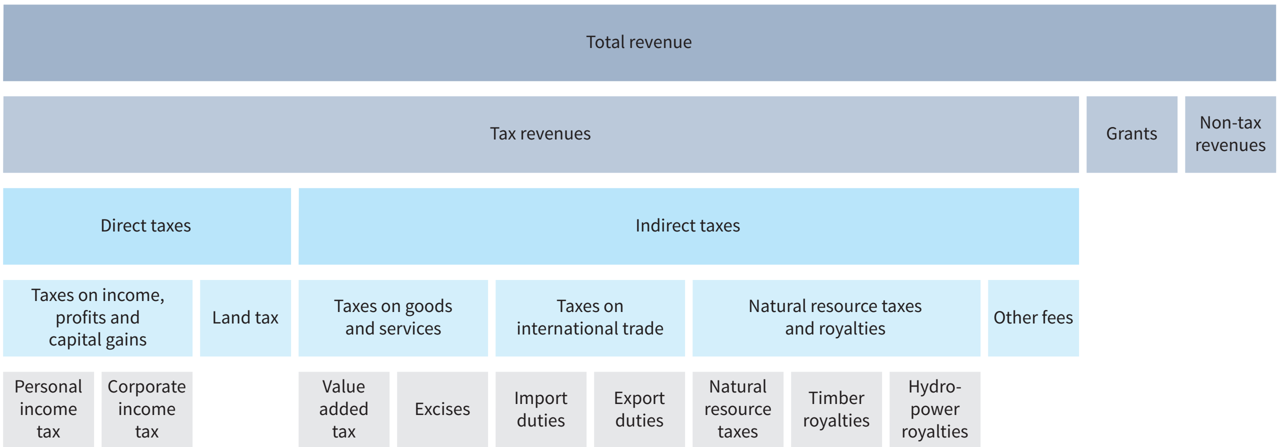
2.1 Background

There is an urgent need to revisit the current revenue mobilization strategy, especially due to mounting macroeconomic challenges. Rising public debt service obligations have sharply increased financing needs, despite significant deferrals in 2020–2022. Coupled with limited access to international capital markets and low foreign exchange reserves, this has contributed to a severe exchange rate depreciation and thus high inflation, jeopardizing macroeconomic stability and economic growth. Poor revenue performance has intensified these pressures, despite strong curbs on public spending. Generous corporate tax exemptions and tax rate reductions have undermined fiscal sustainability and macroeconomic stability. The erosion of fiscal space increases the country's vulnerability to economic, health, and environmental shocks, while threatening economic growth prospects through under-investments in education, health, and infrastructure.

The stated policy objective is to achieve a domestic revenue level of about 16 percent of GDP by 2025, but this will require major reforms. Collecting adequate levels of fiscal revenue is key to supporting the implementation of national development priorities. The Ninth National Socio-Economic Development Plan (NSEDP), which covers the period 2021–2025, sets targets for total revenue (at least 17 percent of GDP) and domestic revenue (at least 15.8 percent of GDP). Proactive reforms are required to meet these targets. In 2022, total and domestic revenue reached 15.0 and 13.3 percent of GDP, respectively. Tax revenue collection averaged only 10 percent of GDP since 2018, while research suggests that a minimum tax-to-GDP ratio of 15 percent is necessary to support economic growth. Below that threshold, economic activity is likely impacted by poor financing of basic public services crucial for growth, such as education, health, and infrastructure (including maintenance). Broadening the tax base, setting tax rates at reasonable levels, and improving the efficiency of revenue collection are key to enhancing domestic revenue mobilization.

The state budget is funded by multiple sources of finance, but the tax framework is the ultimate foundation. Public spending is mainly financed through government revenues and borrowing, and to a lesser extent, asset sales and capital returns. Revenues are typically classified by the nature of the source. Tax revenue is by far the main source, followed by non-tax revenues and foreign grants. Direct taxes are levied on incomes, profits, and capital gains on both individuals and corporations, together with the land tax (Figure 2.1). Indirect taxes are levied on the consumption of goods and services (value-added tax and excises), as well as on international trade. Natural resource taxes and royalties (e.g., from timber and hydropower) are also indirect taxes. Non-tax revenues mainly relate to fees, user charges, fines, and interest. Grants are provided by a range of development partners, such as bilateral and multilateral institutions. In the Lao PDR, social contributions are not considered to be part of government revenue.

Figure 2.1: Classification of government revenues



Source: World Bank staff.
Notes: The sum of tax and non-tax revenues is often referred to as domestic revenue.

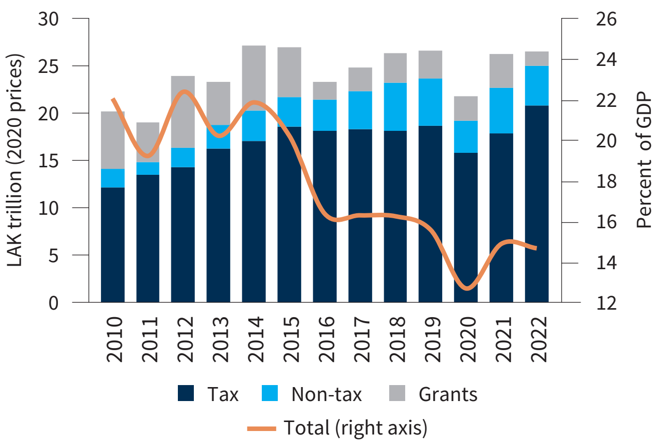
A well-functioning tax system should fulfill certain attributes, such as adequacy, efficiency, and equity. Some of the desired features of a tax system include revenue adequacy (to fund basic public services), efficiency (in revenue collection), equity (through income redistribution), simplicity (of the tax system), and stability (to avoid economic instability). However, trade-offs require careful attention and may need complementary policies. For example, reducing tax rates may benefit some consumers and businesses in the short-term, but can eventually undermine living standards and the business environment by weakening the provision of basic public services (e.g., education and infrastructure). Some reforms can efficiently collect a significant amount of revenue (e.g., VAT rate increase) but may need to be accompanied by measures to protect the most vulnerable households. Evaluating and balancing different priorities will be critical.

2.2 Trends and composition

Revenue collection has deteriorated considerably in the past decade and is low by regional and income standards. Total revenue fell from 22 to 16 percent of GDP during 2014–2019, owing to declines in tax collection and foreign grants. It subsequently dropped to 13 percent of GDP in 2020, but it recovered to 15 percent in 2022 (Figure 2.2). In 2022, about three-quarters of government revenue was collected through taxes. Tax revenue steadily declined from 14 to 11 percent of GDP in 2013–2019, falling further to 9 percent of GDP in 2020 due to the impacts of the COVID-19 pandemic. While tax revenue bounced back to 11 percent in 2022, this was largely aided by inflation (and despite some tax rate cuts). Non-tax revenue averaged 2 percent of GDP during 2010–2022. Grants showed considerable volatility before falling significantly in 2016, partly due to the country's graduation to lower-middle-income status. Total revenue is very low when compared to regional and income peers (Figure 2.3).

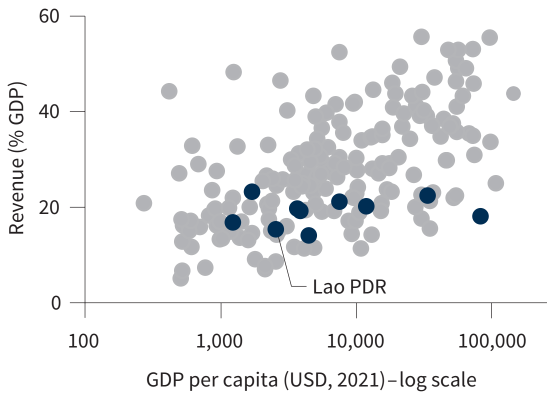
Tax revenue has relied heavily on indirect taxes, particularly the value-added tax and excises. Indirect taxes accounted for most tax revenue, with the value-added tax (VAT) and excises representing 29 and 25 percent of total tax revenue in 2018–2022, respectively. These are consumption-based taxes levied on the purchase of goods and services. Direct taxes averaged 23 percent of tax revenue in the same period and were almost exclusively derived from the corporate income tax (CIT) and the personal income tax (PIT).

Figure 2.2: Revenue (Lao kip and % GDP)



Source: Ministry of Finance and World Bank staff calculations.

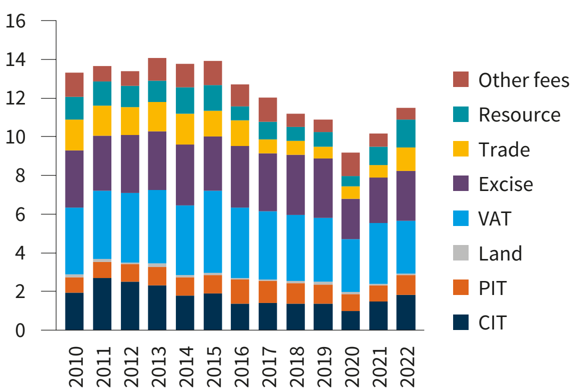
Figure 2.3: Revenue (% GDP, 2016–21)



Source: International Monetary Fund and World Bank staff calculations.
Note: Blue dots represent ASEAN countries.

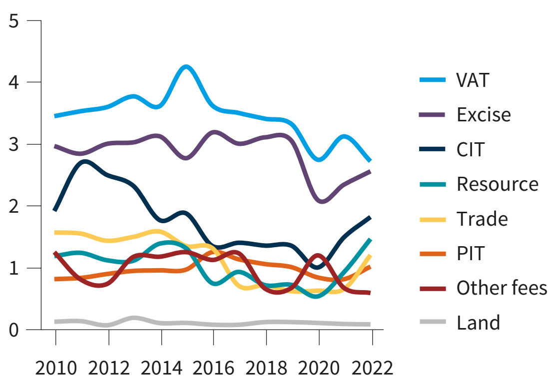
The relative decline in tax revenue is mostly accounted by the underperformance of the CIT and VAT. The poor performance of revenue collection has been observed across most types of tax (Figure 2.4 and Figure 2.5). The CIT declined considerably since 2011, owing to steady reductions in the standard rate and widespread profit tax exemptions. The VAT has declined since 2015, likely also affected by tax exemptions. COVID-19 had a considerable impact on economic activity and, thus, tax revenue. In 2020, revenue collection declined for most taxes, especially excises, although 'other fees' partly offset this trend. Since then, a recovery in consumption and imports has underpinned tax collection improvements, although this is also linked to the exchange rate depreciation and higher (domestic and import) prices. Nonetheless, VAT collection declined in 2022, largely due to the VAT rate reduction from 10 to 7 percent.

Figure 2.4: Tax revenue (% of GDP)



Source: Ministry of Finance and World Bank staff calculations.

Figure 2.5: Tax revenue (% of GDP)

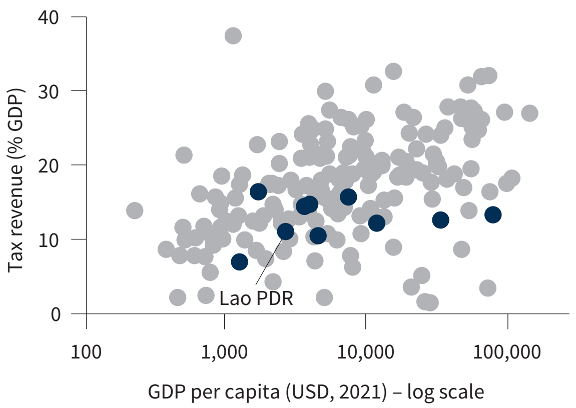


Source: Ministry of Finance and World Bank staff calculations.

Tax revenue collection is considerably lower than regional and income averages. The tax-to-GDP ratio is significantly lower than most regional and income peers (Figure 2.6). While the EAP region is generally known to have low tax rates (and thus tax collection) compared to other regions in the world, tax revenue in the Lao PDR is not only lower by international standards but also by regional standards. Moreover, tax revenue collection has been deteriorating in contrast to many countries in the region. Before 2016, tax revenue was at the lower end of the interquartile range in the EAP region, and it dropped significantly since then (Figure 2.7).

