"Accessing the Underground Economy: A Study of 3 Incentive Programmes of the National Board of Revenue"

A Dissertation

By

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Abstract

For developing countries tax policy is determined primarily by the abilities of its tax administration rather than optimum tax theory. Providing incentives is a common practice to encourage tax payment as opposed to curbing tax evasion through enforcement of laws. The National Board of Revenue in Bangladesh offers many incentives, both permanent and short term, to encourage tax compliance. The purpose of this paper is to assess through the study of three incentive programmes of the NBR whether they are effective in increasing the collect of revenue from the underground economy or act as disincentives to tax compliance. Findings show that while in the short run, revenue is increased the long term effect on tax compliance is inconclusive. Greater steps need to be taken to improve tax administration to reduce reliance on such incentives.

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Asma Dina Ghani

Abbreviations/Glossary

1. NBR - - National Board Of Revenue
2. EPZ - - Export Processing Zone
3. TIN - - Taxpayer Identification Number
4. BIN - - Business Identification Number
5. Assessee - - Tax Payer
6. SRO - - Statutory Regulatory Order
7. CIC - - Central Intelligence Cell
8. VAT - - Value Added Tax
9. Circle - - Tax Field Office
10. Tax Zone - - Largest Administrative Body of the Tax Dept.
11. Crore - - 10 million
12. OECD - - Organization for Economic Development and Cooperation
13. UE - - Underground Economy
14. NGO - - Non Government Organization
15. AIT - - Advance Income Tax
16. LDC - - Lower Division Clerk

Chapter 1

Introduction

1.1 Background

In the post cold war era developing countries have found it more difficult to finance their expenditure through foreign aid and have had to rely on their internal revenue collecting abilities to prop up required level of funds. Various policies have been implemented to boost revenue earnings based on either donor prescription, or home grown remedies all of which have had varying degrees of success, failure or ineffectiveness When formulating policies, either as a result of lack of expertise or insight, a holistic assessment is not made of the ramifications of each policy as a result of which the policy either fails to improve revenue collection or in some cases have led to the reduction of revenue. Bangladesh is no exception to the general trend. Since the 1990s, a number of reforms have been introduced and resources allocated to improve the efficiency of the National Board of Revenue (NBR), the apex government institution given the responsibility to collect tax revenue.

In the opinion of Tanzi and Howell (2000) most developing countries suffer from four major problems which prevent them from establishing effective and efficient tax systems; economies that reduce the possibility of achieving high tax levels and the reliance on modern taxes such as value added taxes and personal income taxes; tax administrations with limited capabilities; poor availability of reliable data; and a political set up which is less amenable to rational tax policy. As a consequence of all these problems countries often develop tax systems that allow them to exploit whatever options they have rather than develop modern and efficient tax systems.

1.2 Situation in Bangladesh

Bangladesh is faced with the similar problems. Bangladesh is characterized by a large agricultural sector which is, in the most part, untaxed, a large informal sector which exists mainly to evade and avoid taxes, a public sector which remains the largest single employer and whose employees do not pay tax on their salaries and many small businesses. All these characteristics reduce the possibility of achieving high tax levels and the possibility of relying heavily on certain modern taxes, such as personal income taxes and value-added taxes.

Despite attracting the best graduates almost each year to the Income Tax and the Customs and Excise Cadres, insufficient resources to pay them good wages and to buy the necessary equipment and provide them with logistic support and to give them specialized training makes it difficult to create an efficient tax administration.

The large volume of informal activities which go unreported, limited reporting requirements, the use of out dated techniques makes it difficult for statistical and tax offices to generate reliable and detailed statistics. Many offices in the public sector still keep records manually. As a result it is difficult to assess the impact of any change to the tax system. This uncertainty makes it highly risky to implement major structural changes because it might result in fiscal difficulties. As a consequence, marginal structural changes are often preferred over major structural changes, even when the latter would be clearly preferable.

Developing countries tend to have less even income distributions than industrial countries so that to generate high tax revenue, the top deciles would have to be taxed significantly more proportionately than the low deciles. However, since economic and often political power is concentrated in the top deciles, richer taxpayers are able to prevent tax reforms that would affect them negatively. (Tanzi & Howell, 2000). Wealth tax was abolished in 2000 in Bangladesh which also has one of the lowest tax rates in the world.

A large portion of the underground economy exists to evade and avoid taxes. Tax avoidance is the legal reduction of tax liabilities by practices that take full advantage of the tax laws while tax evasion consists of illegal and intentional action taken by individuals to reduce their legally due tax obligations (Alm, 1998). While no country is immune to such an economy, developing countries have proportionately larger underground economies. Although a debate exists as to whether an underground economy is good for the economy or bad (which will be discussed in greater detail later), it does lead to revenue loss for the concerned government. It is not uncommon for developing countries to provide many incentives to encourage tax payment in the form of more lenient tax laws, tax exemptions and reduced tax rates as opposed to strong enforcement to encourage tax compliance and retain their money in the formal economy.

1.3 What has the National Board of Revenue done so far?

The NBR uses a combination of permanent as well as temporary incentives to increase tax collection and reduce tax evasion which effectively reduces the size of the underground economy by making it less lucrative to remain outside the official economy. However, no comprehensive study has been done so far as to the effect of these incentives on tax compliance in particular and governance in general.

1.4 Purpose

The purpose of this paper is to multifold. Firstly, it is to study the underground economy, especially of Bangladesh and through the study of 3 incentive programmes of the NBR ascertain the effect of incentives on revenue collection. Secondly, it is to assess the affect these incentives have on tax administration in particular and governance in general. Finally, to explore alternative approaches to revenue collection. This will not be an economic treatment of the subject but rather a look at it from the point of view of good governance. It is hoped that this study will act as a spring board to further study on the issues of tax compliance, the use of incentives and the proper handling of the underground economy of Bangladesh.

1.5 Hypotheses

As already discussed, a large part of the underground economy exists to evade taxes. Although strong enforcement of laws in general and tax law in particular is the logical measure to take to prevent or reduce tax evasion and therefore the size of the underground economy, it is not always an option open to administrations of developing countries. In this scenario, a judicious use of incentives is a more viable option open to tax administrations. This paper will test the following hypothesis:

'The use of incentives leads to greater revenue collection from the underground economy.'

1.6 Outline of Chapters

The paper is divided into nine chapters. Following the introduction in Chapter 1, Chapter 2 provides a literature review on the underground economy, tax compliance and the role of incentives, especially tax amnesties. Chapter 3 discusses the underground economy in greater detail. Chapter 4 describes the methodology used. Chapter 5 includes the study of cattle corridors. Chapter 6 deals with the study of the reward programme of the NBR. Chapter 7 deals with the tax amnesties. Chapter 8 provides an analysis of the data, while chapter 9 concludes the paper and provides some recommendations to improve the existing programmes and suggests some alternative approaches to improve tax compliance and tax collection.

Chapter 2

Literature Review

In the past, the dominant theoretical approach to the design of the tax system was optimal tax theory with its twin objectives of equity and efficiency. Although these two objectives are still desired, what have occurred has been an overwhelming preoccupation with tax structure, and the almost total neglect of administrative feasibility. In developing countries, where administrative feasibility determines the tax structure to a great extent, issues of administration and management are fundamental, for which the recently developing theory of incentives is more relevant (Dasgupta & Mookerjee, 1998). Thus, three areas of literature were reviewed, the underground economy, tax compliance and the role of incentives, especially tax amnesties. Although previously these three areas were dealt with as separate entities, as studies have progressed, a convergence has occurred in both the literature as well as in practice.

2.1 The Underground Economy

From a review of the literature on the underground economy one sees that a lot of work has been done from an economic perspective on specific areas of the underground economy. The areas of contention are extensive, starting from the definition of the underground economy, to how to measure it, to the causes to why it develops, to what effect it has on the official economy.

Extensive work has been done on the underground economies of OECD countries. Friedrich Schneider and Dominik H. Enste have made a comparative study of underground economies of OECD, transitory and developing countries. Unfortunately, none of these works have included Bangladesh.

Reza (1989) estimated the size of the Bangladesh underground economy by using a survey approach. M. Kabir Hassan used a monetary model initiated by Philip Cagan and developed by Tanzi and Shabsigh to estimate the size of the underground economy and then decomposed the size of the underground economy into the domestic, import and export sectors. In Bangladesh, the UE is now widely believed to have become relatively important, autonomous and self-propelling.

Economic theory suggests that taxation, regulation, inefficiency of the bureaucracy and corruption are among the causes of the underground economy. Vast literature exists on the underground economy which exists in part as a means of evading taxes.

2.2 Incentives

In the 1960s economists such as Becker, began to use modern economic analysis to study crime and punishment. Other economists, such as Fleisher (1996) Rottenberg (1968), soon followed and their work dominated the literature for the next three decades. The economic paradigm recognizes two sets of incentives that motivate potential or actual offenders: negative and positive. Negative incentives are those that deter and otherwise prevent would-be and actual offenders from entering or actively pursuing illegitimate activity: the probability and severity of punishment, and the type of punishment to be imposed. Positive incentives are those that induce participation in legitimate alternatives to crime: legitimate employment and earning opportunities, rehabilitation programmes and a lower disparity in the distribution of income in society.'(Ehrlich, 1996). Feinstein (1999) tries to bridge the gap between tax evasion and underground economy literature. Very little literature exists on the effect incentives have on the underground economy in developing countries. However, Dasgupta & Mookerjee (1998) have made a study of the effect of tax amnesties on a taxpayer's decision to whiten money in India.

2.3 Tax Compliance

The literature on tax compliance has also been dealt with from an economic perspective since the pioneering work of Allingham and Sandmo (1972). The idea introduced was that taxpayer compliance is sensitive to economic incentives and that decisions concerning the degree of evasion are similar to most other economic decisions, involving trade-offs at the margin between associated costs and benefits (Dasgupta & Mookerjee, 1998). However, such works have been restricted to developed countries and the United States in particular, such as those conducted by the Taxpayer Compliance Monitoring Program (TCMP). The paucity of relevant empirical data makes it difficult to study tax evasion. No work has been done in Bangladesh on the issue of tax compliance.

From a review of the literature we come to the conclusion that the use of incentives does effect a person's decision to enter or leave the underground economy by way of evading taxes or complying with them. No work on the impact of incentives on tax compliance has been done in Bangladesh. This study will try in part to fill this gap.

Chapter 3

The Underground Economy

3.1 What is the underground economy? The question of definition

'A precise definition seems quite difficult, if not impossible as the shadow economy develops all the time according to the 'principle of running water': it adjusts to changes in taxes, to sanctions from the tax authorities and to general moral attitudes, etc.' (Mogensen, Kvist, Kormendi & Pedersen, 1995, p5)

There is little consensus as to what is meant by the underground economy. People, institutions and countries have defined it according to their own specific needs and the methods used to measure it.

Working definitions:

'..market-based production of goods and services, whether legal or illegal, that escapes detection in the official estimates of GDP.' Philip Smith (1994, p. 18)

'..productive value-adding activities that should be included in the official GNP.' (Schneider & Enste, 2000)

A debate exists as to whether only legal or illegal activities should be included in the estimation of the UE. One definition which tries to include both legal and illegal activities is provided by Mirus & Smith (1997).

