

**Imperatives for Fiscal Policy in
the Federal Budget of 2013-14**



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THE FEDERAL BUDGET OF 2013-14**

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ACRONYMS

AJK	Azad Jammu and Kashmir
AOPs	Association of Persons
BISP	Benazir Income Support Program
BMR	Balancing, Modernization and Replacement
BODs	Board of Directors
CNG	Compact Natural Gas
CSF	Coalition Support Fund
CVT	Central Value Tax
FBR	Federal Board of Revenue
FDI	Foreign Direct Investment
FED	Federal excise duty
GARVs	Gross Annual Rental Values
GDP	Gross Domestic Product
GHPL	Government Holidays (Private) Ltd.
GST	General Sales Tax
IMF	International Monetary Fund
LPG	Liquefied Petroleum Gas
MAT	Minimum Assets Tax
MOF	Ministry of Finance
MTB	Market Treasury Bill
NBP	National Bank of Pakistan
NEPRA	National Electric Power Regulatory Authority
NFC	National Finance Commission
OGDCL	The Oil and Gas Development Company Limited?
OMO	Open Market Operations
PIBs	Pakistan Investment Bonds
PIT	Presumptive Income Tax
PML(N)	Pakistan Muslim League (Nawaz)
POL	Petroleum Oil and Lubricants
PPP	Pakistan People's Party
PSDP	Public Sector Development Program
PSE	Public Sector Enterprise
PTA	Pakistan Telecommunication Authority
PTCL	Pakistan Telecommunication Company Limited
SBP	State Bank of Pakistan
SMEs	Small and Medium Enterprises
SROs	Statutory Regulatory Order
TDS	Tariff Differential Subsidy
VAT	Value Added Tax
WAPDA	Water and Power Development Authority
WTO	World Trade Organization

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The public finances of the Government of Pakistan are in a state of disarray today. The revenues to GDP ratio has fallen sharply, current expenditures have shown explosive growth especially in the heads of debt servicing, grants and subsidies, while development expenditure has been slashed to critically low levels. The budget deficit has risen exponentially to unsustainable levels and is being financed by relatively high cost borrowings. Today, the country is effectively in the 'debt trap'. All convenients of the Fiscal Responsibility and Debt Limitation Act have been increasingly violated over the last few years.

The situation has reached a point where the capital market and the banking system are unable to pick up the large amounts of government paper which are being floated to finance the fiscal deficit without massive injections of liquidity by the Central Bank. This has inevitably meant more printing of money by the SBP, increasing thereby the risks of an upsurge in the rate of inflation.

There are, therefore, hard policy choices in the Budget of 2013-14 if the fiscal situation is to be even partially restored. Fortunately, the recent elections have given a strong mandate to the party of PML(N) which will assume power prior to the presentation of the Federal Budget and can start afresh the process of economic policy making.

The objective of this paper is to highlight the imperatives for fiscal policy in the Budget of 2013-14. Section 1 gives a summary of trends in federal finances. Thereafter, different sections of the paper deal with different parts of the budget, namely, tax revenues, non-tax revenues, net revenue receipts, current expenditure, development expenditure, financing of the fiscal deficit and prospects for 2013-14. The last section presents a summary of recommendations for the 2013-14 Budget.

1. TREND IN FEDERAL FINANCES

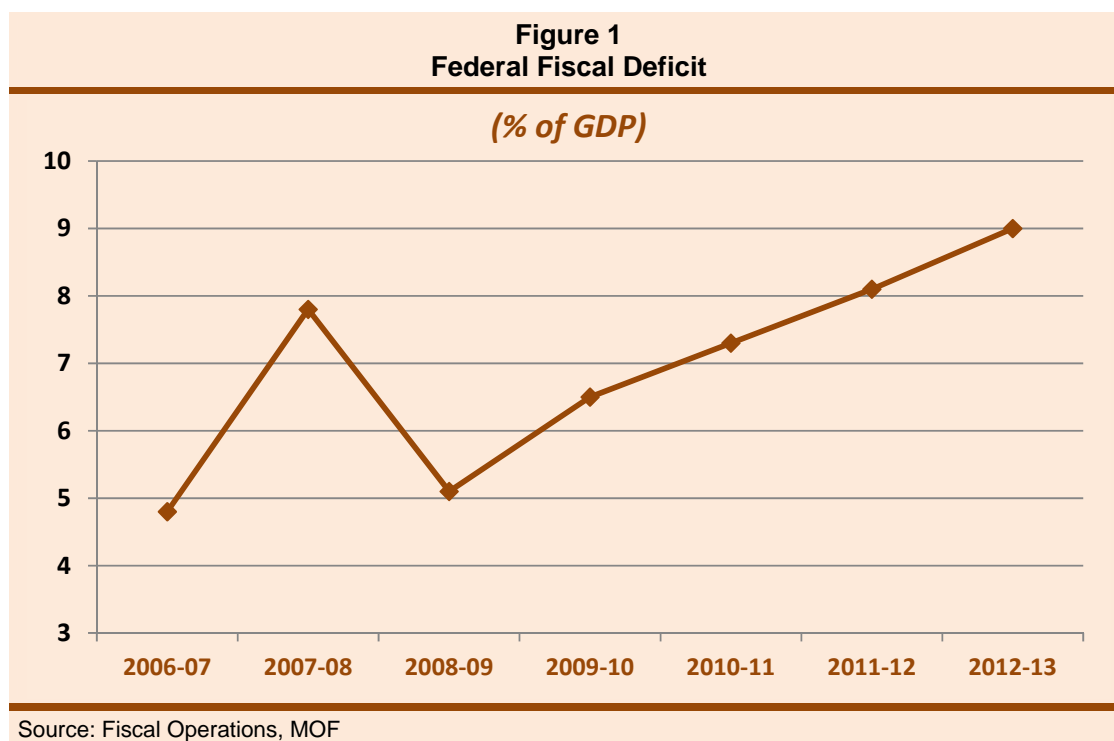
The summary of trends in federal finances is given in Table 1 and the details in Statistical Appendix. The first budget was presented by the PPP government for 2008-09 and the last budget for 2012-13. The last year prior to the induction of the PPP government witnessed a big jump in the size of the federal fiscal deficit by almost 3 percent to 7.7 percent of the GDP. This was caused primarily by the failure to adjust domestic POL prices to the sharp jump in the international price of oil and by large pre-election spending.

The PPP government initially took some difficult decisions and adjusted fully the POL prices. Fiscal deficit reduction was also facilitated by higher defence receipts from the Coalition Support Fund (CSF). Consequently, the fiscal deficit was brought down to 5 percent of the GDP.

	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
A. Gross Federal Receipts	14.2	13.7	13.7	13.3	11.9	11.7
Tax Revenues	9.8	9.9	9.1	9.6	9.1	9.4
Non-Tax Revenues	4.4	3.8	4.6	3.7	2.8	2.3
<u>Less Provincial Share</u>	<u>-4.6</u>	<u>-4.5</u>	<u>-4.1</u>	<u>-4.3</u>	<u>-5.5</u>	<u>-5.3</u>
<u>Net Federal Receipts</u>	<u>9.6</u>	<u>9.2</u>	<u>9.6</u>	<u>9.0</u>	<u>6.4</u>	<u>6.4</u>
B. Total Expenditure	14.4	16.9	14.6	15.4	13.7	14.5
Current Expenditure	11.6	14.2	12.1	12.4	11.9	12.6
Development Expenditure	2.5	2.6	2.4	2.9	1.7	1.9
<u>Net Lending</u>						
Others	0.3	0.1	0.1	0.1	0.1	0.0
C. Fiscal Deficit	-4.8	-7.7	-5.0	-6.4	-7.3	-8.1

Source: Fiscal Operations, MOF

Thereafter, as shown in Figure 1, there has been a continue increase in the deficit, to almost 6.5 percent in 2009-10, to 7.3 percent in 2010-11 and 8.1 percent of the GDP in 2011-12. Latest estimates, inclusive of unpaid claims, by the Planning Commission, of the federal fiscal deficit indicate that it may even exceed 9.0 percent of the GDP. This is an unprecedented level and highlights that public financial management at the federal level has, more or less, lost control.



