

# Tax Evasion: Need for Remodelling the System

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 away. This is the source of corruption and tax administrators must be made liable to explain why they don't treat similar cases similarly. That is what any supervision will have to deal with, not looking at particular cases and letting tax administrators justify that that particular action is okay.



**Dr. Debapriya Bhattacharya**  
 Senior Research Fellow of BIDS: There have been three excellent papers presented which were very much to the point. They argued for instilling more efficiency in the tax administration of the country. These papers are coming in the backdrop of fiscal '98-99 which has its own features being a flood year. Despite that fact, the backdrop is also drawn by such figures that the revenue GDP ratio of the country, which happens to be one of the lowest even in comparison to South Asian countries, is still stagnating with the old national income account system for the last couple of years.

There are significant apprehensions that even that 12 per cent, 12.2 per cent rate may not stick even for the '98-99 given the fact that the real rate of increase of tax collection or revenue increase is something around three per cent to four per cent. And if you are expecting a GDP growth rate of three to four per cent, then there may be a stagnation in the revenue GDP ratio which is obviously not good news at all.

The other case is that there is much desired structural change that we all wanted to bring about in the revenue structure, that is the change from indirect taxes to direct taxes and within the direct taxes, from the import-based taxes to the domestic-based taxes in some way. Those structural changes are also not forthcoming. So when we have a discussion on tax evasion and tax avoidance, obviously it has a particular implication.

We agree on a couple of general principles. Over here there is broad consensus on what needs to be done. There is a broad consensus on the expansion of the coverage of the tax base. The tax base needs to be expanded. There is no doubt about that, particularly in relation to individual tax payers as well as having more effective tax payers from the corporate sector.

There is a consensus that lower rates will have higher compliance. There is no doubt about that.

The system in which we want to have our tax administration has to be hassle-free, very low transaction cost, less discretionary power and as much as possible on the basis of self-assessment in a manner which does not create that kind of moral hazard or incentive failure which we see between the principals and the agents.

There is a need to build the capacity within the tax administration and institutional capacity building means not only improving human resource, human capital which is there in the system, but also the computerisation and other initiatives which are already on to some extent.

Let me come to two or three concrete issues. The first one is on the expansion of the tax base. In recent years, under the leadership of the current Finance Minister, some mea-

asures were taken to put in new indicators of identification of new taxpayers, such as having more than 1600 sq. ft. of dwelling in a corporation of city area, having a motor car. You need to have your TIN number while opening an LC, trade license renewal and submission of tender.

Should we pursue more this kind of indirect identification method? For example, I was with a bank. While we are now allowing new loans for house building, we are insisting that the TIN number of the person who is asking for loan be submitted.

There is another suggestion that I put forward to our bank that we are identifying a new borrower. The bank management always asked why we aren't in NBR. This is not what you see at all. Why should we be asking for a TIN number from a person who has applied for a house building. I don't know and probably an answer will be given.

Then I suggested to the bank, if we are identifying a new borrower, we go to CIB to get a clearance on what is the default status of a particular person.

What is the loan return status of that company or those who were directly involved? We want to assess the credit worthiness of that particular individual. Shouldn't we also ask the NBR whether the gentleman has something rather ask, has some unpaid VAT over there? Is that good? Some people think that given our institutional background it will create more obstruction, more rent seeking.

On the other hand, questions may arise as to whether this person had unpaid dues anywhere in the market or not. That is how it came in.

To what extent do we want to have an inter-locking system with this kind of tax and other transactions which go on in the society? That decision needs to be taken.

On the VAT issue, VAT has been stagnating in some respect and in domestic sector there may have been some deceleration as well.

VAT coverage has been expanded on 75 items. Also the service sector has been brought under the coverage. These are attempts to identify new sectors so that it is back-to-back coverage. The issue is not being able to identify those ideas well.

Even apart from that, some discussion with the small entrepreneurs brought out a very simple task that VAT domestic sector is now creating a major problem.

