



বাংলাদেশের উন্নয়নের স্বাধীন পর্যালোচনা

CPD's Budget Recommendations for FY2020-21

*Submitted to
National Board of Revenue (NBR), Bangladesh*

Centre for Policy Dialogue (CPD)
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1. Fiscal Stance for the National Budget for FY2021

State of the economy on the eve of FY2021

During the first eight months of fiscal year (FY) 2020, major economic indicators of Bangladesh economy have exhibited some worrying signals. Barring a healthy remittance flow, performance of the external sector has been negative. Remittance earnings registered a growth of 20.1 per cent in the first eight months of FY2020. Both export and import, during the first eight months of FY2020, were negative. While export earnings grew at (-) 4.8 per cent during the first eight months of FY2020, imports grew by (-) 4.4 per cent in the first seven months of FY2020. Foreign Direct Investment (FDI) increased by only 4.0 per cent during the first seven months of FY2020 compared to FY2019. The balance of payment (BoP) position remained rather weak as of January 2020.

Along with subdued economic parameters, state of macroeconomic management also evinced disquieting signals as can be gleaned from available data till date. Progress in terms of both public expenditure and domestic resource mobilisation have been below the targets set for FY2020. Available data on public finance indicate that actual spending under the Annual Development Programme (ADP) during the first eight months of FY2020 was 38.5 per cent of the originally planned allocation of Tk. 202,721 crore. This is 0.3 percentage point lower than the corresponding figures of FY2019. In FY2019, total revenue-GDP ratio was as low as 9.9 per cent and the tax-GDP ratio was only 8.9 per cent. To contrast, the respective targets set out in the Seventh Five Year Plan (7FYP) were 15.1 per cent and 13.1 per cent. The projected figures in the 7FYP for FY2020 were 16.1 per cent and 14.1 per cent. The actual performance in the first six months of FY2020 has been way below the targets. Indeed, if the revenue targets are to be fulfilled, revenue collection has to grow by 87.5 per cent over the remaining six months of FY2020.

In FY2019, revenue shortfall i.e. the gap between revenue mobilisation target set in the budget and actual attainment was Tk. 87,402 crore. It is worth mentioning here that the

Centre for Policy Dialogue (CPD) had earlier projected that the revenue shortfall in FY2019 would be in the range of Tk. 85,000 crore. Tax revenue constituted 91.5 per cent of this shortfall while the remainder originated from non-tax revenue. Taking cognisance of the current trends, CPD has now projected that, the total revenue shortfall in FY2020 may reach Tk. 100,000 crore. Consequently, the fiscal deficit as percentage of GDP will be higher than the target figure of 5.0 per cent. These estimations are based on available data from the Ministry of Finance (MoF).

The emerging scenario in the backdrop of COVID-19

While the economy was already facing stress on different fronts, the novel coronavirus (COVID-19) has turned a disquieting situation. Uncertainty in the global economy in view of COVID-19 and consequent repercussions for Bangladesh economy is already creating added pressure both from the demand side and from the supply side. This in turn will have adverse implications for revenue mobilisation during the remainder of FY2020 and also beyond. This will originate from lower collection of revenue from customs duty, value added tax (VAT) and supplementary duty (SD) at the import stage due to downturn in trade, particularly that of import payments (on account of both price effect and quantity effect). Shut down of enterprises, job losses and income reduction will lead to lower income tax collection. Affected private and multinational companies suffering revenue losses will likely to pay lower corporate tax.

On the other hand, the government is also having to incur unforeseen immediate expenditures. These include expenditure for medical accessories and equipment, stimulus package for enterprises and direct income support for the low-income groups in the informal sector and the vulnerable groups. The government may also go for open market sale of food at subsidised prices for the poor families.

CPD feels that in view of the current trends in revenue collection and public expenditure, budget deficit may increase to 5.5 per cent of GDP in FY2020. Depending on the extent of COVID-19 and associated costs and policy measures, this may rise further. Higher demand for cash incentives in the wake of COVID-19 may put additional fiscal pressure.