Table 1
UNDERGROUND ECONOMIC ACTIVITIES

Type of Activity	Monetary Transactions		Non-monetary Transactions	
Illegal Activities	Trade in stolen goods; drug dealing and manufacturing; prostitution; gambling; smuggling and fraud		Barter: drugs, stolen goods, smuggling, etc. Produce or growing drugs for own use. Theft for own use.	
	Tax Evasion	**Tax Avoidance**	**Tax Evasion**	**Tax Avoidance**
Legal Activities	Unreported income from self-employment; Wages, salaries and assets from unreported work related to legal services and goods	Employee discounts, fringe benefits	Barter of legal services and goods	All do-it-yourself work and neighbour help

Source: Rolf Mirus and Roger S.Smith (1997, p. 5))

From the definition provided in table 1 we see that both legal as well as illegal, monetary transactions as well as non-monetary, and tax evasion as well as tax avoidance can lead to the creation and growth of the underground economy.

3.2 Reasons for the growth of the underground economy

The reasons for the growth of the underground economy vary for developing and developed countries.

In OECD countries, the rise of the burden of taxes and social security contributions, a complex tax system, increased regulations, forced reduction of weekly working time and a decline of civic virtue are believed to be some of the major causes for the expansion of the

UE. For developing countries, where governments are not able to provide social safety nets the question of social contributions and the reduction of weekly working time does not arise. In fact, since one receives very little benefits from the formal economy there is very little incentive to remain within it. However, the other causes for the rise of the UE in developing countries are the same. A more complex tax system allows greater tax avoidance than a simple one by providing various tax exemptions and reductions. Most governments opt for more regulation and laws in trying to reduce the shadow economy rather than improving enforcement. However, what that does is increase the power of bureaucrats and size of the government. Eric Friedman, Johnson, Kaufmann and Zoido-Lobaton(1999) argue that institutional aspects like efficiency of the administration, the extent of control by politicians and bureaucrats, the amount of bribery, and especially corruption play a big role.

3.3 How is it measured?

'Obtaining accurate statistics about the allocation of a country's resources in the shadow economy is important for making effective economic policy decisions' (Schneider & Enste, 2000). However, since most of the activities are illegal, and/or unrecorded, it is very difficult to measure the UE accurately.

Direct approaches

Sample surveys are widely used in a number of countries to measure the shadow economy. The main advantage of this method lies in the detailed information that can be gained about the structure of the shadow economy. But, as with all surveys, precision and results depend upon the respondents' willingness to cooperate. Most interviewed hesitate to confess fraudulent behavior, and quite often responses are unreliable, making it difficult to estimate the extent of undeclared income (Schneider & Enste, 2000).

Estimates of the shadow economy can also be based on the discrepancy between income declared for tax purposes and that measured by selective checks. Fiscal auditing programs have been particularly effective in this regard. This approach has a number of setbacks. First, using tax compliance data is equivalent to using a sample that is not a random one of the whole population. Second, estimates based on tax audits reflect only that portion of shadow economy income which the authorities succeeded in discovering, and this is likely to be only a fraction of hidden income. (Schneider & Enste, 2000)

Indirect Approaches

- Discrepancy between National Expenditure and Income Statistics:

If an independent estimate of the expenditure side of the national accounts is available, the gap between the expenditure measure and the income measure can be used as an indicator of the extent of the shadow economy. The problem with this approach is that the discrepancy includes all omissions and errors everywhere in the national accounts statistics as well as the shadow economy. (Schneider & Enste, 2000)

- Discrepancy between Official and Actual Labour Force:

A decline in labour force participation in the official economy can be seen as an indication of increased activity in the shadow economy, if total labour force participation is assumed to be constant, *ceteris paribus*. The weakness of this method is that differences on the rate of participation may have other causes. Moreover, people can work in both the shadow and the official economies. Therefore, such estimates may be viewed as weak indicators of the size of the shadow economy. (Schneider & Enste, 2000)

There are many other indirect approaches which are used to measure the size of the UE each with its own strengths and weaknesses. In fact the large number of methods creates a problem in itself in that since countries use different methods, cross-country comparisons become difficult.

3.4 What is the size of the underground economy?

Disagreement persists about definition and estimation procedures. This leads to varying estimates of the UE in the same country and time frame. Very broad ranges are usually the closest that have been possible in determining the size of UEs.

Table 2
SHADOW ECONOMY AS PERCENTAGE OF OFFICIAL GDP, 1988-2000

Country Group	Percentage of GDP
Developing	35-44
Transition	21-30
OECD	14-16

Source: Friedrich Schneider with Dominik Enste (2002)

Very little research has been done on the underground economy of Bangladesh. Although none of the literature generated by the west includes Bangladesh, we know that it should be between 35 to 44% of GDP although some countries have underground economies as high as 74% (Nigeria) and as less as 13% (Singapore) of the GDP. M. K. Hassan (1997), using a ratio currency model, has estimated the underground economy to be 23% of the formal GDP. This estimation is lower than the accepted rate for developing countries because he included only that part of the economy that exists to evade tax. Abul Barkat (1991) estimates that the underground economy is one third of the GDP of the official economy, about Taka 70,000/- crore in 2004-2005 financial year. However, it has not been possible to find out what method was used to arrive at this estimate.

3.5 Is it good or bad?

Like all debates, this has both elements of good and bad. It is bad in that a sizable underground economy presents also a particular problem for the government's fiscal position. While the UE benefits from government services, the government suffers a loss in tax revenues. If the underground economy is growing at a faster rate than the formal economy, Government expenditure will grow, but its revenue will grow at a slower rate since it is from the formal economy that the government collects taxes. A reaction to this by the government could be to raise the tax rate and/or impose new taxes. Without improving tax compliance or tax base, this would force more activities into the underground economy and cause a reallocation of resources from the formal economy to the underground economy. Deficit financing has more significant adverse economic consequences for developing countries with weak tax bases (Shabsigh, 1995). A decrease in state revenue also reduces the quality and quantity of publicly provided goods and services, such as the public infrastructure and of the administration, with the consequence of even stronger incentives to participate in the shadow economy.

Another major problem is that a large underground economy makes official statistics unreliable and gives a distorted picture of the economy to policy makers and makes their policy recommendations less effective. An example that Shabsigh (1995) gives is, if output and employment is growing at a faster rate in the UE than in the formal economy, then an expansionary policy designed to stimulate a perceived slow growth could be more inflationary than intended.

The reallocation of resources to the UE also reduces net welfare since UE activities, which are usually small scale, labour intensive and have limited access to formal financial markets, are less productive than formal economy activities. A vibrant shadow economy may lure workers and capital away from the official economy. The fact that black money is used to finance terrorist activities is another source of concern and a major reason the UE has to be controlled and monitored.

From an ethical point of view, the existence of a UE implies the employment of double standards and treatment. Those of society who pay taxes bear the added burden of paying the taxes of those who do not and yet receive no greater benefit from the state.

Substantial reduction of the shadow economy leads to a significant increase in tax revenues and therefore to a greater quantity and quality of public goods and services, which ultimately can stimulate economic growth.

The negative impact of the informal sector activities on economic growth is not broadly accepted (Schneider & Enste, 2000). In the neoclassical view, the underground economy, responding to the economic environment's demand for urban services and small–scale manufacturing, adds to the economy a dynamic and entrepreneurial spirit and can lead to more competition, higher efficiency, and limits on government activities. The informal sector may also contribute 'to the creation of markets, increase financial resources, enhance entrepreneurship, and transform the legal, social, and economic institutions necessary for accumulation'(Asea 1996, p166). The voluntary self-selection between the formal and informal sectors may provide a higher potential for economic growth and, hence, a positive correlation between an increase in the informal sector and economic growth. Empirical findings by Schneider (1998b) show that over 66 percent of earnings in the shadow economy are immediately spent in the official sector, with positive effects for economic growth and for indirect tax revenues. The effects of the shadow economy on economic growth therefore remain ambiguous. What is clear, however, is that close interaction exists between the underground and formal economies.

Smaller shadow economies appear in countries with higher tax revenues, often achieved by lower tax rates, fewer laws and regulations, and less bribery facing enterprises. Countries with better rule of law which is financed by tax revenues also have smaller shadow economies. Transition countries have higher levels of regulation leading to a significant higher incidence of bribery, higher effective taxes on official activities, and a large discretionary framework of regulations - and consequently, larger shadow economies (Schneider & Enste, 2000).

Eliminating the underground economy is neither feasible nor possible. Trying to handle the UE is no easy feat either. Attempts by developing countries, which have poor governance track records, have resulted in greater tax evasion and the expansion of the UE. An alternative approach often employed is not to directly try to regulate the UE but to extract revenue from it and re-circulate it into the formal economy. This method does not require high levels of good governance nor strong enforcement capabilities and therefore is within the administrative capabilities of most tax authorities. The performance of some programmes under this approach will be studied in this paper.

Chapter 4

Methodology

4.1 Steps

The methodology for conducting the study was designed in such a way as to encompass both qualitative and quantitative approaches and comprised of the following steps:

- Preliminary Discussion with NBR officials to determine the feasibility of the study
- Case studies
- In-depth interviews with parties related to the case studies under consideration
- Collection of primary information and data to test hypothesis
- Data editing ,data entry and data processing
- Data analysis and interpretation

Both primary and secondary sources of data were used in the study.

4.2 Primary Sources

Depending upon the case in question interviews with officials of the NBR, tax lawyers and advisors, businessmen and other categories of assessees, officials of Bangladesh Bank and academics were taken. Rather than search for consensus of opinions, the purpose of the interviews were to get a holistic overview of each issue from the people who have access to the information or have worked in those areas or have a clear understanding of how the mechanism works.

Thus officials who have worked in the corridors and are posted at the desk at the NBR that deals with smuggling were interviewed as well as officials at Bangladesh Bank who have in-depth knowledge of money laundering and smuggling practices. Interviews were also taken of those who have received rewards and those who man the reward desks of each wing of the NBR. Assessees who have taken advantage of tax amnesties, lawyers and tax practitioners who have encouraged or discouraged their clients to avail tax amnesties have also been interviewed along with tax officials who work at the field offices. Academics and other persons who have extensive knowledge of the either the underground economy or the revenue system of Bangladesh were interviewed to get a balanced picture of each case.

4.3 Secondary sources

Data and information were also collected from books, journals, newspapers and reports and downloaded from the web. Statistics and reports were gathered from the NBR and concerned head offices of different tax zones.

4.4 Area of Study

Three incentive programmes of the NBR have been chosen. Two of the programmes, that is the cattle corridors and tax amnesties are positive incentives given by the NBR while the reward programme acts as a disincentive to evade taxes. Each programme has been chosen as unique examples of innovative methods to handle a problem with the administrative capabilities and resources available as well as their effect on the issue of governance. On a more practical level, these three programmes where chosen because sufficient data was available, in terms of revenue collection, at least.

4.5 Problem

Do incentives work? To test the hypothesis statistics will be used to see whether there has been any significant increase in revenue earnings as a result of the introduction of each incentive. Are there other results of these programmes, positive or adverse which outweigh the revenue concerns? Interviews with diverse quarters will shed light on this issue.

4.6 Limitations

This is not a look at the issue from an economic perspective. It is hoped that this study will act as the basis for future study on this subject from an economic perspective. Availability of data, or lack thereof, played a strong role in determining the extent of the study. Secondly, although smuggling plays an integral part in the cattle corridor programme and the interview of smugglers involved in the trade would have given a more rounded view of the programme, it was not possible to interview any smugglers.

