



FAIR TAX MONITOR

Bangladesh

December 2015



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Fair Tax Monitor

The Fair Tax Monitor (FTM) is a unique online advocacy tool that identifies the main bottlenecks in tax systems and provides strong evidence for advocacy work. At the same time, the tool allows for a comparison of tax policies and practices in different countries, using a standardized methodology and unified approach in the research. At later stages of the project, it will also be possible to monitor countries' progress over time. At the international level, the Fair Tax Monitor contributes to global advocacy efforts by providing solid evidence and by showcasing the relative fairness of selected issues in tax systems.

Oxfam Novib and the Tax Justice Network-Africa (TJN-A) launched the Fair Tax Monitor in collaboration with partners from Bangladesh (SUPRO), Pakistan (Indus Consortium), Senegal (Forum Civil) and Uganda (SEATINI). The first step was the creation of a common research framework and an online evidence-based advocacy tool, which were subsequently tested in the selected focus countries. It is anticipated that the project will grow in terms of number of countries and in terms of the quality of the framework and methodology. The project envisions regular updating and becoming a reliable source of information and analyses related to fiscal policies and practices.

The FTM Report for Bangladesh was created using the common research framework jointly developed by Oxfam Novib, TJN-A and the above partners. The data collected in this report provides the basis for the online advocacy tool that can be viewed at www.maketaxfair.net. This online tool provides an overview of the main issues this report addresses and compares them with the information collected in other focus countries. FTM's Composite Report 2015 summarizes the findings from Bangladesh, Pakistan, Senegal and Uganda and includes additional explanations of the online tool. It is available at the website stated above.

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List of acronyms

ACC	: Anti-Corruption Commission
BCS	: Bangladesh Civil Service
BDT	: Bangladeshi Taka
BFIU	: Bangladesh Financial Intelligence Unit
BIN	: Business Identification Number
CIT	: Corporate Income Taxes
CSO	: Civil Society Organization
CPD	: Centre for Policy Dialogue
EU	: European Union
ECF	: Extended Credit Facility
ERD	: Economic Relations Division
FY	: Fiscal Year
FD	: Finance Division
GDP	: Gross Domestic Products
IBFB	: International Business Forum of Bangladesh
IMF	: International Monetary Fund
IFC	: International Finance Corporation
IFS	: Illicit financial flows
IRD	: Internal Resources Division
MoF	: Ministry of Finance
MPO	: Monthly Pay Orders
NBR	: National Board of Revenue
NGO	: Non Government Organization
OOP	: Out-Of-Pocket
OECD	: Organization for Economic Co-operation and Development
PIT	: Personal Income Tax
PRI	: Policy Research Institute
RMG	: Ready-Made Garments
SD	: Supplementary Duty
SRO	: Statutory Rules and Order
SAARC	: South Asian Association for Regional Cooperation
SMEs	: Small and Medium-sized Enterprises
SoEs	: State-Owned Enterprises
SUPRO	: Shushashoner Jonny Procharavizan (Campaign for Good Governance)
THE	: Total Health Expenditure
TT	: Turnover Tax
TIN	: Tax Identification Number
TV	: Television Channel
TDS	: Tax Deduction at Source
TK	: Taka
USD	: United States Dollar
VAT	: Value-Added-Tax
WDI	: World Development Indicator
WCO	: World Customs Organization

Executive summary

Bangladesh, as a developing country, is committed to increasing tax revenues and achieving fiscal discipline with a view to increasing self-reliance. The external environment influencing the tax performance of Bangladesh has changed remarkably as the country more and more integrated with the global economy during the 1990s. In recent years, the Government of Bangladesh has initiated some administrative and policy reforms in the tax system. An improved tax administration in association with some pragmatic policy initiatives has of late resulted in a modest improvement in the tax to GDP ratio. However, the performance is still unsatisfactory as compared to other countries at a similar stage of economic development.

The narrow tax base, widespread exemptions, and administrative inefficiencies are the main factors behind the low tax to GDP ratio in Bangladesh compared to the neighbouring or comparative countries. This also implies why tax reforms over the last decades have not brought about significant changes in Bangladesh's tax efficiency and productivity. The most basic challenge has been the overall weakness of the policy framework, which is characterized by an enormous range of exemptions, incentives and special regimes. These range from simplified regimes associated with VAT to significant scope within the law for tax officials and political elites to grant discretionary benefits. This directly undermines revenue collection, but equally complicates administration, undermines equity in the system and introduces significant scope for officials to exercise discretion in both policy and administration.

Hence, attaining an optimal income tax system becomes critical for revenue generation, required for accelerating growth and improving the quality of life of citizens. A long-term sustainable solution to enhance transparency, promote growth, improve tax compliance and thus to increase tax to GDP ratio is a much desirable issue in the context of Bangladesh.

With an aspiration to make Bangladesh's tax system fair, equitable, transparent and compliant with people's aspirations, this study was undertaken to understand the country's overall tax system, its loopholes and potential, so that the advocacy agendas are drawn up on solid research-based knowledge.

Through employing an exploratory study methodology based on secondary data and archival resources, the study generates information on seven broader areas: (1) description of the tax system, (2) distribution of the tax burden and progressivity, (3) revenue sufficiency and tax leakages, (4) tax exemptions, (5) effectiveness of the tax administration, (6) government spending, and (7) transparency and accountability. These clusters of topics were selected to best capture the complex character of tax systems in order to evaluate a tax system's fairness.

This study marks the significance of making the tax system more progressive by establishing a well functioning governance mechanism, enhancing stakeholders' participation, raising transparency and ensuring that everyone pays their share of taxes.

The findings and policy recommendations presented in this study are important for a better design and execution of future tax reforms and for making Bangladesh's tax structure more equitable.

Study Background and Rationale

Bangladesh is increasingly focussing on internal resources mobilization in order to enhance socio-economic development and to cover budgetary expenditures. Like many other developing countries, Bangladesh struggles to meet its potential in mobilizing domestic resources, due to poor tax administration, outdated tax and fiscal policies and weak tax collection practices. Therefore, from the perspective of a campaigning and advocacy organization, our strategy is to mobilize grassroots activism in order to raise the collective voice and influence policy-makers and duty-bearers to introduce a fair taxation system that prevents tax evasion and reduces tax avoidance at the individual and corporate levels (including national and multinational companies).

SUPRO, a rights-based campaign and advocacy organization, proposes the following measures to reduce income inequalities the current system causes. People with the ability to pay tax should not be left out of the tax net, loopholes in tax system should be closed and revenue collected by the government of Bangladesh should be spent in an equitable and transparent way. SUPRO also wants to bridge peoples' concerns, reactions and opinions on tax reform, tax administration and the tax collection process. SUPRO believes that once tax justice is secured government revenue will increase. That will lead to an increased allocation of resources to essential services for the benefit of poor and marginalized people, which will ultimately contribute to reduced income inequality.

Hence, for undertaking an evidence-based advocacy on tax issues it is crucial to understand the overall tax system, its loopholes and potential. This is also important in order to convince the authorities and mobilize people. This study generates crucial knowledge for understanding tax issues and will eventually contribute to identifying campaign and advocacy agendas with solid arguments for tax justice.

Study Goals and Objectives

The broader strategic goal of this study is to contribute to a better understanding of, and insight in tax issues in Bangladesh, providing a firm basis for both civic education and advocacy campaigns to promote a fairer tax system. Aligning with the broader aspiration, the study defines its very specific and target oriented objectives e.g.:

- To identify main bottlenecks in the tax systems of focus countries.
- To provide strong evidence-based support for country-level advocacy work.
- To create a framework for comparing the tax systems of selected countries over time.
- To contribute to global-level advocacy on taxation through an evidence-based tool showcasing the relative fairness of selected tax systems.

Study Methodology

The study mainly uses exploratory methods. Information is acquired by researching secondary data and archival resources and by using rapid assessment techniques such as key informant interviews

Initially, the study's scope and methodology were presented at an experts' and stakeholders' meeting and their feedback and recommendations were incorporated and applied in the process of

implementing the study. A limited number of persons were interviewed for their expertise, experience and perceptions on the country's tax system, tax administration and on overall revenue structure.

Study Framework

The study framework is divided into 7 clusters of topics: description of the tax system, distribution of the tax burden and progressivity, revenue sufficiency, tax exemptions, effectiveness of the tax administration, government spending, and transparency and accountability. These clusters were selected to best capture the complex character of tax systems in order to a tax system's fairness.

CHAPTER 1

Tax System in Bangladesh: An overview

This part provides a comprehensive overview of the structure of the tax system, the authorities responsible for collecting taxes and the overall approach to tax administration. It also determines the impact of the changes that were made to the tax system in recent years and whether the country has been moving towards a fairer tax system or away from one.

1.1 Evolution of Tax System: A Historical Perspective

The term 'tax' has been derived from the French word '*taxe*' which means 'to charge'. Review of different literature suggests that 'tax' was introduced to generate public and state revenues to cope with the situation after major crises like famine, devastation of war etc. Likewise, in the Indian Sub-Continent 'tax' was introduced to raise additional finances in order to replenish the revenue deficit caused by the Sepoy Mutiny of 1857 (K I Interview)¹. Following the Mutiny, the British government took over the rule of India from the East India Company, which was in a bad financial state. To find a way-out, the government appointed a Finance Member in India, named Mr. James Wilson, who introduced a bill to the Indian Legislature entitled "An Act for Imposing Duties on Profits arising from Property, Professions, Trades and Offices" in 1860.

However, the Act did not work well in 1865 and was reintroduced in 1867 as certificate tax, which in turn was converted into regular income tax in 1869. Though the changes over the years improved the tax system in form and coverage, the income tax was altogether abolished in 1873-74 when there was a comfortable budgetary surplus (Bala Swapan Kumar 2009)². However, in 1879-80 taxes were raised in the form of license taxes and continued until 1885-86. Meantime, in 1886 the Indian government adopted the Indian Income Tax Act, which was again amended substantially in 1916 and consolidated in the income tax law of 1916. In 1922 the All-India Income Tax Committee was appointed. It recommended a broad-based 'Income Tax Act' and necessary institutional arrangement for tax collection. Based on the recommendations the Indian government adopted the 'Income Tax Act 1922 (Act XI of 1922) and established the Inland Revenue Board as the highest authority for income tax. The very 'Act' tried to address few fundamental issues and peoples' concern, such as the basis for assessing income, profits and gains, the taxpayer's choice, etc., but still it was a continuation of the reactive and centralized tax system of the British ruler and people's views and concerns were not reflected in a structured manner.

¹ Dr Muhammed Abdul Mazid former Secretary to the Government of Bangladesh and former Chairman, NBR, interviewed on 17.08.2015

² Bala Swapan Kumar, Complexities in the Income Tax Laws: A Quest for a Simpler Taxation System, International Business Forum of Bangladesh (IBFB), December 2009

Bangladesh, as a part of Indian Sub-Continent, inherited the British-Indian tax system, in use until well after its liberation from Pakistan in 1971. However, during the Pakistani regime from 1947 to 1970, there was a significant change in Bengal's land ownership: the abolition of the Permanent Land Revenue Settlement. The Settlement Regime, introduced by the English Lord Cornwallis in 1793, made the Zamindars hereditary owners of the land in their possession and gave them total control over lands, whereby the survival of cultivator (also called *Rayot*) would depend on the mercy of the Zamindars. The Zamindars were inducted into the colonial state system; they were also granted the privilege of holding property rights at a perpetually fixed rate of land revenue (Islam 2003)³.

In the context of weak Company administration of land settlement in Bengal, the Permanent Settlement was instituted, considered a better arrangement than the Company's direct involvement. However, the Zamindar system largely failed to produce any social change and to improve production and well-being of Rayots. Acting as Calcutta-based absentee landlords, the Zamindars, just siphoned off wealth for their luxury living. The Rayots's surpluses were continuously and systematically extracted by the Zamindars and their intermediaries in the form of different *chandras*, *nazrana*, *salami* etc. This situation resulted in the 'Peasants Uprising' against Zamindars, who demanded the abolition of permanent settlement in many different places in Bengal. This demand also got political attention when the Krishok Proja Party, led by A.K. Fazlul Haque, declared its intention to abolish permanent settlement when people voted them to power to form the Bengal Provincial government in 1937⁴. Following the election, the Krishok Proja Party became part of a Coalition government of undivided Bengal and passed the Moneylenders Act of 1940, which abolished many unjustified fees and taxes imposed by the Zamindars and also conferred the rights of occupancy to all categories of Rayots (Islam 2003).

The Coalition Government of Bengal also appointed a Land Revenue Commission in 1938 to examine the prevailing land revenue system and put forward recommendation for its modification. The commission, headed by Sir Francis Floud, recommended the abolition of the permanent settlement and direct payment of land taxes to the government. The Commission's recommendations were executed in 1950, and abolished the colonial legacy of permanent settlement.

Though the then political processes succeeded in abolishing some colonial legacy, the State government continued to follow the colonial tax system. Even after the liberation of Bangladesh, the country followed the British-Indian Income Tax Act 1922. It was only in 1984 that Bangladesh replaced the 1922 Income Tax Act by introducing the country's Income Tax Ordinance, 1984 (XXXVI of 1984) which came into force on the 1st July, 1984.

Ironically both tax systems (e.g. the Income-tax Act 1922 until 1984 and the Income Tax Ordinance 1984 from July 1984 onwards) that Bangladesh applied were developed or enacted without any consultation with its stakeholders, especially with the income tax payers. The former originated with British hegemony in the Indian Sub-Continent and the later was developed in absence of democracy in Bangladesh (KI Interview)⁵. Nevertheless, Bangladesh upholds a very democratic proposition on tax and the tax system. Article 83 of the Constitution of Bangladesh says that "no tax shall be levied or collected except by or under the authority of an Act of Parliament".

³ Islam, Sirajul: Permanent Settlement in Bangladesh; National Encyclopedia of Bangladesh, Vol 8, Edited by Sirajul Islam et al. Asiatic Society of Bangladesh, 2003

⁴ Helal Uddin Ahmed: The Permanent Settlement and its effect in Bengal, <http://www.thefinancialexpress-bd.com/2015/01/17/76206/print>

⁵ Dr Muhammed Abdul Mazid former Secretary to the Government of Bangladesh and former Chairman, NBR, interviewed on 17.08.2015

1.2 Current Revenue Regime

The current fiscal regime of Bangladesh consists of direct and indirect taxation. It is governed by the National Board of Revenue (NBR). Revenue is also generated from non-NBR sectors and under the laws and acts of related ministries. The NBR taxes include Customs Duty, Value Added Tax (VAT), Supplementary Duty (SD), Personal Income Taxes (PIT) and Corporate Income Taxes (CIT).

Personal and Corporate Income Tax, the single largest source of direct tax, is governed by the Income Tax Ordinance, 1984 (XXXVI of 1984). The income tax laws consist of the following statutes (apart from the main statute) (Bala, Swapan Kumar 2009):

- Income Tax Ordinance 1984 – the parent statute;
- Income Tax Rules 1984;
- S.R.O. (Statutory Rules and Order)/Gazette Notification;
- Income Tax Circular;
- General or Special Order;
- Explanation/Office Memorandum;
- Verdicts of Appellate Tribunal for equivalent fact;
- Verdicts of the High Court Division on question of law; and
- Verdicts of the Appellate Division on judgment of the High Court Division.

Besides fiscal income from direct sources (e.g. income tax) Bangladesh generates a substantial share of its revenue from indirect sources through import and excise duties (customs duties). Customs duties are normally payable on the following goods: a) imported and exported goods; b) goods brought from any foreign country to any customs station and without payment of duties there, transhipped or thence carried to and imported at any other customs station; and c) goods brought in from one customs station to another. The main legislation relating to customs and excise duties are:

- The Central Excises and Salt Act, 1944;
- The Central Excises and Salt Rules, 1944
- The Protective Duties Act, 1950;
- The Customs Act, 1969;
- The Customs Tariff Act, 1969/2000;

The customs duties were the biggest contributors to the tax revenue until the late 1980s. That is when their decline started, due to reduced rates and levies to comply with the demands of global and globalized trade and the fiscal policies of market liberalization, and also for shifting of economy from trading to local manufacturing. It then became necessary to think of other options for revenue generation. Given the context, in 1986 the World Bank suggested to introduce VAT in Bangladesh. With the aim of greater revenue generation for the government and stimulating economic growth, the VAT Bill 1991 was proposed in the National Parliament on 1st June 1991 and a month later the Bill was passed and made into the VAT Act 1991. The VAT Act 1991 contains over 70 laws that guide a business in VAT related issues, from registration to penalties on non-compliance. It also dictates the structure of the VAT authority and the power it may exert on businesses regarding the three taxes within the realm of the Act as the situation demands.

