TOPIC ONE : ENDING EXPLOITATIVE TAXATION

ARTICLE WRITING COMPETITION

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❖ Zakat as a Pathway to Reforming Pakistan's Inequitable Tax Framework

➢ Introduction

Pakistan's taxation system has long faced criticism for its structural imbalances and inability to generate sufficient revenue while maintaining equity across different income and wealth groups. Many citizens, particularly salaried workers, feel the burden of taxation disproportionately falls on them, while wealthy individuals and businesses often exploit loopholes to minimize contributions (INTELLINews, 2025). Amidst growing calls for comprehensive fiscal reform, Zakat, an obligatory form of almsgiving in Islam, offers a culturally and socially resonant method to complement conventional taxation and address systemic inequities that have persisted for decades. This article examines Pakistan's tax challenges, explores Zakat's principles and mechanisms, and evaluates its potential to create a more equitable fiscal framework that serves all citizens fairly and transparently.

➢ Structural Weaknesses of Pakistan's Tax System

Tax-to-GDP Ratio and Revenue Mobilization

A key indicator of fiscal health is the tax-to-GDP ratio, representing the proportion of economic output collected as taxes relative to total national economic activity. Pakistan's ratio remained around **15.7%** in the fiscal year 2024-25, marking the highest level in over two decades according to recent government reports (INTELLINews, 2025). However, analysts note that much of this increase results from temporary revenue measures and one-time collections rather than fundamental structural reform of the tax system itself. Regional peers in South Asia, including India and Sri Lanka, maintain ratios closer to **19 to 20 percent** of GDP, highlighting Pakistan's ongoing gap in revenue mobilization and fiscal capacity (OECD, 2025). This gap represents billions of rupees in lost government revenue that could fund essential public services including education, healthcare, and infrastructure development.

The Heavy Burden of Indirect Taxation

Pakistan's system heavily depends on indirect taxation, particularly sales tax and excise duties, which disproportionately affects low-income households across the country. Households with modest earnings spend a higher proportion of their income on consumables and necessities, resulting in a regressive tax burden that penalizes those least able to pay (Arif, 2023). Conversely, wealthier individuals who invest or save extensively are less impacted by consumption-based taxes because their spending represents a smaller percentage of their total wealth and income. This creates a system where those who can least afford taxation contribute the most relative to their means, while those with substantial resources and accumulated wealth minimize their contributions through various legal and semi-legal mechanisms.

Concentration of Wealth and Income Inequality

Wealth and income inequality exacerbate the system's regressive nature significantly and represent one of the most pressing economic challenges facing Pakistan. Recent data show the top **10 percent** of Pakistanis capture approximately **42 percent** of national income, while the bottom **50 percent** controls only a small fraction of total national wealth (Oxfam Report, 2025). Wealth disparities are especially pronounced in landholdings, commercial assets, and financial portfolios, creating opportunities for tax avoidance and underreporting across multiple sectors of the economy. When such concentration exists, the fiscal burden inevitably shifts downward to ordinary workers who cannot hide their income from automatic withholding systems and transparent employer reporting.

The Informal Economy Challenge

The informal economy accounts for an estimated **35 to 60 percent** of Pakistan's GDP, encompassing cash-based businesses, unregistered trade, and under-the-table labor arrangements that exist outside formal regulatory frameworks (Pakistan Today, 2025). This makes conventional taxation insufficient and ineffective, as many productive economic activities remain unrecorded and untaxed, depriving the government of crucial revenue. The sheer scale of the informal economy means that Pakistan loses substantial tax revenue that could otherwise fund schools, hospitals, infrastructure projects, and social safety nets that benefit all citizens. Addressing this challenge requires innovative approaches that can reach beyond traditional tax administration mechanisms.

➢ Zakat: Principles, Mechanisms, and Scope

Definition and Religious Foundation

Zakat, one of the five pillars of Islam, is a wealth-based religious obligation that differs fundamentally from conventional income taxation in both mechanism and philosophy. Eligible Muslims are required to contribute **2.5 percent** of their accumulated wealth above a minimum threshold known as nisab annually, as specified in Islamic jurisprudence (Al-Qaradawi, 2000). The nisab is typically calculated based on **87.48 grams** of gold or its equivalent cash value, adjusted periodically according to market prices (Quran, 9:60). This mechanism ensures that those with significant assets contribute proportionately to the wellbeing of their communities while those below the threshold are exempted from the obligation.