Chapter 5

Programme 1: Tax Amnesties

The advantage of reward as opposed to punishment is that even weak administrations can use it. Whereas punishment requires strong authority and the ability to extract compliance, to be imposed, reward is much easier to implement. Here, reward does not mean just giving prizes; it means any positive incentive which brings about the desired behaviour.

5.1 Permanent incentives

In the Income Tax Ordinance, 1984 there are many positive incentives provided for people so that they invest in the Bangladesh economy and pay taxes. For instance, five-year-tax holidays are given to businesses to encourage them to establish their industries in the less developed regions of the country (Sections 45 and 46). Remittance is now tax free if brought through official channels (SRO. No.111/law/2003) so that any income earned abroad, which would have previously been included in the world income of a taxpayer (Section 18) and taxable, is now tax free. While in income tax law unexplained investments are deemed to be income and taxable(Section 19) exemptions are given in respect of investment in new industries or the purchase of shares (Section 19A, 19AA,19AAA) or investment in houses (Section19B), land property (Section 19BB) and purchase of vehicles (Section 19BBB). Usually, for such investments the positive incentive given is that no question is asked about the source of the funds required to make the investment and/or the tax rate is lower than the normal prevailing rate at the time or one just does not have to pay any taxes at all (Section 19AAA).

Table 3

TAX EXPENDITURE BY TAXPAYERS AFFECTED, FY 2005-2006

	Revenue foregone		
Taxpayer	**In Taka (million)**	**In % of total Revenue Loss**	**In Percentage of GDP**
Exporter	320	0.0311	0.0086
Businesses	5900	0.5740	0.1591
Donors	100	0.0097	0.0027
Employees	100	0.0097	0.0027
Financial institutions	0	0	0
Government	1190	0.11578	0.0321
Hospitals	50	0.0049	0.0013
Non profit organizations	100	0.0097	0.0027
Personal Income Tax Payers	220	0.0215	0.0059
Retirees	100	0.0098	0.0027
Property owners	0	0	0
Primary producers	1240	0.1206	0.0334
Real estate promoters	0	0	0
Nonresidents	800	0.0778	0.0216
Miscellaneous	160	0.0155	0.0044
Total	**10280**	**1.0000**	**0.2772**

Source: NBR, National Board of Revenue (2006), Income Tax Incentives: Concept Note on Tax Incentives and Exemptions, Dhaka.

Table 4

REVENUE FOREGONE BY TYPE OF INCENTIVE, FY 2005-06

	In million Taka	In % of GDP
Tax Holiday	2670	0.0721
Exemption & Deduction	2790	0.0752
Tax Rate Reduction	1820	0.0491
Deferrals	1290	0.0347
Tax Credit	220	0.0060
Others	1490	0.0401
Total Revenue Loss	**10,280**	**0.2772**

Source: NBR (2006) Income Tax Incentives: Concept Note on Tax Incentives and Exemptions.

Table 4 shows the revenue foregone by type of incentive provided to the class of assessees mentioned in table 3 during the financial year 2005-06. Tax holidays, do exempt industries from paying taxes for a certain amount of time, it is still not a complete loss. Although the industry is exempt from tax payment on its profits, the employees' salaries and wages are not. Through the multiplier effect, the setting up and operation of the industry leads to even greater economic activity and revenue generation. The real loss occurs when this increased activity goes untaxed.

From a global perspective, these incentives act as motivation for international businesses to set up their plants and do business in Bangladesh. When most developing countries can offer cheap labour, a tax incentive package could tip the scales in one's favour. From a national point of view, making foreign remittance tax free, not only increases the foreign currency reserve but also generates economic activity in the country. Furthermore, all the incentives combined are only a fraction of total GDP but their positive impact is far greater. Although it is true that abuse of these incentives and exemptions does occur it is more the fault of tax administration rather than the exceptions themselves.

The above exemptions have been in force for many years. The present Income Tax Ordinance provides the legal support for these incentives while S.R.O.s issued under the Ordinance authorize the government to make complete or partial exemptions of income from the payment of tax (NBR, 2006).

5.2 Temporary Incentives

The most controversial of these laws is S.R.O 200/law/2005 made under the authority of Section 44(4)(b) of the Income Tax Ordinance of 1984, providing tax amnesty, more popularly known as the Black Money Whitening Scheme. Although there are three types of tax amnesties, revision amnesty (opportunity to revise past tax returns), investigation amnesty (a promise not to investigate the source of the income disclosed) and prosecution amnesty (immunity from prosecution for detected offenders), only investigation amnesties have been offered in Bangladesh. In the past 35 years such schemes have been offered 6 times with limited success. A total of Taka 3,695 crore was whitened in the six schemes combined. See table 5. Although the first two amnesties had no conditions attached, in the third amnesty the tax rate was 20% and only 10% for those who invested 90% of the money in the industrial sector. In the sixth tax amnesty the tax rate was 10%, provided the money was invested in the production or service sectors or spent on the purchase of shares.

Table 5

REVENUE EARNED IN LAST 7 AMNESTIES

Financial Year	**Normal Tax Rate**	**Rate of Tax Amnesty**	**Money Laundered (In Crore Taka)**	**Revenue earned (in Crore Taka)**
1975-76	60%	15%	70	10.5
1987-88	50%	20%	200	40
1988-89	50%	10%	250	35
1989-90	50%	10%	400	40
2000-01	25%	10%	1,000	100
2002-03	25%	10%	2,000 (In 3 Yrs)	200
2005-2006	25%	7.5%	4,603	345.24

Source: Rejaul Karim Byron, (2006) Last Dash for making Black Money White: Record Tk. 4,603cr. Whitened, 2/7/06, Daily Star

Serious doubts of the rationality of such schemes arose (Ahsan, 2005) because not only did they fail to access money from the underground economy at any significant amount, it was felt that it encouraged people to evade tax even more and discouraged honest taxpayers to pay their taxes. The schemes amounted to admission by the government of its failure to curb tax evasion in the past and constituted an attempt to provide taxpayers with the opportunity to launder their black assets into white.

However, in the 2005-2006 financial year another tax amnesty was offered. Under this scheme income not previously declared income could be declared on payment of $7^1/_2$ percent tax with out any fear of punishment. The scheme whitened Taka 4603.21 crore which raised the question again - do such positive incentives really work to access revenue from the underground economy or create greater incentives to remain in it?

5.3 Pros and cons

A justification frequently offered by governments is that an amnesty is an equitable transition measure to a period of stepped up enforcement. This argument appears far from clear as an amnesty allows lenient treatment of amnesty participants, in comparison to offenders punished either before or after it.

Citizens are encouraged to voluntarily declare such assets and directly or indirectly pay a fee based on these on these disclosures, in return for which the government promises not to investigate the sources of such assets or initiate prosecution.

Table 6 shows, zone wise, the number of taxpayers who showed previously undeclared income, the amount of the income previously undeclared and the tax paid on it at seven and a half percent. A total of 7246 taxpayers availed the opportunity to declare a total income of Taka 4,603 crore, in exchange for paying Taka 345.24 crore in tax.

Table 6
DATA ON DECLARATION OF UNTAXED INCOME DURING FY 2005-2006

Tax Zone	No. Of Taxpayers who Declared Untaxed Income	Undeclared Income (In Crore Taka)	Tax Paid (In Crore Taka)
LTU	177	531.87	39.89
Zone 1	897	502.53	37.69
Zone 2	740	421.07	31.58
Zone 3	657	377.60	28.32
Zone 4	857	499.20	37.44
Zone 5	250	320.00	24.00
Zone 6	419	266.67	20.00
Zone 7	546	360.00	27.00
Zone 8	483	318.00	23.85
Central Survey Zone	125	30.27	2.27
Zone 1, Chittagong	471	193.33	14.50
Zone 2, Chittagong	425	273.87	20.54
Zone 3, Chittagong	520	253.33	19.00
Zone Khulna	134	61.73	4.63
Zone Rajshahi	162	101.60	7.62
Zone Rangpur	67	12.67	0.95
Zone Sylhet	250	61.47	4.61
Zone Barishal	66	18.00	1.35
Total	**7246**	**4603.21**	**345.24**

Source: Research and Statistics Department, NBR, 2006

Usually, this money is income which was not declared previously and as such no tax was ever paid on it. As such most of this tax was paid by professionals (doctors, teachers, lawyers and so on) bureaucrats, armed force personnel and businessmen.

The reason why people can evade paying their taxes so easily in developed countries in general and Bangladesh in particular has already been discussed. According to Abul Barakat (2004) approximately 89% of the underground economy exists to evade and avoid tax payment. While it is the National Board of Revenue's goal to limit tax evasion and encourage greater tax compliance, by simplifying procedures, setting up a Tax

Ombudsman (this was done by the government), creating greater awareness of tax laws and the rights of taxpayers, and so on, it is well aware that tax evasion will not go away over night. It may never go away for that matter if you consider that even developed countries suffer from tax evasion. To try to eliminate the underground economy by increasing tax compliance is a challenge even if it were feasible. In the mean time undeclared income continues to rise yearly, expanding the underground economy even further. The NBR has used positive incentives to access this undisclosed (undeclared) income, which at first glance may appear to be like encouragement to tax payers to evade tax payment.

Considering, the fact that to tackle the problem would be beyond the abilities of the NBR and fool hardy, these steps at least reduce the drain on the official economy. What would be the alternative? If these schemes were not provided, and the administrative capability of the NBR remained the same, the government would have been Taka 345.24 crore poorer and remain trapped in that vicious cycle already mentioned above. Since the NBR in particular and the government in general is unable to implement negative incentives such as punishment for all tax evasion, providing positive incentives, backed by the threat of punishment, if not actual punishment, for non-compliance is a more effective policy to tackle the underground economy in the context of current realities.

Chapter 6

Programme 2

Reward for Detecting Tax Evasion

A negative incentive is a situation which has the effect of deterring a person from doing something. It can take the form of punishment but is not restricted to only punishment. There are many disincentives incorporated in the Income Tax Manual, 1984 to deter tax payers from evading taxes and promote tax compliance. Chapter XV deals with the imposition of penalties and includes penalty for concealment of income (Section 128). Chapter XXI deals with offences and punishment including punishment by imprisonment for up to five years for the concealment of income (Section 166). However, punishment only works if they there is strong conviction that, if caught, the evader is punished. It is therefore not enough for a law to exist to punish tax evaders; it has to be operational in which case the threat of punishment is as effective as the punishment itself. Unfortunately, not only person has gone to jail for tax evasion in the 35 year history of Bangladesh and that was more a political issue than anything else. Thus, the fact that hardly anyone has gone to jail for tax evasion acts as a greater positive incentive to evade taxes than the law acts as a disincentive.

For the assessment year 2006-2007, six crore taka has been given to the National Board of Revenue to reward persons for outstanding performance in the conduct of their duties. More specifically, four NBR wings have been given this money to reward officers and employees and informants. Although this money will not be distributed until the end of

September, in the financial year 2004-2005, 1.50 crore was distributed in the following manner:-

Table 7
DISTRIBUTION OF REWARD MONEY AMONG GOVERNMENT DEPARTMENTS

1	Bangladesh Rifles	Tk. 13,00,000/-
2	Bangladesh Police	Tk. 6,00,000/-
3	Coast Guard	Tk. 6,00,000/-
4	Bangladesh Navy	Tk. 6,00,000/-
5	Customs Department	Tk. 56,00,000/-
6	VAT	Tk. 14,00,000/-
7	Income Tax	Tk. 14,00,000/-
8	Central Intelligence Cell	Tk. 10,00,000/-

Source: NBR, Research and Statistics Wing, Dhaka (2006)

This reward is given to government officials and their informants for detecting tax evasion or any other criminal activity (depending upon the nature of work of each department) on the basis of separate orders of each establishment.

