Giving Voice, Promoting Inclusive Policy

CENTRE FOR POLICY DIALOGUE

POLICY BRIEF

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Highlights

The NBR should set its revenue mobilisation targets in a manner which is doable and will not weaken the macroeconomic management.

The NBR should design tax measures and revisit its current fiscal incentives considering the ongoing COVID-19 crisis.

This year, the primary focus of the NBR should be strengthening the monitoring and enforcement mechanisms to effectively curb tax evasion and illicit financial flows.

The NBR should continue to implement its medium-term reform plans including full implementation of the VAT and SD Act.

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Budget Recommendations for FY2021

Fiscal Stance of the National Budget[1] 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 (Bangladesh Bank, 2020). Both export and import, during the first eight months of FY2020, were negative (Bangladesh Bank, 2020). Export earnings grew at (-) 4.8 per cent during the first eight months of FY2020 and imports grew by (-) 4.4 per cent in the first seven months of FY2020 (Bangladesh Bank, 2020). Foreign Direct Investment (FDI) increased by only 4.0 per cent during the first seven months of FY2020 compared to FY2019 (Bangladesh Bank, 2020). The balance of payment position remained rather weak as of January 2020 (Bangladesh Bank, 2020).

Along with subdued economic parameters, the 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 has been below the targets set for FY2020. Available data on public finance indicate that actual spending under the Annual Development Programme during the first eight months of FY2020 was 38.5 per cent of the originally planned allocation of Bangladeshi Taka (BDT) 202,721 crore (IMED, 2020). This is 0.3 percentage point lower than the corresponding figures of FY2019. The total revenue-GDP ratio was as low as 9.9 per cent and the tax-GDP ratio was only 8.9 per cent in FY2019 (MoF, 2020). To contrast, the respective targets set out in the Seventh Five Year Plan (7FYP) were 15.1 per cent and 13.1 per cent respectively (GED, 2015). 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 (MoF, 2020).

In FY2019, revenue shortfall i.e. the gap between revenue mobilisation targets set in the budget and actual attainment was BDT 87,402 crore. It is worth mentioning here that CPD had earlier projected that the revenue shortfall in FY2019 would be in the range of BDT 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 BDT 100,000 crore. Consequently, the fiscal deficit as a percentage of gross domestic product (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) (MoF, 2020).

The emerging scenario in the backdrop of COVID-19

While the economy was already facing stress on different fronts, the novel coronavirus has turned a disquieting situation. Uncertainty in the global economy given the context of COVID-19 and consequent repercussions for Bangladesh economy are already creating added pressure both from the demand and supply side. This, in turn, will have adverse implications

[1] Recently, the Centre for Policy Dialogue (CPD) has submitted its Budget Recommendations for FY2021 to the National Board of Revenue (NBR), Bangladesh. This policy brief contains the abridged version of those recommendations.

for revenue mobilisation during the remainder of FY2020 and also beyond. This will originate from the 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 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 also has to incur unforeseen immediate expenditures. These include expenditure for medical accessories and equipment, the stimulus package for enterprises and direct income support for the low-income groups in the informal sector and the vulnerable groups. The government will also go for open market sale (OMS) 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 the 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 GDP of Bangladesh (MoF, 2019). This is even lower than the target of 1.12 per cent of GDP set out in Bangladesh's 7FYP (GED, 2015). 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 (World Bank, 2020).

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 the efficacy of public expenditure. 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.

- It will be critically important for the NBR to set its revenue mobilisation targets in a more prudent manner. This will help the MoF to balance public expenditure in view of realistic estimates of resource mobilisation.
- The NBR should revisit its current fiscal incentives to this end with a view to reprioritisation and restructuring.
- This year, it will be difficult for the NBR to raise tax expanding the tax net to include new sectors. The primary focus should be strengthen monitoring and enforcement mechanisms to effectively curb tax evasion and illicit financial flows (IFFs).
- The immediate task of addressing the adverse effects COVID-19 should not deter the NBR from prioritising implementation of medium-term reform plans including full implementation of the VAT and SD Act.

