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Low-Tax to GDP Ratio: Causes and Recommendations

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Abstract

Tax to GDP reflects the Governments revenue collection through control over all the gross productivity of the nation. The present study highlights the causes of lack of resources for economic development of the country. It further suggests evidence-based policy for Pakistan to make it an industrialized and developed economy by 2025. Secondary data were used to conduct this research. The research found that lack of Political will, the rule of few through exclusion, biased and nepotism in legal & institutional environment like SROs in finance, industry and FBR, are the main causes of low tax to GDP ratio. The study concluded that Pakistan needs to improve its regime of tax collection for one-point agenda of leaving no income untaxed in the country. It should also focus on eliminating exemptions.

Keywords: gross domestic product, taxation, federal board of revenue, government

Introduction

The tax-to-GDP ratio is the ratio of the tax revenue of a country compared to the country's gross domestic product (GDP). It's ratio to measure how well the government can collect revenue compared to the size of its Gross Production (Kagan, 2023). A country's economic resources. Tax-to-GDP ratio is calculated by dividing the tax revenue of a specific time by the GDP. "Pakistan's tax system is ineffective, unfair, fragmented, and leaves out entire sectors of the economy, worsening structural economic imbalances," states Mr. Shahrukh Wani, Country Manager International Growth Centre, Zambia (International Growth Centre, 2023).

There are a few research in Taxation as a tool for development. This paper summarizes these and emphasise the reason for taxation, this paper made use of Professor Lewis seminal work," Taxation for development." Later economists like Sohail Ahmed, concluded that tax reforms were rolled back after 2008. While Shahid Kardar and Zubair Soomro gave a thought to smarter and leaner governments in the role of regulator only, thus

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unleashing the secular market fundamentals to boost the GDP growth & Pakistani economy.

Pakistan is one of the low performing economies in term of poverty elevation. Very little revenue is collected through tax to jump start any viable development plan by any government and it is forced to raise revenue by deficit financing through raising Public Debt. Till 2022, the economic system in the country was functioning business as usual, debt financing the Budget through International Donors and domestic credit borrowing, lack of incentive for any long term policy to avoid excessive debt and try to put in order their own house by increasing tax base and by including all sectors into net as per share in the GDP.

Experts have expressed disappointment over State's failure to collect taxes. Pakistan's lack of generating revenue through indigenous resources by tax net expansion and digging into the deep pockets of the less taxed sectors, are hampering economic development of the country. Pakistan is stumbling while regional competitors are leaping forward by increasing tax to GDP ratio- the vital source for the large-scale infrastructure and social sector development, in the absence or increase in it the take off stage of economic growth is impossible and the vision of present Government to make Pakistan an industrialized and developed economy by 2025 will remain an illusion.

There are historical and political factors behind this dismal state of affairs in revenue generation through taxation, which shall be discussed at length in the subsequent sections of this thesis, in brief the dependence and ease with which the foreign loans were made available to Pakistan were more to do with its strategic alliance in Afghan war and subsequent support to War against Terrorism, it lost the opportunity to use these funds in developing large scale public projects like Dams and Capital goods industries, which could provide the steel frame in which the economy can be built and dissipation of these funds in short term idiosyncrasies by dictatorial rulers both civilian and Military led to the drying up of this funding . Simultaneous inability to tax the citizens based on incomes in progressive manners did not develop the tax culture in Pakistan. The undocumented economy flourished and grew so large that it is next to impossible to bring in it in the accounting. Political expediency stopped valid Data-collection exercise of Population and economic census, without any concrete and accurate data any effort by the governments for redistribution of income and expenditures in the less developed sectors have created a stark income disparity in the federation and within the federating units also. The inability of public utilities to deliver and the social unrest due to inferior quality of life cannot leave the horizon of political decision making. The government will have to increase tax revenues and broaden tax net to jump start the economy. This should result in rise of employment rate, & in better social welfare Sector development.

Statement of Problem

Low Tax to GDP ratio is a persistent and perennial problem for Pakistan to sustain economically development for extended period. The overall tax-to-GDP ratio has varied between 9.5% to 11.4% 12. According to the latest data available, the tax-to-GDP ratio in Pakistan was 5.6% in December 2022 (CEIC, 2022). This is lower than the average of 7.6% for low-income countries and 14.1% for lower-middle-income countries (The World Bank, n.d.). The tax-to-GDP ratio in Pakistan has been a major economic issue for more than a decade now, the low tax-to-GDP ratio is mainly due to structural deficiencies in the tax and administration system.

Literature Review

A great deal of research, internationally & nationally, available about taxation and its general use in development. However, a few Pakistani scholars have delved into the subject per se. The open economic model for development and free trade and flow of capital favoured for the developing countries Lewis (1984), was also adopted by Pakistan with mixed success. Other researchers focused on historical facts of the Pakistani Taxation system through the eyes of collectors, Sohail Ahmed, according to whom the reforms were rolled back after 2008. While Shahid Kardar and Zubair Soomro gave a thought to the researcher of smarter and leaner governments in the role of regulator only, thus unleashing the market economy.