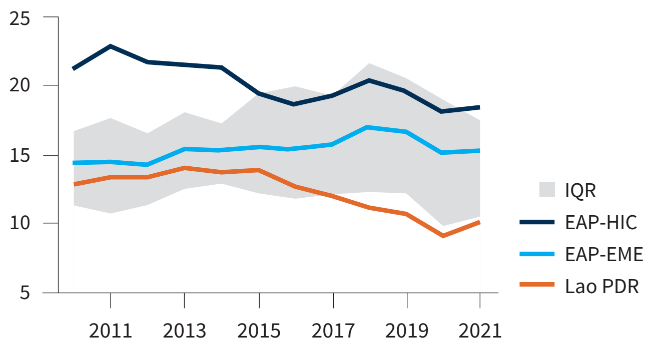
The tax system relies heavily on consumption taxes, with limited income tax collection accounting for most of the gap to international benchmarks. Taxes on (corporate and individual) income account for most of the shortfall in revenue relative to other countries in the region (Figure 2.8). CIT collection amounted to 1.4 percent of GDP in 2018, less than half the average collected in EAP countries and LMICs (Figure 2.9). Despite large foreign investments, CIT revenue is low because of generous profit tax exemptions. PIT collection is also relatively small due to lower average incomes and higher informality (i.e., low share of wage and salaried workers in total employment). VAT revenues are sizable, but still low by international standards. Taxes from international trade are also much lower than peer countries, likely due to exemptions for large investment projects. Among the main taxes, only excises perform comparatively better.

Figure 2.6: Tax revenue (% GDP, 2016–21)



Source: International Monetary Fund and World Bank staff calculations.

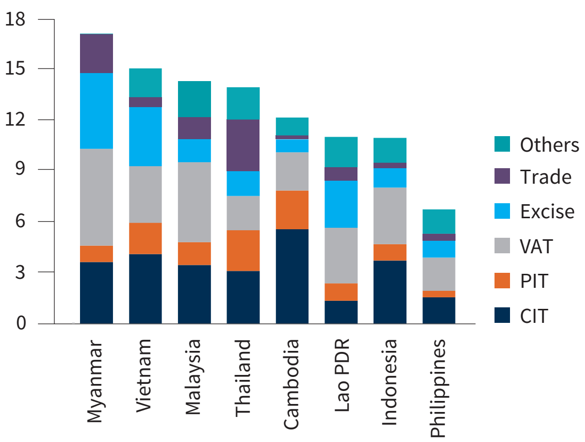
Figure 2.7: Tax revenue (% GDP)



Source: International Monetary Fund and World Bank staff calculations.

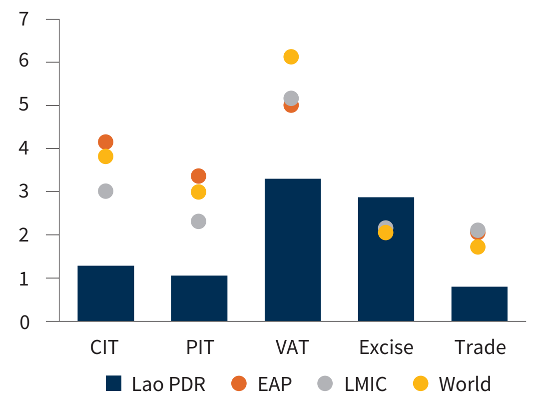
Note: IQR: interquartile range, EAP-HIC: East Asia and Pacific, high-income countries, EAP-EME: East Asia and Pacific, emerging market economies.

Figure 2.8: Tax revenue (% GDP, 2016–21)



Source: International Monetary Fund and World Bank staff calculations.

Figure 2.9: Revenue by type of tax (% GDP, 2016–20)



Source: International Monetary Fund and World Bank staff calculations.

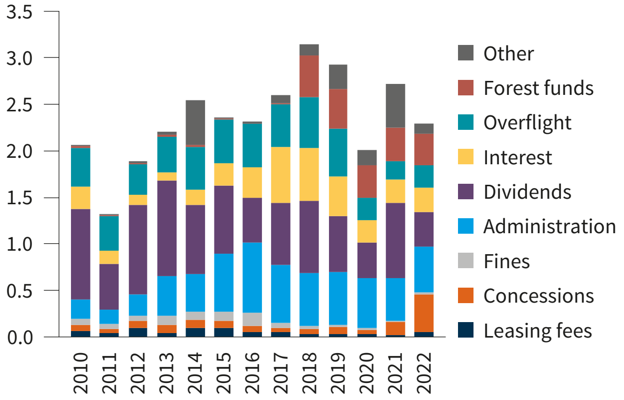
Non-tax revenue collection is sizable, but it remains below regional standards. Non-tax revenue mainly relates to fees, user charges, fines, interest, and dividends. For instance, this includes administration fees (e.g., registration and document processing), dividends from corporations where the government holds equity, interest from on-lending to SOEs, and charges relating to the use of Lao PDR's airspace (overflight rights).[65] Non-tax revenue averaged 2.3 percent of GDP during 2010–2022 (Figure 2.10). Forest Preservation Funds significantly increased to 0.4 percent of GDP since 2018, while concessions rose to 0.4 percent of GDP in 2022. In ASEAN countries, the Lao PDR's non-tax revenue was higher only than the Philippines and Indonesia (Figure 2.11).

While economic growth has been predominantly driven by natural resources, government revenues accruing from the resource sector have been limited. Resource-related revenues, such as taxes, royalties, and preservation funds, are relatively small. Their combined (tax and non-tax) revenue averaged about 8 percent of total domestic revenue in the period 2010–2022 (or 1 percent of GDP), which is much lower than the combined share of forestry & logging, mining & quarrying, and electricity in total gross value added (about 20 percent).[66] These revenues have been undermined by tax incentives, volatile international commodity prices, and depleting reserves (e.g., copper).

[65] Asset sales and capital returns (e.g., loan repayments from SOEs) are not reported under revenue as they are included in net financing in GFS-compatible fiscal accounts.

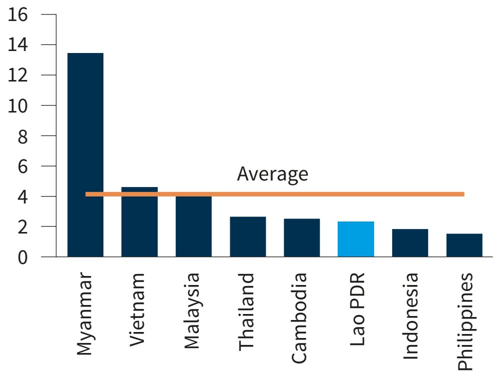
[66] Resource exploitation is also taxed through CIT, trade taxes, and VAT, but these likely yield limited revenue due to generous exemptions.

Figure 2.10: Non-tax revenue (% GDP)



Source: Ministry of Finance and World Bank staff calculations.

Figure 2.11: Non-tax revenue (% GDP, 2016–21)



Source: IMF and World Bank staff calculations.

Note: Non-tax revenues (mainly from SOEs in the energy sector) account for most revenue In Myanmar.

Tax buoyancy

Tax revenue collection has not kept pace with economic activity, with poor performance mainly driven by the CIT. Tax buoyancy (or tax elasticity) assesses whether growth in tax collection has been keeping pace with economic growth over time. A buoyancy coefficient of 1 would suggest that a 1 percent increase in GDP leads to an average rise of 1 percent in revenue collection, implying that revenues grow at the same pace as economic activity. The buoyancy for the period 2010–2019 for all combined tax revenues stood at 0.69, meaning that tax collection performance has been low in relation to economic growth (Table 2.1). Tax buoyancy is above 1 for PIT and excises, while for the VAT, it is nearly 1. However, the buoyancy for CIT, trade taxes, and natural resource taxes & royalties is low or even negative. This is mainly due to the impact of tax exemptions for large projects (including those in mining, electricity, and transport), along with the reduction of the CIT rate, trade liberalization, and volatility of commodity prices. Strong reforms are needed to mobilize adequate revenues since these need to increase much faster than economic growth to reach stated policy objectives, as well as regional and international benchmarks.

Table 2.1: Revenue responsiveness to GDP growth (2010–2019)

Tax	Bouyancy
Tax revenue	**0.69**
Personal income tax (PIT)	1.51
Corporate income tax (CIT)	-0.03
Land tax	0.74
Value-added tax (VAT)	0.98
Excises	0.10
Trade taxes	-0.47
Import duties	*-0.36*
Export duties	*-2.34*
Other fees	0.67
Natural resource taxes & royalties	-0.15

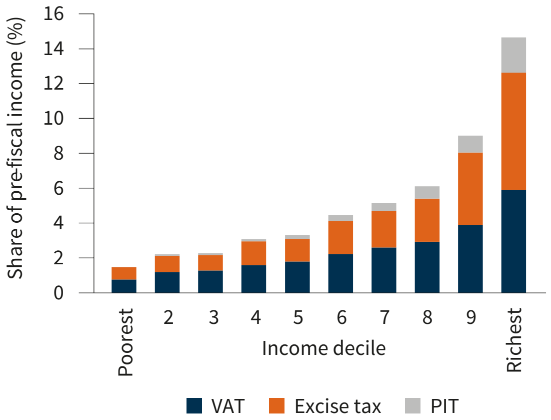
Source: World Bank staff calculations.

Distributional impact

Taxes levied on consumption impose a larger burden on better-off households, which implies that they are progressive. Although the standard VAT rate was 10 percent in 2018, poorer households faced much lower effective VAT rates due to large shares of informal consumption (e.g., self-produced food or services provided by unregistered vendors). For poorer households, a large part of VAT payments is the VAT component hidden in VAT-exempted and informal goods and services that use inputs subject to VAT (e.g., fuel). In total, VAT payments represent only 0.8 percent of the income of the poorest households, compared to 5.9 percent for the richest households, suggesting that the VAT is a progressive tax (Figure 2.12). Therefore, the VAT rate reduction introduced in 2022 has had a negative redistributive effect. Excise taxes are found to be slightly more progressive than VAT, as better-off households spend more on goods and services subject to excise taxes. Spending on alcoholic beverages, tobacco, fuel, large vehicles, luxury goods, and recreation together constitute 23.5 percent of income for households in the richest decile, compared to 3.4 percent in the poorest decile. The amount of excise taxes paid represents 1.1 percent of the income of the poorest decile and 8.2 percent of the income of the richest decile.

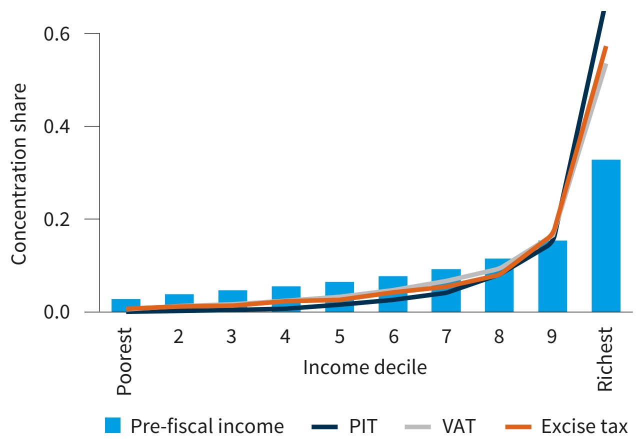
The PIT is progressive and imposes a relatively small burden on households. PIT progressive rates and the minimum income threshold, combined with high rates of informality among poorer households, mean that the PIT is structurally progressive. The amount of PIT paid increases with household income. The richest households account for 67 percent of total PIT payments, more than double their share in total household income, while the contribution of the poorest households is less than 0.1 percent (Figure 2.13). However, overall PIT revenue collection and its burden on households are relatively small due to the high prevalence of informality. Among PIT taxpayers, PIT payments represent around 2–5 percent of their income. Broadening the tax base through formalization and increasing PIT rates (especially for the top income brackets) could support revenue collection without placing a heavy burden on low-income households.

Figure 2.12: Incidence of taxes



Source: World Bank staff calculations.

Figure 2.13: Concentration share of taxes



Source: World Bank staff calculations.

Tax revenue potential

There are several methods to estimate a country's domestic revenue mobilization potential. There are various factors affecting domestic revenue collection, pertaining to both tax policy and administration. Domestic revenue can be considerably below its potential due to suboptimal tax rates and the proliferation of exemptions (which relate to tax policy), as well as low compliance and limited capacity to collect revenue (which relate to tax administration). It is therefore crucial to identify the most binding constraints to prioritize reforms. A simple method of estimating the amount of additional tax revenue that could be potentially collected is to compare a country's tax-to-GDP ratio with that of other countries with similar characteristics, such as the level of economic and institutional development. This can be undertaken through a simple benchmarking exercise, including tax productivity, VAT c-efficiency, or through an empirical exercise.[67]

'Tax effort' measures a country's effort to raise tax revenues, while the 'tax gap' is often driven by both policy and administration weaknesses. Tax potential (or taxable capacity) provides a reference point for the maximum amount of revenue that could be collected through tax policy changes or improvements in the efficiency

[67] Tax productivity (or tax collection efficiency) is calculated as the ratio of tax revenue as a share of GDP to the standard tax rate. This measures efficiency in both tax policy and administration, and it is often computed for the CIT, PIT, and VAT. VAT c-efficiency is measured as the ratio of actual VAT revenues to the product of the standard rate and final consumption.

of collection given a country's socioeconomic factors (e.g., a country's specific macroeconomic, demographic, and institutional features). Tax effort is the ratio between actual tax collection and tax potential, which measures a country's effort to raise tax revenues. The tax gap is the difference between tax potential and actual tax collection, and it comprises the 'policy gap' and 'compliance gap'. The policy gap quantifies the extent to which tax collection is affected by policies that reduce the tax base and tax rates. Examples include tax exemptions and reduced rates, which reduce tax liabilities and thus revenue. The compliance gap conveys the extent to which poor tax administrative capacity and active tax avoidance may explain the gap between potential revenues and actual collection.