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.

Proposals for Fiscal Measures concerning Domestic Economic Activities and External Sectors

Proposed fiscal measures for agro-based economic activities

- The NBR may consider several fiscal measures for the affected agro-based industries. These may include a 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 making losses during FY2020 may be allowed to 'carry back losses' against the taxable profits for the two previous years, FY2018 and FY2019.
- There is limited scope to address the challenges faced by these farmers' through fiscal measures. The best way to go will be to provide them low-interest credit facility before the next planting season.
- The NBR may consider following a 'go slow' policy as regards incentivising labour-displacing mechanisation. Further reduction of duties at import stage for agricultural machinery (Total Tax Incidence: 12.4 - 27.5 per cent) should be stalled perhaps till FY2022. Similarly, disbursement of credit at a subsidised rate to farmers for agricultural mechanisation should be slowed down in the next one year.

Proposals for fiscal measures for the manufacturing and services sectors

- 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 letter of credits, reduction of repo rate and Cash Reserve Ratio to increase liquidity in the economy. Besides, the government has announced a BDT 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 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 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.

- The NBR should assess 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 FY2018 and FY2019.

- Considering the adverse financial condition facing particularly by cottage, micro and small and medium enterprises (SMEs), the NBR may review raising tax exempted yearly turnover limit for SMEs from BDT 50 lakh to BDT 1.0 crore for FY2020 and FY2021. Indeed, domestic market-oriented industries, particularly cottage and micro, small and medium enterprises (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 also consider introduction of tax credits for amounts paid by businesses to sanitise work premises for FY2020.

- Doctors, nurses, and other support staff 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 tax 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 the authorised public and private hospitals and clinics, should not be considered taxable for FY2020.

Proposed fiscal measures at the individual level

- The government has announced a number of support measures for the marginalised people in March 2020 which include operation of Vulnerable Group Development (VGD) and Vulnerable Group Feeding (VGF), operation of OMS services, selling rice at a subsidised price of BDT 10, and food support for six months under social safety net programmes (SSNPs) at the district levels. The government should prepare a list of all eligible beneficiaries for expanded SSNPs that would cover maximum number of needy people.

- The NBR should consider raising the tax-free income threshold levels from BDT 250,000 to BDT 350,000. Further, it may review 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 the next two years. Moreover, the NBR may consider allowing payment of individual income taxes for FY2020, by instalments, by March 2021.

- 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 basis based on price, supply situation and projections about production.

Proposals related to Reforms and Strengthening of Administrative Capacity

Reform measures to be taken

- 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 the NBR to introduce an e-TDS system to this end. This system will enable the NBR to issue tax certificates against an electronic Tax Identification Number (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 the NBR should introduce taxes for proxies for pollution by tax region as mentioned in the "Public Financial Management (PFM) Action Plan 2018-2023 to implement The PFM Reform Strategy 2016-2021." This will provide the NBR with 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. As suggested earlier by CPD, a Benami Property Bill could be introduced to tackle the problem of black money.

Administrative capacity should be strengthened

- 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 the 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, the NBR should eliminate all hurdles regarding registration and getting Business Identification Numbers (BINs), updating information, installation of devices and submission of returns. It should also clarify the ambiguities concerning the VAT law including a 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.

- The NBR should launch a comprehensive online 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.

- The NBR must be restrained from all ad-hoc provisions of tax incentives. The 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. The 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.

- The 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 trade-based money launderings (TBML) in order to find out vulnerable channels, products, payment methods and magnitude; and, ii) establish connectivity of BFIU with ASYCUDA world of the 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 the NBR should work very closely with BFIU and CIID to curb 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.

- The 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, the NBR, the Special Branch of Police, the National Security Intelligence, Bangladesh Investment Development Authority, Bangladesh Export Processing Zones Authority, and the NGO Affairs Bureau must devise a collaborative mechanism to cope with the problem. The NBR should take the lead here.

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Independent Review of IRBD Bangladesh's Development

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