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POLITICAL ECONOMY OF TAX REFORMS: THE PAKISTAN EXPERIENCE

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POLITICAL ECONOMY OF TAX REFORMS:
THE PAKISTAN EXPERIENCE

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Pakistan's tax system is characterized by a number of structural problems. First, the overall level of fiscal effort is low and the tax-to-GDP ratio has remained, more or less, stagnant at between 12 to 13 percent. This is one major explanation why budget deficits have been high, generally in excess of six percent of the GDP. Second, there is over dependence on indirect taxes, which until recently accounted for a share in revenues of over 80 percent. This has increased the regressivity of the tax system and imposed a higher excess burden of taxation. Third, within indirect taxes there is domination of taxes on international trade, which has promoted inefficiency, distorted the allocation of resources and encouraged illicit trade. Fourth, the effective tax bases of most taxes is narrow due to wide ranging exemptions and concessions and rampant tax evasion. For example, there is less than one income tax assessee per 100 persons and less than 60 percent of imports actually pay duty. Consequently, tax rates have had to pitched at high levels which has created a vicious circle of more tax base erosion and higher tax rates. Fifth, the tax administration is characterized by primitive and out moded procedures, complex laws and considerable arbitrariness and discretion. The common perception is one of high levels of corruption and inefficiency.

Despite these problems which have been manifest for a long time Pakistan has been slow to embark on the path of tax reforms. In the 80s, higher fiscal effort was substituted for by large bank and non-bank borrowings. However, the extremely rapid growth in debt servicing clearly indicated that the task of resource mobilization from taxes could not be postponed indefinitely. The commencement of the decade of the 90s coincided with the induction of a newly elected (IJI) government, strongly committed to the process of privatization and deregulation and a return to the market economy. Also, the Gulf War led to one the largest budget deficits (almost 9 percent of GDP) in the history of Pakistan and a major surge in the rate of inflation. Given its commitment to change and the adverse turn of events the new government was compelled to embark on the process of tax reforms. Within three months of the formation of the government a high powered Tax Reforms Committee (TRC) was constituted followed by the establishment in 1991 of a full-fledged Resource Mobilization and Tax Reforms Commission (RMTRC). Therefore, the year, 1990-91, can be said to mark the beginning of the process of major reforms in the taxation system of Pakistan, which is still going on. In 1993, Pakistan signed the agreement for Structural Adjustment Facility (SAF) with the IMF, which envisages further reforms including a major scaling down of tariffs and broad-basing of sales and income taxes.

The objective of this paper is to analyze the experience of Pakistan with tax reforms during the decade of the 90s. The emphasis is on issues of political economy and governance capacity so as to highlight the constraints confronted and factors which have influenced the success or failure of different components of the overall reform package. We discuss four major reform episodes as follows:

- introduction of presumptive and withholding taxes in income tax
- removal of exemptions and rate reductions in income tax
- broad-basing of the general sales tax
- tariff reforms

The paper is organized as follows: Section 2 describes some of the general methodological tools for analysis of political economy of tax reform and for assessing governance capacity. Section 3 deals with the experience of introduction of presumptive and withholding taxes, Section 4 with removal of exemptions and rate reductions in income tax, section 5 with broad-basing of the sales tax and Section 6 with the on-going tariff reforms. Finally, in Section 7 we present the key conclusions.

2. POLITICAL ECONOMY OF REFORMS AND GOVERNANCE CAPACITY

Developments in the field of political economy have begun to provide a better understanding of how political choice is interwoven with economic decisions. Of particular relevance in this regard is the theory of social choice which seeks to describe the process whereby society collectively decides on tax policy and on priorities among different public expenditures, especially in the absence of markets to signal consumer preferences (through relative prices), as in the case of public goods. The theory suggests that the process by which decisions are made will affect the ultimate choice and that different political structures, even voting rules, could lead to radically different outcomes which may clash with some objective notion of rationality, like rules for optimal taxation developed by neo-classical economics.

Political economy emphasizes the role of special interest groups and what they can gain at the expense of the general population. It demonstrates that through lobbying efforts and formation of effective coalitions there can be incentives to pursue actions in the interest of the few which conflict with general considerations of economic efficiency and equity. This is especially likely to be the case where the gainers from a particular political action or policy change are few while the losers are many and dispersed, for whom the informational problems and transactions costs of getting together to block the move are too high.

The phenomenon of rent seeking is frequently referred to in the political economy literature whereby a person or a group of persons may seek to expropriate some surplus, without contributing to its creation, by extracting some special dispensation or concession through a discriminatory application of a rule or some discretionary change in the rule itself. This phenomenon is important not only for its income distributive implications but also because it may distort workings of the organs of state and create deadweight losses through the use of resources in the process of rent seeking. One of the basic recommendations of political economy analysis is the design and establishment of rules and policies which reduce opportunities for special interest and rent-seeking activities. Often this has entailed development of transparent arrangements with clear lines of accountability.

The issue of governance capacity is closely related to the ability to successfully undertake reform. In the context of this paper, governance is understood as the capacity of the state to organize the tax system according to some basic and universal principles, and to enforce compliance with rules. Governance also implies a minimum degree of autonomy from pressure of special interests in the formulation of policy. Vital determinants of governance capacity are the ability of the political leadership to articulate the need for reform within the context of an integrated economic and social vision, cohesiveness and co-ordination among government agencies, success in putting together support coalitions and mechanisms for compensation of losers (if necessary) and presence of capable bureaucratic cadres committed to the proposed reforms.

We turn now to an analysis of Pakistan's experience in each major area of tax reform.

3. INTRODUCTION OF WITHHOLDING AND PRESUMPTIVE TAXES

During the decade of the 90s, the focus of tax reforms in Pakistan has been on the broad-basing of direct taxes through extension of withholding and presumptive taxes with the objective of reducing the quantum of tax evasion, especially in the declaration of capital income, generation of revenues from hard-to-tax sectors, and minimising compliance costs of tax payers.

3.1 Progress in Implementation

Withholding taxes have traditionally represented, more or less, ad hoc deductions at source at the point of accrual of income with subsequent adjustment following assessment by the tax department of the statement filed of income from all sources. In this sense they have the obvious merit of preventing the leakage of income from the tax net. However, responsibility to collect withholding taxes is essentially decentralized, and there exists the possibility of collusion between the withholding tax authority and the tax payer. Therefore, there is tendency to restrict the role of the tax collector to government agencies, public corporations and large companies. Another problem is that if withholding tax rates are set at too high a level then they can create the problem of refunds by the tax department. These refunds are prone to misuse and corruption. Initially, in the reforms process in Pakistan there was a tendency to convert withholding taxes into presumptive taxes representing fixed and final settlement of tax liabilities. The primary objectives were increased simplicity and reduction in the compliance cost of taxpayers.

