

STANDING COMMITTEE REPORT NO. 13-186

RE: C.B. NO. 13-123/W&M

SUBJECT: IMPORT DUTIES

OCTOBER 26, 2004

The Honorable Peter M. Christian
Speaker, Thirteenth Congress
Federated States of Micronesia
Fourth Regular Session, 2004

Dear Mr. Speaker:

Your Committee on Ways & Means to which was referred C.B. No. 13-123 entitled:

"A BILL FOR AN ACT TO FURTHER AMEND TITLE 54 OF THE CODE OF THE FEDERATED STATES OF MICRONESIA, AS AMENDED, BY AMENDING SECTION 221 THEREOF TO CHANGE THE IMPORT DUTIES APPLICABLE TO CERTAIN PRODUCTS, BY AMENDING SECTION 805 THEREOF TO DESIGNATE THE USE OF CERTAIN REVENUES COLLECTED UNDER SECTION 221, AND FOR OTHER PURPOSES.",

begs leave to report as follows:

The intent and purpose of the bill are expressed in its title.

Public hearings were held on C.B. No. 13-123 in Chuuk on September 14, 2004; in Yap on September 17, 2004; in Kosrae on October 7, 2004; and in Pohnpei on October 20 and 26, 2004. In addition, the Yap State Government and the Governor of Kosrae submitted written comments. During the hearings in Pohnpei, a number of members of the business community raised issues concerning the National Government tax structure. Particular unhappiness was expressed that the current tax laws permit no deductions for employee expenses, utility payments, Social Security contributions or other business expenses. Questions were raised as to what incentives are being provided by the tax laws for small businesses. Your committee is sensitive to the concerns expressed by these businessmen. However, the committee also notes that the identified issues relate to the gross revenues tax, not the import duties that are the subject of C.B. No. 13-23. Your committee assured the witnesses that their comments would be considered in the course of the broader tax reform process that is currently underway in the FSM.

Your committee has the following views with respect to C.B. No. 13-123:

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To offset the scheduled decrement in sector grant funds under Compact II, the Federated States of Micronesia needs to take steps to increase revenues from other sources. It has come to the attention of your committee that, under current law, the duties levied by the FSM on imported goods are substantially lower than those imposed by other countries in the region. This is particularly true of the so-called "sin taxes"—i.e., the taxes on tobacco and alcohol. For example, the current FSM import duty on cigarettes is 25 percent *ad valorem*, which typically amounts to less than 15 cents per pack. In contrast, Palau imposes a \$2.00 per pack tax on cigarettes. The import duty imposed by the Republic of Marshall Islands is 100 percent *ad valorem*.

Your committee submits that there is no good reason to maintain low import duties on tobacco and alcohol, particularly considering that those products cause health problems and impose increased health care costs on the nation. By increasing the import duties on those products, the FSM can both raise additional revenues and discourage the consumption of substances that have adverse health consequences. C.B. No. 13-123 has the principal purpose of amending section 221 of title 54 of the FSM Code to increase these "sin taxes". Your committee supports increasing the duties on tobacco and alcohol; however we recommend that the duty on imported beer be increased to 25 cents per 12 ounces, rather than to 15 cents, as proposed in the bill.

C.B. No. 13-123 also would reduce the import duties on fruit juices from 25 percent *ad valorem* to 12 percent *ad valorem*. It is the understanding of your committee that the current tax rate was established with the purpose of encouraging consumption of locally-produced fruit drinks in preference to imported beverages. Considering that there is currently no significant local fruit juice industry and that consumption of fruit juice can have health benefits, your committee believes that the reduction in this import duty is appropriate. Your committee would recommend, however, that the duty be reduced to three percent.

While generally supporting the purpose of C.B. No. 13-123, your committee, based on further study and upon comments received from the states, recommends a number of amendments to the bill. The committee suggests deferring the proposed increase in the import duties on motor vehicles, pending further analysis of the effects of that change. Your

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committee also recommends deletion, at this time, of the provision that would increase the general import duty rate from four to five percent. The committee received a number of comments to the effect that the current 100% duty on laundry bar soap should be reduced. The committee agrees. The committee also recommends a reduction in the duty on fresh citrus fruit from twenty-five percent to three percent, the same rate that is applicable to most other food items. Considering the health benefits associated with consumption of fresh fruit, it does not seem advisable to discourage the purchase of fresh fruit by imposing high import duties. Comments from the states indicate that the language of the amendment to subsection 805(1)(b) needs to be clarified. Finally, your committee supports the earmarking of a portion of cigarette duty collections for academic scholarships, but recommends that those funds be used exclusively for graduate school, medical school, law school and other post-graduate programs. We also propose that the President be named as allottee of the funds.

Specifically, your committee recommends the following amendments to C.B. No. 13-123:

1. Page 2, line 8, delete the number "12" and insert "three" in lieu thereof.
2. Page 2, line 11, delete "0.15" and insert "0.25" in lieu thereof.
3. Page 2, lines 18-19, delete "fresh citrus fruit and".
4. Page 2, line 22, delete "one hundred" and insert "twenty-five" in lieu thereof.
5. Page 3, delete lines 1 through 3 and renumber the following subparagraph.
6. Page 3, line 5, delete "five" and insert "four" in lieu thereof.
7. Page 3, line 19, delete "An amount equal to Twenty" and insert "twenty" in lieu thereof.
8. Page 3, line 19, following "of", insert "of the amount remaining, after the transfer of funds pursuant to subsection 1(a) of this

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section, of".

9. Page 3, line 22, delete "post-secondary" and insert "post-graduate" in lieu thereof.

10. Page 3, lines 23 through 25, delete "Secretary of the Department of Health, Education and Social Affairs" and substitute "President of the Federated States of Micronesia or his designee" in lieu thereof.

With these amendments, your Committee on Ways & Means is in accord with the intent and purpose of C.B. No. 13-123 and recommends its passage on First Reading, and that it be placed on the Calendar for Second and Final Reading in the form attached hereto as C.B. No. 13-123, C.D.1.

Respectfully submitted,

Sabino S. Asor, chairman

/s/ Roosevelt D. Kansou
Roosevelt D. Kansou, vice
chairman

Claude H. Phillip, member

/s/ Henry C. Asugar
Henry C. Asugar, member

/s/ Peter M. Christian
Peter M. Christian, member

/s/ Dohsis Halbert
Dohsis Halbert, member

Isaac V. Figir, member