Taxing tax strategy?

EDITORIAL (November 28, 2012) : Although tax mobilisation performance of the FBR has generally been poor, it is never short of innovative ideas to raise the amount of revenues to the desired levels. According to a news item in the *Business Recorder* on 25th November, 2012, the FBR has now finalised a Three-Year Strategic Plan which will focus on expenditure-based assessment of the potential taxpayers. Under the plan, it will electronically document life pattern expenditures of the individuals for assessment of income tax and monitoring of expenditures will be done with the help of electronic database and information available with the tax department. Taking into account the expenditures made by any individual, the FBR would be in a position to serve "electronic notices" to undocumented persons. Once the base widens, tax rates would be brought down. The FBR is confident that its ongoing efforts will expand the number of taxpayers by another 4 million. The plan also talks about major steps on the sales tax side. The sales tax base would be enlarged with the help of electronic data available with the tax department and bogus sales tax refunds and input tax adjustments could be checked with the help of risk-based system. The inadmissible input tax adjustments would be controlled through effective checking of sales tax invoices and purchases made within the supply chain of VAT. Again, the checking of fake and flying invoices would be done with the help of electronic verification system to plug in the loopholes within the VAT regime. With these stringent measures in place, the standard rate of sales tax would be reduced from 16 percent to 10 percent and that of corporate income tax from 35 percent to 30 percent. The plan would also pay special attention to the border controls by the customs department. Border controls would be made more effective by setting up new checkposts at all important stations and employing a new force of efficient customs staff. The plan is reported to have been shared with the Ministry of Finance and would be discussed with the IMF. For the current year, the FBR is optimistic about amassing the targeted tax revenue of Rs 2,381 billion and raising the tax-to-GDP ratio to 10 percent as against 9.1 percent in 2011-12. It expects to collect Rs 150 billion by improving effective sales tax rate, Rs 120 billion through registration and investment schemes and Rs 50 billion through a recovery drive against non-duty paid smuggled cars during FY13. On the face of it, there seems to be nothing wrong with the Strategic Plan devised by the FBR. Tax revenues in Pakistan have continued to be at a dismally low level of below 10 percent of GDP during the past several years and need to be raised substantially by adopting a different approach in order to meet mounting expenditures of the government and improve the image of the FBR. The present performance of the FBR could be gauged from the fact that only 0.9 percent of the population in Pakistan is persuaded or forced to pay taxes as against 4.7 percent in India, 16.5 percent in Argentina, 58 percent in France and 80 percent in Canada. Another bad news is the revelation by the media that even this highly poor percentage of 0.9 percent was an overestimate due to overlapping of taxpayers - a discrepancy that has emerged from the data of Nadra when compared with the figures compiled and maintained by Pakistan Revenue Automation (PRAL), a subsidiary of the FBR. Embarrassing is also the fact that efficiency of tax officials in Pakistan is quite dismal. For instance, the number of active taxpayers per tax administrator in Pakistan is 64 as against 537 in India, 232 in Sri Lanka, 1990 in the US and 3182 in Switzerland. This is despite the fact that the government has increased the salaries of tax officials in Pakistan quite substantially and provided other incentives to improve efficacy of the tax department. Whether the proposed Strategic Plan is going to alter the situation and improve the ratios to the desired levels is of course a matter of conjecture but the experience suggests otherwise. In the past, FBR had devised many such plans, sometimes with the assistance of multilateral financial institutions, but the results have been generally disappointing. Besides, the new Strategic Plan seems only to be a rehash or retooling of the existing systems at the disposal of the FBR for which no such Plan was required. For instance, nobody is stopping the FBR from using life pattern/consumption expenditures as a secondary evidence for the purpose of assessment of income tax. In fact, in Pakistan like most other countries, income of an individual is the primary source for tax determination and he could always be asked to explain his pattern of expenditures for double checking or for the sake of consistency between the two. The present practice, if used skilfully, is, therefore, definitely a better approach for a variety of reasons including transparency and convenience. Similarly, a lot of emphasis has been placed on the use of electronic means in the new plan without realising that FBR could make use of such devices in a more professional manner without making any fuss or noises about this. These are routine improvements which, in our view, need to be carried out as a matter of course with the passage of time. Realistically speaking, the FBR, instead of depending on such plans, must concentrate most of its attention on improving efficiency and checking rampant corruption in its cadres without losing more time to deepen and widen the tax net. If it fails to do that, even the expected amount from various measures during FY13 would not be realised and the tax target of up to 10 percent of GDP would not be possible to achieve. Also, it is essential to do away with all sorts of tax exemptions and treat all kinds of incomes uniformly for tax purposes to eliminate various loopholes in the tax regime. If the political leadership of the country fails to guarantee such a level playing field, raising the tax-to-GDP ratio to a respectable level would continue to be an elusive goal. Besides, the economy of the country has to be revived and the writ of state has to be firmly established in all parts of the country to enable the FBR to bring more people into the tax net and deal properly with tax evaders. All these actions need a very close co-ordination between the government and the FBR (read: compiling correct data and using it) and unity of purpose among all the stakeholders. In the absence of a firm resolve and enabling measures on ground, strategic plans devised from time to time by the FBR would just be like gimmicks, spelling out attractive scenarios without much hope of successful outcomes.