

Document of
The World Bank

Report No: ICR00002147

IMPLEMENTATION COMPLETION AND RESULTS REPORT
(IBRD-72640 IDA-40070 TF-54392)

ON A

CREDIT

IN THE AMOUNT OF SDR 53.3 MILLION (US\$78.5 MILLION EQUIVALENT)

A LOAN IN THE AMOUNT OF US\$ 24.4 MILLION

AND A GRANT IN THE AMOUNT OF GBP 12.152 MILLION

TO THE

ISLAMIC REPUBLIC OF PAKISTAN

FOR A

TAX ADMINISTRATION REFORM PROJECT

June 25, 2012

Governance and Public Sector Management Unit
South Asia Region

CURRENCY EQUIVALENTS

Exchange Rate in original PAD
Currency Unit = Pakistani Rupee (PKR)
PKR 1.00 = US\$ 0.016
US\$ 1.00 = PKR 61.05

Exchange Rate Effective May 15, 2012
US\$ 1.00 = PKR 90.87

FISCAL YEAR
July 1 – June 30

ABBREVIATIONS AND ACRONYMS

ADR	Alternate Dispute Resolution
APL	Adaptable Program Loan
ATL	Active Taxpayers List
BS	Basic-pay Scale
CAS	Country Assistance Strategy
CBR	Central Board of Revenue
CCFR	Cabinet Committee for Finance and Revenue
CEG	Customs and Excises Tax Group
CPS	Country Partnership Strategy
DCA	Development Credit Agreement
DFID	Department for International Development (UK)
DLI	Disbursement Linked Indicator
DPL	Development Policy Loan
EAP	East Asia and Pacific Region
ECA	Europe and Central Asia Region
EMP	Environmental Management Plan
ERR	Economic Rate of Return
ERS	Expeditious Refund System
FATE	Facilitation and Taxpayer Education
FBR	Federal Board of Revenue
FM	Financial Management
FMR	Financial Monitoring Report
FRR	Financial Rate of Return
GDP	Gross Domestic Product
GoP	Government of Pakistan
GST	General Sales Tax
HQs	Headquarters (FBR)
HRIS	Human Resource Information System
HRM	Human Resources Management
IBRD	International Bank for Reconstruction and Development
ICB	International Competitive Bidding
ICR	Implementation Completion and Results Report
ICT	Information Communication Technology
IDA	International Development Association
IMF	International Monetary Fund
IMS	Information Management Systems
IRS	Inland Revenue Service
ISR	Implementation Status and Results Report

IT	Information Technology
ITG	Income Tax Group
ITMS	Integrated Tax Management System
KPI	Key Performance Indicator
LAC	Latin America and Caribbean Region
LTU	Large Taxpayer Unit
MoF	Ministry of Finance
MCC	Model Customs Collectorate
MDGs	Millennium Development Goals
M&E	Monitoring and Evaluation
MTR	Mid-term Review
MTU	Medium Taxpayer Unit
OECD	Organization for Economic Cooperation and Development
PAD	Project Appraisal Document
PCR	Project Completion Report
PDO	Project Development Objective
PEA	Political Economy Analysis
PIFRA	Project to Improve Financial Reporting and Auditing
PIP	Project Implementation Plan
PKR	Pakistani Rupee
PMU	Project Management Unit
PPF	Project Preparation Facility
PRAL	Pakistan Revenue Automation Ltd
PRSC	Poverty Reduction Structural Credit
PRSP	Poverty Reduction Strategy Paper
PSDP	Public Sector Development Program
QCBS	Quality and Cost Based Selection
RFP	Request for Proposal
RGST	Reformed General Sales Tax
RMU	Risk Management Unit
Rs	Rupees
RTO	Regional Taxpayer Office
SAC	Structural Adjustment Credit
SBD	Standard Bidding Document
SDR	Special Drawing Right
SOE	Statement of Expenditures
SOP	Standard Operating Procedures
SP&S	Strategic Planning and Statistics Wing (FBR)
STARR	Sales Tax Automated Refunds Repository System
TA	Technical Assistance
TAMS	Taxpayers Audit Management System
TARP	Tax Administration Reform Project
TFC	Taxpayer Facilitation Center
TTL	Task Team Leader
UNDB	United Nations Development Business
VAT	Value Added Tax