Fiscal stance in view of COVID-19

To address the health emergencies of COVID-19, to help mitigate the risks and shocks originating from COVID-19, to stimulate domestic demand at a time of reduced income and livelihood opportunities and to strengthen supply side response, the government will need to pursue an expansionary fiscal policy and go for expanded public expenditure in view of the budget for FY2021. The shock absorption capacity of Bangladesh economy will critically hinge on efficacy of how this is done to stimulate demand, generate supply response and create employment opportunities. Increased budget deficit should be managed through prudent reallocation and prioritisation of public expenditure. The COVID-19 situation emphasises the need for higher allocation for the health sector. Sadly, the share of health budget is only 0.9 per cent of Gross Domestic Product (GDP) of Bangladesh. This is even lower than the target of 1.12 per cent of GDP set out in Bangladesh's 7FYP. Hence, out-of-pocket expenditure on healthcare in Bangladesh is 71.9 per cent of the current personal health expenditure, which is the highest in South Asia.

Since the expansionary fiscal public expenditure stance will need to be pursued at a time of weakened fiscal-budgetary scenario, and shrinking fiscal space, there must be renewed efforts towards both better mobilisation of resources and raising efficacy of public expenditure. These aspects must be reflected in the budgetary proposals for FY2021 and their implementation. The fiscal space to be created due to higher budget deficit should be used efficiently and with inclusivity.

In view of the above, the NBR should prepare its Budget FY2021 proposals by pursuing the following approach.

- i. It will be critically important for the NBR to set its revenue mobilisation targets in a more prudent manner. Overambitious target setting may lead to weak macroeconomic management as has been the case in the recent past. This will help the Ministry of Finance to balance public expenditure in view of realistic estimates of resource mobilisation.
- ii. The NBR should design its proposals for tax measures considering both the mitigation urgency and the subsequent economic recovery in view of the ongoing Coronavirus pandemic. The NBR will be well-advised to revisit its current fiscal incentives to this end with a view to reprioritisation and restructuring.

- iii. This year, it will be difficult for the NBR to raise tax rates or expanding the tax net to include new sectors. The primary focus should be to strengthen monitoring and enforcement mechanisms to effectively curb tax evasion and illicit financial flows (IFFs).
- iv. The immediate task of addressing the adverse effects COVID-19 should not deter the NBR from prioritising implementation of medium-term reform plans. It will be of crucial importance to accelerate the preparatory works to this end so that the reforms are effectively implemented at the earliest. The unfinished ongoing reform agendas including full implementation of the VAT and SD Act should be accorded the attention that the tasks deserve.

Pursuing the above will help avoid the temptation and risks of a ballooning fiscal deficit in view of FY2021 budget.

Focus of the document

In a recent review of the economy carried out by the CPD it was noted that domestic supply chains concerning major economic activities are being severely disrupted in view of the outbreak of COVID-19 which has been rolling out since January 2020. To address the emerging challenges, the government has announced a number of fiscal, monetary and sector-specific measures in March 2020. Considering the economy-wide impact of the corona outbreak, these measures may at best be considered as only the initial policy response on the part of the government. It is expected that more comprehensive fiscal, monetary and sectoral measures will be announced in the upcoming national budget for FY2020-21 and even before the national budget. The present document prepared by CPD comes up with a set of suggestions for consideration by the NBR in view of the upcoming FY2021 budget. These proposals include both sector specific suggestions and also the needed reforms and measures to raise NBR's administrative capacity. CPD's proposal on selected fiscal budgetary reforms and measures focus on domestic and external sectors which are under the jurisdiction of the NBR.

2. Proposals for Fiscal Measures concerning Domestic Economic Activities and External Sectors

Proposed Fiscal Measures for Agro-based Economic Activities

Major affected agro-based economic activities include poultry, livestock and dairy sectors, and SMEs with businesses concerning poultry- and fish-feed and processed food; and production and export of crab and eel (CPD, 2020). The transmission channels of disruption affecting the agro-based supply chains are: loss of production and low price due to restrictions in movement of transport and people during shut down period; difficulty in storage of perishable products; disruptions in imports of raw materials and their delivery at the factory gate, discontinuation and delays in export to China and other countries. To mitigate the risks, help cope with the losses and improve cash flow situation, enterprises and farmers/producers in the agro-based supply chains will need targeted fiscal policy support.

