



Reporting on Tax Expenditures in Pakistan

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CHIEF INCOME TAX POLICY

BACKGROUND

- ▶ Public Finance Management Act 2019 made it mandatory for the Federal Government to include a statement of estimated tax expenditure of the Federal Government in the Annual Finance Bill.
- ▶ Since then Federal Board of Revenue has prepared detailed 03 Tax Expenditure Statements 2020, 2021 and 2022. Part of Annual Finance Bill passed by the Parliament.
- ▶ Prior to the year 2020 scattered information pertaining to tax expenditure was available in Economic Survey Report published by the Federal Government every year
- ▶ A step forward towards effective fiscal governance

Salient features of Tax Expenditure Reports

- ▶ These reports document the estimated fiscal cost of Federal Tax Expenditures: Income Tax, Sales Tax and Customs
- ▶ Relevant legal provisions in Income Tax Ordinance, 2001, Sales Tax Act 1990 and Customs Act- the governing statutes
- ▶ They provide brief details on each tax expenditure, including its beneficiaries, costing methodology, sources of data, and historical information etc. <https://www.fbr.gov.pk › tax-expenditure-report>
- ▶ “revenue foregone” approach towards estimating tax expenditures has been adopted as against “revenue gain” and “outlay equivalence”

METHODOLOGY

▶ INCOME TAX

- Source of data is either Income Tax Returns, available in Federal Board of Revenue data base or third party information.
- Electronic e- filing of Returns since 2014- IRIS
- the scope of this data is limited by the number and nature of questions and fields on the tax return itself.
- expanding the questions and fields on tax return could increase the data available for estimating tax expenditures, this would also increase the compliance cost for the taxpayers

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- ▶ Third party data is collected from various federal and provincial government departments, relevant regulators, private organizations, industry associations, surveys and official websites-

-In case of insufficient data to produce a reliable estimate for a tax expenditure clause, the same are left as “not applicable”. In cases, where sufficient data is not available in the relevant year, it is assumed that the figures of tax expenditure would remain same as per last year's figures

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▶ SALES TAX

- In addition to the revenue foregone approach tax expenditure has also been calculated on VAT-GAP Model Estimation.
- Tax at benchmark rate of 17% applied on sales tax returns data, retrieved from Federal Board of Revenue data base, as if these goods were not exempt or zero rated. 18% for year 2023
- The total tax forgone is taken as a cost of exemption, and later necessary adjustments are made thereon, to rationalize the estimates.

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▶ Customs

- Again the data is taken from Federal Board FBR's official database, and estimations are calculated against statutory rates of duties, using revenue forgone approach.
- Tax Expenditures stand 2.8% of GDP

LIMITATIONS

- ▶ The tax expenditure estimates presented in these reports relate to Federal revenues only. Changes in FBR tax expenditure may have consequences for provincial revenues. However, these reports do not account for the provincial revenue expenditure. Constitutional limitations
- ▶ each tax expenditure is estimated independently by assuming that all other tax provisions remain unchanged. However, elimination of a tax expenditure would not necessarily yield the full amount of revenues shown in these report as multiple tax expenditures interact with each other.



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- ▶ The actual revenue impact due to elimination of a tax expenditure depends, amongst other factors, on the enforcement by field formation and also on the conclusion of tax litigations. The report cannot make a conclusive finding on these factors