Vice President:	Isabel M. Guerrero
Country Director:	Rachid Benmessaoud
Sector Manager:	Tony Verheijen
Project Team Leader:	Daniel Alvarez-Estrada
ICR Team Co-leaders:	M. Taqi Sharif and William V. Mayville

COUNTRY
Islamic Republic of Pakistan

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A. Basic Information			
Country:	Pakistan	Project Name:	Pakistan Tax Administration Reforms Project
Project ID:	P077306	L/C/TF Number(s):	IBRD-72640,IDA-40070,TF-54392
ICR Date:	06/26/2012	ICR Type:	Core ICR
Lending Instrument:	SIL	Borrower:	GOVERNMENT OF PAKISTAN
Original Total Commitment:	USD 102.90M	Disbursed Amount:	USD 48.41M
Revised Amount:	USD 46.70M		
Environmental Category: B			
Implementing Agencies: Federal Board of Revenue			
Cofinanciers and Other External Partners: Department for International Development (DFID)			

B. Key Dates				
Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	07/29/2003	Effectiveness:	04/07/2005	04/07/2005
Appraisal:	05/19/2004	Restructuring(s):		09/01/2010 12/15/2011
Approval:	12/07/2004	Mid-term Review:	09/15/2007	08/15/2007
		Closing:	12/31/2009	12/31/2011

C. Ratings Summary	
C.1 Performance Rating by ICR	
Outcomes:	Moderately Unsatisfactory
Risk to Development Outcome:	High
Bank Performance:	Moderately Unsatisfactory
Borrower Performance:	Unsatisfactory

C.2 Detailed Ratings of Bank and Borrower Performance (by ICR)			
Bank	Ratings	Borrower	Ratings
Quality at Entry:	Unsatisfactory	Government:	Unsatisfactory
Quality of Supervision:	Moderately Satisfactory	Implementing Agency/Agencies:	Moderately Unsatisfactory
Overall Bank	Moderately	Overall Borrower	Unsatisfactory

Performance:	Unsatisfactory	Performance:	
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C.3 Quality at Entry and Implementation Performance Indicators			
Implementation Performance	Indicators	QAG Assessments (if any)	Rating
Potential Problem Project at any time (Yes/No):	Yes	Quality at Entry (QEA):	Satisfactory
Problem Project at any time (Yes/No):	Yes	Quality of Supervision (QSA):	Moderately Satisfactory
DO rating before Closing/Inactive status:	Moderately Unsatisfactory		

D. Sector and Theme Codes		
	Original	Actual
Sector Code (as % of total Bank financing)		
Central government administration	95	100
Sub-national government administration	5	
Theme Code (as % of total Bank financing)		
Administrative and civil service reform	20	30
Tax policy and administration	40	60
Trade facilitation and market access	40	10

E. Bank Staff		
Positions	At ICR	At Approval
Vice President:	Isabel M. Guerrero	Praful C. Patel
Country Director:	Rachid Benmessaoud	John W. Wall
Sector Manager:	Antonius Verheijen	Simon C. Bell
Project Team Leader:	Daniel Alvarez Estrada	Mudassir Khan
ICR Team Leader:	Mohammed Taqi Sharif	
ICR Primary Author:	Daniel Alvarez Estrada	
	Mohammed Taqi Sharif	
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F. Results Framework Analysis

Project Development Objectives (from Project Appraisal Document)

According to the DCA, the PDOs of the project were to: (i) improve the effectiveness, responsiveness, efficiency, integrity and fairness of tax administration; (ii) promote compliance with tax laws and broaden the tax base; and (iii) promote trade facilitation.

Revised Project Development Objectives (as approved by original approving authority)

In August 19, 2010, the project was restructured and the PDOs were reformulated and streamlined. The PDO became: "To improve the effectiveness of Pakistan's revenue administration".