Tax collection is only reaching about 60 percent of its full potential, implying that there is ample scope for tax policy and administration reforms. Tax effort was estimated at about 0.6 during 2010–2016, meaning that tax collection was lower than the average tax yield for countries with similar characteristics. Hence, there is considerable potential to mobilize additional domestic revenues. Tax effort is affected by the tax structure (e.g., tax rates and tax base), as well as tax administration and compliance. Tax effort can be increased by raising tax rates, expanding the tax base, and improving tax compliance and enforcement. When compared to taxation levels and (structural and institutional) determinants in peer countries, Lao PDR had an average tax potential of 21 percent of GDP, with the corresponding total tax gap at 8 percent of GDP – as tax revenue averaged just over 13 percent of GDP in 2010–2016.[68] The tax gap has likely increased in recent years due to tax rate cuts.

Tax rates are low when compared to regional and income peers, which considerably undermines revenue collection. The standard CIT rate (20 percent) is low in international terms (Table 2.2). This rate already represents a significant tax incentive, but tax exemptions further hamper the effective tax rate. The PIT top marginal tax rate (25 percent) is also below most regional and income peers. The VAT rate of 7 percent places the Lao PDR among the countries with the lowest VAT rates in the region and the world. Recent trends suggest that countries in the region are raising VAT rates. For instance, Indonesia raised its rate to 11 percent in April 2022.

Table 2.2: Statutory tax rates (%, 2022)

	CIT (standard)	PIT (top rate)	VAT (statutory)
Cambodia	20	20	10
Indonesia	25	30	10
Lao PDR	**20**	**25**	**7**
Malaysia	24	30	6-10
Myanmar	25	25	5
Philippines	30	35	12
Thailand	20	35	7
Vietnam	20	35	10
Asia	21	28	12
Latin America	27	32	14
Africa	27	33	16
OECD	23	42	19
World	24	31	15

Source: International Monetary Fund, PwC, and KPMG.

Note: In Myanmar, a 5 percent rate on certain goods and services is considered turnover tax rather than VAT. Malaysia levies a 10 percent sales tax and a 6 percent services tax.

[68] See the World Bank's Tax Revenue Dashboard.

2.3 Assessment of major taxes

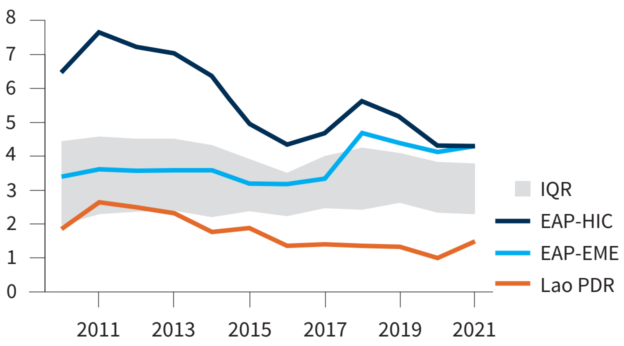
2.3.1 Income taxes

Corporate income tax

The CIT rate has been progressively reduced, while additional tax incentives have been provided across several sectors. Companies registered in the Lao PDR (including foreign companies operating in the country) are taxed at a standard rate of 20 percent, with some exceptions. The profit tax rate is 35 percent for mining companies and 22 percent for tobacco companies. Training and research centers are taxed at 5 percent, while activities using innovative or green technologies face a 7 percent tax rate. Companies listed on the Lao Stock Exchange pay 13 percent in the first four years. Microenterprises voluntarily registered in the VAT system only pay 0.1 percent, while small- and medium-scale entities newly registered in the VAT system pay 3 and 5 percent in the first 3 years, respectively. The standard profit tax rate was cut from 35 to 28 percent in 2012, then to 24 percent in 2015, and finally to 20 percent in 2020. Meanwhile, the Law on Investment Promotion provides tax incentives depending on the business activity and location, while concessions negotiated on a case-by-case basis provide even more generous tax benefits.[69]

CIT revenue collection and CIT productivity ratio are the lowest in the region. CIT revenue steadily dropped from 2.7 to 1.0 percent of GDP during 2011–2020, although it recovered to 1.5 percent in 2021 (Figure 2.14). It has increased to 1.8 percent of GDP in 2022, but it remains one of the lowest levels in the world. Very low CIT revenue collection is due to a combination of tax rate cuts and the widespread use of tax incentives. CIT productivity, measured as the ratio of actual CIT collection (as a percentage of GDP) to the highest statutory marginal rate, was also very low at 0.05 (Figure 2.15). This ratio is significantly lower than the averages observed in the EAP (0.15) and other regions.

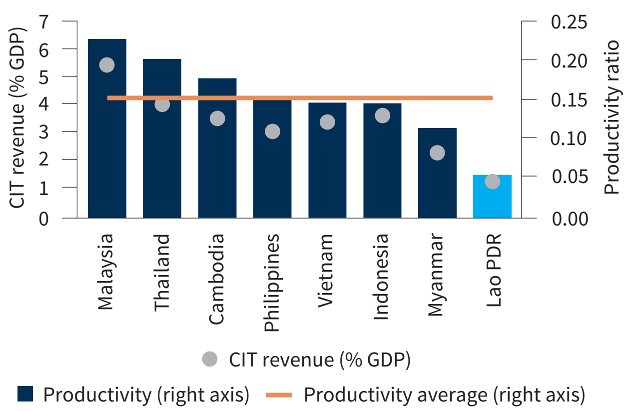
Figure 2.14: CIT collection (% GDP)



Source: International Monetary Fund and World Bank staff calculations.

Note: IQR: interquartile range, EAP-HIC: East Asia and Pacific, high-income countries, EAP-EME: East Asia and Pacific, emerging market economies.

Figure 2.15: CIT productivity ratio (2016–21)



Source: International Monetary Fund and World Bank staff calculations.

CIT gaps are estimated to be very high, indicating a very large amount of foregone revenues. The estimation of tax gaps is crucial for policy making since it provides a measure of the revenue gains that can be achieved with tax policy and administration reforms.[70] Estimates suggest that the overall CIT gap amounts to 87 percent of potential revenue, which implies that only 13 percent of potential revenue is being collected.[71] This is due to both tax policy (e.g., exemptions that reduce the tax base) and tax administration issues (e.g., weak compliance and enforcement). The CIT gap is very high across most economic sectors, including those dominated by large companies operating in the formal economy. Agriculture and accommodation &

[69] Additional benefits are often granted to individual companies as part of concession agreements.

[70] It is not possible to estimate the CIT gap with microdata because of the limited scope of the CIT return form. This report uses income data from the national accounts following the IMF's RA-GAP methodology. The tax base is derived using 2020 value-added by sector, adjusting for the share of value-added that is earned by labor, land, and capital, as well as other deductible expenses (e.g., depreciation). Therefore, these CIT gap estimates are merely indicative.

[71] This exceeds the CIT gap estimated in an earlier analysis by the IMF, which found foregone revenues ranging 78–82 percent when excluding the agriculture and natural resource sectors.

food services, which are overwhelmingly informal, have CIT gaps above 95 percent. Mining, electricity, manufacturing, and transport & storage have CIT gaps ranging between 75 and 90 percent. At the other end of the spectrum, information & communication and financial & insurance services have CIT gaps below 40 percent. While informality may explain some of the gaps observed (by narrowing the tax base), measures of informality suggest that this does not account for most of the gaps. Hence, a large portion of the tax gap is likely caused by generous tax incentives and potentially base erosion and profit shifting (BEPS).

Poor CIT performance has its roots in the extensive use of profit tax holidays to incentivize foreign investment. The Law on Income Tax allows the use of tax holidays, with the targeting criteria specified in the Law on Investment Promotion and the decree on its implementation.[72] The duration of profit tax holidays varies by type of business activity and location, ranging between 4–15 years. The length of tax holidays for investments in concession activities and special economic zones (SEZs) is not detailed in the legislation. In practice, profit tax holidays (including their duration) are negotiated on a case-by-case basis.[73] While these tax incentives are aimed at attracting investment, there has been no cost-benefit analysis to evaluate value for money.

Evidence suggests that firms do not rank tax incentives as the primary reason for choosing where to invest. The effectiveness of incentives largely depends on the investor's motivation for undertaking the investment. Surveys and empirical research often find that political stability, macroeconomic stability, the legal environment, and labor skills are the key determinants of FDI.[74] Incentives can be more effective for attracting investors in traditional export-oriented sectors (efficiency-seeking) since these are largely driven by competitive cost advantages in the host country. By comparison, investors are less responsive to incentives when mainly serving the domestic market (market-seeking) or drawing on natural resources (asset-seeking). In the case of the Lao PDR, many large investment projects are location-based, as they rely on the presence of natural resources (e.g., minerals and rivers) or the country's geographic position in Southeast Asia (e.g., for transport and logistics services). Therefore, addressing barriers to investment should focus on regulatory issues (e.g., licenses, permits, and immigration requirements), infrastructure (e.g., utilities and roads), and the quality of the labor force (e.g., skills).

Profit tax exemptions should be phased out and replaced by cost-based incentives. International evidence suggests that profit tax exemptions are highly inefficient. This is because tax holidays do not explicitly target investment, with the amount of tax relief often being disproportionate to the investment. In fact, firms can benefit even when they are not investing. The incentive heavily favors firms with high profits, which least need government support. This contributes to high redundancy of expenditure on incentives since an investor anticipating high profits would likely have proceeded in any case. Also, host governments face the risk of losing substantial revenue when a firm earns extraordinary profits. In addition, CIT holidays facilitate aggressive tax avoidance, as profit from investments that do not qualify for exemption may be artificially transferred through related party transactions. Profit-based incentives should be replaced by cost-based tax measures (e.g., accelerated depreciation and investment tax allowances or additional deductions), which reward companies only if they invest. The tax relief provided is often set as a percentage of investment expenditure. Following good international practice, tax incentives should be consolidated in tax laws, with clear and transparent eligibility criteria under the purview of the Ministry of Finance.

The need to reform tax incentives is high, given the upcoming global minimum corporate tax. More than 130 countries have agreed to start implementing a global minimum tax (GMT) rate in 2024.[75] The agreement aims to achieve a global minimum effective tax rate of 15 percent for multinational enterprises (MNEs) with a global turnover above 750 million euro.[76] The GMT does not directly obligate countries to adopt this rate, but it creates a strong incentive to raise CIT rates.[77] Countries that continue employing tax holidays and reduced rates are effectively giving

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[72] The 2009 Law on Investment Promotion introduced a range of tax incentives (e.g., profit tax holidays, reduced royalty rates, and import duty waivers on machinery, equipment, and raw materials) in selected sectors (e.g., mining and power generation). The duration of tax holidays in special economic zones (SEZ) is negotiable. The law was revised in 2017 to reduce the degree of discretion, but it is not clear how strictly this is being implemented. The law is currently under review.

[73] The Law on Investment Promotion allows for incentives beyond those stipulated by the law, which require approval of the National Assembly.

[74] See World Bank Global Investment Competitiveness Report 2020.

[75] These countries are members of the of the OECD Inclusive Framework on Base Erosion and Profit Shifting (BEPS). The G20 has endorsed this agreement.

[76] Even a small company operating in the Lao PDR that is a part of an MNE with a global turnover above the threshold will be subject to GMT.

