

TEST-04QNO1:Introduction:

The economy of Pakistan is struggling due to poor tax systems, reliance on external borrowing and inequitable economic environment. The major reasons responsible for this poor performance is the low-tax-GDP ratio, tax evasion culture and complex tax system of Pakistan. The economy of Pakistan is working on the constant supply of external borrowing in the form of bilateral and multilateral debts. There is a need to overhaul the whole tax system by simplifying the tax system, digitization of tax system, introducing export-oriented economy, and eliminating tax exemptions.

# ECONOMIC PROFILE OF PAKISTAN:

According to Pakistan Economic Survey 2023-2024, the economic profile of Pakistan shows that the revenues are collected from indirect taxes as compared to direct taxes.

## REVENUE COLLECTION

• DIRECT TAX = 48.7%

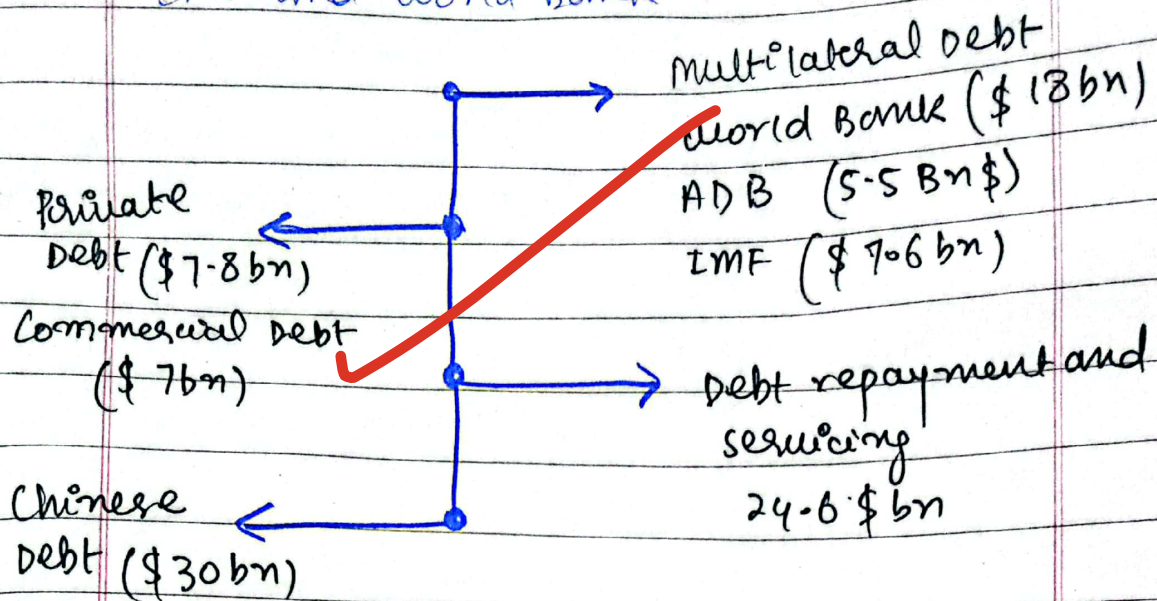
• Indirect Tax

Income Tax	17%
Sales Tax	15%
Custom Duty	5%
GST	18%

Source = PBS

Moreover, the economy of Pakistan is in shambles and it shows the heavy reliance on the external borrowings, debts from the

Bretton Wood institutions including IMF and World Bank.



### Other Indicators of Economic Profile:

GDP Growth Rate	2.4%
Per capita income	1680 \$
Inflation	26%
FDI	1.5%
Remittances	23.8%
Trade deficit	17.7%
Tax to G.V.P. ratio	10pc
Exports	25.7%
Imports	43.4%
Current Account deficit	0.2 \$bn
Budget deficit	6.5%

# Major Challenges to Tax System of Pakistan:

## (i) Tax Evasion:

The system of tax evasion is quite common in Pakistan. It is showed by the low tax-to-GDP ratio that is standing only at 10pc.

## (ii) Inefficient Tax Administration and Inadequate Tax Enforcement:

The tax administration of Pakistan is quite inefficient as a lot of complaints and corruption cases are registered against FBR. Moreover, the tax collection system and progress also showed this.

## (iii) Limited Tax Base:

The tax base of Pakistan is quite limited. The

major source of tax collection is from indirect taxes as compared to direct taxes.

### Direct Tax (RS in billions)

- Income tax 3682
- WWF, WPPF 39

### Indirect Tax

- Sales Tax 3607
- Custom duty 1324
- Federal Excise duty 600

### (iv) Complexity of Tax System:

The tax system of Pakistan is quite complex as it is based on federal and provincial, direct or indirect, special taxes and levies. It makes it quite difficult to understand this system.

# TAX SYSTEM REFORMS TO INCREASE REVENUE COLLECTION:

## (i) Implementing World Bank's Recommendations:

Pakistan needs to implement the recommendations of the World Bank that includes improving the federal and provincial coordination to collect tax.

## (ii) FBR Digitisation to Collect Increased Revenue:

Pakistan needs to digitize the FBR system to increase revenue collection. The digitization of FBR will increase revenue collection from tax 8% to around 18% of the GDP. The current tax potential is 15%.

### (iii) Increase in Excise Duty and Closing Exemptions:

Pakistan needs to increase the excise duty to collect more tax and close the exemptions given on IPPs and other major projects to increase the revenue collection. The concession is given to renewable energy resources, they are exempt from custom duties and sales tax.

Seeds, fertilizers, pesticides	Exempted from sales tax
Machinery	concession
Textiles, IT sector	Exempt from Income tax
IPPs SEZs SMEs	Exempt custom duty & sales taxes

## (iv) Single Tax System to reduce Compliance Cost:

Pakistan must introduce single tax system to reduce compliance cost. As the system is comprised over different levels that make it quite difficult for people to understand and industry need to hire an consultant to understand the system of tax in Pakistan.

## REDUCE RELIANCE ON EXTERNAL BORROWINGS:

The debt profile of Pakistan shows that it is heavily relies on the external debts and borrowings and Pakistan need to restructure its debts.

### (i) Debt Restructure and Management:

Pakistan need to restructure its debt by



discussing it with foreign lenders including IMF and World Bank.

The repayment term must be extended by discussion. Moreover, Pakistan needs to explore some alternative options including green bonds, bilateral loans, and reduce interest rates and sovereign wealth funds.

## Fostering Equitable Economic Environment:

The equitable economic environment can be fostered by making economy export base and attracting FDI in IT and other sectors.

### (i) Attracting Foreign Direct Investment:

Pakistan needs to attract FDI in the country to stabilize the economy. In this regard, the economy of China is

an example. China offered tax exemption in its SFZ's and now the FDI inflow in China is standing at \$ 100 bn.

### (ii) Exploiting IT Potential and Job Creation:

Pakistan needs to explore its IT sector for equitable economic environment. The freelancing sector generate \$ 400 million. The IT sector of India is an example that is standing at \$ 250 bn currently.

### (iii) Export-Based Economy:

Pakistan needs to explore the option of introducing export based economy in Pakistan. The process of exports is quite complex

because of unavailability of raw material to add value. Pakistan need to explore the indigenous resources to promote equitable economic environment.

## Conclusion:

In conclusion, the major reforms in the tax system are needed to promote equitable economic environment in Pakistan and to cut reliance on external borrowings. By taking action on the digitization front, the revenue collection of tax can be increased.

Pakistan need to overcome the complexity of tax system so that an educated and illiterate both person can understand the system and pay taxes for the progress and prosperity of Pakistan.