



Analyze The Tax Reduction Policy Implemented by The Government of Timor Leste

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ABSTRACT

This article analyzes the political and economic implications of the VIII Government of Timor-Leste's decision to reduce the selective tax rate. The objective of this research is to assess the impacts of this policy on national economic growth, income distribution, and social welfare. Employing a qualitative approach, the research utilizes government documents, political speeches, and tax data to examine the motivations behind the policy and its effects. The findings suggest that while the reduction in the selective tax aims to stimulate consumption and economic activities, concerns persist regarding long-term fiscal sustainability and the fairness of benefit distribution. A comparative analysis with tax policies in other developing nations highlights potential risks, such as increased reliance on selective taxes and their effects on inflation. Furthermore, the research emphasizes the need for alternative strategies to ensure economic stability and equitable growth. This research contributes to the broader discussion on fiscal policies in Timor-Leste, advocating for a balanced taxation approach that considers both revenue generation and economic equity. The insights gained from this analysis are crucial for policymakers to design effective fiscal strategies that promote sustainable development and enhance social welfare in the country.

Keywords: tax analysis; selective tax; fiscal policy; economic growth; timor leste

INTRODUCTION

Economic development in developing countries is often hampered by various factors, one of which is an inefficient tax structure and income distribution inequity (Barbier, 2019; Hess, 2016; Leigh, 2024; Marlina & Natalia, 2017). In the global context, many countries face the challenge of designing fiscal policies that not only encourage economic growth but also create social welfare. Timor-Leste, as a country emerging from a period of conflict and instability, faces significant challenges in creating policies that can stimulate growth while ensuring that the benefits of this growth can be felt by all levels of society (Broughel & Thierer, 2019; Nguyễn & Phan, 2023; Surya et al., 2021; Udeh et al., 2016). The importance of effective fiscal policy is increasingly urgent amid rapidly changing global economic dynamics, especially in the wake of the COVID-19 pandemic. Countries around the world have sought to adjust their tax policies to respond to rapid economic changes and support recovery. In this context, tax cuts are one of the instruments used to stimulate consumption and investment. However, tax cuts also carry risks, especially related to fiscal sustainability and income distribution inequality.

The selective tax reduction policy implemented by the 8th Government of Timor-Leste aims to stimulate consumption and economic activity. This policy, which is more focused on certain sectors such as food, beverages, tobacco, and furniture, is an attempt to increase people's purchasing power and encourage real sector growth. However, although this policy is expected to increase consumption, there are growing concerns about long-term fiscal sustainability and fairness in the distribution of benefits among the people. One of the main issues is how this tax reduction can affect state revenue. Given Timor-Leste's dependence on oil and gas sector revenues, tax cuts could result in a reduction in much-needed domestic revenues for financing infrastructure and public services. In addition, there are questions about the long-term impact on inflation and people's purchasing power. If tax cuts are not accompanied by a clear strategy to maintain fiscal balance, there could be serious risks to the country's economic stability.

In studies of tax reduction policies, several previous studies provide valuable insights. Yujuan, M., Guangli, Y., & Bo, L. (2022) in their research entitled “A comparative research on the tax and fee reduction policies for sustainable development” analyzed how three major economies—the United States, the European Union, and China—are facing the challenges of COVID-19 through tax reduction policies, showing that although these policies can stimulate growth, there are risks related to fiscal sustainability. Meanwhile, Kuo, T. C., Hong, I. H., & Lin, S. C. (2016) in their article “Do carbon taxes work? Analysis of government policies and enterprise strategies in equilibrium” explore the impact of carbon taxes, highlighting the importance of considering the effects of tax policies on economic sectors to achieve a sustainable balance. These studies emphasize the need for in-depth analysis of the impact of tax policy, especially in the context of a small country like Timor-Leste, which faces unique challenges in designing effective and fair fiscal policy.

The novelty of this research lies in its in-depth focus on the specific context of Timor-Leste, which is often neglected in global discussions on tax policy. By conducting a comprehensive analysis of the selective tax reduction policy, this research aims to provide new insights that can help policymakers formulate more effective strategies. The existing gap is the lack of research linking tax policy to the specific challenges faced by small, newly developing countries, especially in terms of sustainability and economic justice.

The purpose of this research is to conduct an in-depth research of the impact of selective tax reduction policies on economic growth and income distribution in Timor-Leste. By analyzing data and conducting interviews with various stakeholders, this research aims to produce recommendations that can help the government design more sustainable and fair fiscal policies. The benefits of this research are expected to be felt not only by policymakers, but also by the wider community, who will gain a better understanding of how tax policy affects their daily lives. As such, this research can contribute to the broader discussion on tax reform and inclusive economic development in Timor-Leste.