Taxation is a powerful tool that can help finance the achievement of the Sustainable Development Goals (SDGs) and promote inclusive and sustainable development. Taxation plays a central role in promoting sustainable development, and developing countries face significant challenges in developing their tax capacities and mobilizing domestic resources.

According to Stephen R. Lewis' book, Taxation for Development: Principles and Applications, tax policy can have a significant impact on economic development in developing countries. The author focuses on open economies and the ways in which openness to international trade and to movements of capital and skilled labour influence the scope for, and the effects of, tax policy.

In general, taxation can affect development in several ways. First, it can provide governments with the necessary resources to fund public goods and services such as infrastructure, education, and healthcare. Second, it can help reduce income inequality by redistributing wealth from high-income earners to low-income earners. Third, it can encourage economic growth by providing incentives for investment and entrepreneurship. Fourth, it can promote good governance by increasing transparency and accountability in government spending.

However, the relationship between taxation and development is complex. The effectiveness of tax policy depends on several factors such as the level of economic development, the structure of the economy, the political environment, and the administrative capacity of the state. Therefore, designing an effective tax policy requires careful consideration of these factors.

Pakistan has seen period of rapid growth in economy, but its failure to sustain it independently and to redistribute the created wealth amongst the have-nots; curtailed surplus wealth in the hand of few with very little propensity to save. Problem of revenue generation through broadening and deepening of tax net is always linked to the purpose for which Tax revenue is used, there is a big issue of credibility contributing to low tax levels. Obvious question is how to achieve it given the above narrative, in the absence of credibility of the State.

Investment in its Human Resource and Infrastructure is essential for taking off to the next stage of economic development (Khan et al., 2023), despite experimenting both military & democratic after the 1971 debacle. The Pakistani political class has been criticized for resisting reforms in important areas such as landholding and taxation. According to Zahoor (2018), for transforming predominantly agrarian economies of the world., in a broader perspective, land reforms encompass breaking up iniquitous concentration of land, reducing income disparities, improving land productivity, promoting rural employment, preserving socio-political stability, recording the tenant-landlord relationship on respectable basis, encouraging adoption of modern technologies for mass production and improving the overall income distribution of the economy. The same paper also investigates the history and politics of land reforms in Pakistan and analyses land reforms of Zulfikar Ali Bhutto in particular.

According to McCartney & Zaidi (2019) Pakistan has one of the lowest tax-to-GDP ratios in the world. It has been argued that Pakistan's class structure has been reconfigured over the past fifty years as the middle classes have become increasingly powerful and adept in their demands for political representation, government services and the redistribution of national wealth. However, its ruling classes - which are defined specifically as the economic and political 1% - have retained their hold on political and economic resources very successfully.

It is in the heart of the challenge facing Pakistan, in terms of achieving sustained higher rates of growth. International Growth Centre (2023) (IGC) research on property taxation, while working with the Excise and Taxation Department Punjab, deduced that increased revenue is possible if incentives are given to tax-collectors, same is true for incentives on compliance of for taxpayers. So, these are the kinds of building blocks that over time will lead to higher rates of compliance and higher rates of revenue generation. The last thing Pakistan needs is a proliferation of new taxes. What Pakistan needs is to make existing taxes much more effective in generating revenue by broadening the base. Propensity to save increase with the income, while in Pakistan, with the fall of national income savings have fallen too (Zahoor, 2018)

The deterioration of fiscal discipline was amplified by authors like Burki (2007), and Hussain (2004) paint a picture of deliberate political expediency to avoid the problem of internal revenue collection. Pakistani newspapers are always full of news of strikes called by powerful traders' lobbies and service sectors against documentation of economy and expansion in Tax net.

Methodology

This paper has used multiple methods to conduct the research on the topic, but it is all secondary in nature. Frequent recourse to Internet and web browsing acceded gold mine of information in fact, the real test of researcher's acumen was to sift through the information and research conduct internationally and nationally. The deduction method is used to untie the knots in mind of mine regarding the subject topic. What is gathered is exceptionally large but what could not be is larger still.

Regional Analysis

Competitiveness Rank in Pakistan averaged 111.77 from 2007 until 2019, reaching an all time high of 133.00 in 2014 and a record low of 83.00 in 2007.

Pakistan was at 133rd position out of 148 countries, in the Global Competitiveness Report 2013-14 (Schwab, 2013). It was at 133, 124, and 118; in last three annual reports of 2013-12, 2012-11, and 2011-12. Now it is at 110th ranked country in GCI in latest report of 2022.

