REFORMED GENERAL SALES TAX: Myth & Reality

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Abstract
This research article aims to provide an insight to the readers regarding the prevailing issue in the country- implementation of Reformed general Sales Tax (RGST). The thrust is to answer the questions such as, what is its nature. What are its limitations? And what would be the future implications upon the country's social and economic environment after its implementation. Moreover, some suggestions are put up to the Government, which ought to be implemented for the amicable solution of the imminent problem.

A nation wide debate is going on in the country regarding the implementation of Reformed general Sales Tax (RGST). The Government of Pakistan is all set to implement 16% of it. Different forums such as media and the parliament etc are being used to build up the national consensus for its implementation. However, irrespective of the government commitment, the proposed bill for the implementation of the RGST has been facing nation wide resistance.

This article is an attempt to unveil some facts about the said tax, which to a great extant, becoming controversial with every passing day..

What is RGST?

Reformed general Sales Tax (RGST) is a value added tax (VAT) or for a man in the street it is a "consumption Tax". It is a value added tax, levied upon each stage of value addition. It is almost implemented in more than 140 countries with different names. In Germany, Dr Wilhem von Siemens recognized the problems with turnover taxes and developed

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what he referred to as the "improved turnover tax" or "the refined turnover tax".[‡]Admas discussed as value added concept in the United States in 1921.[§]

Most of the countries have been implemented VAT for the last fifty years owing to its effectiveness. It brings all the sectors of a national economy under the tax net. Hence, acts as a major source of revenues generation. The importance of VAT can be gauged from the following points.

- It brings the whole economy under tax net, leaving meager chances of tax evasion.
- By virtue of this taxation system economy is documented
- It acts as a major source of revenues for the government.
- It is, relatively, an easy and systematic means to collect tax by the government.

General Sales Tax VS VAT:

The difference between General Sales Tax (GST) and Value Added Tax (VAT) is quite clear. In GST the tax is levied on end product and final consumer pays it. However, VAT is assessed and collected on the value of goods or services that have been provided every time there is a

[‡] C.SULLIAN, THE TAX ON VALUE ADDED, COL.U. Press 1965[thereinafter Sullivan, Tax on Value Added], p.12, citing Gerhard Calm, "Methods of Financing Unemployment Compensation," Social Research, II (May, 1935), 161.

[§] Sulliavn, Tax on Value Added, supra note 14, at 41, citing Adams, "Fundamental Problems of Federal Income Taxation." Quarterly Journal of Economics, XXV (1921), 553. Adams referred to his proposal as a tax on "appropriate net income" or "modified gross income, "and recommended it to replace the direct personal income tax.

transaction. Furthermore, especial invoices are to be maintained and provided to the government.

Exemplifying VAT:

- The manufacturer pays rupees 1.10(1+1x10%) for the raw materials, and the seller of the raw materials pays the government rupees 0.10.
- The manufacturer charges the retailer rupees 1.32(1.20x10%) and pays the government rupees 0.02(0.12-0.10), leaving the same gross margin of rupees 0.20.
- The retailer charges the consumer rupees 1.65(1.50+1.50x10%) and pays the government rupees 0.03(0.15-.12), leaving the same gross margin of 0.30.

Through VAT, the consumer has paid and the government received the same as with sales tax.

The value added has been criticized by some of its critics as according to their view point the burden of tax lies on the shoulders of the poor consumers. It also considered, by some critics, as a regressive tax as poor pay more in percentage than rich. Furthermore, it has severe implications as far as inflation is concerned. Irrespective of the critics' opinions regarding VAT, however, it is in fact the secret of the thriving economies of the West and industrialized countries.

RGST & PAKISTAN:

In 2008, owing to its financial crises, Pakistan had to knock the doors of international Monetary Fund (IMF) and the World Bank. The international lenders, keeping in view the past performance of the country and unprecedented economic development which it showed in

2000-2007, advanced $7.5 billions as a loan for five years. Latter on , the volume of the loan swelled up to $11.5 billions owing to Coalition Support Program(CSP) and Stand By Agreement(SBA). According to the contract inked between the IMF and the government of Pakistan, the IMF would transfer $1.5 billions quarterly in the country's national exchequer. In return, Pakistan pledged to take the following steps

- To increase the electricity tariffs from April 2009.
- To implement the value added tax (VAT).
- To gradually abolished the subsidies for the cash bleeding public corporations such as WAPDA, Pakistan Steel Mills, and Pakistan International Airlines etc.

Contrary to that commitment, the government failed to fulfill its pledges with IMF the World Bank and the Asian Development Bank which, resultantly, jeopardized the whole program and the fifth tranche of $1.6 billions was halted for six months. There were chances of rolling back of the IMF program and an imminent danger of bankruptcy was staring in to the eyes of Pakistan as it had not the budget for even to pay the salaries of its employees. By the efforts of the Finance Minister Abdul Hafeez Shaikh and his team, however, the matter has been apparently settled with the following main conditions.

- Reformed General Sales Tax will be implemented.
- Electricity tariffs will be gradually jacked up.