(a) PDO Indicator(s)

Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
Indicator 1 :	FBR gross and net revenue collection as a percentage of tax revenue targets (annual)			
Value quantitative or Qualitative)	Rs 517 bn (FY 2003/04)	Rs 875 bn (FY 2008/09)	Rs. 1,327.4 bn (FY 2009/10)	Rs. 1,558 bn.(FY 2010/11), against a (post-floods) target of Rs 1,604 bn.
Date achieved	06/30/2004	06/30/2009	06/30/2011	06/30/2011
Comments (incl. % achievement)	97.1% achievement			
Indicator 2 :	FBR total tax collection/GDP (annual): increase			
Value quantitative or Qualitative)	11.5%	12.2%	9.8%	8.6%
Date achieved	06/30/2004	06/30/2009	06/30/2011	06/30/2011
Comments (incl. % achievement)	GDP to Tax ratio at closing was 8.6%.			
Indicator 3 :	Survey based ratings for the FBR: improved perception by stakeholders;			
Value quantitative or Qualitative)	2007 survey results	N/A	N/A	2011 survey showed improvements in overall level of transparency and LTU operations, and deterioration in tax filing procedures and disposal of appeals.

Date achieved	12/31/2007	12/30/2011	12/31/2011	12/31/2011
Comments (incl. % achievement)	As shown above.			
Indicator 4 :	Stop-filers as percentage of registered active taxpayers			
Value quantitative or Qualitative)	Stop-filers (FY 2008/09) : Income tax 67%; and Sales tax 4%	N/A	N/A	Income tax: 28%, and Sales Tax 8% (FY 2010-11)
Date achieved	06/30/2009	12/31/2011	12/31/2011	06/30/2011
Comments (incl. % achievement)	Income tax: 28%, and Sales Tax 8%.			
Indicator 5 :	Additional tax paid after audit as percentage of total tax collection of domestic taxes: increase			
Value quantitative or Qualitative)	At restructuring (FY 2009/10) :Rs. 7,560m (0.56%);	N/A	Rs. 7,700m.	Rs 6,231m (0.39%)
Date achieved	06/30/2010	12/31/2011	06/30/2011	06/30/2011
Comments (incl. % achievement)	Revised target not achieved.			
Indicator 6 :	Modernized FBR organization structure			
Value quantitative or Qualitative)	Organization based on tax-type	Same as above.	Fully functional FBR organization by the end of the project.	Moderate to significant shortcomings in achieving full functional FBR organization.
Date achieved	12/31/2009	12/31/2009	12/31/2011	12/31/2011
Comments (incl. % achievement)	As above			

(b) Intermediate Outcome Indicator(s)

Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
Indicator 1 :	Administrative cost of collection as % of total revenues (annual)			
Value (quantitative or Qualitative)	At appraisal: 0.60 %	0.77%	Under 1%	0.87%
Date achieved	12/31/2004	12/31/2009	12/31/2011	12/31/2011
Comments (incl. % achievement)	Achieved.			
Indicator 2 :	No. of staff trained			

Value (quantitative or Qualitative)	Unkown	N/A	5,000 annual	2694
Date achieved	12/31/2004	12/31/2011	12/31/2011	12/31/2011
Comments (incl. % achievement)	Target not achieved.			
Indicator 3 :	Percent of tax returns filed electronically			
Value (quantitative or Qualitative)	N/A	N/A	36%	100% for sales tax and corporate income tax; 32% for the rest of taxpayers.
Date achieved	12/31/2011	12/31/2011	12/31/2011	12/31/2011
Comments (incl. % achievement)	Target generally achieved.			
Indicator 4 :	Number of registered taxpayers			
Value (quantitative or Qualitative)	At appraisal: 1.683 million	2.895 million	4.047 million	3.766 million
Date achieved	12/31/2004	12/31/2009	12/31/2011	12/31/2011
Comments (incl. % achievement)	Target not achieved.			