A number of key fiscal ratios are presented in Table 2 and discussed below:

Tax-to-GDP Ratio: has consistently been below 10 percent of the GDP, with a somewhat declining trend.

Share of direct taxes: The share of direct taxes has fluctuated at around 38 percent and has shown a tendency to decline somewhat in recent years.

Share of non-tax revenues: Non-tax revenues have demonstrated slow growth and their share in total revenues has fallen sharply from 31 percent in 2006-07 to below 20 percent in 2011-12.

Provincial share in federal receipts: The share of provinces is mandated by the NFC. Prior to the 7th NFC Award, this share stood at below 33 percent, which has jumped to almost 47 percent after the Award.

Revenue Surplus/Deficit as % of GDP: This key ratio indicates a very alarming trend. Revenues are proving to be increasingly inadequate in even financing current expenditure. The revenue deficit which was about 2 percent has increased to above 5 percent of the GDP. In effect, a large part of current expenditure is being met through borrowings. Therefore, the country is effectively in the 'debt trap'.

Table 2
Key Fiscal Ratios of the Federal Government

Ratio	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	Trend
1. Tax-to-GDP Ratio (%)	9.83	9.86	9.10	9.58	9.07	9.42	↘
2. Share of Direct Taxes (%)	39.18	38.40	38.00	37.28	36.38	37.60	→
3. Share of Non-Tax Revenues in Total Revenues (%)	30.88	27.89	33.39	28.19	23.76	19.73	↘
4. Provincial Share in Federal Receipts (%)	32.42	32.66	30.22	32.08	46.60	44.96	↗
5. Revenue Surplus (+) / Deficit (-) as % of GDP	-1.94	-4.98	-2.54	-3.38	-5.52	-5.22	↗
6. Current Expenditure as % of Total Expenditure	80.33	84.09	82.71	80.66	86.58	86.59	↗
7. PSDP as % of GDP	2.90	2.74	1.68	1.98	1.29	1.51	↘
8. <u>Fiscal Deficit as % of GDP (federal)</u>	<u>-4.77</u>	<u>-7.67</u>	<u>-5.06</u>	<u>-6.36</u>	<u>-7.37</u>	<u>-8.08</u>	↗
9. % of external financing	48.21	19.26	23.26	20.07	8.1	7.7	↘
10. % of bank financing	n.a.	67.26	40.42	33.34	56.29	60.67	↗
11. % of non-bank financing	n.a.	13.48	36.32	46.59	35.61	31.63	↘

Source: Fiscal Operations, MOF

Current Expenditure as % of Total Expenditure: Rising levels of current expenditure are increasingly ‘crowding out’ development expenditure, mostly on the PSDP. The share of the former in total expenditure has increased from 80 percent to 87 percent. Only 13 percent of the federal budget is being devoted to development activities.

PSDP as % of GDP: The cut backs on the development side have implied that the size of the PSDP as percent of GDP has fallen to a critically low level, from almost 3 percent to only 1.5 percent of the GDP. At this level, even the replacement needs of public infrastructure are probably not being met and the productive capacity of the economy is not expanding significantly.

External financing of deficit: Another adverse development is the large decline in access to external assistance, especially to grants and concessional aid. The net contribution of external financing to the federal fiscal deficit has fallen precipitously from 48 percent to less than 8 percent.

Financing by the Banking System: This has emerged as the principal source of financing the deficit, with a share of 61 percent in total borrowing in 2011-12, with its concomitant implications on inflation and ‘crowding out’ of the private sector.

Non-Bank Financing: The dependence on non-banking sources, especially through the National Savings Schemes, reached a peak share of 47 percent in 2009-10 and has since declined to below 32 percent.

What is the likely budgetary outcome in 2012-13? The Ministry of Finance has released the data on the fiscal operations for the first nine months. Our projections for the year are given below in Table 3, based on estimates by the Planning Commission and on reports in the media.

	Budget Estimate	% of GDP	Projection	% of GDP	Difference
Revenue Receipts	3234		2807	11.9	-427
Tax Revenues	2504		2115	8.9	-389
(FBR)	(2381)		(2000)	(8.5)	(-381)
Non-Tax Revenues	730		692	2.9	-38
<u>Less Transfers to Provinces</u>	<u>1458</u>		<u>1231</u>	<u>5.2</u>	<u>-227</u>
<u>Net Revenue Receipts</u>	<u>1776</u>		<u>1576</u>	<u>6.7</u>	<u>-200</u>
Total Expenditure	2986		3374	14.3	388
Current Expenditure	2395		2833	12.0	438
Development Expenditure and net Lending	591		541	2.3	-50
Fiscal Deficit	1210	5.1	1798	7.6	588
Unpaid Claims	-		377	1.6	
Overall Fiscal Deficit	1210	5.1	2107	9.2	897

Source: Budget-in Brief, 2012-13, MOF and own estimates.

It appears that there will be a massive slippage in the Federal Budget of 2012-13, probably the largest in the history of the country. Not only is there likely a very large short fall in revenues but also substantial over expenditure. FBR was given a target for revenue collection at the start of the year of Rs 2381 billion. Following successive downward revisions in the target, it is expected to close the year with revenues of about Rs 2000 billion, a shortfall of almost 16 percent in relation to the original target. Reasons for the shortfall are discussed in a subsequent section.

On of the expenditure side, current outlays are expected to exceed budget estimates by as much as Rs 438 billion. Subsidies to the power sector are likely to be higher than anticipated by Rs 215 billion, interest payments by Rs 114 billion, defence expenditure by Rs 30 billion and other expenditure by Rs 79 billion.

Overall, the federal fiscal deficit is projected at 7.6 percent of the GDP as compared to the original target of 5.1 percent of the GDP. In addition, the Planning Commission expects that there will be pending unpaid claims of Rs 377 billion due to the fertilizer subsidy, commodity operations (especially in wheat) and the Tariff Differential Subsidy (TDS) in the power sector. If these are accounted for, then the federal fiscal deficit rises to the unprecedented level of 9.2 percent of the GDP in 2012-13. This represents the culmination of four years of flagrant '*busting of the budget*' by the previous Government. It leaves behind a mountain of debt, which is also quantified in a subsequent section.

As shown in Table 4, the projected increase in fiscal deficit over the level in 2006-07 is due almost 64 percent to lower net revenue receipts. The remaining 36 percent is contributed by higher expenditure, especially on the current account.