Withholding and fixed taxes have primarily been used to extend the coverage of income tax to various forms of capital/unearned income. Traditionally, Section 50 of the Income Tax Ordinance (ITO) which covers such taxes was restricted largely to salary income with deduction at source on a monthly basis by employers. In the 80s this was extended to cover other forms of income like interest income of financial institutions from government securities, the income of non-residents, the income of contractors, suppliers and importers. From 1991 onwards there have been significant developments in the withholding/fixed tax regime. In the Finance Bill of 1991 the coverage of existing provisions was expanded, a fixed tax at the flat rate of 10 percent was levied on interest income from financial institutions and on dividends and at 5 percent on rental income above Rs 100,000. This was followed in the Finance Bill of 1992 by the extension of a fixed tax (at 0.5 percent to 1 percent of value) on exporters to be collected by the State Bank of Pakistan at the time of realization of foreign exchange proceeds.

Use of withholding/fixed taxes has not remained restricted only to deductions at source in Pakistan. Increasingly, these taxes have been levied at points where it is possible to get a proxy of the income of a taxpayer. This innovation in the tax system is largely attributed to the desire to detect tax evasion. For the first time a withholding tax was levied on commercial and industrial consumers of electricity in the Finance Bill of 1992. The objective was to bring a large number of small to medium-sized taxpayers into the income tax net on the assumption that there is a relationship between electricity consumption and income. The magnitude of the withholding tax was linked progressively to the value of the electricity bill, with collection responsibility resting with the power utilities. A similar concept has been applied to justify the imposition of withholding tax in 1992 at the time of granting/updating registration of private motor vehicles, in 1993 at the rate of 5 percent at the time of issue of foreign exchange for travel abroad (withdrawn in 1994) and at the rate of 2 percent of estimated cost at the stages of approval of building plans and issue of completion certificate to developers.

Altogether, there has been considerable success in reducing evasion by extending the network of withholding and presumptive taxes. Total revenues under Section 50 of the ITO have grown very rapidly during the last two years with a cumulative increase of almost 150 percent in 1991-92 and 1992-93 (see

Table 1). This is the major factor responsible for the unprecedented growth in income tax revenue in recent years. Simultaneously, the component of refunds has been largely eliminated from the tax system (see Table 2). These were equivalent to over 11 percent of gross revenues in 1990-91 but were down to about 4 percent only by 1992-93. As a result, tax deductions at source currently account for over 70 percent of total income tax revenue.

The extension of presumptive/withholding taxes has not only contributed to a rapid growth in revenues but it has also probably implied greater equity in the tax system. The share of direct taxes has increased dramatically and there has been more effective taxation of capital income like interest, dividends, rent, etc., which accrue largely to upper income households. In addition, the change in tax regime has meant greater elasticity of income tax revenues which are now linked to fast growing income streams like interest income from bank deposits, interest on government securities (due to rapid growth in government borrowing), income from the rendering of professional services, etc.

3.2 Gainers and Losers

Relatively honest taxpayers who declared a higher proportion of their income in the old system are likely to be gainers while tax evaders lose. All tax payers gain due to reduction in compliance costs. The government generally is also a gainer unless the withholding/presumptive tax rates are pitched at very low levels. The clear loser from the reform is the income tax officer who no longer has the power to extract bribes. It is interesting to note that agents of the state belonging to the tax collection machinery have a strong vested interest in blocking this reform and are, therefore, unlikely to adopt a neutral or promotional stance.

3.3 Determinants of Success

Role of Gainers

In its vision of change, the previous elected government, which was sympathetic to business interests, forcefully articulated the view that the income tax system had failed on the one hand to generate enough revenue due to the presence of rampant evasion and corruption and on the other hand it had become a hindrance to the smooth conduct of private sector economic activities because of the high level of taxpayer compliance costs and the frustration resulting from harassment by tax officials and the arbitrary nature of assessments which led to lengthy and time consuming appeals processes. In his public statements, the Prime Minister went to the extent to saying that evaded income was as much as four to five times the declared income and that while this was due to fundamental problems of taxpayer compliance and morality it was also the consequence of a thoroughly inefficient and corrupt tax machinery. Newspapers frequently carried information about retrenchments and transfers in the income tax department.

The Resource Mobilization and Tax Reforms Commission which was charged with the responsibility of proposing and implementing reforms in the tax system (based on the earlier report by the TRC) was adequately represented by large business interests along with political representatives, professionals and tax experts. In its initial meetings with Chambers of Commerce and Industry and various Trade Associations there was unanimous affirmation of the need to simplify the income tax system by introduction of presumptive/withholding taxes so as to reduce discretion of tax officials, decrease harassment and compliance costs. It was also commonly asserted that simplification of the tax system could actually generate more tax revenues through curbing of tax evasion. The common argument put forward by businessmen was that rather than pay bribes which went into the pockets of corrupt tax officials they would prefer that these payments were converted into revenues for the government.

Lobbying activities to bring about the desired changes in the tax system were intensive in character. The Nawaz Sharif government made a significant departure from past practice by substantially "opening" up the budget-making process to outside interests. Traditionally, this task had been performed by the bureaucracy in a climate of, more or less, complete secrecy. A high powered Budget Committee was constituted (chaired by the Prime Minister) with representation by leaders of trade and industry. These representatives forcefully argued in favor of mechanisms for reducing tax evasion because in its presence they were compelled to pay higher tax rates for achievement of target level of revenues. They also presented proposals for simplification of the tax through introduction of presumptive/withholding taxes on different streams of income and in different sectors of the economy.

Role of Agents of State

This area of reform is unique in the sense that one component of the state, the tax collecting machinery, actually had a vested interest in the non-implementation of this reform. Presumptive/withholding taxes reduce the role of the income tax department and lead to a decentralization of the process of tax collection. At the individual level, tax officials find their income level drastically reduced because of fewer bribes.

However, the CBR as a whole and the income tax department in particular had been subjected to a great deal of criticism already because of the historically poor performance in tax collection, as reflected in the low and stagnant tax-to-GDP ratio. Therefore, revenue officials found themselves in a position where they could not forcefully argue against the violation of the traditional norms of income taxation based on filing of returns of global income by tax payers. The aggressive attitude of the Prime Minister and the Finance Minister and the danger of punitive action in the form of large scale removal and sacking of tax officials constituted a credible threat of their position. The tax bureaucracy decided in the face of criticism that the best policy was to go along with the reforms at least temporarily and see how presumptive/withholding taxes performed. Also, the tax department was effectively bypassed by the handing over the responsibility of development and implementation (via provisions in the Finance Bills) of proposals to the RMTRC and with actual responsibilities of collection shifting to large public sector and corporate entities.

