A New Personal Income Tax as An Incentive to Buy Life Insurance

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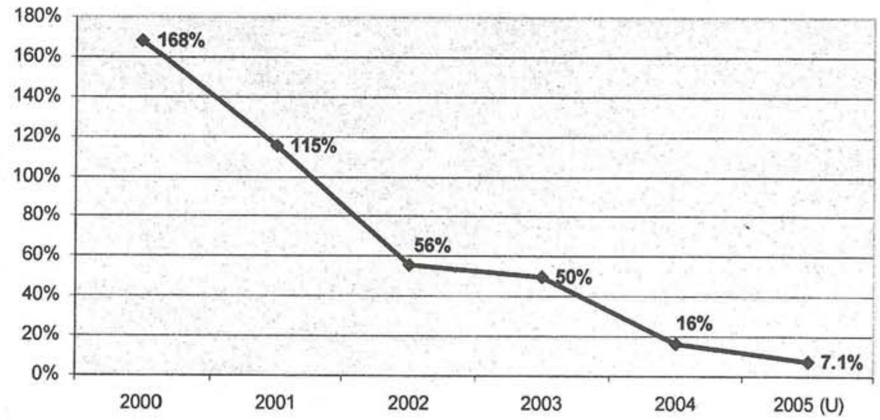
1. Insurance market and personal income in Vietnam

The life insurance business in Vietnam in the past 10 years has made good progress and provided jobs for thousands of laborers. It has played well the role as a financial intermediary and an effective instrument for repairing human losses in production and ordinary life.

The growth rate of this market, however, is stagnating, as shown in the Figure 1. Main causes of this situation are high interest rate and inflation rate, which made buying insurance less profitable. In addition, the insurance companies face competition from similar products that offer higher interest rates. When the economic growth rate tends to slow down (7.1% in 2005) the insurance business finds it hard to meet the target set by the Strategy to Develop the Life Insurance Market up to 2010 that reads, "[we should try to increase the] life insurance premium by 28% a year, from VND4,400 in 2002 to 12,500 billion in 2005 to 31,000 billion by 2010."

Figure 1: Growth of life insurance premium in 2000-2005



Source: Vietnam Life Insurance Association

In the coming years (2006-2010), insurance companies in Vietnam should diversify their products and distribution channels, improve quality of services and enhance efficiency of their investments in order to reach the planned target. The Government had better take measures to support this effort and one of measures is to adopt a new policy on personal income tax.

The current law on personal income tax requires citizens who earn more than VND5 million a month to pay personal income tax according to the following tax brackets.

At present, taxpayers are not allowed to take away insurance premium from their taxable income. To encourage the public to buy the life insurance, the Government had better allow them to do so.

Table 1: Some facts about the life insurance

Facts	2002	2003	2004	2005 (estd.)
1. Insurance market				
- Premiums (VND bil.)	4,368	6,575	7,636	8,023
- Income from investment (VND bil.)	833	986	1,832	3,354
- Share in the GDP (%)	0.81	1.09	1.07	1.1
- Premium per capita (VND1,000)	88	125	152	175
2. Contribution to socioeconomic life				
- Insurance paid (VND bil.)	745	941	1,441	2,319
3. Investment (VND bil.)	9,955	14,602	23,002	32,011
4. Jobs supplied	76,600	125,700	136,900	145,800

Source: Ministry of Finance 2004

Table 2: Personal income tax rates

Grade	Personal income (VND1,000)	Tax rate
1	Up to 5,000	0%
2	More than 5,000 to 15,000	10%
3	More than 15,000 to 25,000	20%
4	More than 25,000 to 40,000	30%
5	Above 40,000	40%

2. Possible effects of the suggested policy

- Firstly, the taxable income will be lower, and moreover, taxpayers will realize that they and their families will enjoy some financial safety in cases of accidents or disasters, which encourages them to buy insurance for themselves and members of their families.

- Secondly, the tax take will reduce, but it's worth noting that the taxation must be considered as an instrument for maintaining sources of tax payments and supporting the economic growth. According to my calculations, the tax agency could collect from the insurance company some 25% of payments that turn into premiums instead of going directly to the tax agency.

Table 3: Policies by OECD countries on deduction of life insurance premium from taxable income

Country	Premium taken away	Country	Premium taken away
Austria	25%, $10,000 per year at most	Luxembourg	LuxF18,000 at most
England	No deduction *	Mexico	No deduction
Belgium	No deduction	Finland	No deduction
Canada	No deduction	France	No deduction
Denmark	Deduction allowed	Sweden	No deduction
Germany	Deduction allowed for 12-year policy	Spain	No deduction
Netherlands	Deduction allowed, G500 at most	Swiss	Deduction allowed
Italy	L2.5 million at most for 5-year policy	Australia	No deduction

(*) Most countries of this group allow deduction of payments to social securities from taxable income.

- Thirdly, the society will enjoy many benefits which are larger than the reduction in the tax take caused by this proposed policy. These benefits are: (1) More jobs are created in the insurance business and industries where insurance companies invest in, which help reduce the unemployment rate; (2) Insurance companies turn idle money from the public into sources of long-term capital needed for both governmental bodies and companies; and (3) Insurance companies help provide some social security for the public when this system built by the Government fails to cover all social classes and communities.

- Fourthly, many countries have applied this policy because of different reasons. Generally, most countries allow part of insurance premium to be taken away from the taxable income for a certain period of time.

3. Calculation of the sum deducted

Life insurance premium could be deducted from the taxable income if it is not higher than 10% of the regular income in the year. After deducting, no tax payment is required if the total regular income in the year is lower than the tax base. The following are two examples:

- Regular income in the year: VND65 million
- Tax base: 60 million
- Taxable income according to current law: 6 million
- Life insurance premium in the year: 10 million
- Amount allowed to be deducted from the regular income (10%): 6.5 million

After deducting, no tax payment is required in this case.

The second example is as follows:

- Regular income in the year: VND80 million
- Tax base: 60 million
- Taxable income according to current law: 20 million
- Life insurance premium in the year: 10 million
- Amount allowed to be deducted from the regular income (10%): 8 million
- Taxable income: 20-8 = 12 million
- Required tax payment: 1.2 million

Data gathered during my research allow me to suggest a level of 10% for deductible premium because most insurance buyers spend such percentage of their income on insurance. And only life insurance policies with maturity of at least five years can enjoy such deduction. I don't suggest an absolute sum because I want to encourage high-income earners to buy life insurance. Under this policy, the higher their income, the bigger deduction they can enjoy. The following is an example:

- Regular income in the year: VND300 million
- Tax base: 60 million
- Taxable income according to current law: 240 million
- Life insurance premium in the year: 45 million
- Amount allowed to be deducted from the regular income (10%): 30 million
- Taxable income: 240 - 30 = 210 million
- Tax payment for the first 180 million: 180 x 10% = 18 million
- Tax payment for the remainder: 30 x 20% = 6 million
- Total income tax payment: 24 million

I believe that such a policy could help the life insurance market grow again within a short period because it is an incentive to buy life insurance policies. And this measure will benefit the insurance companies, their customers and the whole economy as well.■

Photo by Huỳnh Thơ