In South Asia Association for Regional Cooperation (SAARC) all members are ahead of it, India is at (71), Sri Lanka is at (73), Nepal is at (102), Bhutan is at (103), and Bangladesh is at (109). In 2022 report India ranked 37th a jump of six places from 43rd in 2021, and Bangladesh is at 105 in Global competitive index report of 2019.

Pakistan has shown deficient performance on diversion of public funds from 76 in 2012 to 103 in 2013, in the same report. Ranking in the wastefulness in government spending have further deteriorated from 96 in 2012 to 116 in 2013. In comparison, India's despite declining 11 places in the index is still way ahead of Pakistan. It is comparing itself with ASEAN and BRICS, whereas Pakistan is lagging even in SAARC!

Pakistan even failed to cash on surplus funds available with west in the wake of 2008 recession when business investment was all time low in developed economies and emerging and less developed were important destinations for investment by foreign investors.

Burgeoning government regulations have hampered the ease of doing business, dropping to 82 from 62 in CGI 2013. The legal system of Pakistan is more non-responsive to private sector complaints as is stated by the report. Certainty of laws and regulations is not good in the eyes of the foreign analysts. Crony capitalism and monopolistic controls in every sector of economy suggests that there is collusion to restrict entry in the businesses.

In Pakistan, the important sources of provincial and local taxes are property, mineral, & agriculture income, tax on sales of services, which are still untapped by these provinces. At federal level collection of taxes proportionate to GDP is little lower than in India, Bangladesh, China, and Indonesia.

Pakistan tax its corporate sector heavily as compared to tax on incomes and profits at Federal level. It relies heavily on the regime of indirect taxes and withholding taxes to muster up resources.

The 3.4 percent of employed labour in Pakistan is a taxpayer, while registered taxpayers hover around 1.7 million this figure pales in comparison with total number of employed 58.31million, labour force in Pakistan (Sustainable Development Policy Institute, 2013).

Another index to compare regional competiveness is ability to 'Pay tax' index in the World Bank's Doing Business Report 2013. Pakistan's rank is at 162 in it (The World Bank, 2013).

Table 1

Statistics of South Asian Countries in World Bank's doing Business Report 2013

South-Asian Countries	Rank	Payments (number/year)	Time (hours/year)	Profit tax (%)	Labour tax and Contributions (%)	Other taxes (%)	Total tax rate (%profit)
Afghanistan	94	20	275	0	0	36.4	36.4
Bangladesh	97	20	302	25.7	0	9.2	35
Bhutan	71	8	274	36.3	0	4.4	40.8
India	152	33	243	24.6	18.2	19	61.8
Maldives	57	17	252	13.5	7.9	9.3	30.7
Nepal	114	34	326	17.2	11.3	3	31.5
Pakistan	162	47	560	17.9	15.1	2.3	35.3
Sri Lanka	169	61	254	1.6	16.9	31.6	50.1

The extent of revenue loss through tax evasion is estimated between 2 to 4 percent of GDP.

All of this suggests that Pakistan's competitiveness is disappearing internationally and regionally, very fast. It is due to war against terrorism which has led to neglect in R&D in all sectors of the economy. Pakistani Private sector is habitually rent seeker and has not yet attuned themselves to the new realities of global markets. It lobbies for relief in tax, from Governments in almost every year before budget, at the expense of the public. The large sectors of economy are untaxed or evade taxes. This leads to no improvement in the living conditions of the common person and simultaneously makes it less competitive internationally.

In Global Competitiveness Index, Pakistan's performance in Pillar of governance is exceptionally low. Nepotist patronage, & corruption have negatively impacted food, water, environmental security of Pakistan. It can be described as a weak & compromised state with a large black economy lurching with a legacy of political patronage.

Structure of Pakistani Taxation System

According to the Federal Board of Revenue (FBR), the tax collection system in Pakistan consists of two main types of taxes: direct taxes and indirect taxes. Direct taxes are collected directly from individuals or entities based on their income, wealth, or property, while indirect taxes are collected from goods and services (Maheshwari, 2023).

The FBR is responsible for collecting direct taxes in Pakistan, and it has released tax collection details for the fiscal year 2021-22. According to the data issued by FBR, the tax collection for the year 2021-22 was Rs5349 billion (ARY News, 2022).

After the passage of the 18th Constitutional amendment in 2010, collection of general sales tax on services has been devolved to provinces and they have constituted their own authorities to collect taxes and made some headway as far as collection is concerned. Services constitute 59.6% and agriculture 19.5% of GDP. Provinces have been empowered to collect taxes on agriculture as well as sales tax on services (ARY News, 2022).

It is true that where tax collection is more tilted towards indirect taxes, it burdens different segments of society differently and has an impact on economic development as savings of the middle and poor class are badly affected. In such a situation, there is a need for a gradual paradigm shift to achieve the goal of revenue targets on the basis of principle of justice and equity.