Another factor contributing to success was that other organs of sate, primarily senior officials of the ministries of finance, industry and commerce fully supported the move. Not only was there a desire to increase the flow of revenues into the exchequer through curbing of evasion but there was also a general sympathy with the view that the existing tax system had failed due to complexity of laws and inefficiency and misconduct on the part of tax officials. In more cynical terms it seems that other elements of the bureaucracy felt that there was a disportionate allocation of lucrative positions to the tax department and this imbalance needed to be removed.

Role of Losers

Losers from the reform belong to two distinct groups, income tax officials and tax evaders (who either did not file any return or underdeclared a substantial proportion of their income and subsequently escaped assessment). As indicated above, the former could not lobby aggressively against the reform because of the prevailing climate of hostility to their role and the prospect that if revenues did not improve quickly then there could be large-scale retrenchment of the income tax department. Within this group, the few honest officers were inclined to support this reform as it considerably simplified their jobs and reduced their assessment load.

Chronic tax evaders did not fall into a homogenous category. By definition, it was difficult for them to reveal their identity lest they become targets for any future revenue drive. Also, there was a realization that the government meant business and the alternative to the reform was potentially worse as it meant stronger investigation and enforcement activity by the department. As such the pragmatic approach was to pay somewhat more in the form of presumptive or withholding taxes while preserving anonymity and not coming into contact with tax officials.

Of course, not all opposition to the reform was muted. Income tax practitioners, lawyers and accountants found that their practices would be severely eroded by the transition to a simpler tax system. There were also some tax purists who felt that the introduction of presumptive and withholding taxes was a vulgarization of the system. A campaign was launched in the newspapers and voiced occasionally in the higher echelons of government that the shift from global to schedular income taxation (for example, of interest income) would reduce the progressivity of the tax system, that levy of fixed taxes on crude proxies to income like turnover would convert a direct tax to an indirect tax leading to shifting of the tax burden, that the problem of inequity would be exacerbated by the fact that the presumptive/withholding tax regime would not be able to distinguish between persons with income below exemption limit and those with taxable income. Consequently, the system would end up taxing poor households, widows, orphans, etc. However, all these arguments paled in face of a government which appeared to be determined to simplify the tax system, reduce arbitrariness and harassment by tax officials, broaden the base of income tax by checking evasion and generate more tax revenues.

The extraordinary success achieved in implementation leads to the identification of the key elements of governance capacity which contribute to successful reform. In the context of this reform episode these are as follows:

i) a government which was able to adequately articulate the need for the particular reforms as part of its overall vision of social and economic change and to successfully project to the general population the losers from the reform (tax evaders and income tax officials) as the `devils' of the system who had exploited the laws and led to a breakdown of the tax machinery, implying a slackening of the overall fiscal effort;

ii) an approach to reform which was demonstrated to be superior to other approaches in terms of costs imposed on society at large and the time frame for achieving gains. Mechanisms for tackling evasion were shown to be better than a policy of raising tax rates (to generate more resources from existing tax payers) or stronger enforcement activity (leading to more harassment and corruption);

iii) ability to build a strong base of diversified support to the reform from business, employee and other interest groups;

iv) strong leadership from the chief executive, the Prime Minister, and the Finance Minister who personally campaigned for the reform and presented proposals for its implementation;

v) adoption of an approach which essentially `bypassed' one major loser, the income tax department, by decentralizing the process of tax collection;

vi) presence of credible threats to losers that if the reform was not implemented they would actually be even worse off. For the income tax department, this meant large-scale retrenchment and for tax evaders the prospect of stronger enforcement activity and detailed investigations. In a perverse way, therefore, potential losers stood to gain from the reform, which pre-empted even stronger action;

vii) opening of the budget-making process, leading to greater transparency and access to new, innovative approaches;

viii) lack of homogeneity and difficulty in co-ordination within one major group of losers, the tax evaders. Transactions costs of building an organization and a common front were too high. Lobbying against reform had to be done by surrogates like tax practitioners, lawyers, accountants, etc., whose level of commitment was not too high;

ix) the reform package gained momentum over time as it was able to demonstrate very quickly a considerable degree of success, as measured by the phenomenal growth in revenues.

Altogether, this reform experience was unique in the Pakistan setting as most positive aspects of governance capacity came together in ensuring its success.

4. REMOVAL OF EXEMPTIONS AND RATE REDUCTIONS IN INCOME TAX

One of the major elements of the strategy of tax reforms is to broaden the base of taxes (especially direct taxes) and simultaneously bring down tax rates. This will not only protect (and perhaps even increase) revenues by reducing the incentive for evasion but will also lead to a more neutral and efficient tax structure with less distortionary impacts on the economy. We study in this section the success Pakistan has had in achieving this component of the tax reforms. Broadening the base, through withdrawal of major exemptions, is an excellent case study in highlighting the political economy of tax reforms.

4.1 Progress in Implementation

The income tax system of Pakistan is characterized by a large number of exemptions, tax credits, rebates, concessions, etc., which have led to substantial revenue losses. The estimated magnitude of tax expenditures (revenue cost of the differential tax treatment] is colossal and in excess of revenues actually collected, as shown in Table 3. Major tax expenditures include the statutory exemption of major public corporations [like Water and Power Development Authority (WAPDA) and Pakistan Telecommunications Corporation (PTC)], interest income from government savings instruments, agricultural income and wealth, capital gains on financial assets, tax holidays, salary perquisites in cash and in kind, export income, accelerated depreciation allowances, owner-occupied properties, etc. The total revenues foregone due to these exemptions/concessions is over 2 percent of the GDP. This is one major explanation why the direct tax-to-GDP ratio is low at less than 3 percent of the GDP as compared to over 7 percent for developing countries at a comparable stage of development as Pakistan [see Burgess and Stern (1989)].

Given these large-scale concessions, tax rates have had to be pitched at relatively high levels. During most of the decade of the 80s, the maximum marginal tax rate for personal income tax was as high as 60 percent. The corporate tax rate for public companies was 55 percent. These high tax rates had placed a premium on tax evasion.

The sequencing of tax reforms pursued in Pakistan appears to have been an upfront announcement of reduction in tax rates without any link necessarily with a simultaneous removal of exemptions. In this sense, the approach of bargaining with particular social groups has not been adopted. This had made it politically more difficult to subsequently withdraw concessions.

In the Finance Bill of 1991 the government announced an immediate slashing down of personal income tax rates, with the maximum marginal tax rate falling to 35 percent. For the corporate sector, it was proposed to bring down rates substantially over a five year period starting from fiscal year, 1992-93. The decline envisaged by 1997-98 is from 66 percent to 55 percent in the case of banking companies, from 44 percent to 30 percent for public companies (other than banking companies) and 55 percent to 40 percent for other companies. In addition, the super tax or surcharge on companies was withdrawn. This measure is likely to have contributed greatly to reduction in uncertainty about future tax rates and facilitated better investment planning.

