When Taxation Fails Justice: Institutional Zakat and the Future of Public Finance in Pakistan

By: Sania Abbas

Abstract

The Pakistani economy faces a host of issues, and some of these issues include inflation, rising levels of income inequality, continuously rising debt, and an uneven taxation system in which the middle class shoulders the load while the upper class receives a significant reprieve. The existing financial structure relies heavily on indirect taxes, which fuel inequality and poverty. This paper discusses an alternative zakat-based model of public finance, representing an obligation to redistribute wealth based on mutual trust. Far from a discretionary act of charity, Zakat is institutional and organized, a mechanism for the recycling of wealth, a means of assisting people experiencing poverty, and encouraging moral governance of the economy. This paper critically analyzes the present taxation system in Pakistan.The concept and history of Zakat have been discussed, and a state-level model for Zakat implementation was conceptualized. Moreover, it illustrates how an economy based on Zakat can lead to less dependence on exploitative taxation, enhance transparency, decrease poverty, and help regain confidence in the financial system. The current issue or problem under discussion provides a very practical and ethical approach for policymakers to react to the economic and societal circumstances in Pakistan.

Methodology statement

This study adopts a qualitative, conceptual policy-analysis approach grounded in Islamic political economy and public finance.

Introduction: Pakistan Stands at an Economic Crossroads

Pakistan stands at that critical stage in the development process of its economy. Inflation, income inequality, increasing national debt, and an unworkable tax system have all brought an uneasiness to the state of affairs that erodes public confidence in the state's ability to deliver economic justice.

Nonetheless, despite various attempts at fiscal reforms, the country relies mainly on the imposition of hidden taxes, sales tax, and excise duty, which tend to have a larger toll on the lower and middle classes of citizens and facilitate, rather than prevent, the concentration of income within the highest classes of citizens, with the very tools and mechanisms of funding public welfare themselves constituting a source of public economic stress.

The issues facing the public finance regime in Pakistan are not only technical; more importantly, these are morally and politically embedded. That is, the tendency towards regressive taxation, accompanied by constant foreign borrowing, has placed the economy in a cycle of thrift, inflation, and dependence. The type of policy advice issued by global financial bodies focuses on short-term fiscal extraction without giving any attention to distributive justice, therefore leaving little room for indigenous fiscal architecture that fits into the socio-religious context.

On the contrary, Islamic economic principles are another paradigm, based on equality, social solidarity, and human dignity. A compulsory system of redistribution, or Zakat, lies at the heart of such a paradigm-not part of charity, but an institution of public finance. Historically, Zakat stood at the center of governance as a method whereby Islamic states could look after welfare and social security for people without recourse to exploitative forms of taxation. The article thus contends that Pakistan continues to depend on an inequitable tax regime. Yet this is neither possible nor desirable in the Pakistani context. Instead, by conceptualizing a new framework for public expenditure grounded in Zakat, Pakistan can aim to ensure a balance between economic accountability and social justice in its financial model.

The Political Economy of Taxation in Pakistan

Pakistan's taxation system is characterized by a complex interplay between politics and economics, making it challenging to find appropriate solutions to its structural problems. Pakistan's tax-to-GDP ratio is just 11-12 percent, which is alarmingly low compared to other countries.

Reliance on Indirect Taxes

The government secures a good proportion of its revenues from indirect taxes, which, although easy to administer, are by their nature regressive. Such taxes take up a much larger share of low-income people's income than of the rich's, thereby increasing inequality and social discontent. Instead of equity, the current system is structurally shifting the fiscal burden onto those least able to bear it.

Elite Capture and Tax Evasion

Elite capture is one of the defining features of Pakistan's fiscal structure. The exemptions, preferential treatment and non-enforcement generally occur for the rich, the largest companies, and those with the best connections. As a consequence, fewer than one percent of the population makes any contribution to the income tax base. In turn, there is little public compliance and little public trust in the state.

Dependence on External Borrowing

The fiscal policy of Pakistan is restricted by reliance on external borrowing, particularly from institutions such as the International Monetary Fund-Conditional debt arrangements often emphasize indirect taxation and cuts in expenditures to a large extent and thus leave the government with limited ability for progressive and socially responsible fiscal reforms. The ultimate burden of adjustment would therefore fall on the average citizen, and underfunding hurts social welfare.

Institutional Weakness and Social Consequences

This has been further undermined by weak administrative capacity, high levels of corruption, and a lack of transparency in revenue allocation. In short, low revenues coupled with lack of state capacity create a self-reinforcing process that promotes the growth of the unorganized sector as well as tax evasion. Other social consequences that have occurred include political instability, reduced social mobility as well as increasing poverty.