	2006-07	2012-13 (Projected)	Difference	% Contribution to Higher Deficit
Revenue Receipts	14.2	11.9	-2.3	51
Tax Revenues	9.8	8.9	-0.9	20
(FBR)	(9.6)	(8.5)	(-1.1)	
Non-Tax Revenues	4.4	2.9	-1.4	31
<u>Less Transfers to Provinces</u>	<u>-4.6</u>	<u>-5.2</u>	<u>-0.6</u>	<u>13</u>
<u>Net Revenue Receipts</u>	<u>9.6</u>	<u>6.7</u>	<u>-2.9</u>	<u>64</u>
<u>Total Expenditure</u>	<u>14.3</u>	<u>15.9</u>	<u>1.6</u>	<u>36</u>
Current Expenditure	11.8	13.6	1.8	40
Development Expenditure and Net Lending	2.5	2.3	-0.2	-4
<u>Fiscal Deficit</u>	<u>-4.7</u>	<u>-9.2</u>	<u>-4.5</u>	<u>100</u>

Source: Fiscal Operations, MOF and own estimates.

2. TAX REVENUES

The trend in the federal tax-to-GDP ratio since 2006-07 is given in Table 5. In 2006-07, the ratio was already very low at below 10 percent of the GDP, making Pakistan one of the least taxed countries in the world.

Years	Direct Taxes	Sales Tax	Excise Duty	Customs Duty	FBR	Petroleum Levy	Total
2006-07	3.85	3.56	0.83	1.52	9.76	-	9.76
2007-08	3.59	3.76	0.82	1.47	9.64	-	9.64
2008-09	3.29	3.55	0.91	1.17	8.92	0.88	9.80
2009-10	3.57	3.49	0.81	1.09	8.96	0.60	9.56
2010-11	3.30	3.50	0.76	1.03	8.59	0.46	9.05
2011-12	3.54	3.92	0.59	1.06	9.11	0.29	9.40
2012-13 (E)	3.20	3.73	0.49	1.07	8.49	0.41	8.90

(E) = Estimated
Source: Fiscal Operations, MOF

The performance, thereafter, has been even more disappointing. The tax-to-GDP ratio has continued to fall and by 2012-13 it is expected to be even below 9 percent. The only tax which has shown a rising trend with respect to the GDP is the sales tax, which has emerged now as the largest source of tax revenue.

Despite being a potentially buoyant tax, income tax has not performed well, and the direct tax-to-GDP ratio has fallen by 0.65 percent of the GDP since 2006-07. Excise duties are consciously being phased out, while the customs duty contribution has been limited by the large non-dutiable imports and presence of SROs. Overall, the FBR tax-to-GDP ratio has fallen by as much as 1.27 percent of the GDP.

The fall in the FBR tax-to-GDP ratio has been partially compensated for by the introduction of the petroleum levy, a carbon tax, in 2008-09. This yielded 0.88 percent of the GDP in the first year of its introduction. However, given the specific nature of the levy, its contribution is expected to fall to 0.41 percent in 2012-13. Also, the levy has been effectively reduced in periods of rising oil prices, as in 2011-12.

Why have federal taxes performed poorly during the last five years? Is this because of rampant and growing tax exemptions? Is it the consequence of slow growth in the economy and in the relevant tax bases? Or is it the result of a failure of tax administration in the presence of large-scale tax evasion and corruption?

We have analysed the reasons for the fall in the FBR tax-to-GDP ratio between 2007-08 and 2010-11. It appears that 80 percent of the fall is due to the '*base effect*', that is, relatively slow growth of tax bases like imports and large-scale manufacturing value added in relation to the growth of GDP. The remaining 20 percent is attributed to the '*rate effect*' indicating either a fall in tax rates, more exemptions and concessions or a deterioration in the quality of tax administration.

How has tax policy evolved over the tenure of the PPP government? A listing of taxation proposals in the last four budgets is given in the Appendix. The following policy preferences emerge from the examination of the proposals:

- (i) Tendency to raise rapidly the exemption limit of personal income tax. It has more than doubled from Rs 180,000 to Rs 400,000 since 2009-10. This has limited the number of returns being filed.
- (ii) Propensity to tinker around with Presumptive Income Tax (PIT) rates. For example, the PIT on commercial importers was raised from 2 percent to 4 percent in the 2009-10 budget, increased further to 5 percent in 2010-11 and then brought down once again to 3 percent in 2012-13.
- (iii) More incentives for investment including for BMR, enlistment in the stock exchange, etc.
- (iv) Variation in the standard GST rate, increase from 16 percent to 17 percent in 2008-09 and brought down once again to 16 percent in 2011-12.
- (v) Enhancement in excise duty on cigarettes, while phasing it out on other items like cement, beverages, etc.

Some innovations and measures to expand the tax base must be recognised as follows:

- (i) Introduction of the Petroleum Levy in 2008-09.
- (ii) Levy of a Minimum Income Tax at 1 percent on the turnover of companies in 2008-09.

- (iii) Introduction of an excise duty in VAT mode on banking services, import cargo handlers, stock brokers, insurance companies and advertisements in 2008-09.
- (iv) Introduction of a PIT on short-term capital gains on shares in 2010-11.
- (v) Imposition of a withholding tax at 5 percent on air travel in 2010-11.
- (vi) Elimination of zero-rating of domestic sales in six export-oriented industries, including textiles in 2010-11.
- (vii) Withdrawal of exemption from sales tax to agricultural inputs like fertilizer, tractors, etc, in 2010-11.
- (viii) Introduction of withholding tax on bank withdrawals at 0.3 percent on transactions above Rs 25,000 in 2010-11.

However, some of these proposals were withdrawn subsequently due to pressure from influential lobbies or not implemented effectively. Overall, discretionary changes in tax policy have not been enough to raise the tax-to-GDP ratio or even sustain it. In fact, the fiscal effort appears to have visibly slackened after 2010-11, following Pakistan's exit from the IMF SBA.

The 2012-13 Budget is the last pre-election budget of the PPP government. As such, it contains a relatively large number of concessions including the following:

- (i) Enhancement in the income tax exemption limit from Rs 300,000 to Rs 400,000.
- (ii) Minimum Income Tax reduced from 1 percent to 0.5 percent of turnover.
- (iii) Reduction in PIT rates: 5 percent to 3 percent for commercial importers, 1 percent to 0.5 percent for exporters and from 3.5 percent to 2.5 percent for supplies.
- (iv) Reduction in GST rate to 16 percent on all items.
- (v) Elimination of excise duty on 10 items.
- (vi) Further reduction in excise duty on cement.
- (vii) Scaling down of the highest tariff from 35 percent to 30 percent.

Clearly, these tax breaks have implied some revenue losses. In addition, the tax base of imports, in particular, has grown slowly. For example, POL products are the largest contributor to indirect taxes, with a share of 35 percent. Imports of these products have grown at 7 percent upto to March in 2012-13, as compared to over

22 percent in 2011-12. Automobile imports, the other major revenue spinner, are down by 7 percent. On top of all this, the morale of FBR has been badly affected by frequent changes of the Chairman and large-scale transfers of officials during 2012-13. Consequently, the growth rate of FBR revenues is projected at only 6 percent in 2012-13, the lowest since 2001-02. This will imply a fall in the tax-to-GDP ratio of FBR of 0.62 percent in one year.

