TAX ON BANKS AND ITS RELATION WITH CREDIT INTEREST RATES, MONETARY POLICY AND ECONOMIC GROWTH

The Vietnamese economy is changing into the market mechanism under the Government's management. The economic renovation requires the rapid access to theories and realities of economic management of many countries in the world. The national economy includes many markets that strongly relate to each other, every change has effect on the balances in other markets and common balance of the economy. The macro-economy shows interest in these relations with the aim to analyze and describe the nature of economic changes with a view to finding out causes of the unrest that affects common activities of the whole economic system. The macro-economy also studies economic policies and their tools for economic stability and growth.

To achieve the macro-economic goals, the State may use various tools and policies, each policy has its own tools as follows:

The fiscal policy regulates income and expenditure of the government so as to develop the economy, the fiscal policy has two such tools as the government's spending and taxation. The government's spending has direct influence on the scale of public spending, so it may affect the aggregate demand and output. Taking a long view, taxation also has effect on investment, economic structure and sustainable growth and development.

The monetary policy mainly affects investment. It has two major tools such as money supply and interest rate. When the central bank changes money supply, interest rate will go up or down, so impacts on investment.

The income policy composes numerous steps the government takes with the aim to make direct impact on income for inflation control. This policy uses such tools as wage and salary , price, income tax.

The policy of external relation aims at stabilizing foreign exchange rates and keeping payment imbalance in an acceptable condition.

In reality, the demonstration and usage of four above-mentioned policies are diverse, especially in the countries which have developing economies. Every policy has its own independent position but there is interaction between them for economic growth, unemployment alleviation, price stabilization, foreign trade balance.

1. TAX POLICY

The Vietnamese taxation has been reformed since 1990, the targets of this tool are economic growth, the ensuring of increasing revenues for national budget, social equality. After four years of implementation, in addition to increasing revenues, inflation control, production encouragement, carrying out equality in tax obligations between economic sectors, there are remaining problems just arising in the open economy that have not been foreseen as follows: enterprise engaging in many industries, numerous forms to mobilize capital such as share, stock, bond, stock market... Although the import duty can concentrate revenues for the Treasury but it has shortcomings such as collecting even special consumption tax, so the tax rate is high; not unifying tax level so as to be able to compare the result of investment for production with that of importation of the same products. The turnover tax is complicated with many tax rates and shows multiple taxation.

The plan of tax renovation in the second stage has been approved. Besides the targets which should be attained as in the first stage, Vietnam's taxation should also be made appropriate to the region's one with the aim to create conditions for Vietnam to join international organizations such as ASEAN and WTO. This plan requires the reform to be in uniform manner, so it can secure results of the reformation as follows:

a. Indirect taxes

- Value added tax (VAT) should be applied to replace turnover tax with the aim to overcome deficiency of multiple taxation, in the meantime taxable commodities should be expanded, not only including domestic products but also imports. Exports are also subject to VAT, but with 0% rate, so they will be given back the tax paid for the input. The countries in the world applying VAT use two technical measures of taxation. Firstly, exports enjoy 0% VAT rate due to exportation encouragment, secondly some special commodities and services are exempt from tax. The significance of VAT exemption policy is that the value added is tax-free, but as for the whole consumption value of that unit the taxpayer though has VAT receipts but the payments are not returned.

To fit itself for the region's tax policy, the import duty rates should be reduced to 60% at most but at the same time even special consumption tax is applied to exports. So special consumption tax must be applied to domestic products and exports.

The three above-mentioned indirect taxes has their own effects but have relations between them in order to achieve the targets of tax policy. Reforming uniformly these taxes will lead to the result that a commodity such as imported beer will be liable to three kinds of tax: import duty, VAT, special consumption tax. To do so will affect the proper calculation of indirect tax payment of the enterprise, that is, the enterprise domestically producing beer need not pay import duty, when paying VAT it is allowed to deduct the tax collected from its purchased goods. if the materials imported by the enterprise enjoy 0% or low tax rate, it can lower the production costs and employ workers inland.

b. Direct taxes

The two major direct taxes in Vietnam are profits tax and income tax on highly-earning persons. These taxes should be studied and supplemented in order to fit themselves for the region's taxation.

