

FBR's audit policy approach

Federal Board of Revenue (FBR) is likely to approve the audit policy for year 2017 by (i) applying universal parameters for the general population of taxpayers; and (ii) risk-based sector specific parameters for different sectors including educational institutions, construction industry/builders, textiles, sugar, iron and steel and oil and gas exploration companies. This must be fully supported because there is a need for audit within several sectors/sub-sectors, for example, Independent Power Producers (IPPs) routinely claim millions of rupees for idle capacity by maintaining that the government does not have the transmission network to vacate full capacity. The question however is whether this is a new audit policy and whether FBR has the capacity to undertake this extremely challenging task?

The 2017 audit policy approach was introduced in 2016 when FBR claimed that it is a paradigm shift from the past as its focus has been 'realigned from random to parametric selection and from general to a risk-based approach.' FBR further argued at the time that the new approach would 'minimise chances of selection of compliant taxpayers resulting in increased confidence in the system...will not only promote compliance with the existing tax laws but will also generate increased revenues through better declarations for better public spending by the government. The right audit approach will help FBR in broadening the tax base and in focusing on high risk areas.' These ambitious objectives have clearly not been realised. In 2017-18 audit generated only 9 percent of total collection and in the last 10 years, tax collected by field officers through audit was never more than 7 percent of total collections.

According to data released by FBR, up to 15 September 2018, 1.55 million returns were filed while in 2003 the figure was 1.05 million and in 25 years there has been a decline in filers of tax returns by a whopping 100 percent. To boast of 1.8 million filers for 2018 with yet another extension for filers till 30 April 2019, with the first date for filing returns given by FBR as 30 September 2018, hardly gives a comfort level to the general public that those who are evading or avoiding taxes are being vigorously pursued by FBR.

The Tax Reform Commission (TRC) report identified lack of capacity to undertake any meaningful audit in FBR and recommended establishing an independent unit to conduct audit and disturbingly wrote "it is not surprising that an overwhelming number of tax audits are conducted in haste and are perfunctory." To improve effectiveness of the existing audit process, TRC further recommended reorganisation to reduce taxpayer/tax collector interface, provide pre-audit anonymity of auditors, assign and distribute functions and responsibilities in a manner that reduces discretion of assessing officers, promotes one window operation, assign functional responsibilities to specialised divisions, relieve assessing officers from non-assessment functions, and move to a systematic basis for selection of cases for tax audit. In November last year it was reported that FBR is seriously considering separating audit from FBR and creating a special Audit Division to separately handle audit. However four months later, there has not been any meaningful progress in this regard.

Be that as it may, there is no tax intelligence system in place in spite of the establishment of Pakistan Revenue Automation Limited (PRAL), a revenue market wage-based company, to effectively monitor the corporate/business sectors without which effective audit cannot be carried out.

To conclude, the need for an effective audit function is considerable and independent economists have calculated generation of an additional 200 to 300 billion rupees per annum if audit is carried out effectively.