Other factors that influenced the introduction of VAT were the complications and inefficiency in the implementation of the Sales Tax Ordinance 1982 and Business Turnover Tax Ordinance 1982. Hence the VAT Act 1991 came into force on 1st of July 1991, replacing the Ordinances of Sales Tax and Business Turnover Tax

1.3 Major Policy Reforms and Their Impact

There have been some policy discussions about the tax law in Bangladesh, although not very effective. The income tax legislation dates to the Income Tax Ordinance 1984, and was promulgated under the military rule. According to the 1984 Ordinance there are seven forms of income on which tax is levied: salaries, interest on securities, income from house or property, agricultural income, income from business or profession, capital gains and income from other sources (*Income Tax Manual Part-1*, 2009).⁶

A number of efforts were made to strengthen the revenue mobilization and improve the tax structure. In 1991 Bangladesh embarked on a major tax reform through the introduction of the VAT system. Simultaneously there was a significant reduction of import tariffs. Prior to these reforms, trade-based taxes dominated the tax structure in Bangladesh with customs duties alone accounting for about a third of tax revenue during the first two decades of the country's independence.⁷

Following the introduction of VAT in 1991, the share of VAT revenue increased substantially to reach 29% in 2014, while the share of customs duties declined to 10.8%. Even though the base of the VAT system has been expanded, numerous distortions were also introduced for reasons of political expediency. Because of these problems, the VAT system underperformed considerably in terms of revenue generation compared with its potential. It is evident that a narrow tax-base, widespread exemptions and administrative inefficiencies are the main factors behind the low tax-to-GDP ratio in Bangladesh compared to the neighbouring countries. This also implies that the tax reforms of the last decades did not bring about significant changes in Bangladesh's tax efficiency.⁸

In recent years much simplification and rationalization has been introduced to reform the taxation system. Tax assessments were made less complicated and an attempt of attracting more taxpayers into the tax net was made. The automation of tax collection was begun, and compliance with the standards and systems introduced by WCO has increased. The practice of honouring the taxpayers and recognizing their contribution received institutional shape in the NBR. In the case of legislative reforms, the new Value Added Tax and Supplementary Duty Act of 2012 were enacted and will be effective from July 2016. A draft Direct Tax Code was posted on the government's website and steps will be taken to get it passed by Parliament by next year. There are plans for a comprehensive/maximum reduction in the rate of Import and Supplementary Duty in the budget for the 2016-17 financial year, which will eventually shift the burden of revenue collection to Individual and Corporate Tax along with Value Added Tax (VAT).⁹

⁶ Nashid Rizwana Monir, 2012, Political Economy of Corruption: The Case of Tax Evasion in Bangladesh, Monash University

⁷ Fiscal Management and Revenue Mobilization by Dr. Ahsan H. Mansur, Policy Research Institute of Bangladesh, Prepared as a background paper for the Seventh Five Year Plan

⁸ Fiscal Management and Revenue Mobilization by Dr. Ahsan H. Mansur, Policy Research Institute of Bangladesh, Prepared as a background paper for the Seventh Five Year Plan

⁹ Abul Maal Abdul Muhith, Minister, Ministry of Finance, Budget Speech 2015-16

1.4 Institutional Arrangement for Revenue Generation

Like other developing countries, Bangladesh underscores the importance of revenue generation to meet the country's revenue needs and development expenditures with a view to accomplishing some economic and social objectives, such as a redistribution of income, price stabilization and discouraging harmful consumption. However, the revenue structure in Bangladesh is complex and centralized, and involves several agencies, departments and ministries. All the generated revenues are directed into one basket i.e. Account No 1 of the Bangladesh Bank, which then distributes them through annual budgetary allocation, projects, schemes, block grants etc., as if Ma Durga (known as Devi or Shakti in Hinduism, who is believed to have 10 hands) is distributing *Bhog* among the devotees (KI Interview).¹⁰

There are two broad categories of revenue: a) tax revenue, which is again divided into NBR tax and Non-NBR tax, and b) non-tax revenue. The following figure gives an overview on the institutional arrangements and sources of revenue generation.

The NBR sources include customs duty, value added tax (VAT), supplementary duty (SD), excise duty, income tax, foreign travel tax, electricity duty, wealth tax (collected as a surcharge of income tax since fiscal year 1999-2000), turnover tax (TT), air ticket tax, advertisement tax, gift tax and miscellaneous insignificant taxes.

Other taxes, often referred as non-NBR sources, include narcotics duty (collected by the Department of Narcotics Control, Ministry of Home Affairs), land revenue (administered by the Ministry of Land and collected by local Tahsil offices), Non-judicial stamp (collected under the Ministry of Finance), Land Registration fee (collected by the Registration Directorate of the Ministry of Law, Justice and Parliamentary Affairs) and Motor vehicle tax (collected under the Ministry of Communication).

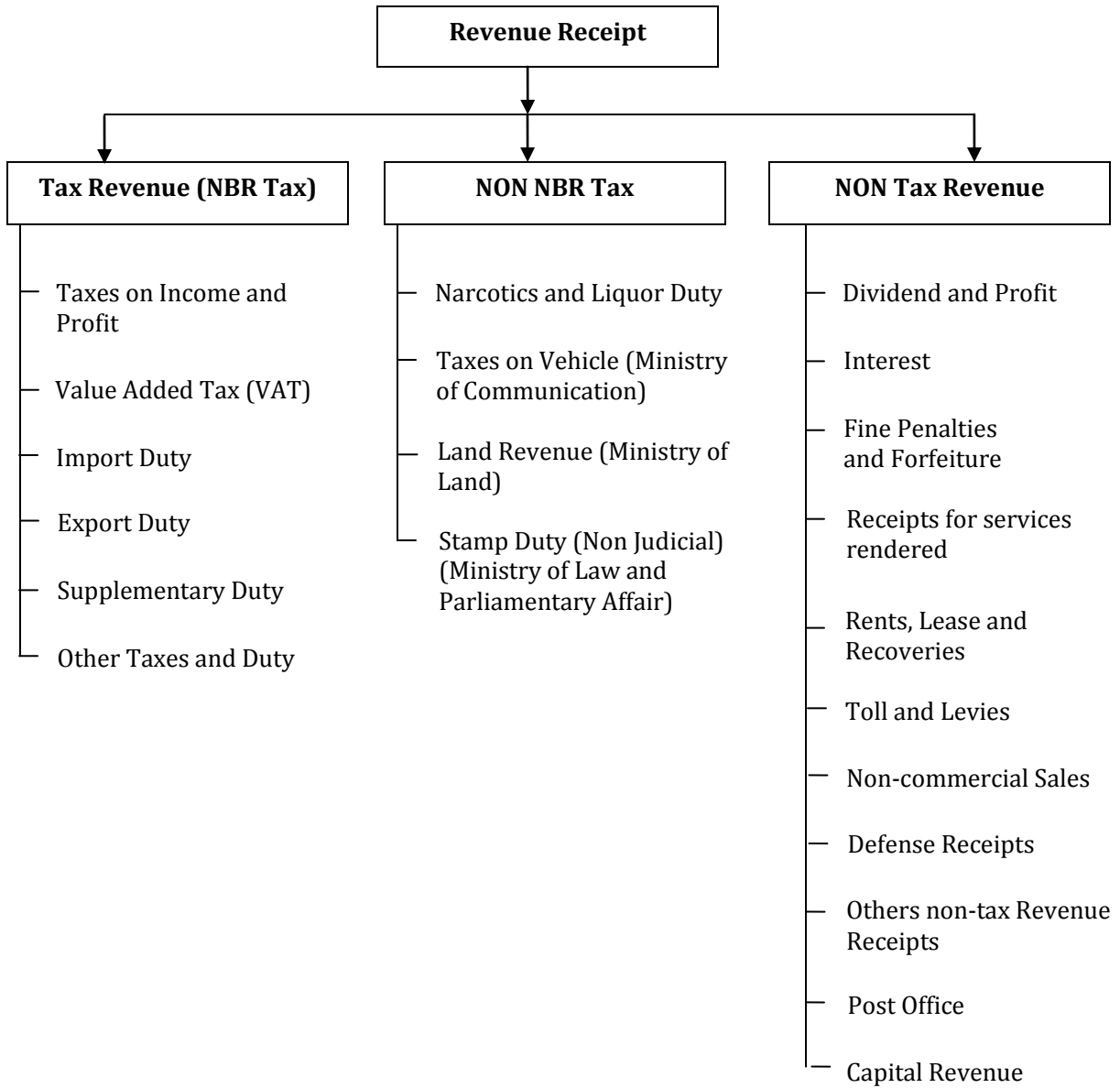
The non-tax sources include dividends and profits, interest, administrative fees, penalties and forfeitures, services, rent and leases, tolls and levies, non-commercial sales, defence, non-tax receipts, railway, post office department, T&T Board, and capital receipts, etc.

¹⁰ Towfiqul Islam Khan, Research Fellow, Center for Policy Dialogue-CPD, interviewed on 18. 08.2015

Figure 1: Institutional arrangement and details of revenue receipt in Bangladesh

Broad Details of Revenue Receipt

(Excluding Grants, Loan and Food Account Transactions)



Tax Structure in Bangladesh

Again, among the tax revenue sources VAT delivers the major portion (36.98%), followed by income tax (35.61%). Table 1 and the Figure 2 clearly show the share of tax revenue sources in FY 2013-14.

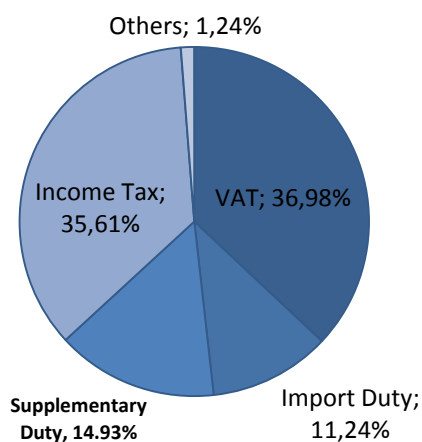
Table 1: NBR Tax Structure in Bangladesh, FY 2013-14 (in Crore Taka)

	Import Duty	VAT at Import Level	SD Import level	Export Duty	Sub total	Excise Duty	VAT Local	SD Local	Turn Over Tax Local	Sub Total
	1	2	3	4	5	6	7	8	9	10
Tax in Crore ¹¹ Taka	1,354.82	15,318.9	4,344.43	26.46	33,230.61	822.39	29,252.11	13,647.19	4.72	43,726.41
% of Total	11.24%	12.71%	3.60%	0.02%	27.57%	0.68%	24.27%	11.32%	0.004%	36.28%

	Total Indirect Tax	Income Tax	Other Taxes Duties	Total Direct Tax	Grand Total
	11	12	13	14	15
Tax in Crore Taka	76,957.02	4,2915.5	640.31	43,555.81	120,512.83
% of Total	63.86%	35.61%	0.53%	36.14%	100.0%

Source: Bangladesh Economic Review 2014-15

Figure 2: Composition of tax in FY 2013-14



Source: Bangladesh Economic Review 2014-15

¹¹ 1 crore = 10 million

CHAPTER 2

Distribution of Tax Burden and Progressivity

One of the basic concepts of designing and implementing an equitable taxation regime is 'Broad Basing', meaning that the taxes should be spread over as wide as possible a section of the population, or sectors of the economy, to minimize the individual tax burden. While indirect taxes (e.g. VAT) levied on goods or services affect the rich and the poor alike, direct taxes may create burdens on a certain income group. Indirect taxation is commonly used to generate tax revenue paid indirectly by the final consumer of goods and services. It is paid by everyone in society, regardless their financial situation. Hence, indirect taxation can be viewed as regressive as it imposes a greater burden (relative to resources) on the poor than on the rich. In contrast to direct tax, the taxpayer and the tax-bearer are not the same person. Hence, to reduce an individual's tax burden, the taxation regime should be diverse and broad-based with an equitable balance of both direct and indirect sources.

On the other hand, the term "progressive" refers to the way the tax rate progresses from low to high, with the result that an individual on average pays less than the person's marginal tax rate. This also means that people with lower income pay a lower percentage of that income in tax than those with a higher income. Unlike indirect taxes, direct taxes are linked to the taxpayer's ability to pay, and hence are considered to be progressive.¹²

In Bangladesh, direct taxes consist of taxes from income tax and other taxes. The sources of income tax can be classified in 7 categories:¹³

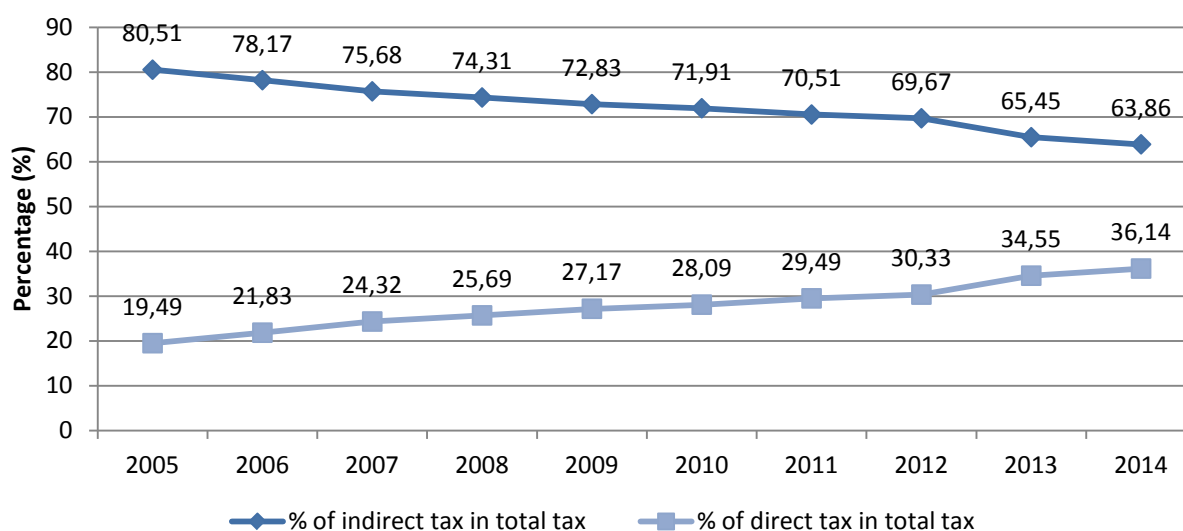
1. Salaries
2. Interest on securities
3. Income from house property
4. Income from agriculture
5. Income from business or profession
6. Capital gains
7. Income from other sources.

Indirect taxes are collected by intermediaries from the person who bears the ultimate economic burden of the tax. The intermediary later files a tax return and forwards the tax proceeds to the government with the return. The major indirect taxes in Bangladesh include: value added tax (VAT), excise duty, trade tax and turnover tax. Nevertheless, the tax structure of Bangladesh is perceived to be regressive as it is heavily dependent on indirect taxes (about 64% in 2014). The gap between direct and indirect tax has reduced since 2005 as the share of direct tax has increased (Figure 3).

¹² Prashant Prakash, Property Taxes Across G20 Countries: Can India Get it Right? 2013, CBGA and OXFAM India

¹³ NBR, Income Tax at A Glance, <http://www.nbr.gov.bd/Publications.php?lan=eng>

Figure 3: Ratio of direct and indirect taxes in Bangladesh, FY 2005-14



Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

However, to understand the burden and progressivity of a tax system it is important to understand components of both direct and indirect taxes and their implementation integrity.

2.1 Direct Taxes

Direct Taxes consist of income tax and other taxes. The sources of income tax can be classified on 7 categories:¹⁴

1. Salaries
2. Interest on securities
3. Income from house property
4. Income from agriculture
5. Income from business or profession
6. Capital gains
7. Income from other sources.

2.2 Personal Income Tax

The rates of Personal Incomes Taxes (PITs) are determined on the basis of differentiated income of different income groups. Bangladesh's tax system has five income brackets. There are differentiated rates and tax exemptions for different types of taxpayers, for instance the threshold of taxable income for women and senior citizens of 65 years and above is 3.00 lakh, 3.75 lakh for physically challenged persons and 4.25 lakh for war-wounded gazette freedom fighters. The tax tables (income slabs) are updated on a regular basis, at least once a year considering the changes in price level. For example, for

¹⁴ NBR, Income Tax at A Glance, <http://www.nbr.gov.bd/Publications.php?lan=eng>

FY2015-16, the tax exemption threshold for individual taxpayers was raised from Tk. 2.2 lakh¹⁵ to Tk. 2.5. Other thresholds were also revised accordingly.

Table 2 shows the slabs of individual tax rate in FY 2015-16; this does not include the exemptions listed above. Figure 4 shows the share of PIT in total tax revenue during 2005-2013.

“Considering prevailing inflation, increased cost of living and to reduce tax burden for marginal taxpayers I propose to raise tax-exemption threshold for individual taxpayers from Tk. 2 lakh 20 thousand to Tk. 2 lakh 50 thousand. To empower women and integrate them more in the economic activities and to reduce tax burden for senior citizens, I would propose to increase tax exemption threshold for women and senior citizens, aging over 65 years from Tk. 2 lakh 75 thousand to Tk. 3 lakh”.

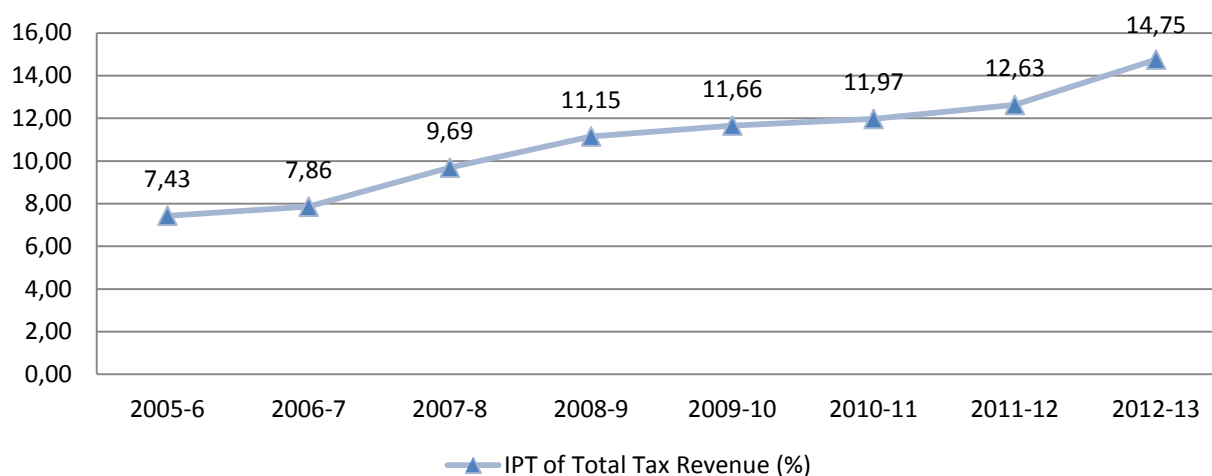
- Budget Speech 2015-16, Abul Maal Abdul Muhith, Minister, Ministry of Finance, Government of the People’s Republic of Bangladesh, 4 June 12015).

Table 2: Individual Tax Rate

Total Income	Tax rate
On first, Tk. 2.5 lakh of total income	Nil
On next, Tk. 4 lakh of total income	10%
On next, Tk. 5 lakh of total income	15%
On next, Tk. 6 lakh of total income	20%
On next, Tk. 30 lakh of total income	25%
On the balance of total income	30%

Source: Abul Maal Abdul Muhith, Minister, Ministry of Finance, Budget Speech 2015-16

Figure 4: Share of personal income tax in total tax revenue (%), FY 2005-2013



Source: NBR Annual Report 2012-13

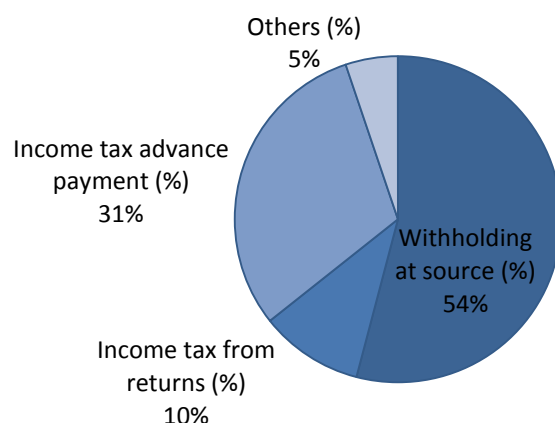
The trend analysis of the PIT shows that though the share of PIT in total tax revenue has steadily been increased over the years, it is not much considering the total population of the country. One of the

¹⁵ 1 lakh is equivalent to 100 thousand.

major reasons is a very narrow taxpayer base. According to the budget speech of the finance minister for FY 2014-15, there are only 1.8 million registered TIN holders. Among them nearly 1.2 million filed tax returns. The taxpayer base needs to expand rapidly with major registration drivers. The Direct Tax Laws and Codes are outdated and require fundamental changes based on the principle of universal taxation. In the income tax structure, withholding at source is a major component (54%); advance payment of income tax represents 31% and payment through submission of return only 10%. Figure 5 shows the relative sizes of income tax components in 2013. Income tax advance payment is a voluntary (pro-active) initiative of paying income tax by instalment to reduce pressure of paying a bulk amount at once at the end of the financial year.

