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IMF proposal to tax salaried class on hold

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ISLAMABAD:

Prime Minister Shehbaz Sharif has deferred the approval of a politically and socially sensitive budget proposal to increase the effective income tax rate for salaried individuals, giving hopes to block the controversial condition by the International Monetary Fund (IMF). Sources told The Express Tribune that during the last meeting on the taxation proposals for the new budget, the prime minister did not endorse the condition to increase tax burden of the salaried class. Instead, the premier instructed the finance ministry to revert back to the IMF with the request to drop the proposal. Pakistan's salaried individuals are the fourth highest payers after the bank depositors, contractors and taxes collected at the import stage. Their purchasing power is sharply shrinking with constantly high double-digit inflation. Yet the global lender is after them to milk another Rs600 billion annually from salaried and non-salaried business individuals. During the first eight months of this fiscal year, the salaried individuals paid Rs216 billion in taxes. The government is aiming at a Rs12.9 trillion tax collection target for the FBR for the next fiscal year, which requires a 40% or Rs3.6 trillion increase at this year's expected collection. The idea is to recover at least Rs600 billion in additional tax from salaried and non-salaried individuals by clubbing their tax rates and adjusting the income thresholds. The sources said that the IMF has recommended rationalising the tax rates for individuals by removing the salaried and non-salaried distinction and reducing the number of rate slabs to no more than four. It has also asked to lower the income threshold for the higher-rate slabs. If the IMF's conditions are accepted and the government starts taxing the salaried and business individuals at a single income threshold by lowering the highest taxable income limit of the salaried people, the highest tax rate of 35% will apply at a monthly income of over Rs333,000. At present, business individuals are charged the 35% rate at Rs333,000 monthly income while the salaried persons' highest tax rate starts at over Rs500,000 per month salary. Salaried individuals have five tax brackets with rates of 2.5%, 12.5%, 22.5%, 27.5% and 35% and the highest tax bracket starting at an annual income of Rs6 million. The global lender has also demanded to retain the current income-tax exemption threshold at Rs50,000 monthly income instead of further relaxing it. This will adversely hit the lower middle-income groups earning from Rs51,000 to Rs100,000 a month whose purchasing power has significantly eroded due to constant double-digit inflation. The IMF is of the view that the annual non-taxable threshold is Rs600,000 was equivalent to about $2,160 at the current exchange rate, which was close to regional averages. In addition to the fear of being exposed to higher tax rates, the citizens are set to brace another wave of inflation in the shape of the withdrawal of various sales tax exemptions, which would result in an immediate increase of 18% in the prices of goods and services. The IMF management has not yet agreed to sign a staff-level agreement with Pakistan and linked the deal with the prior approval of the budget in line with its conditions and also sought the prior endorsement of the executive board of the Fund. In its set of recommendations for the budget 2025, the IMF has also asked Pakistan to withdraw all income tax credits and allowances particularly available to teachers and researchers. It wants an end to an education expense allowance and workers' welfare fund-related tax credits. The sources said that the government has also not yet taken a decision on imposing tax on the pensioners. There are official voices in favour of introducing tax on the pensions but the threshold of the pension has not yet been agreed. The sources said that the PM was not in favour of imposing tax on the pensioners. The IMF also wants to end preferential treatments to fringe benefits to employees in specific sectors and an end to the tax credit for investment in shares. It also recommended withdrawing the benefit of a reduction in tax rates for mortgage payments. The IMF has also asked Pakistan to significantly enhance penalties to improve enforcement of the tax laws, as the current penalties are not enough to deter people from violating these laws. It has recommended that a robust penalties regime is critical in enforcing tax laws and promoting tax compliance, and a review of Pakistan's tax penalty regime across various tax types to ascertain its effectiveness could be very helpful. The IMF has also asked to repeal the discretionary power of FBR to award tax incentives for industrialists besides seeking an end to the discretionary power of the cabinet to award tax incentives.