Traditionally taxation system in the country remained regressive as is given in the table below

Table 2
Pakistan's Taxes

Canon	Federal	Provincial	Local
Progressive	No	No	Not implemented
Certainty	#	Yes	#
Convenience	Partial	Partial	#

Canon	Federal	Provincial	Local
Economy	Yes	No	#
Productivity	No	#	#
Elasticity	#	#	#
Simplicity	Partial	Partial	#
Diversity	Yes	No	#
Flexibility	No	#	#
Desirability	#	Yes	#
Popularity	#	No	#
Buoyancy	#	#	#
Coordination	#	Yes	#

There arises from it, issue of legitimacy of the state to levy taxes.

Analysis & Discussion

In Pakistan, the reasons for weak tax culture are mainly the absence of clear agreement based on equity and greater good of public in revenue generation between the state and the elite, inefficient and archaic state tax collector apparatus, poor governance and public service delivery, perception of corruption in public institutions and a widely held belief that tax money will not be used for a better value, complicated filing of tax return and costly taxation system, a sense of joy ride for rich, arising from exemptions, and informal economy etc.

All these arguments have been used in other countries we have to see how they had transformed, as one great leader said that it is the responsibility of the state to convince the people what is best for the country and not that what is wished by the people. If egalitarian distribution and honesty of purpose is translated into result of greater service delivery, tax culture of Pakistan can change.

Culture

Laws are developed out of customs and social needs, oblivious to this important priori; Pakistani taxation laws are asynchronised with cultural realities of society, as society in general have no incentive to pay taxes, thus no culture of paying taxes could be deepened in Pakistan.

The urban-based power groups and political parties may argue, to appease their constituents, that taxes on urban businesses are not justified unless agriculture and agro-based businesses located in the rural areas are taxed (political argument). Taxes other than religious levies i.e. zakat and usher are not in line with the injunctions of Islam, hence paying taxes is not justified to a state that is not Islamic (religious argument but fallacious). The sub-continent was ruled by the colonial powers for a long time and whenever a colonial power, imposed taxes on its subjects, it had to face resistance from the people. Only Parliament under Constitution of Pakistan can impose taxes in the country, which sadly is filled with MNAs, who would never like to impose taxes, because they own the major share of wealth and income. Further, they represent the peculiar interests, and it is difficult for them to rise above the class or petty interest to think nationally. Thus, they never go against the interests and preference.

Literacy

Literacy rate and increase tax collection go hand in hand as literacy makes documentation easy and bring more transactions in tax revenue collection. That is why, it is proven through studies that, backbone of an effective tax system is the documentation of the economy. Documentation comes from a literate tax base. In the present-day world literacy does not only being able to keep records on books but also includes knowledge of information technology and its usage. Taxes yield less revenue in less literate economies.

One study by Bahauddin Zikria University found that instead of a positive relation between literacy rate and tax revenue collection, it is reverse in case of Pakistan due to high tax evasion in Pakistan (Chaudhry & Munir, 2010)

Inefficiency of FBR

The total number of registered tax number in Pakistan is 1.44 million file tax returns out of which around 900,000 can be traced to their places of business or residence according to NADRA when it compared the list prepared by PRAL with its own record. It is yet another classical folly of FBR, symptomatic of its inefficiency over the years.

Instead of increasing the taxpayers the number is decreasing in last few years. The ten years of reforms in FBR, through WB funded project could only add a new service of IRS to the feather. The division of the board on functional lines, in which Tax returns, Recovery, and Audit are, separated lack coordination at senior level. Posting of other occupational group's officers at senior level and of other branch within the FBR is cause of heart burns of many.

When a person is chosen for Audit through computerized balloting, sometimes it turns out that he has not even filed the return, when enforcement officer is requested to get compliance it is the whim of the officer to do it or not, no track is kept of persons who have been issued notices over the years.

Workload of tax collectors has increased many folds in pursuit of more revenue generation, the pay incentive is at risk, leading to superficial investigations and audit.

It is much trumpeted (ARC), is *'pain in the neck'*, creating abrupt changes in the system. Pakistan Revenue Automation Private Limited (PRAL) is not error free and leads to discrepancies which the industrialists face every day. This is a continued fall out of unsuccessful reforms of FBR during Musharraf era. The low literacy rate in public has compromised these fancy window operations and another hassle to cost of doing businesses is added. The Taxation laws in Pakistan were modified changed in the last sixty or so years but the administrative machinery has not changed much.

Narrow Tax Base

In last decade, manufacturing sector contributes 20 percent to GDP while it pays approx. 2/3 to the taxes. Service sector contributes 56 percent to GDP while it pays approx. 1/3 percent to the taxes. Agricultural sector contributes 24 percent to GDP and pays less than 1 percent to the taxes. Tax generation increased by 25 per cent out of which four per cent was due to GDP growth, 12 to 14 due to inflation, four per cent due to administrative measures and three per cent due to revenue measures.

