Ending Exploitative Taxation.

(A Zakat-Based System for Justice, Economic Growth, and Welfare for All)

INTRODUCTION — The Core Problem

Pakistan gives more zakat than most countries in the world, yet its poor remain trapped in the same cycle of poverty. According to SBP EasyData, Pakistan’s formal zakat system collects only PKR 12.24 billion, while Pakistanis actually give around PKR 619 billion annually. Over 98% of zakat bypasses the state and goes informally. Meanwhile, the current taxation system is exploitative. It disproportionately burdens low-income families, who pay taxes on basic goods, services, and even their salaries, while wealthier individuals often avoid their fair share. As a result, there is little national welfare impact, and economic inequality persists. This highlights the urgent need for a structured, transparent zakat system that can reduce exploitative taxation and promote justice, economic growth, and welfare for all.

But how can a structured, transparent zakat system replace or reduce exploitative taxes while promoting justice, growth, and welfare? This question forms the basis of the analysis that follows.

Why Does The Current System Fail?

Even though zakat has a **huge** potential to help the poor, support those in need, and **boost** economic growth, the way Pakistan currently collects and distributes it is highly disorganized and ineffective. The system suffers from fragmentation, inefficiency, and a lack of transparency, which stops it from having any significant positive effect on the economy or society.

But banks deduct zakat only from savings accounts, not from total wealth. For example, a low-income father saving for his daughter’s marriage may have already fulfilled his zakat obligations by giving to a mosque or welfare organization, yet his zakat is still automatically deducted on the 1st of Ramadan unless he submits an exemption form or withdraws the money beforehand. This system does not take into account his other financial responsibilities, creating confusion and extra effort for those already struggling. At the same time, he continues to pay regular taxes on income or profits, such as from a mudaraba account, adding a further financial burden. For instance, a saver with PKR 48,330 in their account might earn a monthly mudaraba profit of PKR 127.22 (≈0.26% of the balance), but the government may deduct PKR 50.89 as withholding tax (≈40% of the profit), leaving a net gain of only PKR 76.33, or 0.16% of the account balance. For low-income families, this shows how even small savings are heavily burdened by taxation.

Low-income households also pay indirect taxes on basic goods and services, which can amount to 20–25% of their income. For a family of six to seven members dependent on a single breadwinner, this is a significant burden. Combined with automatic zakat deductions and taxes on small savings profits, the financial strain becomes overwhelming. Meanwhile, wealthier individuals, whose wealth may be spread across multiple assets, often avoid equivalent obligations. This imbalance highlights one of the key structural flaws in Pakistan's current system, showing how the poor carry a disproportionate share of the fiscal burden while the benefits of zakat remain largely untapped.

These structural and operational issues mean that, instead of functioning as a strategic tool for economic justice, zakat largely operates as charity. It fails to reduce poverty systematically, improve welfare, or relieve exploitative taxation. The result is that billions in charitable contributions leave little lasting impact, low-income families remain trapped in financial strain, and public trust in both the zakat and taxation systems continues to erode.

These challenges make it clear why Pakistan can learn from countries like Malaysia and Indonesia, where centralized and digital zakat systems have increased transparency, accountability, and the social and economic impact of collected funds.

Zakat as an Economic Institution (Islamic Perspective)

In Islam, zakat is **farz**. It is not an optional act of kindness or a personal choice. The Qur'an repeatedly mentions zakat alongside salah, showing its central importance in the Islamic system. Allah commands, *"Establish prayer and give zakat"* (Qur'an 2:43). This command appears again and again in the Qur'an, making it clear that zakat is one of the core pillars of Islam. Its position next to prayer shows that zakat is not only a spiritual duty but also a foundation of social and economic life.

This does not mean zakat is only a form of personal worship. Islam does not separate faith from daily life. Belief, morality, and economic behavior are deeply connected. Zakat is part of a broader system that governs how wealth should be earned, held, and shared. Through zakat, Islam directly links religious obedience with social responsibility.

