**The Trinity of Taxation (Part I)**

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The purpose of the Government is to uphold and protect the natural rights of its citizens. So long as the Government fulfils this purpose, the laws given by it are valid and binding but, when it ceases to fulfil them, then the laws would have no validity and the Government can be thrown out of power. In Locke’s view, unlimited sovereignty is contrary to natural law. The government derives its authority to collect taxes from the constitution which is the ‘grundnorm’. According to Hans Kelsun, the grundnorm is a part of a normative theory of law and the constitution is the highest form of normative structure.

In taxation, this normative structure provides the social contract between the people and the government. People reside their trust in the government by electing the public representative and giving them authority to levy taxes and the government is bound to spend the revenue so collected on the social and economic well-being of the people.

As Pakistan is facing the challenge of low tax collection, a detailed gap analysis was completed by the World Bank, which indicates that Pakistan’s tax revenue potential would reach 26 per cent of GDP if tax compliance were raised to 75 per cent, which is a realistic level of compliance for lower-middle-income countries (LMICs). This means that the country’s tax authorities are currently capturing only half of this revenue potential.

The values and attitudes of people in a society or an organization, both positive and negative, toward the tax system are part of the culture of taxation.

However, recent studies have indicated that tax collection could be enhanced by improving tax culture and removing the trust deficit between taxpayers and tax collectors through positive changes in their mindsets. Therefore, the challenge for Pakistan is to transform its tax culture which is shaped by interaction among the trinity of taxation i.e. the tax policy givers, tax collectors, and taxpayers.

The literature on taxation in Pakistan brings forth two sets of terms seeking to explain our lackluster tax performance i.e. terms related to tax policy and tax governance e.g. distortionary exemptions, concessions, weak enforcement, low compliance by taxpayers, reliance on indirect taxes and issues in improving tax administration. The second set of terms emanating from literature on public finance treats tax governance as a science and identifies its various characteristics such as buoyancy of the tax system, tax elasticity and tax yield as explanatory variables.

The op-ed series will explore the origins of these terms and the phenomenon associated with them in the mindset of the tax collector, tax policy giver and taxpayer and then develop a collective picture to show how the respective mindsets about these three sets of actors, through their mutual interaction, constitute a tax culture which is unhealthy. This op-ed series also uses concepts such as the Stanford Sociologist W. Richard Scott’s trichotomy of Regulative, Normative and Cultural Cognitive pillars and explains how the normative and cultural-cognitive approaches may be used for nudging citizens to be more responsive taxpayers.

Starting with Culture is that complex whole that includes knowledge, belief, art, law, morals, custom, and any other capabilities and habits acquired by man as a member of society. More aptly, culture in each society and organization is mobile, and is derived from a complex relationship between everyone in society and organization; it includes what those individuals “think” (i.e., ideas, knowledge etc.) and “do” (i.e. their behaviours and habits) as a member of a society or organization.

The term “culture of taxation” is not used frequently in social science literature. A country-specific tax culture is the entirety of all relevant formal and informal institutions connected with the national tax system and its practical execution, which are historically embedded within the country’s culture. The tax culture is the relationship between taxpayers and tax collectors in a tax system. The values and attitudes of people in a society or an organization, both positive and negative, toward the tax system are part of the culture of taxation.

From the tax collector’s side, the cultural issue is about the use of discretion. How do tax collectors use their authority to deal with a taxpayer? If tax collectors feel that they have more power than taxpayers, the posture of tax collectors is likely to dominate the taxpayer. The behaviour of the actors in a tax system is important.

The behaviour of taxpayers is about their decisions regarding tax compliance, tax avoidance, and tax evasion. The decision to comply with the tax law depends on the cost-benefit ratio in terms of the value of the tax evaded amount and the tax with penalties if caught. The tax and penalties are payable only if there is a high probability of being caught. The higher the probability of detection the more is compliance as the tax and penalty amount is higher than the original tax.

Tax Morale is also an essential part of tax culture. Tax morale is the intrinsic motivation of individuals to pay taxes which is determined by several factors. Trust in government institutions plays a significant role in tax morale and emanates from a perception of fairness. Once people perceive the tax system and tax authorities as fair, they will have more trust in those authorities and vice versa. Thus, the degree of tax compliance might rely on how people consider themselves and interpret their situation relative to others and they might not pay taxes if they perceive unfairness. Tax Policy Maker: Tax law and policy affect taxpayers’ behaviour, especially when the tax system is complex. The complexity of the tax system is the sum of compliance costs and administrative costs. Several studies find that high compliance costs are responsible for large informal sectors in developing countries. A good tax system needs to be least distortionary, have ease of collection, not discriminate, and be politically acceptable but Pakistan’s tax policy is not based on these well-known and clear principles. Ad-hoc tax revenue-enhancing measures through SROs and mini-budgets have developed a complex tax system that confounds principles of rational tax policy.

(To be Continued)

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