Zakatable Assets and Comprehensive Coverage

Zakat applies to a comprehensive range of assets, including cash and savings in banks and at home, precious metals such as gold and silver, business inventories and merchandise, investments and certain financial instruments, and agricultural outputs and other productive assets (ICTD & LUMS, 2024). Unlike conventional taxation that focuses on income flows, Zakat is asset-focused, targeting accumulated wealth rather than periodic income earned during the year. This approach means that someone cannot simply reduce their obligations through clever accounting, income minimization strategies, or creative financial structuring. The wealth itself, regardless of how it is held or in what form it is structured, remains subject to the obligation and cannot escape accountability.

Zakat Rates and Recipients

Zakat maintains a fixed rate of **2.5 percent** on most wealth categories and higher rates for agricultural output, typically ranging from **5 to 10 percent** depending on irrigation methods and farming practices (Al-Qaradawi, 2000). Islamic law specifies eight categories of eligible recipients, including the poor and destitute, the needy facing hardship, those managing Zakat collection and administration, individuals whose hearts require reconciliation with Islam, enslaved persons and captives, those burdened by debt they cannot repay, those engaged in religious teaching and service, and travelers in need away from home. This ensures direct redistribution to those in genuine need and reduces opportunities for diversion or bureaucratic inefficiency. The clarity and specificity of these categories prevents Zakat from being misappropriated for purposes unrelated to poverty alleviation and community support.

➢ Zakat versus Conventional Taxation in Pakistan

Targeting Accumulated Wealth Rather Than Income

Pakistan's current income-based taxation often fails to capture the wealth of affluent individuals due to numerous loopholes, exemptions, and underreporting through informal channels and unreported income sources. Many wealthy individuals structure their finances strategically to minimize reported income while continuing to accumulate substantial assets and property holdings. In contrast, Zakat's focus on total assets ensures that individuals holding significant property, financial portfolios, business inventories, or other valuables contribute proportionately regardless of their reported income. This shift could reduce the overburden on salaried workers and small businesses who cannot easily hide their economic activity from employers and government authorities.

Reducing Regressive Burden on Low-Income Groups

Indirect taxes disproportionately affect low-income groups because spending on consumption represents a larger share of their total resources compared to the wealthy. By imposing obligations on wealth rather than consumption, Zakat shifts fiscal responsibility to those better able to contribute economically (Arif, 2023). Consequently, wage earners with minimal accumulated assets would owe little or nothing in Zakat, while wealthy landowners and investors shoulder a fairer share of redistribution responsibilities. This represents a fundamental rebalancing of how the fiscal burden is distributed across society, moving from a consumption-based system to a wealth-based system.

Enhanced Compliance Through Moral and Religious Obligation

Zakat operates as a religious and moral duty rooted in Islamic faith, which encourages voluntary compliance among the faithful without requiring constant enforcement mechanisms. Citizens perceive it as a spiritual obligation connected to their deepest religious beliefs rather than coercion by a government they may distrust due to past experiences with corruption (ICTD & LUMS, 2024). This internal motivation contrasts sharply with conventional taxation, which often relies heavily on enforcement mechanisms, penalties, and audits to achieve compliance rates. When people view a financial obligation as fulfilling a divine command and spiritual responsibility rather than surrendering to state authority, their willingness to comply naturally increases substantially.

Targeted Assistance to Vulnerable Populations

Unlike general tax revenue, which is absorbed into broad government budgets and allocated according to political priorities that may shift with election cycles, Zakat is allocated explicitly to vulnerable groups defined by Islamic law (Al-Qaradawi, 2000). This targeted approach ensures that funds reach intended recipients effectively, contributing to poverty alleviation and social cohesion while avoiding bureaucratic inefficiencies that plague many government welfare programs. The religious framework ensures accountability to principles rooted in Islamic tradition rather than political interests or temporary government preferences.

➢ The Scale of Zakat Contributions in Pakistan

Recent Zakat Collection Figures

Recent studies reveal the remarkable scale of existing Zakat contributions already occurring in Pakistan through voluntary giving, demonstrating the potential of this mechanism. Approximately **50 million Pakistanis** contributed **619 billion rupees**, equivalent to roughly **2.19 billion dollars**, in Zakat during 2024 according to comprehensive surveys (ICTD & LUMS, 2024; ProPakistani, 2025). This amount surpassed significant state programs such as the Benazir Income Support Programme disbursements of **592 billion rupees** and Federal Excise Duty collections of **577.4 billion rupees**, putting Zakat's scale into perspective relative to government welfare mechanisms. The average contribution per donor was roughly **15,000 rupees**, demonstrating that community-based redistribution already mobilizes resources on a scale comparable to major government welfare programs and revenue sources.