Islam teaches that all wealth ultimately belongs to Allah. Human beings are not absolute owners but trustees. Managing wealth responsibly is therefore a form of obedience to God. Zakat reflects this idea by reminding believers that their wealth is not meant only for personal comfort. It carries the rights of others within it.

Zakat also purifies both wealth and the heart. By giving a fixed portion to those in need, a believer frees themselves from greed, selfishness, and excessive attachment to money. Wealth in Islam is not morally neutral. It must serve a purpose beyond individual benefit. Social responsibility is built directly into the concept of ownership.

In this way, Islam connects money with morality. Every financial action like earning, saving, spending, or giving is part of a person's accountability before Allah. Ignoring zakat is therefore not just an economic failure but a spiritual one as well. Zakat was designed to shape a just economic order, not to function as casual charity, and understanding this distinction is essential to restoring its true role in society.

It is important to clearly distinguish between **zakat** and **sadaqah**, as the two are often confused today. This confusion has weakened the role zakat was meant to play. Sadaqah is voluntary charity, given by choice and motivated by personal goodwill. Zakat, on the other hand, is mandatory and governed by clear rules. Its rates, eligibility threshold (nisab), and eligible recipients are specified in Islamic law. The Qur'an clearly defines these recipients in Surah At-Tawbah: *"Zakat is only for the poor, the needy, those employed to collect it, those whose hearts are to be reconciled, for freeing slaves, for those in debt, for the cause of Allah, and for the traveler"* (Qur'an 9:60). This shows that zakat was designed as a structured system of wealth redistribution, not as informal charity dependent on personal emotions.

It was collected and distributed through organized public systems. The goal was clear: to reduce poverty and make sure people could meet their basic needs with dignity. Zakat was meant to protect the weak, not just offer occasional help. This shows that Islam did not design zakat to exist alongside systems that heavily burden the poor. Instead, zakat was meant to shift responsibility toward those with surplus wealth. When zakat is reduced to scattered charity and kept separate from economic policy, its real purpose is lost, and the poor continue to suffer under unfair taxation.

How a Structured Zakat System Could Replace Exploitative Taxation

A well-organized and transparent zakat system has the potential to ease the financial burden on low-income families while ensuring wealth is redistributed effectively. By channeling zakat directly into social welfare programs, the government could reduce, or even eliminate regressive taxes on essential goods and services. For instance, if formal zakat collection reached just 25% of the actual contributions currently given informally (roughly PKR 154.75 billion), these funds could cover critical needs for millions of low-income households, reducing their dependence on harmful indirect taxes.

Digital platforms and centralized tracking would ensure accountability, making it easier to monitor contributions and disbursements in real time. This would prevent duplication and unnecessary deductions, so that low-income savers are not taxed repeatedly on small profits or savings. High-income individuals could also be encouraged to contribute voluntarily, knowing that funds are transparently allocated. Lessons from Malaysia and Indonesia show that such systems not only increase compliance but also maximize social and economic impact.

Concrete Implementation Steps / Policy Recommendations

Implementing a structured zakat system in Pakistan requires a combination of technology, governance, and public awareness. First, a centralized database should be established to record zakat contributors and recipients. This ensures that funds are tracked efficiently, avoids duplication, and provides transparency, making it easier to audit collections and disbursements. Banks and financial institutions can integrate automated systems that deduct zakat from eligible accounts monthly or quarterly, based on predefined thresholds such as the nisab. This approach reduces missed contributions and ensures that everyone fulfills their obligations fairly.

Next, digital disbursement channels should be created to ensure that collected funds reach the intended recipients directly. Approved welfare programs could include food assistance, education support, healthcare, housing, and skill-development initiatives. By using technology, the government can minimize leakages, improve accountability, and allow donors to see where their contributions are going.