Something has to be done. It is not only to deal with documentation. They are ending up paying more and at the end of the day, the effective taxation is higher at this moment than not getting the real benefits which VAT promised. It is a very elegant system in theory, so that problem is very much there and as a result they are being forced to evade and the tyranny of the tax inspectors is common knowledge now.

Regarding the company corporate tax, FICCI came up with the figures that FICCI members pay 60 per cent of the corporate tax. Its a staggering figure. The NBR Chairman will be able to give us the actual figure, how many thousands of companies do actually submit returns and actually what percentage of them actually show profit. If they are not showing profit, there is something wrong with the auditing.

Here we will have to expand our issue going from not the audit of the tax itself, but the auditing of the chartered accountants, how they operate in this country. With the audits we have problems over here and a major issue which is there regarding putting in place an international standard of auditing. It is an issue very much under discussion, even the allowing of foreign auditors in the country.

The major point over here is that computerisation is going on. Then there is capacity building within the tax administration. When we really have a change within the tax administration regarding their promotion, their cadre, problems

and other things without dealing with the major problem of public administration reforms. In order to have these kind of things, legal measures and other things, it also demands some kind of a legal framework essentially enforcement of contract in a much less costly way. Even the bankruptcy act really did not give much respite in this respect. So the legal framework is the other aspect which has to grow in tandem with the tax administration.

A taxpayer is finally motivated to pay a tax if he sees its return. So the credibility of the public expenditure portfolio, the real value of the public expenditure will, to a large extent, motivate taxpayers even when they are not harassed by tax collectors.



**Mahfuz Anam, Editor of The Daily Star:** Since I am a media person, let me deal with this whole other side of the tax evasion issue. The atmosphere in which a society operates, images that are carried in the public mind, if the image is that the rich, powerful, the politically connected can get away with breaking the law, that image does far more damage to the functioning of the government, to implementation of law than anything else. If I see that I can break the law and get away with it, then the incentive to break the law by others rises. That is the crux of the problem. If I have the right political connection, if I am rich enough, I get away. I can even influence the judicial process. That is a serious problem of credibility. As a media person, I would like to highlight that.

When your government came, the Prime Minister made a promise that all the income and wealth of ministers will be made public. Now imagine the strength your government would have gained if, from day one, this practice was followed and renewed every other year, showing this was the income of this minister last year, this is the percentage of his increase and this is how much he paid tax. Unfortunately, the PM, I am told, got the information, but had kept it to herself, a very serious damage to the credibility of an honest government.

The Finance Minister a few minutes ago said that tax evasion is a citadel of corruption and that you need more time. You have been in power for almost three years. It's not really an insignificant amount of time. You have made efforts, but again, the image is that you can still get away. There had been instances of big companies with very powerful connections with ministers who were able to get away with tax evasion. We reported it in the media. Nothing happened. That eroded the credibility that reinforced the environment of evasion that we are now dealing with.

So my humble submission to the Hon'ble Minister is to reinforce the point made by Mr. Moazzem that let us have a freedom of information act. Let us make it mandatory that audit reports of big companies be made available to the public on request. The whole process of this financial auditing must be made more transparent. It can be done through the legislative process.

The story of bank directors again breaking laws, but using the process of stay order from the court has also added to the image that I can get away. Ninety per cent of obedience to the law is based on the impression that if I break the law, I will be punished. It is impossible for the police to enforce it on everybody. It is the image, the impression that if I break the law I will be punished, that actually makes discipline in the society. If the impression is reversed, that I can get away by breaking the law, then law enforcement relaxes.

It is my humble opinion that tax evasion cannot occur without direct collusion with the authorities that enforce tax. It is an unholy alliance. For an elected government of a five-year term, it is an enormous task, but a beginning has to be made. That beginning, you sir, can make and I urge you to do so.

This whole question of auditing political party funds, there is a link between tax evasion and political party funding. If a very clear auditing system could be brought about, how political parties are funded, then some of the evaded tax money perhaps would not go there. Some efforts should be made to make political party funding accountable and they should be audited and made transparent.