In Bangladesh, withholding taxes are usually termed as tax deduction and are collected at source. Under this system, both private and public limited companies and any other organization specified by law are legally bound to withhold taxes at some point of making payments, and deposit the amount with the Government Exchequer.¹⁶ Withholding tax is important as it comprises a major portion of income tax in Bangladesh.

Figure 5: Components of income tax in %, 2013



Source: NBR Annual Report 2012-13

The structure of tax withholding in Bangladesh is very old-fashioned and does not indicate a proactive management of tax withholding agents. Withholding at source has been applied recently. However, because of the absence of a central database, there is no way for the tax administration to follow up on additional tax payments and to administer the withholding agencies.

In FY12, withholding at source was extended to twelve new sources, which does indicate that the list is reviewed and the NBR is looking for potential sources for generating additional revenue. Some of these new items are royalty from technical know-how fee, rental of power companies, newspapers, magazines, privately-owned TV channels, etc.

In most cases, the NBR relies on captive sources to collect the withheld tax - using public offices (for contracts and supplies), financial institutions (withholding of interest and dividend income) and customs

¹⁶ http://www.nbr-bd.org/incometax_at_a_glance.html

points (advance income tax from importers).¹⁷ Such a practice in some way makes people bound to pay taxes, which is not a good practice. It is important to motivate people to pay tax on a regular basis. Currently, the NBR collects tax from 58 sources, ranging from contractors and bank deposit holders, to exporters and importers. The tax authority plans to impose specific at-source tax on foreigners, based on their professions and types of services they provide. Employers will have to deduct 30 percent tax before making payments to foreign consultants, artists, singers and players. For contractors, suppliers and companies engaged in oil and natural gas exploration, 5 percent and 5.25 percent tax rates have been proposed. Companies offering services such as catering, cleaning, contract or toll manufacturing, credit rating, event management, security, product processing, stevedoring or berth operations will face a 10 percent advance income tax on commissions or charges. The same rate will be applicable to mobile banking service providers, including technical service providers or service delivery agents. A 10 percent tax at source was fixed for various services before, but the services were not defined individually. It created ambiguity for both taxpayers and the tax authority; the new measures will eliminate ambiguity for both service providers and service recipients.¹⁸ In order to monitor the collection of Tax Deduction at Source (TDS), there is a plan to set up a separate Taxes Zone.¹⁹ Although expansion of the tax base will increase the amount of PIT collected, it requires adequate consultation with the taxpayers and companies and needs to establish a separate monitoring cell to oversee tax collection from the aforementioned sources.

2.3 Wealth Taxes

Despite having a structured mechanism of corporate and personal income taxation, the country still lacks a systematic wealth tax mechanism. There is no systematic effort of assessing property and financial assets, and of collecting taxes accordingly, yet there are provisions of imposing a 10% surcharge on net wealth²⁰, the threshold is TK. 2 crore and 25 lakh of the price of net wealth in 2015-16.

Table 3 presents different slabs of wealth with the percentage of surcharge, and Table 5 shows the number of people who paid the wealth tax and the amount of revenue raised between FY 2011-12 and FY 2013-14. The collection of the wealth surcharge increased four times within two years. Revenue collected from this source increased at a faster pace compared to total tax collected.

Table 3: Rate of surcharge on net wealth

Price of net wealth	Rate of surcharge
Up to 2 crore 25 lakh	NIL
2 crore 25 lakh to 10 crore	10%
10 crore to 20 crore	15%
20 crore to 30 crore	20%
Above 30 crore	25%

Source: NBR Report 2014

¹⁷ Fiscal Management and Revenue Mobilization by Dr. Ahsan H. Mansur, Policy Research Institute of Bangladesh, Prepared as a background paper for the Seventh Five Year Plan

¹⁸ <http://www.thedailystar.net/business/nbr-widen-reach-withholding-tax-93577>

¹⁹ Abul Maal Abdul Muhith, Minister, Ministry of Finance, Budget Speech 2015-16

²⁰ Including land, real estate and financial assets minus liabilities

Table 4: Number of wealth tax payers and amount of revenue raised in FY 2012-13 and FY 2011-12

FY	No of people reported to have wealth above 2 crore	Revenue raised
FY 2013-14	10,152 persons	Tk 2,060 million
FY 2012-13	5,662 persons	Tk 603.6 million
FY 2011-12	4,446 persons	Tk 446.20 million

Source: NBR Report 2014

Table 4 shows that the revenue raised through wealth taxes (collected from those who reported to have wealth above Tk 2 Crore) has increased over the last three years. In FY 2012-13, only 5,662 persons had a net wealth above 2 crore in their income tax return, which is unrealistic.²¹ The wealthy households of Dhaka and Chittagong city are avoiding their taxes due to the surcharge system.

There is a trend of increasing wealth tax income during last three financial years. By imposing property tax, the government of Bangladesh can collect an additional 1,000 to 2,000 crore in taxes and it will have a progressive effect on the distribution of resources.²²

Under the surcharge system there are complexities in determining the price of assets and taxes. According to the NBR report, one in 10,152 persons (almost 1% of all taxpayers) in the country possesses assets worth over Tk 2 crore (Tk 20 million). This was revealed in their income tax statements submitted to the National Board of Revenue (NBR) over FY 2013-14. They paid surcharge imposed on this income tax and as a result the Revenue Board earned Tk 2,060 million (Tk 2.06 billion). According to NBR, fewer than 1% of these taxpayers own assets worth over Tk 20 million, which is unrealistic and unbelievable. The actual value of their assets was not properly assessed. There must be extensive reforms to determine the true value of property.²³

NBR first imposed a surcharge on property in 2011-12. In that fiscal year, only 4,446 taxpayers reported to have over Tk 2 million worth of assets. By imposing a 10% taxation, NBR earned Tk 446.20 million. Within three years, owners of Tk 2 crore worth of assets raised more than double that figure. In 2012-13 only 5,662 persons paid a surcharge, with NBR raising Tk 603.6 million. It was not ascertained how many people paid a surcharge this year.²⁴

The existing surcharge system also distorts investor incentives in favour of land holdings and stock market speculation vs. real economic activities. Without taxation there will be a large demand for land and real estate that can easily have a spiralling effect on prices, especially in a densely populated country like Bangladesh.²⁵

2.4 Corporate Income Tax

Rates of corporate income tax also vary from company to company on the basis of their type. Usually the agro-based industries enjoy low taxation in comparison to manufacturing and service providing industries. Yet, a number of export oriented manufacturing industries, e.g. readymade garments (RMG), enjoy tax holidays and other advantages like low import tariffs on imported materials.

²¹ Prothomalo, 31 May 2014, <http://www.prothom-alo.com/opinion/article/229474/>

²² Binayak Sen, *May 31, 2014, Wealth and Inequality*,

²³ <http://en.prothom-alo.com/bangladesh/news/67715/Each-of-10-000-owns-assets-worth-Tk-20m>, Aug.18, 2015

²⁴ <http://en.prothom-alo.com/bangladesh/news/67715/Each-of-10-000-owns-assets-worth-Tk-20m>, Aug.18, 2015

²⁵ Ahsan H. Mansur and Mohammad Yunus, 2011, *An Evaluation of the Tax System in Bangladesh*, PRI, Dhaka

In FY 2015-16 the highest tax rate (45%) was imposed on cigarette manufacturing and non-publicly traded mobile phone companies. Certain agro-based industries e.g. horticulture and pisci-culture that used to enjoy a zero tax rate, now have to deal with minimum taxation. However, for publicly traded companies, publicly traded banks and insurance companies, there are lower tax rates than for the non-publicly traded companies.

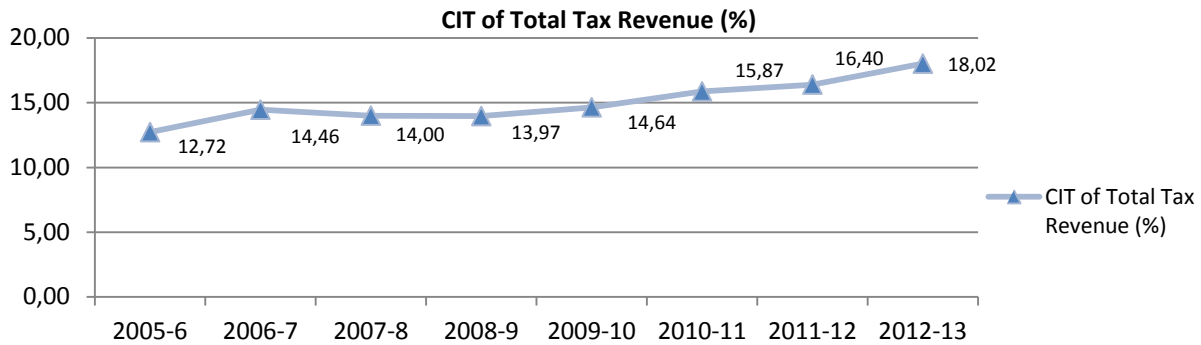
Table 5 shows tax rates for different companies for FY 2015-16. In recent years, the rates have been revised downward. For example, for publicly traded companies, the corporate tax rate was cut from 27.5% to 25%. The differentiated tax rates are applied to different companies to provide incentives. For example, the tax rates are lower for publicly traded companies to attract companies which are listed in stock exchanges. The average corporate tax rate in Bangladesh is also higher than the non-OECD country average (25%).

Table 5: Company tax rate

Category	Tax rate		
	FY 15-16	FY 14-15	FY 13-14
Publicly Traded Company	25%	27.5%	27.5%
Non-Publicly Traded Company	35%	35%	37.5%
Publicly Traded-Bank, Insurance and Financial Institution(other than Merchant Bank)	40%	42.5	42.5
Non-Publicly Traded.-Bank, Insurance and Financial Institution	42.5%	42.5	42.5
Merchant Bank	37.5%	37.5	37.5
Cigarette Manufacturer publicly traded company	40%	45%	40%
Cigarette Manufacturer non-publicly traded company	45%	45%	45%
Mobile Phone: Publicly Traded Company	40%	40%	40%
Mobile Phone: Non- publicly Traded Company	45%	45%	45%
Dividend Income	20%	20%	20%
Minimum Turn Over Tax	0.30 percent (0.10 percent in first 3 assessment years of commencement of commercial production)	0.30%	0.50%
Income from poultry industry	<ul style="list-style-type: none"> • On first, Tk. 10 lakh - 3 percent. • On next Tk. 20 lakh - 10 percent. • On the balance - 15 percent. 	Nil	Nil
Poultry feed, dairy, mulberry, apiculture, horticulture, pisciculture etc.	<ul style="list-style-type: none"> • On first, Tk. 10 lakh - 3 percent. • On next Tk. 20 lakh - 10 percent. • On the balance - 15 percent. 	3%	Not Found
Shrimp/poultry/fish hatchery	<ul style="list-style-type: none"> • On first, Tk. 10 lakh - 3 percent. • On next Tk. 20 lakh - 10 percent. • On the balance - 15 percent. 	General Tax Rate	Not Found

Source: Abul Maal Abdul Muhith, Minister, Ministry of Finance, Budget Speech 2015-16, 2014-15 & 2013-14

Figure 6: Share of CIT in total tax revenue (%), FY 2005-2013

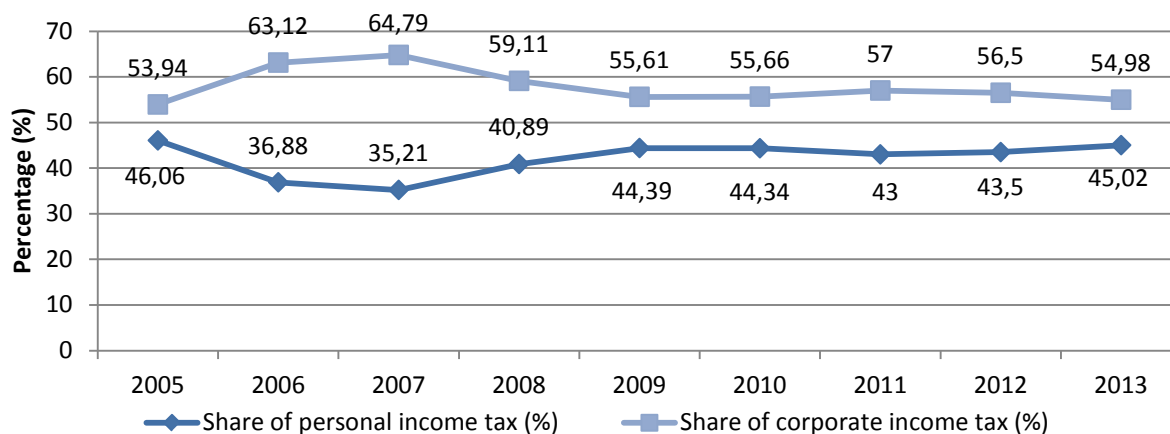


Source: NBR Annual Report 2012-13

The trend analysis of the CIT reveals that the share of CIT in total tax revenue has increased only from 12.72% in 2005 to 18.02% in 2013. Studying different reported and unreported sources, it was observed that tax avoidance and the lack of efficiency and accountability of tax collectors are the major factors for the low levels of tax collection. As shown above, the share of income taxes (PIT and CIT) in total tax revenue is still low. In 2004-5, it was 20.16%, which increased to 32.77% in 2012-13. As a result, indirect taxes, particularly the VAT, have been the main sources of tax revenues (37.73% in 2013). The tax burden thus falls upon the general population, including the poor and the marginalized, increasing inequality.

Figure 7 shows that among the sources of income tax, corporate income tax has always been the major source, with a share of around 55% in 2013. Since 2005 the gap between corporate and personal income tax has remained between 10% (in 2013) and 13% (in 2011); but a significant gap is visible during 2006 to 2008. During this period, the share of personal income tax went down to 35.21%. Presumably, this was due to the emphasis the military based caretaker government placed on corporate tax. The share and volume of the income tax first started increasing when the democratic government came to power in 1991, following almost a decade of military rule. However, no study has been done so far to measure the effect of a democratic environment on revenue administration and governance in Bangladesh. It could be inferred that the sudden increase was the result of a transition towards good governance and major structural change of the income tax department. Figure 7 shows a comparison between the share of corporate and personal income tax over the period from 2005 to 2013. The increasing share of personal income tax is a result of higher tax collection from this source. Income tax collection from individuals increased at a faster rate, which resulted in the change in shares during the last five years.

Figure 7: Share of personal and corporate income tax in %, FY 2005-2013



Source: NBR 2014

In Bangladesh, there is no limit on companies carrying forward losses and there are no rules which limit interest deductions. However, there are penalties for a failure to pay tax on due date. The penalties are as follows:

- imposition of penalty amounting to 10% of tax on last assessed income subject to a minimum of Tk. 1,000
- in case of an individual assessee whose income was not assessed previously - Tk. 5,000
- in case of an individual assessee whose income was assessed previously, fifty per cent (50%) of the tax payable on the last assessed income or Tk. 1,000, whichever is higher.
- in case of a continuing default by any type of assessee, a further penalty of Tk. 50/- for every day of delay

2.5 Excise duty

Bangladesh has no excise tax as such, it is an excise duty. An excise duty is a tax on sales or production for sale. Such duty is considered as an indirect tax, meaning that the producer or seller who pays the tax to the government is expected to try to recover or shift the tax by raising the price paid by the buyer. The excise duty applies to only two items: bank deposits and domestic air tickets. Excise duty on Bank deposits starts with Tk 150 per deposit account per year, if the balance ranges between Tk 20,000 to Tk 100,000. The highest charge is Tk 150,000 when the balance, whether credit or debit, exceeds Taka Five crore at any time during a year. However, no excise duty shall be imposed in cases where the balance, whether credit or debit, does not exceed Tk 20,000 at any time during a year. In the case of air tickets, the rate varies for different nationalities: Tk 500 per seat for single journey for Bangladeshi nationals, Tk 1,000 for SAARC countries and Tk 1500 for the EU and the rest of the world.

Even though the share of excise duty is miniscule compared to other tax types, its share in total tax has been increasing, from 0.48% in 2005 to 0.68% in 2014. It was found that the share of excise duty was below 0.5% between 2005 and 2009. The upward trend started from 2010 and reached 0.7% in 2013. Table 6 presents share (%) and volume of excise tax from FY 2005-2014, while figure 9 shows the growth of the share of excise duty over the same period.