However, up to the budget for the current fiscal year, no major success appears to have been achieved in the rationalization of the major exemptions and concessions in direct taxes mentioned above[1]. The last caretaker government (from July to October 1993) had made an attempt at introducing both income and

[1] Some minor exemption embodied in the second schedule of the Income Tax Ordinance have, of course, been withdrawn. This includes tax credit on balancing, modernization and replacement of machinery, income of chambers of commerce and industry and stock exchanges, moderabas (after the first three years), some welfare trusts and financial institutions.

wealth taxation in the agricultural sector by promulgation of ordinances. These were proposed as schedular, presumptive (linked to produce index units of land) taxes in order to simplify the process of administration. Tax rates were deliberately kept low so at to minimize resistance. However, the elected government has allowed the agricultural income tax ordinance to lapse (except in the NWFP) while the wealth tax proposal was accepted and embodied into law, but in the 1994 Finance Bill the special exemption to wealth in the form of agricultural land has been increased ten times, from Rs 100,000 to Rs 1,000,000. This implies that although agricultural land is part of the wealth tax net very few landowners will actually end up paying this tax.

4.2 Gainers and Losers

Determination of gainers and losers from reform involving broad-basing of income tax coupled with a reduction of tax rates depends upon the percentage increase in taxable income and the percentage decrease in the average tax rate. A tax payer is worse (better off) if the former is greater (less) than the latter. Therefore, tax payers can be separated into losers and gainers from a reform package, involving broad-basing of direct taxes and reduction of tax rates, depending primarily on the extent to which their income was originally in taxable forms.

However, this essentially assumes that there is simultaneously a reduction in tax rates and withdrawal of exemptions. If, however, a two-step procedure is followed, as happened in Pakistan, then the results could be very different. If in the first step only tax rates are lowered, then all taxpayers benefit and there is unambiguous support for this reform. If, subsequently, at attempt is made to withdraw exemptions then all tax payers potentially lose (in relation to their position after the first step) and there is every likelihood that this phase of the reform will be strongly resisted. Therefore, the optimal strategy which maximizes changes of success is a simultaneous movement on both fronts of broad-basing taxes and reducing tax rates.

4.3 Determinants of Success

<u>Role of Gainers</u>

The real gainers from reform are the general population of relatively poor households who can expect that a rise in direct tax collections will lead to some alleviation of the burden of indirect taxes which mostly fall on them or that the overall increase in tax revenues will lead to a some reduction in the budget deficit and less resort to inflationary financing which imposes a disguised tax on them.

However, given the complexity of the income tax code and the generally low level of literacy in Pakistan, there are serious information problems with regard to gainers. Very few people have knowledge of the wide array of exemptions and concessions embodied in the direct tax system. It is only recently that research undertaken by academic institutions like the AERC has demonstrated the sizeable tax breaks that exist, especially for the rich, in Pakistan. But an awareness campaign remains to be launched. The government has been reluctant to disseminate this information lest it sharpen the class struggle and lead to a further decline in voluntary taxpayer compliance due to increased perception of inequity in the tax system.

Knowledge of the favored treatment granted to agricultural income is, however, widespread. This has been a flash point of debate over the last forty seven years, since creation of Pakistan. It has now become a symbol of the conflict between the emerging urban middle class and the traditional rural feudal elite. By now, the degree of polarization on this issue is complete.

Other gainers are social groups who traditionally have received most of their income in taxable forms. This includes salaried tax payers, who have benefited significantly from the large decline in personal income tax rates. However, this group is apprehensive that any change in the tax treatment of salary perquisites in cash or in kind will once again raise tax liabilities. The corporate sector has also benefited, although in the short run the quantum of gains is not so sizeable. Resistance, however, is likely to efforts to broadening the tax base by withdrawal of tax holidays, accelerated depreciation allowances, exemption on bonus shares, etc.

Role of Agents of State

The attitude of agents of state to the reforms has been a mixed one. On the one hand there is the commitment to a more neutral tax regime which is less distortionary in character but on the other hand there is the concern that if specially targeted concessions are withdrawn then there could be adverse economic consequences and the government could be accused of being anti-agriculture, anti-exports, anti-savings, anti-investment or anti-backward areas and so on. Consequently, the same degree of commitment has not been visible on the part of government to this part of the tax reforms as has been demonstrated, for example, in the extension of presumptive and withholding taxes.

For example, in the context of withdrawal of exemption of agricultural income, the previous elected government was particularly vulnerable to the criticism that it was anti-agriculture, as it had strong support from business and trade interests in the cities. The government had to consider the fact that the feudal class still had considerable political clout and would play a vital role in future elections. It is ironic that even though the Nawaz Sharif government did not promulgate the agricultural income wealth tax, it still lost in the rural areas of Pakistan in the 1993 elections.

Tactically, it appears that the government did not play its cards well in the reforms process. The opportunity that existed for engaging in bargaining with different social groups for a trade-off between withdrawal of exemptions and reduction in tax rates was not availed. There was too much of a hurry to appease the vote bank of business interests by announcing a reduction in corporate and personal income tax rates. Also, the government was convinced that purely from the viewpoint of increasing private investment in the economy it was necessary to reduce corporate tax rates. This was perhaps motivated by a more dynamic understanding of the relationship between growth of tax bases and tax rates (or supply-side economics).

Role of Losers

Behind each major tax exemption or concession there is a strong, entrenched vested interest group in Pakistan. Each group has organized itself as an effective lobbying entity, which has not only blatantly demonstrated its power in political terms but also has in more subtle terms played the game of patronage seeking through party donations, supporting influential politicians, etc., and developed credible arguments why retention of these exemptions and fiscal incentives is actually in the greater national interest.

Perhaps the best example of this is the agricultural lobby. It is extremely well organized and enjoys enormous political power. Over 80 percent of the elected members of the parliament either represent the feudal class or are sympathetic to the interests of this group. It is not surprising, therefore, that any legislation to change the status quo is effectively blocked. A number of arguments have also been developed to justify the tax exemption of agricultural income ranging from the fact that the sector is already `overtaxed' through the pricing mechanism [domestic prices below world prices], that food production is vital for national security and that the high costs of collection of the tax on agricultural income will not be justified because of the likely low revenue yield.

Tax holidays have been aggressively supported by industrial interests who have formed an alliance with the provincial governments of backward areas. They have been successful in playing up the sensitive issue of large and widening regional disparities in the country. The Ministry of Finance (a key agent of the state itself) has justified the exemption of interest income on government savings instruments on the grounds that this actually improves the income distribution because bulk of the participation in such savings schemes is by lower and middle income households and that this incentive reduces the need to resort to inflationary mechanisms for financing the budget deficit.

