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Less duty, more taxes?

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By Sultan Ahmed

Pak. Eco

AS the new year begins, the officials of the Central Board of Revenue commence formulating their budget proposals for the next financial year. In a country wanting larger revenue resources all the time a number of new taxes are proposed, some earnestly and some to ascertain public reaction to them.

We are told the maximum import duty is to be brought down from 25 per cent to 20 per cent from next financial year. Several countries in the region have lower rates of import duties. For Pakistan it is a great climb down from 125 per cent duty in 1990-91 and 80 per cent in 1993-94. Finally, it dropped down to 25 per cent in 2002-03 and we may have a 20 per cent maximum duty from July. This is a global trend, and the WTO wants a duty-free world so that trade between nations is conducted on the basis of the survival of the fittest.

Anyway, high import tariff or non-tariff restrictions are a temptation to various smugglers to crack the system and gain by that in a big way, while such countries lose their customs revenues. The best example of such illegal transactions is the flourishing informal trade between India and Pakistan, which is on the rise.

Now the chairman of the Central Board of Revenue Abdullah Yousuf says the entire export of textiles and related items are to be brought under zero-rated tax which will help resolve 70 per cent of the sales tax refund problems. If that helps stop textile traders from claiming rebates for exports which they did not make that will be a significant achievement. There has been too much fraud in this sector, often with the connivance of the taxa-

tration of the current tax base has been stabilised. When will that be?

The fact is that sales tax is the largest single source of revenue for the government. It is budgeted to provide Rs. 249 billion this year against Rs. 174 billion from income tax. And the government has reasons to be delighted by the large income from this single source with its hefty levy of 15 per cent. But the CBR argues the sales tax revenues from domestic sources have been falling, and that demands sales tax on goods produced and used in the country, and the varied services like real estate operations.

But there can be stiff opposition to taxing bricks and cement blocks on three valid grounds. Firstly, it will make house-building far more costly after cement and steel price have shot up. Secondly, it will be cutting across the official policy to promote small industries and micro-enterprises. Thirdly, it will deprive a number of kiln workers of their employment at a time when the government has

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engineers etc., are charged sales tax on their services the income of the government can be very large. But will these professionals pay the full tax. And will those who hold coaching classes in institutes and collect large sums pay full tax?

The government will be trying to levy sales tax on new items and services at a time when inflation or consumer price index has risen to 9.95 per cent by the end of February. There is no abating of inflation despite the directive of the President Musharraf to the chief ministers to lower the inflation and reduce the high prices. In such a context should the spread of sales tax to new areas be allowed to make the situation far worse, except in real state?

Inflationary pressures are bound to go up and assert themselves when the demand pressure increase. And demand pressure will increase when the money supply increases drastically as has been happening in Pakistan and banks with surplus credit are looking for credible borrowers. When the banks prefer the high paying consumer banking the demand pressure on the market will be felt all the more. And the money will circulate fast as is happening in Pakistan now.

Money supply in the country in the current financial year rose up to February by 10.4 per cent, while the target for the whole year is 14.4 per cent which will be fulfilled, says the prime minister. The private sector until February received bank credit of Rs. 309 billion compared to Rs. 230.5 billion in the same period last year.

If more money is chasing the same volume of goods, prices are bound to go up despite the faltering administrative steps at price control. The supply has to be increased to match the larger volume of money or meet the real needs of the people.

Amidst the discouraging

in this sector, often with the connivance of the taxation officials. Anyway, the genuine exporters have to be helped in a highly competitive textile world, with China in the lead, following the end of the quota system in 2004.

But one good news is to be followed by many bad news. The CBR proposes to make up for the loss of five per cent import duty by spreading the stiff sales tax of 15 per cent over a number of items and services, which can make life far more costly. In the case of sales tax, the government always says it has not levied a new tax but merely withdrawn the old exemption as sales tax is levied on every conceivable goods and services and then withdrawn to be re-applied when it suits the government. So even when it comes up with hefty additional taxes it claims it has levied no new tax which is technically correct but factually not. And a 15 per cent sales tax on any item or service is hurting the tax-payers who get very little or nothing in return for the taxes they pay.