Table 3
Sector-Wise GDP and Tax Share

Sector	GDP Share	Share in Tax	Point Contribution to GDP
Agriculture	22.5	1.2	1.5
Manufacturing	17.9	62.2	2.2
Construction	2.1	2.9	0.4
Electricity & Gas Distribution	3.5	3.5	0.1

Sector	GDP Share	Share in Tax	Point Contribution to GDP
Transport, Storage & Communication	10.4	10.4	0.4
Wholesales & Retail Trade	18.6	2.8	2.0
Finance & Insurance	4.0	3.9	1.0
Public Administration & Defence	5.9	5.0	0.04
Social &Community Services	9.5	7.8	0.6
Others	5.6	4.4	0.1
Total	100.0	100.0	9.0

Note. Government of Pakistan (2008)

The way forward is quite clear, but the vested political interest based in urban trader classes and rural feudal lobbies are not ready to allow the elected representative to see beyond their immediate interest and look to national prosperity by contributing more to taxes. The FBR has time again identified three key reforms one of which is the tax on agriculture income tax and VAT on goods and services.

Tax Exemptions

Culture of the Statutory Regulatory Order has over time massively misused in the country's tax administration at the behest of the incumbent ruler; it was a delegation of legislative powers delegated by parliament through laws to the tax authorities. This practice in constitutional democracy like Pakistan cannot be condoned; the connivance of powerful lobbies with the tax authorities in disguise of economic revival to some sector is to be cleared in open debate.

SRO, by very definition is restricted to framing rules and procedures for implementing a tax law or laws. Or it can be used to remove hardships and ambiguities (without involving new levies, exemptions, concessions, waivers, etc.) that taxpayers may encounter during the enforcement of a tax law. In Pakistan, FBR through simple finance bill is given the power to give unlimited tax concessions, waivers and exemptions without parliamentary approval. That is why experts find the excessive misuse of delegated legislative powers favouring powerful interest groups at the cost of honest taxpayers to be at the root of our tax woes. The practice of handing out massive financial favours in the name of tax exemptions, concessions and waivers is not restricted to one particular government or the other.

It is estimated that last five years saw the siphoning away of Rs1trillion to different powerful lobbies through SROs. It was with a view to putting an end to the misuse of SROs that the IMF had made the government agree to withdraw tax exemptions to the tune of Rs350bn in three years in exchange for a bailout. In Pakistan, annually, monetary loss worth Rs500 billion is incurred on the national exchequer through Statutory Regulatory Orders (SROs) exempting the rich and the powerful from paying taxes. Last year alone 80 SROs were issued even though tax imposition or exemption is the sole prerogative of the legislature (Parliament).

Weak Audit and Enforcement

The Tax Gap is 79%- the difference between what taxpayers owe to government of Pakistan and actual amount paid in taxes by them. While another study by WB, estimated tax evasion in 2007-08, at 796 billion PKR, against potential of Rs 1.1 trillion; in September 2009.

Only a minute portion of total evaded or avoided tax could be collected after FBR Audit and legal proceeding, at an exorbitant cost; because of multifarious political and economic factors, including corruption[1].

The difference of Taxpayer's data which resulted in the audit of the missing 600,000 plus ghost taxpayers is another example of audit and enforcement. Functional delinking and lack of communication between revenue collectorates, audit and enforcement have put oil on fire.

Corruption

Perception about public servants plays a key role in compliance of laws by public more so is the case of tax collectors, who are generally believed to be corrupt, as admitted by former finance minister Shoukat Tarin.

Public perception in global corruption index about Pakistan is evident from thinking that it is better to donate Billions in donations rather than

[1] [In Pakistan, all returns are filed under Universal Self-Assessment Scheme. Taxpayers are selected and the audit proceedings are conducted. In Pakistan, the primary objective of the audit has always been to create deterrence, improve and encourage compliance to the tax laws on voluntarily basis i.e. promoting self-assessment system. Treating audit as source of revenue has been a secondary objective] *authors note.*

paying due taxes. which is considered a waste of hard-earned money. What is looted from public through taxes is spent on VVIP corruption-such is the negative perception about Government.

On the other hand, The Guinness World Records declares Pakistani charity, the Edhi Foundation, as one of the largest private ambulance service networks run on millions of rupees in donations.

Scandals of Export rebates, under invoiced imports, and over invoiced exports are abundant in FBR collectorates in big cities. Scandals of clearance of stolen cars, imported at private terminals at Karachi, and containers of Afghan transit trade unloaded in Pakistan with the connivance of Customs, are fresh in our memories.

Press sources talk of billions of rupees invested in Switzerland, Dubai, and London by ruling elite. Even the laws are made to favour corruption.