Clearly, one of the primary tasks ahead for the newly elected government will be to raise the tax-to-GDP ratio, after the fall over the last five years. The PML(N) has already indicated in its Manifesto the key elements of its tax reform strategy as follows:

- Informal economy to be brought into the tax net
- Tax base will be broadened
- Taxation of all incomes
- Documentation of the economy
- Reduction in tax evasion by rationalizing tax rates
- Reform of tax administration
- Publication of a Tax Directory
- No increase in tax rates, subsequently reduction to attract FDI
- Provincial governments to raise their tax revenues
- Broadening of the scope of the sales tax
- Elimination of money laundering and whitening of black money
- Reduction in number of taxes
- Improvement in the process of self-assessment and audit
- Discouragement of non-essential imports by regulatory duties

The PML(N) manifesto targets for an increase in tax revenues from 9 percent to 15 percent of the GDP by 2017-18. This implies an increase annually of 1.2 percent of the GDP. Based on the assumption of a nominal increase in GDP of 12 percent in 2013-14, the tax revenue target will have to be set accordingly at Rs 2677 billion, an increase of Rs 562 billion or 26.5 percent over the projected level of Rs 2115 billion in 2012-13. This is an ambitious target, and will require an extraordinary level of fiscal effort, especially if tax rates are not to be enhanced. It carries the risk of further slowing down the economy.

We have prepared a menu of potential tax reforms which are largely consistent with the principles of tax reform enunciated above in the PML(N) manifesto and promise greater equity in the tax system, while yielding additional revenues. These reforms both in the tax policy and in tax administration are listed below.

Effective Agricultural Income Taxation: The present structure, as per the Agricultural Income Tax Act enacted by the Provincial governments in 1947, is either a fixed presumptive tax (with an exemption limit) per acre or a progressive rate structure on actual agricultural income (with scope for substantial deductions). The presumptive tax rates vary from only Rs 150 to Rs 250 per acre, which are less than 1 percent of the net income per acre. These rates need to be raised substantially. Simultaneously, the penalty for non-filing of a return may be raised from a maximum currently of Rs 1000 only to 100 percent of the assessed tax following the detection of non-filing.

Development of PIT is considered as a pre-requisite for signaling greater equity of the tax system. This could help in raising tax payer compliance generally.

Taxation of Assets: As indicated earlier, there was wealth tax on individuals upto 2000. It was an indicator of equity in the tax system and wealth returns also provided collateral evidence on income. This tax may be re-introduced. Alternatively, a Minimum Assets Tax (MAT) may be levied at 1 percent of global net assets, as the minimum income tax payable.

Minimum Tax on Turnover: A small percentage, less than 10 percent, of companies actually pay the corporate income tax. As such, a minimum tax on turnover was introduced in the Finance Bill of 2009-10 but has been partially withdrawn in the Finance Bill of 2012-13. There is a strong case for re-introduction of this tax, with the usual carry forward provisions, in order to curb corporate tax evasion.

Withdrawal of Tax Expenditures: There is need for introducing transparency and proper accounting of tax expenditures (cost of exemptions and concessions) in Pakistan, as part of the information provided at the time of presentation of the Budget to the Parliament, as in India. This will enable public debate on which exemptions and concessions are justified.

Direct Taxes

In direct taxes, the following tax expenditures need to be effectively targeted initially:

- a) Capital gains (short and long term) on shares and property
- b) Elimination of tax holidays beyond five years except for investment in the power sector
- c) Reduction in the first year depreciation allowance except for export-oriented industries and power sector
- d) Tax deduction on loan provisioning by banks to be only allowed only for priority sectors like SMEs, agriculture and exports.

Rationalization of Tax Rates: The divergence in tax rates between individuals, small and large companies needs to be eliminated. The corporate tax rate on large companies (especially publicly quoted) may be brought down gradually to 30 percent and raised to 30 percent for AOPs, small companies and individuals. This will encourage the process of corporatization in the economy and imply a more progressive personal income tax structure.

Moving from Schedular to Comprehensive Income Taxation: Currently, most forms of unearned income are taxed at source as separate blocks of income at a fixed and final rate of 10 percent. As highlighted earlier, this has reduced progressivity. As such, these fixed taxes may be converted into withholding taxes in the case of income from bank deposits, savings schemes, dividends, interest on securities, prize bonds, etc. This will also enable persons with total income below the exemption limit to claim refunds.

Further, fixed taxes are also levied on income proxies. In the case of contractors, suppliers, service providers and importers a scheme is proposed whereby the current fixed rate may be raised for tax payers who want to make this the final payment and a lower rate be prescribed for those who prefer to make a withholding tax payment and include the income derived in their returns. This could promote the process of documentation in the economy.

Development of the property Tax: This will involve extension of rating areas, higher taxation of commercial properties and reassessment of Gross Annual Rental Values (GARVs).

Incentives for Filing Returns: Numerous incentives may be offered to taxpayers (AOPs and small companies) who have regularly filed a return over a period of two years with no under-declaration or short payment. These incentives could include the following:

- a) Some preference in contracts for supplies to government departments
- b) Guaranteed refund within the stipulated time
- c) Access to a bank loan up to certain limit
- d) Provision for carry forward of losses
- e) Partial or full exemption from withholding taxes, contributing thereby to improvement in the cash flow position
- f) Preferential treatment in getting access to public services like issue of passport; electricity or gas supplies, etc.,
- g) A tax credit.

These incentives could induce a significantly higher number of tax returns.

Indirect Taxes

Proposals in the domain of indirect taxes include the following:

Introduction of a Broad-based Integrated VAT: There is need to reconsider passage of the VAT Bill of 2010. Recent developments like the establishment of a separate tax machinery for collection of the sales tax on services by the Provincial Governments of Sindh and Punjab have made the task of integration more difficult. It has complicated the process of input tax invoicing of services in manufacturing and of manufactured goods in services. There is need for introducing a system of recording tax invoices issued across provincial boundaries and of credits/refunds between governments.

Broad-basing has considerable scope, especially in the area of services. For example, the Services Tax in India is levied on 125 services and generates 1 percent of the GDP. Major services which have not been covered by the Sales Tax on Services in Pakistan include credit card services, security services, consultancy services, accountancy services, legal services, airport services, air travel agents, etc. These services are mostly consumed by corporate entities or upper income groups. The standard rate may be brought down to 12.5 percent once again, following the broad-basing.

Rationalization of Customs Duties: The statutory tariff rates (by nature of the good in terms of value added) must be adhered to with essentially three slabs only of 5 percent, 15 percent and 25 percent respectively. Simultaneously, most of the SROs, except those pertaining to trade agreements, may be withdrawn.

Also, in order to eliminate the problem of underinvoicing, a system of *minimum import prices* may be introduced for some commodities, with the provision that these prices will be revised periodically. This system was in operation in Pakistan in the 90s and is not violative of WTO rules, if used selectively.

Tax Administration

FBR: Radical changes are required to make FBR more effective in implementing reforms in tax policy and collecting more revenues. The following measures are needed to be undertaken on a priority basis:

- a) Conversion of FBR into an autonomous Revenue Authority
- b) Strengthening of the Revenue Division in the federal Ministry of Finance for formulation of tax policy
- c) Filling of asset declaration periodically by tax officials
- d) Strengthening the Tax Ombudsman and vesting him/her with judicial powers
- e) Internal strengthening of FBR in the areas of audit and intelligence
- f) Development of a Data Warehouse, linked particularly to withholding tax payments
- g) Streamlining the process of payment of refunds
- h) Augmenting the quality of human resources
- i) Publishing a Tax Directory annually of payments by tax payers.

3. NON-TAX REVNEUS

Non-tax revenues are seldom focused on discussions on the budget. Historically, they have been a fraction of tax revenues. But what has not been realized is that, as shown in Table 4, these revenues are responsible for a bigger part, over 60 percent, of the fall in the revenue-to-GDP ratio since 2006-07. Yet the emphasis has primarily been on tax revenues.