The results of this research are expected to provide valuable insights for policymakers, academics, and other stakeholders in understanding the relationship between tax policy and economic growth in Timor-Leste. In addition, this research is expected to encourage further discussion on tax policy reforms that can support more equitable social and economic development. By understanding the impact of tax reduction policies, the government can take more appropriate steps to achieve community welfare and ensure that the resulting economic growth can be enjoyed by all levels of society.

RESEARCH METHOD

This research uses qualitative research methodology, which allows for an in-depth understanding of changes in fiscal policy and its socioeconomic impact. Primary data sources include government reports, legal documents, and statistical records from relevant national institutions. In addition, interviews were conducted with tax experts, government officials, and business stakeholders to gain insights into the practical implications of selective tax reductions. A comparative approach was also applied, analyzing similar policies in neighboring countries to assess the results and relevance to the economic context of Timor-Leste. This research follows a case research approach, with a particular focus on the selective tax reduction policy implemented by the 9th Constitutional Government. Data triangulation was carried out to ensure the reliability and validity of the findings.

RESULTS AND DISCUSSION

The Government of Timor-Leste is committed to supporting the national economy by encouraging and facilitating the legitimate. As a government agency responsible for the movement of goods through our borders, the government plays the main role of protecting the country from import and export of illegal or prohibited goods, and helps to ensure that tax and rate are collected properly on behalf of the government (Sukarno et al., 2024; Worku, 2016). Customs tax is a tax that the government applies to goods when imported into Timor-Leste from other countries. If a

person who is commercially imported goods into Timor-Leste is required to pay the following fees and taxes as applicable under the law: (1) Customs Tax (2) Sales Tax (3) Consumer Tax in the National legislation these fees and taxes are tax and tax acts. Customs tax is a tax that the government applies to goods when imported into Timor-Leste from other countries. When the Customs Tax is on behalf of the government which is used to help protect the domestic industry and to obtain revenue. To identify the Customs Tax we have, research calculates 5% of the price material to increase shipping costs and increase insurance costs. Consumption tax applies to the Government for material and other assistance, typically to goods that are harmful to the economy or danger to society. The purpose of this fee is to increase revenue for the government and to avoid the use of goods that have a fee. The consumption tax is different from Customs or Sales Tax because this rate applies to specific marketing. The sales tax is a tax that the government applies to goods when imported into Timor-Leste from other countries. When this tax is paid, it is the name of the government that will be used to assist various public services and to obtain revenue.

In the five-year vision of the VIII Government to see Timor-Leste a prosperous, healthy, educable, qualified, improved and dynamized overall supply of goods and services that are important in production and employment in all productive sectors can respond to the emerging economic situation. In view of the VIII Government's objectives in this programmed five important things are the strengthening of the democratic rule of law, investing in capital and social development, investing in infrastructure development, promoting economic development, strengthening governance, promoting good governance and corruption. The target of 2028 is to reduce the tax and economic growth by an average of 5%, private investment will increase by 10% per year, inflation tax keep cannot exceed 4.4% and also create a lot of jobs to reduce the tax of unemployment. The Government proposes to increase the import tax from 2,5% to 5, so it is hoped that with these increases, domestic revenues will increase from \$153.7 million to \$174 million with a rise of 13,8%. Therefore, the Government introduced a program to reduce the impact of inflation and increase the cost of life for citizens, thereby increasing the ability to buy. These initiatives, the government made adjustments to the selective tax rate on consumption and customs rights for imports that could be applied by 2023.

On the other hand, the National Parliament approved the proposed 2023 State Budget Law which is expected to increase the selective tax rate for the country. The tax rate to be applied to tobacco and other products comes from tobacco, going forward from \$50 per kg to \$100 per kg. But the VIII Government Constitutional introduced some amendments such as tobacco tax, which in this year is \$50 per kg, the Government proposed to increase the tax of \$100 per kg. This will contribute to domestic revenue and protect the health of its citizens. Vehicles with a value of more than \$10,000, forward will have a tax rate of 10% and vehicles with a value of more than \$25,000 will have a tax rate of 25%, while vehicles with a value of more than \$5,000 will have a tax of 30%. These taxes are a fiscal instrument used by the government to increase domestic revenue collection over the years to reduce the expenditure on the petroleum fund.

The following table present a comparison of tax rates before and after the changes, along with the anticipated impact on various economic sectors and consumer behavior. This analysis help evaluate whether the new selective tax policy can achieve a balance between increasing government revenue and maintaining consumer purchasing power.