The income law only affected organizations, individuals making profits from doing businesses in Vietnamese territory, therefore it cannot adjusts incomes of foreign organizations and individuals (not residing in Vietnam) having incomes generated in Vietnam. This is a considerable revenue that should be immediately added in taxation. The developing countries will make profits by investing their capital in underdeveloped countries. On the contrary, underdeveloped countries want investment but lack capital, so they attract capital by loaning, jointventuring, renting machines and equipment...and they must pay interests, divident, rent, for buying patent to developing countries. As a result, if Vietnam does not levy tax on these incomes, then foreigners when remitting these incomes to their homeland, they must declare income tax in their country. Taxation in countries regulates that tax is deducted at the source, that is, before paying incomes to those not residing in the host country, organizations, individuals must deduct tax. The rates of tax deducted at the source are defined as follows: 20-25% for loan interest, divident, selling patent, 10-15% applied to countries signing agreements of avoiding multiple taxation.

The income tax on highly-earning persons only regulates incomes from salary, wage and other incomes excluding incomes from trade, but the profits tax stipulates business people are liable to profits tax, these regulations aren't compatible with the international practices.

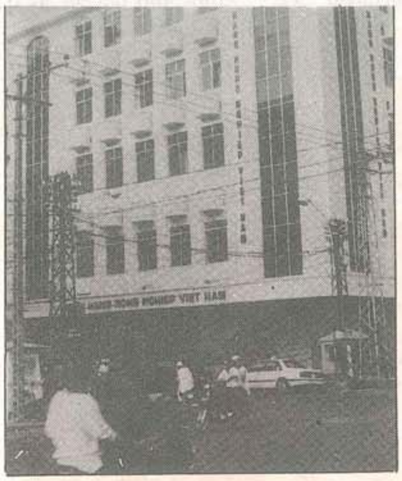
Therefore in addition to uniform reformation of the three indirect taxes, the simultaneous reformation of the two direct taxes are very essential. To do so, the Government can secure stable revenues of the Treasury on the base of changing revenues structure: reducing revenues from some items but increasing revenues from other items with a view to fitting taxation for international and regional practices.

2. BANK AND TAX ON BANK

a. Activities of commercial banks in Vietnam

So far, there are 72 units including 4 state-owned commercial banks, 4 joint ventures, 18 foreign branches and 46 joint stock commercial ones. The four commercial banks have a wide range of activities; such industries as aviation, petroleum, electricity, railway are their major customers. In comparison with other banks, the commercial banks made great contribution to the Treasury with high level: VNĐ586 billion in 1994 (VNĐ316 billion of turnover tax, VNĐ270 billion of profits tax). The joint ventures, foreign branches got into the red in the early years, but since 1995 many banks produce profits such as ANZ Bank, Chifong Bank. Some joint stock commercial banks have good performances, for example, their payments to the Treasury are as follows:

	Total (billion)	Turnover tax (billion)	Profits tax (billion)
The Maritime Joint Stock Commercial Bank	24	7	17
Vietnam Exim Bank	23	5	18
Đông Á Bank	15	3	12



b. Taxes on banks

As a business, the bank must pay two kinds of tax: turnover and profits taxes. Taking theoretical view, turnover tax is an indirect tax, the bank pay tax for its customers (borrowers). A business never use self-provided capital only, it needs loans. Therefore turnover tax will impact on interest policy that does not stimulate investment. But considering the bank's performance, many countries regard it as special one as well as finance house, insurance company. Just because of this special feature, many countries' tax policy has separate regulations.

As for turnover tax: in the world there are currently some 100 countries applying VAT in replacement of turnover tax. In these countries, most of banks are exempt from VAT, VAT is a tax on the rise in value, it is calculated by subtracting input tax from output tax. Exemption of banks from VAT means no tax on the rise in value that banks made, the tax on value that banks purchased and had VAT receipts of suppliers cannot be returned. Besides VAT exemption, there are countries, Thailand for example, applying special business tax with 3% tax rate to banks. In China, turnover tax levied on banks is collected from the difference.

Consequently, studying VAT policies in other countries and proposing their application in Vietnam with the two completely different mechanisms defining tax rates seems unstable.

In the past Vietnamese tax authorities collected turnover tax from banks on bank loan interests, this is irreasonable. As a result of this, later they collected tax on the difference between bank loan interest and deposit interest. So turnover tax on the difference is collected from banks as well as from trading businesses. This is a measure to limit multiple taxation, it partly reflects the way to collect VAT. Therefore in case Vietnam hasn't applied VAT yet, turnover tax on the difference of bank credit is still a transitional step before applying VAT.