G. Ratings of Project Performance in ISRs

No.	Date ISR Archived	DO	IP	Actual Disbursements (USD millions)
1	06/03/2005	Satisfactory	Satisfactory	3.06
2	12/03/2005	Satisfactory	Satisfactory	6.81
3	05/18/2006	Satisfactory	Satisfactory	8.67
4	12/27/2006	Moderately Satisfactory	Moderately Unsatisfactory	10.99
5	06/15/2007	Moderately Satisfactory	Moderately Unsatisfactory	12.57
6	12/17/2007	Moderately Satisfactory	Moderately Unsatisfactory	15.62
7	06/25/2008	Moderately Satisfactory	Moderately Unsatisfactory	18.80
8	12/27/2008	Moderately Satisfactory	Moderately Unsatisfactory	22.22
9	06/29/2009	Moderately Satisfactory	Moderately Unsatisfactory	24.44
10	12/29/2009	Moderately Satisfactory	Moderately Satisfactory	25.62

11	10/10/2010	Moderately Satisfactory	Moderately Satisfactory	33.80
12	12/27/2011	Moderately Unsatisfactory	Moderately Satisfactory	44.49

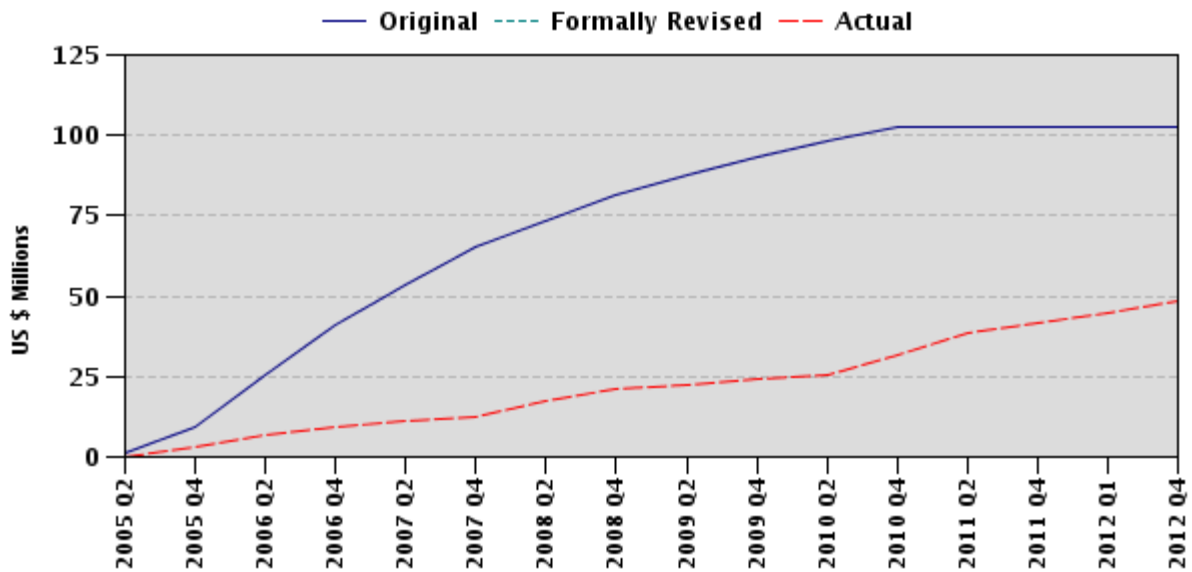
H. Restructuring (if any)

Restructuring Date(s)	Board Approved PDO Change	ISR Ratings at Restructuring		Amount Disbursed at Restructuring in USD millions	Reason for Restructuring & Key Changes Made
		DO	IP		
09/01/2010	Y	MS	MS	32.68	Sharpen PDO, realign activities, cancel loan amounts, reclassify environmental category, extend closing date
12/15/2011		MS	MS	44.49	Amend DCA

If PDO and/or Key Outcome Targets were formally revised (approved by the original approving body) enter ratings below:

	Outcome Ratings
Against Original PDO/Targets	Moderately Unsatisfactory
Against Formally Revised PDO/Targets	Moderately Unsatisfactory
Overall (weighted) rating	Moderately Unsatisfactory