Election expenses is another

linkage between tax evasion because, after all, tax evasion money is black money. That money is used for political purposes. If I am evading tax and if I can get the MP of that type, he will put up with me. So we all know that three lac ceiling for a candidate in election is not really that realistic. Yet we hang on to that. The candidate spends 50 lacs on his election while the law says three lacs.



**Abdul Awal Minto, President of FBCCI:** When we talk about tax evasion, tax avoidance, obviously it centres around the people in the private sector. So representing private sector on the issue is not going to be easy for me, but even then I think in the interest of the country, I will say a few things. In a large, I agree with the keynote speech of Mr. Moazzem. Leaving Mahfuz bhai alone, I think the rest of the suggestions and the points raised, I agree more or less.

Why does the question of evasion come? High taxes, direct or indirect, is one of the fundamental reasons. I will give you the example of sugar. If sugar import would be privatised today, the consumer would get the sugar at the rate of at best 11 taka per kg. But if you buy sugar, it is 31 taka. Obviously we are encouraging smuggling because across the border it is open. Why should I pay 30 taka when I can get it at 12 taka from someone else without paying any taxes? So the high rate of taxes is one of the fundamental reasons of why people have tendency to evade taxes.

This high rate of taxes coupled with the high input in production also fundamentally causes the people to think of evading taxes. Why is it the high input of the production? We pay a lot more for energy in the production system than any of our competitors. If you add the low voltage, no power at times, peak hour rate, we pay three times more than any of my competitors. So obviously our cost of production is very high, local product it very high. Therefore it encourages smuggling. Smuggling is a way of how you can evade taxes.

The other reason is the arbitrary power at sources, whether it is income tax or customs duties. I spoke to the Chairman of NBR yesterday. One guy had told me only five days ago one commodity was assessed at 410 dollars per ton. Four days later another guy went to assess the same goods and the customs authority wanted to assess it as 1000 dollars per ton. This gentleman had to go to court, file a writ petition, get a stay order and get his goods out. In the meantime he had to pay 25 days demurrage. So the arbitrary power is one of the single most dangerous things which allows the pollution between those who pay and those who evade.

We have to attack the roots, the reason why people tend to evade.

On the income tax side, 72 to 80 per cent of the human resources we have in the taxation department are used on the people who are filing their tax returns. Yet it is so easy to find out who is avoiding their taxes. If you make a list of all the shops, all the apartment owners and find out if they are paying taxes or not, I would like to request the respected Chairman and the Minister not only to make the assessment cleaner and simpler, do not harass the people who are already filing the tax return.

None of the banks have completed their assessment beyond 1992, 1993. I am not even talking about the private companies. I am talking about companies like banks. They cannot evade any taxes. They cannot have two books. Government banks I think never file returns. The private banks are under scrutiny at every given moment of time from various sources, the income tax department, the Ministry of Finance, Bangladesh Bank. After all this, none of the banks could clear their income tax assessment beyond 1992-93. In National Bank, the last time we assessed was in 1994. We had a whole department set up to deal with the income tax department.

On corruption, the people with illegal money, obviously they are avoiding taxes. People with legal money, earning money through hard work, they probably would like to pay taxes to make it more halal. Who has the money? Only those involved in corruption.

The wealth today is not with the private sector business people. It is somewhere else. This money, I support Mr. Mahfuz

Anam, is changing the attitude, behaviour, culture of society. This money is going out of this country. This is severely limiting our investment in the country because there is hardly anybody who is making this illegal wealth, doesn't have somebody sending this money out of the country. They are changing the culture of the society. So this corruption has to be stopped. Corruption can only be stopped if accountability is there, if they are brought to the book.

If I evade tax, I have to be punished. At the same time, what about those who are helping me? How many court cases are there against them? What right have I to go against them in court? No public can oppose those people because it is out of the law. So both parties have to be brought to justice.

Now discrimination in income tax laws. In a country if some particular group doesn't have to pay tax and some do, it will obviously encourage people not to pay tax. Law has to be par. Everyone working in the government, the private sector or in business, everyone has to pay taxes. Anything less than that will not bring justice.