[77] The first rule allows countries where the parent company of an MNE is taxable to impose a top-up tax on the profits of any foreign subsidiaries paying an effective tax rate of less than 15 percent. If the home country of the parent company chooses to impose a CIT rate of less than 15 percent, then the second rule allows the host country where the MNE subsidiary carries out its business activities to charge top-up taxes on the subsidiary.

away their taxing rights to FDI exporting countries or countries where MNE subsidiaries operate. Moreover, MNEs will no longer benefit from these tax incentives because there will be one or several countries that will bring their effective tax rate to 15 percent. Countries that provide generous tax incentives and do not act upon the GMT could lose out when other countries introduce domestic tax rules to top up under-taxed profits. Several countries in the region are advancing implementation (e.g., Australia, Japan, Korea, Malaysia, and New Zealand). Thailand and Vietnam are also considering the adoption of GMT for effectiveness in 2024.

The Income Tax Law does not provide a legal foundation for international taxation. There are no 'transfer pricing' rules or 'thin capitalization' rules in the 2019 Law on Income Tax, and there is no definition of a 'permanent establishment' (Box 3). There is no legal provision to require taxpayers to use arm's length pricing, or provide the authority for the MoF's tax department to audit the transfer pricing of MNEs or impose penalties to deter taxpayers from non-compliance. MNEs tend to shift profits more easily out of countries without transfer pricing legislation. Currently, all ASEAN countries have adopted transfer pricing legislation, except for the Lao PDR and Myanmar. As a result, Lao PDR is facing the risk of CIT tax base erosion due to non-arm's length (i.e., artificial) prices charged on transactions between related parties or excessive interest deductions.[78] There is also no provision for direct taxation of digital businesses operating outside the country but generating profit from the country's market.

Box 3: Definitions

Transfer pricing refers to the prices and other conditions used in transactions between related parties (e.g., goods, services, and capital). Although it is a legitimate practice for MNEs, it can be used to artificially shift profits between the members of an MNE (toward low tax jurisdictions) to lower overall tax obligations.

Thin capitalization is when a company is financed through a very high level of debt (compared to equity), which significantly lowers taxable profits because debt usually creates an interest expense that is deductible. Many countries have taken steps to counter this practice.

Permanent establishment is a term used in tax treaties between countries to define tax liabilities in each jurisdiction.

Arm's length pricing refers to the pricing of transactions between unrelated persons subject to normal market forces. Transfer pricing rules typically substitute 'arm's length pricing' for the actual pricing in transactions between related persons, for the purpose of computing taxable profit.

Personal income tax

The PIT regime has the feature of a dual income tax system, which includes a progressive tax schedule for labor income and a flat rate tax for capital income. Personal incomes are subject to a progressive PIT regime with rates ranging from 0 to 25 percent. The PIT is applied to all income earned in the Lao PDR from salary, wage, benefits in kind, and other remuneration, both for Lao nationals and expatriates, regardless of the length of their employment and stay in the country. The basic exemption for an employee earning a salary or wage income is 15.6 million kip. In 2021, the PIT exemption was higher than Myanmar's but lower than other regional peers in US dollar terms (Table 2.3). The threshold of the top PIT rate of 25 percent is 780 million kip, with a ratio of 32 (to GDP per capita). Domestic-source income from dividends, interest, capital gains, rent, and royalties is subject to withholding at different flat rates. Foreign-source capital income is currently exempt from taxation.

[78] While there is no data to quantify the tax erosion risk to revenues, some research indicates that this can be high. For instance, a study found a significant trade mispricing in Lao exports of copper concentrate and coffee beans during the period 2012–2017 (see "Commodity Trade Mispricing: Evidence from Lao PDR").

Table 2.3: PIT basic exemption (2021)

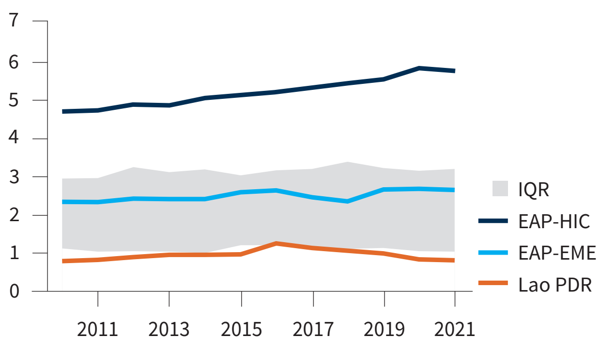
Country	PIT (%)	GDP pc (USD)	Exchange rate (avg.)	Exemption threshold			Highest threshold		
				LCU (‘000)	USD	Ratio	LCU (‘000)	USD	Ratio
Cambodia	20	1,625	4,099	15,600	3,806	2.3	150,000	36,597	22.5
Indonesia	30	4.333	14,308	-	-	-	5,000,000	349,451	80.7
Lao PDR	**25**	**2,536**	**9,698**	**15,600**	**1,609**	**0.6**	**780,000**	**80,430**	**31.7**
Malaysia	30	11,109	4	20	4,827	0.4	2,000	482,707	43.5
Myanmar	25	1,210	1,614	2,000	1,239	1.0	30,000	18,587	15.4
Philippines	35	2,70	49	250	5,076	1.5	8,000	162,421	46.9
Thailand	35	7,006	232	150	4,691	0.7	5,000	156,362	22.1
Vietnam	35	3,756	23,160	-	-	-	960,000	41,451	11.0

Source: PwC and World Bank staff calculations.

Note: PIT is the statutory top rate. The hyphen (-) indicates there is no zero percent tax bracket.

PIT collection is lower than most peer countries, while the PIT productivity ratio is also low. PIT collection steadily increased from 0.8 to 1.3 percent of GDP in 2010–2016 but gradually declined to 0.8 percent of GDP in 2021 (Figure 2.16). Despite increasing to 1.0 percent of GDP in 2021, it remains one of the lowest levels in the region. PIT productivity, calculated as the ratio of actual PIT collection (as a percentage of GDP) to the highest statutory marginal rate, provides a measure of tax efficiency. PIT productivity is estimated at 0.035, which is low when compared to peer countries (Figure 2.17). This suggests that PIT collection efficiency is low. This is partly due to a narrow tax base (due to a focus on payroll rather than income, profits, and capital gains) and high levels of informality.

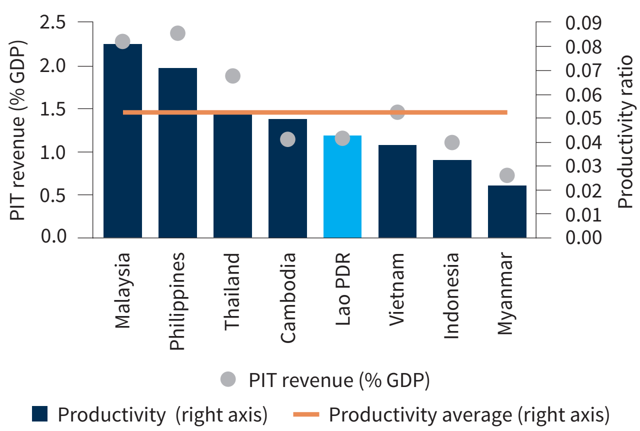
Figure 2.16: PIT collection (% GDP)



Source: International Monetary Fund and World Bank staff calculations.

Note: IQR: interquartile range, EAP-HIC: East Asia and Pacific, high-income countries, EAP-EME: East Asia and Pacific, emerging market economies.

Figure 2.17: PIT productivity ratio (2016–21)



Source: International Monetary Fund and World Bank staff calculations.

The 2019 Law on Income Tax has addressed several weaknesses of the PIT regime, but further improvements are needed. Taxes on labor income are now paid on a monthly basis but only reconciled annually. This helps deal with the volatility of monthly income and the risk that taxpayers artificially smooth their income to avoid the higher tax rate (e.g., year-end bonuses). The new law also simplified the tax rate schedule from six to five tax brackets, which can help improve compliance. However, tax brackets are not indexed to inflation. This may result in ‘bracket creeping’, as inflation erodes real wages and wage earners are subject to higher tax rates. Given low average incomes and higher informality when compared to other countries in the region, reforms should focus on enhancing efficiency and fairness. For instance, the PIT system could be simplified through a further reduction of the number of tax brackets (from five to four), which could help improve the efficiency of the PIT regime. In addition, tax brackets should be indexed to inflation to avoid bracket creeping.

2.3.2 Consumption taxes

Value-added tax

The statutory VAT rate was reduced from 10 to 7 percent in 2022, significantly undermining tax collection. The VAT was introduced in 2010 with a 10 percent rate, with some products being zero-rated. The 2021 amendment of the Tax Law introduced several changes to the VAT regime. The applicable VAT rate on the import of goods and services, supply of goods and services in the Lao PDR, and export of services was reduced from 10 to 7 percent from January 2022. The supply of goods outside a special economic zone (SEZ) by an enterprise registered for operation in the SEZ became subject to VAT.[79] Activities currently exempted from VAT include electricity imports, electricity supplied to any electricity enterprise within the country, and electricity and minerals exported overseas or to SEZs.

The VAT regime includes numerous exemptions, which pose several drawbacks. VAT exemptions create economic distortions by benefiting some sectors more than others.[80] Businesses unable to credit input VAT because they buy inputs from exempt businesses experience increased costs. On the other hand, if the exemption is applied at the end of the supply chain, it reduces VAT revenues. These negative effects of VAT exemptions make it important to examine the rationale for all exemptions.

VAT collection is relatively low compared to most regional peers, and so is VAT productivity and c-efficiency. VAT revenue dropped from 4.3 to 2.7 percent of GDP between 2015–2020, before recovering to 3.1 percent of GDP in 2021 (Figure 2.18). This was partly due to the economic slowdown (including COVID-19) but also VAT exemptions on imports of capital goods related to some investment projects. VAT collection declined to 2.7 percent of GDP in 2022, owing to the reduction in the VAT rate from 10 to 7 percent, which more than offset higher consumer prices. Although the VAT accounts for a significant share of domestic tax revenues, VAT collection is comparatively lower than in most ASEAN countries. In fact, it was the lowest revenue among peers with the same VAT rate, implying that it is underperforming considerably (Figure 2.19). Thailand collected 3.4 percent of GDP from VAT, even with a rate of 7 percent. Moreover, VAT productivity and c-efficiency have also been relatively low (Figure 2.20 and Figure 2.21). VAT productivity (0.35) and c-efficiency (0.64) were lower than the EAP average (0.44 and 0.67, respectively).

The recent reduction of the VAT rate has already had a negative impact on tax collection. The government reduced the VAT rate from 10 to 7 percent in January 2022, with the declared aim of expanding the tax base (by providing a stronger incentive for tax registration) and providing temporary relief to ease the impact of COVID-19. Meanwhile, the authorities tried to balance this cut with excise rate increases for selected products. However, since the rate increases were small, applied on a very narrow tax base, and subject to exemptions, the revenue gains are not sufficient to compensate for the VAT reduction of 3 percentage points on most goods and services. The VAT revenue loss is estimated at about 1 percent of GDP in 2022, while there is little evidence of an impact on consumer prices.[81] The 2021 revision of the Law on Income Tax aims to promote formality by encouraging SMEs to register for VAT through a favorable income tax regime. However, revenue increases through formalization will not be significant (as the experience of other countries suggests), since most VAT revenue comes from large (formal) taxpayers. Moreover, tax cuts may not necessarily lead to greater VAT registration due to other factors (e.g., additional costs such as bookkeeping).

Several VAT exemptions should be reviewed for elimination, particularly those that are costly. While some VAT exemptions for public services (such as health care and education) could be retained, other exemptions should be removed. For example, agriculture and forestry are common exemptions in developing countries, mainly because of the small scale of most agricultural activities and the low income of most people engaged in them. However, there are large agribusinesses and forestry operations in the Lao PDR that generate substantial revenues. Subjecting these sectors to the standard VAT regime is highly advisable. Small farmers will not be affected by this change, as they would be under the VAT registration threshold of 400 million kip. Subjecting these goods to VAT could allow producers and traders to claim credit for input VAT, improving efficiency.

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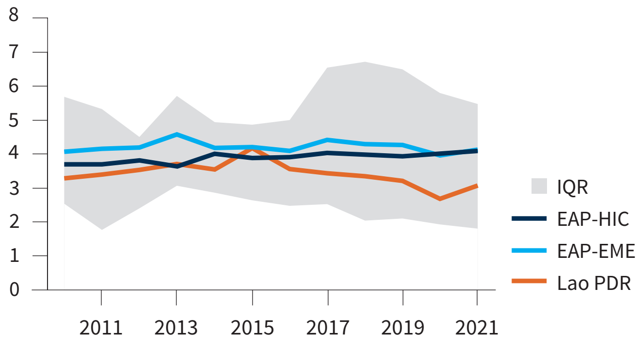
79 Previously, only the supply of services outside a SEZ by a SEZ registered enterprise was subject to VAT.