6.1 The Law

In the case of the income tax department there are provisions to reward any person for detecting evasion of taxes or for furnishing any information leading to the detection of tax evasion under **Section 184D of the Income Tax Ordinance, 1984.** (Annex 2). Rules were never made in compliance with Section 184D but an order known as the 'order for monetary reward to informants of the concealment of income and evasion of taxes', dated, 21st November, 1980 was made(See Annex 2)

In the case of the VAT wing, **Section 71 of the VAT Law, 1991,** provides provisions for rewarding the detection of tax evasion.

The Customs (Grant of Reward) Order, 1986 governs the rewarding process of the Customs and Excise Wing of the NBR.

Since the Central Intelligence Cell (CIC) was a part of the Income Tax Department it still follows the rules concerning reward that that department follows. However as a result of its elevation to a separate wing process is under way to formulate a new reward order for the CIC.

6.2 The Process

There is no process whereby the Board or the Commissioner can assess the merit involved in detecting tax evasion unless it is brought to its attention. The process for receiving reward as it is practiced in the Income Tax Wing is as follows. If an applicant feels that he has used 'extraordinary initiative' in the detection of tax evasion (s)he can apply to the NBR for a monetary reward. Thus, whether an act is reward worthy is already determined by the applicant even before the Board decides. One official may think that what he has done is reward worthy and apply for reward but another official may think that s/he was just doing his/her job and not apply even though it may have taken great diligence and effort on the part of the official.

Anyway, the applications are then submitted to a committee comprising of usually 12 members. The actual scrutiny of the individual cases is divided among a number of Second Secretaries of the Board depending upon the number of applications submitted which also determines how many times a year the committee sits. If there are many applications, the committee will sit as many as four times a year and if there are a few(applications), only once a year. If the Second Secretaries (usually two working together), find that the tax has not been collected from the taxpayer the application may be left to be scrutinized on a later date when the whole of the tax is collected. The remaining applications go to the committee for final recommendation along with the findings of the Second Secretaries. Those cases which are thought to lack sufficient merit or deemed to be routine work are turned down. Those cases in which it was deemed that the official(s) involved showed remarkable ingenuity, perseverance and merit are given rewards based upon the effort felt to have been applied by the applicant(s). Thus, it is a subjective assessment of merit that determines the size of the reward and not just the amount of tax evasion detected. On scrutinizing the case if it is found that the official did not use due diligence or did not follow procedure departmental proceedings may be started against him/her. Since many officials may be involved in any one case, starting from the Additional Joint Commissioner to the Stenographer, more than one person may be rewarded for the same case in which situation the money is divided among all of the officials. The amount of money they will receive will depend upon their basic pay, the amount of concealment they detect and the availability of funds. (See Annex 2 for the order)

The method applied in the VAT wing, CIC wing and the Customs and Excise wing differs very little from that applied in the Income Tax wing except in three areas. Firstly, in the VAT and Customs and Excise wings the amount of the reward is in proportion to the amount of concealment detected and the amount of tax collected from that detection (usually 10%) rather than on any subjective assessment of the effort utilized. Secondly, if any tax evasion is detected, each and every person, starting from the commissioner to the Lower Division Clerk (LDC), is entitled to a part of the reward even if he/she was not directly involved. Finally, a part of the reward automatically goes to the Customs, Excise and VAT benevolent fund. The money to pay for these rewards, as do all other rewards paid in the government, comes from the budget head 4748 which is reserved for funding rewards.

6.3 Pros and Cons

Instances of providing monetary reward to civil servants have grown in recent years partly due to the influence of New Public Management theories. To encourage the dynamism and drive perceived to exist in the private sector into the public sector, private sector tools of motivation are being used. In some countries, such as Georgia, the civil servants that man the Revenue Department are given higher pay and better logistic support than the rest of the administration, to encourage better performance. This has not been possible in Bangladesh and as fast promotions or promotions that break the seniority list, is as yet not an option in the Bangladesh civil service, reward is the main motivational tool used so far.

When a person knows that s/he will be rewarded for detecting concealment then it will obviously encourage greater effort on his/her part. One may question why a person whose job is to detect concealment be rewarded for doing only his/her job. The answer to this is of degree. If a customs official gets a tip that a certain passenger of a specific flight is carrying contraband and that passenger is caught, then that would be deemed as his/her regular job. If the same customs official got a tip that a passenger of a certain flight was carrying contraband but did not know which passenger it was and s/he through sheer effort was able to detect that passenger out of the 540 or so passengers on board, then that would be deemed as an act of merit. That is why the reward scrutiny process is subjective; to assess the amount of effort that was required to detect the concealment.

Chapter 7

Programme 1: Cattle Corridors

7.1 Smuggling

Smuggling is an illegal underground activity which according to some, accounts for taka 4,680 crore (Barkat, 2004) of revenue loss annually to Bangladesh in unpaid customs duty. The most common good to be smuggled into the country is cattle. The most common goods to be smuggled out of Bangladesh are gold, oil and currencies. In the National Board of Revenue there is an anti smuggling task force which deals with stopping the illegal export and import of goods through smuggling over land and by air and sea. In this endeavour it holds monthly high power meetings with various agencies including the police, BDR, ansars, magistrates, officials from the Narcotics Bureau and other concerned bureaucrats and locally elected officials. A concerted effort is made to try to curb smuggling.

7.2 Smuggling by Air

At the Zia International Air port risk assessments are made of all flights as to the chances of its passengers carrying contraband and/or its passengers evading taxes. For example, flights from Singapore or the Middle East are considered high risk flights and customs officials remain on high alert during those flights and intensive scrutiny of luggage, passengers and fight crew is made only limited by the baggage check rules which prohibits the opening and checking of more than 10% of luggage per flight. Other flights like ones from the United States or Great Britain are considered low risk and very little man power is utilized to check the luggage of these flights. As mentioned earlier, customs officials keep close liaison with their sources and receive tip-offs from them which lead to the capture of smuggled goods which would have otherwise remained undetected. Years of experience make it possible for officials to detect smugglers by observing their countenance or behaviour. The presence of a high number of officials and check posts acts as a deterrent or negative incentive to smuggle goods into the country by air.

However, it is well known even in the National Board of Revenue that the greatest amount of smuggling that goes undetected is possible through the connivance and collusion of customs employees, flight crew and ground crew, immigration officials, officials of Zia International, luggage handlers and so on. Smugglers can get information about the official that will be on duty at the time that the flight they plan to take will arrive in Dhaka. Only if the environment is felt to be favourable do they attempt to smuggle goods into the country. Countless persons have been caught smuggling, even flight crew against whom cases are filed at the Zia International Airport Police Station. Unfortunately, so far, not one crew member has been tried in court for smuggling. This absence of the threat of punishment acts as a positive incentive to smuggle.

7.3 Smuggling by Land and Sea

Similarly, smuggling occurs across the border by land and by sea. It is here that smuggling becomes less sensational because it involves everyday ordinary people who are trying to make a living in the only way they know how. It is here that my last case study lies.

In India cows are sacred animals and as such they cannot be eaten, killed, bought or sold. Due to religious reasons India does not trade in cattle but would be overrun by cows if not removed from the country. On the other hand Bangladesh is a beef eating nation of 140 million people in need of cheap sources of protein which it cannot domestically produce at the rate that is required to meet the demand of its citizens. With such a long and porous boundary between India and Bangladesh it was inevitable that a thriving cattle smuggling business would develop between the two countries. During the pre-corridor years any cattle that was captured by the BDR were put into quarantine and then auctioned off in due time. The problem with this procedure was that it was expensive to feed and house the cows before they were auctioned off and a lot of the cows died as a result of poor maintenance.

7.4 Process

In 1992 a special task force in Netrakona came up with the idea to set up a corridor through with cattle could enter Bangladesh from India. Currently there are 21 corridors strategically placed along the border through which cattle can enter Bangladesh. Since it is illegal to export cows in India, a legal fiction is created whereby a Bangladeshi citizen claims that (s)he has found a cow which has wandered into Bangladesh and (s)he, being a upstanding citizen, is handing it over to the customs authority.

The concerned authority confiscates the cow and auctions it off, on the same day, so that the person who had captured the cow is able to purchase the cow. Depending on the size of the cow, small, medium or large, the person had to pay taka 500/-, taka700/- or taka 800/-

respectively in customs duty for the cow. At the moment the rate is taka 500/-, to remove instances of collusion that used to take place to reduce the rate. Table 8 shows the number of cattle that has passed through the corridors from 1993-94 to 2005-06 and the amount of revenue earned in crore taka. The number of animals that enter vary from year to year depending upon how aggressively the Indian and Bangladeshi border guards man the borders.

Table 8

TREND OF CATTLE TRADE THROUGH THE CUSTOM CORRIDORS FROM FY 1993-94 TO 2004-05

Financial Years	Number of Cattle	Revenue in Crore Taka
1993-1994	N.A	N.A
1994-1995	446,128	33.04
1995-1996	727,615	53.40
1996-1997	744,336	55.31
1997-1998	394,835	30.92
1998-1999	458,065	24.60
1999-2000	723,064	36.96
2000-2001	721,022	36.56
2001-2002	956,053	48.00
2002-2003	959,890	48.11
2003-2004	716,583	35.87
2004-2005	1,037,006	51.90
2005-2006	973,163	48.61

Source: National Board of Revenue Annual Report 2004-2005 (2006), Research and Statistics Wing, National Board of Revenue, Dhaka, p102 (yet to be published)

