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ESSAY

THE CHALLENGE OF TAX EVASION AND THE INFORMAL ECONOMY OF PAKISTAN

OUTLINES

1) INTRODUCTION

Tax evasion is a key problem in Pakistan's economic sector as most of Pakistan's economy is informal.

2) Understanding the Concepts of Tax Evasion and Informal Economy.

How Tax is Evaded in Pakistan.

3.1) By undervaluing the property, to avoid the payment of actual tax rate on the property.
Case in Point: Arbitrary land prices lead to tax evasion, says Miftah Ismail

3.2) By influencing government for tax exemptions based patron clien relations.
Case in Point: Shabbar Zaidi argues that agriculture sector pay no direct tax because political patronage

3.3) By reporting less sale to the FBR.
Case in point: Services sector.

3.4) By fabricating the FBR issued NTN code.

3.5) By developing industries in tax free zones
Case in Point: "Shair Ghee Mills" in Malakand

3.6) By regestering business under the umberrilla of a welfare trust.

3.7) Transaction of money through "Hawala Hundi"
Case in Point: Labour in Gulf countries send money through hawal hundi not banking sector.

3.8) By gifting property instead of formal inheritance.

Case in Point:- Qaiser Bengali argues in his book that, as gifted property is exempted from tax, it is the most common method in land lords.

4) TAX EVASION IS THE RESULT OF INFORMAL ECONOMY

5) WAYS OF HALTING TAX EVASION

5.1) Digitalization of the economic sector.

5.2) Spreading awareness regarding the importance of tax for a country.

6) CONCLUSION

In modern and developed economies, tax collection has been of utmost significance. Taxation enables government to develope sustainable economies. This eventually improves the individual standards. However, the evasion of tax by public has severe implications for state and general masses of the state in informal economies like Pakistan, tax collection becomes one of the most difficult problem. As in informal economies, governments mostly remain in dark about the actual economic activities in the countary. Pakistan has also been grappling with the challenge of tax evasion since its birth. corporate sectors avoid tax by not showing the actual value real-estate assets. Salaries and deal transactions are mostly made through cash. Businesses are registered under the umbrailla of welfare trusts. The inflow and outflow of cash in form hawal hundi, People also exploit tax-free zones by shifting industries to tax-free zones. This tax evasion results in weakening the formal sector and strengthening informal sector. The government ought to address this problem by digitalization and spreading awareness regarding tax importance for any countary.

Real-estate sector is one of the key sectors of Pakistan's economic landscape. This sector runs from buying land to constructing societies and multi-stories buildings. This sector brings huge profits to the owners, but not the countary. They often undervalue the projects in documents. This is done to avoide paying the actual tax ratio to the state. In this way, the state receive less share and the actual value is more. This results in the bulgeoning of informal sector. This sector does not add directly to the national enchecquer. It mostly benefit the private parties involved in the deal. Thus a system evolves where more money circulates in the market, but the state remains in dark about it.

Agriculture sector is the backbone of Pakistan's economy. It employes about 38% of the total labour of the country. Despite its big share in the economy of Pakistan, this sector pays no direct tax to the state. **Shabbar Zaidi**, former Chairman of FBR, claims that this sector cause the most loss to national economies. The landlords of agricolture sector use their political strength to get tax exemption from the government. This sector enjoys complete tax-exemption from the countary. It is because of the patron-client relationship. The government gives them tax exemption, and in return the help them in election funding and voting.

The economic sector in Pakistan is divided between tax-free zone and tax zone. These tax free-zones are either declared by government to attract investment or the uplift any backward area. The former fedrally administered tribal areas (FATA) and provencially administered tribal areas (PATA) are mostly tax-free areas. The aim of the government was to uplift these areas. People will invest in these areas and so a healthy economic environment will evolve. However, these industaries have to operate within the defined area not outside it. Business tycoons exploit this opportunity. They develope industaries in tax-free zones. In this way, they do not have to pay tax on their production to government. They not only evade tax, but also smuggle their products to other regions of the country. This gives them double profits. For example, "Shair Ghee Mills" is located in tax-free zone of Malakand, but they sell their products througout the province. This eventually impact formal economy as the industaries in tax-zones find it difficult to compete them in open-markeet. Thus, they also explore ways of evading tax.