Despite an increase in income tax revenue, indirect taxes still form 68 per cent of the tax revenues. A fair mix is said to be 50 per cent of the revenues as taxes on income and 50 per cent as indirect taxes. But in Pakistan indirect tax revenues still form more than two-thirds of the tax revenues. In reality, the industrialists, importers and traders charge the people far more than they pay as taxes. Direct tax revenues, too, are adjusted while fixing the prices so that the seller is always the gainer by several times than the taxes he pays. There is no competition in this but a consensus on high profits in an overhaul high profit economy, in fact the highest in the region.

The CBR now proposes the government should levy 15 per cent sales tax on bricks, cement blocks, computers — hardware and software — certain specified machinery and real estate. It proposes 15 per cent sales on all services, except residential rent and health, education and financial services once the administration promised to provide more employment, particularly for the very poor.

When it comes to taxing the computers — hardware and software, there will be widespread resistance. The protesters can argue that even before computers can become popular and widely used the government is cutting across its own enlightened policy. There may be a nationwide support for levying sales tax on real estate but if that means further increase in rent rates, that will be opposed.

The fact is that property prices have risen four to eight times in recent times. And those who made Rs. two to Rs. three crore on a small plot of land with a modest house and far more on large houses did not pay any income tax, while a widow or pensioner getting Rs. 100 out of her or his bank deposits paid Rs. 10 withholding tax. The law should force those who made crores of rupees out of a small investment to pay proper income tax, though not the standard rate. But now the property rates have come down by 20 to 30 per cent, they will argue following a sales tax on real estate transactions, they are being made to lose at both ends and their bonanza has become a bane.

There is resistance to sales tax, and desperate attempts to evade that by businessmen while charging their customers full sales tax, as it has a very high 15 per cent rate. In South-East Asia it is between three and six per cent. In Japan, it used to be three per cent, as in Singapore. But Pakistan raised its sales tax rate from 10 per cent to 12.5 per cent and then to 15 per cent, and for some categories even 20 to 22 per cent.

Earlier there were reports the GST would be lowered to 10 per cent and spread to more items. But now it seems the rate would remain 15 per cent, and yet be spread to a larger number of new items and services.

It has been reported that professionals, too, will be charged sales tax for their services. If lawyers, doctors, architects, needs of the people.

Amidst the discouraging news in the consumer sector, comes the statement of the minister for water and power Liaquat Jatoi, that the government is fixing power rates for four to five years. Will that really come to pass before we have the large dams for hydel power that we are seeking and when world oil prices are high and the oil producers, particularly the Opec members, intend to keep it that way so that they can get 40 to 50 dollars a barrel regularly.

Meanwhile the Asian Development Bank has cancelled some important project loans in the water sector as the loans were not used well in time.

Simultaneously the World Bank has asked the Pakistan government to finalise its water policy within a month, complete with the dams proposed to be built for power and water. Tariq Hameed, chairman of WAPDA, says the WAPDA is ready to start work on the Kalabagh dam or Bhasha dam depending on which dam the government finally chooses. Much work has been done on the Kalabagh dam and so it is easy to start work on that immediately. If instead the President settled for Bhasha dam work on that will begin right earnest. Anyway the World Bank is forcing the government to take a decision quick instead of dragging its feet for too long.

The old project to bring 1,000 MW of power from Tajikistan to Pakistan via Afghanistan is also to be revived. The project was conceived in the days of Nawaz Sharif as prime minister and referred to from time to time. The disturbed state of affairs in Afghanistan stood in the way. But things are much better in Afghanistan now, and one final bid should be made to implement the project or given up for good for better times in the region.

The prime minister has now appointed a committee of 12 members comprising ministers, secretaries to government and members of parliament to keep a watch on prices and monitor the supply and demand situations.