As far as punishment, tax evasion should be taken as a criminal act. I think not only fine, there should be a jail term. Every country which achieved something, had a jail term for tax evasion.

I agree with avoidance. If there is a loophole in the law, I will take full advantage of it. That is my right. But evasion is a criminal act and jail sentence is a must.

It is high time to restructure and reform NBR itself. Custom duties and VAT should be one and income tax a completely separate department. One has nothing to do with the other. NBR should be a place where we should go. I love to pay taxes provided I am respected there. But if I go to NBR and see that I am treated like a criminal, I am afraid of going there. So I don't go there. The mind and the attitude of the people who want to collect taxes also should be changed.

PSI is a most important element. Why was it taken out from the system. Many people including the World Bank expert have brought in force this reform about five or six years ago. Why is it eliminated? If somebody has abused the PSI system, they should be brought to justice. They should go to jail. But instead of doing that, they have eliminated the total PSI and I will request the Hon'ble Minister to please make PSI mandatory in the next budget with a punishment clause in it.

Tariff anomaly. Tariff should only be in three. The raw material, intermediary raw material and the finished product. Another one can be for the capital machinery. If we have to have seven tax ranges, five, seven, 20, 40, 50, it is very difficult to administer. So PSI will abolish tax anomaly and help a lot to boost the collection of taxes at source as well as income tax on the investment.

Then accountability. If the people with auditing powers misuse this power, there must be a law to bring them to justice. Without that, there will be no easy way out.



**Amir Khasru Mahmud Chowdhury, MP, Chairman of CSE:** My mind was working on certain areas until Mahfuz came up with his thought-provoking ideas.

We have talked about road tax a lot in the past. If we take 250 thousand vehicles, talking in the range of take 6000 per vehicle, we are having 150 crore taka straight away. If you charge more for the income generating vehicles like buses and trucks, its going to be much more than that.

In the transportation sector as a whole, including the private sector ownership, it is somewhat high. A person today buying a new car in Bangladesh is paying to the government exchequer in the range of Tk. 2-5 lacs. Actually it is same with the import duties. We are paying anything from two and a half per cent VAT and other tariff.

We should not kill the golden goose.

At the import level we should reduce. At least in the transportation sector as a whole we should bring it down to absolutely minimum, something like 50 per cent, may be a little bit less on commercial vehicles.

The monthly line rent of a cellular phone is Tk. 500 which makes Tk. 6000 per year for a phone which costs around Tk.

15,000. On the other hand, for a car worth Tk. 5-15 lacs we are paying road tax of Tk. 1200 per year using all the infrastructure. This is where we should concentrate. The road tax is the area we should use for internal resource mobilisation.

We should reduce tariff at import level on all the vehicles including private vehicles. That should bring down the cost of transportation also.

If we go from Chittagong to Dhaka we cross three bridges and between the three bridges we pay about Tk. 27. Just imagine the stretch of road from Dhaka to Chittagong we are using, paying only Tk. 27. And if you charge Tk. 100 per vehicle, I

have a figure of something around 50000 vehicles crossing, it would bring around taka 182 crore a year from road tax. So rather than killing the golden goose at the import level let people buy more cars at a cheaper rate. Let there be more transport on the road and let us earn more income from road tax.