Category	Previous Tax Rate (%)	Revised Tax Rate (%)
Tabacco (perkg)	50	100
Vehicles(>\$10,000)	5	10
Vehicles (>\$25,000)	5	25
Vehicles (>5,000)	20	30
Alcohol & Beverages	7	12
Furniture & Equipment	5	8

Resource : DG Finanças, Ministerio das Finanças Timor Leste, 2024

The table above illustrates the key changes in tax rates and their estimated effect on economic sectors and consumer. The government's rationale behind these adjustments is to increase domestic revenue while controlling imports of non-essential goods. However, there are concerns about the long-term sustainability of such tax increments, particularly regarding their effect on inflation and consumer purchasing power.

In the fiscal area, the Public Finance Management Reform aims to diversify revenues, allowing the Government to achieve at least 15% of domestic revenues from the total Gross Internal Product (GDP) in 2028. This is very important so that we can be free from our revenue from the Petroleum Fund (Abdul Gani et al., 2020; Odo et al., 2016; Ojonye et al., 2024; Utami & Widarjo, 2022). In order to achieve this objective, the Government will continue to improve its administration, human resources, systems and infrastructure of the Tax Authority and Customs Authority, review the Tax Law and introduce the additional Value Tax (VA). On the other hand, the Government intends to increase revenue through greater efficiency and effectiveness of the fiscal system, while maintaining the neutral and comprehensive fiscal responsibility of the region, through the identification and regulation of the existing potential revenue and through the improvement of the capacity of public institutions that aim to achieve fiscal and non-fiscal control. The main objective is to increase and improve revenue, so that the Government can ensure the proper installation of the bodies, services and personnel of the Tax Authority, Customs Authority and other public entities responsible for collecting non-tax revenues.

The change in the percentage of the Consumer Price Index (CPI) All monthly groups decreased (-0.1%) for August 2024, compared to July 2024 also decreased (-0.1%). All group price changes (-0.1%) were due to the contribution of the Food and non-alcoholic beverages (-0.1%), clothing and shoes (-0.2%), and alcohol and tobacco (-0.1%) groups. Transport group (+.2%) and mobile equipment and household maintenance (+ 0.1%) are the opposite of all group inflation. The group Food and non-alcoholic beverages decreased (-0.1%), because it has a majority impact on

the sub group sugar, Marmalade, honey bees, Chocolate in sweet food (-2.0%), oil and fat (-0.9%), rice (-0.2%), fruit (-1.9%), water, Drinks and fruit Juice (-1.4%) in milk, cheese in eggs (-0.2%). Sub-group vegetable (+1.1%), coffee, tea, cocoa (+ 0.7%) were the opposite of food and non-alcoholic food group inflation.

The annual Consumer Price Index (CPI) change was increased (+ 1.8%) compared between August 2024 and August 2023, with contributions from the Food and non-alcoholic beverages group (+ 3.6%), Education (+ 2.0%), recreation and culture (+ 1.9%), Health (+ 2.3%), Clothing and shoes (+ 0.4%), and Transport (+ 0.4%) for the year August 2024. The alcohol and tobacco (-4.5%), equipment and mobile maintenance of the house (-0.6%) and the house (-0.1%) were the opposite of all group inflation for the year August 2024. Tradable Inflation (-0.1%) and Non-tradable Inflation did not change monthly, compared between August 2024 and July 2024. Tradable inflation increased (+ 2.1%) and non-tradable have not changed monthly. compared between August 2024 and July 2024. Tradeable Inflation has increased (+ 2.1%) and Non-tradable Inflation has also increased (+ 0.8%) on an annual compared between August 2024 and August 2023.

The first contribution of the Food and non-alcoholic beverages and transport groups is the largest contribution to the annual of August 2024.