The need for retention of the capital gains on financial assets has been successfully argued by representatives of the stock exchanges in the country. The various associations of members of the stock exchanges have portrayed the share market as a barometer of the performance of government and the economy. They have stressed the need for fiscal incentives to attract foreign private portfolio investment and thereby improve the balance of payments position, and so on.

Altogether, tax reform involving broad-basing of direct taxes by removal of major exemptions and concessions has been effectively frustrated by entrenched, powerful, well-organized and articulate interest groups. The government has had to retreat in the face of opposition from such groups. It has been left with the worst possible outcome. Tax rates have come down while the multitude of tax expenditures continues.

The failure of government to broaden the base of direct taxes by reducing tax expenditures leads to the identification of a number of factors which mitigate against success of reform initiatives as follows:

i) Lack of commitment to the reform by agents of the state, arising from a perception that the reform may damage vital national interests like food production, savings, exports, etc.

ii) "State capture" by special interest groups like the traditional feudal elite, bureaucracy and the emerging corporate business interests which extract substantial rent from the existing tax-expenditure system and are unwilling to give up their privileges;

iii) Wrong strategy of implementation of reforms. By first reducing tax rates the opportunity which existed for bargaining with (and compensating) losers was lost.

5. BROAD-BASING OF THE GENERAL SALES TAX

The primary motivations for broad-basing the general sales tax, following its conversion to a VAT type of tax in 1990-91 with tax invoicing features are, first, to compensate for revenue losses resulting from the on-going tariff reforms (discussed in the next section), second, to move the tax base towards consumption in order to encourage savings, third, to achieve a more neutral tax structure by taxation of a broad range of items (excluding food and other necessities) and, fourth, to bring about the process of greater documentation of economy as result of the incentives created for invoicing so as to claim tax refunds.

5.1 Progress in Implementation

The GST was levied on 59 additional industries between 1991 and 1993. However, many of these industries are small in terms of value and revenue gains have been marginal. In an attempt to cover small units, a non-invoicable GST at the rate of 5 percent has also been introduced. Simultaneously, in the case of some industries a kind of forfeit (shoora-e-tashkees) system has been introduced leading to negotiated fixed tax liabilities of all units within an industry. Some tentative attempts have been made to extend the GST to the wholesale and retail trade sector and thereby give it more of the character of a consumption tax. The Nawaz Sharif government was reluctant to fundamentally extend the tax net to this sector because of a virtual absence of documentation of transactions and as the urban trading community constituted a major support base for the IJI government. In the budget of 1993-94, primarily out of considerations of revenue enhancement, the standard GST rate was raised from 12½ percent to 15 percent.

The Finance Bill of 1994 represents a major effort at broad-basing of the GST. As additional 277 industries, excluding those producing food items, have been brought into the tax net. Simultaneously, the fixed sales tax system has been abandoned on the grounds of inelasticity of revenues and low effective rates. However, this reform led to a nationwide strike by business and trading interests which compelled the government to temporarily suspend the withdrawal of the fixed tax system and evaluate industries proposed to be brought into the GST regime.

5.2 Gainers and Losers

The potential gainers from reforms of sales tax are the recepients of benefits financed by the additional revenues or from the decline in inflation resulting from less resort to deficit financing. Of particular significance in this context is the fact that 80 percent of the revenues from GST accrue to the provinces and are likely to be used largely for enhanced provision of social and economic services like education, health, roads, water supply, etc. Also, large scale units which have been placed at a competitive disadvantage are likely to support the collection of the tax from smaller units.

Losers are essentially those industries which are brought into the tax net as a result of the broad-basing measures. However, depending upon the relevent price elasticities, at least part of the burden of the tax is shifted forwards to consumers, who in this sense are the real losers. Opponents of the reform have argued that this will put a regressive tax burden on households. Given that the burden of the tax can be shifted, it is perhaps surprising as to why there is so much resistance from industry to the imposition of this tax. Reasons for this are, first, greater documentation of transactions increases the ability of the tax department to also more efficiently ascertain income tax liabilities, second, even though the system is based on self-assessment rather than on supervised clearance of consignments (as in the case of excise duties) there is the prospect of payment of bribes to tax officials at the time of registration and annual audit, third, the VAT nature of the tax imposes substantially higher compliance costs on tax payers arising from the need for maintaining proper records and accounts. These factors are responsible for the strong preference of industry for the fixed sales tax system. Also, it appears that special factors have been operative in 1994. Given the conditions of an economic recession, business is of the view that enhancements in indirect taxes at this time can only add to the problem of stagnant or declining output levels.

5.3 Determinants of Success

Role of Gainers

The support for mobilizing revenues from the GST has been greatly diminished by the indirect nature of this tax and the fact that it tends to raise prices. There is widespread opposition in Pakistan to further enhancements in indirect taxes, which already account for over 75 percent of revenues. These taxes are generally considered as regressive, distortionary and inflationary in character. It is unlikely, therefore, that there will be major spontaneous support for the broad-basing of the sales tax even if it is shown that it can fetch substantial additional revenues. From the viewpoint both of equity and efficiency, the popular demand is more for resource mobilization through reduction in evasion and elimination of concessions in the direct tax system.

Role of Agents of State

There is apparently a degree of contradiction in tax policy which highlights problems of commitment on the part of the agents of state. In the context of direct tax reform, the philosophy has essentially been one of simplification, reduction in compliance costs and less direct contact with tax officials. This explains the move towards presumptive and withholding taxes (discussed in Section 3). In the area of indirect taxes, however, the thrust is on introduction of a broad-based VAT, a sophisticated tax which has found place internationally only in the last two decades or so (for example, there is no VAT in the USA). It will require high levels of documentation and force substantially higher compliance costs on tax payers. This contradiction has sent confusing signals about the broad directions of tax reform in the country. Many of the senior officials of the CBR are not entirely clear about the mechanisms of operation of a VAT and its economic benefits. The lack of commitment to a pure form of VAT is evidenced by the eagerness with which improvisations in the form of presumptive, fixed or non-invoicable GST have been adopted in special cases. More recently, the retreat from the fixed sales tax system probably does not represent as much an enhanced commitment to VAT as the process of assertion by the tax department of its right to assess tax liabilities on an on-going basis from individual units and not once-for-and all following group negotiations. Perhaps, in recognition of the perceived lack of commitment to reforms in GST, the Prime Minister in her speech on the eve of the presentation of the budget for 1994-95 extolled the virtues of a sales tax.

