

Books

Huzaima Bukhari and Ikramul Haq. *Tax Reforms in Pakistan: Historic and Critical View*. Islamabad: Pakistan Institute of Development Economics, Islamabad. 2020. 299 pages.

In their book entitled *Tax Reforms in Pakistan: Historic & Critical View* authors Huzaima Bukhari and Ikramul Haq take up the important yet often under-researched topic of the taxation system in Pakistan. The book is a collection of various writings on the topic by the authors spanning over three decades and has been published online by the Pakistan Institute of Development Economics (PIDE).

The opening sections include a coherent overview of the issue by PIDE Vice-Chancellor Dr. Nadeem Ul Haque in the Foreword, along with the Preface in which the authors themselves provide a succinct summary of the dilemma at hand. The main body content of the book is further divided into three sections: *Issues, Past Legacy & Current Challenges, and Solutions*.

In the Preface, the authors begin by mentioning an instance that is representative of successive governments' general attitude towards the issue of taxation in Pakistan. In 2014, the government set up a Tax Reforms Committee (TRC) to "review and rationalise direct and indirect taxes, customs tariffs, the structure of FBR, evaluate the possibility of creation of border security force and ponder any other issue that it seems fit." Interestingly enough, the TRC was given just 120 days to complete its task. The finance minister and the management within the Federal Board of Revenue (FBR) were "naïve" enough to assume that a task as monumental as coming up with a well-researched reformative agenda for the tax system in the country could be completed in just 120 days. Naturally given the size of the work at hand, TRC took 500 days to submit its final report. This report has not yet been published by the government despite it being in circulation through alternate channels. Among the many important points the TRC's report makes, it also lists which according to the authors is one of the fundamental issues that afflicts Pakistan's tax system i.e. the system is regressive in that it "exhorts from the masses" while continuing to give out innumerable tax exemptions and concessions to the rich and mighty. Indicative of this regressive trend is the record level of tax expenditure (concessions) of about 1.5 trillion rupees handed out by the government in FY 2019-20. Another significant issue that the authors take up here is the dire need for an effective tax administration system. According to them, the failings of the current system under the FBR are highlighted by the fact that the bulk of all income tax revenue comes from withholding taxes.

In the first section titled *Issues*, the authors revisit the often misleading narrative that most people in Pakistan do not pay taxes. They feel that it is absolutely important to point out the simple yet often not understood difference between "taxpayers" and "return-

filers". The fact is that even in the government and within the tax administrative setup itself there are those who mix up the two concepts. While there are only about 3 million tax return filers in the country, this is not fully reflective of the number of people who pay taxes since many more people pay taxes at source in the shape of withholding taxes and sale taxes on the consumption of goods and services. In fact, since 1991-92, FBR has mainly relied on a combination of indirect sales taxes and withholding taxes to generate the bulk of its revenues. Authors mention that in the latest amended version of the Income Tax Ordinance (2001) there are about 65 withholding tax provisions.

The poor performance of FBR at collecting the revenues has meant that the government most of the time is in deficit; with this deficit hitting record figures of about 8.9 percent of the GDP in 2019. In response to pressure from governments that are perpetually in deficit, the FBR has resorted often at the behest of IMF and donors' consultants to increase the effective tax rates on the existing narrow base of taxpayers. The authors believe that this policy is misguided as it stifles the ease of doing business and incentivises tax evasion by those present within the existing narrow base. A better approach in their opinion is to reduce the effective tax rate and build a broader base. If the tax rate is suitably low, the base would be broadened as the businesses would have less incentive to evade taxes given the low compliance costs.

Furthermore, the authors point out how the revenue collection performance of the provinces is even worse than that of the center. The share of provinces in the total revenue collected by all federating units fell to 11 percent in 2019. For the authors, the fragmented tax system is partly to blame for the poor performance of the provinces and that the time is ripe for the FBR and all other provincial tax authorities to be abolished in favour of a consolidated National Tax Agency (NTA). A consolidated tax agency will bring simplification and clarity within the system which currently is overly complicated and cumbersome. For instance, there are about 70 different unique taxes administered by 37 different tax authorities.

Another important issue that the authors bring to attention is the huge untapped black/informal economy in Pakistan, which, according to them is worth around 50 trillion rupees. Effective measures to bring even a small fraction of this informal economy into the system can significantly add to increasing the formal tax-to-GDP ratio.