What do non-tax revenues consist of? There are three types of non-tax revenues, viz, income to the federal government from property and enterprises, receipts from civil administration and other functions and miscellaneous receipts. The first type includes profits, dividends from and interest payments by provincial governments and PSEs. The second type consists primarily of SBP profit, defence receipts (especially from the CSF since 2002), and revenue from user charges on different services. The third type of non-tax revenues are primarily royalties and surcharges on oil and gas and passport fees.

The trends in different non-tax revenues since 2006-07 is given in Table 6. Overall, between 2006-07 to 2012-13, there is likely to be major fall in the non-tax-to-GDP ratio of over 1.4 percent as compared to 0.9 percent in the tax-to-GDP ratio.

	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
Income from property and Enterprise	1.18	1.28	0.79	0.55	0.44	0.35	0.33
Receipts from Civil Administration	1.72	1.32	1.85	2.35	1.40	1.04	1.60
Miscellaneous Receipts	1.50	1.22	1.92*	0.85	0.99	0.93	0.99
Total Non-Tax Revenues	4.39	3.82	4.56	3.76	2.83	2.32	2.92

*inclusive of petroleum levy
Source: Fiscal Operations, MOF

The biggest decline of 0.85 percent of the GDP has occurred in income from property and enterprises. This is yet another indicator of the decline in the performance of state enterprises. Organizations like NBP, GHPL, OGDCL, PTCL, etc., have not generated profits in line with the growth in the nominal GDP. Others like WAPDA and Pakistan Railways have been unable even to honor their debt servicing obligations with the federal government.

Receipts from civil administration and other functions have been the largest source of non-tax revenues. They have fluctuated in line with the variation in SBP profits and in receipts from the CSF. Miscellaneous receipts have fallen by 0.50 percent of the GDP as royalties/surcharges on oil and gas are mostly specific in character and have not been adjusted in line with inflation. The federal government has had little

incentive to develop this source in view of the fact that most of the revenues are reverted to the provincial governments as straight transfers.

Clearly, more emphasis will have to be laid on the revival of non-tax revenues in the Budget of 2013-14 by implementing some or all of the following measures:

- (i) Replacement of government nominees in the Board of Directors of the PSEs by sector professionals, financial experts and persons of proven integrity and management experience. Profitability targets may be set by these BODs on the basis primarily of enhancement of efficiency in operations, such that dividend pay outs increase.
- (ii) Ensure that revenues of upto Rs 79 billion are realized finally by PTA by the auctioning of 3-G Licences.
- (iii) Ensure that the disbursement of the CSF funds due takes place in 2013-14.
- (iv) Index charges on services like issue of passports to inflation.
- (v) Raise rents on government land leased out.
- (vi) Introduce a levy, similar to the levy on LPG, on consumption of CNG.
- (vii) Increase regulatory fees on insurance companies.

4. NET REVENUE RECEIPTS

As shown in Table 4, the share of transfers to the Provincial Governments has increased sharply after 2009-10, following the 7th NFC Award. These transfers are of two types, viz, transfers from the divisible pool and straight transfers respectively. The former are based on a share determined by NFC, while the divisible pool consists mostly of FBR taxes.

Table 7 presents the evolution of net revenue receipts of the federal government from 2006-07 onwards. These have declined from 9.6 percent to 6.7 percent of the GDP in 2012-13. It is estimated that 80 percent of this fall is due to lower gross revenue receipts as percentage of the GDP. The remaining 20 percent is due to the increase in transfers to the provinces.

It has sometimes been argued that the 7th NFC Award is one of the major reasons for deterioration in the state of federal finances and a corresponding improvement in provincial finances. It has undoubtedly contributed to greater fiscal decentralization

in the country. Perhaps the problem is more due to the failure to faithfully implement the provisions of the 18th Amendment on devolution of functions. The federal government has accepted the responsibility to continue funding a number of devolved functions including higher education, vertical programs, etc.

	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13 (Projected)
Gross Revenue Receipts	14.22	13.67	13.67	13.33	11.89	11.74	11.90
Less Transfers to Provinces	-4.61	-4.46	-4.57	-3.76	-5.54	-5.28	-5.20
Net Revenue Receipts	9.61	9.21	9.10	9.57	6.35	6.46	6.70

Source: Fiscal Operations, MOF

The 8th NFC is likely to be constituted in 2014-15, the last year of the present award. Any downward adjustment in transfers is precluded by the Article 160(3A) of the Constitution as follows:

“The share of the Provinces in each award of the National Finance Commission shall not be less than the share given to the Provinces in the previous Award”

Therefore, discussions in the 8th NFC will need to primarily focus on the appropriate sharing of expenditure.

5. CURRENT EXPENDITURE

As highlighted earlier, one of the principal reasons for the malaise in federal finances is the explosive growth in current expenditure, especially after 2010-11.

The increase in current expenditure between 2006-07 and 2012-13 is estimated at almost 2 percent of the GDP as shown in Table 8. The big jump is in the subsidy bill, especially to the power sector, of 2.80 percent of the GDP. Interest payments and grants have been, more or less constant in relation to the GDP while defence expenditure has declined by about 0.5 percent of the GDP.

Table 8
Trend in Components of Current Expenditure

	(% of GDP)						
	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
Interest Payments	4.25	4.78	5.01	4.34	3.87	4.30	4.39
Defence	2.88	2.78	2.59	2.53	2.50	2.46	2.43
Grants	1.29	1.17	1.22	2.24	1.58	1.35	1.31
Subsidies	0.97	1.49	1.09	1.57	2.20	2.95	3.77
Others	2.17	3.97	2.16	1.74	1.72	1.53	1.70
TOTAL	11.56	14.19	12.07	12.43	11.87	12.58	13.60

Source: Fiscal Operations, MOF

The outlook for 2013-14 depends on actions on the following fronts:

Interest Payments: In 2012-13, the fiscal deficit is expected to be virtually financed completely by domestic borrowing in the absence of net inflows of external assistance. The former are relatively high cost borrowing in terms of the rate of interest, which is estimated at 10 percent in 2011-12.

Therefore, if the present pattern of financing continues in 2013-14, then the level of interest payments may rise from Rs 1040 billion in 2012-13 to over Rs 1200 billion, an increase of almost 15 percent. This rapid increase implies, as highlighted earlier, that today Pakistan finds itself in the domestic debt trap.

It has been argued that interest costs have been held down by the high share of incremental debt in the form of short-term borrowing, with lower interest rates. But while this is the optimal policy in period of falling interest rates it may imply higher costs when interest rates are rising. If, for example, interest rates rise in 2013-14 by one percentage point then this could add over Rs 50 billion to the debt servicing bill.

Subsidies: The largest component of subsidies, almost 80 percent, is the Tariff Differential Subsidy (TDS) to the distribution companies in the power sector. The budgeted allocation on this head has been consistently exceeded by a wide margin in recent years. For example, it was expected that the TDS would be restricted Rs 185 billion in 2012-13 but the year is likely to end with the figure at over Rs 400 billion.

The TDS per kwh is the difference between cost (as determined by NEPRA) and the average tariff. Estimates are that in the presence of rising costs and lack of any upward adjustment in tariffs upto now in 2012-13, the TDS per kwh now exceeds

Rs 5. This implies that if business continues as usual then the total TDS will approach Rs 500 billion in 2013-14.

The challenge for the newly elected government is to proceed on a priority basis to implement measures to contain the TDS to, say, to about Rs 300 billion, if there is to be any success in reducing the overall fiscal deficit in 2013-14.