80 It is challenging to estimate foregone VAT revenues. For instance, VAT paid by businesses at importation (to customs department) is deducted from output VAT collected (by tax department), so there is a need to combine different data sources. Also, not all VAT exempted at the importation is revenue foregone. For example, large infrastructure projects are entitled to VAT refunds, since input VAT will be accumulated while output VAT is zero (in the development phase), so the VAT exemption at importation is merely to support cash flows and avoid VAT refund claims.

81 There was no discernible impact on the consumer price index. Even if the VAT rate reduction was fully passed on to consumers, consumer prices would only be reduced by 3 percent, while VAT revenues are immediately cut by 30 percent. Limited revenue contributes to depreciation pressures, which are much more impactful on consumption.

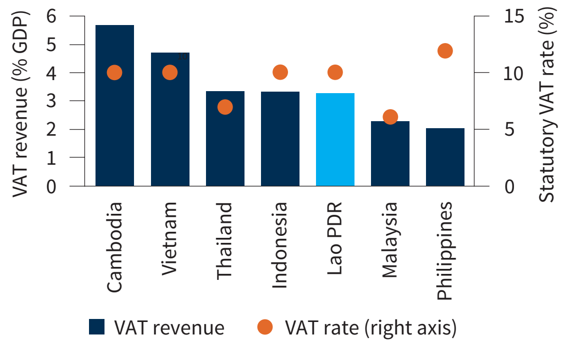
The management of VAT refunds needs to be improved to avoid negative impacts on businesses. The cost of VAT falls on businesses when refunds are not processed in a timely manner. A significant improvement in the amended 2018 Law on VAT was that all VAT taxpayers with a net credit could claim a VAT refund. Previously, only exporters and large-scale investors were entitled to VAT refunds, and all other taxpayers had to carry forward the excess input credits. However, there are challenges with the administration of VAT refunds. All refunds are subject to examination prior to the VAT refund decision. Businesses have experienced substantial delays in obtaining refunds, sometimes of more than one year. The VAT refund process could be improved through the adoption of a risk-based approach, improvements in the TaxRIS system to support VAT management, and adequate budget allocations for VAT refunds.

Figure 2.18: VAT collection (% GDP)



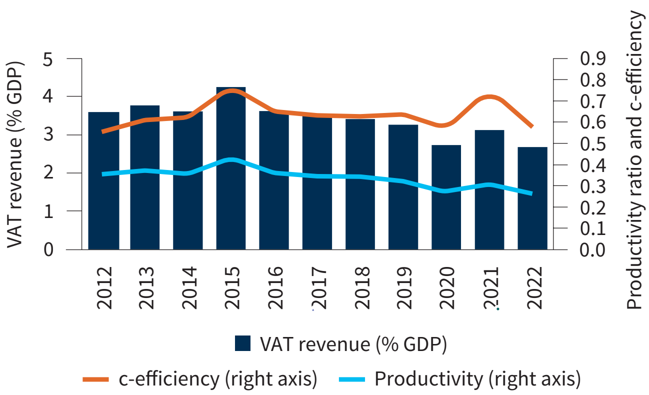
Source: International Monetary Fund and World Bank staff calculations.

Figure 2.19: VAT rate and collection (2016–21)



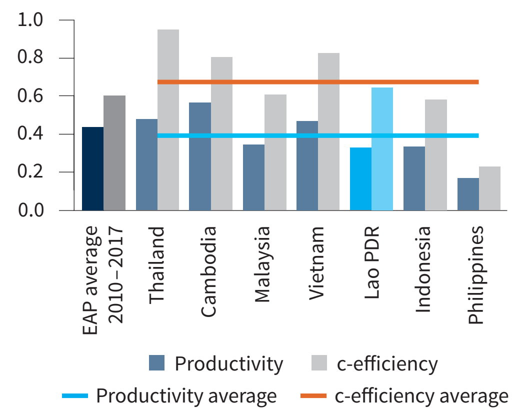
Source: International Monetary Fund and World Bank staff calculations.

Figure 2.20: VAT revenue, productivity, and c-efficiency



Source: Ministry of Finance and World Bank staff calculations.

Figure 2.21: VAT productivity and c-efficiency (2016–21)



Source: Ministry of Finance, USAID, and World Bank staff calculations.

Excise tax

Excises are levied on several products and services, mainly through ad valorem taxes. Excise taxes are applied to a wide range of domestic and imported goods and services, which are paid at importation and by domestic producers before releasing the products for distribution. Most excises use an ad valorem rather than a specific tax structure, with rates ranging from 3 to 110 percent. Some tax rates have fluctuated considerably over time, through both increases and reductions (Table 2.4). Fuel excise rates have gradually increased through time, despite some volatility, although they have been recently cut as a response to higher international fuel prices and exchange rate depreciation. Excise rates on vehicles (e.g., motorcycles and transport vehicles) vary significantly according to their engine volume. Alcoholic and non-alcoholic excise rates have increased marginally in the past 10 years. Tobacco has a mixed tax structure, with both ad valorem and specific taxes. However, some of these taxes are subject to reduced rates or exemptions under investment agreements. Moreover, some rates are levied at the early stages of the supply chain, which results in low effective tax rates.

Table 2.4: Selected excise rates (%)

	Product	2012	2019	2022
Fuels	Gasoline (super)	25	35	40
	Gasoline (normal)	20	30	31*
	Diesel	10	20	21*
	Kerosene (for aircraft)	10	8	8
Vehicles	Motorcycles (depending on engine volume)	10–25	25–100	28–110
	Transport vehicles (depending on engine volume)	-	25–90	26–102
	Speed boats, yachts, motorboats	15	20	25
Beverages	Alcoholic beverages (depending on alcohol content)	60–70	50–70	62–70–80
	Beer (depending on alcohol content)	50	50	20–60
	Non-alcoholic beverages (e.g., soft drinks, sodas, fruit juices, etc.)	5	5	7
	Non-alcoholic beverages (energy drinks)	10	10	12
Tobacco	Cigarettes	60	50	57**
	Tobacco (shredded)	60	35	42

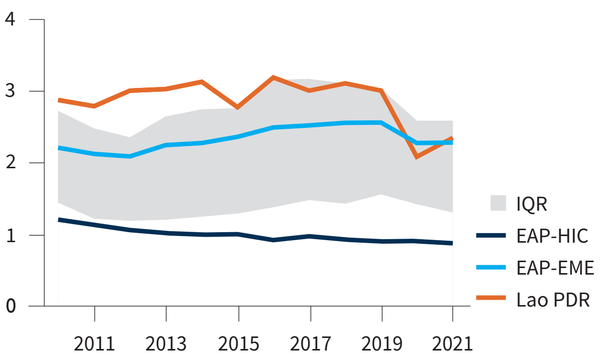
Source: Ministry of Finance, DFDL Co. Ltd. and VDB-Loi Co. Ltd.

Note: * Rates were significantly reduced in mid-2022 to 16 percent for normal gasoline and 0 percent for diesel. ** The rate can be reduced to 15 or 30 percent under an investment agreement. Some of these products are also subject to a specific tax per unit (e.g., cigarettes).

In most countries, excises are limited to a narrow set of goods with inelastic demand or negative internalities and externalities. Inelastic demand for a good makes its taxation convenient because the increase in consumer prices caused by the excise does not reduce demand to a significant degree.[82] Moreover, the negative internalities and externalities of some goods mean that their consumption has negative effects on the consumer and society. For example, fuel consumption creates pollution, tobacco creates health problems, and alcohol creates both health problems and anti-social behavior.[83] Taxing these goods more heavily than normal goods discourages their use (increasing overall social welfare) while also generating sizable revenues. However, the current tax level and tax structure are not sufficient to reduce the negative effects of these products and support revenue mobilization.

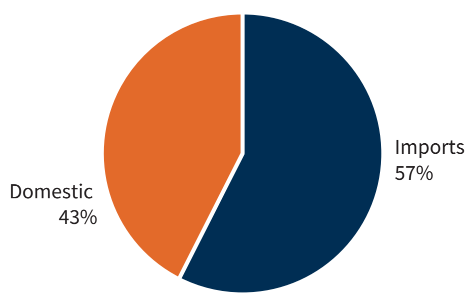
Excises comprise an important share of tax revenue, and collection is relatively high compared to regional peers. Excise revenue collection averaged 3 percent of GDP during 2010–2019, although it declined to 2.1 percent of GDP in 2020, partly due to the COVID-19 pandemic. This is reasonably high by regional standards (Figure 2.22). In 2022, revenue collection benefited from higher domestic and international prices, but this was partly offset by fuel excise rate reductions in mid-2022. Excises accounted for 23 percent of total tax revenues in 2021–2022. It is thought that most of the excise revenue accrues from vehicles and fuel, and thus collected from imports (Figure 2.23). The relative contribution of excises is high because the overall tax system generates relatively small revenue.

Figure 2.22: Excise collection (% GDP)



Source: International Monetary Fund and World Bank staff calculations.

Figure 2.23: Excise collection by source (2016–21)



Source: Ministry of Finance and World Bank staff calculations.

[82] Nonetheless, raising taxes too much could lead to lower revenue collection, due to a higher incentive to evade tax.

[83] 'Health taxes' are excises applied to products such as tobacco, alcohol, and sugar-sweetened beverages that cause health-related problems to individuals and society more broadly. These are one of the most cost-effective ways to reduce consumption of unhealthy products while raising much-needed revenue.

Recent reductions in fuel excise rates have produced large foregone revenues, while the tax structure could also be improved. An ad valorem excise is levied on several fuel types. It is estimated that recent rate cuts have generated losses (i.e., foregone revenues) of over $160 million between mid-2022 and mid-2023. While these measures were introduced to protect consumers from inflation, these cuts have predominantly benefited wealthier households. In addition, fuel imports reported by the Lao PDR are much lower than that reported by trading partners (e.g., Thailand and Vietnam). This suggests that a significant amount of fuel is not being taxed, which generates considerable revenue losses. Finally, as the price of fuels fluctuates frequently, the resulting excise revenue may not correspond to the externalities produced by fuel consumption. An alternative is to apply a specific tax system on fuel, whereby the specific tax considers the costs of air pollution, carbon emissions, vehicle accidents, congestion, and road damage, among others.

The Lao PDR has among the lowest tobacco taxes and prices in the region. The excise tax on tobacco accounts for 11 percent of the retail price of the most sold brand in 2020, the lowest in the region. This is much lower than the WHO's recommendation that excise taxes on tobacco should account for at least 70 percent of retail prices. Furthermore, the Lao PDR has the second-lowest retail prices in both US dollar and PPP-adjusted terms. Concerningly, cigarettes have become considerably more affordable in recent years. The most sold brand is nearly twice as affordable in 2020 when compared to 2010. Data for alcohol and non-alcoholic beverages were not available to conduct a similar analysis.

The tax structures for tobacco, alcohol, and non-alcoholic beverages can be improved. Tobacco has a mixed tax structure with a specific tax of 600 kip per pack of 20 cigarettes and an ad valorem rate of 57 percent of ex-factory prices (for domestic production) or the cost, insurance, and freight (CIF) price (for imports).[84] However, most cigarettes qualify for a 15 percent tax rate due to an investment agreement. Alcohol and non-alcoholic beverage excises are ad valorem applied to the ex-factory price for domestically produced goods and the CIF price for imported goods. Alcohol taxes are based on alcohol content, with tiers employed for beer with alcohol content above or below 5 percent. The most recent rates for other alcoholic beverages employ tiers with alcohol content below 10 percent, between 10 and 23 percent, and greater than 23 percent. Ad valorem taxes are considered less effective than specific taxes. From a fiscal perspective, they are more difficult to collect, more prone to tax avoidance and evasion, and result in less stable and lower revenue streams. From a health perspective, they result in lower prices on cheaper brands, which promotes consumption and makes products more accessible to vulnerable populations (e.g., youth, poor, and people with alcohol use disorders). Furthermore, tax increases are less effective since they provide greater opportunities for users to trade down to cheaper products to avoid the tax increase. The global trend indicates that modern tax administrations are leaning toward a simplified specific excise tax structure with indexation to maintain the value in real terms for all three products.[85]

The weakness of ad valorem taxes is compounded by applying them early in the supply chain. Using wholesale/ex-factory price or CIF as a tax base invites tax avoidance and evasion, since this information is provided by manufacturers and importers that have an incentive to lower their tax liability. Using retail price as the tax base is preferable because these can be verified independently by the authorities. However, this is still a less effective policy option compared to higher uniform specific taxes.