- The NBR may consider several fiscal measures for the affected agro-based industries which could include waiver of VAT at the domestic stage for the period March-June, 2020, deferred payment of quarterly advance income taxes till June, 2020 and payment of corporate taxes for FY2020 by instalments till March, 2021. These waivers could be continued in FY2020 budget. Besides, companies which are in loss-making position during FY2020 may be allowed to 'carry back losses' against the taxable profits for the two previous years: FY2018 and FY2019.

Farmers producing perishable goods such as chillies, cauliflowers, leaf vegetables, tomato etc. were affected by drop in sales, low market price and disruptions in the movement of goods to wholesale markets.

- There is limited scope to address the challenges faced by these farmers' through fiscal measures. Best way to go will be to provide them with low-interest credit facility before the next planting season.

In view of urban to rural migration and lower number of workers going abroad for overseas jobs, it is likely that there will be increased pressure on rural labour market.

- NBR may consider following 'go slow' policy as regards incentivising labour-displacing mechanisation. Further reduction of duties at import stage for agricultural

machineries (TTI: 12.4-27.5 per cent) should be stalled perhaps till FY2022. Similarly, disbursement of credit at subsidised rate to farmers for agricultural mechanisation should be slowed down in the next one year.

Proposals for Fiscal Measures for the Manufacturing and Service Sectors

Manufacturing enterprises are being affected differently and in different degrees depending on type of the activities, size and locations. Most are being adversely affected because of disruptions in the supply chains and demand depression. These include finished leather and leather goods, garments accessories and packaging, pharmaceuticals, cosmetics, and toiletries, woven and knit garments, live and chilled food, plastic, electrical merchandise manufacturers industry, jute spinners industry, medical instrument and hospital equipment, eyeglass, computer & computer accessories, electronics, jute spinning, medical instrument, and hospital equipment. Many domestic market-oriented SMEs are being affected due to the closing down of economic activities. Particularly those enterprises that are dependent on sales during the festival of 'Pohela Boishakh' in April, 2020 will be most hard hit. Major affected service-oriented industries and activities include travel and tourism-related activities such as airlines, air cargo carriers, tourists, hotel, MICE (meetings, incentives, conferences, and events); wholesale and retail trade, transport including app-based transport, hotel and restaurants, hospitals & clinics, media and petty businesses.

Main transmission channels of the disruption include cancellation/withholding/deferment of export orders, difficulty in the import of raw materials particularly from China and rise in the price of imported raw materials, loss of income due to shut down of economic activities, payment of workers' wages and in extreme cases, shut down of factories/businesses. In general, these enterprises are facing challenges owing to rising cost of raw materials, limited cash flow and loss of earnings and profit.

- The government has announced a number of monetary and sector-specific measures in March, 2020 which include deferred payment of loan-instalment, deferred payment of fees of public utilities without late charge, an extension of time for payment of the bill of entry of import-related L/Cs, reduction of repo rate and CRR to increase money flow in the economy. Besides, the government has announced a Tk.5000 crore package for export-oriented industries to meet the expenses related to wages and salaries.

However, the coverage of the package should be broad-based; it should include enterprises exporting below 80 per cent of their production (and those do deemed exports) such as textiles, accessories, processed and frozen food, footwear, pharmaceuticals, plastic and ceramic etc.