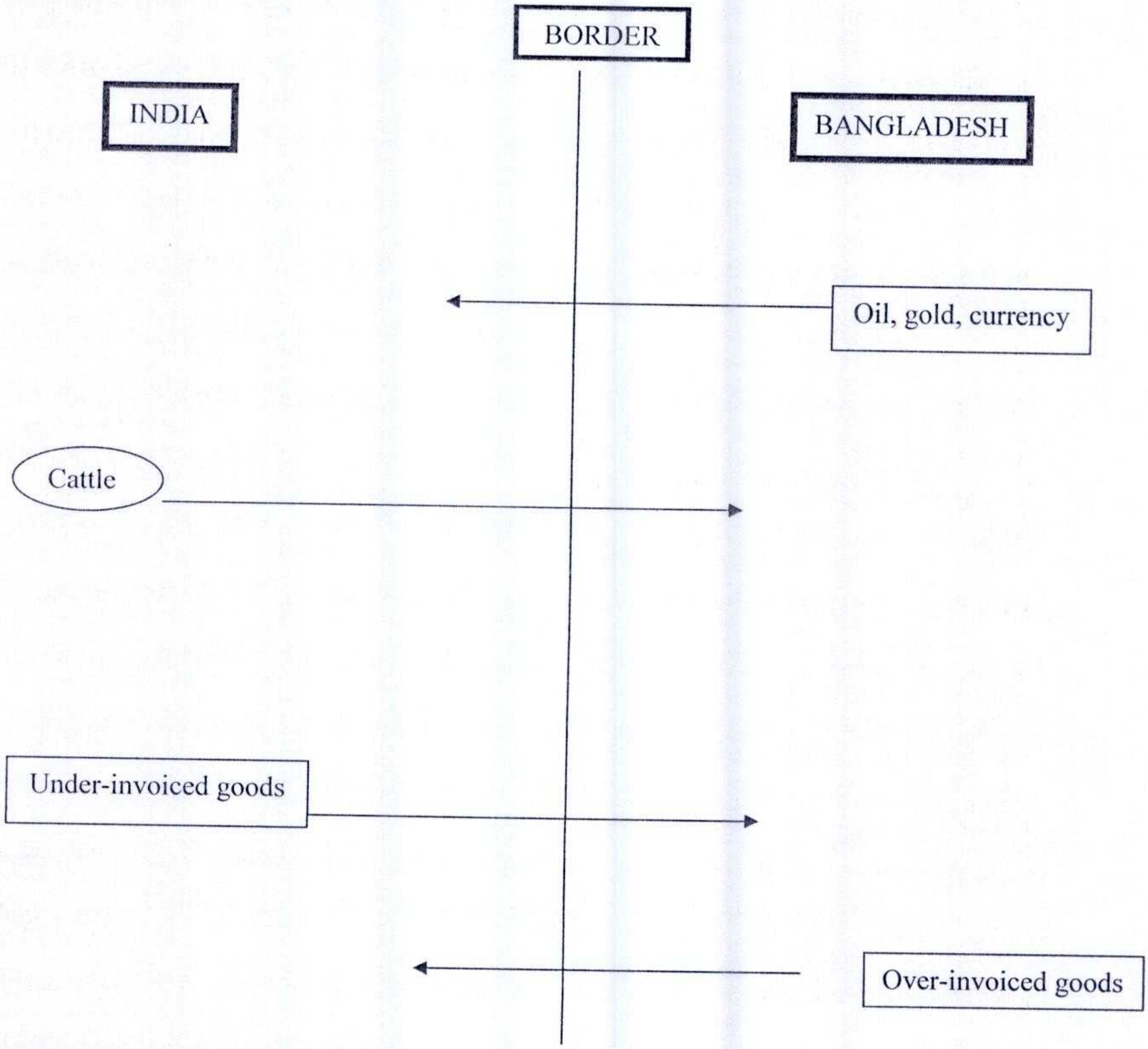
This is only one part of the transaction. The cow has arrived in Bangladesh. Its owners have papers which state that as he has paid the customs duty, he is now the official owner of said cow. He can now sell the cow in the open market. However, the Indian who owned the cow has not received any money for the cow. Money has to now travel from Bangladesh to India to pay for the cow. From talking to officials who have worked at the corridors it is known that this payment is made in gold, oil or currency which is smuggled into India by people who act as regular transporters. The fact that oil in Bangladesh is less expensive than in India since it is subsidized makes it an acceptable mode of payment. Taka 500/- notes are openly used in the markets of Calcutta along with the Indian Rupee. 'Hundi', is also a common method of payment. Another method used is over invoicing imports and under invoicing exports. By over invoicing one pays more for what is being imported so that the excess can be utilized for the payment of goods smuggled into the country. Similarly, by under invoicing one receives less money for the export, the remaining that should have been received being considered as payment for goods smuggled into the country. The fact that there is no cross verification by Indian Customs and their Bangladeshi counterparts as to whether what Bangladeshi importers are claiming to be in the trucks is the same as what the Indian exporters are claiming to be in the same trucks or of the same amount. Furthermore, it is this set up which gives proof of the existence of an intricate net work involved in the smuggling business because the spice importer is obviously not also involved in the cattle business. However, all these transactions occur simultaneously and there is a system which acts like a clearing house so that each participant pays what should be paid and receives what (s)he is due to him/her. So it is not really necessary for the payment to go directly from Bangladesh to India or to go to India at all. The development of communications and off shore banking and on line banking has made life not only easier for everybody, it has made it easier for smugglers too because it has expanded their network.

7.5 Pros and Cons

At first glance it may be perceived as unethical on the part of the Government of Bangladesh to regularize the smuggling of cows in this manner. However, let us look at the reality. We have a border with India which does not create any natural barrier between the two countries. There man-made structures have to be built and manned. Bangladesh does not have the resources to build an effective barrier along its border nor the man power needed to guard over it. People on opposite sides of the border are of the same ethnicity and speak the same language making it harder to differentiate between the two and thus more difficult to detect smugglers. Smuggling across the boarder does not require a lot of capital, skill or expertise. Women, children and men, young and old are involved in smuggling over the land borders. So to stop smuggling completely would be a monumental if not impossible task requiring a lot of resources which neither country has. More importantly, there is absolutely no legal way by which we can import cattle from India. If we were to legally import beef from any other country, it would be more expensive involving a greater outlay of foreign currency. Hypothetically, since this would be a legal transaction, it would have a negative impact on the balance of payments, leading to a fall in the value of the Bangladesh Taka. So even if it were possible to completely stop the smuggling of cows from India, the total benefit to the country would diminish. We would have to seek for alternative sources of protein which would not necessarily be cheaper or conducive to our palates.

Figure 1

Cattle Transfer and its Payment Diagrammatically Presented



Chapter 8

Analysis of Data

A serious problem in studying tax evasion is the paucity of relevant empirical data, especially in the context of developing countries (Dasgupta & Mookerjee, 1998). The case of Bangladesh is no exception. However, from the limited data that was available certain facts have come to light that are both interesting and thought provoking. (See annex 3)

8.1 Programme 1: Tax Amnesties

When asked why people do not take advantage of these schemes at the expected extent, tax officials, tax practitioners and tax payers alike provided a number of reasons.

Firstly, unfortunately, most lawyers and tax payers believe that they (tax payers) can continue to evade taxes and so why pay 10% or $7^1/_2$ or anything at all when one can get by not paying anything?

Secondly, bureaucrats do not like to use the scheme because, although the tax authorities will not ask any questions of them the government will. They will remain accountable to the rules and regulations of the government which deem such acts as misconduct and may result in punitive action or even loss of jobs. A better response occurred in the last amnesty mainly as a result of the conviction felt by bureaucrats that no action would be taken against them as well as the activity of the CIC which increased the chances of their concealment being caught.

Thirdly, there are so many other tax exemptions that can be used where one does not have to pay any tax that there is no emergency to avail tax amnesties. Tax payers will be more reluctant to disclose assets in an amnesty that is likely to be used as the basis of more intense scrutiny from the tax department in the future.

Moreover, the effects of an amnesty may depend on the information taxpayers have about the seriousness of the government's intention to strengthen enforcement in the future: two identical amnesties in different political environments may therefore induce very different participation levels. (Dasgupta & Mookerjee, 1998)

Past amnesties have garnered low response because they were anticipated, that is, taxpayers knew that there would be another amnesty in the near future and there was no urgency to avail the current one. Secondly, people were not sure what the tax authorities would do with the information if they disclosed their undeclared income. Fear of investigation and prosecution deterred them from availing the amnesty.

When asked why the 2005-06 scheme did so well compared to past schemes, tax officials unanimously agreed on the following reasons.

Firstly, 2007 is an election year and it is difficult to guess which party will come into power. This uncertainty has encouraged many to legalize their income so that they will not face prosecution or persecution later on.

Secondly, the tax rate - seven and a half percent - is the lowest tax rate to be offered in any of the schemes and many taxpayers thought that it was lower that what he/she would have had to pay his/her lawyers and bribes to officials and less hassle.

Thirdly, the tax rate applicable to disclosures was below the maximum marginal tax rate on ordinary income disclosures prevailing at the time. For tax payers whose disclosures were large enough to fall in the highest income bracket (25%), therefore, this amnesty amounted to allowing a concessional tax rate relative to taxes liable for earlier and even contemporaneous disclosures.

Fourthly, the tax rate was so low that tax payers were disclosing white incomes in the amnesty year to disguise them as black income disclosures instead, in order to take advantage of the lower liability rate. Many tax advisors were able to convince taxpayers to avail the amnesty by emphasizing this opportunity to pay taxes at concession rates for future incomes.

Fifthly, greater media coverage was utilized to create awareness of the scheme than ever before.

Sixthly, those already detected by the Income Tax Department for concealment could declare and escape having to pay the highest tax rate as well as penalties.

Seventhly, the government made it clear that there would be no more tax amnesties in the near future. This encouraged many people to take the opportunity provided.

However, the most interesting and thought provoking reason given for such a good result was the work done by the Central Intelligence Cell (CIC) of the NBR. Manned by the officers of both the Taxation Cadre and the Custom and Excise Cadre this cell has formidable powers of calling for information. In the time that they have been in operation (less than two years) Taka 106,95,24,578 of tax evasion has been detected. Prominent people have been unable to explain their (or members of their family) phenomenally large bank balances.

This reasoning is interesting in that it conforms to the literature on positive incentives which argue that positive incentives work the best when there exists a disincentive in conjunction to it. The fact that the scheme worked better because of the threat posed by the existence of the CIC and their imposition of the highest tax rate on the income of tax evaders, if caught, confirms this. 'Economic incentives for tax compliance depend on the institutional environment for detecting and penalizing non-compliance encompassing tax administration, the legal system, accounting norms, information technology besides the tax structure and macroeconomic variables' (Dasgupta & Mookerjee, 1998).

While the amnesties have been effective incentives to make people pay taxes on previously undeclared income, whether or not they encourage greater tax compliance is not evident. However, it can be said that positive incentives are more effective if there are negative incentives attached to them. The Tax Amnesty of 2005-2006 received greater response because of the existence of the threat of strong measures taken against people who were to be found to have evaded taxes. Although the NBR has warned of severe punishment for tax evaders before, never before had this threat been so rigorously implemented than it has been done, especially through the CIC. Thus, we see that Tax Amnesties in the past had performed poorly because of the lack of accompanying negative incentives.

This conforms to the available literature on incentives which stipulates that a taxpayer's decision to conceal will depend on the relative strength of 'temptation' to conceal income and the possibility of 'punishment' if caught. Dasgupta & Mookerjee (1998) opine that 'the degree of voluntary compliance will increase whenever the probability of punishment and pecuniary fines increases: slacker enforcement reduces the punishment effect, while leaving the temptation effect unchanged.'

Responses to tax amnesties were the greatest when the rates were the lowest. However this means that the gain in comparison to potential revenue earnings was lower. Secondly, the amnesty lowers involuntary collections from penalties to an extent that tends to outweigh the direct amnesty receipts, and the revenue gains from increased compliance. Third, once the government repeatedly offers these amnesties they will come to by anticipated by taxpayers. This dilutes the deterrent effect of enforcement efforts further, causing an increase in tax evasion in the years prior to the amnesty' (Dasgupta & Mookerjee, 1998). Thus we see that when the taxpayers knew that an amnesty would be given, response was low.

Those interviewed were unanimous in their opinion that tax amnesties were not a good programme in the long run because of their negative impact on tax compliance. It encourages dishonest people to continue evading taxes and discourages honest tax payers from continuing to pay taxes. Amnesties may be short term solutions to revenue constraints but not a permanent substitute for tax enforcement.