The current tax administration of the excise regime could be strengthened, especially for the cigarette market. A 25-year Investment License Agreement (ILA) signed in 2001 between the government and two tobacco companies established a joint-venture cigarette manufacturer. Under the ILA, the joint venture benefits from a reduced excise tax rate on tobacco products (15 percent of production costs if less than 1,500 kip per pack, and 30 percent if greater than 1,500 kip per pack) and exemptions from other taxes. Local tobacco companies are not complying with the mandatory contribution to the Tobacco Control Fund established in 2013.[86] The government should seek legal support to revoke or not renew the ILA. Furthermore, additional improvements would help to manage or mitigate potential losses associated with the lack of compliance (e.g., strengthened audits, enhanced data inputs and analytics, and a revised system of physical excise stamps leveraging digital technology).

The list of goods and services subject to excise taxes could be reviewed for rationalization. While many goods are subject to excise taxation, their rationale is not always clear since many do not produce significant

[84] Since the ad valorem tax is levied early in the supply chain, the excise collection as a share of retail prices is significantly lower. In 2022, the tax stamp fee was increased from 5 kip to 500 kip, but it appears to be collected unevenly.

[85] The indexation of specific unit taxes averts revenue erosion when the prices of excise goods increase. Unit rates can be indexed to inflation.

[86] The fund is supposed to receive 2 percent of the profit of tobacco companies and an additional 200 kip levied on each cigarette pack.

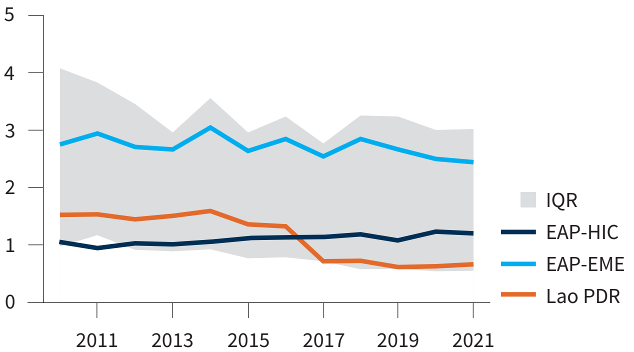
internalities or externalities. It is important to ensure that all goods and services in the excise list are worth the administrative and compliance costs that their collection entails. Excises can only be justified if they raise a reasonable amount of revenue and correct internalities or externalities.

2.3.3 Other taxes

International trade taxes

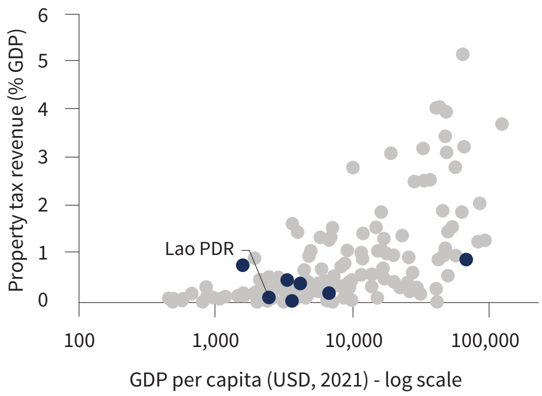
Revenues from trade taxes have been on a declining trend over the last ten years. Most trade taxes are derived from import duties. Revenue from trade taxes averaged 1.5 percent of GDP between 2010 and 2016 and sharply declined to about 0.7 percent of GDP since 2017 (Figure 2.24). This value increased to 1.2 percent of GDP in 2022, owing to rising imports (driven by higher prices), but it remains one of the lowest in the region. Trade tax rates have been reduced trough time. The average tariff rate applied (weighted mean) declined from 14 to 1 percent between 2000–2020, partly due to growing regional integration (particularly in ASEAN) and the World Trade Organization accession in 2013. However, this does not explain the performance gap to other countries in the region. Instead, generous tax incentives for large investments have significantly undermined trade tax collection.

Figure 2.24: Trade taxes collection (% GDP)



Source: International Monetary Fund and World Bank staff calculations.

Figure 2.25: Property tax collection (% GDP)



Source: IMF and World Bank staff calculations.

Note: Blue dots represent ASEAN countries.

Land and property taxes

Effective land tax rates are low, which considerably undermines revenue collection. The land tax exhibits low non-buoyant revenues, as tax amounts are determined by land type and size rather than land value. This is accompanied by rising tax inequity across land tax parcels and high economic and administrative inefficiencies. The unit tax rates are very low and have not been updated since 2007. Considering that land prices are rising rapidly, especially in urban areas, the effective tax rate for commercial and industrial land is estimated to range from about 0.005 to 0.01 percent. For instance, commercial land parcels in the Saysettha District (in Vientiane Capital) are estimated to pay an effective tax rate of 0.01 percent (maximum of 300 kip/m^2 on land valued at 3 million kip/m^2), while industrial land has an effective tax rate of 0.006 percent. In the same area, residential land owners pay an effective tax rate of 0.003 percent (80 kip/m^2).[87]

The revenue collected through the land tax is very low, but there is potential to enhance revenue mobilization. The land tax generated revenue equivalent to about 0.1 percent of GDP in 2021. This is very low by international standards, as similar taxes have generated 0.3–0.6 percent of GDP in low- and middle-income countries and up to 2–3 percent of GDP in several advanced economies (Figure 2.25). In 2016–2019, land tax collection ranked the second-lowest in the region (only behind Vietnam, where land tax rates are very low) and much lower than the average for the EAP region. These benchmarks suggest there is considerable potential to increase land tax revenues.[88]

[87] An analysis of land taxpayers in one village in Saysettha District shows they were paying a median land tax of 100,000 kip per year, with individual land tax bills ranging from 12,000–1,664,000 kip per year.

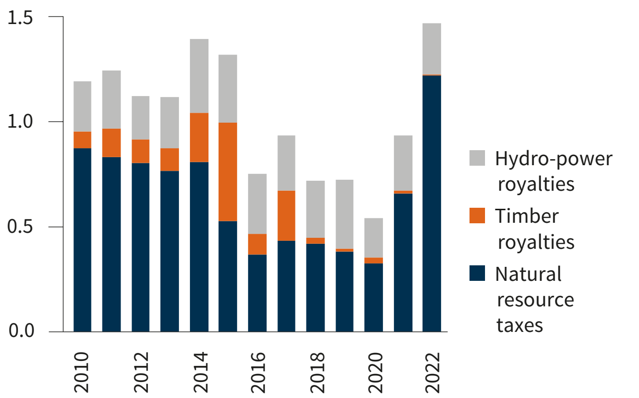
[88] Revenue could possibly double to 0.16 percent of GDP within 3–5 years, and perhaps double again to over 0.3 percent of GDP within 10–12 years.

To improve revenue mobilization, the unit rates should be revised and subsequently adjusted on a regular basis. Based on international norms, the effective tax rate should range between 0.1–0.2 percent for residential constructed land and between 0.3–0.5 percent for non-commercial/industrial constructed land. This would require a revision of the current unit rates, followed by adjustments on a periodic basis (e.g., every 3–5 years). These unit rates should be calibrated to the underlying absolute real land values. Capturing the absolute and relative changes in the underlying real land values would improve revenue buoyancy and the yield of land taxes. It would also improve taxpayer equity across land parcels and the cost efficiency of the land tax administration. Developing and implementing an adequate land valuation system will be key to supporting tax collection.

Natural resource taxes & royalties

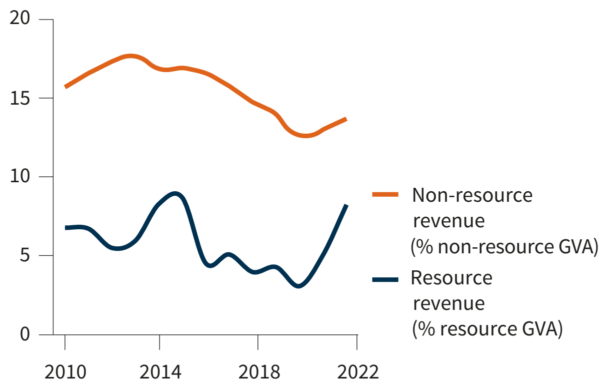
Revenue from natural resources has recently increased, but it remains low considering the weight of the sector in overall economic activity. Natural resource taxes & royalties declined from 1.4 to 0.5 percent of GDP during 2010–2020, but they have subsequently risen strongly to 1.5 percent of GDP in 2022 (Figure 2.26). Natural resource taxes mainly relate to mining activities. These revenues have increased partly due to a sharp exchange rate depreciation, since they are mainly collected in foreign currency, as well as higher production. Timber royalties were sizable in the mid-2010s, peaking at about 0.5 percent of GDP in 2015, but have recently become negligible.[89] Hydropower royalties have been relatively stable, at about 0.3 percent of GDP. However, this is very small compared to the level of investment and revenue generated by the hydropower sector. Overall, revenue collection has not kept pace with the exploitation of natural resources (e.g., mining and hydropower) and their contribution to economic growth, largely due to widespread and generous tax incentives (Figure 2.27).

Figure 2.26: Natural resource taxes & royalties (% GDP)



Source: Ministry of Finance and World Bank staff calculations.

Figure 2.27: Resource and non-resource revenue (% GVA)



Source: Ministry of Finance and World Bank staff calculations.
Note: Resources include forestry, mining, and electricity.

There is a need to undertake a comprehensive review of the regimes for natural resource revenues. The weak performance of natural resource revenues can be explained by the volatility of commodity prices, the complexity of tax arrangements, and the generous tax incentives provided by investment promotion policies or negotiated concession agreements. Domestic revenue improved significantly in the period 2003–2014, partly as strong commodity prices (e.g., copper and gold) led to significant investments in mining. Lower commodity prices and dwindling production have undermined revenues in recent years. Moreover, it is difficult to conduct a detailed assessment in the absence of relevant data on tax incentives. Given the importance of the sector to the economy, a comprehensive review of the legal framework and implementation arrangements of natural resource revenues is warranted to inform a reform agenda.[90]

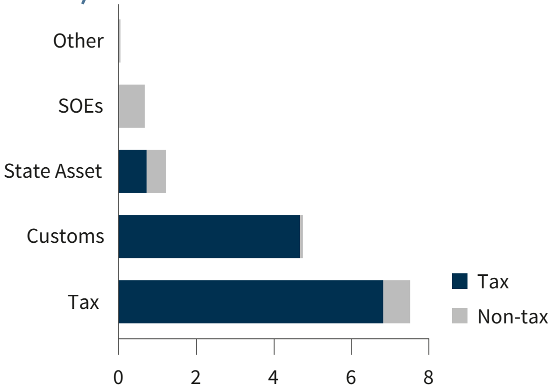
[89] This decline might be related to the rise in Forest Preservation Funds. Despite new legislation, policies, and plans to promote economic development through socially and environmentally sustainable forest management, illegal logging remains a challenge. There remain risks associated with the land allocation process (i.e., granting concessions).

[90] The government was expecting to collect significant revenues from cryptocurrency mining and trading, but these have not materialized.

2.4 Tax administration

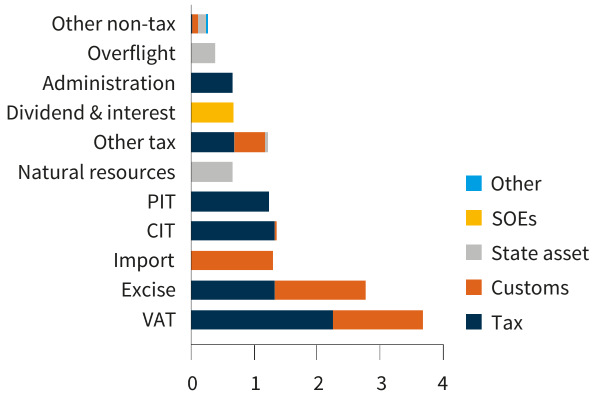
Domestic revenue is collected by several departments of the Ministry of Finance, but transparency has declined. Budget transparency has deteriorated in recent years, as the amount of information published in the state budget implementation reports has been considerably reduced, particularly for revenue. Detailed information on revenue collection ceased to be published in 2017 (e.g., disaggregation by province and department). Data for 2016 suggests that the MoF's tax and customs departments collect most of the revenue, although the state asset and SOE departments still collect important amounts (Figure 2.28). The tax department collects most income taxes (i.e., CIT and PIT) and administrative fees, as well as part of VAT and excises (Figure 2.29). The customs department collects VAT and excises at the border (levied on imports), as well as import duties. The state asset department receives natural resource revenues and overflight fees, while the SOE department collects dividends and interest from corporations with state equity. More granular information would be critical to evaluate tax performance over time.

Figure 2.28: Domestic revenue by department (2016, % GDP)



Source: MoF and World Bank staff calculations.