The Tax to GDP Ration in Pakistan:

Pakistan is one of the countries of the world having low percentage of tax to GDP, it ranges from 9-10%. Pakistan's tax-to-GDP ratio stands today at just above 11 per cent. It has been falling steadily from the peak of 122 per cent attained in 1995-96, with the first signs of some recovery in 1999-2000. As a whole over the ten year period, 1990-91 to 2000-02, there has little improvement in the tax-to-GDP ratio. The time path of this ratio during the 90's is an inverted U-shape, with a significant increase in the first half of the decade up to 1995-96, followed in the second half by a sharp fall[**]

S.No	Country	Tax to GDP Ratio (%)
1.	Denmark	50.0
2.	Belgium	46.8
3.	France	46.1
4.	Cuba	44.8
5..	Norway	43.6
6.	Austria	43.4
7.	Germany	40.6
8.	Iceland	40.4
9.	United kingdom	39.0
10	United states	28.2
11.	India	17.7
12.	Pakistan	10.2

Source: Heritage Foundation

The data available in the above mentioned table shows that Pakistan has a very paltry share of its tax in its GDP as compared to the other countries of the world

The General Reaction on RGST:

The reasons for the unwillingness of different factions of the society towards the implementation of RGST are as below.

[**] Why Has The Tax-To-GDP Ratio Fallen? *Policy paper no.21Hafiz A. Pasha*i*Aisha Ghauspasha andMuhammad Sabir,2001-2002 Karach,p..*

- Lack of home work done by the government prior to the implementation of RGST such as educating people about it.
- The people's inertia against the status quo.
- Unawareness of the common people masses about its procedures, benefits and its implications upon the economy.
- A misperception prevailing in general public including business community that it would exacerbate the prices of the commodities.

To answer the above mentioned questions nurturing in the minds of the people, the government should fulfill its obligations and play its legitimate role. Following are some suggestions which, if implemented, could address the existing problems.

- A team of economic and financial experts should be convened to conduct seminars regarding the effects and benefits of RGST.
- Common people should be taken into the confidence, since they are the real stake holders.
- Business community should be properly guided, educated, trained and persuaded regarding the documentation a prerequisite for RGST.

Economists Point of View:

All economists have consensuses on imposition of taxes for covering expenditure done by govt. economists believes on wider tax base so that each and every capable citizen contribute to state treasury. But differences arise on such questions like who should be taxed? How much should be the tax amount? Who should pay more and who should get relaxations and why? Again tax is not a tool of filling state treasury but actually it is a way of stabilizing economy. No doubt Pakistan is in trouble, that is, in financial crises and we all should come forward to sacrifice a proportion of our income for survival. The common people, industrialists the politician and the businessman etc all have to pay for Pakistan or at least those should now pay which are not paying. So far RGST is concerned, we economists, at least I myself, have clear cut stand. It will creates burden on common people, it is more inflationary and it discriminatory. If we need money for covering larger fiscal deficit, than there are more than dozen ways for doing this simple job. We can work effectively for bringing down large scale corruption of rupees 500 billions in CBR close to zero, we can impose wealth tax, we can cut the unproductive current expenditure especially we can reduce the size of cabinet, we can reduce the cost of legislation in both the houses, we can reduce the PM and President house expenditure by larger sum, we can impose tax on agriculture sector which has remained untaxed since 1947. If government is really interested in raising funds for covering expenditure than all these open policies are there but the fact is that govt. has compulsion by group of people which are in power and working for their own interest. This is clear bias is reflected in govt. policy. If RGST is imposed than it would be a blow to poverty and inflation shaken publics and would result in more hyper inflation and instability with high unemployment which will in turn increase crimes and thus reduce investment. It would discourage productivity and thus reduce govt. taxes and thus raise more need of more loans in future. So this would cause economic instability and public disorder. We therefore think that RGST would be a blinder at that stage of development.

Conclusion:

Pakistan is one of the few countries where tax to the GDP ratio is very meager which totals almost 9%. This is insufficient for the smooth journey of economic development. Unfortunately, the tax ratio could not be aligned, in the past years, to the economic development. Resultantly, the fourth largest economy of the Asia having 7.2 growth rate in 2007 is in shambles now. It is high time to document our economy and bring it under the tax net. However, being a democratic country the decision regarding the RGST should not be taken at the whims of an individual rather national consensus should be developed. Both, the government and the public should know its duties and responsibilities in this regard. The goal is same, to pull the national economy out of the abyss of foreign debt for this we have to rely upon our own resources and implementation of RGST is the only solution. Here it is pertinent to mention that as it is the first time nation is acquainting with a modern and systematic taxation system so the government should implement it, keeping in view, the following factors.

- Poverty level
- Purchasing power of the people.
- Consumption pattern
- Effects of "Global War on Terror" on the country's economy
- The mood and culture of the country.

The government and the people are the two important stake holders of the joint stock corporations – Pakistan. The survival of the corporation is in the interests of both of the stake holders. As some one rightly said "do not yield to misfortunes, but bear them with fortitude*."*

References

C.SULLIAN, THE TAX ON VALUE ADDED, COL.U. Press 1965[thereinafter Sullivan, Tax on Value Added], p.12, cited in Gerhard Calm, "Methods of Financing Unemployment Compensation," Social Research, II (May, 1935), 161.

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