



*“Enhancing Efficiency in Tax Administration”*

## **TAX REFORMS PROCESS IN PAKISTAN** **Communication Strategies and Impact Evaluation**

### **Executive Summary**

Reforms processes in an organization should flow from a continuous discourse undertaken by all the stake holders, adopting a clear communication policy considering the internal and external dynamics of the organization. Broadly speaking, Pakistan tax policy structure consists of two types of Taxes: Federally Administered Taxes and Provincially Administered Taxes. All Federal taxes are administered by the Federal Board of Revenue (FBR) through two major departments; Inland Revenue Service (IRS) and Pakistan Custom Service. Inland Revenue Service is managing all three federal domestic taxes namely Income tax, Sales tax and Federal excise duty whereas the cross borders taxes like Customs duty is managed by Pakistan Customs Services. All the Provincial taxes like Agricultural Income Tax (negligible-levied on units of land and not on produce/income), Capital Value Tax (Levied on purchase/transfer of immoveable properties), Motor Vehicle Tax, Land Tax, Property Tax, Cesses like Cotton Cess, Sugar Cane Cess, and most importantly Sales Tax on Services are managed by the respective Provinces.(Provincial Revenue Boards/Authorities have been Established which are mainly looking after sales tax on services). It is important to note that more than 90% of tax revenue of the country is collected by FBR; and 75% to 80% of the Government expenditure is met by FBR resource mobilization efforts.

The need of Tax Reforms in FBR was felt at the national level. The factors leading towards reforms were mainly Weak economy, Low Tax to GDP Ratio and Narrow Tax Base. To realize the Tax reforms, a task force on tax administration reforms was appointed in June 2000 and a tax reform strategy was approved in November 2001. Considering the recommendations of this task force, IMF presented its report on tax reforms in May 2004. Later on, Tax Administration Reforms Project (TARP) funded by the World Bank was launched in January 2005. The original completion target for TARP was in 2009, which was enhanced up to 2011. The total cost of these reforms culminated into US \$149 million.

The objectives of reforms were to achieve overall increase in revenue collection, increase in tax to GDP ratio, taxpayer friendly environment and facilitation, automation of processes, withdrawal of Exemptions, less dependence on withholding taxes, broadening of tax base and simplification of tax laws.

Tax Reforms had a comprehensive package covering policy, procedures, administrative and organizational aspects. On policy side major changes were made by replacing all the existing Federal Tax Laws. Newly redrafted laws namely Income Tax Ordinance 2001, Income Tax Rules 2002, Federal Excise Act 2005 and Sales Tax Rules 2006 were promulgated. Policy reforms revolved around new concept of Universal Self Assessment Scheme (USAS) for promoting voluntary Tax compliance through maximum facilitation to the tax payer.



*“Enhancing Efficiency in Tax Administration”*

Through procedural reforms all income tax returns are treated as Assessment Orders; no returns are audited unless selected by the system randomly or on the basis of specific information. The processes are automated, electronic tax return filing has gradually been made mandatory for all except individuals below certain threshold. Thus the contact between tax officials and taxpayers was minimized substantially.

The administrative reforms were introduced through establishment of Regional Tax Offices (RTOs) and Large Taxpayer Units (gradually the number of RTOs increased to 18, LTUs to 4 and TFCs to 75). Further, Two Chief Collectorates and 15 Model Custom Collectorates (MCCs) were also established. Another important aspect of administrative reforms was the special double salary package for FBR officials along with meritorious rewards for high achievers; capacity building for officials through trainings in reputed national and international Institutes, and refurbishment of existing infrastructure along with new transit accommodations constructed for officers posted to other stations.

As far as organizational reforms were concerned, In Sep2009 the Income Tax Group became defunct and Inland Revenue Service (IRS) was formed which was a major transformation from the earlier system. Pre IRS, the Sales Tax and Federal Excise Duties were dealt by the Pakistan Customs Service. Whereas, post IRS- all three Inland Federal Taxes had been brought together under the administrative control of IRS.

In order to execute the reforms more effectively, in its initial phase, the professionals/ technocrat members were hired from private sector to ensure provision of latest techniques in fields like HRM, Taxpayer Audit/ Enforcement and Compliance etc. Later on the same functions were taken over by the department's own officers. There are various programs of automations developed through the technical assistance of Pakistan Revenue Automation Limited (PRAL).

TARP concluded in 2011. In pre reforms era, there was cylindrical system where one officer used to perform all core functions for the assigned areas at each level of hierarchy. Whereas in post reforms era the separate officers had separate functions for the same assigned areas. Due to various reasons different wings of same jurisdiction were unable to co-ordinate properly. Thus at Commissioner Level the composite system was restored in March, 2011 and down the line, Functional system continued.

Another tax reform commission was formed in 2014 to review and rationalize Direct and Indirect Taxes; customs tariff rationalization, review of autonomy and administrative structure of FBR, creation of border force to deal with illegal movement of persons and goods across international borders and any other related issues.