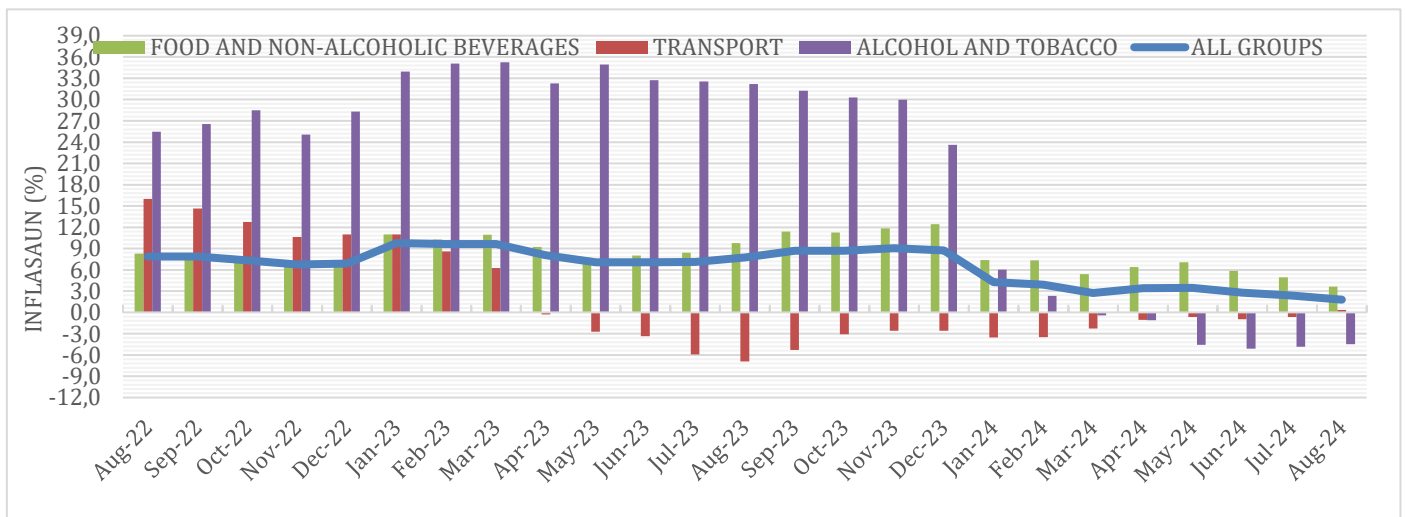


Figure 1. The annual inflation rate of Timor-Leste shows fluctuation

Table 2 in the article illustrates fluctuations in the annual inflation rate in Timor Leste, with the food and non-alcoholic beverages and transportation groups as the main contributors. Below is an analysis based on the data presented:

Monthly inflation decrease (-0.1%) in August 2024

1. Main factors behind the decline:
 - a. the price of food and non-alcoholic beverages decreased (-0.1%). Primarily due to lower prices of sugar, chocolate, oil, rice, and fruits

- b. Clothing and footwear prices fell (-0.2%). Reflecting low demand or pricing adjustments by procedures/importer.
- c. Alcohol and tobacco prices also declined (0-.1%), possibly due to tax policy changes or reduced consumption.

2. Sectors that Experienced Price Increases:

- a. Transportation rose (+0.1%), possibly reflecting higher fuel costs or increased public transport fares.
- b. Household equipment increased (+0.1%), possibly reflecting higher cost of imported raw materials.

Annual Inflation Increase (+1.8%) from August 2023 to August 2024

1. Main Contributors to the Increase:

- a. Food and non-alcoholic beverages (+3.6%) show significant inflationary pressure, possibly due to global supply chain disruptions.
- b. Education (+2.0%), recreation and culture (+1.9%), and health (+2.3%) have increased, reflecting higher service costs and changes in government subsidies.

2. Categories Experiencing Deflation:

- a. Alcohol and Tobacco (-4.5%), likely due to changes in selective tax rates or import policies.
- b. Household equipment (-0.6%) and housing (-0.1%) showed slight declines, possibly related to stability in the real estate market and household consumption.

Comparison of Tradable vs. Non-Tradable Inflation

- a. Tradable inflation increased (+2.1%) indicating rising prices for imported goods

Non-Tradable inflation also rose (+0.8%), suggesting price increases in local services such as transportations, healthcare, and education.

CONCLUSION

In a democratic law state, the government invests in both capital and social development, focusing on enhancing public infrastructure to promote economic growth and strengthen its control. This investment aims to improve governance through measures such as tax inflation and tax reduction. The article concludes that the reduction of selective taxes is a crucial factor for fostering development in our country, particularly because we have not achieved a sustainable economy and still rely heavily on oil and imports. Therefore, it is essential for all stakeholders to engage in activities that promote and develop our economy.

Regarding policy implications and recommendations, the impact on consumer purchasing power is significant. While lower prices for essential goods, such as food, could enhance consumer purchasing power, increasing costs in other sectors like transportation, education, and healthcare may counteract these benefits. Consequently, there is a need for price stabilization policies. The government should consider implementing subsidies or market interventions to maintain price stability in food and transportation sectors. Additionally, the role of selective taxation cannot be overlooked; tax rates on alcohol, tobacco, and motor vehicles directly influence prices and

consumption patterns. Further analysis is necessary to evaluate the balance between generating government revenue and promoting social welfare.

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