- Besides, the NBR may consider a number of support measures which include increased depreciation of assets for companies for two years: FY2020 and FY2021, special reduced rate of VAT for the domestic purchase of goods and services for six months, relief from penalties and interest for tax-related payments till December, 2020, deferred payment of quarterly advance income taxes till June, 2020 and relief of VAT during the period of January-June, 2020 for travel and tourism sectors/related activities.
- The NBR should consider allowing domestic and export-oriented companies to pay their corporate taxes for FY2020 in instalments, perhaps by March, 2021. Besides, companies may be allowed to 'carry back losses' that are in a loss-making position in 2020 against the taxable profits for the two previous years (FY 2018 and FY2019).
- Considering the adverse financial condition facing particularly by cottage, micro and SMEs, the NBR may consider raising tax exempted yearly turnover limit for SMEs from Tk. 50 lakh to Tk. 1.0 crore for the year FY2020 and FY2021. Indeed, domestic market-oriented industries, particularly cottage and MSMEs, need a special package with a revolving loan fund facility at a subsidised interest rate.
- The NBR can consider a reduced rate of corporate taxes against the earnings during fourth quarter (March-June, 2020) of the FY2020 and first quarter (July-September, 2020) of the FY2021 for pharmaceutical companies, hospitals, clinics, and other health facilities that are involved in the production of medicines and in prevention, diagnosis, control, attention, and treatment. Besides, it may consider introduction of tax credits for amounts paid by businesses to sanitize work premises for FY2020.
- Doctors, nurses, and other support staffs working in hospitals with corona patients and related matters may be incentivised through offer of special financial package either through one-time bonus (in public entities) or through reduced rate of taxes on their income (in private entities) for FY2020. Hospitals, clinics, diagnostics, and laboratory involved in corona related treatment and research should get a waiver as regards advance income taxes for the period of March, 2020 to June, 2020.

- Grants or donations in cash for the prevention, diagnosis, control, attention, and treatment of the COVID-19 in favour of authorized public and private hospitals and clinics, should not be considered taxable for FY2020.

Proposed Fiscal Measures at the Individual Level

At the household and individual levels, the main affected segments are low-income earners and the marginalised people. Major transmission channels of disruptions at the individual and household levels include loss of employment and income opportunities and livelihoods, high price of essential commodities and consequent erosion of purchasing power. Besides, access and availability of essentials are also an emerging concern at household levels because of because of limited supply in the market.

- The government has announced a number of support measures for the marginalised people in March, 2020 which include operation of VGD and VGF, operation of OMS services, selling rice at a subsidised price of Tk.10, and food support for six months under social safety net programmes at the district levels. Government should prepare a list of all eligible beneficiaries for an expanded social safety net programme that would cover maximum number of needy people.
- In the FY2021 budget, the NBR should raising the consider tax-free income threshold levels from Tk.250,000 to Tk.350,000. Besides, it may consider restructuring the first three slabs of income tax from 10 per cent, 15 per cent, and 20 per cent to 5 per cent, 10 per cent, and 15 per cent respectively at least for next two years. Moreover, NBR may consider allowing payment of individual income taxes for FY2020, by instalments, by March 2021.

Keeping food prices low should be seen as a strategic objective of the NBR in FY2021. Food security of low-income people during the period of uncertainties of the corona outbreak must be seen with utmost importance. Reduction of import related tariffs (such as AIT and VAT) on essential food items such as onion, lentil, garlic, ginger and soybean oil etc. should be considered on a dynamic of basis based on evolving market condition in terms of price, supply situation and projections about production.

3. Proposals related to reforms and strengthening of administrative capacity

At a time when the government is under immense pressure to pursue an expansionary fiscal-budgetary stance, every effort should be taken to create fiscal space by taking appropriate measures to deal with tax evasion, tax avoidance and illicit financial outflows. Maximum effort should be deployed to raise efficiency of the tax administration and efficacy of tools. NBR will need to raise its institutional capacity and enforcement ability through reforms and concrete actions on the ground.

Reforms

- For the upcoming FY2021 budget, a viable completion timeline should be chalked out for reforms which are already under consideration (e.g. Customs Act and Direct Tax Act), so that the implementation process can be set off as early as possible.
- Broader use of technology may bring forth some uptick in revenue mobilisation efficiency. CPD urges NBR to introduce an e-TDS system to this end. This system will enable NBR to issue tax certificates against an e-TIN linked to the ‘tax-deducted-at-source (TDS)’ collection system. This will make evasion of TDS difficult.
- CPD would like to reiterate its earlier proposals urging the NBR to initiate wealth and property tax in Bangladesh. Also, an inheritance tax, informed by global best practices, may also be introduced. Besides mobilising additional revenue, such initiatives could also provide an opportunity to build a more equitable society.
- CPD stresses that NBR should introduce taxes for proxies for pollution by tax region as has been mentioned in the “Public Financial Management (PFM) Action Plan 2018-2023 to implement The PFM Reform Strategy 2016-2021”. This will provide NBR a new and desirable source of tax revenues.
- The existing black money whitening facility through voluntary disclosure of undisclosed income discourages honest taxpayers while tax evaders are encouraged. This provision should not be continued from the next fiscal year. It has also failed to register any notable response. To tackle the problem of black money, a Benami Property Bill may be introduced as was suggested earlier by CPD.