There was a substantial increase in collection in that year, Taka 7,140 crore, up from Taka 5,577 crore in 2004-05 which is a 28% increase in revenue collection (Rejaul,2006). But only future revenue collection will show if the amnesty has helped depending on whether they rise or fall.

8.2 Programme 2: Reward

From the data collected and the interviews taken, rewards have had positive effects on both revenue collected as well as tax compliance.

Table 9
Reward Given as a Percentage of Revenue Collected from Detected Concealment During FY 2005-2006 (in Taka)

	Revenue	Reward	Related Income	Reward as % of Revenue
VAT	26,56,63,638.69	50,00,000	23,61,45,456*	1.88%
Customs & Excise	8,41,88,653.15	60,00,000	15,21,78,747.87	8.43%
Income Tax	3,42,65,573.00	13,00,000	13,70,62,292**	3.79%
CIC	51,61,55,792.00	57,50,000	688,20,77,230***	1.11%
Total NBR	**90,02,73,657.57**	**1,80,50,000**	**740,74,63,725.87**	**2.00%**

Source: NBR (2006),

From Table 8.1 we see that Taka 18.05 million was given as reward to the officials of the four wings of the NBR and their informants during the financial year 2005-2006 for collecting over Taka 900 million in revenue from detecting tax evasion. This reward is equal to 2% of the revenue earned. Put another way, if we consider reward as a type of expense, then it cost 2 paisa to collect every 1 taka of revenue. Although by any estimation this is cost effective, it does not show the complete picture.

Firstly, since reward can be claimed for detecting evasion of any financial year, the revenue collected shown may not necessarily be of 2005-2006. This may reduce the actual revenue significance of the programme. Furthermore, the reward does not reflect the amount of evasion detected. Considering the amount of evasion detected the reward should be greater. However, the policy is to reward everyone who applies, so that ultimately everyone gets only a fraction of what s/he is entitled to.

However, what is more significant is the fact that this does not denote the total evasion detected for that year. Due to the fact that an official has to apply for a reward for himself and his/her informant, many acts of detection go unrewarded just because s/he did not apply for a reward either because s/he just did not have the time to apply or s/he did not think it reward-worthy.

Secondly, according to those interviewed, the existence of this programme acts as an incentive to officials to remain honest. Many officials use this reward to augment their salaries. So it acts as an incentive to detect concealment or evasion more vigorously. From a governance point of view, this result is of more significance than the revenue collected.

Thirdly, although rewards have been received by the same people many times this does not mean that the reward system is dominated by a handful of officials. There are a number of reasons for multiple-reward recipients. One obvious reason is that some officials are better at detecting tax evasion and so are eligible to apply for rewards. Another reason is that although tax evasion can potentially occur in every jurisdiction, evasion occurs more frequently at certain posts, such as custom's border posts and Zia International Airport or the CIC. Thus, officials posted in those offices detect more evasion and thus get rewarded more frequently.

Fourthly, despite being operational for only 2 years, the CIC has been the most successful wing in detecting tax evasion, contributing to 58% of the revenue collected from detecting tax evasion. The officials of the CIC have the authority given to them by the Chairman of the NBR to perform the duties, execute and enforce the provisions of the Income Tax Ordinance 1984, the Customs Act 1969, the Value Added Tax Act 1991 and the rules, regulations and statutory orders issued under those laws. Although the powers bestowed upon them are quite formidable, the real strength of the Cell comes from its close ties to the Chairman of the NBR. All assignments are approved by the Chairman himself in writing. It is a well known fact that the Chairman takes an active interest in the work of the CIC and media coverage has helped to get this message out to the general public. It has worked as a disincentive to taxpayers to evade taxes and has created greater wariness among them if not encouraged complete tax compliance. The impact of the CIC is also felt in programme1, tax amnesties.

An interesting fifth finding is that many officials said that reward does not need to be monetary to be effective and that recognition of one's efforts is equally motivating. Censure is a common enough occurrence for mistakes but to be congratulated for work well done is rare in the civil service. It is not the practice nor in the culture of the Bangladesh civil service for senior officers to praise junior officers. If it is done it is an exception rather than the case. However motivation to excel can come from praise and recognition just as well as from the prospect of getting reward.

Most officials are dissatisfied with the current reward programme for a number of reasons. Firstly, reward is given only if full collection of revenue has been made. However, collection depends on the wishes of the taxpayer to pay and this should not detract from the efforts made by the officer to detect evasion. Secondly, reward is limited only to detecting evasion and not for any other criteria. Many officials interviewed feel that other performances such as exceeding the annual target in revenue collection should also be made reward worthy so that whole zones may be motivated to do better as is done in Sri Lanka.

8.3 Programme 3: Cattle Corridor

The use of this method to deal with cattle smuggling has a number of advantages. Firstly, Bangladesh has access to a cheap source of protein and India gets rid of its excess cows which would plague the country like rodents if Bangladesh were not to take them. Secondly, the government gets tax revenue worth Taka 48,11,79,000/-annually (2002-2003 figures) with the minimum amount of administrative cost and hassle. Even if it could legally import cattle from India, which it cannot, it would still involve the same amount of money as it does now, maybe even more, with administrative costs and bribes to officials. Then the obvious step would be to increase the number of corridors to increase revenue collection. Each corridor has to be headed by an inspector of customs but unfortunately, there are an insufficient number of inspectors to man more corridors and the revenue earned is not high enough to justify the expense.

Although it was hoped that through this simplification of procedure related to the cattle brought through the corridors would reduce cattle smuggling, it has not completely wiped it out. People who are in the position to know believe that if one cattle comes through the corridor, at least two more cross the border without paying customs duty. The reason for this is that then they do not have to pay the taka 500/- as customs duty. They can pay less to a BDR official or nothing at all if they do not get caught which is a strong positive incentive to continue smuggling. However, another reason provided is that the amount of customs duty is not the problem, rather it is the accompanying bureaucratic red-tape and bribery which it entails that acts as a deterrent or negative incentive of using the corridor. Furthermore, the receipt received from the customs office is sometimes used once or twice more on the same day for cattle smuggled in at check posts that lie between the border check posts and the cattle's final destination.

However, one positive side of the corridor cannot be overlooked. Many officials who have worked at the corridor have described the incredible growth of activity which immediately arises as a result of the set up of a corridor where there was no or little economic activity. Hotels, roadside restaurants, gas pumps, grocery shops, barber's shops confectionaries spring up as if overnight to meet the needs of the cattle merchants who come to the corridor. Without the corridor it would not have been possible for this to take place. That is why many customs officials are asked by locally elected officials to establish corridors in their localities.

Although corridors are an innovative way to deal with cattle smuggling, it is not an option to curb other forms of smuggling. The corridor option would reduce the revenue earned through official channels. Lowering of customs duty as an obligation under the WTO has led to a greater reduction in smuggling than any other method attempted so far. Large scale importers and exporters are more willing to pay the reduced customs duty than to risk their investment in the uncertainty of smuggling.

General Findings

Positive incentives do lead to increase in revenue collection from the underground economy. What is more significant is the amount of money that leaves the underground economy and enters the formal economy as a result of these programmes as is summarized in table 10.

Table 10

PERFORMANCE OF THE 3 PROGRAMMES IN F/Y 2005-2006 (in Crore Taka)

Programme	Revenue Collected	Money entering the Formal Economy from the UE
Cattle Corridor	48.61	973.16
Reward	38.41*	52.53*
Tax Amnesty	345.24	4603.00
Total	**432.26**	**5628.69**

Source: NBR, 2006

*These figures are low because when the CIC detected evasion, they asked the taxpayers to avail the tax amnesty and pay 7.5% tax. Thus the revenue collected by the CIC and the money affected are already included in the figures for the tax amnesty.

If 973,163 number of cattle entered the country through the corridors in the financial year 2005-06 and we assume that the average value of a cow to be Taka10,000/- then we can estimate that the amount of money that enters the formal economy is Taka 973.16 crore. We already know that Taka 4603 crore was whitened under the amnesty. This means that approximately Taka 5628.69 crore entered the formal economy from the underground economy in the financial year 2005-06 from these three programmes alone. This is not very high if one considers that Taka 40,000 crore to Taka 50,000 crore still remains in the underground economy, according to some estimates (Bhorer Kagoj,2006), but the amount is not negligible either if one takes into consideration the revenue requirements of the state and the need to contain the underground economy within manageable proportions.

Chapter 9

Conclusion and Recommendations

9.1 Conclusion

When one asks the question, what is the main objective of the NBR, and the answer is revenue collection even that is not achieved if present increased revenue collection is at the cost of future revenue earnings as a result of weak enforcement and dilution of penalty measures.

The results of the programmes become even less favourable if the answer to the question what is the objective of the NBR is not revenue collection. The NBR is the key instrument of fiscal management of the economy and as such has more responsibilities than mere revenue collection. Through the NBR the mandate of the government, and thus theoretically the people of Bangladesh, is implemented. Social, political as well as economic goals are achieved through the fiscal policy.

An example to explain the point. The NBR could tax the agriculture sector which contributes about 29.67% of the GDP (GOB,2006) and make large revenue collections and yet the income of people whose sole source of income is from agriculture remains tax free in Bangladesh as does the income from poultry and fisheries. This is because the agricultural sector is the largest employer in the country and continues to feed the population of Bangladesh despite it burgeoning to 140 million, on increasingly less cultivable land and without almost any government subsidizes. More is achieved by not taxing this sector than the benefit of increased revenue collection, besides being political suicide for any party which attempted it.

The argument of revenue needs is not supported by many of those interviewed. Revenue is only one side of the equation. If revenue is limited, attempts should be made to curb unnecessary expenditure rather than increasing revenue to support it. All out efforts to increase tax collection at the expense of reduced tax compliance to pay for exorbitant phone bills of Parliamentarians, to keep sick industries running and/or to avoid taking stringent but necessary fiscal measures rather defeat the purpose.

Thus, revenue collection is not the main concern. Garnering respect for the law in general and tax law in particular are more important objectives. The idea that misdeeds shall not go unpunished is an important prerequisite to the establishment of law and order in any state the absence of which leads to loss of faith and respect in the government and all other institutions. Thus ensuring tax compliance is a more important objective of the NBR. Civil servants did not pay taxes on their salaries in the past. Since the financial year 2005-2006, all civil servants who were receiving salaries of a taxable level had to pay taxes. The tax payments that are made are reimbursed. Book transfers could have been made with the same result but the objective is to encourage tax compliance which does not only involve tax payment but the submission of returns in due time, declaring accurate and honest income figures as well as carrying out the duties and responsibilities that fall to one as per tax law. Developing this habit will have far better effects not only on revenue collection but respect for the rule of law in general.

If we come back to the question of how to tackle the problem of a large underground economy and keeping it within manageable limits, especially from the point of view of tax policy, the three programmes have varying degrees of success. Tax amnesties do move money from the UE to the formal economy but not at a high rate and does not do anything to stop future tax evasion. If the government has to resort to another tax amnesty, it should be for only one year, and have some form of conditionality so that the money is invested or remains in the country. It also should not be anticipated or it will encourage people to evade taxes until the time of the amnesty. The reward programme indirectly reduces tax evasion by encouraging greater diligence of officials to detect evasion. It too however does not directly lead to greater tax compliance. The cattle corridor is a unique case. It allows cattle to enter the country through the payment of customs duty. Although this makes it official in essence it still remains an act of smuggling. The number of cattle that enter through the corridor also still remains insufficient in comparison to the number that get smuggled in. However, the programme, even if it has no effect on reducing the underground economy, does not have any negative impact on the formal economy either. It is a solution to a unique predicament which should be developed more so that more cattle enter the country through these corridors. As already stated, none of these programmes strike at the root causes of the UE but rather deal with it from the perspective of 'live and let live' in which the beast is not killed but milked of its power, that is its money.

