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Evaluating FBR's performance

Federal Board of Revenue's (FBR) total tax collection in 1HFY20 is unsurprisingly off the mark, leaving serious questions marks over the fiscal side of macroeconomic stabilisation. But in light of recent economic data, the performance is perhaps not as bad as some perceive. (See BR Research's FBR's mid-term report card, Jan 3, 2020)

Let's take a look at the import side first. Considering that total imports are down nearly 17 percent in the first half ended December 2019, the 7 percent decline in direct tax collection at import stage is rather understandable. So is the 16 percent growth in sales tax collection at import stage, which was partially helped by 20 percent year-on-year average exchange rate depreciation.

If direct tax at import stage was helped by the fact that FBR decided to apply taxes at the retail price of the product, sales tax at import stage was not helped by the fact that import of crude oil and POL products was down by 19 percent and 21 percent in value and volume terms respectively, when in fact as of FY19 POL products had contributed 27 percent to total sales tax collection at import stage.

Similarly, import of vehicles contributed 8 percent to total sales tax collection at import stage last year, but that sector's import has dropped 45 percent in dollar terms in 1HFY20. Considering that no major upward revision in sales tax rates (save for the removal of zero rating) was announced in budget FY20, growth in collection at import stage despite a fall in import points towards better administration and better policy.

Now let's look at the domestic front. Consider the fact that the manufacturing sector bears the brunt of FBR's taxation. Consider also, as was highlighted in this space last week, that the country's manufacturing output has been contracting for the last five quarters with 5MFY20 witnessing a decline of nearly 6 percent in output terms. Despite this, growth in direct tax collection from domestic sources stood at 21 percent in 1HFY20, whereas growth in sales tax collection from domestic sources stood at 36 percent. (See Manufacturing recession: five quarters and counting, Jan 21, 2020)

Admittedly, this is helped by growth in prices (1HFY20 CPI at around 11%), and by rationalisation of sales tax on POL products and electricity that had a combined share of 47 percent in total domestic sales tax in FY19. Increase in domestic fuel prices and rationalisation of power tariffs must have also helped grow sales tax on electricity. But consider also that domestic POL sales dropped 5 percent in 1HFY20 in volume terms, whereas power generation output tapered off by 3 percent in 5MFY20.

The combined impact of price increase and fall in output is estimated to be around Rs60 billion, according to BR Research's back-of-the-envelope calculations, which still leaves 16 percent growth in domestic sales tax collection, a sizable growth considering that LSM is down 6 percent in 5MFY20. So, while it can be argued that collection on POL and electricity may have contributed to growth in sales tax (domestic), surely there must be other forces at play as well such as the documentation drive that is estimated to have led to 16 percent growth in non-fuel-non-electricity growth in domestic sales tax.

As for the removal of zero rating on domestic sales of export-oriented sectors, sources in FBR have told BR Research that about Rs17 billion has been collected (on net basis) under that head so far, against a full year target of Rs85 billion. Last year's collection under that account was merely Rs7 billion.

Federal Board of Revenue (FBR) does not have a great record in sharing detailed monthly or quarterly reports with the public that may shed light on its during-the-year tax collection performance. It publishes its annual report six months after the year ends, by which time stakeholders can only perform post-mortem analyses.

But in the absence of other relevant datasets such as sectoral GDP or the number of filers, facts discussed here point towards relatively better administration and better policymaking at the FBR, even as these efforts are not enough to meet the full year target. Then again, these are only initial estimates and it's just too bad that final lab results will only be available by December 2020. (See BR Research's How not to write FBR's revenue yearbook?, Dec 2, 2019)