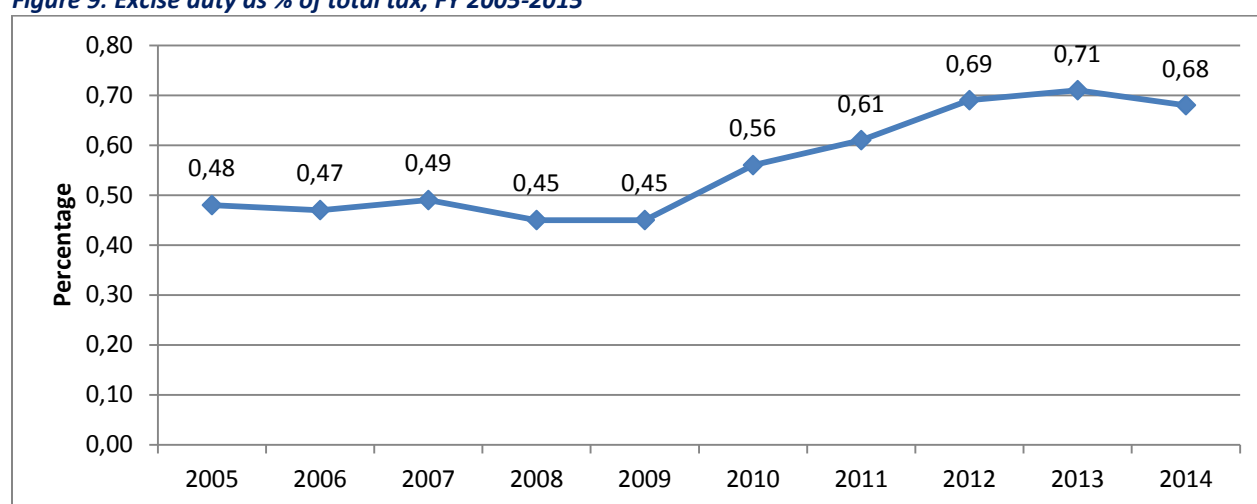
Table 6: Share of excise duty in total tax for the period of FY 2005-14

	2005	2006	2007	2008	2009
Total Tax	29904.46	34002.43	37219.32	47435.66	52527.25
Excise tax	144.39	161.15	183.49	214.33	238.34
% of total tax	0.48	0.47	0.49	0.45	0.45

	2010	2011	2012	2013	2014
Total Tax	62042.16	79403.11	95058.99	109151.73	120512.83
Excise tax	347.49	486.18	660.36	772.53	822.39
% of total tax	0.56	0.61	0.69	0.71	0.68

Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

Figure 9: Excise duty as % of total tax, FY 2005-2015



Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

In Bangladesh major luxury goods, domestically produced or imported, are subject to supplementary duties. This is collected under the VAT law (See Section 2.6 and Section 2.7).

2.6 Value Added Tax (VAT)

The Value Added Tax (VAT) was introduced in Bangladesh in 1991 to replace the sales tax (VAT Act No. 22 of 1991). Since then, VAT has remained the single-largest source of revenue for the Bangladesh government.

The share of VAT is the highest in the tax structure, about 37% in 2014. The share of VAT increased from 35% in 2005 to 39.44% in 2010 (Table 6). Despite remaining in the highest position, VAT has been declining to 36.98% of total tax revenues in 2014, due to an increase in the share of all direct sources.

Table 6 presents the percentage and volume of the VAT share over the period from 2005 to 2014, while figure 8 shows a steady increase of the VAT share with its percentage value.

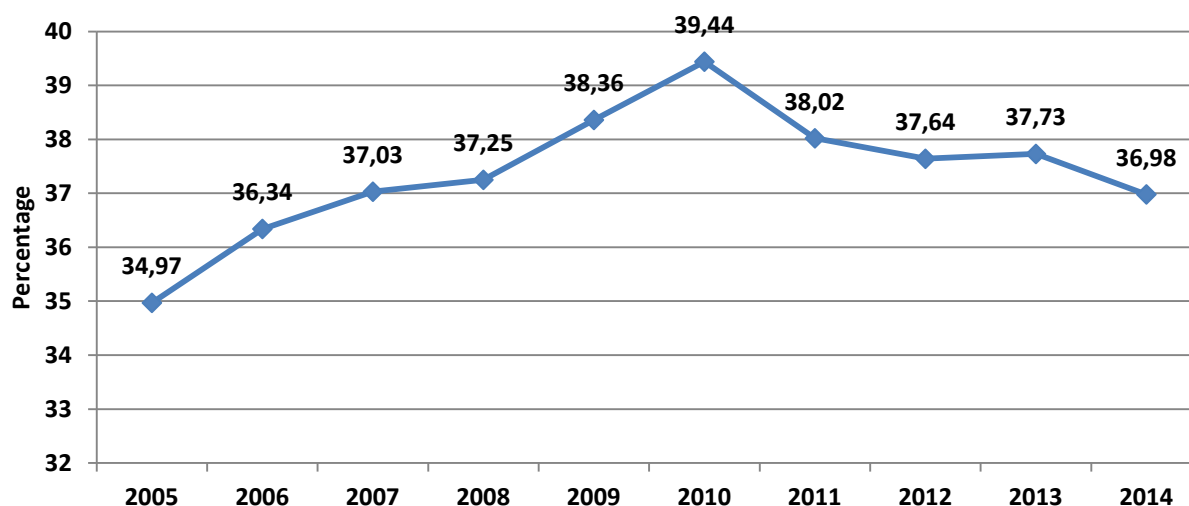
Table 7: Share of VAT in Total Tax for the Period of 2005-2014

	2005	2006	2007	2008	2009
Total Tax	29,904.46	34,002.43	37,219.32	47,435.66	52,527.25
VAT	10,458.47	12,358.17	13,782.3	17,671.36	20,146.85
VAT % of Total Tax	34.97	36.34	37.03	37.25	38.36

	2010	2011	2012	2013	2014
Total Tax	62,042.16	79,403.11	95,058.99	109,151.73	120,512.83
VAT	24,468.05	30,190.68	35,777.43	41,182.42	44,571.01
VAT % of Total Tax	39.44	38.02	37.64	37.73	36.98

Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

Figure 9: Share of VAT in total tax in %, FY2005-14



Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

Under the VAT Act 1991, a number of items enjoy exemption. Cottage industries are kept outside the VAT net. The general VAT rate is 15%, but on luxurious products a supplementary duty (SD) is also imposed in addition to VAT. Exported items, essential commodities and certain non-food products get a zero VAT rate. However, essential women's products are not exempted from VAT. There are lower VAT rates also for certain products or services that benefit mostly the rich. Some special sectors within the small industries category enjoy VAT exemptions and differential rates (truncated rates). These are 1.5%, 2%, 2.25%, 4%, 4.5%, 5%, 5.5%, 6%, 7.5%, 9% and 10%.²⁶ Over the last two and half decades, the rules under the VAT Act 1991 have been revised and amended from time to time through a number of Statutory Regulatory Orders (SROs).

A new Value Added Tax and Supplementary Duty Act 2012 has been enacted and will be effective from July 2016.²⁷ The new Act proposes to bring significant changes in the earlier VAT rules and regulations.

²⁶ Md. Zakir Hossain, 2015, Value Added Tax: Act, Rules and Usage, Dhupradi Publication, Dhaka

²⁷ Abul Maal Abdul Muhith, Minister, Ministry of Finance, Budget Speech 2015-16

The new Act will cover three forms of taxes: VAT, SD and TT. As the previous one, the new VAT was one of the conditions of the IMF's Extended Credit Facility (ECF) programme which is currently being carried out. The major changes under the new act are:²⁸

- The new VAT and SD Act will have a *broader coverage*. VAT will now be applied to all sectors. Besides imports, production, trading and services, it will cover a wider range of services, including the provision of services and import of services, immovable property, leases, grants, licenses, permits, rights, facilities etc.
- VAT *registration thresholds* have been changed, Tk. 80,00,000 BDT (80 Lakh Taka). However, every person who carries out economic activities of manufacturing any supplementary dutiable goods in Bangladesh or supplies any supplementary dutiable service in Bangladesh is required to be registered.
- Under the new act, the VAT rate is 15%. The *truncated value base*²⁹ will be discontinued and will be termed as a 'distortion under the present VAT system'.
- Besides TT, all the entrepreneurs will be treated equally. The current broad based 'exemption list' has also been narrowed down significantly in the new Act.

Currently, Bangladesh's VAT system is one of the most inefficient in the world with the lowest VAT productivity. Only 60,000 out of nearly 700,000 companies pay VAT regularly. The number of firms that should pay value added tax should be 3-6 lakh.³⁰

NBR is preparing a change under the modernization programme with the support of the World Bank, IMF and IFC. If successfully implemented, this reform strategy will result in much higher revenues. Achieving the required increase in VAT revenue (including supplementary duty) in relation to GDP will still not be an easy task. In addition to complete reorganization and retraining of VAT staff and replacing most of the field level staff with new revenue officers, the transformation will require other major changes: (i) replacing tariff values on hundreds of products with their normal market prices; (ii) reducing the number of products subject to supplementary duty from 1,400 to under 200; (iii) eliminating the current practice of price approval on most items; and (iv) eliminating the excise type current account system for VAT payments and moving to a proper return-based VAT administration.³¹

A study conducted by Nahida Faridy and Tapan K. Sarker (2011), using the Household Income Expenditure Survey 2005 data, found that the VAT in Bangladesh is regressive. It also found that the VAT burden in the lowest income range is 6.92%³², which is extremely high given the fact that the VAT burden of the highest-income group is only 4.56%. The average effective VAT rate is 6.01%, which is also higher than that of the highest four income groups. This means higher income groups are bearing less of

²⁸ Towfiqul Islam Khan and Md. Zafar Sadique, 2014, *VAT and SD Act 2012: Concerns and Implementation Challenges*, CPD, Dhaka

²⁹ With the standard VAT rate 15%, there were lower rates like 1.5%, 2%, 2.25%, 4%, 4.5%, to 10% called truncated value base

³⁰ Abul Maal Abdul Muhith, Minister, Ministry of Finance, <http://www.thedailystar.net/business/tax-evasion-irks-muhith-111646>

³¹ Dr. Ahsan H. Mansur, Fiscal Management and Revenue Mobilization, Policy Research Institute of Bangladesh, Prepared as a background paper for the Seventh Five Year Plan

³² Percentage of household income

the VAT burden than the lower income groups. Based on the findings, the study gives the following policy recommendations that could help design a better VAT system in Bangladesh. They are:³³

- Extensive exemptions cause distortion and induce elements of tax evasion in the tax system. However, some exemptions are unavoidable. Hence, VAT exemptions in Bangladesh should be limited only to basic health services, public transport, agriculture and agro-based industries and government education.
- Poor people usually buy goods at markets and small community shops that operate in the informal sector. A reasonably high threshold can help reduce the regressivity of VAT. It can also reduce the burden borne by the lower income groups and ensure the equity of VAT.

2.7 Trade Tax

Bangladesh's revenue structure has been burdened by taxes from indirect sources for a long time and is characterized by heavy import and export duties. Bangladesh, like many other countries, has to reduce such duties and levies to face the challenge of globalization and market liberalization.

The share of import and export based tax in total tax receipts has been declining; it was 73.98% in 2005 and dropped to 27.57% in 2014. The major decline happened from FY 2009 onwards: in 2009 it stood at 68.84%, dropping to 36.83%. The rates of trade tax vary from product to product; higher rates are usually put on luxury goods, and lower rates on essential goods that are not produced locally. There is zero import duty on some products e.g. computer and computer accessories.

Table 8 presents share of trade tax (export and import) from the total tax over the period from 2005-14, while figure 10 shows declining trend of the trade share during that period.

Table 8: Share of import/export based tax in total tax, FY 2005-14

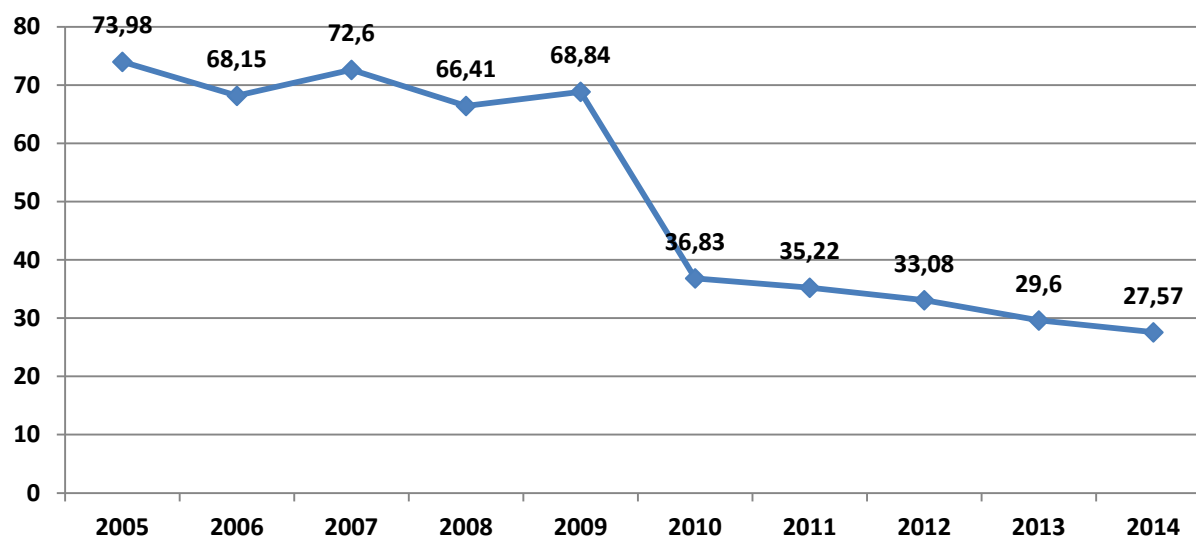
	2005	2006	2007	2008	2009
Import duty	7,912.13 (35.75%)	7,825.43 (33.77%)	8,154.76 (30.18%)	9,601.42 (30.48%)	9,371.23 (25.92%)
VAT at import level	12,358.17 (55.86%)	13,782.3 (59.48%)	17,671.36 (65.39%)	20,146.85 (63.95%)	24,468.05 (67.67%)
Supplementary duty at import level	1,853.48 (8.38%)	1,563.42 (6.57%)	1,196.63 (4.43%)	1,753.85 (5.57%)	2,318.24 (6.41%)
Export duty	0	0	0	0	0
Total import & export based taxes	22,123.78	23,171.15	27,022.75	31,502.12	36,157.52
Total Tax	29,904.46	34,002.43	37,219.32	47,435.66	52,527.25
% of Total Tax	73.98	68.15	72.60	66.41	68.84

³³ Nahida Faridy and Tapan K Sarker, *Progressivity of VAT in developing country: empirical evidence from Bangladesh*, Asia-Pacific Tax Bulletin, May/June 2011

	2010	2011	2012	2013	2014
Import duty	8,997.12 (39.37%)	11,566.05 (41.35%)	13,268.07 (42.19%)	13,227.55 (40.94%)	13,540.82 (40.75%)
VAT at import level	10,651.22 (46.61%)	12,375.81 (44.25%)	13,769.64 (43.79%)	14,846.48 (45.95%)	15,318.9 (46.10%)
Supplementary duty at import level	3,203.13 (14.02%)	3,998.71 (14.30%)	4,368.9 (13.89%)	4,205.01 (13.01%)	4,344.43 (13.07%)
Export duty	0	28.71 (0.10%)	38.95 (0.12%)	33.47 (0.10%)	26.46 (0.08%)
Total import & export based taxes	22,851.47	27,969.28	31,445.56	32,312.51	33,230.61
Total Tax	62,042.16	79,403.11	95,058.99	109,151.73	120,512.83
% of Total Tax	36.83	35.22	33.08	29.60	27.57

Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

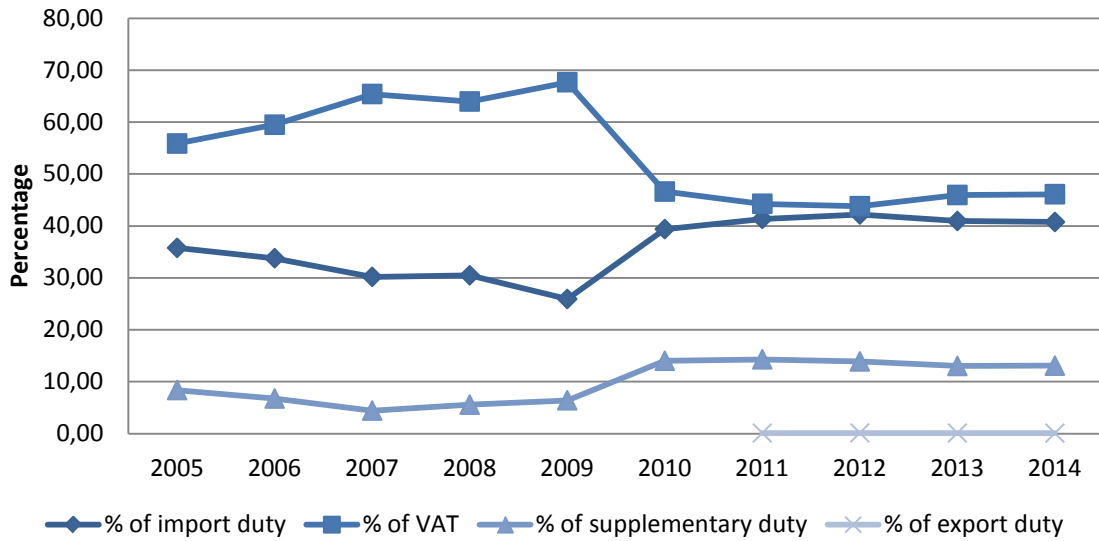
Figure 10: Trade tax as% of total tax receipts, FY 2005-15



Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

The share of VAT in total tax revenue is the highest, followed by import duty and supplementary duty; 46.1%, 40.75% and 13.07% respectively in 2014. Secondly, since 2009 the contribution of VAT has been declining rapidly; from 67.67% to 46.61%; it stood at around 46% in 2013 and 2014 (Figure 11).

Figure 11: Share of different taxes/duties in trade tax, FY 2005-15



Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

Compared to countries with a similar per capita income level, Bangladesh’s dependence on taxes from international trade is higher. For example, according to World Development Indicators data, in 2011 the share of taxes from international trade was 24.6% in Bangladesh. The corresponding figure for Cambodia was 15.6%.

Recent measures in import/export based tax

- Existing import duty rates of 0%, 5%, 12% and 25% have been rationalized to 0%, 5%, 10% and 25%. This means that the tax rate for the import of intermediate goods has been reduced from 12% to 10%. Keeping the highest tax rate of 25 % unchanged, the import tariff for the import of capital machinery and ICT related equipment has been reduced from 3% to 2%.
- Supplementary duty rates were re-organized into 10 different slabs. They are 10%, 20%, 30%, 45%, 60%, 100%, 150%, 250%, 350% and 500%. This means that a new slab of 10% supplementary duty was introduced. It is to be mentioned here that the highest three slabs in the supplementary duty structure (ie. 250%, 350% and 500%) apply to the import of luxury goods and commodities that represent a health hazard, like tobacco products, alcohol and luxury cars.
- The existing specific duty for raw and refined sugar, at the rate of 1,500 and 3,000 taka per MT, remains unchanged.
- Specific duty on billets and ingots was increased to Tk. 3,500 per metric ton from Tk. 2,500 per metric ton, whereas that of metal scrap remains unchanged at the rate of Tk.1,500 per metric ton. On the other hand, the specific duty on gold bullion and silver bullion remains unchanged at Tk.150 and Tk.6 per 11.664 gramm.
- It was decided to continue for another year the regulatory duty at the rate of 5% on finished and luxury items.
- In order to promote the use of renewable energy, the customs duty on the import of equipment for biogas plants and solar lamps has been reduced.
- Import duty on more than 50 commodities, including raw materials for glass, ceramic, steel melting, printing and optical fibers, has been reduced to lower duty rates.