Also, it appears that the pace of implementation of the reform has been artificially increased by the presence of IMF conditionalities. Consequently, the broad-basing is taking place without adequate strengthening of the tax department, proper survey, registration and education of tax payers and printing and circulation of forms. This will jeopardise the successful implementation of the reform proposals.

The strong resistance to extension of the GST has motivated government to take some potentially significant actions. The most important move in tactical terms is to bifurcate the present chambers into separate bodies for trade and industry respectively, on the grounds that interests fundamentally differ. Traditionally, industry has had the necessary lobbying powers in the corridors of Islamabad (as demonstrated by the effectiveness of All Pakistan Textile Manufacturers Association [APTMA]) while trade has provided the street muscle at times of agitation. The break up of this coalition could potentially weaken opposition to reforms like a scaling down of tariffs or broad-basing of the GST. It is also possible that in subsequent attempts at reform, government may attempt to split existing tax payers from new entrants into the tax net by simultaneously announcing a reduction in tax rate (say, back to 12½ percent) alongwith a major broad-basing initiative, like extension of GST to the retail level.

Role of Losers

The effectiveness of losers in organizing a coalition to resist the reform has already been demonstrated. The success achieved while strengthen the motivation to block future changes. A crucial time is next year when a fundamental step is proposed by government (as part of the agreement with IMF) of across-the-board extension of the GST to wholesale and retail trade. There is the possibility that the opposition to this move may even acquire a political dimension.

The experience with reforms of the GST demonstrates how an effective coalition of potential losers can be organized in the presence of weak support for the reform from potential gainers due primarily to the dispersed, uncertain nature and uneven distribution of gains and of agents of state who have demonstrated some lack of vision, commitment and preparedness for the reform.

6. TARIFF REFORMS

Pakistan's taxation system is characterized by excessive dependence on taxes on international trade. Customs duties, surcharges, import licence fee (equivalent to a tax levy) and sales tax on imports contributed revenues of over Rs 87 billion in 1992-93, equivalent to 6.4 percent of the GDP. Statutory tariffs are high and while these were justified in the past on the basis of the `infant industry' argument their continuation has perpetuated excessively high levels of protection across-the-board to a large number of industries including those which are inefficient (either with negative value added at world prices or high domestic resource costs). This has led to a large-scale diversion of resources towards import substitution and created a strong anti-export bias. High tariffs have also encouraged rampant smuggling (of over 5 percent of GDP according to PIDE [1993]) which has not only eroded the tax base and adversely affected industrial production but has also implied all the social evils associated with the generation and use of illicit incomes.

Technical flaws have also crept into the tariff structure. Ad hoc tinkering with rates largely for revenue purposes has created fiscal anamolies. There is no rational `cascading' of rates and average rates do not vary significantly by stage of processing. High statutory tariffs have led in many cases to the promulgation of Statutory Rules and Orders (SROs) to grant exemptions or concessions by region, type of end use or nature of importer. This has greatly complicated customs administration and promoted corruption and rent-seeking activity. In 1992-93, almost 46 percent of dutiable imports paid concessionary duties under the provisions of some SRO. Therefore, tariff reforms are required not only from the viewpoint of influencing the future process of industrialization of the country in the desired directions but also for rationalizing the tax regime, making it simpler to administer and transparent while using fiscal policy as the prime instrument for tackling the problem of smuggling.

6.1 Progress of Implementation

A gradual process of reforms in the trade regime has been on-going in Pakistan for some time. In the first phase, quantitative restrictions on imports were largely removed and the `negative' list consists now largely of items which are prohibited for religious or other reasons. During the last few years, the maximum tariff rate (except for automobiles) has been brought down from 225 percent to 80 percent. However, efforts at reform have been piecemeal in character and no attempt has been made to bring about comprehensive changes which eliminate fiscal anamolies and provide well-defined signals for allocation of domestic resources.

The last caretaker government constituted a Tariff Reforms Committee to develop a new tariff structure to be implemented over a three year period, keeping in view the impact of the proposed changes on levels of effective protection to industry, on overall tax revenues and on the trade balance. The Committee had inter-ministerial representation and also sought the view of leaders of key industries.

The Committee made a large number of recommendations including; first, the abolition of para-tariffs; second, scaling down of the effective (inclusive of surcharges and licence fee) maximum tariff from 92 percent to 50 percent over the three year period; third, cascading of tariffs with lowest rates for non-competitive primary raw materials and highest for finished goods; fourth, promotion of exports by duty free imports of raw materials, intermediate goods and machinery for export-oriented sectors with phasing out simultaneously of the cumbersome and difficult to administer export rebate scheme; fifth, protection to existing and proposed deletion programs and locally fabricated machinery; sixth, duty free imports of food and other basic items; seventh; sizeable tariff reductions on items prone to smuggling; eighth, large-scale withdrawal of SROs including removal of differential treatment between industrial and commercial importers and concessions to public sector entities and, ninth, introduction of minimum tariffs to reduce rate dispersion.

The Committee carried out case studies of effective protection, pre-and post-reforms. Contrary perhaps to expectations, it was able to demonstrate that protection actually increased in over half of the industries studied following reform despite lower levels of tariffs due primarily to the cascading. Also, revenue-neutrality was preserved with 50 percent of the revenue losses being recovered by phasing out of SROs, 35 percent by broad-basing of the sales tax and 15 percent by withdrawal of exemptions in the income tax regime. Impact on the level of imports was not considered to be sizeable as the stimulatory effect exercised by lower tariffs was likely to be counter balanced by the withdrawal of concessions and introduction of minimum tariffs.

Soon after the presentation of the report of the Committee, the newly inducted elected government included a major tariff reforms package as part of the Structural Adjustment Program with the International

Monetary Fund. This package incorporates many of the principles of reform enunciated by the Committee. However, it envisages a faster program of reduction of tariffs, whereby the maximum tariff is to be brought down to 35 percent (rather than 50 percent as recommended by the Tariff Reforms Committee) by beginning of fiscal year, 1996-97. The first phase of this reform package has already been implemented in the 1994 Finance Bill whereby para-tariffs have been merged into the basis tariff structure, the maximum tariff has been brought down to 70 percent, the number of rate slabs has been reduced from nine to six, some SROs have been withdrawn including the distinction between commercial and industrial importers and drastic reductions have been announced in rates on items prone to smuggling. Neutrality of tax revenues has been, more or less, preserved by the revenue gains due to consequential effects on sales tax collections arising from the merger of para-tariffs. However, there has been a sizeable revenue loss of over Rs 15 billion due to the abolition of the import licence fee.

Impact on levels of protection is not very pronounced in the first year of reform because of the merger of para tariffs. While industries with competitive imports at the maximum tariff rate have experienced some decline, most industries have yet to receive the shock of downward adjustment in tariffs on competitive imports. For the same reasons, impact on the level of imports is unlikely to be significant.