Undocumented Economy of Pakistan

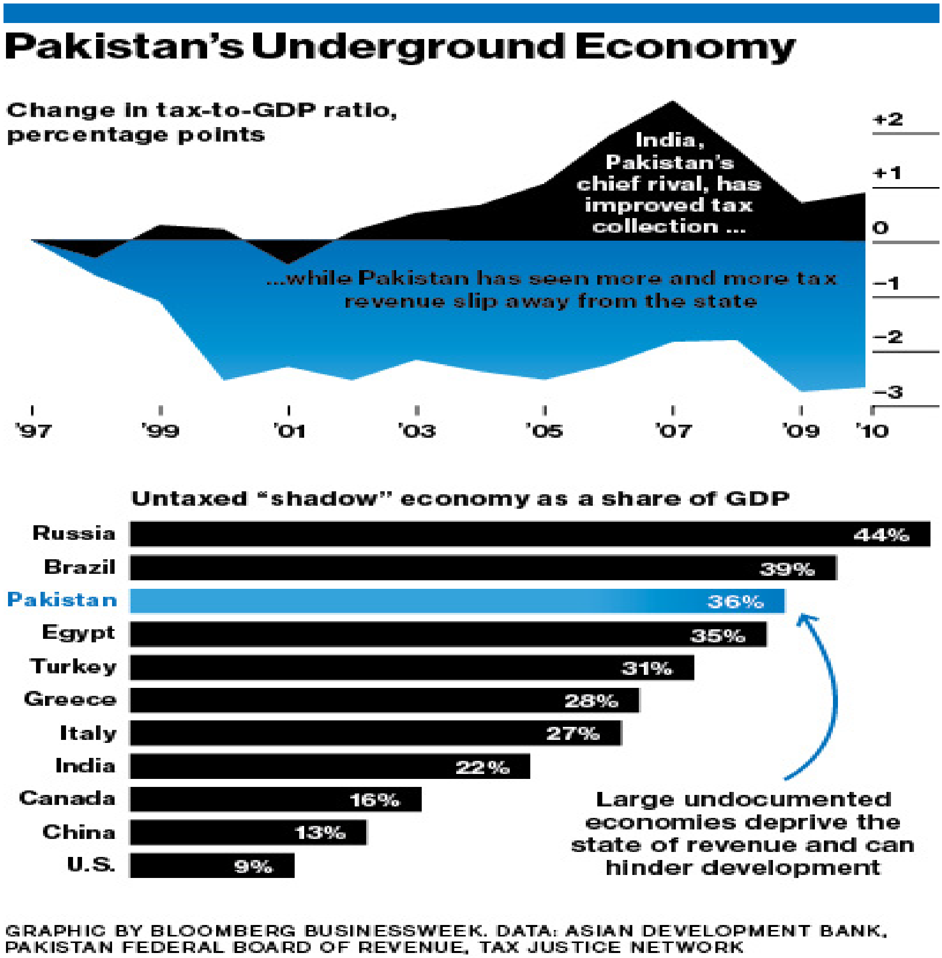
Appreciation about importance of documenting their internal and external economic activity is lacking in almost all businesses of the Pakistani economy, whether service, manufacturing or agriculture. Its estimates may vary, which is one of the leading research questions[2]. However, prima facie, scale of hidden or shadow economy is larger than the documented one. Only one estimate is given in table for realisation of the readers in below table.

According to "KQ" approach or discrepancy approach Kemal and Qasim (2012) true estimates of the GDP (total private consumption from the household survey for the total population and adjustment for trade Wrong-invoicing) when compared with the GDP estimates reported in the National Accounts (at current prices). The difference between the two is the size of the informal economy of Pakistan i.e. 91 percent of the formal economy in 2007-08.

This has not dropped by any means after a lapse of 6 years. As no effort to document the economy or enforce VAT is visible.

[2] Most popular among these approaches is monetary approach. Other approaches are Labour market approach, fiscal approach, etc. However, all these approaches have number of problems among which the first and foremost is that they do not give the actual estimates of the underground economy instead they give the trend estimates of it. (KQ Model)

Figure 1
Pakistan's Underground Economy



Lack of Commitment by Provinces

Pakistan's tax-to-GDP ratio was 8.6 percent in June, one of the world's lowest, according to in Islamabad. Only 25 percent of the economy is taxed if the undocumented sector is considered. Developing economies usually have a tax-to-GDP ratio of from 13 percent to 18 percent; Former Finance Minister Shaukat Tarin said in 2010 that Pakistan loses eight hundred billion rupees a year in tax evasion: The government collected 1.7 trillion rupees in tax last fiscal year. That is not enough to close the budget gap, which is 6.3 percent of GDP.

After 18th amendment, Federal Government can tax certain sales of goods and on the capital value of financial assets. It has been exercising these powers on behalf of Provinces in the name of increased efficiency of tax collecting administration. Now, Provinces have also been asked to take off this responsibility from Federal government and shoulder it themselves. These provincial taxes are on immovable property, estate and inheritance taxes, value-added tax (VAT) on services, and zakat and usher (religious taxes).