Source: NBR, 2014

2.8 Presumptive/Turnover tax

The contribution of the turnover tax to total tax revenue is very little: 4 to 6 crore Taka from FY 2005 to 2014 (Table 9). The share of turnover taxes has also declined over the period: from 0.019% to 0.004% (Figure 12). Turnover tax (TT) has preferential provision for small enterprises with an annual turnover below Tk. 80 lakh. They pay turnover tax at a lower rate of 3 percent. Under the 'turnover tax' provision, an entrepreneur has to keep a minimum ledger accounting that could reduce his administrative cost.³⁴ Based on a feasibility assessment, the presumptive tax is adapted to different types of business so that it benefits small and low-income businesses, and there are clear rules for calculating the tax-base. There is a legal provision for a businessman to challenge presumption. However, in practice, this is difficult as the cost of challenging is comparatively higher for a small businessman. There is neither a threshold for paying the presumptive tax, nor a policy to move businesses from the presumptive regime to the CIT regime.

³⁴ Towfiqul Islam Khan and Md. Zafar Sadique, 2014, *Value Added Tax and Supplementary Duty Act 2012: Concerns and Implementation Challenges*, CPD, Dhaka

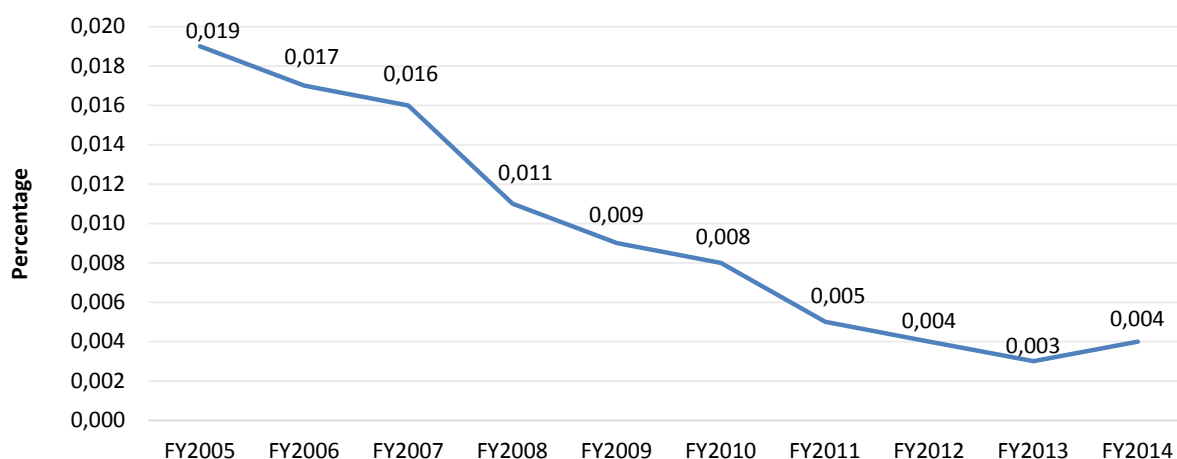
SMEs in Bangladesh enjoy a tax waiver in case turnover is under Tk. 7 lakh, and are subject to reduced tax rates for turnovers under Tk. 24 lakh a rate of 2 percent, under Tk.60 lakh at a rate of 3 percent and over 70 lakh a rate of 15 percent.

Table 9: Turn over tax (in crore taka) and % of total tax, FY 2005-2014

FY	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Total Tax	29,904.46	34,002.43	37,219.32	47,435.66	52,527.25	62,042.16	79,403.11	95,058.99	109,151.73	120,512.83
Turn Over Tax	5.71	5.77	6	5.12	4.91	4.67	3.63	3.45	3.68	4.72
% of total tax	0.019	0.017	0.016	0.011	0.009	0.008	0.005	0.004	0.003	0.004

Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

Figure 12: Turnover tax as % of total tax receipts, FY2005-14



Source: NBR Annual Report 2012-13 and Bangladesh Economic Review 2015

2.9 Gender Analysis

The gender implications of fiscal policy are a critical concern in a country like Bangladesh, where a number of problems affect mostly women. The unequal property ownership, wage discrimination and the unequal distribution of power in the household, these need to be taken into account in designing fiscal policies. Women have been considered only in the tax-exemption threshold for individual taxpayers; in other areas of taxation, there is no different rate for women and men. In the exemption threshold for individual taxpayers, there is different rate for women and men. The proposed tax-exemption threshold for individual taxpayers was raised from Tk. 2 lakh 20 thousand to Tk. 2.5 lakh and from Tk. 2.75 lakh to Tk. 3 lakh for women.

An assessment of gender implications of fiscal policies is not easy, as the literature available on gender implications of taxation is limited. It is difficult to obtain sex-disaggregated data on the tax incidence; and studies on this topic are very rare.

Chapter Summary and Recommendations

The analysis in this chapter shows that the major reform of tax administration occurred in the 1990s, in a democratic regime following military rule in the country. However, there is no study to measure the effect of democratic environment on the revenue administration and governance. The analysis also shows that indirect taxes are still the primary source of government income and contribute the lion's share of total tax receipts in Bangladesh.

The administration of direct taxes is outdated and based on territorial and geographical administrative units. As long as withholding taxes at sources has no central database, there is no way for the tax administration to follow up on additional tax payments and also administer the withholding agencies. The combined effect of all these deficiencies is the very low tax efficiency and the very low direct tax to GDP ratio in Bangladesh. Given the context the main recommendations are:

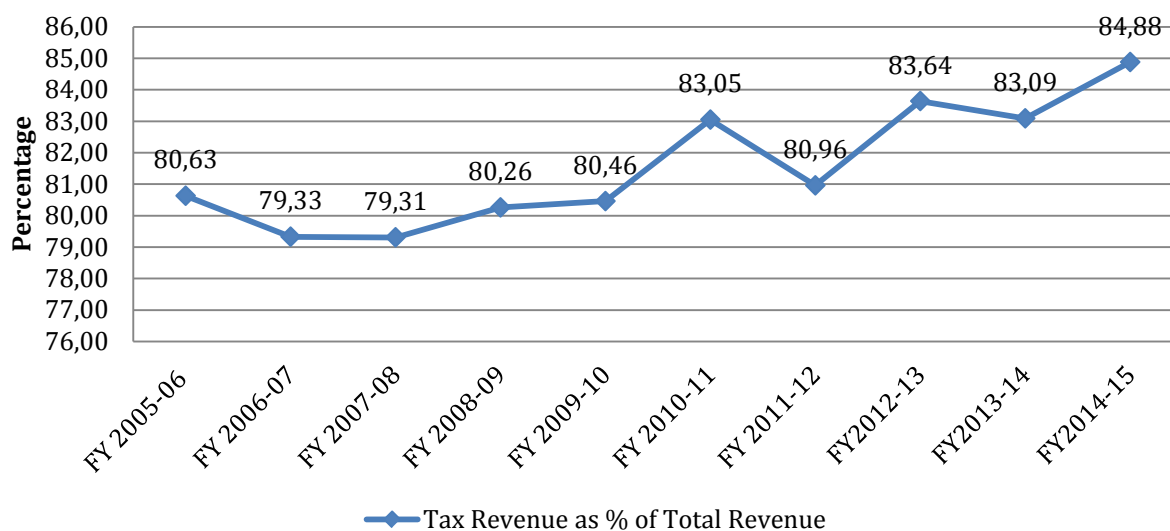
- Broadening of the taxpayers' base and identification of sectors. This will require the monitoring of the ownership of all sizable physical and financial assets of taxpayers to determine the income generated by those assets.
- Broadening of the tax revenue sources from the traditional dependence on taxing financial institutions and a few large non-financial corporations. The tax administration has the tendency to increase the tax burden on existing and compliant taxpayers and to not work hard on identifying new taxpayers by gathering information from multiple sources.
- Focussing on income from service providers and self-employed (who are difficult to tax).
- Treating all sources of income equally for tax purposes without discrimination of households. This would imply taxation of capital gains from land, real estate and housing, and the stockmarket. Wealth accumulation in Bangladesh primarily happens through the accumulation of urban land and real estate, untaxed or low tax income of the rapidly growing RMG (Ready-Made Garments) sector, and relatively low tax incidence on income through financial instruments.
- The simplistic manner of imposing Wealth Tax in the form of an Income Tax surcharge of 10% should be abandoned. The NBR should move to develop a proper "Wealth Tax" or "Property Tax" and reform measures are needed to determine the true value of property and apply property tax to it. The current practice essentially increases the marginal tax rate by an additional 10% and amounts to distorting the incentive to work or to increasing tax avoidance. NBR has to build its capacity for the proper administration of the property and wealth tax, with proper study and identification of the right way to collect the tax, not simply by adding to income tax in the form of a surcharge.
- VAT in Bangladesh could be made less regressive by making a distinction between luxury goods and basic-needs goods. Supplementary taxes can be imposed on luxury goods.
- VAT exemptions in Bangladesh should be limited to basic health services, public transport, agriculture and agro-based industries and government education.

CHAPTER 3 Revenue Sufficiency

3.1 Tax Revenue

In Bangladesh, tax receipts made up 80.63 to 84.88 percent of total revenues between FY 2005-06 and FY 2014-15. That, the share of tax revenue increased from 80.96 to 84.88 from FY 2011-12 to FY 2014-15 (Figure 13).

Figure 13: Share of tax and non-tax revenue in total revenue, FY2006 - 2015



Source: Bangladesh Economic Review 2014-15

Despite a lot of effort to generate tax revenue, the tax system of Bangladesh is characterized by a low tax to GDP ratio, as seen in the table 10. Though the tax to GDP ratio has increased from 7.5% to 9.69% from FY 2006 to FY2013-14, in terms of revenue generation the performance has been rather disappointing, with the tax to GDP ratio still standing below the 10% mark, one of the lowest in the world. Compared with the Sixth Five Year Plan's target of increasing the tax to GDP ratio by 4.6 percentage points to 12.4 percent of GDP by FY2015, the actual tax to GDP ratio only increased to 9.3 percent of GDP, which is an increase of 1.5 percentage points. In the newly adopted Seventh Five Year Plan the government set a target to raise the tax to GDP ratio to 14.1% in FY2019-2020, but failed to include effective measures to reach the goal.

Table 10: Tax-to GDP Ratio, FY 2006 to 2015

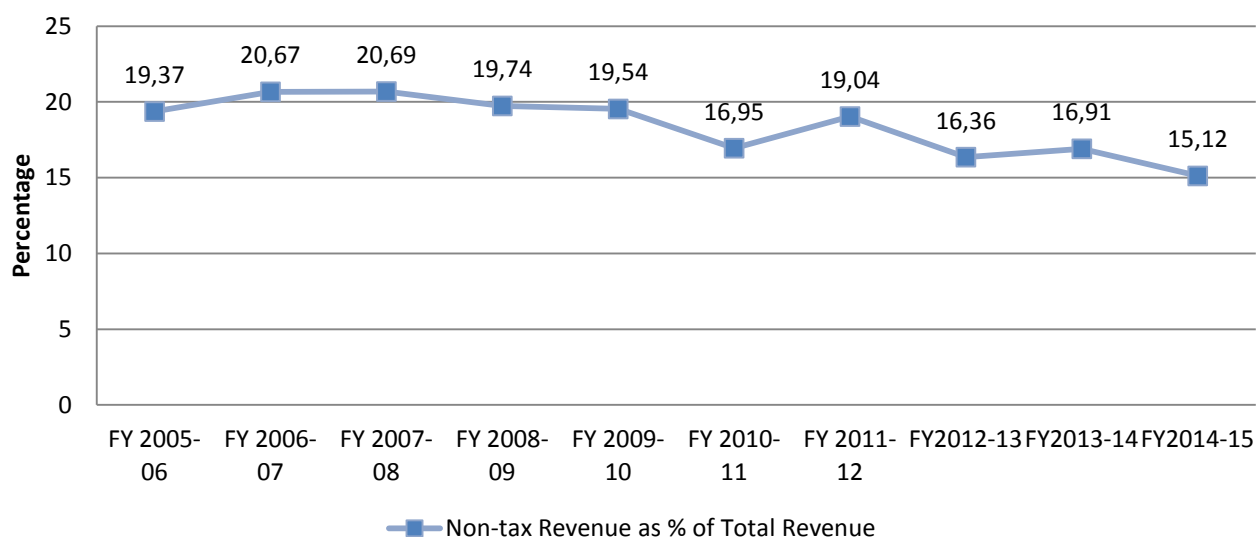
FY	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Tax-to GDP Ratio (%)	7.50	7.14	7.64	7.88	8.02	8.63	9.12	9.74	9.69

Source: NBR Annual Report 2013 and Bangladesh Economic Review 2014-15

3.2 Non-tax Revenue

In Bangladesh, non-tax revenue made up 19.37 and 15.12 percent of total revenue from FY 2005-06 to FY 2014-15. From FY 2011-12 to FY 2014-15 the share of non-tax revenue has decreased gradually. It was above 19% from FY 2005-06 to FY 2011-12, and decreased to 15.12% in FY 2014-15 (Figure 14). Sources of non-tax revenue include rents, concessions and royalties collected by the state when it contracts out the right to profit from some goods or services to a private corporation. The fiscal framework for the extractive industry in Bangladesh is not very clear and lacks the necessary regulations. In addition, the extractive companies sometimes enjoy lower corporate income tax rates in confidential agreement with the government.

Figure 14: Share of tax and non-tax revenue in total revenue, FY2006 - 2015



Source: Bangladesh Economic Review 2014-15

It is noteworthy that in Bangladesh, the non-NBR and non-tax revenues remain out of focus and untapped despite having significant potential for revenue generation. Therefore, it is important to give proper attention to non-NBR and non-tax sources to diversify and expand tax coverage³⁵. Also, efforts should be made to make state-owned enterprises (SoEs) more efficient and to ensure the auditing of state-run and state-supported commercial enterprises that fall under different ministries.

3.3 Taxpayers

Income taxes, both personal and corporate, are considered the major potential sources of the country's revenue. The number of individual taxpayers has been increasing over the last few years. However, less than 1% of the population pays income tax.³⁶ In a country of around 160 million people, only around 1.2 million individuals and companies and organizations currently pay Income Tax.³⁷

³⁵ Towfiqul Islam Khan, Research Fellow, Center for Policy Dialogue-CPD, interviewed on 18.08.2015

³⁶ Nasir Uddin Ahmed, Chairman NBR, Government of Bangladesh, IGC Growth Week 2011, London School of Economics, Sept. 2011

³⁷ Abul Maal Abdul Muhith, Minister, Ministry of Finance, Budget Speech 2015-16

Table 11 shows that the total number of taxpayers in different categories has increased in the last three years. But still, a large number of potential taxpayers are out of tax net. According to the NBR Survey 2014, 79% businessmen are out of tax net.³⁸

Table 11: No. and composition of Taxpayers

Category	FY 2011-12		FY 2012-13		FY 2013-14	
	No. of tax payer	%	No. of tax payer	%	No. of tax payer	%
Salaried	387,478	21.27	441,440	20.53	501,025	21.52
Company	51,443	2.82	57,656	2.68	59,581	2.56
Others (withholding tax)	1,382,385	75.90	1,651,576	76.79	1,767,851	75.92
Total	1,821,306	100.0	2,150,672	100.0	2,328,457	100.0

Source: Annual report of NBR 2012-13

Furthermore the NBR identified 1 lakh 66 thousand 546 potential house owners and business houses in urban areas that are not paying taxes. The NBR is taking the initiative to file cases against these potential payers,³⁹ who were identified from the national survey data and household survey. In Bangladesh there are many house owners who rent out their houses (apartments) and earn a taxable income. But as the money and rent transactions between the 'house owner' and the 'tenant' is informal in most cases (direct cash payment at the end of the month), the income is not reported officially.

Tax collection in Bangladesh has been well below the level of most countries at a similar stage of economic and social development. This indicates the relative weakness of the tax system in Bangladesh compared to other countries in the region. This below-par resource mobilization has impeded economic growth and social development. Until recently, the collection of tax revenue in Bangladesh has been, low averaging at about 10.2 percent of GDP until FY14 (Table 12).

Table 12: Tax Effort in South Asian Countries, Average 2010-2014 (As % of GDP)

Country	Average Tax Revenue as % of GDP
Bangladesh	10.2
India	16.6
Nepal	14.4
Pakistan	10.6
Sri-Lanka	12.4

Source: Ministries of Finance of Pakistan, Nepal, India. Central Bank of Sri Lanka, NBR Bangladesh, IMF World Economic Outlook

The narrow tax-base, widespread exemptions, and administrative inefficiencies are the main factors behind low the tax to GDP ratio in Bangladesh compared to the neighbouring and comparator countries.⁴⁰

Among developing countries Bangladesh is the country that makes the least effort to collect taxes. According to a study⁴¹ conducted by the policy analysis unit of the Bangladesh Bank found that when it

³⁸ <http://www.bonikbarta.com/printpage/preview/9248.html>

³⁹ <http://www.bonikbarta.com/2014-09-30/news/details/215.html>

⁴⁰ Fiscal Management and Revenue Mobilization by Dr. Ahsan H. Mansur, Policy Research Institute of Bangladesh, Prepared as a background paper for the Seventh Five Year Plan

⁴¹ A Panel Study on Tax Effort and Tax Buoyancy with Special Reference to Bangladesh, Lutfunnahar Begum, Policy Analysis Unit Bangladesh Bank, Working Paper Series: WP0715, June 2007

comes to assessing the tax effort, Bangladesh scores poorly, with an average tax effort index⁴² of 0.493. This has important policy implications, in the sense that Bangladesh and other countries with low tax effort (less than unity) are not utilizing their full tax raising capacity, and therefore fail to raise the tax revenue to cover budgetary imbalances. The tax effort index for both direct and indirect taxes is below 0.6, implying that Bangladesh has the potential of raising revenue collection from both direct and indirect taxes. Table 13 presents tax effort index ratio of both direct and indirect tax over the period from 2000 to 2011.

