Ending Exploitative Taxation: A Zakat-Based System for Justice, Economic Growth, and Welfare for All

ARTICLE

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Economic inequality is a long-standing challenge in the modern world, where traditional tax frameworks have not always ensured equitable wealth distribution and sustainable economic growth. Although governments all over the world use elaborate tax systems to finance their social services and welfare services, most of these systems unintentionally tax the poor downwards, as they do not sufficiently deal with wealth accumulation among the rich [1]. However, as an alternative, the Islamic economic concept of zakat provides a mechanism of wealth redistribution based on moral obligation, economic justice, and social welfare, which has shown quantifiable effects in reducing poverty and promoting economic growth.

Taxation: A Dilemma of Crisis

Modern tax systems of both developed and developing countries are becoming more dependent on regressive taxation systems that disproportionately impact the lower-income earners. A study conducted in 125 countries shows that even though international financial institutions publicly support progressive taxation, low- and middle-income countries are disproportionately encouraged to take regressive policies like value-added taxes and consumption taxes [1]. These indirect taxes are more of a burden to the working-class families than the rich because the poor households utilize a bigger percentage of their income on consumables and services.

The modern taxation system is an inherent issue in the world economic system. In third-world countries (developing and underdeveloped regions), the income and wealth direct taxes that would lead to progressive redistribution and play a role in the total revenue are inadequate [2]. In the meantime, corporate income taxes are major impediments to economic growth, and research in European Union (EU) countries has shown that corporate income taxes have a negative effect on economic growth [3, 4]. Moreover, evasion and avoidance of taxes by multinational corporations and the rich deprive developing countries of much-needed revenue, which results in what is termed by scholars as fiscal impoverishment- where tax systems drive households into even greater poverty instead of pulling them out [4].

The inefficiencies are also caused by the administrative burden of traditional taxation. The complicated tax laws necessitate elaborate enforcement mechanisms and, hence, high compliance costs to both the taxpayers and governments [5, 6]. In developing nations, the tax net expansion is usually obsessed with informal sectors and small businesses. It does not effectively tax the privileged citizens and big businesses [5, 6]. This practice not only creates a lack of revenue but also continues to create economic injustice.

Zakat: Principles and Economic Philosophy

The Zakat is a fundamental obligation among the five pillars of Islam and is a unique and completely different way of recycling wealth among the population. Zakat opposes the traditional taxation system. In contrast to traditional taxes, which are entirely based on imposing fines and collecting externally, the Zakat is a religious duty of Muslims who have a Nisab limit [6]. The Nisab limit is 85 grams of gold or its equivalent. The Muslims possessing Nisab limit pay 2.5% on surplus wealth on their own will. This threshold system makes sure that only the rich pay taxes, and this automatically safeguards the poor and the lower-middle classes against the burden of taxation. [6].

The zakat system has several principles that make it different to traditional taxation. To begin with, it levies a flat rate of 2.5% per annum on qualifying wealth that has been held in one lunar year (haul) [7]. This rate is charged equally irrespective of the level of wealth, but the Nisab exemption ensures the system is progressive in nature, as those who do not have surplus assets are not subject to it. Second, zakat does not focus on income but on accumulated wealth and stimulates productive investment and discourages hoarding [8]. Third, the Quran explicitly identifies eight groups of recipients (Asnaf), namely: the poor (Fuqara), the needy (Masakin), those in charge of zakat (Amil), new converts (Muallaf), those in bondage, debtors (Gharimin), those in the path of Allah (Fi Sabil), and travelers in need (Ibn Sabil) [9]. This particularity of categories of recipients guarantees that zakat resources are delivered straight to the most vulnerable groups, as well as supplementing social infrastructure. These categories have been broadened in contemporary interpretations to respond to contemporary socio-economic issues, such as education, healthcare, disaster relief, and empowering small businesses [10].

Empirical Evidence: Economic Development and Poverty Reduction Under Zakat

Empirical studies conducted recently indicate strong support for zakat in terms of economic growth and the reduction of poverty. A multi-country panel study of Indonesia, Malaysia and Singapore conducted from 2003-2020 concluded that the positive and significant impact of zakat distribution on economic growth exists [11]. The study shows that the more zakat funds are channeled to higher consumption, investment and government spending, the more they can stimulate more economic activity [11].

Additional data from eight Muslim countries in the period of 2004-2017 proves that zakat is a powerful economic growth stimulator, which has a greater effect than some traditional development tools. It is worth noting that, in comparison to Foreign Direct Investment (FDI), zakat was found to have a higher coefficient in the increment of per capita income [12]. This high performance is because zakat directly targets the consumption and productive capacity of the lower-income groups, which has direct multiplier impacts on the local economies [12].

The effect of zakat is even more drastic at the poverty reduction level. Research in Morocco has shown that possible zakat collection would not only be able to cover resource gaps in extreme poverty eradication but also create a large surplus [13]. In Indonesia, where the zakat potential is estimated to be around 327 trillion rupiah every year, effective zakat initiatives have boosted MSME (Micro, Small, and Medium Enterprise) incomes by up to 40 % in two years and helped to reduce poverty rates in target populations by 1.76 % [6].