A feasible plan that could be implemented is as follows:

	Reduction in Subsidy (Rs in Billion)
• 10 percent increase in power tariffs	47
• 20 percent increase in gas supplies to the power sector	39
• 20 percent reduction in transmission and distribution losses	34
• 10 percent higher rate of recovery of bills	61
• 25 percent recovery of arrears each year	25
TOTAL	206

Grants: The provision for grants in 2012-13 is Rs 312 billion. This includes Rs 56 billion to the Provincial Governments and Rs 256 billion to others. The latter consist of grants of Rs 31 billion to Pakistan Railways, 11 billion to the AJK government and Rs 17 billion to the government of Gilgit-Baltistan. In addition, there is a provision of Rs 150 billion for contingent liabilities and Rs 35 billion for miscellaneous grants. Presumably these provisions mostly cover the cost of subsidy on imported fertilizer, commodity operations and potentially even higher power subsidy. In 2013-14, efforts will have to be made to reduce contingent liabilities.

Costs of Civil Administration: The costs of civil administration have also risen rapidly due to frequent and large hikes in pay and allowances. The PPP government has been prone to give big annual increases, of 15 percent in 2009-10; 50 percent in 2010-11; 15 percent in 2011-12 and 20 percent in 2012-13. On top of this, a few days prior to the exit of the PPP government, the Prime Minister announced a special allowance at 20 percent of basic pay with effect from 1st of March 2013 to all the officers and staff working in the Federal Ministries/Divisions only.

The rise in costs of pay, allowances and pensions of federal employees is given in Table 9. These have risen by almost 21 percent per annum, over 10 percent above

the annual rate of inflation. As such, federal employees have seen substantial increases in their real incomes during the tenure of the previous government.

	Budget Estimates				
	2009-10	2010-11	2011-12	2012-13	ACGR (%)
Employees Pay and Allowances	92.7	113.9	123.0	155.0	18.7
Pay	43.4	47.7	44.0	69.7	17.1
Allowances	49.2	66.2	79.0	85.3	20.1
Employees Retirement Benefits	76.3	98.6	104.2	144.1	23.6
TOTAL	169.0	212.5	227.6	299.1	20.8

Source: Fiscal Operations, MOF

This generosity will have to be more restricted in coming years. Already, the Federal Budget of 2013-14 will have to factor in the full year cost of the 20 percent special allowance. Future increases may at best be indexed to the rate of inflation. Salary increases have a disproportionate impact (almost three times) on provincial governments.

6. DEVELOPMENT EXPENDITURE

One of the unfortunate developments is the ‘*crowding out*’ of development expenditure, primarily on the PSDP, due to the phenomenal increase in current expenditure, especially after 2009-10.

The trend in development expenditure is given in Table 10. The size of the federal PSDP will fall by 1.4 percent of the GDP from 2006-07 to the projected level of 1.9 percent of the GDP in 2012-13. This is an extremely inadequate level of outlay on development projects, at a time when critical bottlenecks have emerged in infrastructure, especially of power and water.

	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
PSDP	2.90	2.74	1.68	2.92	1.29	1.52	1.50
Net Lending	-0.43	-0.13	0.34	0.29	0.13	0.11	0.34
Other	0.00	0.00	0.40	0.65	0.25	0.32	0.36
TOTAL	2.47	2.61	2.42	3.86	1.66	1.95	2.30

Source: Fiscal Operations, MOF

A new category of expenditure, called '*other development expenditure*' was added to the budget in 2008-09. This primarily includes the allocation for the Benazir Income Support Program (BISP), subsidy on fertilizer import, transfer to export investment development fund, etc. the allocation for BISP is probably more legitimately a current expenditure and should be included under the head of 'social protection'. This would imply that the revenue deficit is actually somewhat higher.

The low level of allocation in the budget for the PSDP has not been accompanied by efforts at rationalizing the portfolio of on-going projects and formulating clear priorities for funding. Currently, the '*throw forward*' (cost to be incurred yet on on-going projects) is close to Rs 2500 billion, equivalent to over seven times the present size of the PSDP.

With regard to the power sector, the total allocation for projects is Rs 145 billion, equivalent to 40 percent of the planned size of the PSDP in 2012-13. The throw forward of power projects (excluding Daimer-Basha dam) is Rs 473 billion. As such, the on-going projects will take on average three years to execute. The process of implementation of power projects needs to be expedited.

The recommendations on the development side for the budget of 2013-14 are as follows:

- (i) The size of the PSDP may be set at Rs 450 billion, as proposed in the Budget Strategy Paper of the MOF. This will imply a growth rate of 25 percent and a rise in the level of PSDP to 1.7 percent of the GDP. By 2015-16, this should be raised to 3 percent of the GDP. This increase will promote the process of revival of the economy.
- (ii) The share of the PSDP allocated to projects in the power sector must be increased to 60 percent. This will raise the outlay by over 86 percent in 2013-14 and enable completion of bulk of the on-going projects within two years.
- (iii) The BISP may be continued with changes, following an independent third party audit. The Peoples Works Program may be converted into a Rural Employment Guarantee Scheme, especially for youth in backward districts.

7. FINANCING OF THE FISCAL DEFICIT

Financing of the fiscal deficit has become a really daunting task in the face of the massive increase in the absolute size of the deficit from Rs 414 billion in 2006-07 to the projected level of Rs 1786 billion in 2012-13, an increase of 331 percent!

The consequential impact of these deficits on the level of outstanding government debt is given in Table 11. Domestic government debt is estimated to reach Rs 9815 billion by end of 2012-13. This represents an increase of Rs 6540 billion on the level at the time at the time of assumption of power by the PPP, equivalent to cumulative growth of almost 200 percent. The increase in external debt is Rs 1823 billion, equivalent to a jump of 66 percent. Therefore, the composition of outstanding debt has changed substantially, with the share of domestic debt rising from 54 percent in 2006-07 to 68 percent in 2012-13. Total outstanding debt of the government as percentage of GDP is expected to exceed the ceiling of 60 percent imposed by the FDRL Act of 2005.

	(end of year position)					
	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
Government Domestic Debt						
Stock	3275	3861	4651	6012	7638	9815
Increase		586	790	1355	1626	2177
<u>% of GDP</u>						
Government External Debt						
Stock	2762	3452	3667	3988	\$46.2 (4364)	4685
Increase		690	215	321	376	221
<u>% of GDP</u>						
Total Government Debt						
Stock	6037	7313	8318	10000	12002	14400
Increase		1276	1005	1682	2002	2398
Government Debt as % of GDP	58.93	57.48	56.19	55.45	58.11	60.84

Source: Fiscal Operations, MOF

The flow of external assistance has collapsed and there is virtually no net inflow expected in 2012-13. This has been pronounced after 2009-10, following Pakistan's withdrawal from the IMF SBA, as shown in Table 12. In 2009-10, the net inflow of external assistance was large at Rs 430 billion, which fell to Rs 162 billion in 2010-11, to Rs 89 billion in 2011-12 and expected at virtually zero in 2012-13.