Table 13: Tax Effort in Bangladesh, 2000-2010

FY	Direct Tax Effort Index	Indirect Tax Effort Index
2000	0.614	0.468
2001	0.588	0.477
2002	0.612	0.504
2003	0.609	0.520
2004	0.560	0.540
2005	0.513	0.553
2008	0.573	0.589
2011	0.601	0.604

Source: Tariq Saiful Islam, 2014⁴³

In terms of tax buoyancy⁴⁴, Bangladesh ranks the second highest among the sample countries, with a tax buoyancy ratio of 1.235, meaning that tax revenue is quite responsive to GDP and effort has been made to increase tax revenue over the period.⁴⁵

Bangladesh's tax effort is also low compared to other Asian countries. Indonesia, Philippines, Singapore, South Korea and Sri Lanka each have an estimated tax effort index above unity implying the full utilization of their revenue potential. Among others, Pakistan and Thailand have an average index greater than or equal to 0.9. The average for Bangladesh is 0.657. It may be noted that Bangladesh is ranked the lowest in terms of tax effort among selected countries. Additionally, the effort in collecting VAT is slightly higher than one other country in the list, and the effort in collecting income tax is higher than two countries on the. The comparator table also indicates that efficiency in the collection of VAT is somewhat better than that of income tax. Tax efforts remain higher even among the comparator African countries. Table 14 presents tax effort ratios of selected countries.

⁴² Tax effort has been used as an indicator of how much a country is utilizing its taxable capacity; If the value of the index is less than one, it means that the country is not utilizing its full revenue potential. Conversely, if the value of the index is greater than one, it implies that the country is collecting more taxes than would be predicted.

⁴³ Tariq Saiful Islam, 2012, Taxation and Future Economic Development of Bangladesh at Development Constraints and Realization edited by Mustafa K. Mujeri, UPL Dhaka

⁴⁴ The tax buoyancy provides a dynamic index of tax performance, which measures the sensitivity and response of the tax system with respect to income/GDP.

⁴⁵ Dr. Ahsan H. Mansur, Fiscal Management and Revenue Mobilization, Policy Research Institute of Bangladesh, Prepared as a background paper for the Seventh Five Year Plan

Table 14: Tax Efforts in Selected Countries (for the most recent years)

Country	Tax Efforts	Income Tax Efforts	VAT Efforts
Bangladesh	0.657	0.531	0.567
India	0.850	1.491	0.765
Pakistan	0.920	1.279	1.007
Sri Lanka	0.983	0.640	1.722
Nepal	0.668	0.522	0.729
Korea Republic	1.004	2.953	2.953
Philippines	1.040	1.324	0.743
Bhutan	0.690	1.066	0.687
China	1.015	0.923	1.170
Ghana	1.613	0.692	1.082
Kenya	1.309	1.886	1.394
Malaysia	0.848	1.104	0.614
Thailand	0.891	0.495	0.992
Vietnam	1.556	1.902	1.080

Source: Policy Research Institute, 2014

However the country's tax effort is characterized by several untransparent and flexible measures in tax systems. They include weakness in expanding the tax net, tax evasion and avoidance, illicit or black money, tax exemption and illicit financial flows.

3.4 Informal Sector

The NBR has recently tried to bring small informal businesses into the tax net, which will help these firms to formalize. The NBR undertook a survey, as mentioned above, to register businesses and provide them with a TIN and VAT registration number or BIN. According to a CPD study⁴⁶, about 96% of small manufacturing firms are paying some tax (either income tax or VAT). However, they are not necessarily filling out their tax returns or complying with the tax law. The study also found that 70% of the surveyed firms are not interested in compliance and receiving the tax benefits on offer, mainly to avoid hassles and the high costs of compliance. The non-compliance of service providers operating in the informal sector is higher. The NBR's effort to formalize these firms and businesses do not include any clear guidance that the businesses will not be taxed retroactively when formalized.

3.5 Illicit Financial Flows (IFS)

Illicit financial flows are cross-border transfers of funds that are illegally earned, transferred or utilized. They can be generated in many different ways that are not revealed in national accounts or balances of payments figures. They include trade mispricing, bribery, money laundering, criminal profits, corruption, smuggling, etc. Both companies and individuals can generate these illicit financial flows from one country to another. The outflow of capital is facilitated by a shadow international financial system, especially offshore financial centres and tax havens.⁴⁷

⁴⁶ Mustafizur Rahman, Towfiqul Islam Khan, and Md. Zafar Sadique. *The Impact of Value-Added-Tax (VAT) on Enterprise Development*. Country Study Report: Bangladesh. 2014. Islamabad: Governance Institutes Network International (GINI).

⁴⁷ *Whose money and whose interest? Illicit money flies off Bangladesh, EquityBD Position Paper, February 2014*

The incidences of capital flight and the practice of disguising the origins of illegally-earned money are high in Bangladesh. According to Global Finance Integrity (2001-2010), the average illicit financial flow from Bangladesh was USD 1,406 million and the cumulative amount was USD 14,059 million for the period from 2001 to 2010. Bangladesh ranked first as origin of illicit capital outflow in the period of 1990 to 2008, with USD 34.8 billion. The position of Bangladesh is 44th among 143 developing countries. Nepal, Pakistan and Sri Lanka are ranked 58th, 94th and 105th, which mean that the highest amount of laundered money came from Bangladesh.⁴⁸

The central bank of Switzerland recently disclosed in its annual report that ‘secret’ money from Bangladesh deposited in different Swiss banks rose by 62 percent year-on-year in 2013. The deposits, which stood at BDT 32.36 billion (USD 415 million) at the end of 2013, were BDT 19.91 billion (USD 255 million) in 2012, showed in the latest data of the Swiss National Bank. It means that while the illicit financial flows from developed countries to Switzerland are declining, it is skyrocketing for Bangladesh. There is information on illicit financial flows from Bangladesh to Canada and Malaysia too. To take up residence in Malaysia under its ‘My Second Home (MM2H)’ programme, one needs to show liquid assets worth at least about BDT 122 million (USD 0.16 million) and offshore income of about BDT 0.25 million (USD 3,141 million) per month. Since the programme was launched (in 2002) until April 2014, 25,500 people from across the world have migrated to the country. Of them, 2,874 (11%) were from Bangladesh, according to the Malaysian government’s website. This means that Bangladeshis laundered about BDT 35 billion (USD 448 million) at least to acquire a second home in Malaysia and none was required to seek approval with the authorities in Bangladesh, as Malaysia does not ask about the source of the money. Similarly, a citizen of Bangladesh can get residence permit in the US or Canada by showing liquid assets worth USD 500,000 (BDT 38.7 million). Statistics are hard to come by, but reportedly hundreds of wealthy Bangladeshis have made these two countries their second home. Again, the US and Canada will not ask where the money has come from, experts say.⁴⁹

The government is trying to combat the IFFs, however the government’s attempt to trace and fight IFFs is political. When a political party comes in power, the ruling government becomes hostile to the opposition party leaders and tries to trace any IFFs directed by them. In most of the cases the government’s initiative is found to be limited in fighting IFFs and getting the money back. In recent times, a number of legal reforms and administrative efforts have been put in place to curb illicit financial flows. The Anti-Money Laundering Law was revised, based on recommendations from FATF. NBR has also proposed a new cell under the Income Tax Wing towards this end. The Bangladesh Financial Intelligence Unit (BFIU) of the central bank has become an independent body. It is to be noted that these government initiatives will only bring results when these reforms are translated into actions. Global rules in this area also need to be reformed.

3.6 Tax Evasion and Avoidance

Tax avoidance is the way to reduce tax by using the loopholes in laws, while tax evasion does the same by violating the law. Taxable objects, property transfer, and so on are underreported and concealed. Tax evasion and tax avoidance incentives reduce the tax to GDP ratio by 5 percentage points, or about Tk. 400 billion (NBR2011).⁵⁰

⁴⁸ *Revenue Mobilization and Economic Growth, Bangladesh Economic Update, November 2013, Unnayan Onneshan, Dhaka*

⁴⁹ *Whose money and whose interest? Illicit money flies off Bangladesh, EquityBD Position Paper, February 2014*

⁵⁰ *Revenue Mobilization and Economic Growth, Bangladesh Economic Update, November 2013, Unnayan Onneshan, Dhaka*

The absence of a participatory policy-making process, lack of research and reform of the tax system, short-term oriented and politically motivated tax policies, loopholes, anomalies and complexities of tax laws and policies are responsible for creating tax evasion.

There is a provision for investigating tax evasion, but the institutional weaknesses of the tax administration, lack of professional support for tax officials and inappropriate behaviour of tax officials have undermined the efficiency of the tax policy implementation process, resulting in not addressing and combating tax evasion in an efficient manner. During the compliance process, the absence of a tax culture among income earners, inadequate taxpayer services, complexities and unfairness in tax assessment, the weak enforcement by and the negative image of the tax department work as influential driving forces for tax law non-compliance. The empirical findings also revealed that the corrupt nexus of self-interested policy-makers, rent-seeking tax officials, selfish taxpayers, including business people, professionals, self-employed persons, and their intermediaries and tax agents, facilitates tax evasion.⁵¹

3.7 Illicit wealth and black money

The amount of unreported money is between 45 percent and 81 percent of gross domestic product in 2011 (MoF, 2011). Those who own the majority of the wealth and income of the country are still outside the tax net. According to both government surveys and the Finance Minister, a large amount of the government's money is unaccounted. In economics or regular parlance, one would call this "black money." A small part of this may be valid income, but because no tax has been paid on this for various reasons, it has now been listed as "undisclosed" income. One can be certain that the right epithet for this is "illicit" wealth, earned through theft, looting, corruption, fraud, aggression and terror. This includes bribes, investment fraud, commissions, the expropriation of governmental or public property, extortion, the sharing of funds allocated for unfinished development projects, over and under-invoicing, and so forth. It is obvious that only the powerful can do this, and that with the support and encouragement of the administration. This is precisely why we keep hearing about the whitening of "black money" during the tenure of each government, but rarely see any effort to stop its source. It is because administration officials and the owners of black money are the one and the same.⁵²

Chapter Summary and Recommendations

This chapter analysis shows the disappointing feature of the tax to GDP ratio still standing just over the 10% mark, one of the lowest in the world. The tax collection in Bangladesh has been below the level of most countries at a similar stage of economic and social development, which indicates the relative weakness of the tax system in Bangladesh compared to other countries in the region. The tax net is too narrow; the rates of tax avoidance and tax exemption are high. In addition there is no effective measure to tackle illicit financial flow and curb black money. Given the context the recommendations are:

- The number of income tax payers in Bangladesh is very low. The NBR should ensure a taxpayer friendly environment to bring more people into the tax net. The law must act against people who are evading taxes, so honest taxpayers do not feel treated unequally.

⁵¹ Nahida Faridy and Tapan K Sarker, *Progressivity of VAT in developing country: empirical evidence from Bangladesh*, *Asia-Pacific Tax Bulletin*, May/June 2011

⁵² Anu Muhammad, *Who's prospering on whose labor?* <http://alalodulal.org/2013/06/20/anu-muhammad-budget/>

- While bringing informal businesses into the tax net, it is important to ensure that new taxpayers are treated without hassle.
- Strong political decisions need to be made to not allow the whitening of black money.
- To curb illicit financial flows, reforms are not enough. They need to be acted upon.
- Focus on non-NBR sources and non-tax sources, as they have a significant potential of revenue generation. Study and analyse the non-NBR and non-tax sources to diversify and expand tax coverage. Efforts should also be made to make SoEs more efficient and the auditing of the income of state-run and state supported commercial enterprises should be done by different ministries.

CHAPTER 4

Tax Exemptions

4.1 Governance

Bangladesh, like other developing countries, provides various kinds of support to major and emerging industries with a view to enhancing industrialization in the country. Tax exemption and concessions are provided under the directives of the country's industrial policy, export and import policy, SME policy and fiscal policy. Direct tax exemptions and incentives are: tax holidays, exemptions and deductions, tax rate reductions, deferrals, tax credits and others. Indirect tax measures are: exemptions and deductions.⁵³

According to Mortaza and Begum (2006), there were a total of 106 measures under direct (55 measures) and indirect taxes (51 measures) for providing various kinds of tax exemptions and incentives. Tax holidays are provided to newly set up firms, physical infrastructure, tourism, etc. Exemptions and deductions apply to enterprises located in export processing zones, power generation companies, agriculture related industry, etc. Concessionary rates apply to textiles and jute industries and to those who do not enjoy tax holidays.

To encourage the growth of agricultural production and setting-up of local manufacturing industries, the government provides incentives in the form of tax reductions and tax exemptions. The activities and industries listed below enjoy tax exemptions and varying rates. Although there are clear and transparent rules for granting tax exemptions, they are not supported by any cost-benefit analysis and they are not subject to parliamentary oversight. There are also mal-practices in availing tax deductions and exemptions, for instance when the political leaders submit their wealth statement to the Election Commission (it is a necessary precondition for all participants in any national election), they often state their income as income from the shrimp, poultry and fish hatcheries (tax exempted) to hide the fact that they do not pay taxes on their income or wealth. There are also examples of secret agreements on tax exemptions for companies, which the media later revealed.

*The national budget for FY 2015-16 provides the following exemptions.*⁵⁴

- *A separate and reduced tax rate of 15% for co-operative societies other than its income related to agriculture and cottage industry.*
- *Reduced tax rate for shrimp, poultry and fish hatcheries.*
- *Special incentives packages are in the offing to encourage investment in developing the Bangladesh Economic Zone and Hi-Tech Park, along with investment in these areas. In consideration of the rising demand for vehicles and to ensure suppliers use the domestic workforce, along with reducing foreign currency expenditure, tax holidays for automobile manufacturing sector as heavy industry are provided.*
- *Tax holidays for the tire manufacturing industry.*
- *Exemption of taxes on interest income from Wage Earners Development Bond, US Dollar Premium Bond, US Dollar Investment Bond, Euro Investment Bond, Euro Premium Bond, Pound Starling Investment Bond and Pound Starling Premium Bond.*

⁵³ Tax Policy and Enterprise Development in Bangladesh, CPD, Dhaka

⁵⁴ Abul Maal Abdul Muhith, Minister, Ministry of Finance, Budget Speech 2015-16

4.2 VAT Exemption

The minimum threshold for paying VAT applied to small business was increased from Tk 6,000 to Tk. 9,000 in the national budget for FY 2013. VAT exemptions include products under the categories of food and agriculture, poultry, and agricultural inputs etc.⁵⁵

- *Withdrawal of existing VAT levied at the rate 15 percent on the domestic production of "Nutrition Premix in Animal Food".*
- *Total exemption of existing VAT on the electricity bills for cold storage services.*
- *With the progress of civilization outbreaks of new types of diseases are observed. Fatal viral diseases like hepatitis C are today quite common. The treatments for these diseases are very expensive. In order to reduce people's medical expenses, VAT is not levied on the domestic production and import of medicines for acute liver related diseases.*
- *Exemption of VAT for the supply of broken iron pieces or iron scrap.*
- *Though the custom duty is levied at the rate of zero percent at the import stage of PET Chips, a raw material of polyester yarn, the Advance Trade VAT at the rate of 4 percent is still there at the same rate. For the protection of domestic industry, there will be exemption of current VAT in this sector.*
- *Exclusion of the „capitation grant“ allocated for both public and private orphanages from the VAT net.*
- *Total withdrawal of VAT currently levied on the photography industry.*
- *Withdrawal of existing 15% VAT on Iron Oxide at the local manufacturing stage.*
- *As a substitute to import, glass tube and energy saving bulb, and the raw materials used to manufacture them were exempted from the payment of VAT up to 30 June, 2015. This VAT exemption facility will be extended to 2017 as an incentive for this industry.*
- *Full exemption from existing VAT on the electricity bills of the relevant developers of the High Tech Park, and on the procurement provider service of the relevant developers and investors of the same.*
- *Withdrawal of existing 15 percent VAT on the manufacturing of plastic crystals through the recycling of plastic waste.*
- *Exemption from VAT on producing and supplying batteries up to the capacity of 60 ampere for the IDCOL registered solar panel manufacturers in the battery manufacturing industries.*
- *Withdrawal of the existing trade VAT on local sales of jute products; withdrawal of the existing 15 percent VAT levied on the license issuance and license renewal fee of jute and jute products.*
- *VAT exemption threshold on the export of sample medicines from Tk. 30,000 to Tk. 1 lakh.*

The supply of broken iron pieces or iron scrap may cause the largest revenue loss. In Bangladesh iron pieces or iron scrap (mostly from the ship demolition industry) are used for making iron bars, for which there is a big market demand in housing and infrastructure development.

4.3 Transparency

The NBR is not transparent in providing information about what it calls sensitive information to the public. For example, there is no information available at the tax department on the revenue foregone

⁵⁵ Tax Policy and Enterprise Development in Bangladesh, CPD, Dhaka

due to tax exemptions. Neither does the NBR publish the list of companies benefiting from tax exemptions.

4.4 Revenue Forgone

In Bangladesh there is no good estimate of revenues forgone due to tax exemptions. At the time of preparing tax incentives, the revenues estimates are also not prepared. As a result, the actual cost-benefit accounting is not prepared.

Chapter Summary and Recommendations

This chapter's analysis shows that exempting a range of essential goods and services from VAT, benefits everyone and especially the poor. The VAT exemptions for agricultural inputs is also of benefit to a large percentage of the Bangladesh population, and by keeping prices lower than they would otherwise be, they support the Government's efforts to get farmers to use more agricultural inputs to improve production and reduce poverty. Although there are clear and transparent rules for granting tax exemptions, they are not supported by any cost-benefit analysis and they are not subject to parliamentary oversight. There are also mal-practices in availing tax deductions and exemptions. Given the context, the recommendations are:

- Curb tax exemptions and ensure that all existing exemptions are approved by Parliament and open to public scrutiny. This is both feasible and necessary. Importantly, this transparency should move beyond the realm of 'duty free' exemptions alone to capturing tax exemptions granted across all tax types.
- The key to a more effective management of tax incentives and exemptions is likely to lie in reduced discretionary powers in the granting of tax benefits, total transparency about the recipients of such benefits and an unambiguous mandate for the NBR to implement and monitor all incentives and exemptions.
- VAT exemptions and zero rates are still revenues foregone and there need to be explicit criteria for determining what goods and services are exempted or zero rated.