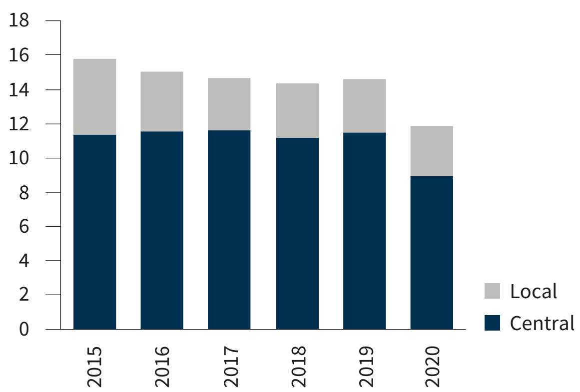
Figure 2.29: Domestic revenue (2016, % GDP)



Source: MoF and World Bank staff calculations.

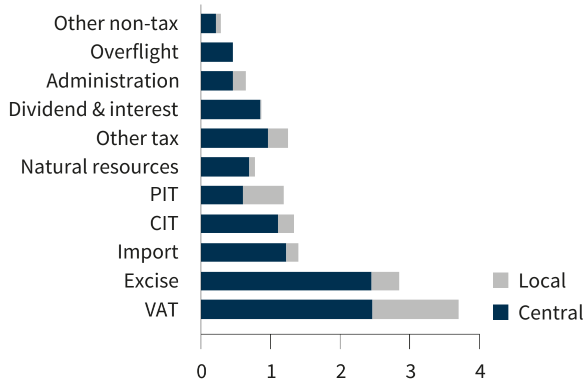
A significant amount of revenue is collected at the sub-national level, but further decentralization may create challenges. Most domestic revenue is collected at the central level, but local authorities have been collecting considerable amounts (Figure 2.30). There have been different waves of decentralization and recentralization of revenue collection over the past few decades. Local authorities collected significant amounts of PIT and VAT in 2016 (Figure 2.31). There has been a recent move to place many large taxpayers under the responsibility of provinces, with a view to support self-sufficiency. However, this can create inefficiencies and weaken existing controls.

Figure 2.30: Domestic revenue (% GDP)



Source: MoF and World Bank staff calculations.
Note: Data includes asset sales and capital return.

Figure 2.31: Domestic revenue (2016, % GDP)



Source: MoF and World Bank staff calculations.

The administration of taxes has generally improved in recent years, but there remains considerable room to further enhance performance. The implementation of the Tax Revenue Information System (TaxRIS) provides a good platform to modernize the tax administration, particularly with the aim of improving the efficiency of tax collection, reducing leakages, and increasing revenue. Nonetheless, the current system lacks critical features (e.g., automated late filing/payment notice, automated risk analysis, and data analysis capabilities) and staff are not using all functionalities. The approval of the Tax Administration Law has strengthened the legal framework, but it is crucial to ensure that the law is adequately implemented. Efforts to build the capacity of tax officials are aimed at increasing operational efficiency. However, developing a modern, efficient, and effective tax administration requires further improvements in processes, technology uptake, staff capacity, and transparency.[91]

There is no strategic planning function at the central level, which likely undermines tax performance. Strategic plans should cover all aspects of the tax administration and must be revisited regularly, since the operating environment is not static. There is a division in the MoF's tax department responsible for planning, but it has not yet performed activities typically performed by a modern tax administration. Effective strategic planning would enhance operational performance and facilitate the allocation of scarce resources to areas that pose greater compliance risks. This should cover all core business activities and take into consideration the environment in which the tax administration operates.

The tax department has not yet adopted a comprehensive risk management framework. A risk-based audit approach has been piloted in the past several years. A risk-based analysis unit has been established, but the concept of risk management is limited to the audit function at headquarters and the Vientiane Capital tax office, although there is a plan to expand implementation to other provinces. There is a need to develop and implement a comprehensive compliance improvement strategy and the related annual compliance improvement plans across tax administration functions.

Recent changes are likely undermining compliance risk management, particularly for large taxpayers. It is critical to adequately manage the special risks that large taxpayers pose (e.g., by ensuring consistency of treatment for a corporation that has subsidiaries and branches in different provinces). Centralizing the management of large taxpayers in a single unit would significantly improve tax compliance and efficiency. International evidence shows that, on average, large taxpayer offices or programs employ less than 10 percent of total revenue staff and collect over 50 percent of revenue.[92] Most tax administrations in advanced economies and the EAP region have dedicated large taxpayer offices (LTOs).[93] However, current arrangements are limited in the Lao PDR. The MoF's revenue management division at headquarters previously assumed the management responsibility of about 400 large taxpayers, but this has been undermined by the reallocation of responsibilities for many taxpayers to provinces. Recent organizational changes (e.g., the split of the revenue management division) represent a further deviation from good international practices.

Tax audits can increase compliance, but there is a significant gap between current and good international practices. Tax audits are undertaken for several reasons, such as detecting and redressing individual cases of non-compliance. They also promote voluntary compliance by increasing the probability of detection and penalties for non-compliant taxpayers. Moreover, they enable the gathering of information on the performance of the tax system and the evasion techniques used by taxpayers. Finally, audits provide an opportunity to educate taxpayers on their legal obligations and bookkeeping requirements, thereby improving future compliance. However, there is currently a significant gap between current audit processes and good international practices. For instance, there is no structured approach to audit planning and implementation, and no systematic cross-checking using third-party information (e.g., customs data). Moreover, tax inspectors are routinely rotated from and to non-audit functions, which is not efficient.

Audit strategies need to be developed within the context of compliance risk management. Compliance risk management is a structural process for the systematic identification, assessment, ranking, and treatment of tax compliance risks. The tax administration should seek to maximize voluntary compliance (e.g., through taxpayer assistance and education programs), but it must also have effective enforcement strategies to deter, detect, and address non-compliance. The level of scrutiny and intensity of audit activity should depend on the level of risk to revenue, which is related to the segment where the risks occur. Segments may be based on business size (e.g., large taxpayers), industry (e.g., mining), or the type of tax (e.g., corporate income tax). Different types of audits are appropriate for different objectives, aiming to focus tax audits on taxpayers that pose a higher risk to revenue.

[91] Using the World Bank's Tax Administration Index tool would provide a brief assessment of the revenue administration.

[92] IMF Revenue Administration Fiscal Information Tool (RA-FIT).

[93] See the OECD report "Tax Administration 2015" and the ADB report "A Comparative Analysis of Tax Administration in Asia and the Pacific".

Modern tax administrations are increasingly using technology to support audit operations. Tax administrations are leveraging new technologies to combine automated audits with comprehensive ones (e.g., to detect fraud). This allows increases in audit coverage and risk perceptions, as well as a better allocation of resources. Higher compliance rates are often achieved when information from third-party sources is systematically matched with the information contained in tax returns. Tax administrations are increasingly using big data to effectively monitor compliance with tax obligations. Recent advances in artificial intelligence are already being deployed in this area.

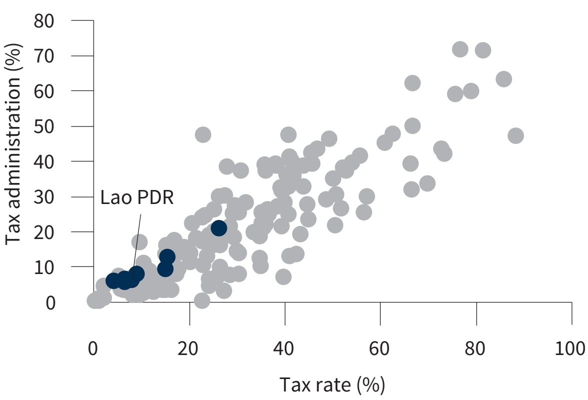
Taxpayer services can improve tax compliance, but there is currently no dedicated unit or strategy to deliver these services. Taxpayer services can be defined as a set of strategic initiatives to assist taxpayers in complying with their tax obligations. These often comprise outreach and tax education programs. Taxpayer services and information can be tailored by taxpayer segments, based on attitudes and the underlying factors of non-compliance. Tax administrations often set service delivery standards and measure performance (e.g., time to answer taxpayer inquiries, process tax refunds, and resolve disputes). While some services are currently provided to support the rollout of TaxRIS (e.g., e-filing and e-payment), there is no dedicated unit or strategy to provide services in support of voluntary compliance.

The collection of taxpayer data is insufficient, and there is limited access to third-party information. Tax returns provide limited information for compliance and analytical purposes. For instance, the CIT return form is one-page long and only includes eight data fields. It does not provide information on financial performance (e.g., turnover, investment, and depreciation) or relevant information to estimate the cost of tax incentives (e.g., income subject to CIT and exempted income). In comparison, the CIT return form in Cambodia is 20 pages long and has over 100 data fields. The absence of relevant information precludes assessments of tax policy (e.g., estimation of tax expenditures). Moreover, the MoF's tax department does not have access to third-party information, except for customs data. Even then, customs data is rarely used for systematic cross-checking. Therefore, it is crucial to improve data collection, integration, and analysis to strengthen evidence-based policy making.

Adequate staff levels and capacity are critical to perform the different functions of a modern tax system. An efficient and effective tax administration requires a solid regulatory framework, clear processes, suitable technologies, and adequate staffing. While capacities are low, the transition to electronic filing and payment provides an opportunity to reallocate staff resources. The staff levels needed in return processing will decline with the increasing uptake of electronic processing. With appropriate training programs, staff can be re-trained to work in other functions currently under-resourced, such as taxpayer services, debt management, or even audit.

The tax administration places a significant burden on business, while corruption is a major concern. Only a small proportion of firms identified tax rates or tax administration as a major constraint to their business (Figure 2.32). The former is not surprising, owing to low statutory tax rates and the widespread granting of reduced rates and exemptions. However, complementary evidence suggests that businesses need to make a significant number of tax payments per year, which require a considerable amount of time to prepare, file, and pay (Figure 2.33). The total tax and contribution rate is relatively low as a share of profits, but the post-filing score is also low,

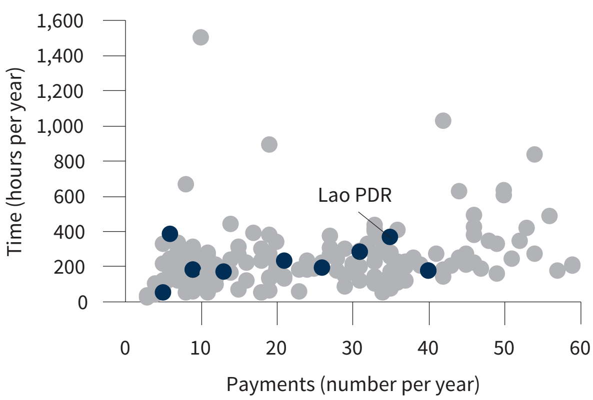
Figure 2.32: Firms identifying tax as a constraint (%)



Source: World Bank Enterprise Surveys.

Note: Blue dots represent ASEAN countries.

Figure 2.33: Burden of paying taxes

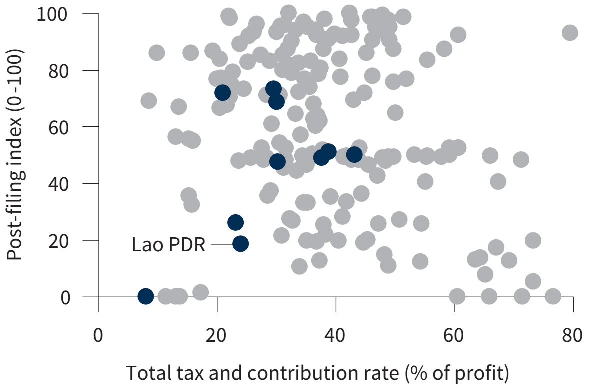


Source: 2020 Paying Taxes.

Note: Horizontal axis restricted to 60 to improve readability.

suggesting challenges with VAT refunds and CIT corrections (Figure 2.34). Most firms (85 percent) were visited or required to meet with tax officials, with an average of three visits per year, which is higher than regional and income averages. Concerningly, a significant proportion of firms (35 percent) were expected to give gifts in such meetings, the eighth largest value of 155 countries (Figure 2.35). Accelerating the modernization of the tax administration (e.g., through further digitization and adoption of a risk-based approach) would help reduce bureaucracy, as well as mitigate corruption and tax fraud.