One must remember here that reducing the size of the underground economy is not an end in itself. If that were the case them we could legalize gambling, prostitution, drinking alcohol and drug use to substantially reduce the UE! Rather, the purpose is to ensure that everybody has the same rights and obligations under the law and that no one escapes from fulfilling his/her obligations at the expense of others. Thus the objective would be to reduce tax evasion and encourage greater tax compliance. Side by side with tax reform other measures such as liberalizing foreign trade sector, especially the import sector, which is a major contributing factor to the growth rate of the underground economy, encouraging private investment by opening more investment opportunities in the formal sector and fiscal discipline should be introduced (Hassan, 1997). However, this paper will only concentrate on alternative approaches that can be pursued by the NBR, to address the issue.

Recommendations

As already mentioned tax evasion accounts for 89% of the UE (Barkat, 2004) and there is nothing that improves tax compliance more than improving the tax administration and the institutions with which it works.

Training of officials of all three wings of the NBR is crucial to improving the tax administration. I do not mean just training on administration or tax laws or accounting which are of course important but the development of expertize in specific fields. Although the general belief is that it is sufficient for officials to have common sense to do his/her job much more can be achieved through specialization. Customs officials with specialized knowledge in narcotics can have a greater chance of detecting drug smuggling. Currently they have to depend upon chemical tests conducted by a second party to confirm what they have captured is really narcotics, by which time it has turned into talcum powder. 'The right man for the right job' is still not what determines who works in which post in the civil service in general. There are many officials who have trained as well as studied abroad on specific issues related to the revenue department. However, their expertize is never sought nor are they placed in any position where it may be utilized. This is a waste of human resources and results in that resource being depleted as a result of disuse.

Furthermore, due to limited resources, the training provided is usually of poor quality and since the training has no effect on the job of the official just as long as s/he passes, the trainee is equally reluctant to learn. The training must be improved and have an affect on either promotion prospects or even postings to be beneficial to the official and improve administration as well.

Expertise should also be developed in the courts to which the taxpayer can appeal if aggrieved of any assessment made against him/her. Many judges do not have a clear grasp of income tax law as a result of which cases are heard which are not admissible in the courts. Some tax officials should develop legal expertize so that they can oppose these cases and have those cases dismissed that are inadmissible in court.

Currently there are dual processes working side by side so that one can submit one's income tax return under self assessment as well as under normal procedure. The difference between the two is that under self assessment one assesses one's own income and pays tax on it accordingly while under normal assessment the department assesses one's income. The advantage of self assessment is that not all returns need to be scrutinized each year. A small number are audited depending on the merit of the case and the official can spend more time on each case. At the moment s/he not only has to audit all the cases selected under the self assessment procedure but all the returns submitted under normal procedure under. This allows very little time to scrutinize cases properly and reduces the likelihood of detecting evasion. The recommendation is to introduce universal self assessment so that everyone submits under one procedure. This will greatly reduce the workload of each officer and increase the quality of each assessment as well as increase the likelihood of detecting tax evasion. Furthermore, the philosophy should be not to go after everyone, only the serious cases and make an example of them to create a deterrence to tax evasion. Currently, tax evasion is treated as a civil offence and offenders are only fined. Work is in progress to create the Criminal Investigation Department (CID) which will be given the responsibility to take criminal action against tax evaders and put them in jail.

Ignorance is a big reason for low tax compliance. Tax education through the media is crucial. Many assessees are misled by unscrupulous tax advisors as to their rights and responsibilities and become defaulters through no fault on their part. Public awareness building would reduce the opportunity to be misled and also keep taxpayers up to date on such things as when to submit their return and whether they are eligible to submit returns or not and so on. Mass media has the advantage of getting the message through quicker. The picture of the Chairman of the NBR having a BMW cut up into pieces because the owner had not paid the right custom duty on it sent a clear message that the Board was serious about taking action against tax evasion. Simplification of procedures would also improve tax compliance.

Modest expansions in the number of assessing officers would increase taxpayer compliance substantially even at prevailing efficiency levels. (Dasgupta & Mookerjee, 1998)

The fact that files, registers and records are still kept manually is a serious hindrance to the job of detecting tax evasion because it keeps officials tied up keeping record by hand for hours on end. Computerization would eliminate this tedious task and give more time to officials to spend to scrutinize files and detect concealment. More than that, it will make reports more accurate and studying each file much easier. Although the NBR has two websites on the internet, they are still in their infancy. They should be made more interactive so that they one can not only download the return form but can get answers to tax related questions, submit their returns on the internet and get certificates. This will reduce the interface between tax officials and the general public which is known to lead to greater instances of corruption. The fear of what might happen in the hands of officials also leads to people trying to evade the tax net. All these problems can be solved as well as providing better service by installing a more interactive website which is updated regularly. Computerization would also improve the monitoring capabilities of the NBR. At the moment each circle gives TINs to taxpayers under its jurisdiction and then sends this information to the NBR. If the same person has received two TIN numbers the NBR informs the concerned circle by which time the assessee has already submitted his/her return. Unscrupulous taxpayers and their lawyers do keep more than one file so that they can show different sources of income in each file so that they can take advantage of lower tax rates and the 0% tax limit. Local area networking connecting the circle office computers to the NBR computers would make it possible to check immediately whether or not a taxpayer already has a TIN. At the moment there are two identification numbers for VAT payers and tax payers who are in many cases the same person. CIC has detected a lot of concealment by comparing and finding discrepancies in the information given by taxpayers in their VAT file and the income tax file. This idea can be taken one step further so that every tax payer has one identification number. This would make cross referencing easier and tax evasion harder.

Greater work needs to be done in Bangladesh on the issues of tax compliance and the underground economy so that a tax policy can be formulated that will decrease the incentive to enter the underground economy through tax evasion and increase tax compliance.

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Annex

1

184D. Reward for collection and detection of evasion of taxes.—

Notwithstanding anything contained in this Ordinance or any other law for the time being in force, the Board may, in such manner and in such circumstances and to such extent as may be prescribed, grant reward to the following persons:-

(a) an officer or employee of taxes department for outstanding performance in collection of taxes and detection of tax evasion;

(b) any other person for furnishing information leading to detection of tax evasion.

This section was inserted by the Financial Act, 2000. As per this act, rules were supposed to be established as to the criteria for eligibility and amount of reward to be paid. Unfortunately, so far no such rules have been formulated. In the Income Tax sub department, this reward is given on the basis of the Income Tax (Reward) Order, 1980:

ORDER FOR MONETARY REWARD TO INFORMANTS OF THE CONCEALMENT OF INCOME AND EVASION OF TAXES

(Dated the 21st November, 1980)

C. No.8(53)T-111/78.-Whereas the National Board of Revenue, Government of the People's Republic of Bangladesh, deems it expedient to detect concealment of income and evasion of taxes by an individual, firm, association of persons, company or Hindu undivided family and to encourage information to this end from members of the public or Officials of the Taxes Departments, the Board has been pleased to pass an order as follows:

2. The Order may be called the Income Tax Reward Order, 1980, and applicable to the whole of Bangladesh.

3. (a) 'Board' means the National Board of Revenue constituted under the National Board of Revenue Order, 1972

(b) 'Tax' means Income Tax, Wealth Tax, Gift Tax, Sales Tax and Estate Duty as defined in the respective Acts.

(c) 'Income' includes any income defined in the aforesaid Acts

(d) 'Dispute' includes appeal, revision and reference to Hon'ble Supreme Court

4. (a) The following shall be scales of reward to the members of the public;-

(i) Where the tax sought to be evaded is Tk.20,000/- or less	25% of the tax sought to be evaded
(ii) Where the tax sought to be evaded exceeds Tk.20,000/- but does not exceed Tk.5,00,000/-	Tk.5,000/- + 12 $^{1}/_{2}$ of the tax to be evaded as exceeds Tk.20,000/-
(iii) Where the tax sought to be evaded exceeds Tk.5,00,000/-	Tk.65,000/- +5% of the tax sought to be evaded as exceeds Tk.5,00,000/-

(b)Taxation Officials including the ministerial staff but not above the rank of an [Inspector]* who show extraordinary initiative and render meritorious services in detecting tax evasion may be given cash reward which shall not ordinarily exceed two year's salary in any one case.

5. (a) Every Commissioner of Taxes shall be competent to sanction reward not exceeding Tk.10,000/-.

(b) Any reward exceeding Tk.10,000/- will be sanctioned by the National Board of Revenue.

(c) Payment may be made provisionally up to half of the admissible reward on completion of assessment and the granting authority is satisfied that the assessment is likely to stand the test of appeal or revision or reference.

(d) The balance of the reward may be made after the final decision of dispute, if any, arising there from and realization of the amount thereof.

6. Reward cannot be claimed as a matter of right.

7. The proposal for reward is to be submitted to the Commissioner of Taxes by D.C.T., I.J.C.T. and to the Board by the Commissioner of Taxes, as the case may be, in the form to be prescribed by the Board.

8. Any action towards reward should be processed most confidentially as a safeguard to the informer.

9. The National Board of Revenue may prescribe any guideline from time to time in implementing the Order.

Table 11

Trend in Revenue Collection of Bangladesh from Financial year 1972-73 to 2004-05

Financial year	GDP (at market price)	Total Revenue	Revenue as % of GDP	Total Tax Revenue	Tax Revenue as % of GDP
1972-1973	4625.8	171.23	3.7	169.8	3.67
1973-1974	7327.6	292.29	3.99	288.89	3.94
1974-1975	12690.5	505.46	3.98	430.49	3.39
1975-1976	11044.9	848.26	7.68	713.39	6.46
1976-1977	10976.1	923.08	8.41	770.23	7.02
1977-1978	14763.4	1152.94	7.81	998.21	6.76
1978-1979	17416.3	1418.81	8.15	1216.58	6.99
1979-1980	28077.7	1695.41	6.04	1458.79	5.2
1980-1981	32213.6	2295.45	7.13	1831.44	5.69
1981-1982	36174	245.43	6.48	1978.53	5.47
1982-1983	40830.8	2470.65	6.05	2134.24	5.23
1983-1994	48978.7	2789.57	5.7	2372.49	4.84
1984-1985	56194.4	3576.38	6.36	2967.22	5.28
1985-1996	63269.1	4083.11	6.45	3302.97	5.22
1986-1987	72771.1	4685.2	6.44	3866.2	5.31
1987-1988	79992.9	5202.71	6.5	4423.71	5.53
1988-1989	89059.8	5771.97	6.48	4845.49	5.44
1989-1990	100328.8	6711.87	6.69	5715.01	5.7
1990-1991	110518.1	7995.35	7.23	6587.5	5.96
1991-1992	119542.4	9876.72	8.21	7900.72	6.61
1992-1993	125369.5	11321.98	9.03	9254.98	7.38
1993-1994	135412.3	12388.53	9.15	9724.74	7.18
1994-1995	152517.8	14089.53	9.24	11356.03	7.45
1995-1996	166324	15408.04	9.26	12174.1	7.32
1996-1997	180701.3	16663.9	9.22	13452.92	7.44
1997-1998	200176.6	17589.75	8.79	14792.83	7.39
1998-1999	219697.2	18805.36	8.56	15750.21	7.17
1999-2000	237085.6	21029.41	8.87	16081.36	6.78
2000-2001	253546.4	23180.44	8.54	19777.44	7.29
2001-2002	273201.1	25900.21	9.48	21315.21	7.8
2002-2003	300580	30871.12	10.27	24717.12	8.22
2003-2004	332973.1	30943.77	9.29	27430.77	8.24
2004-2005	370707	38268.46	10.32	31325.46	8.45

