**Taxation and inflation**

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The Federal Board of Revenue (FBR) has claimed collection of net revenue of Rs4,493 billion in the first eight months of the current financial year against Rs3,820 billion collected in the corresponding period of last year, depicting a year-over-year growth of 18 per cent. The FBR needs to collect Rs3,148 billion in the remaining four months (Rs787 billion per month).

The FBR's target for FY2022-23 was revised from Rs7,470 billion to Rs7,641 billion in the wake of the Finance (Supplementary) Act, 2023 (commonly known as mini-budget). However, the FBR did not revise the monthly target of Rs527 billion for February 2023, despite a massive increase in federal excise duty and one per cent increase in general sales tax (GST).

In its press release, the FBR has claimed the following: “as per the provisional data, direct tax collection grew at a robust pace of 47 per cent during the first eight months of the current financial year which is reflective of the government’s policy of making taxation progressive and equitable through shifting tax burden towards society’s wealthy and affluent segments…” Second, “….[the] FBR has also stayed on top of addressing exporters’ liquidity needs through issuance of Rs235 billion in refunds during the first eight months of the current financial year as against Rs198 billion during [the] corresponding period of last year-a year-over-year increase of 19 per cent”.

In the FBR’s press release, there is no bifurcation of collection under the heads: income tax, sales tax and federal excise duty. Out of the total collection for the eight months of FY 2022-23, according to a news report, 53 per cent came from indirect taxes. Even under income tax, major collection is from advance taxes, before computing real income or loss, and withholding taxes on transactions. These have serious impacts on businesses, already facing severe cash flow issues due to the prevailing precarious position of the economy.

The report, while confirming the FBR’s main reliance on indirect taxes, mentions income tax collection upto February 28, 2023 at Rs1.96 trillion. Though it admits that the FBR exceeded the target of income tax by Rs47 billion, it points out that on the last day, collection under this head was Rs39.9 billion, “which was unparalleled, thus deepening suspicion of resorting to the old habit of taking advances”.

It is well-established that many withholding provisions in the Income Tax Ordinance, 2001 bear the nature of indirect taxes that not only adversely affect the salaried class and the poor but are also among the factors triggering high inflation that reached 31.5 per cent in February 2023.

The dilemma of our successive governments – civil and military alike – has remained the same: on the one hand, they want to lower inflation and on the other they praise growth in regressive taxes. By reducing and rationalizing taxes on fuel used for electricity generation (ultimately passed onto consumers), the government could have avoided a further increase in tariffs, especially the permanent electricity surcharge of Rs3.23 per unit imposed on March 1, 2023. The FBR collects sales tax based on 100 per cent billed amount, irrespective of recovery or otherwise.

All retailers, having commercial connections but not falling in Tier-1, pay five per cent sales tax with electricity bills where total monthly bills do not exceed Rs20,000, and at the rate of 7.5 per cent where the monthly bill exceeds this threshold and additional three per cent sales tax in the case of unregistered retailers. The electricity supplier is bound to deposit this amount without adjusting any input tax.

Sales tax collected through electricity bills was Rs149.5 billion in FY 2021-22. It was the highest number, followed by petroleum, oil and lubricant (POL) products at Rs107 billion. Income tax collected with electricity bills, for other than companies, is not adjustable up to Rs43,200 under Section 235 of the Income Tax Ordinance, 2001. In FY 2021-22, total collection under this head was Rs71 billion. These indirect taxes through withholding provisions are a big burden on small and medium enterprises (SMEs) but never highlighted in any research or in briefings to the prime minister by the FBR or members of the Economic Advisory Council (EAC).

According to the Pakistan Telecommunication Authority (PTA), the total number of cellular subscribers as on January 31, 2023 was 193 million (86.19 per cent teledensity), out of which 123 million were mobile broadband subscribers (54.91 per cent penetration), three million fixed telephone subscribers (1.17 teledensity) and 126 million broadband subscribers (56.31 per cent penetration). Thus, at present, the entire taxable population and even those having no income or income below taxable limit are paying advance and adjustable 15 per cent income tax as prepaid or postpaid mobile users. However, there is no recognition of this fact.

Around 110 million unique mobile users are paying advance/adjustable income tax but Pakistanis are labelled as tax cheats – a highly lamentable act. Total income tax filers, according to the FBR’s Active Taxpayers’ List, updated on March 13 2023, were 3.3 million. The FBR should register all taxable persons to bridge the huge tax gap and stop extorting 15 per cent oppressive tax from the poorest of the poor.

The above facts and the following figures of the Sensitive Price Indicator (SPI) released by the Pakistan Bureau of Statistics (PBS) for the week ending on March 9, 2023, escaped the attention of the prime minister, members of the EAC and leaders of the PDM: The year-on-year inflation increased to 42.27 per cent. Prices of onions shot up almost 305 per cent, followed by 78.63 per cent increase in prices of eggs, 78.14 per cent in broken rice, and 82 per cent in wheat over a year.

Cooking oil prices were higher by 51 per cent and wheat flour by 56 per cent. Food inflation rose more in rural areas than in cities. In rural areas, it increased to 47 per cent and in cities, it jumped to 42 per cent.

Core inflation, calculated by excluding food and energy items, also increased in March 2023 to 22 per cent in rural areas and 17 per cent in cities – considering the State Bank of Pakistan increased its policy rate from 17 per cent to 20 per cent. It will further push stagflation.

The prime minister and his economic team need to be reminded of the famous quote of Milton Friedman: inflation is taxation without legislation. In the coming federal budget, if they want to give relief to people, they must reduce rates of all taxes, eliminate collection of sales tax and income tax at import stage and withholding taxes on electricity and internet/mobile use – in fact all withholding provisions having no nexus with income. There is a need to increase income tax for equity.

There is also a need to broaden the tax base. The FBR has 7.4 million registered income tax persons but return filers are even less than 50 per cent, including registered companies. Those who paid Rs1,534.3 billion as withholding taxes in FY 2021-22 under the Income Tax Ordinance, 2001 alone, conducting transactions worth billions of rupees, but not filing returns, should immediately be tapped. This action is long overdue.

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