CHAPTER 5

Effectiveness of the Tax Administration

5.1 Organization

The National Board of Revenue (NBR), the apex tax authority of Bangladesh, is administered under the Internal Resources Division (IRD) of the Ministry of Finance (MoF). The MoF has 4 Divisions, namely, the Finance Division (FD) the Internal Resources Division (IRD), the Banking Division and the Economic Relations Division (ERD). Each division is headed by a Secretary to the Government. The Secretary of the IRD is the ex-office Chairman of NBR. The NBR is responsible for the formulation and continuous re-appraisal of tax-policies and tax-laws in Bangladesh. The National Board of Revenue (NBR) is the central authority for tax administration in Bangladesh.

As a centralized revenue authority the NBR is responsible for the formulation and continuous re-appraisal of tax-policies and tax-laws in Bangladesh. There is also a section under the NBR dedicated to large taxpayers, however it does not co-operate with local governments in revenue collection.

An effective tax administration is crucial for revenue generation to contribute to accelerating growth and to improving the quality of life of citizens. A sound tax system means to remove complexity and limit the collection points for taxation, making the system more transparent, thereby making the public more certain that everyone is paying what they are due, which is more comfortable with the fairness of the system (Mazid, M.A 2015.)⁵⁶

In terms of growth in achievements compared with previous years, the nominal rate is satisfactory; it is above 20% from 2010 (Table 15).

Table 15: Target, achievement and growth of taxes in terms of previous year in crore taka, FY 2005-13

FY	Target	Revised Target	Growth in terms of previous year	Achievements
2004-05	32,190.00	30,500.00	12.75%	29,904.46
2005-06	35,652.00	34,456.00	12.97%	34,002.43
2006-07	41,055.00	37,479.00	8.77%	37,219.32
2007-08	43,850.00	45,970.00	22.66%	47,435.66
2008-09	54,500.00	53,000.00	15.29%	52,527.25
2009-10	61,000.00	61,000.00	15.09%	62,042.16
2010-11	72,590.00	75,600.00	23.93%	79,403.11
2011-12	91,870.00	92,370.00	22.18%	95,058.99
2012-13	112,259.00	112,259.00	21.53%	109,151.73

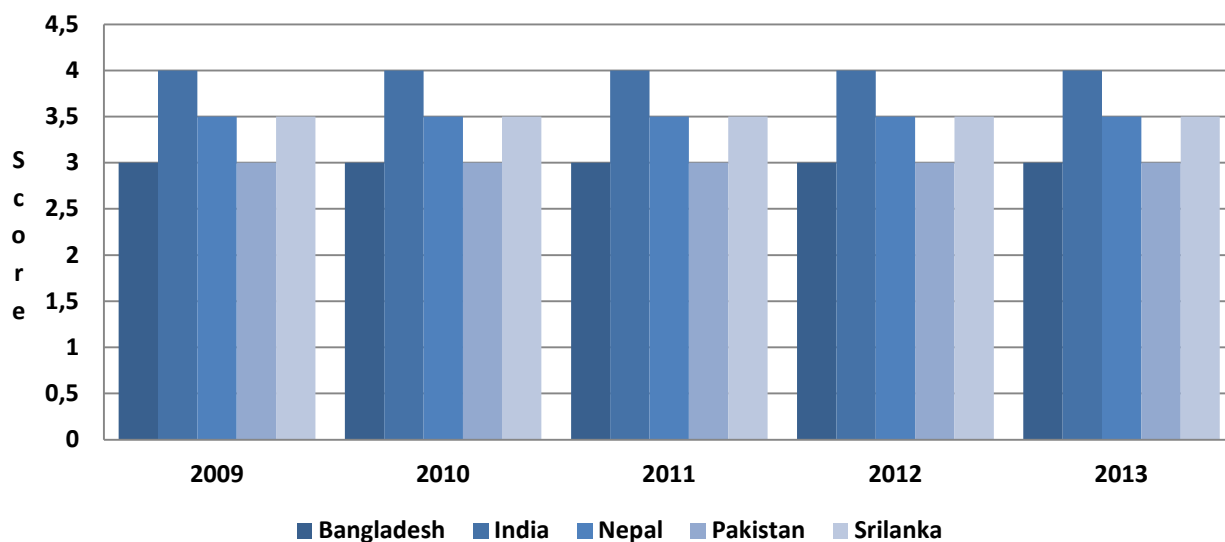
Source: NBR Annual Report 2012-13

In FY 2008, 2010, 2011 and 2012 the collection of taxes exceeded the target set by the NBR, while in most of the remaining years achievement was above 90% of the actual target. Figure 15 shows of achievement in percentages in tax collection in the FY 2004-5 to 2012-13.

⁵⁶ Mazid, M.A. (2015): Tax Regime in Bangladesh: An Evaluation; published in Daily Star on 08.03.2015, <http://www.thedailystar.net/tax-regime-in-bangladesh-an-evaluation-41737>

Another important feature of Bangladesh’s tax systems is its inefficiency, especially in tax administration. Among the South Asian countries, Bangladesh and Pakistan have one of the lowest efficiency scores (Figure 15). Furthermore, no improvement was reported between 2009 and 2013.

Figure 15: CPIA efficiency of revenue mobilization rating (1=low to 6=high)



Source: WDI, World Bank Databank, <http://data.worldbank.org/indicator/IQ.CPA.REVN.XQ>

5.2 Administration

Over the years, the NBR has made efforts to digitize its tax administration. Now it is easier to have a digital TIN, and as a result the number of TIN holders has increased over the years. The tax administration however lacks digitalization in rural areas. The TIN is now required to get certification and licenses for business. Filing of tax returns by an individual and the submission of tax return online is still not possible, as NBR still maintains an outdated ‘control’ based system, which relies on the physical monitoring of taxpayers in order to enforce compliance. This allows NBR officials to retain enormous discretion and, in turn, opportunities for collusion with or extraction from taxpayers. The discretion enjoyed by tax officials, as well as the overall inefficiency of data management within the NBR, are exacerbated by a high degree of administrative fragmentation. Whereas there has been a trend across low-income countries towards greater integration of administrative units, the NBR remains divided into three highly autonomous divisions: direct tax, VAT and customs. The relative absence of data sharing across departments severely undermines administration, and opens space for collusion, arbitrariness and abuse, while fragmentation also creates additional costs for taxpayers. These challenges have been consistently aggravated by significant human resources constraints within the NBR.⁵⁷

5.3 Human Resources

The NBR often struggles with a lack of human resources. During the 1990s the NBR could not recruit new officers due to a legal barrier. At present, the total number of positions in NBR is 22,136. However,

⁵⁷ Mirza Hassan and Wilson Prichard, November 2013, The Political Economy of Tax Reform in Bangladesh: Political Settlements, Informal Institutions and the Negotiation of Reform, ICTD Working Paper 14

currently, only 11,831 people are employed. Among them only 3,750 are first and second class officers who are directly involved in tax collection. About 4,715 vacant positions are yet to be filled. Taking them into account, currently, the ratio of tax officers to taxpayers or potentially active population is about 0.4:10,000. Even if the vacant positions are filled, the aforesaid ratio will remain less than 1.

The NBR regularly organizes training programme for its tax officials. In FY 2013-14, 287 tax officials were trained at the BCS (Tax) Academy while 30 tax officials were trained abroad. However, in certain areas the capacity of human resources needs to be enhanced. For example, the NBR has recently established the transfer pricing cell. However, it does not have adequate capacity to audit the international transactions of multinational companies. Indeed, due to a lack of human resources, the proportion of audited tax files is also very low.

5.4 Conventions

Currently, Bangladesh has signed double tax treaties with 33 countries. However, Bangladesh, has not signed the Multilateral Convention on Mutual Administrative Assistance in Tax Matters yet.

5.5 Cost of Tax Collection

According to the NBR’s report for 2012-13, the costs of tax collection has reduced but there still is scope to reduce costs further. Currently NBR spends Tk. 1.35 for every Tk. 100 in revenue collected, which is less than 2.5% of OECD cost standards. The costs of collecting direct taxes are higher than that of indirect tax. Table 16 presents costs of collecting direct and indirect taxes in FY 2012-13.

Table 16: Cost of tax collection in FY 2012-13

	Cost of collecting Tk.100
Cost of tax collection	1.35
Cost direct tax collection	0.58
Cost of indirect tax collection	1.09

Source: NBR Annual Report 2012-13

Under the overall control of IRD, the NBR administers the excise, VAT, customs and income-tax services, made up of 3,434 officers of various grades and 10,195 supporting staff positions. Considering the country’s active population (aged 15-64) of 60,000,000, the ratio of tax officers to active population is 1: 17,472, and to taxpayers (1.3 million) it is 1: 379.

5.6 Corruption

Bangladesh is perceived as one of the most corrupt countries in the world. According to the Transparency International’s Corruption Perceptions Index 2014, Bangladesh ranked as the 14th most corrupt country in the world. In Bangladesh, one of the weaknesses of tax administration is the insufficient oversight mechanism to check corruption. There are also no protection mechanisms for whistleblowers. There is no tax ombudsman office in Bangladesh. There is no particular code of conduct for the tax collectors. Cases of tax evasion have been investigated, but they are often not resolved in due time. The Anti-Corruption Commission (ACC) also lodges tax evasion cases. However, the cases are often influenced by political nepotism.

Chapter Summary and Recommendations

The tax administration in Bangladesh has been successful in achieving annual targets of tax collection; however the cost for tax collection is still high. In terms of accountability and transparency, the tax administration seems to be less accountable to taxpayers, not transparent in decision-making and sometimes reactive. Without transparency, the public will not be able to accurately assess how their money is spent and thus be unable to hold their representatives appropriately to account⁵⁸. At the institutional level there has been limited effort and openness in data sharing across administrative units responsible for tax collection. Hence the recommendations are;

- To monitor the ownership of all sizable physical and financial assets of taxpayers and determine the income generation out of those assets.
- There is no comprehensive mechanism to monitor and administer withholding agencies. The development of a central data base under the NBR, with assigned human resources, would help follow up on additional tax payments and also administer the withholding agencies.
- Tax related laws and rules are often found to be complex for an ordinary taxpayer. It is important to simplify tax rules in order to make them taxpayer friendly.
- The formulation of tax policies should be backed by evidence based research. Often tax policies are formulated in an arbitrary manner. For a progressive taxation, consultation must be held with taxpayers, including individuals and business communities, and other stakeholders such as independent experts and civil society.
- It is important that parliamentary watchdogs are closely involved in formulating tax policies and monitoring related activities. In Bangladesh, discussion and debates in parliament are not adequate as regards tax related policies. Enhancing the members of parliament's capacity on tax related policies and practices, and empowering the Public Accounts Committee need to be prioritized.
- Strengthening and decentralization of the tax administration with professional tax officials and changing the behaviour of tax officials to tackle tax avoidance. The capacity of tax officials also needs to be enhanced, while the vacant positions at the tax office need to be filled as soon as possible to ensure services to the taxpayers.

⁵⁸ Mazid, M.A. (2015): Tax Regime in Bangladesh: An Evaluation; published in Daily Star on 08.03.2015, <http://www.thedailystar.net/tax-regime-in-bangladesh-an-evaluation-41737>

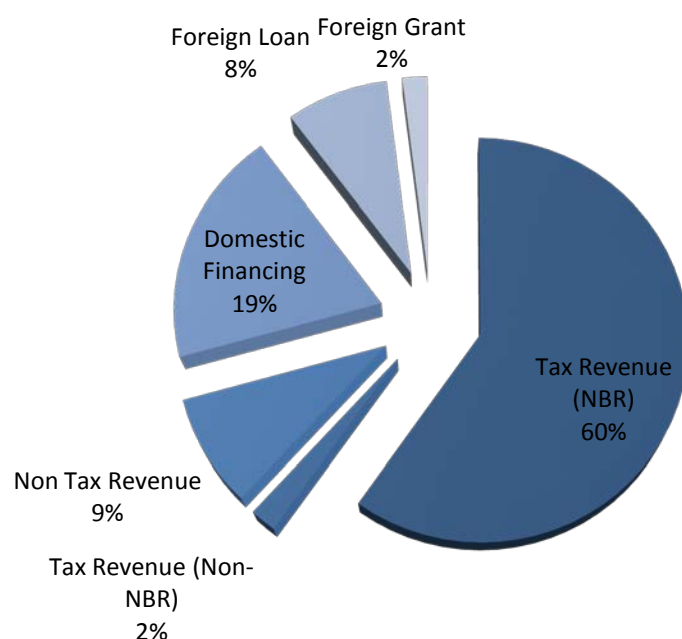
CHAPTER 6

Government Income and Spending

6.1 Components

Government income mostly (90%) depends on domestic sources; only 10% comes from foreign loans and grants. Tax and non-tax revenue are the main sources of government income, namely 60 percent in the national budget 2015-16, followed by domestic financing⁵⁹ (19%) and foreign grants and loans. Borrowing from banks is the major source in domestic financing, which creates the fiscal burden of interest payments. Figure 16 shows the sources of income in FY 2015-16.

Figure 16: Gov. Sources of Income, Budget 2015-16



Source: Budget in Brief 2015-16, Ministry of Finance, Gov. of Bangladesh, www.mofgov.bd

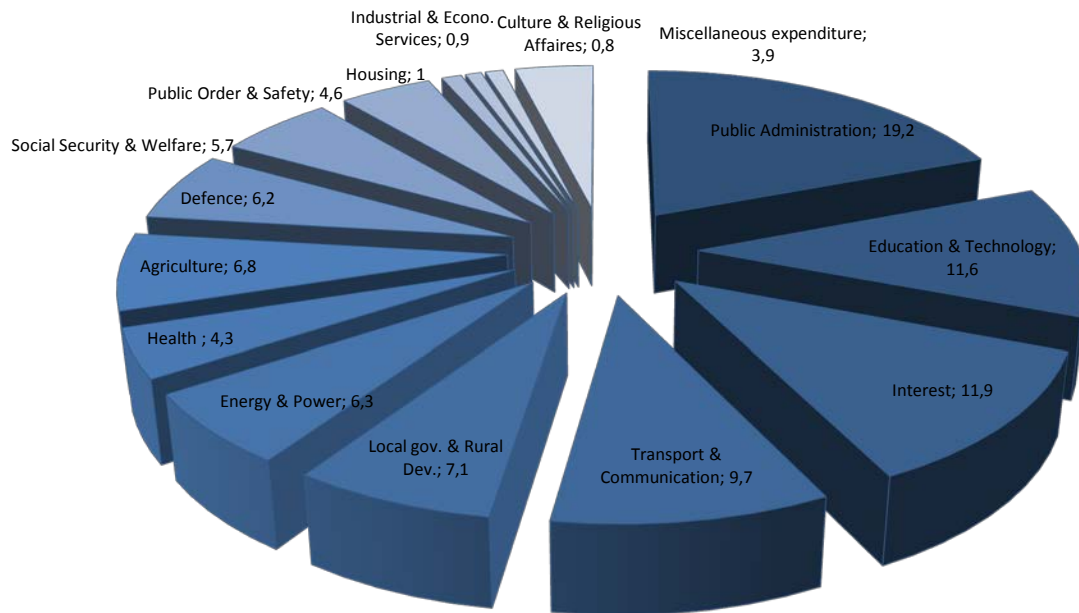
Figure 17 below shows that the public administration receives the highest allocation (19.2%) in 2015-16, followed by interest payment (11.9%) and education (11.6%).⁶⁰

The allocation for interest payment is more than double that for health sector (4.3%) (Figure 16). The allocation for health is less than defence budget (6.2%). Figure 18 shows the main sectors of government spending in FY 2015-16.

⁵⁹ Domestic financing means the government financing sources for deficit budget and it is borrowing from banking and non-banking sources

⁶⁰ In order to show higher allocation in education, government shows budget of education and technology together

Figure 17: Components of govt spending in %, Budget 2015-16



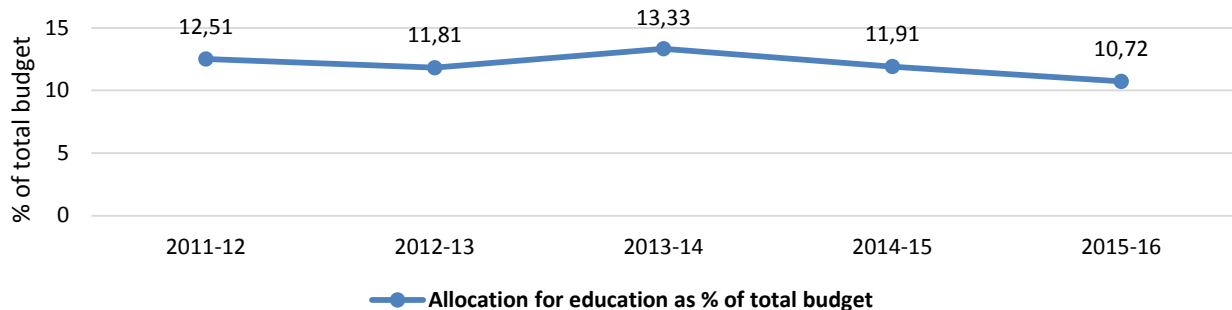
Source: Budget in Brief 2015-16, Ministry of Finance, Gov. of Bangladesh, www.mofgov.bd

The Education Sector expenditure is represented as ‘Education and Technology’ in the graph above. Under the technology part, the government allocates money to the military run universities and technical colleges. There is a strong CSO position to keep technology apart from education, but the government is reluctant to do so. This is presumably because the government does not want to show that the defence expenditure is much bigger, as it includes other associated costs, e.g. cost for military institutions. Figure 17 also shows that the allocation for social sectors like education and health has been poor. Expenditures on education and health have remained either stable or declined in relation to GDP, and certainly declined in relation to total budgetary expenditure.

