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Doing taxes better

The Pakistan Institute of Development Economics (PIDE) recently organized a conference, 'Doing Taxes Better: Shifting the Paradigm on Tax Policy and Administration', to unbundle the taxation system of Pakistan for critical reforms by considering key questions: what is wrong with our tax policy? Why can't we fix it? Tariffs for trade or revenue? Technology, administration and documentation trio to improve tax collection and tax policy certainty?

Renowned national

and international

experts addressed

these questions and

put forth solutions.

Why do we need

taxes in the first

place? We certainly

don't like them. The

simple answer is

that taxes are the

only way to generate revenue for public spending on goods

and services. One can argue why we need to spend in the first

place, but let's put that question away for some other time.

But for the time being we know that the government spends

and we need taxes to finance that as the government don't

have many resources other than that. So, an ideal taxation

system would generate sufficient revenue to meet the needs

of the government without discouraging economic activities

and promote justice.

Pakistan's government, on the one hand, is working hard to

increase tax revenues to overcome budget deficit and finance

its fiscal needs. Official data, as reported by the Economic

Survey of Pakistan 2018-19, predicts that total tax revenues

will increase from 9.1 percent of GDP in FY2009 to 13.9

percent of GDP in FY2019 (budget estimates) with a possible

composition showing that 40 percent tax revenue is

generated from direct taxes while 60 percent is generated

from indirect taxes.

On the other hand, empirical literature has documented a

negative impact of taxes, especially if taken as percentage of

GDP on economic activities. This implies that a simple tax

increase to finance expenditures is not useful to promote

economic growth or development. Especially if there are

fissures in the economy and it faces structural challenges

ranging from low productivity, low economic growth, weak

and unproductive industrial base, increased poverty and

inequality, stagnant exports and above all the climate change.

So, the apprehensions for the current tax regime and

structural challenges in the economy present a daunting task

for tax policy reforms. We have had quite a few of them ever

since the beginning of Pakistan's economic life. So, it has to have a perspective of efficiency, equity and be revenue buyout. The ultimate question is: how can the tax system be best designed to promote inclusive growth? The decline in growth requires a debate on how tax policy can be used to bring back economic growth or at least stop the haemorrhage it is inflicting on it.

The conference provided useful insights to design a 'growth-oriented tax policy'. The prevailing tax system is unjust, outmoded and unproductive with high taxes, yielding low revenues made worse by complex, time-consuming and costly operational procedure as narrated by Dr Ikramul Haq who was one of the panellists of the conference. He further asserted that haphazard tax collection through multiple authorities at the federal and provincial levels is a major hindrance towards optimizing revenue collection.

The IMF resident representative argued that Pakistan's tax system is characterized by a low level of collection, large level of complexity, aimed at addressing too many objectives, fragmented, and with a large underutilization of certain taxes. As a consequence, the system leads to widespread economic distortions, inequality and an erosion of competitiveness. Pakistan urgently needs structural reforms to ensure robust revenue mobilization, while maximizing efficiency, equity, neutrality, and simplicity.

This call for simplification of the tax policy as well as a need to impose the same level of tax on income irrespective of source. There is a need to remove distortions through comprehensive taxation of personal incomes and move away from notions of fixed taxation on incomes from dividends and interest.

The conference also highlighted the need to shift the tax mix away from income tax towards taxes that have a less negative impact on economic growth, including property, wealth, inheritance and last but not the least consumption taxes. There are looming questions on the role of political economy, the debate of 18th amendment related ownership of tax bases to name a few. Dr Ikramul Haq raised a very pertinent argument that after the 18th Amendment raising revenue is a federation question not a central government domain only.

The one-liner takeaway is that there is an urgent need of governance reforms to make a growth-oriented tax policy but the 'will' to reform the tax system by the stakeholders is missing – thanks to elite capture and crony capitalism. The question to "how to break this vicious circle of elite capture" remained unanswered – despite knowing the answer.

The conference provided a platform to kick-start a new debate on tax system reform in Pakistan by examining the country's prospects for inclusive growth while going through the demographic dividend phase. It will help policymakers and other stakeholders to connect the missing dots in tax policy not only to increase tax collection but also to promote growth and equity in the country.

We believe the debate on tax policy needs many rounds. There is also an urgent need to reconsider inheritance taxes as a sustainable source of resource growth and an equitable resource transfer among generations. Unfair resource redistribution across generations can reduce the competitive growth perspective. We used to, but can we again use wealth taxes as a tool to mitigate income and wealth inequality and promote social mobility with equal opportunities?

Environmental taxes, such as carbon taxes, principle-based taxes and others offer a potential source of expanded revenue with equity across generation and across fiscal jurisdictions.

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