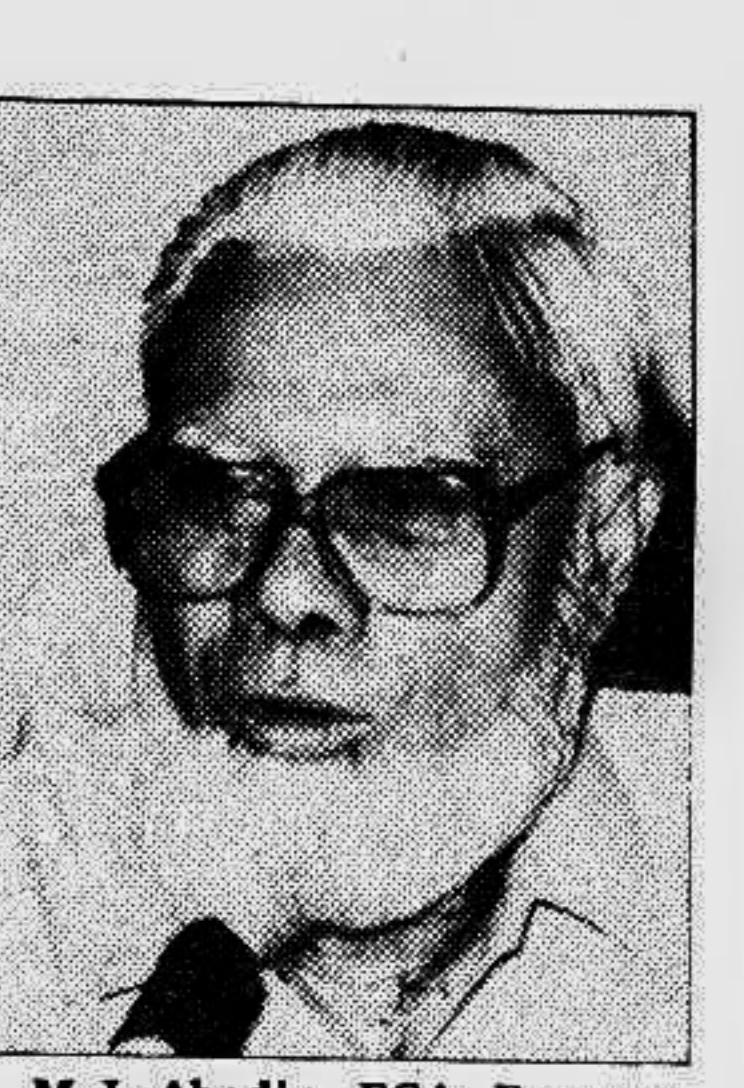
On the capital market I need to say a word or two since I represent the Stock Exchange. Looking at Indian budget this year they have done quite well since they manage to have a little boost of their capital market by totally tax exempting all the income on mutual funds. So this is an area perhaps the Finance Minister will concentrate. I would also like to request all the listed companies corporate tax to be further reduced.

Now coming back to Mahfuz's point on the MP's and ministers' income I think he is very right and he didn't go far enough. Actually we would like to see how these members of parliament or ministers or ex-ministers having no business at all, no track of business record, these politicians, members or parliament, ministers, ex-ministers have houses in Gulshan, Baridhara, Banani, Dhanmondi driving Pajero jeeps, brand new cars. We should take a list of these politicians. What is the source of their income? I am a third generation businessman turned politician because I had to step into my father's shoes. I don't own a house in Dhaka. It is so expensive I can't afford it. To own a house in Baridhara, Banani you need to be a fairly rich man. What is the source of these politicians' income? That should be a very good beginning to start.

I will go back to my original point, let us increase the road tax. Let us charge on the infrastructural facility users for using the facilities rather than having a high import tax for the transportation for the vehicles as a whole.



**Salam Talukdar, President of Bangladesh Tax Lawyers Association:** It is very difficult to say about the system we brought in. But the key-note paper presented before us touched all points about the evasion. Evasion is everywhere, some speakers said about the doctors, and about advocates. I must say not only doctors and advocates, Doctors, advocates and the professionals, and the consultants. We should think about the process of how to net the tax payers. There are so many areas where it has not been asked even. Mr. Amir Khasru pointed out correctly but in the communication sector one thing he has forgotten that a bus plying from Dhaka to Chittagong air conditioned costs about 80-90 lac taka. He did not explain the money from where he invested and at the same time he is paying over Taka 2000 income tax. In all countries like USA, UK, the lion share of this revenue, internal revenue comes from salary. But in our country its different. Government officers will not pay tax. The tax is deemed to have been paid by the government. It was a day in 1973 Bangabandhu said that the highest salary was Taka 2000 and tax deemed to have been paid by the government. But today they are not paying taxes. And the private sector shall have to pay. A country should not differentiate tax payers. Everybody should be equal in the eye of the law. This should be taken into consideration.