6.1 Education

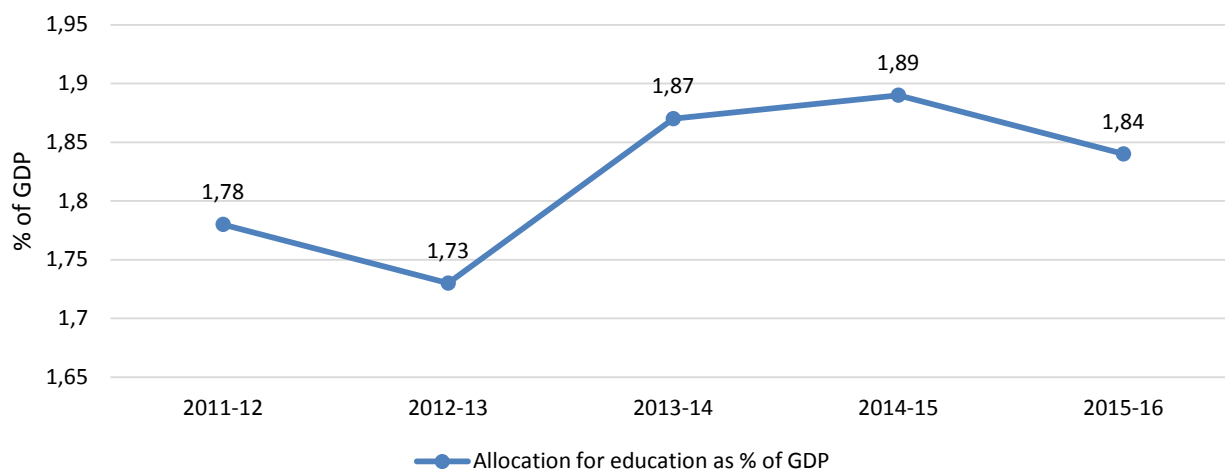
Figure 18 shows a declining trend in government spending on the education.

Figure 18: Spending on education in % of total budget, FY11-2012 to 2015-2016



Source: *Child Budget 2015-16*, http://www.mof.gov.bd/en/index.php?option=com_content&view=article&id=322&Itemid=1

Figure 19: Spending on education as % of GDP, FY11-2012 to 2015-2016



Source: Child Budget 2015-16,

http://www.mof.gov.bd/en/index.php?option=com_content&view=article&id=322&Itemid=1

Public expenditure and education in Bangladesh

The average public education spending of low-income countries is consistently higher than that of Bangladesh over the last decade, at around 3.2–3.7 percent of GDP. Almost all government schools—secular and religious—are funded by public resources, both in primary and secondary education in the form of Monthly Pay Orders (MPOs) to cover teachers' salaries. They provide free tuition and a stipend to rural female students. Teachers' salaries represent more than 90 percent of the total education budget, both at government and non-government schools, and essentially come from the revenue budget. This leaves little room for operational expenditures. According to the benefit incidence analysis, the poorer households receive more public education spending at the lower education levels, but the higher education spending is directed moved toward the richer population.

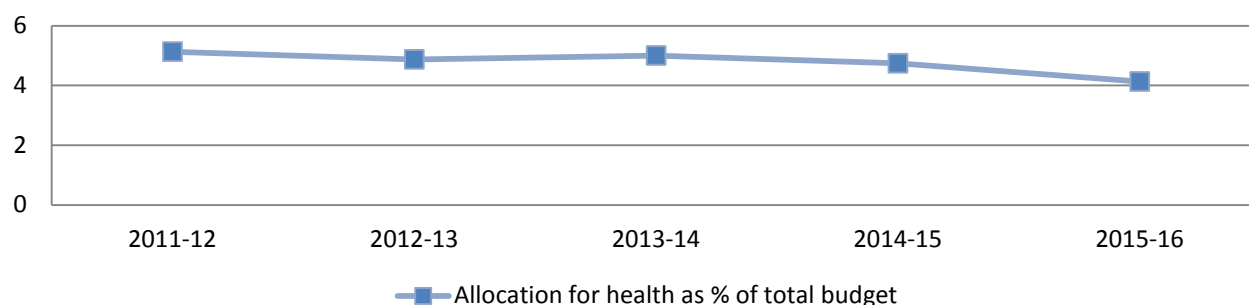
- Bangladesh has improved access and completion at all levels of education, especially at the primary level. As a result of a massive expansion of supply, targeted stipends to bring the poorest and girls into schools, and continued investments in education, Bangladesh has achieved almost universal access to primary education.
- Bangladesh has achieved gender equity in both primary and secondary education, well ahead of the Millennium Development Goal target set for 2015. Girls are ahead of boys in primary and junior secondary, but behind them in higher secondary and tertiary education completion rates.
- Repetition and dropout rates have declined, but they are still high; combined with low transition rates across various levels of education, they imply low levels of learning in the country.
- About 5 million children are still out of school, either because they did not enroll in school or dropped out very early, mostly due to poverty.
- Although Bangladesh has succeeded in providing greater educational access for its people, learning is low and unequal. An assessment of literacy and numeracy in grade 5 indicates that only 25 percent of grade 5 students master Bangla, and only 33 percent master Mathematics competencies. In grade 8, competencies in Bangla, English, and Mathematics are respectively 44, 44, and 35 percent. Regional differences exist in students' learning outcomes. Dhaka and Chittagong perform better than the national average, but performance in Rajshahi and Sylhet lags significantly behind.
- The performance difference that appears in grade 3 becomes more severe by the end of the primary education cycle, particularly so in the Barisal and Sylhet divisions. Students from poor households across the nation perform generally lower than students from wealthy households. It is estimated that the children from poor families are at least three-fourths of a school year behind their richer counterparts in Bangla, and half a school year behind in Mathematics.

Source: Bangladesh Public Expenditure and Institutional Review 2010, World Bank

6.2 Health Care

The allocation for healthcare has declined from 5.13% to 4.13% from 2012 to 2016. Figure 20 shows a declining trend in government spending on healthcare. Figure 21 shows expenditure on healthcare as % of GDP, FY11-2012 to 2015-2016.

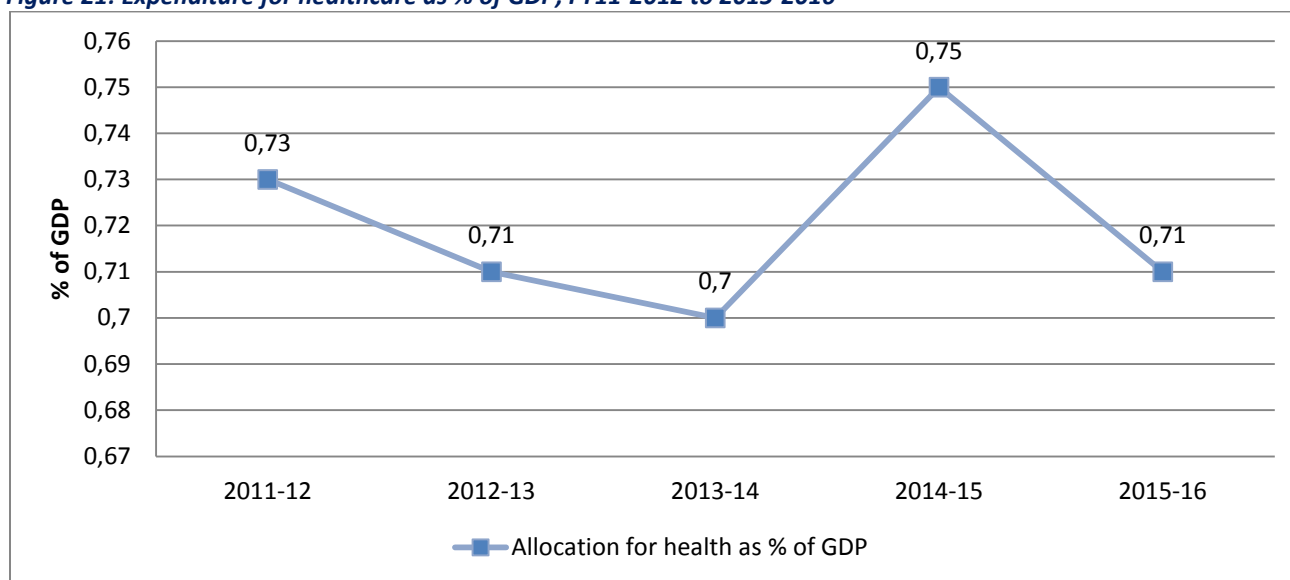
Figure 20: Spending for healthcare in % of total budget, FY11-2012 to 2015-2016



Source: Child Budget 2015-16,

http://www.mof.gov.bd/en/index.php?option=com_content&view=article&id=322&Itemid=1

Figure 21: Expenditure for healthcare as % of GDP, FY11-2012 to 2015-2016



Source: Child Budget 2015-16,

http://www.mof.gov.bd/en/index.php?option=com_content&view=article&id=322&Itemid=1

Health facilities are neither adequately funded, nor are the allocated funds effectively utilized. The allocation of resources is not pro-poor, because health services are only extended to the Upazilla level and do not reach the poor. In addition, the Upazilla based health centres are not well managed and are not equipped with the required professionals and equipment. This contributes, among other, to the wide disparities in health outcomes.⁶¹

⁶¹ Bangladesh Public Expenditure and Institutional Review, June 2010, World Bank

Government has appropriately targeted 60-65% of total resources towards the Upazila and lower administrative levels' provision of primary care. However, the disaggregated figures of revenues and development expenditures show that in recent years the proportion of expenditure going to the Upazilla and lower levels to total development expenditure has decreased from 65% in 2001/02 to 52% in 2007 (HEU 2010).⁶²

The main source of finance for total health expenditure (THE) in Bangladesh is 'out of pocket' (OOP) spending by households (64%), followed by government spending (26%), and external resources (8%). Households' cash on hand spending mostly purchase drugs (66%). Cash on hand spending also includes both formal fees (paid at public, private and NGO facilities) and informal fees (paid to informal providers).⁶³

Government spending on social sector programmes has declined in terms of total budget. In all major categories of social spending, like education, health and social protection, there is a steady decline in the level of spending compared with the total size of the budget. With spending on education and public health at about 2% of GDP and 0.7% of GDP respectively, Bangladesh cannot expect to provide the quality of education and health care services that the citizens of a middle income country would need. It will not be able to develop the skill levels of its rapidly growing labour force and transform the demographic dividend into a real acceleration of GDP and income growth.

Chapter Summary and Recommendations

Taxation has four roles: (i) it is a *source of government revenue* required to run any government; (ii) it provides finances for public services and investment (public goods), particularly at a time when the availability of finance for development (including overseas development assistance) is lean; (iii) it is a strategic tool for government to promote certain sectors with a view to supporting investment, economic growth and employment; and (iv) it is an instrument to ensure social and economic equity and justice. It is felt that the ongoing taxation reform agenda in Bangladesh is more biased towards the first two roles.⁶⁴

The allocation for education and health has been falling, major allocations are provided to feed the civil and military bureaucrats and for payment of interests on the loans of the last few years. The motives behind the loans are not the people's wellbeing. The wealthy people are exempted from paying taxes as a wealth tax is practically nonexistent. In addition, tax exemptions create and perpetuate social inequality in Bangladesh.

Most subsidies in the last few years have gone into the electricity sector. In 2012 this amount was Tk. 32,000 crore. 28,000 cores of that were spent on Quick Rental Power Plants. The large capital needed to buy electricity at a higher price from Quick Rental and the import of oil was paid from loans. The burden of these loans falls on the people. This is why interest payments comprise the largest expenditure, right after administration, in this year's budget. However, a one-time expense of Tk. 1,000 crore could have given Bangladesh the same amount of electricity if it had been spent it on the renewal, repair,

⁶² *Expanding Social Protection for Health: Towards Universal Coverage, Sept.2012, Health Economics Unit, Ministry of Health and Family Welfare, Government of Bangladesh*

⁶³ *Expanding Social Protection for Health: Towards Universal Coverage, Sept.2012, Health Economics Unit, Ministry of Health and Family Welfare, Government of Bangladesh*

⁶⁴ Towfiqul Islam Khan and Md. Zafar Sadique, 2014, *Value Added Tax and Supplementary Duty Act 2012: Concerns and Implementation Challenges*, CPD, Dhaka

maintenance, and reform of the energy sector. Bangladesh would then not have to pay subsidies and increase the amount of loans every year. Neither would it be forced to import extra oil. The economy would not be under added pressure. The allocations make it seem as if the government favours the energy sector, but in reality, the increased expenditure is to ensure good business for a few preferred groups. The result of this is the cycle of debt and the hike in costs of both electricity and oil.

Given the context the recommendations are;

- It is important to emphasize the mobilization of tax revenue with transparency and accountability to ensure more resources for public spending. If government can generate more resources from domestic sources then government can earmark more funds for public services.
- CSOs should also put pressure on the government for better public service delivery and efficient use of domestic revenue.
- The government must enhance budget allocation to the essential service sectors like health, education, social safety nets, food security etc. And ensure a balanced distribution of resources among sectors.

CHAPTER 7

Transparency and Accountability

7.1 Tax System Transparency

In terms of accountability and transparency, the tax administration does not appear accountable to taxpayers, because the tax departments always try to generate income unilaterally and without any discussion and dialogue with taxpayers. The NBR does not have any policy that ensures the publication of information on the tax system and tax collection rates. However, tax rates (direct and indirect) are available in the budget document.

The information on non-tax revenue collection targets is available with the budget proposal. However, the management is not adequately transparent. The targets set for these heads of revenue collection are often set in an arbitrary manner.

7.2 Information Availability on Companies

Certain information (e.g. company's direct shareholders) is publicly available, but only when a company is registered with the stock exchange. The information on companies' ownership or financial statements is available for all companies; however, it is not possible to find the information about companies' ultimate owners.

7.3 Audit

As a transparency measure, the NBR commissions an external body to carry out audits. The office of the Controller and Auditor General of the government of Bangladesh carries out regular audits, but not annually. The audit results are not debated in parliament and are not available publicly.

7.4 Budget Documentation

The executive budget proposal includes information on different sources of tax revenue (such as income tax or VAT), different sources of non-tax revenue (such as grants, property income, and sales of government-produced goods and services), and extra-budgetary funds for the budget year. The aforesaid information is available only three to four weeks before the end of fiscal year. As a result these figures are often not scrutinized in an adequate manner. The year-end report for the preceding year is also published in the budget proposals. However, the differences between the enacted levels and the actual outcome for revenues are not explained.

7.5 Citizens' Engagement

The Ministry of Finance meets the CSOs, think-tank organizations, business associations and professional bodies to seek their opinions on revenue generation and spending. However the views of CSOs and others are merely considered in budget decision. While there is an established process to facilitate CSOs in annual budget discussions, there is no opportunity for the CSOs to influence revenue policies at the national and local levels.

There is no grievance mechanism for citizens to complain about errors and the misconduct of tax authorities. Even while taking decisions on sensitive issues, the government does not consider the creation of mass awareness and raising people's opinion on those issues. The recent initiative of the government of Bangladesh in imposing 7.5 percent VAT on the tuition fees of private universities and private medical colleges is such a critical issue where government should have been more transparent in decision-making. There is a concern that imposing VAT on student's fees would hit middle income and lower income families and would curb the basic right to education.⁶⁵ Amid CSOs' criticism of this decision, on 9 August 2015 the High Court division issued a ruling asking the government to explain within three weeks why imposing 7.5 percent VAT on private universities would not be illegal. Finally, following a continuous protest of the private university students, government moved away from its decision of imposing VAT on students' fees.

Chapter Summary and Recommendations

There is an urgent need to improve the transparency and accountability of tax policies in Bangladesh. While a number of reforms have been initiated in recent years, civil society in Bangladesh needs to be more active to ensure the implementation of these initiatives in a timely manner. From the perspective of civil society activism in Bangladesh and in the context of promoting a fair tax system, the following recommendations are relevant:

- The enforcement of monitoring and accountability mechanism in a transparent way needs to be ensured. Towards this end, the government agencies need to ensure openness, reliability and timeliness of the tax related data.
- Tax related data also needs to be published in a user friendly manner. Make use of information technology in tax governance and make the information public.
- The tax system should be transparent and inclusive so that citizens have easy access to detailed information on revenue collection and spending. Importantly, this information must be presented in a way that is meaningful and understandable to the majority of citizens.
- Tax enforcement should be fair, so that every taxpayer is treated equally according to the law. The need for greater fairness in enforcement is thus universal, and is relevant to all of the major tax types.
- Publicly available information about revenue collection and expenditure is important at all levels of the government. It is worth noting that the media and civil society representatives have recently made demands on local councils to publish the data on revenue collection and spending.

⁶⁵ A.Z.M Arman Habib: No Vat on Education: Education should be equally accessible; published in the Daily Star on 25.08.2015.

Conclusion

Taxation is indispensable in order to support the basic function of a sustainable state and to create the context for economic growth. An improved tax system is the key to financing public services, reducing inequality, making government more accountable and helping to improve self-reliance.

Over time, the NBR has had major achievements as it invested time and efforts to achieve its objectives and to reform the tax system. The tax system in Bangladesh is gradually improving, raising more revenue and reducing the dependency on aid. However, Bangladesh is still a low tax effort country with a high buoyancy ratio, implying that the policy-makers of Bangladesh have the scope and potential to opt for greater revenue mobilization through internal resources in order to meet the budgetary deficit.

This report analyzed seven areas of the tax system: tax system in general; distribution of the tax burden and progressivity; revenue sufficiency and tax leakages; tax exemptions; effectiveness of the tax administration; government spending and transparency and accountability. With the objectives of looking into the complex character of tax systems in order to evaluate the fairness of a tax system under review.

The report reveals the situation in Bangladesh and provides a set of recommendations at the end of every chapter for a better understanding by readers. The recommendations indicate that fair taxation is possible if the government follows standard norms of policy implementation and if it improves the transparency and accountability based on participatory approaches.

The study finds that there remains a lot to improve in terms of the tax collection to achieve the desired tax to GDP ratio. Tax exemptions and tax evasion in general also contribute to the low revenue mobilization. However, tax reform is an overwhelmingly political challenge as vested interests strongly resist reform. Furthermore, the tax system continues to suffer from unfair enforcement, widespread corruption and the failure to translate the tax revenues into public services. Greater political leadership and commitment is needed to overcome the prevailing challenges.

Therefore, the role of civil society must be to generate broad-based political pressure for reform by actively engaging a wide public constituency, while the government must be willing to adopt fair tax policies and practices. The construction of institutions that are independent and easily monitored is an important strategy for curbing corruption and abuse. This should include clear processes and regulations, accompanied by dedicated enforcement capacity.

Transparency and inclusiveness are essential in fair tax systems. This implies that citizens should have detailed information about how taxes are assessed, how much tax revenue is collected and how that revenue is used. Measures to enable citizens to monitor the fairness of tax collection efforts and expenditure are crucial.

To conclude, SUPRO believes that the report covers the major areas of the tax system in Bangladesh and that it provides valuable recommendations for policy-makers and citizens. If the tax system in Bangladesh is to be improved on the basis of equity, these recommendations must be implemented at all levels of the tax administration

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