	2008-89	2009-10	2010-11	2011-12	2012-13
I. EXTERNAL LOANS	347.8	450.2	254.7	180.5	n.a.
A. <u>PROJECT LOANS</u>	<u>64.1</u>	<u>90.5</u>	<u>94.0</u>	<u>165.7</u>	
Federal	41.1	77.5	76.7	127.2	
Provincial	23.0	13.0	17.3	38.6	
B. <u>PROGRAMME LOANS</u>	<u>191.3</u>	<u>172.0</u>	<u>39.0</u>	<u>4.6</u>	<u>n.a.</u>
C. <u>OTHERS*</u>	<u>92.5</u>	<u>187.7</u>	<u>121.6</u>	<u>6.2</u>	<u>n.a.</u>
II. EXTERNAL GRANTS	19.6	127.8	35.1	45.6	n.a.
Kerry Lugar	-	-	11.0	20.4	
Project Aid	8.6	15.8	11.7	18.7	
III. TOTAL	367.4	578.0	289.8	226.2	n.a.
IV. REPAYMENT	121.3	148.1	127.4	136.9	n.a.
V. NET EXTERNAL ASSISTANCE	246.1	429.9	162.4	89.3	-4.1

Source: Fiscal Operations, MOF

Within domestic debt, there have also been major changes in composition by tenure. Permanent debt is long term debt and includes PIBs, prize bonds, etc. The share of permanent debt has increased from 19 percent to 22 percent. Unfunded debt is also long term debt and consists primarily of the National Savings Schemes. It has witnessed a significant decline in share from 31 percent of 23 percent. Short term debt, referred to as floating debt, has the dominant share, which has increased from 50 percent to 54 percent.

In fact, the Government appears to be having increasing difficulty in floating long term paper. In the 11 auctions upto now in 2012-13 of PIBs, only once has there been any interest shown in 20 year bonds and in the last five actions only once has there been any purchase of 5 or 10 year bonds. This indicates high perceptions of long- term risk. Also, the yield curve has a modest slope currently, with a return of 9.25 percent on 3 year bonds going upto 11.75 percent in the case of 30 year bonds. The failure to borrow on a long term basis also indicates that investors probably expect interest rates in Pakistan to rise on a secular basis.

Bulk of the financing at the margin has been through the flotation of MTBs, with maturity period of upto 12 months. Commercial banks have been encouraged to buy MTBs by large OMO injections by the Central Bank, which currently stand at Rs 2.6 trillion on a weekly basis.

The bottom line is that the access to borrowing from banks and the capital market is reaching limits. This reflects a growing loss of confidence in Federal operations. Simultaneously, external agencies are also shy of extending soft credits and loans to Pakistan. This has dangerous implications. First, it means that there will continue to be strong upward pressure on interest rates. Second, the Government may be compelled to print more money through SBP, thereby exacerbating inflationary pressures.

8. PROSPECTS FOR 2013-14

The following are proposed measures and assumptions made to develop the scenario for 2013-14:

- (i) Increase in tax revenues of Rs 400 billion or 20 percent, with taxation proposals of Rs 184 billion. Targeting an increase beyond this would be counterproductive as it could stifle the process of growth in the economy.
- (ii) Finally auction of 3-G licences by PTA fetching about Rs 79 billion.
- (iii) Receipts of CSF funds at the same level as 2012-13.
- (iv) Increase in interest payments of Rs 200 billion.
- (v) Reduction in subsidies, especially to the power sector by Rs 200 billion.
- (vi) Increase in the federal PSDP to Rs 450 billion.
- (vii) Other expenditure on the development account held constant, including the allocation to BISP.
- (viii) Reduction in costs of civil administration by Rs 30 billion in line with the proposed drive for austerity.

As shown in Table 13, based on the above, the federal fiscal deficit on a cash basis can potentially be brought down from 7.6 percent to 6.2 percent of the GDP. Of course, if any of the assumptions does not materialize then the deficit could be higher.

The consolidated fiscal deficit can be targeted at 6 percent of the GDP on the assumption that the four provinces combined will generate a cash surplus of 0.2 percent of the GDP.

Table 13
Feasible Scenario for the Budget of 2013-14
(Change from 2012-13)

	<i>(Rs in Billion)</i>
<u>Gross Revenue Receipts</u>	<u>500</u>
Tax Revenues	400
Non-Tax Revenues	100
<u>Less Transfers to Provinces</u>	<u>-200</u>
<u>Net Revenue Receipts</u>	<u>300</u>
<u>Total Expenditure</u>	<u>130</u>
<u>Current Expenditure</u>	<u>40</u>
Interest Payments	200
Defence	50
Grants	20
Subsidies	-200
<u>Development Expenditure</u>	<u>90</u>
<u>Fiscal Deficit</u>	<u>-170</u>
<u>Level of Fiscal Deficit</u>	<u>1630</u>
GDP	26504
Fiscal Deficit as % of GDP	6.2

Source: Fiscal Operations, MOF

9. SUMMARY OF RECOMMENDATIONS

The measures which have been identified above that can potentially be included in the Federal Budget of 2013-14 are as follows:

Tax Reforms

- (i) Effective agricultural income taxation
- (ii) Taxation of assets
- (iii) Minimum tax on turnover of companies
- (iv) Withdrawal of tax expenditures
- (v) Rationalization of tax rates
- (vi) Moving from schedular to comprehensive income taxation
- (vii) Development of property tax
- (viii) Incentives for filing returns
- (ix) Introduction of broad-based integrated VAT
- (x) Rationalization of customs duties

Tax Administration

Radical changes are required to make FBR more effective in implementing reforms in tax policy and collecting more revenues. The following measures are needed to be undertaken on a priority basis:

- a) Conversion of FBR into an autonomous Revenue Authority
- b) Strengthening of the Revenue Division in the federal Ministry of Finance for formulation of tax policy
- c) Filing of asset declaration periodically by tax officials
- d) Strengthening the tax Ombudsman and vesting him/her with judicial powers
- e) Internal strengthening of FBR in the areas of audit and intelligence
- f) Development of a Data Warehouse, linked particularly to withholding tax payments
- g) Streamlining the process of payment of refunds
- h) Augmenting the quality of human resources
- i) Publishing a Tax Directory annually of payments by tax payers.

Non-Tax Revenues

- (i) Replacement of government nominees in the Board of Directors of the PSEs by sector professionals, financial experts and persons of proven integrity and management experience. Profitability targets may be set by the BODs on the basis primarily of enhancement of efficiency in operations, such that dividend pay outs increase.
- (ii) Ensure that revenues of upto Rs 79 billion are realized finally by PTA by the auctioning of 3-G Licences.
- (iii) Ensure that the disbursement of the CSF funds due takes place in 2013-14.
- (iv) Index charges to inflation on services like issue of passports.
- (v) Raise rents on government land leased out.
- (vi) Introduce a levy, similar to the levy on LPG, on consumption of CNG.
- (vii) Increase regulatory fees on insurance companies.

Subsidies

A feasible plan for reducing power sector subsidies by over Rs 200 billion includes the following:

	Reduction in Subsidy (Rs in Billion)
• 10 percent increase in power tariffs	47
• 20 percent increase in gas supplies to the power sector	39
• 20 percent reduction in transmission and distribution losses	34
• 10 percent higher rate of recovery of bills	61
• 25 percent recovery of arrears each year	25
TOTAL	206

Development Expenditure

- (i) The size of the PSDP may be set at Rs 450 billion, as proposed in the Budget Strategy Paper of the MOF. This will imply a growth rate of 25 percent and a rise in the level of PSDP to 1.7 percent of the GDP. By 2015-16, this should be raised to 3 percent of the GDP. This increase will promote the process of revival of the economy.
- (ii) The share of the PSDP allocated to projects in the power sector must be increased to 60 percent. This will raise the outlay by over 86 percent in 2013-14 and enable completion of bulk of the on-going projects within two years.
- (iii) The BISP may be continued with changes, following an independent Third Party audit. The Peoples Works Program may be converted into a Rural Employment Guarantee Scheme, especially for youth in backward districts.