**M.J. Abedin, FCA, Former President of ICAD:** There is one area which provoked my mind. It is about goods manufactured in Bangladesh. Whatever the manufacturer says to the tax department, these are accounted in the hands of the traders. Suppose if a 1000 crores worth of goods is manufactured sold and disclosed to the tax department by the manufacturers, are these disclosed by traders because these go to the hands of the wholesalers. So here there is a big gap. The tax department can unearth it because all this information is with the tax department. Only what is required is cross check, cross verification which was already said by Dr. Mahmud. When the manufacturers are assessed they are supposed to submit full details of their sales and customer's names and addresses. But in the tax department they utilise those only against the manufacturer, not against the traders. So this information is collected by a particular cell, created by the NBR and this can be well utilised to catch hold of those evaders.

Another point about the auditors and our failure to detect. Taxes can only be evaded by suppressing sales, inflating expenses but by suppressing sales it is done mostly by not disclosing bank accounts, all the bank accounts. So, the auditors cannot dream of what has been not suppressed and they are not supposed to know what bank accounts are there. And for that matter National Board of Revenue or tax department cannot do anything about it. How to deal with this? How to overcome the situation? Auditors cannot do anything about it.

A point about the international accounting standard. Our institute has already adopted the standard and it has made compulsory in the case of listed companies. But who will follow the international accounting standard? It is the companies, it is the enterprises. They are to follow the standard. They must be equipped with proper persons who know what standards are there. We can only report about compliance and non-compliance. So these areas should also be taken into consideration. As the law stands now, there are provisions for penalties, prosecutions, fines - it is very much there. But there is no enforcement.

There is a zone called the investigation zone or intelligence zone but we do not find any case of prosecution, no penalties. Because it cannot be done because of some pressure. If one is caught he will get away, because it's a small country. So there is scope of link-up with high-ups - a simple telephone call will stop it. However, enforcement should be there.

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**Dr. Zaidi Sattar of the World Bank:** As an accountant one would like to say that taxes are basically distortionary. It would be nice to have a tax-free economy, that would be the least distortionary.

However, since that is not possible there is a justification of taxation. And justification of taxation comes from the justification for public spending. And this public spending as we all know is for financing delivery of public services that citizens demand. Now if it turns out that the quality of the delivery of public services like spending on education, on healthcare, on internal security, the services of the police, on national security, on public transportation and so on. If the quality of the delivery of services is on the decline, there is a ground for the citizens not to be in favour of paying taxes.

It does turn out that Bangladesh pays one of the lowest taxes in the world in terms of the tax GDP ratio. Not just in South Asia but throughout the world. From that ratio one would think that Bangladeshis are capable of paying much more taxes out of their income. And that is quite true. But when we look at the facts and when we see the kind of discriminatory treatment that tax payers receive and that has been recorded in many of the presentations, particularly from the foreign investors side, it seems to me that there is a distorted system of incentives resulting from the discriminatory tax paying system. And one would think that the distortion of the tax system itself is now being super imposed by another distortion of rampant tax evasion. I would like to suggest that and this is also universally accepted that a quality of a good tax system lies in its simplicity. A simple tax system is one way you don't have those complex wave of exemptions and allowances, etc. Unfortunately we have a tariff structure full of a complex web of exemptions and variations by products they are more similar than are different. And this is something that really needs to be looked into if the tax system, in this particular case the tariff structure is to be simplified. And simplicity is definitely one of the key ingredients of a good tax system.

Transparency is another. A transparent tax system is a good tax system. And unfortunately our panelists have already stated transparency is not the attribute of our tax system.

The other point that one might add in regard to quality of good tax system is of course rate of taxation. By any reckoning tax rates prevalent in Bangladesh appears to be on the



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