6.2 Potential Gainers and Losers

Tariff reforms of the type envisaged under the SAF will represent one of the major events in the industrial history of Pakistan, with vital income distributive implications, many of which have not yet been fully comprehended. In broad terms, protection levels to a large number of industries will be altered dramatically, some will gain and others will lose. Beneficiaries will include industries where the tariff rate on output will fall less than the tariff rate on intermediate inputs, while the opposite case will apply to losers. However, considerable uncertainty attaches at this early stage of the reforms process as to the industrywise distribution of gains and losses. This uncertainty is partly the consequence of the strategy pursued by government for implementation of the reforms. The Tariff Reforms Committee had recommended that an open and transparent approach be adopted whereby industry was consulted at every stage and at the micro level views incorporated subject to adherance to the broad principles of reform. It was proposed that model tariff schedules be prepared for each year of the three year reform period and circulated in advance to representatives of trade and industry for eliciting views.

This has not happened. Instead, the traditional approach of maintaining total secrecy till the announcement of the Finance Bill has continued. Consequently, there has been a spate of complaints from various industry groups about the emergence of new fiscal anamolies and the Government has had to constitute a Committee to tackle these problems. Perhaps in the view of the policy makers the only viable approach is one of creating a de facto situation and then handling the fall out as the alternative of an advance announcement of the details of the reforms package could lead to the formation of strong coalitions to block the move.

However, while the strategy adopted may minimize in the short run the resistance by losers it also runs the risk of failing to mobilize support from potential gainers. Given the complex nature of the tariffs reforms process and its wide ranging ramifications, it is clear in the political economy sense that the active resistance by potential losers has to be traded off against the aggressive and vociferous support of potential gainers. This can, however, only happen if the potential gainers clearly perceive the gains and are then able to lobby in favor of the reforms.

Serious informational problems also exist in the case of the broad mass of consumers who will benefit from the reduction in the landed costs of imported consumer goods and through a fall in profit margins on smuggled goods due to greater competition from official imports. The government must identify specific cases of price reductions in major consumer items (e.g. bicycles, tractors, electronic goods, etc.) due to the tariff reforms and advertise them in the popular press and media to create broad-based support for the change.

One of key target groups of gainers from the reforms is exporters, who not only benefit in a broad macro sense due to the narrowing in the differential between the effective exchange rate on exports and imports thereby tilting relative profitability in favor of the latter but also in a more direct and visible manner by the elimination of duties on imports of raw materials, intermediate goods, spare parts and machinery for export purposes. However, this coincides with the phasing out of the export rebate regime which had become a mechanism for making large but hidden transfer payments to many exporters. As such, support for tariff reforms from exporters is likely to remain muted.

Following the announcement of the tariff reforms package in the budget speech of 1994-95 there is now a growing recognition of the disequilibrium that this will create in the industrial sector and a, more or less, general apprehension that there will be serious dislocation, large scale plant closures and labor displacement. The downward adjustment in the maximum tariff rate from 92 percent to 35 percent within three years is being seen as too rapid in view of the rigidities in response mechanisms arising from the high costs of capital, union agreements, lack of technology transfer, etc. In the minds of losers this reform will contribute, at least in the short run, to a process of `deindustralisation' in the country and there will be a flood of imported goods which will not only lead to a major deterioration in the balance of trade but will also price out domestic industry. Given that this set of reforms forms a part of the agreement with the IMF there is also the perception that the initiative is not indigenous in origin but has come from abroad on the behest of Western industrial interests who want to gain access to markets in the Third World. This is being treated as one more example of vacillation to IMF conditionalities which is not in the greater national interest.

Withdrawal of SROs is also likely to pose the same problems as confronted in the case of removal of major exemptions from income tax (discussed in Section 4). The government will have to contend with the pressure and lobbying powers of powerful special interests. First, multinationals, which have invested in import-substituting industries with high levels of profitability in a protected market, will be adversely affected by scaling down of tariffs. This includes sectors like chemicals, automobiles, polyester, etc. Second, removal of the preferential treatment given to imports by major public sector importers like WAPDA, PTC, OGDC, etc., will be strongly resisted on the grounds that this will imply higher project costs and necessitate higher levels of borrowing while leading eventually to higher utility prices. Third, the case for retention of fiscal incentives like exemption of import duties on machinery for rural industrialization will be strongly argued for at the political level as a means of removing regional disparities. Of course, as tariff levels come down generally the value of concessions should be decrease substantially. The government has tended to move in the opposite direction to that required by the tariff reforms as indicated by the recent actions of granting duty concessions for power generation and to the power sector.

6.3 Determinants of Success

The true test of implementation of the reforms will come next year when as per the agreement the maximum tariff rate will have to be slashed from 70 percent to 45 percent with consequential downward changes throughout the tariff schedule and it will no longer be possible to cushion the impact by merger of para-tariffs.

Success will hinge largely on the government's ability to orchestrate the process and mobilize support from potential gainers which include specific industries, commercial importers, consumers and exporters while introducing safety nets to minimize the social costs of adjustment including provisions for social security, labor retraining, credit for modernization, etc. It is also of significance to note that up to now resistance has come from owners of industrial capital but as some industries run into structural problems and there are retrenchments, then trade unions could also launch a protest movement. This will create special problems for the present government which has a strong vote bank in unions and is sympathetic to labor interests. There will be difficulties in selling the argument, due to the inevitable presence of time lags, that employment will eventually be promoted by the increase in labor-intensive exports.

Implementation problems are also likely to be compounded by the degree of ambivalence and apparent lack of full commitment of agents of state to the tariff reforms process. First, there are genuine concerns voiced by the tax administration and the Ministry of Finance as to whether the transition can be achieved in a revenue-neutral manner, without exacerbating the already existing problem of the large budget deficit. Reductions in customs duty revenues will require quantum jumps in revenues from domestic taxes like income, sales and excise. Growth in income tax revenues is limited by the presence of large tax expenditures, described in Section 4, and the state appears to be have been captured by special interest groups. Broad-basing of the sales tax will hinge on the level of tax payer compliance and greater documentation of transactions. Existing excise duty rates are high and further enhancements could be counter productive. Also, the federal government could be a major loser, even if overall revenue-neutrality is somehow achieved, given the nature of revenue sharing arrangements whereby customs duties are outside the divisible pool while income and sales are shared with the provinces.

Second, there is a degree of pessimism with regard to the possibilities of export growth in the short to medium run given the limited product diversification and low quality of Pakistani exports and an increasingly competitive international environment. There is some apprehension that any deterioration in the trade balance will lead to a process of destabilisation due to cumulative exchange rate depreciation. In broad terms, a strong level of commitment of agents of state to the process of tariff reforms, as part of the overall vision of the government about industrial development, does not appear to be clearly visible.