Administrative capacity

- Under the online-based new VAT law it is mandatory for the shop owners and business entity to keep records of VAT challan/invoices during sales/supply through Electronic Fiscal Device (EFD) and Sales Data Controller (SDC). To this end, the planned procurement and installation of the devices by NBR must be accelerated in order to ensure effective implementation and augment revenue. At the same time, incomplete components of the VAT online project must be completed in a comprehensive and timely manner so that a hassle-free submission of VAT returns can be ensured.
- Since automation is an integral part of the new VAT regime, NBR should eliminate all hurdles with regard to registration and getting BINs, updating information, installation of devices and submission of returns. It should also clarify the ambiguities concerning the VAT law including central registration system, exemption and registration threshold, definitional complexities to businesses and stakeholders in line with PFM Action Plan 2018-23.
- In order to increase the number of effective taxpayers, the NBR, using their e-TIN database, could identify and pursue individuals and business entities who are registered in the system but do not submit tax returns and who are registered and submit returns but do not effectively pay taxes. A mechanism could be set up to contact the relevant entities via phone calls, SMSs or emails to follow up on their return submissions or tax payments.
- NBR should launch a comprehensive on-line payment system for VAT, income tax and customs together with an interface with iBAS++ and ensure harmonisation and taxpayer data sharing across various wings of the NBR as has been envisaged in the PFM Action Plan 2018-23 at the earliest.
- NBR must be restrained from all ad-hoc provisions of tax incentives. NBR needs to be selective in the next fiscal year as more demand for incentives will be lined up in the wake of COVID-19. Proper cost-benefit analysis must be conducted in case of new provisions. At the same time, some of the existing provisions should be reviewed and discontinued if deemed as of low priority.
- All kinds of tax evasions and resulting IFFs need to be curbed. Bangladesh loses a sizable amount of resources as a consequence of IFF. Coordinated efforts by several policy actors including Anti-Corruption Commission (ACC), Criminal Investigation

Department (CID) of Bangladesh Police, Department of Narcotics Control (DNC), Bangladesh Financial Intelligence Unit (BFIU) of the Bangladesh Bank, and Customs Intelligence and Investigation Directorate (CIID), Central Intelligence Cell (CIC), VAT Audit, Intelligence and Investigation Directorate of the NBR will be required to implement the National Strategy for Prevention of Money Laundering and Combating Financing of Terrorism (NSPMLCFT) 2019-21 in all areas related to tax evasion and IFF.

- NBR in the next budget should particularly focus on few of the activities under NSPMLCFT which are scheduled to be implemented by June 2021. Some of these are: i) conduct a study on TBML in order to find out vulnerable channels, products, payment methods and magnitude; and, ii) establish connectivity of BFIU with ASYCUDA world of NBR.
- Available data from international sources suggests that the major part of the IFF was on account of trade mis invoicing. Transfer Pricing Cell (TPC) of NBR should work very closely with BFIU and CIID to curb trade-based money launderings (TBML). To carry out its responsibilities in an effective manner, TPC should be adequately endowed with the required financial, technical and human resource capacities in the upcoming budget.
- NBR needs to emphasise the need for a comprehensive database on expatriates working in Bangladesh. Their income and outward remittance must be included in the database to address the issue of wide-ranging tax evasion. To this end, NBR, Special Branch (SB) of Police, National Security Intelligence (NSI), Bangladesh Investment Development Authority (BIDA), Bangladesh Export Processing Zones Authority (BEPZA), NGO Affairs Bureau must devise a collaborative mechanism to cope with the problem. NBR should take the lead in view of this.

Reference

CPD, 2020. "Health and Economic Risks of Corona Pandemic and Recommendations" presentation made at virtual media briefing on 21st March 2020 by the Centre for Policy Dialogue (CPD). Available at <https://cpd.org.bd/wp-content/uploads/2020/03/Download-Presentation-Economy-in-the-time-of-Corona-21-March-2020.pdf>, accessed on 2nd April 2020.