The resulting reassignment of taxes is as follows:

Table 4

Reassignment of Taxes to Various Orders of Government

Tax/fee/surcharge	Determination		Tax collection and admin.	Share in revenues (%)		
	Base	Rate		Federal	Provincial	Local
Federal	F	F	Federal	42.5	57.5	o

Even after this amendment, taxation authorities in Provinces have not developed technical skills, and human resource to collect the provincial taxes or expand its base specially in services. Their rent seeking attitude keeps them quite comfortable with federal dole outs under ECC and IPCC.

It is only Sindh & Punjab which were able to establish the provincial revenue authority, however, with lack of skilful people, and administration hitherto used to collect little, need not only cash transfers from the Federal Government but also professionals from FBR.

Governance

In economic opportunities and cost of doing business, Pakistan has fared better in all 111 indicators of GCI (Global Competitive Index) report released at Davos summit, even better than some of the BRICS countries. But on count of Governance Indices, it has failed miserably, even in comparison with Sub-Saharan Countries. Most important, of which are rule of law, Protection of life and property, State is has failed to invest in public assets like Infrastructure, health, & Education, for its citizen

Consequently, the socioeconomic conditions of Pakistani average citizen have created mistrust for State (*commonly the Government in power*). This is reflected by high level of wasteful, demonstrative expenditures and act of charities/philanthropy by the rich/expats, who are simultaneously avoiding taxes. Since they believe that Government will spend, every extra penny collected in wasteful ways.

The stability of state factors in heavily for any business environment therefore no FDI (foreign direct investment) is going to come its way soon. Pakistan besieged with a war like situation, is diverting attention of the rulers and the resources from the core business of socio-economic uplift of the people as enshrined in the Constitution. There are long term challenges like Job creation for the youth bulge which will probably not turn into a youth dividend, due to lack of investment in education, and absence of job opportunities. All this can be done by savings and domestic revenue generation through institutional autarky.

Analysis

Pakistan's poor performance in mobilizing domestic savings, especially for Economic development, in contrast to regional countries is evident in all the Competitiveness Indices of the World, with a gloomy future. Pakistan faces no challenge except domestic challenge of maladministration in public finances. Its culture of dependency on Charity and corruption have come out in relief due to Global recession and drying up of FDIs. Aid it used to receive as a geopolitical ally of USA in wars against communism and terrorism are things of the past. All the dollars are in offshore accounts of the corrupt elite or tied up in wasteful public sector expenses. In the view of one author, Pakistan embarked on investment expenditure through deficit financing since day one (Haq, 1961).

The average growth of 5% and above of GDP in last decades except last 7-8 years, have created rent seeking elite, who is not ready to give away the fruits through redistribution of income in the form of Taxes. It is estimated that all domestic investment is flown to services and consumer sector comprising of traders and real estate without check. All the infrastructure projects and social sector projects are being funded through foreign Loans or FDIs, which leave little scope for economic growth.

Causes of persistent poor tax collections in Pakistani History are ad hoc legal and administrative changes-Culture of SROs. Secondly, Low literacy rate means that public have insufficient knowledge of their obligation return filed are always in English. The leverage which it gives to Tax collectors is substantial in more than ninety percent of cases this discretion is used to mint money and result in tax leakages. Thirdly, changes in taxation policy are not synchronised with field tax collecting formations both in federal & provincial set up. Fourthly, even after spending huge donor grants on FBR organization turn around, it still living in the so-called [Jurassic era of unwieldy management style]. Fifth, the system of incentive and reward is so poor that most of the official are tempted to engage in illicit dealing with wealthy clients. Most of the employees of FBR are in lower ranks with low skill set- Inertia for change. Since citizens specially taxpayers have an inbuilt suspicion of everything government, they consider collectors as instrument of repression and treat them with animosity.

The principles of Taxation developed after process of hundreds of years still hold true, Pakistan has yet to follow these. Importance of these canons requires reiteration in a more detailed manner, with explanation of the concept.

Absence of rule of law, lack of equal opportunity; and feudal priorities of the State has weakened its institutions, for pushing the economic prosperity within reach of its entire citizen through income redistribution (basic function of the state)

Culture of exemptions and privileges exist in public sector of the country, promoting cronyism. Nobody is ready to touch the sacred cows in Pakistan.

Conclusion

The main fault lines in the low tax revenues in Pakistan are many and brewing in the minds of professionals and commoners equally. But the most important of them all is lack or deliberate absence of Political wills, the rule of few is plundering the economy for long periods, and they are used to creating the legal & institutional environment to help them. Examples of SROs in finance, industry and FBR are enough.