The next two years will determine the success or failure of this package of reforms. The government will have to carefully orchestrate the reforms by playing off gainers against losers. The former will have to be identified through micro research and their support for reform mobilized. A vigorous public awareness campaign will have to be launched to acquaint the larger population of the immediate and long term gains from the reforms, including consumer benefits, less corruption and smuggling, etc. Costs to losers will have to minimized by establishment of safety nets including unemployment benefits, credit facilities and subsidized labor training programs. A more open and transparent process of negotiations may have to be resorted to create a greater sense of `ownership' of the reforms. In the absence of these steps, there is the danger that the tariff reforms process may be interrupted by resistance from a broad coalition of industrial and labor interests, as has already happened with the broad-basing of the GST this year.

CONCLUSIONS

The paper has adopted a political economy perspective to analysis of four major components of tax reform during the 90s in the Pakistani setting, one of which has been, more or less, implemented and three are on-going. Within this perspective, it identifies the potential gainers and losers from each reform and the determinants of success or failure depending upon the role played by these gainers and losers and the agents of state in the process of reform.

The paper demonstrates that while a government can meet with exceptional success in some areas it can fail in others, depending primarily on the governance capacity displayed in implementing each reform. For example, the Nawaz Sharif government achieved notable success in extending the network of withholding and presumptive taxes within the income tax system because a number of favourable factors of governance came together. These included the projection of the particular reform as an integral part of its vision of change, demonstration of superiority of the reform over the available actions, building of a strong and diversified coalition of support, strong leadership from the top, by passing of and credible threats to losers, lack of homogeneity of losers and spectacular initial success of the reforms.

In contrast to this, elimination of tax concessions and exemptions, to make the income tax system more neutral and fair, floundered because of a low level of commitment to the reform on the part of agents of state, state capture by special interest groups, lost opportunities for bargaining with potential losers, strong organization and lobbying power of losers, lack of information with gainers and launching of a successful campaign by potential losers that the status quo is actually in everybody's interest.

Similarly, the partial retreat from implementation of reforms in the general sales tax this year reveals how an effective coalition of potential losers can be organized (with street agitation) in the presence of weak support for the reforms from gainers due to the dispersed, uncertain nature and uneven distribution of gains and agents of state with some lack of vision, commitment and preparedness for the reforms.

The impending tariff reforms will require a high level of governance capacity to carefully orchestrate the reforms by skillfully playing off gainers against losers. Imperatives for reform will have to be successfully demonstrated within the overall vision of industrial development. A vigorous public campaign will have to be launched to acquaint the larger population of the immediate and long term gains. Specific groups of gainers like commercial importers, exporters and consumer groups may have to be mobilized. Compensatory mechanisms will need to be developed for losers in the form of safety nets like unemployment benefits, subsidized credit and training, etc. A more open and transparent process of negotiations may also have to be adopted to create a greater sense of ownership of the reforms.

The next year will represent a major milestone in the path of tax reforms in Pakistan. As part of the SAF, deep cuts will have to be made in tariffs and the GST will have to be extended to one of the most difficult to tax sectors, wholesale and retail trade. The basic question is whether the government will demonstrate the ingenuity, capacity and will to successfully pilot through these changes.

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TABLE 1

TREND IN REVENUES FROM WITHHOLDING AND PRESUMPTIVE TAXES UNDER SECTION 50 OF THE INCOME TAX ORDINANCE

(Rs in Million)

Section	Type of Income	1988-89	1989-90	1990-91	1991-92	1992-93	ACGR (%)
50/1	Salary	705	930	1395	1732	2431	36.3
50/2	Interest on Securities	1836	1850	1673	4609	7072	40.0
50/2A	Interest	-	-	-	1020	1963	-
50/3	Income of Non-Residents	264	232	494	2077	539	19.5
50/3A	Technical Fees	-	-	-	3	42	-
50/4	Income from Contracts	2286	2833	3822	5080	6846	31.5
50/4A	Brokerage Fees	-	-	335	55	47	-
50/5	Importers	931	1952	2071	3039	3556	39.8
50/5A	Exporters	-	-	-	-	1190	-
50/6	Transporters	60	106	121	128	286	47.8
50/6A	Dividends	-	-	-	100	124	-
50/7A	Auctions	90	84	139	138	157	14.9
50/7B	Rental Income	-	-	-	12	39	
50/7C	Winnings from Lottenes	-	-	21	47	110	
50/7D	Interest on Bonds	-	-	-	20	68	
50/7E	Electricity Bills	-	-	-	-	334	
	TOTAL	6172	7987	10071	18060	24804	41.6

Sources: CBR Year Book, 1991-92.
Resource Mobilization & Tax Reforms Commission.

TABLE 2

TREND IN INCOME TAX REVENUE BY TYPE, 1988-89 TO 1992-93

	1988-89	**1989-90**	**1990-91**	**1991-92**	**1992-93**
Total Income Tax Revenue (Rs in Million)	13407	15000	19079	27913	35018
[Share (%)]					
Collection of Demand	26.0	22.8	25.3	12.1	9.5
Payment with Returns	38.8	42.4	35.8	28.0	23.4
Deductions at Source	46.0	53.4	53.3	65.1	71.0
Miscellaneous	0.2	0.2	0.1	2.0	0.3
Less Refunds	-11.0	-18.8	-14.5	-.72	-4.2
TOTAL	100.0	100.0	100.0	100.0	100.0

Sources: CBR Year Book 1991-92.
Directorate of Research and Statistics, CBR.

TABLE 3

ESTIMATES OF TAX EXPENDITURE IN DIRECT TAXES*

1990-91

(Rs. in Million)

	Area of Exemption/Concession	Tax Expenditure
1.	Tax Holidays	350[a]
2.	Capital Gains on Financial Assets	1100[a]
3.	Bonus Shares	170[b]
4.	Salary Perquisites	2800[b]
5.	Interest Income from Government Savings Instruments	3100[a]
6.	Income of Public Corporations	5600[b]
7.	Agricultural Income	3000[a]
8.	Agricultural Wealth	3300[a]
9*	Rebate on Export Income	1800[b]
10.	Accelerated Depreciation Allowances	1200[b]
11.	Exemption of Owner-Occupied Properties from Wealth Tax	700[b]
	TOTAL TAX EXPENDITURE	23120
	TOTAL DIRECT TAXES COLLECTION	19868
	TAX EXPENDITURE AS % OF REVENUE	116 %

[a] economic approach
[b] accounting approach

Source: Q.M. Ahmed and others, Study on the Quantification of Tax Expenditure in Income Tax, Applied Economics Research Centre, University of Karachi.