In the section titled *Past Legacy & Current Challenges*, the authors point out how, despite numerous reform efforts, the FBR has neither made any significant headway towards increasing the number of filers in the country at a sustained rate nor has it been able to increase the tax-to-GDP ratio in general. The performance of FBR at being an effective income tax collecting authority can be summed up by the fact that about 67 percent of all income tax revenue came from withholding taxes in FY 2018-19. According to the authors, in addition to FBR's lackluster performance as a revenue collecting authority, another important contributing factor to the narrow tax base in the country is the high effective tax rate which serves as an incentive for individuals and firms to evade taxes. Despite this, the authors state, on the behest of IMF and international donors, successive governments have continued to push for more and higher taxes on the narrow tax base of the country.

Despite their emphasis on income tax in the first part of this section, the authors are quick to point out that income tax revenue is only second to sales tax revenue in the

country with sales tax receipts contributing the most to total revenue collected by the FBR (FY 2018-19) The authors mention how despite tall claims being made, there is no reliable data that is regularly published on the active registered sales taxpayers in the country. Furthermore, the bulk of the sales tax collections is made from a handful of products.

The real issue the authors believe when it comes to successive governments being in deficit is the reckless spending by the state. Due to this wasteful expenditure, the government often finds itself in a deficit and then compulsively borrows from IMF and other sources. It is imperative that the size of the government be reduced and wasteful spending curbed for long-term macroeconomic stability.

In the last section titled *Solutions*, the authors begin by stressing the need to establish a National Tax Agency (NTA) to overcome the fragmentation in the current taxation regime. According to them, the current system is seriously fragmented across the provinces and the center. They suggest abolishing FBR and all other federal and provincial tax authorities and replacing them with the National Tax Agency (NTA). According to them the “mode and working of the NTA can be discussed in the Council of Common Interests (CCI)” and its “control can be placed under the National Economic Council (NEC)”

Furthermore, the authors believe that there is a fundamental level of mistrust between the taxpayers and the tax collecting agencies. While numerous reasons for this mistrust, primary reasons include the “highhandedness, maladministration, inefficiency, abusive behaviour and corrupt practices of FBR officials.” Additionally, the mistrust also stems from the fact that continuous governments have failed to use taxpayers’ money transparently leading to increasingly more and more taxpayers losing confidence and defying taxes. The authors suggest that a “Taxpayers Bill of Rights” should be introduced and adopted, one which “safeguards and strengthens the rights of taxpayers” and ultimately paves the way for a renewed level of trust between taxpayers and tax collectors. In addition to the Taxpayers Bill of Rights, the authors also suggest revamping the current tax appellate process through the formation of a National Tax Tribunal, one that is independent of the tax-collecting agencies and that of the Ministry of Law.

The last section also highlights the fact that Income Tax Laws in Pakistan historically have been drafted and promulgated through non-representative processes. The last two Income Tax Ordinances (1979 and 2001) were promulgated during military rule. The need is to introduce a new income tax law which is only adopted once it has been duly deliberated upon. The new income tax law according to the authors should be drafted as such that it ensures as much “uniformity of treatment” for all taxpayer categories as possible, should target reducing the overdependence on withholding taxes, minimise tax exemptions and encourage voluntary compliance through suitable nudges/incentives.

The authors also mention the need for revamping the sales tax regime in Pakistan. They suggest that the country should introduce a single Harmonised Sales Tax (HST) on all goods and services. The HST should be administered under the ambit of NTA where a balance between provinces and the center can be maintained. Furthermore, the introduction of HST should mean that the policy of taxing different goods at different rates should stop. The harmonised sales tax would ultimately, according to the authors,

simplify the system, increase compliance through a reduction in compliance costs, and reduce the dependence of authorities on a limited group of goods for revenue collection.

To conclude, Huzaima Bukhari's and Ikramul Haq's book is a great starting point for anyone looking to acquaint themselves with the issues that afflict the taxation system in Pakistan. The book is meticulous to the point that it can be used by policymakers, but also at the same time remains accessible to a wider non-technical audience. The authors' analysis although seemingly anecdotal in some parts of the book is generally backed by empirical numbers. The solutions that the authors suggest for the most part are actionable and the authors do an articulate job of manifesting this action-ability by delineating case studies and examples from other countries.

Having said that, despite the many things that the book gets right, it can perhaps be organised in a better manner. There is extensive overlap in information across sections and readers can get the feeling of some information being repeated too often. The repetitiveness perhaps is a byproduct of the fact that the book is a collection of writings spanning over three decades. Given the extremely revealing information presented in the book, the authors can perhaps work on writing a shorter yet thematically coherent book that presents all the information in an order that is conducive to more lucidity.

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