Exploitative Taxation and Social Injustice

The impacts of a regressive tax system on social justice are far-reaching. Indirect taxes on necessities like food, electricity, and fuel have a greater impact on low-income groups. People earning less than $5 per day spend a large part of their earnings on necessities, leaving them with little to save or invest.

This really locks in poverty for future generations, making it hard for people to move up in the world. According to the Pakistan Institute of Development Economics, over 40% of the population lives below the poverty line, mainly due to inflation and taxes.\
There are indications that wealthy and large companies often use deferment agreements, exemptions or loopholes to reduce their tax liability. The rich are shirking financial responsibilities while ordinary citizens are burdened with mobility; The disparity in treatment between the wealthy and the general public reduces citizens' trust in government and increases civil tension.

The effects of indirect taxation and the need to repay debt strain the population's resources, leading to high expenditures on health and education. This leads to livelihood stigma in human development, exacerbating poverty. Informal discontent manifests in popular bases such as tax avoidance and the growth of the informal sector, as well as in periodic popular movements that have called for a more moral and just financial system.

Zakat as a Foundation of Islamic Public Finance

Qur'anic Foundations

Zakat is imposed in the Quran as a means of purifying wealth and ensuring the welfare of society. Sura at-Tawbah, 9:60, states who will benefit from it, hence establishing its purpose as a redistributive tool. Poverty reduction, redistribution of wealth and social cohesion are all the main intentions of Zakat. No other tax in the world combines moral responsibility with fiscal responsibility; Therefore, people voluntarily observe Zakat on the basis of moral belief.

Historical Practice

During the Rashidun Caliphate Zakat was not only a form of charity but also one of the bases of the state structure, through which public works projects, welfare programs and the management of public services were funded. The more clear and accessible systems were in place to collect and distribute Zakat, the less corruption was reduced and the need for further taxation was reduced. The historical perspective shows that Zakat operates beyond mere voluntary donations; It acts as an active fiscal instrument.

Zakat and Conventional Taxation

Table 1: Comparative Features of Zakat and Conventional Taxation

Feature	Zakat	Conventional Taxation
Source of Authority	**Religious and ethical obligation**	**Legal and statutory authority**
Primary Objective	**Social justice and redistribution**	**Revenue generation**
Beneficiaries	**Poor and vulnerable groups**	**State expenditure priorities**
Compliance	**Ethically motivated**	**Legally enforced**

Economic Impact	**Circulation of wealth**	**Often regressive in practice**

A Zakat-Based Public Finance Model for Pakistan

The public finance model based on Zakat in Pakistan should be based on four principles: equity, transparency, efficiency and ethical compliance. The collection of Zakat can be centralized through a digital system administered by federal and provincial governments, which will ensure proper evaluation, minimal leakage, and transparency to the public.

It should be able to distribute funds to measures of welfare in targeted programs, such as income support, education, healthcare, and micro-enterprise development, across all regions in an equitable manner. In exchange for income tax payments, zakat payments can be partially repaid to facilitate the progressive elimination of indirect taxes on basic commodities. This would reduce the strain on low-income families over time and would not cause fiscal instability.

Policy Implications for the Pakistani State

Short-term measures taken towards increasing transparency and efficiency include investment in digital infrastructure and reform of existing zakat institutions. The main objective of the medium-term reform is to reduce regressive taxes and bring zakat into line with other elements of the tax system. In the long term, policies such as establishing an autonomous national zakat authority and integrating zakat into national development planning should reduce dependence on foreign borrowing and increase local revenues.

Such reforms can strengthen the state’s legitimacy and social cohesion, and, beyond their economic advantages, lead to political stability by preventing the causes of inequality and widespread dissatisfaction.

Conclusion

The problems of the Pakistani economy are indicative of more serious structural and ethical failures in the Pakistani state’s financial system. High dependency on regressive taxation, privilege of the elite, and foreign debt have aggravated poverty, institutional distrust, and social injustice. As this article shows, a zakat-based system of public finance is a viable, ethical, and locally applicable alternative.

Zakat is not only a charitable duty; it is a systematic function of distributing money and social security of wealth. With proper management and consideration in fiscal policy, Zakat can, over time, substitute for exploitative levies, build trust among the population, and promote support for sustainable development. With economic governance alongside moral responsibility, Pakistan will be able to make a just, dignified, and inclusive economic future the core of economic prosperity, forming the basis for a fairer and stronger financial economy.

Final policy takeaway

For Pakistan, the gradual institutional integration of Zakat into public finance represents not only an economic reform, but a moral and political commitment to justice, dignity, and sustainable development.

Policy Recommendations

1. Establish an international Zakat authority to coordinate and monitor Zakat activities.
2. Create public awareness programs highlighting the economic and social importance of Zakat.
3. Develop efficient collection and distribution mechanisms to ensure transparency and impact.

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