I. Disbursement Profile



1. Project Context, Development Objectives and Design

1.1 Context at Appraisal

1. Country and sector background: Since the early 1990s, successive governments have tried to reform Pakistan's tax system. Despite these attempts, the tax/GDP ratio has remained low (10 to 13 per cent)¹. This relatively low ratio in Pakistan is primarily due to inherent weaknesses in the tax system including: (i) inefficient tax administration (poor management, weak human resources, lack of adequate supporting systems, excessive scope for discretion and rent seeking behavior); (ii) a narrow tax base (of 39.4 million employed persons, only 3.9 percent pay tax); (iii) skewed tax structure (68% of tax revenue is from indirect taxes); (iv) a complex and non-transparent tax system; and, (v) corruption and tax evasion (low compensation of tax officials, informal structure of the economy).

2. Government Strategy: Recognizing the critical need to increase tax revenue as paramount for fiscal stability, the Government of Pakistan (GoP) adopted a two-pronged strategy: *tax policy change*, to make the tax system more responsive to growth and easier to administer; and, *tax administration improvements* to enhance collection efficiency. Based on the recommendations of a Task Force², supported by the Bank, the Federal Board of Revenue (FBR)³ developed a broad strategy for reforms focusing on: (i) restructuring of FBR along functional lines and integration of income, sales and excise taxes; (ii) reengineering and automating business processes and workflows; (iii) establishing databases for reporting and audit purposes; (iv) introducing a self assessment system for filing tax returns; (v) improving services for taxpayers; and, (vi) strengthening the human resource base. GoP also intended to improve its fiscal position by enhancing the tax/GDP ratio from its stagnant level. Further, GoP made several tax policy reforms, which included change in the organizational structure of FBR, abolition of wealth tax, introduction of two-tier Agriculture Income Tax in all provinces, reduction in multiplicity of taxes at both federal and provincial levels, broadening the base of General Sales Tax (GST), lowering of income tax rate, and gradual withdrawal of Central Excise Duties.

3. Rationale for Bank assistance: Against this backdrop, and following a number of earlier interventions⁴, the Bank provided a Project Preparation Facility (PPF) of US\$2.9 million in 2002 to support implementation of GoP's tax reform initiatives and to prepare a comprehensive

¹ The band of 10% -13% for Pakistan covers the period 1993-2003. As per OECD, the tax/GDP ratio ranges between 30 to 50 per cent for developed countries, with an average of 38%, while for developing countries it is about 18% (PAD, page 5). However, an upward adjustment by GoP authorities to the GDP series data starting in 2000/01 affects tax/GDP data comparisons included in the PAD for the periods before 2000/01 and after 2010/11. As a result of the recalculation of the GDP series, the tax/GDP was adjusted downwards by about 3% of GDP in the year 2000/01.

² Task Force report dated May 2001, which was approved by the President in November 2001.

³ Until July 2007, the revenue agency was called the Central Board of Revenue (CBR). It then became the Federal Board of Revenue (FBR), which designation will be used throughout the ICR.

⁴ These included lending (Institutional Development Fund Grant –IDF 2000; Second Structural Adjustment Credit – SAC 2, 2002; and the Poverty Reduction Structural Credit –PRSC I, 2004) and non-lending (Joint Bank/IMF technical report on Tax Administrations Reforms, 2001; Joint Bank/IMF recommendations on revenue administration reforms, 2003).

strategy with implementation timelines and costs for the medium/long term reform program⁵. The PPF was intended to support the testing of pilot schemes including, *inter alia*, the setting up of Large Taxpayer Unit (LTU), Medium Taxpayer Unit (MTU), sales tax refund program, and human resource information management system. In 2004, the Bank assisted FBR in the preparation of the Tax Administration Reform Project (TARP) to achieve significant progress in the GoP's reform program,⁶ on a phased basis. TARP was prepared to: (i) restructure FBR along functional lines and have an integrated tax administration over the long term; (ii) strengthen FBR through organizational and management reforms, and provide it with necessary autonomy; (iii) improve the level of existing human resource capacity through streamlined training; (iv) re-engineer its operational processes and systems, and introduce modern and automated risk based tax systems that would reduce contact between taxpayers and tax officials, foster voluntary compliance, and strengthen the institutional framework for tax enforcement; and, (v) improve FBR's physical infrastructure.