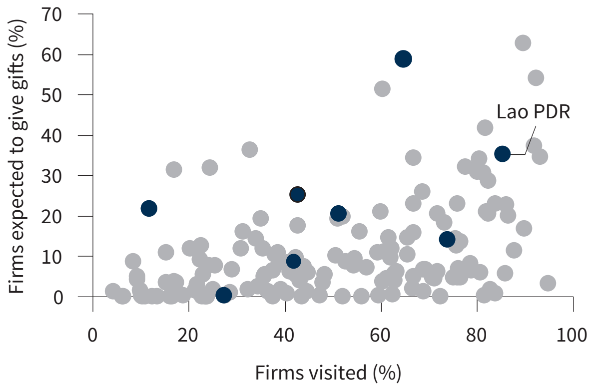
Figure 2.34: Tax burden and post-filing



Source: 2020 Paying Taxes.

Note: Horizontal axis restricted to 80 to improve readability.

Figure 2.35: Corruption in tax collection



Source: World Bank Enterprise Surveys.

2.5 Conclusion and recommendations

Revenue collection has deteriorated considerably in the past decade, constraining fiscal space and undermining fiscal sustainability. Revenue performance was a concern even before COVID-19, as total revenue declined from 22 to 16 percent of GDP during 2014–2019, owing to declines in tax collection and foreign grants. Tax revenue fell from 14 to 11 percent of GDP in that period. Low tax rates, a narrow tax base, and weak compliance and enforcement have undermined tax collection. In particular, generous tax exemptions have deprived the budget from vital fiscal revenues and foreign exchange. Total revenue declined further to 13 percent of GDP in 2020, mostly because of the COVID-19 pandemic, although it recovered to 15 percent in 2022, partly supported by inflation. Revenue levels remain very low by regional and income standards. In 2019, revenue-to-GDP and tax-to-GDP ratios ranked in the bottom 15 percent of the world, and these have deteriorated further since then. Recent measures, such as tax rate cuts and growing fragmentation in the management of large taxpayers, have further hampered revenue mobilization. At 11 percent in 2022, the tax-to-GDP ratio is significantly below the recommended minimum international benchmark of 15 percent. These trends have reduced fiscal space for critical public spending, while threatening fiscal sustainability.

Revenue collection has relied heavily on consumption-related taxes, while limited income tax collection accounts for most of the performance gap. In 2022, about three-quarters of government revenue was collected through taxes. Indirect taxes accounted for most tax revenue, with the VAT and excises representing 29 and 25 percent of total tax revenue in 2018–2022, respectively. These are consumption-based taxes levied on the purchase of goods and services. Direct taxes averaged 23 percent of tax revenue in the same period and were almost exclusively derived from the corporate income tax (CIT) and the personal income tax (PIT). Tax revenue collection has not kept pace with economic activity, with poor performance mainly driven by the CIT. The revenue generated by the CIT declined from 2.7 to 1.4 percent of GDP during 2011–2019, albeit recovering to 1.8 percent in 2022. This remains among the lowest levels in the world. Generous tax incentives have been granted to attract foreign investment, but international evidence suggests that profit tax exemptions are highly inefficient. While economic growth has been predominantly driven by natural resources, government revenues accruing from the resource sector have been limited. Resource-related revenues, such as taxes, royalties, and preservation funds, account for a small share of total domestic revenue (averaging 8 percent in 2010-2022).

Tax rates are relatively low and significant tax incentives have been granted, which undermines revenue collection. The CIT rate has been progressively reduced to attract foreign investment. The rate was cut from 35 to 28 percent in 2012, then to 24 percent in 2013, and finally to 20 percent in 2020. This rate is relatively low in international terms, which is a significant tax incentive by itself. Nonetheless, the Law on Investment Promotion provides several tax incentives (e.g., CIT holidays and reduced rates) ranging between 4–15 years, depending on the business activity and location. Concessions negotiated on a case-by-case basis provide even more generous terms. This approach to investment promotion is highly inefficient and creates large foregone revenues. The PIT top marginal tax rate (25 percent) is also lower than most regional and income peers. The VAT rate of 7 percent is one of the lowest in the world, while some excise rates are also low by global benchmarks. Moreover, taxes levied on household consumption (e.g., VAT and excises) are found to be progressive, in the sense that they impose a larger burden on wealthier households.

Tax collection is only reaching about 60 percent of its full potential, implying that there is ample scope for policy and administration reforms. Tax effort was measured at about 0.6 during 2010–2016, meaning that tax collection was lower than the average tax yield for countries with similar characteristics. Hence, there is considerable potential to mobilize additional domestic revenues. Tax effort is affected by tax structure (e.g., tax rates and tax base) as well as tax administration and compliance. Tax effort can be increased by raising tax rates, expanding the tax base, enhancing tax compliance, and improving tax enforcement. When compared to taxation levels and (structural and institutional) determinants in peer countries during 2010–2016, the Lao PDR had an average tax potential of 21 percent of GDP, with the corresponding total tax gap at 8 percent of GDP. Estimates also suggest that only 13 percent of potential CIT revenue is being collected, largely due to tax exemptions that considerably reduce the tax base.

The administration of taxes has generally improved in recent years, but there remains considerable room to further enhance performance. The implementation of the Tax Revenue Information System (TaxRIS) provides a good platform to modernize the tax administration, particularly with the aim of improving the efficiency of tax collection, reducing leakages, and increasing revenue. Nonetheless, the current system lacks critical features (e.g., automated late filing/payment notice, automated risk analysis, and data analysis capabilities), and staff are not using all functionalities. The approval of the Tax Administration Law has strengthened the legal framework, but it is crucial to ensure that the law is adequately implemented. Efforts to build the capacity of tax officials are also bearing some fruit. However, developing a modern, efficient, and effective tax administration requires further improvements in processes (which should be standardized and transparent), technology uptake (e.g., automation), and staff capacity. This would also help build confidence in the tax administration (e.g., by reducing corruption risks).

Bold tax reforms are needed to ensure that revenue levels are adequate to sustainably finance growth-enhancing public spending and debt service obligations. Poor revenue performance significantly impacts fiscal space and the availability of foreign exchange, thus jeopardizing fiscal and debt sustainability, as well as broader macroeconomic stability. Moreover, a modern tax system should raise revenues efficiently and equitably. A prioritized and sequenced set of tax reforms (relating to both policy and administration) should be pursued in the coming years. Measures to expand the tax base, diversify revenue sources, and improve compliance are key to generating sufficient domestic resources to meet large financing needs (e.g., social spending and debt servicing).[94] However, strong political commitment and ownership is needed.

Restoring the VAT rate to 10 percent would immediately and efficiently raise considerable revenue. The current rate of 7 percent (introduced in 2022) is one of the lowest in the world, which severely undermines revenue mobilization. Restoring the rate to 10 percent could generate at least 1 percent of GDP in additional VAT revenue while having a limited impact on inflation or inequality.[95] Part of the additional revenue should be earmarked to support the most vulnerable households through targeted cash-transfer programs.[96] Even at this level (10 percent), the standard VAT rate would remain very low by international standards. Moreover, VAT exemptions should be reviewed and streamlined, since they distort economic activity and can cause tax cascading. For instance, exemptions for large-scale agricultural and forestry activities (e.g., businesses larger than 400 million

[94] Research shows that large tax revenue increases are associated with reforms of indirect taxes and exemptions, often supported by tax administration reforms, with sustainability hinging on reforms in the key compliance areas (risk-based audits, registration, filing, payment, and reporting). There is also evidence that tax reforms require major political consensus and that these tend to occur following major economic crises. Successful reforms tend to broaden the tax bases by significantly curbing exemptions and other special treatments.

[95] Even if this increase would fully translate into higher consumer prices (leading to a 3 percent increase, albeit in a context of high inflation), this would need to be set against a counterfactual of limited revenue mobilization that fuels further exchange rate depreciation pressures and thus domestic inflation. Moreover, the VAT is a progressive tax, from a distributional perspective.

[96] Even if only 10 percent of the additional revenue was allocated to a cash-transfer program, the budget for social assistance could be doubled from the current 0.1 percent of GDP.

kip) should be eliminated. Finally, adopting and implementing legislation to extend the scope of VAT to cover cross-border digital services could generate additional revenue. In the medium-term, VAT compliance can be improved through the full implementation of the Tax Revenue Information System (TaxRIS), the improvement of tax services, and the enhancement of institutional and technical capacities.

Revising the Law on Investment Promotion would help curb tax incentives and broaden the tax base. The current tax incentive system is predominantly based on tax holidays and reduced rates (relating to corporate income, value-added, import duties, and royalties), which are a costly and inefficient means of encouraging investment. Profit-based tax incentives should be phased out and replaced by cost-based measures, such as investment tax credits and accelerated depreciation. Other tax incentives should also be restricted. The Minister of Finance should be the sole authority issuing tax incentives (in line with international best practice), particularly with a view to rationalizing the incentive regime and reducing discretion. While special incentives currently need to be approved by the National Assembly, stricter requirements should be adopted (e.g., ex-ante cost-benefit analysis). These reforms would require a revision of the Law on Investment Promotion. In addition, improving the monitoring of tax incentives would support improved scrutiny of compliance and enable an assessment of their effectiveness. The creation of a centralized tax incentive database/repository in the Ministry of Finance would enable the authorities to estimate foregone tax revenues and undertake cost-benefit analyses. The corporate tax return form should include relevant information to better monitor and assess tax incentives, while exempt businesses should still submit CIT returns. Meanwhile, undertaking an assessment of the largest concession agreements would provide a tentative estimate of foregone revenues and an evaluation of the legal scope for revision. Finally, the introduction of anti-avoidance rules against profit shifting (i.e., transfer pricing rules) and other international taxation frameworks should also be considered to protect the tax base. This should also include provisions for direct taxation of the digital economy to embrace this growing component of the economy.

Reforming excise tax structures and increasing rates, particularly on beverages, tobacco, and fuel, could provide additional revenue while supporting health, environmental, and social outcomes. Reversing the recent fuel excise cuts would generate considerable revenue while incentivizing a transition to green energy. Reviewing the tax structure of alcoholic and non-alcoholic beverages, with specific taxes replacing or being added to the ad valorem tax and moving the base to retail prices, could raise revenue and benefit health outcomes. Reviewing the scope of products included under the non-alcoholic beverage category to make it a true sugar-sweetened beverages tax would be advisable. Removing exemptions on the tobacco excise and raising the tax rate could produce similar results, while changing the base of the ad valorem tax from ex-factory to retail prices would facilitate monitoring and enforcement. Furthermore, all specific taxes should be indexed to inflation and income growth. Overall, reforming structures and raising excise rates on products with negative (health, environmental, and social) internalities and externalities could generate several positive outcomes.[97] These tax policy reforms ought to be accompanied by improvements in tax administration to avoid leakages (e.g., tax evasion). This can be achieved by accelerating digital transformation (e.g., introducing a track and trace system) and other reform opportunities (e.g., audit). Given existing knowledge gaps (e.g., market size, prevalence, price dispersion, price/income elasticities), it is imperative to improve data collection and analysis to support evidence-based policy reforms.

Reforming the land tax and preparing for the introduction of a property tax would be key to boosting revenue collection. Property tax reform should follow a phased approach. First, land tax rates should be increased significantly to ensure the land tax becomes meaningful. The additional revenue should then be invested in enhancing the administration of land and land taxes, including the digital transformation of land and land tax management. Once tax administration has been improved, the land tax could be transformed into a property tax by including the value of improvements in the tax base. The National Assembly has recently approved the new Land Tax Law, which changes the tax base from size to value of the land. This will help raise effective tax rates and thus improve the fairness of the property tax regime. Developing and implementing an adequate land valuation system will be key to supporting tax collection.

Strengthening compliance risk management by focusing on the administration of large taxpayers would increase revenue and enhance efficiency. Improving tax administration is crucial to increase revenues and efficiency. Strengthening compliance risk management should start with the management of large taxpayers, given their importance to revenue collection and the scarcity of skilled staff within the tax administration.

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[97] Some of these goods can be considered luxury or non-essential. Taxing goods typically consumed by the wealthy can generate considerablerevenue and promote equity (which could strengthen social cohesion), particularly given the difficulty of taxing high incomes and assets.

It is therefore critical to re-establish a dedicated large taxpayer office (LTO) and recentralize large taxpayer management. There is also a need to improve capacities in key functions (e.g., audit, taxpayer services, and data management and analysis) and then expand to other areas. This program should take into account the implementation of the TaxRIS and the issue of staff redundancy associated with automation. Moreover, it would be important to broaden e-services offerings through an integrated ICT solution, which could be done by expanding TaxRIS to include more sophisticated tax administration features. A modern IT system would allow the tax administration to adopt efficient and effective business processes and facilitate business continuity. The use of big data and artificial intelligence can play a key role in modernizing tax administration.

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