The Budget of 2013 is of great importance. It will be the first budget of the newly elected government of PML(N). If the budget pushes for tax reforms and proposes strong measures for containment of expenditure, leading to a sizeable fall in the fiscal deficit, then this will reassure markets and enhance confidence of the private sector in the economy. As opposed to this, if the new Government opts for a relatively soft budget, with stimulatory policies for reviving the economy without proper macroeconomic stabilization, then this may precipitate a financial crisis down the road.

APPENDIX I
STATISTICS ON THE FEDERAL BUDGET
2006-07 TO 2012-13 (July – March)

Rs in Billion)

GDP (mp)	8673	10242	12723	14804	18033	20654	
	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13 (July-March)
A. Gross Federal Receipts	<u>1233.9</u>	<u>1400.5</u>	<u>1739.5</u>	<u>1974.4</u>	<u>2144.5</u>	<u>2424.2</u>	<u>1977.8</u>
Tax Revenues	<u>852.9</u>	<u>1009.9</u>	<u>1158.6</u>	<u>1418.0</u>	<u>1634.8</u>	<u>1945.7</u>	<u>1418.3</u>
Direct Taxes	334.2	387.9	440.3	528.6	594.7	731.9	491.3
Indirect Taxes	518.7	622.0	718.3	889.4	1040.1	1213.8	927.0
Non-Tax Revenues	<u>381.0</u>	<u>390.6</u>	<u>580.9</u>	<u>556.5</u>	<u>509.7</u>	<u>478.5</u>	<u>559.5</u>
Less Provincial Share	-400.1	457.4	-525.6	-633.4	-999.3	-1089.9	-893.2
Net Federal Receipts	<u>833.8</u>	<u>943.1</u>	<u>1213.8</u>	<u>1341.0</u>	<u>1145.2</u>	<u>1334.3</u>	<u>1084.6</u>
B. Total Expenditure	<u>1248.0</u>	<u>1728.6</u>	<u>1857.6</u>	<u>282.0</u>	<u>2473.4</u>	<u>3003.0</u>	<u>2234.3</u>
Current Expenditure	<u>1002.6</u>	<u>1453.5</u>	<u>1536.4</u>	<u>1840.7</u>	<u>2141.5</u>	<u>2600.3</u>	<u>1935.5</u>
Interest Payments	368.8	489.7	6378	642.3	698.1	889.0	772.2
Defence	249.9	285.1	329.9	375.0	450.6	507.2	405.8
Grants	111.5	120.3	154.9	332.4	285.5	278.9	188.6
Subsidies*	84.3	152.3	138.7	232.9	397.1	609.6 ^b	323.0
Others	188.1	406.1 ^a	275.1	258.1	310.2	315.6	245.9
Development Expenditure and Net Lending	<u>213.6</u>	<u>267.3</u>	<u>308.3</u>	<u>432.4</u>	<u>300.1</u>	<u>402.7</u>	<u>251.3</u>
PSDP	251.1	280.5	213.2	293.9	232.7	313.3	203.8
Other	0.0	0.0	51.3	95.5	44.6	67.1	37.3
Net Lending	-37.5	-13.2	43.8	43.0	22.9	22.3	10.3
Others	<u>31.8</u>	<u>7.8</u>	<u>12.8</u>	<u>8.9</u>	<u>31.8</u>	-	<u>47.5</u>
C. Fiscal Deficit	<u>-414.0</u>	<u>-785.5</u>	<u>-643.7</u>	<u>941.0</u>	<u>-1328.2</u>	<u>-1668.7</u>	<u>1149.7</u>
D. Financing							
External	<u>199.6</u>	<u>151.3</u>	<u>149.7</u>	<u>188.9</u>	<u>107.7</u>	<u>128.6</u>	<u>-4.1</u>
Internal	<u>214.4</u>	<u>634.2</u>	<u>494.0</u>	<u>752.1</u>	<u>1220.6</u>	<u>1540.1</u>	<u>1153.8</u>
Bank	n.a.	528.3	260.2	313.8	747.7	1012.5	958.0
Non-Bank	n.a.	105.9	233.8	438.3	472.9	527.6	194.8
Memo Item:							
FBR Tax Collection	846.5	1007.2	1157.0	1327.4	1550.2	1906.5	1335.2
PSDP	251.1	280.5	213.2	293.9	232.7	313.3	203.8
Other	0.0	0.0	51.3	95.5	44.6	67.1	37.3
Net Lending	-37.5	-13.2	43.8	43.0	22.9	22.3	10.3
Others	<u>31.8</u>	<u>7.8</u>	<u>12.8</u>	<u>8.9</u>	<u>31.8</u>	-	<u>47.5</u>

Source: Fiscal Operations, MOF

APPENDIX II

TAXATION PROPOSALS IN BUDGETS

2009-10

- Exemption limit for personal income tax raised from Rs 180,000 to Rs 200,000
- Levy of Petroleum Levy (a carbon tax)
- Enhancement in excise duty on cigarettes
- FED in VAT mode levied on banking services, import cargo handlers, stock brokers, insurance companies and advertisements
- Withholding tax on importers raised from 2 percent to 4 percent
- Increase in rate on CVT from 2 percent to 4 percent
- As a way of financing relief for IDPs, levy for one year at 5 percent on every individual earning more than Rs 1 million and 30 percent on corporate bonuses
- Levy of a Minimum Tax on companies

2010-11

- Reduction in customs duty on import of crude palm oil from Rs 9000 to Rs 8000 per ton
- GST rate raised from 15 percent to 16 percent and exemption limit of turnover raised from 5 Million to 7.5 million Rs
- Elimination of 1 percent special excise duty
- Increase in FED on gas
- Levy of 10 percent excise duty on air conditioners and deep freezers
- Exemption limit in income tax raised from Rs 200,000 to Rs 300,000
- Reduction of withholding tax on electricity from 10 percent to 5 percent
- 10 percent tax credit for BMR
- 5 percent tax credit for stock market enlistment of companies
- Tax rate on AOPs raised to 25 percent
- Tax on capital gains on shares at 10 percent for less than six months and 7½ percent for 6 to 12 months
- Withholding tax on commercial importers raised from 4 percent to 5 percent
- New withholding tax on bank transactions at 0.3 percent for transactions above Rs 25,000
- Withholding tax on air travel at 5 percent of value of ticket

2011-12

- Reduction in sales tax rate from 17 percent to 16 percent
- Elimination of excise duties on 15 items
- Abolition of regulatory duties
- Phasing out of FED on cement in three years
- Elimination of excise duty on beverages in two years
- Revision of excise duty on cigarettes

2012-13

- Exemption limit raised to 400,000 Rs. Reduction in slabs to five
- Tax payer Honour Card
- Minimum tax rate reduced from 1 percent to 0.5 percent
- Reduction in PIT: 5 percent to 3 percent for commercial importers; 1 percent to 0.5 percent for exporters and from 3.5 percent to 2.5 percent for supplies
- Enhancement in threshold for bank withdrawal tax from 25,000 to 50,000 Rs
- Investment allowance limit raised from 15 percent to 20 percent and maximum enhanced from Rs 500,000 to Rs 1 million
- Adjustable sales tax at 1 percent to be collected from distributors and dealers by manufacturers
- All GST rates brought down to 16 percent on all items
- Import duty on black tea reduced from 16 percent to 5 percent
- Elimination of excise duty on 10 items
- Further reduction in excise duty on cement
- FED on foreign travel removed
- The highest import tariff reduced from 35 percent to 30 percent.

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