1.2 Original Project Development Objectives (PDOs) and Key Indicators (as approved)

4. The **PDOs**⁷ of the project were to: (i) improve the effectiveness, responsiveness, efficiency, integrity and fairness of tax administration; (ii) promote compliance with tax laws and broaden the tax base; and (iii) promote trade facilitation.

5. **Key Performance Indicators (KPIs):** These were:

- *Macro indicators:* (a) total tax revenues collected by tax/GDP ratio; (b) tax revenues collected by sector/GDP; and, (c) average time taken by new businesses to register with tax authorities.
- *Organizational efficiency and effectiveness:* amount of taxes collected/number of tax administration staff.
- *Compliance management:* (a) number of registered active taxpayers; (b) tax revenues paid on time/total revenues assessed; (c) ratio of additional taxes collected after tax audit/number of tax audits conducted; and, (d) stakeholder opinion on quality of services provided (collected through a structured survey conducted by an independent firm and through report cards introduced).
- *Trade facilitation:* (a) reduction of the average customs clearance time to less than one day by the end of 2006, and (b) to under four hours by the end of the project at designated sites.

⁵ This PPF followed a series of PRSCs / DPLs that were also aimed at tax reform.

⁶ The reform program was further supported by: (i) *Technical Assistance* which included support to FBR and MoF on GST policy reform and support to TARP implementation starting in 2008; (ii) *Analytical Work*, for a comprehensive study on Pakistan's tax system, launched in January 2007 and concluded in July 2009; and, (iii) subsequent development policy credits supporting key policy and administrative reforms until 2010.

⁷ According to Project's Development Credit Agreement (DCA), dated March 9, 2005.

- *Integrity and fairness:* (a) public perception of revenue administration integrity as measured by periodic surveys; (b) staff perception of integrity as measured by periodic surveys; and, (c) average number of days to complete administrative appeals process.

1.3 Revised PDO and Key Indicators, and reasons/justification

6. In August 2010, the project was restructured⁸ and the PDOs were reformulated and streamlined. The PDO became: To improve the effectiveness of Pakistan’s revenue administration. The reformulated outcome indicators were:

- FBR gross and net revenue collection as a percentage of tax revenue target (total for each tax) (monthly, quarterly, annual): increase;
- FBR total tax collection/GDP (annual): increase;
- Survey based ratings for the FBR: improved perception by stakeholders;
- Stop-filers as percentage of registered active taxpayers (total, type of tax, and taxpayer size): decreased percentage;
- Additional tax paid after audit as percentage of total collection of domestic taxes: increase; and
- Modernized FBR organization structure fully functional.

7. The 2010 project restructuring was intended to: (i) respond to GoP’s renewed commitment to key revenue administration and policy reforms and more effective project implementation in the wake of Pakistan’s macroeconomics challenges⁹; and (ii) produce a more focused project, with a clearer, results-oriented development objective and relevant results indicators in line with FBR’s adopted 2008 Action Plan, based on Bank recommendations. The indicators were similar to the original ones but consolidated to address outstanding organizational and implementation issues, including updated revenue targets, stakeholder perceptions (survey), and several efficiency and effectiveness measures.

1.4 Main Beneficiaries

8. The intended beneficiaries under the original and restructured project were: (i) taxpayers at the household and corporate levels in Pakistan, through simplified tax regulations and reporting requirements allowing, among other objectives, a smoother transition from the informal to formal economic sectors; and, (ii) FBR’s departments and collectorates¹⁰.

1.5 Original Components

9. The TARP comprised seven components: (i) Management and Institutional Development; (ii) Improving Revenue Operations; (iii) Strengthening Revenue Services; (iv) Creating a Tax Compliant Culture; (v) Adopting Responsive IT Systems; (vi) Infrastructure Up-gradation and Development; and, (vii) Project Management and Implementation.