Voice and Accountability are required in the governance model of Pakistan; it is yet to fulfil the constitutional requirement of Local government elections, to reach out to every citizen of this country.

Cleaning and improvement of Domestic Revenue collection mechanism, especially at Federal level is necessary to achieve a one-point agenda, that is, no income is remains un-taxed.

Lack of legitimacy to govern in most of the political history of Pakistan, and non-inclusive style of policy making devoid of consultation has made every effort to increase tax based unacceptable to public at large and a tool of repression to milk them. Political maturity and continuity of policies despite regime changes is a must to create certainty and desirability in tax collection.

Finally, if implemented in the true spirit the 18th amendment shall transform Pakistan into a more decentralized state. This will limit the capacity of the centre for large scale tax reforms and will shift the focus to the provinces with their different political constellations and capacity to generate more revenue through taxation.

Elimination of duplication of jobs & tasks to cut down the sizes of the governments is essential to have space for two million people aspiring to enter job market every year. Consequences of their not getting it, can lead to social unrest and security threat to all without exception.

A progressive income tax and reduced regime of import duties system will provide in the long run incentive for large scale manufacturing sector& SMEs to grow and absorb the non-agrarian job seekers. This can reduce the revenue for government in the shape of withholding duties and custom duties, but it shall be yielding maximum social-economic advantages. It can reduce inequality by making the wealthy pay a progressively higher share of taxes.

Recommendations

In Pakistan, every few years, government is running to IMF to stabilize its Balance of Payment and current account deficit, due to inherent structural problems with our tax collection & enforcement system. Present political governments in Punjab & at Federal level has its base support in services sectors, and MQM has support of the urban traders Sindh. The last GST reforms were due to these parties in 2010 (Rana, 2010), as their demand to link it with good governance & Agricultural income tax were not met by the PPP government. Now a time has come when these hard choices must be made by the PML (N) Government again.

Ideally, States divide functions into three branches i.e., Regulation, Allocation, and Distribution. Taxation is the way of distributing the wealth to the poorer sections of the society. To perform this function, the four core competencies are required, effectiveness, efficiency, continuity, and accountability, in our scenario; Government need to improve them all for all areas of service delivery-more so for tax collection.

Governance Reforms

The public policy choices available to government are hard nut to crack, if it embarks upon them, its own constituency is hit. But if it is interested in improving it, the agenda is to bring government closer to the people as a logical next step of 18th amendment and complete the devolution. This will remove duplication and reduce the sizes of governments, and cost of governance. Secondly, the third tier of Local Governments be implemented through fair elections[3] to bring service delivery to the doorstep of common people by using local & municipal taxes, which are otherwise siphoned off in the absence of the local government. which is mandatory under constitution of Pakistan. The accountability mechanism under Auditor General Office will help to improve the efficiency of Provincial government but also government at the local level.

Third, information about what the government does should be readily available. Third, there is urgent need to improve the human and financial capacity of the more critical field formation for enforcement and audit of taxpayers by FBR.

Tax Reforms

Instead of increasing the rate of tax on already taxed sector and phase out the extensive regime of withholding tax (advance Income tax), on every consumable item of daily life secularly, Finance Ministry need to enact & enforce reformed GST. Simultaneously, it needs to identify new sources of direct taxation without poaching the provincial domain.

1. Immediate enactment of wealth tax and introduction of inheritance tax to control wasteful rent-seeking class is urgently required.
2. Sales Tax on services like traders, transporters be enforced through VAT mode.
3. Establishment of a Cross-Cutting task force is established with FBR, FIA, NADRA, State Bank, SECP, and Auditor General Office, for the Audit of suspected tax evading persons.

[3] 140-A. Local Government— (1) Each Province shall, by law, establish a local government system and devolve political, administrative, and fiscal responsibility and authority to the elected representatives of the local governments.

4. Tax and Customs reform initiatives encompassing development of special skills to identify cases of transfer pricing, techniques to catch tax evaders and use of IT to control tax avoidance.
5. Provinces only collect 8% of total taxes in Pakistan, which is very low. They must realize that they are now having immense powers as far as, tax on services & agriculture is concerned. They need to improve it further to make a worthwhile contribution.
6. Provincial tax on Agri based production & for efficient usage of limited resources of land and water.

Governance Reforms

1. Reduced public sector and the size of Federal & Provincial Government, by reducing non-essential cost of governance, at all tiers. Self-sustainable local governments as per Constitution of Pakistan, bring government closer to people and improve service delivery overall.
2. Greater autonomy of State Bank as was envisaged in the fiscal responsibility Act, 2005, which is implemented in 2021 through finance bill. However, State Bank is the institution which shapes the business mode of the country any change in its policy if secularly done can negate any reform of the federal government. Therefore, autonomy is needed for the government from the influence of the SBP's decisions and the implementation of a system of accountability is required to ensure that the SBP is helpful to government in the achievement of its agenda.

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