Challenges will arise, including resistance from banks, financial institutions, and individuals, gaps in technology access, and limited public awareness. These challenges can be addressed with education campaigns, mobile-based platforms for contributions, partnerships with NGOs for outreach in rural areas, and media campaigns to build trust. Clear guidelines and legal frameworks would also be necessary to ensure compliance and prevent mismanagement.

Quantitative Impact / Case Studies

The potential impact of a structured zakat system is enormous. Currently, informal zakat in Pakistan totals roughly PKR 619 billion annually, while only PKR 12.24 billion is collected formally. If Pakistan could formalize even 50% of informal contributions, around PKR 309.5 billion could be collected and allocated systematically. This amount could support millions of low-income households, providing basic necessities and reducing reliance on indirect taxes that disproportionately affect the poor.

To give concrete numbers, consider a household with five to six members that spends PKR 20,000 per month on essentials. Even partial support through structured zakat could cover 50-70% of their basic consumption needs. If replicated across millions of households, this intervention could lift a substantial portion of the population above the poverty line.

Comparative case studies reinforce this potential:

- **Malaysia:** The Lembaga Zakat Selangor collects over RM1.2 billion annually. Funds are distributed to cover basic needs, health care, education, and small business loans. This approach has not only reduced poverty but has also encouraged voluntary contributions due to increased transparency.

- **Indonesia:** The national zakat board centralizes collection and disbursement, effectively providing direct welfare to a large population. This has improved social cohesion, reduced poverty, and increased compliance with zakat obligations.

Broader Economic Benefits

A structured zakat system would create multiple economic benefits beyond poverty alleviation. First, stimulating consumption and demand is critical. Low-income households receiving zakat funds will spend them immediately on essential goods and services, boosting local businesses and stimulating economic activity.

Second, decreasing dependence on debt is a major advantage. Currently, many families borrow money to meet basic needs due to low savings and high indirect taxes. With systematic zakat distribution, these families would rely less on loans, reducing household debt and financial stress.

Third, such a system promotes social cohesion and trust. Transparent collection and distribution show that wealth is being shared fairly and responsibly, increasing confidence in institutions and reducing resentment toward wealthier individuals.

Finally, encouraging surplus wealth to flow to those in need can strengthen the overall economy. When low-income households have their basic needs met, they can participate more actively in education, skill development, and small-scale entrepreneurship, creating long-term economic growth.

Islamic and Social Justification

A structured zakat system aligns directly with Islamic principles of justice, fairness, and reducing hardship. Zakat is not intended as an optional charity, it is a religious obligation and a fiscal tool. The Qur'an emphasizes wealth redistribution as a duty, stating in Surah At-Tawbah (9:60) the specific recipients for zakat. By implementing a central system, Pakistan can ensure that surplus wealth is used for public welfare rather than informal charity.

Islam teaches that financial responsibility falls on surplus wealth, not on daily necessities. Currently, regressive taxes on basic goods and small savings violate this principle. Restoring zakat as a formal economic institution corrects this imbalance, ensuring that the poor are not burdened while the wealthy contribute their fair share.

Socially, structured zakat reduces inequality, provides dignity to beneficiaries, and strengthens trust between citizens and institutions. It integrates moral and ethical responsibility with practical economic policy, creating a system that benefits society at large.

Conclusion / Call to Action

Ending exploitative taxation in Pakistan requires more than minor reforms. A structured zakat system could replace or significantly reduce regressive taxes, directly improving the lives of millions of low-income families. By formalizing collection, digitizing disbursement, and ensuring transparency, zakat can move from being a fragmented charitable practice to a central pillar of economic policy.

This is not just charity, it is a tool of justice, growth, and welfare. Pakistan has the financial resources within informal zakat contributions; what is needed is effective implementation, accountability, and public trust. By restoring zakat to its intended role, the country can create a sustainable, fair, and economically strong society where wealth serves both individual and social good.