⁸ The restructuring was approved by the Bank’s Executive Directors on September 1, 2010.

⁹ This relates to concerns about high current account deficit, the employment downturn, substantial external financing requirements and insufficient counterpart financing due to limited fiscal space.

¹⁰ The FBR Customs field offices are known as Collectorates.

1.6 Revised Components

10. After restructuring, the original components were reorganized into four components for simplification and more effective implementation and monitoring as follows: A. Enforcement (including audit); B. Organization and Management for increased efficiency; C. Information Technology; and D. Project Management and Implementation. (*Annex 2D shows the linkage between the original and the revised components, and Annex 2E shows the activities planned under various components*).

1.7 Other significant changes

11. The 2010 restructured TARP emphasized: (i) actions to strengthen enforcement and resume audits; (ii) changes in FBR's organization and management to increase efficiency (functional organization); (iii) responsive IT systems; and, (iv) project and program management activities. None of the changes altered the original economic, financial, technical, institutional or social aspects of the project as originally appraised. The financial management and disbursement arrangements remained the same.

12. Other significant changes included: (i) Realignment of project activities to conform to the FBR Action Plan (including internal adjustments in activities), with revised project costs and an updated Procurement Plan; (ii) Reduction of the overall IBRD loan amount to reflect changes in the FBR's IT and automation strategy (basically handled internally by FBR without loan resources), and reallocation of loan, credit and grant funds to finance the revised project activities and costs; (iii) Classification of the project as environmental category "B", to fully conform to OP/BP 4.01 (Environmental Assessment), and inclusion of measures to ensure safeguard compliance; (iv) 100 percent financing of eligible expenditures from IDA Credit and the DFID Grant¹¹; (v) a single disbursement category to simplify disbursements under previous expenditure categories within the overall amounts available under both the IDA Credit and the DFID Grant, to avoid further amendments in the legal agreement; and (vi) extension of the Closing Date of TARP to December 31, 2011.

2. Key Factors Affecting Implementation and Outcomes

2.1 Project Preparation, Design and Quality at Entry

13. **Lessons from earlier operations:** Lessons learned from Bank-supported tax administration reforms in LAC, EAP, ECA Regions, and previous efforts to improve tax administration in Pakistan were incorporated into the original project, including: high level political support and ownership of program; presence of "champions of change" within the tax department; special attention to taxpayer facilitation; reduction in the discretionary powers of tax officials; simplification of procedures for filing and processing of tax returns; and establishment of a consultative process.

¹¹ This was in recognition of the constraints posed by the prevailing fiscal challenges in Pakistan and the paucity of counterpart funds.

14. Project design: Original project design features that **positively impacted** project implementation and outcomes include: (i) adequate resource allocation for FBR's physical infrastructure upgrading and IT deployment required to support the implementation of the tax administration reform agenda, and (ii) significant emphasis on the development of taxpayer services for FBR to reduce taxpayer compliance costs, including the deployment of facilitation centers. On the other hand, project implementation and outcomes were **negatively impacted** by factors related to project design, including: (a) over-optimistic assumptions about the implementation of legislative changes required to reform tax legislation and implement a functionally integrated FBR¹², and (b) underestimation of internal resistance to FBR's integration initiatives by staff of the Customs and Excise Group (CEG) and the Income Tax Group (ITG).

15. Quality at entry: Initial project implementation was negatively affected by lack of preparedness on key strategic choices on information technology (IT) strategy, fiduciary arrangements, and inadequate Bank technical support:

