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THE MINIBUDGET

About IPR

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A minibudget has been announced at the end of the fifth month of the current fiscal year. The objective is to cover the shortfall of Rs 40 billion in FBR revenues for the first quarter. Apparently, this is a pre-condition to be fulfilled before the release of the next IMF tranche. Is this a precursor of more mini budgets in 2015-16, like last year?

What is the strategy for raising the additional resources? It consists entirely of raising tax rates of indirect taxes, especially customs and excise duties. This is tilting the tax system even more towards indirect taxes, which already account for over two-thirds of FBR revenues.

The focus instead should have been on greater austerity in expenditure, especially in non-salary heads, and /or mobilizing additional revenues from direct taxes. In its first budget of 2103-14, the PML(N) Government had promised to make a 30% cut in non-salary expenditure, equivalent to Rs 40 billion. This was not achieved and instead there was an increase of Rs 25 billion . It is vital that at this time when the Budget of 2015-16 already contains heavy additional taxation of over Rs 200 billion that the emphasis be shifted to reducing non-development expenditure. Otherwise, the growth process in the economy will be adversely affected.

The other option is to collect more from direct taxes and ensure that the incremental tax burden is progressive. One option is to introduce a super tax on banking companies, which are currently making record profits. A one-time levy has been introduced in the latest Budget at the rate of 4% on banks' income and at 3% on affluent individuals, AOPs and companies earning more than Rs 500 million in tax year 2015. The revenues to be generated are earmarked for covering part of the costs of rehabilitation of Temporarily Displaced Persons.

The option was to raise the rate on banking companies to, say 6%, on high income tax payers to 4% and to levy 1% additional tax on tax payers with income from Rs250 million to Rs 500 million. Combined with the austerity drive, the budgetary position could have been improved by Rs 40 billion.

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Instead, what are the measures included in the mini budget? The first step is to increase the customs duty by one percentage point across the board. The second measure involves raising the regulatory duty on luxury good imports by 5 to 10 percentage points. The Government is engaged in somewhat contrary moves. While the maximum import duty has been reduced from 30% to 20%, other regulatory duties are being imposed. In addition, the excise duty is being increased on imported cars and domestically produced cigarettes.

Surely, the prerogative of raising taxes rests with the Parliament and not unilaterally with the Executive. Already, after March 2015, on IMF's insistence, all SROs, embodying exemptions or concessions, have to obtain legislative approval. The new taxation proposals should also have been placed before the National Assembly.

The concept of minimum import duty was introduced in the Budget of 2014-15. The initial rate was 1%, which was raised to 2% in the current budget. Now it has been enhanced to 3%. Almost half of imports are covered by this duty. This includes the import of basic food items like pulses, tomatoes, onions and other vegetables, which is indeed oppressive taxation on the poor. The other major source of revenue from the minimum duty is petroleum products. Following the decline in oil prices, not only have the GST rates on these products been raised substantially but also insidiously import duties have been levied. For example, inclusive of a regulatory duty, the import duty on furnace oil has been increased to 8% and on HSD oil to 11%.

The levy of additional regulatory duty on so-called `luxury items` raises the total duty to up to 35%. Most of these items are likely to be smuggled, with such high rates of duty. Some import contraction is possible, but with the prospect of hardly any additional revenues.

The excise duty on cigarettes has been subjected to frequent changes. In the Budget of 2013-14, a transition was made from a composite formula to two flat rate slabs, depending on the retail price. These rates were enhanced in 2014-15. Now they have been increased further by about 5% and 7% respectively.

The Government is pursuing a policy of punitive taxation to curb smoking in line with WHO’s requirement. However, what is happening is more tax evasion than a reduction in consumption. The reported production has declined by 4%, since June 2014.The further enhancement in tax slabs could prove to be counter-productive, unless the enforcement process is strengthened.

Overall, some of the measures are literally ‘cosmetic ‘in character. However, they are likely to be seen positively by the gullible IMF staff mission. It is hoped that the indicative target for FBR revenues of Rs 750 billion will be met in the second quarter. It will require the achievement of a high growth rate of over 18%.If there is a shortfall again; will there be another mini budget in the first quarter of 2016?

Finally, in the presence of a small fall in international oil prices, the Government has opted to keep POL prices unchanged in December, except for kerosene oil. In particular, there is need to reduce the tax component in the price of HSD oil, which is a key input into the transportation of essential goods. The HSD price in Pakistan today is the highest in South Asia. The price (in US$) is 29% higher than in India, 46% higher than in Bangladesh and 28% higher than in Sri Lanka. This has kept the price level artificially high in Pakistan and raised the cost of living, especially for the lower income groups.