Comparison with State Revenue Sources

This data suggests enormous untapped potential for organizing and maximizing Zakat contributions through formal mechanisms and increased awareness of the obligation. If properly formalized and encouraged, Zakat collections could potentially exceed current figures significantly, supplementing government revenues and reducing pressure on conventional taxation. The fact that Zakat already rivals major government revenue sources in absolute terms indicates its potential importance to Pakistan's fiscal architecture moving forward.

➢ Integrating Zakat into Pakistan's Fiscal Framework

Establishing an Independent Zakat Authority

An independent Zakat Authority, separate from the Federal Board of Revenue and other taxation bodies, could oversee collection, assessment, and distribution while ensuring compliance with religious and economic principles simultaneously (ICTD & LUMS, 2024). Such separation would prevent Zakat from becoming entangled with conventional tax policy and potential political manipulation, and would maintain its religious integrity while achieving fiscal objectives. This authority would employ experts in both Islamic jurisprudence and modern finance to ensure proper implementation, accurate calculations, and appropriate distribution according to Islamic principles.

Leveraging Digital Technology for Efficiency

Digital tracking of asset declarations could streamline the process significantly, increase transparency in operations, and reduce administrative burdens associated with manual assessment of wealth (ICTD & LUMS, 2024). Automated systems could assist in accurate Zakat calculation adjusted for inflation and market changes, prevent calculation errors, and maintain comprehensive records that demonstrate compliance across all contributors. Such technological infrastructure would make the system efficient and accessible to all eligible contributors regardless of geographic location, from major cities to remote rural areas.

Public Awareness and Community Engagement

Awareness initiatives are essential to educate citizens about Zakat's social and economic benefits and to encourage broader participation across all economic strata of society. Partnerships with mosques, local religious leaders, and community organizations could enhance participation rates substantially and ensure resources reach those in need most effectively (Al-Qaradawi, 2000). Public campaigns explaining both the spiritual significance of Zakat as a pillar of Islam and its practical impacts on poverty reduction and social cohesion would build consensus for integration into the formal fiscal system.

Complementary Role with Conventional Taxation

Zakat should complement, not replace, conventional taxation in Pakistan's fiscal system. While it effectively redistributes wealth and addresses poverty alleviation, Pakistan still requires broader tax revenue for infrastructure development, healthcare provision, education funding, and defense requirements that affect the entire nation (INTELLINews, 2025). A dual system would leverage the strengths of both approaches to create comprehensive fiscal coverage addressing different aspects of government finance and social welfare.

➢ Challenges to Implementation

Challenges from the Informal Economy

Implementing Zakat at scale presents genuine challenges that require honest acknowledgment from policymakers and implementers. The informal economy creates significant complications because lack of formal records complicates wealth assessment for many citizens operating outside official channels. Determining the actual assets of traders operating informally or small business owners without complete documentation and banking records remains difficult and may require community-based assessment mechanisms.

Religious and Administrative Applicability

Additionally, Zakat applies only to Muslims in Islamic jurisprudence, which means non-Muslim citizens would require separate taxation mechanisms, creating administrative complexity and potential equity concerns regarding different tax bases (Pakistan Today, 2025). This requires careful policy design to ensure fairness while respecting the religious foundation of the Zakat system.

Political Resistance from Elites

Wealthy stakeholders accustomed to current arrangements may resist reforms targeting accumulated assets, as such mechanisms would increase their fiscal obligations significantly. Establishing an independent Zakat authority requires political will, expertise, and significant investment in institutional capacity that may face resistance from entrenched interests and powerful elites who benefit from current arrangements. These obstacles are real and should not be minimized, yet they are not insurmountable when political leadership commits to reform.

Learning from Regional Models

Despite these challenges, countries such as Malaysia, Saudi Arabia, and Bahrain successfully operate parallel systems combining Zakat and state taxation, offering useful models and lessons for Pakistan to consider (Arif, 2023). Their experiences demonstrate that technical solutions exist and that public commitment to reform can overcome elite resistance through sustained political leadership. Pakistan can learn from their institutional designs and implementation strategies to customize an appropriate system.

➢ Conclusion

Pakistan's fiscal system has historically relied on a regressive, indirect, and insufficiently enforced tax regime, overburdening ordinary workers while leaving wealth accumulation largely unaccounted for and undertaxed. Zakat offers a culturally embedded, asset-based, and ethically motivated complement that could help redistribute wealth more fairly, support vulnerable populations effectively, and restore public trust in fiscal processes through transparent mechanisms rooted in religious tradition (ICTD & LUMS, 2024; Oxfam Report, 2025). By integrating Zakat thoughtfully with conventional tax reforms, Pakistan could foster a more equitable, transparent, and socially cohesive fiscal framework, where both religious obligation and economic responsibility reinforce fair wealth distribution and create a society where prosperity is more broadly shared among all citizens rather than concentrated among elites.

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