Source: NBR (2006), Annual Report 2004-2005, (Yet to be published)

Tax revenue is very low in comparison to total GDP, ranging from 3.39% to 8.45%. The only consolation is that the percentage is increasing

Graph 1
Trend in Revenue Collection of Bangladesh from F/Y 1972-1973 to 2004-2005

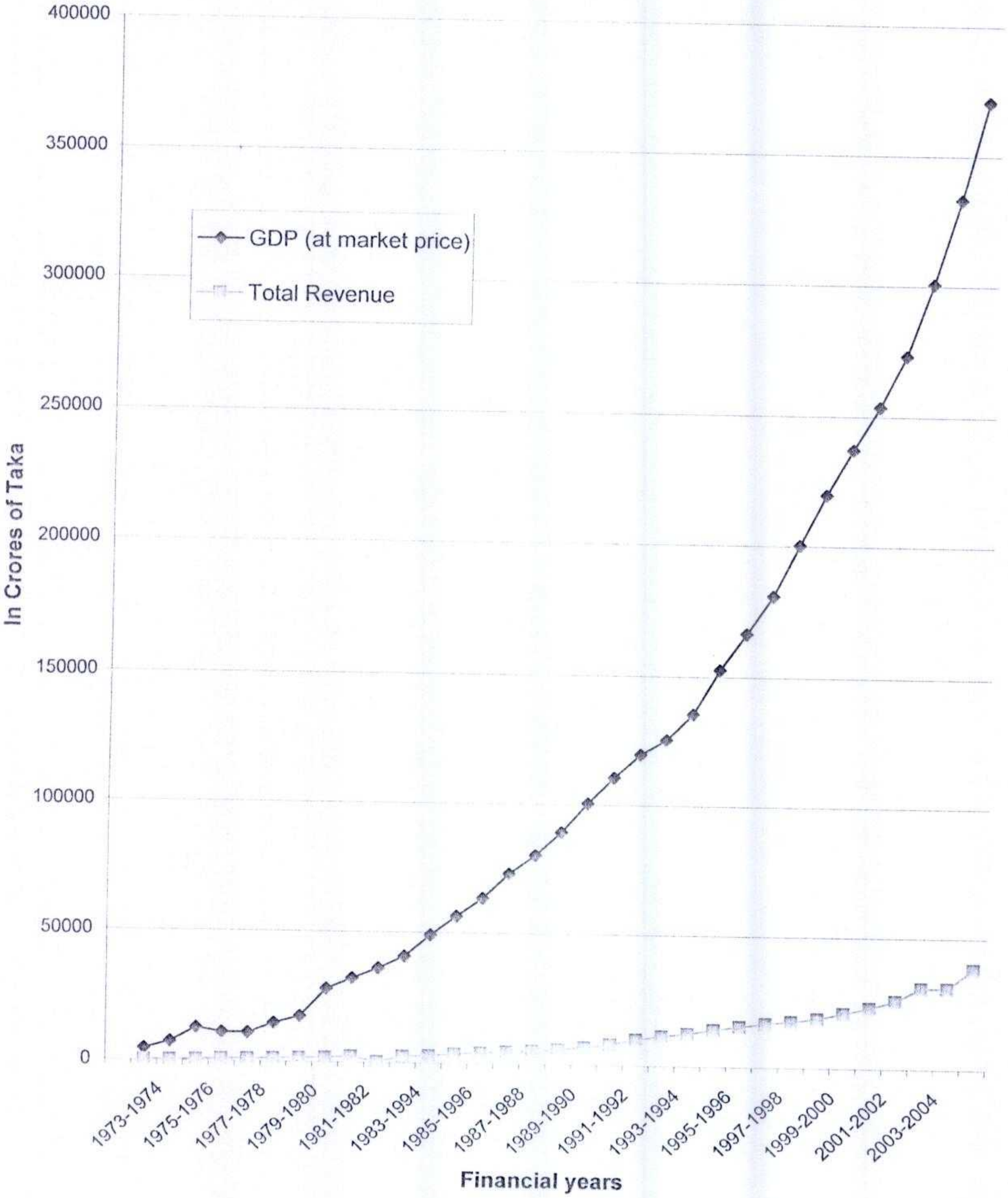


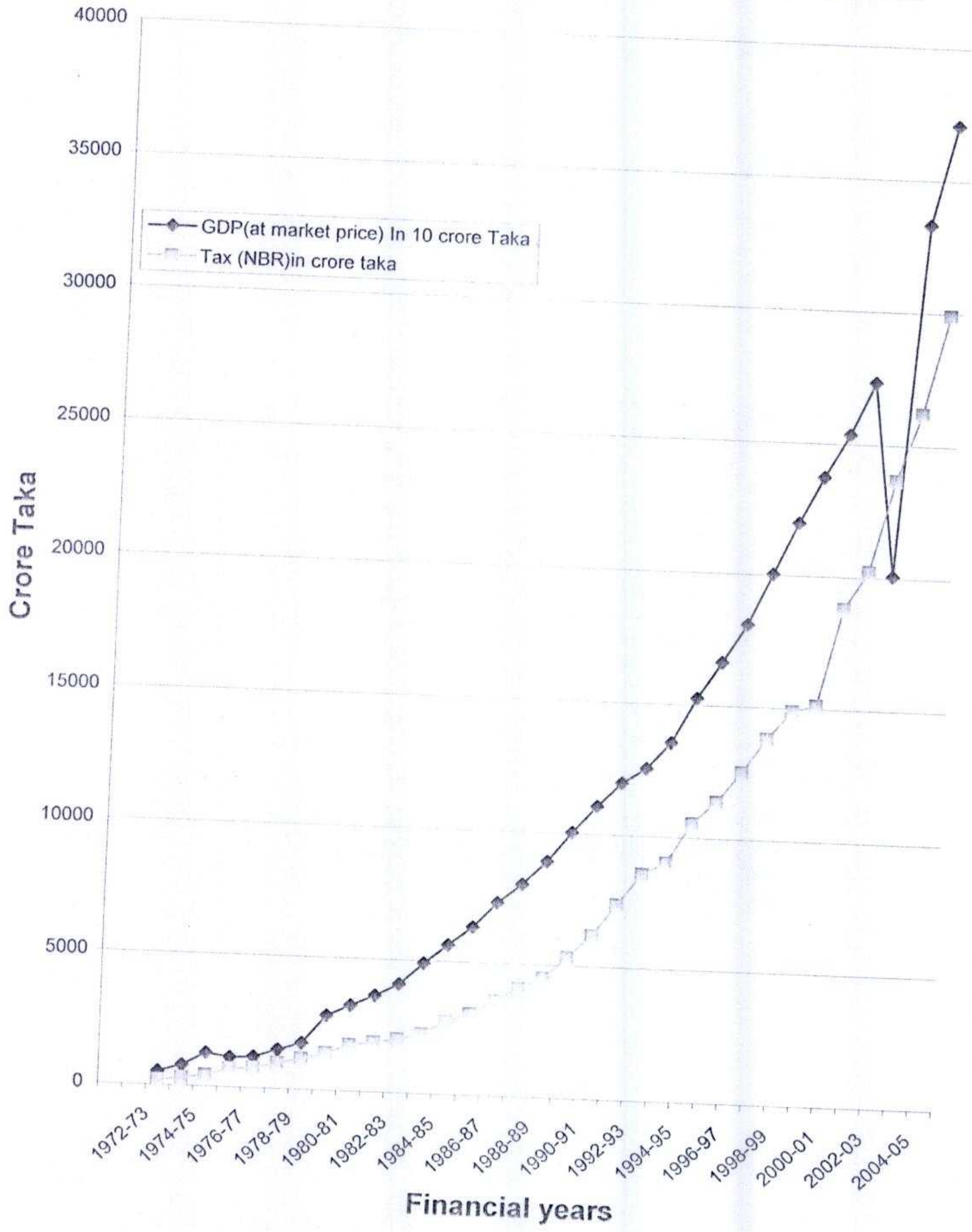
Table 12

Revenue Collection of NBR to GDP Ratio from FY 1972-73 to 2004-05 (In Crore Taka)

Financial Year	GDP(at market price)	Growthin GDP	Tax (NBR)	Growth in Revenue	Revenue(NBR) to GDP ratio
1	2	3	4	5	6
1972-73	4985.30		166.3		3.34
1973-74	7575.20	51.95	278.08	67.22	3.67
1974-75	12436.90	64.18	410.29	47.54	3.30
1975-76	11032.00	-11.30	673.63	64.18	6.11
1976-77	11600.30	5.15	726.07	7.78	6.26
1977-78	14519.40	25.16	939.66	29.42	6.47
1978-79	17404.70	19.87	1146.78	22.04	6.59
1979-80	28077.70	61.32	1378.14	20.17	4.91
1980-81	32213.60	14.73	1722.79	25.01	5.35
1981-82	36174.00	12.29	1853.54	7.59	5.12
1982-83	40830.80	12.87	1999.72	7.89	4.90
1983-84	48978.70	19.96	2231.29	11.58	4.56
1984-85	56194.40	14.73	2724.38	22.10	4.85
1985-86	63269.10	12.59	3054.13	12.10	4.83
1986-87	72771.10	15.02	3572.20	17.09	4.91
1987-88	79992.90	9.92	4068.71	13.77	5.09
1988-89	89059.80	11.33	4490.99	10.38	5.04
1989-90	100328.80	12.65	5292.01	17.84	5.27
1990-91	110518.10	10.16	6152.05	16.26	5.57
1991-92	119542.40	8.17	7347.72	19.43	6.15
1992-93	125369.50	4.87	8537.78	16.20	6.81
1993-94	135412.30	8.01	8995.51	5.36	6.64
1994-95	152517.80	12.63	10522.56	16.98	6.90
1995-96	166324.00	9.05	11370.06	8.05	6.84
1996-97	180701.30	8.64	12503.25	9.97	6.92
1997-98	200176.60	10.78	13801.79	10.39	6.89
1998-99	219697.20	9.75	14869.29	7.73	6.77
1999-00	237085.60	7.91	15123.25	1.71	6.38
2000-01	253546.40	6.94	18774.44	24.14	7.40
2001-02	273201.00	7.75	20207.21	7.63	7.40
2002-03	200580.10	10.02	23651.12	17.04	7.87
2003-04	332973.10	10.78	26192.90	10.75	7.87
2004-05	370707.00	11.33	29904.46	14.17	8.07

Source: NBR, Annual Report 2004-05 (2006), Dhaka. (Yet to be Published)

Graph 2
GDP to Tax Collection Trend from FY 1972-73 to 2004-05



Graph 3
Comparison Between GDP and Revenue Collection Growths from FY 1972-73 to 2004-05