In reality many opinions support the maintenance of turnover tax on the difference between bank loan interest and deposit interest because:

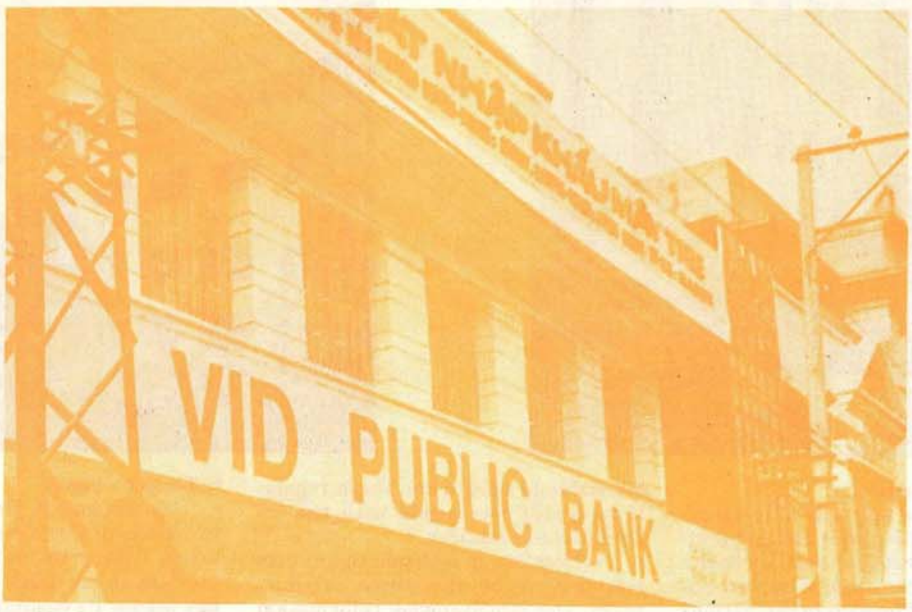
- This collection creates condition for banks to lower loan interest towards production and trading businesses.

- Otherwise it is suitable to the countries near Vietnam such as Thailand, China. These countries also impose turnover tax on bank activities. Other countries though do not impose VAT on bank activities but levy income tax on deposit interest with 20%, 25% tax rates.

- In addition imposing turnover tax on banks can protect domestic banks which have little self-provided capital and mainly borrow to grant loans. As a matter of fact, although banks are liable to turnover tax, they still make big profits.

Regarding profits tax: As presented above, since the profits tax law hasn't affected people not residing in Vietnam who must pay tax deducted from their income generated in Vietnam such as loan interest, divident and selling patent, so if turnover tax on banks is eliminated, then the "tax deducted at the source" must be added in the profits tax law. Bank entities operating in Vietnam and paying profits tax are responsible to deduct tax "deducted at the source" on people not residing in Vietnam.

The above analysis strongly confirm the essential to uniformly reform 5 major taxes such as turnover tax, special consumption tax, tariff, profits tax and personal income tax along with reforming tax policy on banks.



c. Tax on banks and its relation with credit interests

Everyone knows the bank loan interest in Vietnamese currency is bigger than that in foreign currency, the payment for loan interest by enterprises is very big, especially by state run businesses. Some of them must pay more loan interest than tax. To reduce loan interest for effective performance of businesses is an issue of urgency. To do so, there should be uniform measures in the immediate future as follows:

- To alter banks' structure of spending on tax via application of VAT in replacement of turnover tax, exempt banks from VAT and add tax deducted at the source on people not residing in Vietnam.

- To reduce costs of banks: In the market economy due to large scale of capital mobilization, if commercial banks lessen their costs, they will contribute to interest reduction in the market.

In current condition, the input prices of banks are very different due to such causes as:

- The capital attraction with high interest rate holds a big share.

- The credit balance of deposit accounts takes a big part but its interest is low...

As a result of this, to ensure the equality between banks, it is necessary to control over the difference between input and output of banks generally calculated on the sources of capital.

To keep the difference between input and output at 0.3% per month in Vietnam is illogical. We should calculate the interest arising from credit operations. It's really hard to distinguish borrowed capital from self-provided one in the working capital.

According to figures of banks in the world, the difference between output and input is about 0.2%-0.25% per month.

In brief, the tax tool of the fiscal policy as well as the interest tool of the monetary policy has interaction to carry out the macro-economic targets. The study to produce a proper policy is responsibility of finance and banking authorities■

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