The latest reforms have been introduced recently bringing in some major corrective measures besides some new initiatives in Corporate Sector. In July 2016 existing structure was re-visited as per indigenous requirements; bifurcating procedures for Corporate/ Non-Corporate Sectors after 10 to 12 years of functional system. All existing 75 Tax Facilitation Centers (TFCs) are reverted to full fledged District Tax Offices to carry out composite functions for non-corporate sector headed by District Taxation Officers. As new measures the two existing RTOs in major cities (Karachi and Lahore) have been converted into



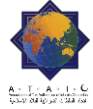
*“Enhancing Efficiency in Tax Administration”*

full-fledged Corporate Regional Tax offices (CROs). Thus currently two different systems are operating simultaneously. The functional based system running successfully for corporate sector is kept intact for all kind of corporate cases; however, the old composite system has been revived for non-documented non-corporate sector which can be handled better through the composite structure.

As far as communication strategies are concerned, we had different strategies at different levels. Before implementation of reforms at policy making level, communication strategy was not much interactive. Feedback of the FBR field officers, despite being major stakeholders, was not incorporated at the policy making level. The domestic conditions and prevalent tax culture was also not given due consideration.

At implementation level, the communication strategy was much inter active. Based upon the new re drafted laws, reforms (though adopted first) were introduced/shared with the field formations and representative bodies of the taxpayers (Tax Bars, ICAP, Chambers of Commerce, Trade Bodies etc) through various seminars, workshops, conferences and dissemination of educational and promotional material. Being a major switch over in a short span of time, feedback of field formations was essential at policy making level. Initially, it was very difficult for both tax officials and taxpayers to co-op with the new system. At its initial stage, the system showed rigidity and had to be implemented as it was perceived originally. However, after Facing practical problems and existing realities, the process gradually turned flexible on the basis of internal/external feedback. Consequently, necessary changes had to be made to harmonize the reforms with domestic needs and conditions. Thus proper inter active communication policy based upon indigenous conditions adopted later during implantation; lead the reform process towards gradual successes.

The impact of these reforms can be evaluated in various aspects. As far as the gains from reforms are concerned, FBR enjoyed regular increase in revenue which initially was 392 billion rupees but now stands at 3110 billion Rs on 30.6.2016. Similarly, tax to GDP ratio did not improve initially, however later on it showed substantial growth. The infrastructure and taxpayer facilitation was improved. A sound electronic data-base was developed. A highly developed web portal of FBR for internal and external communication was introduced and various processes were shifted to e-communication through old and newly introduced soft wares to deal with Income Tax, Sales tax and Customs namely IRIS (latest), ITMS (Income Tax Management System), TAMS (Taxpayer Audit Monitoring System), CREST (Computerized Risk Based Evaluation of Sales Tax), STRIVE (Sales Tax Real-Time Invoice Verification System), WEBOC (Web Based One Customs). Despite many challenges, the reforms processes had certain visible short comings too for significant reasons. Firstly because they were derived from the taxation system of developed countries having much stronger and fully documented economy. These reforms were not in conformity with Pakistan’s mostly non-compliant tax culture where almost all non-corporate sector is undocumented. The reforms remained highly effective in respect of LTUs, also effective for corporate sectors whereas not delivering for Non-corporate sector being undocumented. Further, the remote areas where earlier full-fledged taxation offices of high level remained operative, with introduction of reforms these were converted into mere facilitation centers. Audit along with enforcement functions in respect of remote areas were carried out in head offices of respective RTOs only, making it difficult for



*“Enhancing Efficiency in Tax Administration”*

both the department and taxpayer. Moreover the non presence of taxation officers in respective areas resulted into increasing non compliance. Due to non-compatibility of the reforms with the non-corporate sector, adjustments had to be made during and after conclusion of reforms.

Despite many successes, FBR is still facing great challenges like further increase in tax to GDP ratio, sizeable tax evasion, non-filing of existing taxpayers and narrow tax base.

However, despite challenges, the FBR being a dynamic organization & fully conscious of the cost it was causing to Govt. Exchequer, took the reforms process as a challenge that brought many successes. The FBR has gradually formulated a clear communication policy based upon feedback from every stakeholder. Moreover, it is worth mentioning that any reforms, particularly tax reforms, are an evolutionary process and irritants are gradually removed.

The way forward for the FBR to make full utilization of the reforms introduced, lies in bringing about further improvement in communication strategies, simplification of laws, broadening of tax base, revisiting USAS keeping in view the indigenous circumstances, facilitation with deterrence, taking VAT to retail stage in real sense, further enhancement of use of Information Technology, improvement in Federal-Provincial Tax coordination and rationalization of workforce and expansion of FBR to lowest administrative units.

FBR as an organization is open to change: In line with domestic needs through inter active communication policy, it is moving ahead, filtering the irritants and saving the best.

TASNEEM REHMAN

CHIEF COMMISSIONER INLAND REVENUE  
CORPORATE REGIONAL TAX OFFICE LAHORE, PAKISTAN

[tasneemrehman@yahoo.com](mailto:tasneemrehman@yahoo.com)

Phone No.042-99211825