**[Five-point agenda for tax reform](https://www.dawn.com/news/1768282/five-point-agenda-for-tax-reform)**

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PAKISTAN has a history of turning to international financial institutions (IFIs) for a solution to its long-drawn tax issues. The World Bank, Asian Development Bank (ADB), IMF, and the UK’s FCDO have been supporting tax reforms at the federal and provincial levels for years. Since FY20, the IMF has been providing technical assistance to the FBR on medium-term tax policy and revenue administration. In August 2022, the ADB [announced a loan of $200 million to Pakistan](https://www.dawn.com/news/1703853) for a resource mobilisation programme. From a macroeconomic perspective, given the critical role of revenue mobilisation in Pakistan’s fiscal sustainability, the donor-funded tax reforms seem conceptually tenable.

The [2019-2023 IMF programme](https://www.dawn.com/news/1491889) had envisaged an increase in tax revenue mobilisation by four to five per cent of GDP through reforms of personal and corporate income taxes and GST to bring it close to the tax level in lower- and middle-income countries at 15pc to 20pc. However, at the end of the programme, notwithstanding an increase in absolute terms, Pakistan’s tax collection as a ratio to GDP declined.

Ironically, despite multiple foreign-funded tax reform projects, the outcomes have been disappointing. The history of World Bank’s 2005-2011 Tax Administration Reforms for Pakistan is a classic example; the bank itself noted in the project evaluation report that “the project [TARP] was not able to substantially contribute to strengthening revenue mobilisation capability of the government of Pakistan, the primary development challenge that the project aimed to address … the overall outcome is rated moderately unsatisfactory”. Similarly,the outcome of the bank’s 2019 Pakistan — Raises Revenue Project also does not seem too fruitful: by the end of FY23, Pakistan’s tax-to-GDP ratio was 10pc (of which FBR taxes constitute 8.5pc) compared to the project’s target of 17pc by FY24.

In part, the reason why IFI-led reforms fell short of the objectives is because external technical consultants typically come up with one-size-fits-all solutions, which in most cases do not work. For instance, it was delusional to expect the system of voluntary tax compliance (on which TARP was centred) to deliver in a country where it is hard to implement procedures of strong and effective tax audits, enforcement, and strict penal actions against tax evaders. At the same time, however, a lot boils down to the lack of political will, loopholes in tax policy rooted in fiscal federalism, institutional weaknesses, and corrupt practices within the tax system.

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Ergo, the country needs tailored, strategic solutions to our tax woes that address the underlying issues and are supported by domestic efforts, strong political determination, and equitable taxation policies. Coming to home-grown solutions, we need to deal with everything ranging from addressing policy-related gaps to issues of implementation and interface with taxpayers. Here I propose a five-point agenda, that confronts the realities of Pakistan’s underlying problems, as the foundation of various facets of reform.

First, there is a need to define and clearly communicate the vision of our tax policy and exercise strict adherence to it. The principle of equity — both horizontal and vertical — should supersede all other tax objectives. Horizontal equity means that all equals should be taxed equally, and vertical equity means that all unequals should be taxed unequally. In Pakistan, both these principles have been consistently compromised. The rich pay the least, whereas the salaried class and a few industrial and business sectors carry the entire tax burden.

Second, weak provincial tax collection means that the centre remains under pressure to spend on matters that lie under the provincial domain. In addition, weak provincial taxation exacerbates the problem of equity. Although provinces enjoy the constitutional authority to levy and collect agriculture income tax, sales tax on services, and provincial property tax, the slackness in their efforts is evident from the fact that they collectively cannot mobilise taxes even up to 1pc of GDP. Despite such performance, provincial tax authorities do not receive the kind of flak the FBR gets for low resource mobilisation.

Third, adhocism has to be done away with. In their desperate attempts to meet revenue targets, governments take stopgap measures to improve tax numbers. The use of tax/duty rate increases, imposition of advance/withholding taxes, or withdrawal of exemptions are the easiest tools to raise incremental tax revenues. The frequent recourse to these measures has made our tax system highly inelastic and is often in conflict with long-term economic policy objectives and strategic goals. For instance, the imposition of withholding taxes on cash withdrawals and non-cash banking transactions in the not-too-distant past impaired financial inclusion and increased informality in the economy.

Fourth, there needs to be a strong and effective audit mechanism in place. Voluntary compliance is important. However, results from over-reliance on half-hearted administrative measures to minimise evasion have been elusive. Therefore, voluntary compliance must be backed by robust audits along with stern enforcement against tax dodgers and delinquents. Heightened risk of being caught and associated penalties can be a strong deterrent to concealment and under-reporting of income.

Fifth, a serious institutional reform of the FBR is crucially needed. This institution needs to be restructured into a professional, autonomous organisation with an independent board consisting of eminent personalities qualified in the fields of economics, public policy, law, chartered accountancy, finance, business administration, and IT. The board should drive the vision and strategic direction of tax policy and exercise oversight over the management of tax administration. Its members, having no conflict of interest, should be appointed for a fixed term with legal protection against undue pressure. A change in the incentive structure in FBR will promote a culture of transparency and integrity. Such a restructuring plan is also needed in provincial revenue authorities. Indeed, without first fixing the institutions, all other types of reforms may be akin to throwing good money (often borrowed foreign exchange) after bad!

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