The process of such spectacular outcomes is in the distribution methodology of zakat. Productive zakat focuses on long-term empowerment as opposed to traditional welfare programs that tend to offer temporary relief. Not only do recipients get consumable aid, but business capital, vocational training and continued support to become economically independent. This strategy converts Mustahiq (zakat receivers) into Muzakki (zakat givers), and the economic process is virtuous [14].

Zakat and Taxation: Comparative Analysis of Advantages

The comparative study of zakat and conventional taxation indicates that the zakat system has several structural benefits. First, zakat has better rates of voluntary compliance, which is motivated by religious motivation and faith. Whereas traditional taxation systems need a large bureaucratic apparatus and struggle with the issue of tax evasion, zakat payment is inherently driven by religious faith and the need to gain Godly reward. Research indicates that religiosity and faith are positively and significantly related to intention to pay zakat and that believers perceive payment as a cleansing of wealth and soul and not a liability [15].

Second, the wealth-based evaluation of zakat instead of taxation based on income generates a more equal distribution. Traditional income taxes do not necessarily reflect wealth concentration among the highest earners, who do not receive their income because of wages but through capital gains and investments [16]. The accumulated assets-based approach of the zakat system targets the root cause of wealth inequality.

Third, the administrative efficiency of zakat is higher than that of traditional tax systems. Zakat has a fixed rate of 2.5% with distinct Nisab limits, which means that it does not demand much bureaucratic sophistication. The digitalization, mobile applications, and combined financial technology platforms have made modern zakat institutions more efficient in collecting the funds and lower the transaction costs, increasing transparency [7]. Examples of zakat institutions indicate that good corporate governance practice is a great way of enhancing efficiency in collection and economic sustainability [7].

Fourth, zakat enhances financial inclusion in a better way than traditional fiscal systems. The use of zakat structures by Islamic finance institutions is a direct involvement of underserved groups that are not included in the formal banking systems. Zakat, combined with other Islamic financial tools like waqf and qard-al-hassan, form holistic social safety nets that cater to both short-term and long-term economic growth [17].

Zakat's Modern Challenges and Solution: Pakistan as a Case Study

Despite the prime religious economic obligation, the zakat system in Pakistan is surviving with multi-sectoral challenges like other underdeveloped Islamic parts of the world. The poor administrative system, lack of technological advancement, and structural issues in collecting and distributing the zakat are hindering the national welfare system. The 18th Amendment decentralized the Zakat control system. This decentralization raised concerns of inter-provincial coordination, which resulted in fragmentation and duplication. The unresolved issues deepened the inefficacy of resource distribution [18]. The major areas of wealth are not included; corporate organizations are underreporting zakatable assets, agricultural Ushr collection is not functioning at all, and the huge informal economy, which employs most of the workforce, is not covered by formal zakat systems [19]. Poor digital infrastructure also restricts transparency and trust, and financial and zakat literacy is discouraged. The mistrust of the people has been worsened by institutional inefficiencies, bad governance, and lack of accountability, which lowers the level of formal compliance [20]. The reforming of the zakat system should be based on the alignment of federal and provincial laws to restore tax incentives, introduce the responsibility of zakat in the corporate sector, and reinstate the Ushr collection to assist the rural economy. The use of fintech services like mobile-based zakat payments and QR-codes can increase access, transparency, and institutional credibility [20]. Simultaneously, a simplified form of digital platform must be provided to allow informal sector involvement with the support of literacy and awareness campaigns, both to payers and beneficiaries. The issues of inter-provincial cooperation and coordination, data management, and fair distribution of Zakat could be mitigated through a few legislative and administrative changes. One of those influential administrative and legislative developments is creation of federal Zakat management council under the governance and surveillance authority of the Council of Common Interests [19]. Therefore, well well-established Zakat policy supported through technological advancement, aligned with the current national fiscal policy, resilient toward modern challenges, is effective to enhance poverty reduction, mobilization of domestic funds, economic insulation, and social justice in underdeveloped communities like Pakistan [20].

Conclusion:

The facts clearly show that zakat is a plausible alternative to the traditional exploitative taxation systems. Having proven effects on economic growth, poverty alleviation, reduction of income inequality, and financial inclusion, zakat fills the inherent shortcomings of retrogressive tax systems that impose on the poor and concentrate wealth in the hands of the elites. The moral basis of the system in religious duty produces better voluntary compliance than coercive taxation, and the wealth-based assessment and targeting of recipients make the redistribution fair. With the levels of global inequality approaching a crisis and the traditional fiscal policies being found insufficient, it is now time to take the idea of zakat-based systems as the means of thorough economic reform seriously. Be it complete implementation in Muslim dominated states or the blending of zakat concepts into the secular systems, this 1,400-year-old system provides eternal insight into the realization of justice, inclusive development, and welfare of everyone. Whether zakat is effective or not is no longer a question, but whether the policymakers have the foresight to put it into practice.

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