- **Policy uncertainty on an IT modernization strategy.** The decision to outsource customs automation as a public-private partnership activity instead of the investment planned under the project, took some US\$28 million of intended disbursements out of the project. In addition, FBR management and its internal IT group could not agree on whether an off-the-shelf integrated solution vs. in-house development of an Integrated Tax Management System (ITMS) would be the right option. In general, prolonged disagreements in the development of IT software and infrastructure led to a delay of more than two years in implementing the procurement plan.¹³
- **Lack of policy dialogue on key policy and legislative reform measures needed to achieve project's development objectives.** Excessive focus on the minutiae of project implementation in the initial years resulted in the Bank's team inattention to the importance of having regular high-level policy dialogue with GoP/FBR and providing TA to FBR to support tax administration reform efforts.
- **Lack of Bank technical assistance to support initial stages of project implementation.** The depth and comprehensiveness of the proposed reform of tax and customs administration, combined with uneven technical and absorption capacity at FBR, required strong TA guidance at the outset to develop an action plan with breakdown of actions and tasks. The PPF inputs and pilot results were not followed, leading to disconnected inputs and products and little or no institutionalization of assistance rendered in many key functionalities.
- **Initial misclassification of project's environment category.** Despite a large civil works component aimed at the refurbishment of several existing FBR buildings and facilities¹⁴,

¹² For the integration of FBR into a full, function-based organization to be successful and sustainable, due diligence work was required at the outset to test the extent of reforms needed in key pieces of legislation and FBR's internal rulings, and its likelihood of success.

¹³ IT strategy at entry was not implemented as planned, which left an undisbursed balance of nearly \$51 million at the originally scheduled closing of the project (December 31, 2009). The procurement processes involved (single and two stage bidding) also proved to be a disruptive element at this stage.

¹⁴ According to the project's PAD, the infrastructure up-grading component was estimated at US\$24 million, which represented about 17 percent of total project cost.

and the construction of some new facilities, the project was classified as “C”, instead of “B”, leading to insufficient attention to full compliance with Bank OP/BP 4.01 on environmental assessment.

16. Identification of risk factors and mitigation measures: The project was implemented within a more volatile and risky environment than originally estimated, due to a combination of factors, such as: adverse economic circumstances, a challenging political environment with frequent changes of political authorities and FBR staff at the senior levels, turnover on Bank supervision teams, strong internal resistance to change, adverse country security issues, and unstable infrastructure needs, such as power supply.

17. Most risk factors were adequately identified in the original project design, except for the following:

- **Lack of implementation of critical tax policy reforms.** The achievement of development objectives targeted at the outset in terms of revenue mobilization¹⁵ required substantial and parallel efforts in both tax policy and tax administration. Mutually supportive reforms in both are not only a desirable strategy aligned with best practice in tax reforms worldwide, but in the particular case of Pakistan, represented a key element for success. Reform of FBR alone was insufficient to bring in expected collection targets operating within a narrow based, non-transparent, and complex tax legislation.¹⁶ In particular, the lack of approval of a broad-based VAT legislation, or reformed GST, proved a major constraint for the project to achieve PDOs.
- **Needed reforms on legal framework.** Structural changes to FBR, as originally envisioned in the PAD, entailed the need to anticipate legal constraints embedded in different pieces of legislation and ordinances with the potential to reduce the scope of project implementation in key areas. This was particularly critical for the integration of revenue administration structure to operate under functional lines, and for the harmonization of tax procedural rules required to administer different taxes under a common institutional platform.¹⁷ The legal constraints imposed in the Tax Acts limited FBR’s ability to reorganize and to take computerized actions or reallocate functions to different staff, as this could only be done through appropriate amendments in the legislation.
- **A highly volatile political and security environment.** The project was implemented within an unstable and contentious political period, characterized by significant public activism, changes in government, and increasing insecurity in the country. These unpredictable circumstances had severe consequences for project implementation,

¹⁵ Original project design estimated a buoyancy coefficient (ratio of percent change of tax revenue to GDP or other underlining tax base) of 1.2, signaling an increase of 0.20 percent of tax-GDP ratio for each one percent increase of GDP.

¹⁶ A complete description of the tax policy role on the reform of the tax system in Pakistan is described in “*Tax Policy Report, Tapping Tax Bases for Development*”, Report no. 50078-PK, World Bank, 2009.

¹⁷ For example, tax legislation in Pakistan empowers only specific FBR authorities (e.g. commissioners) to carry out key operational procedures (e.g. some refunds or enforcement actions), limiting the scope of the reform to reorganize and reallocate functions across the organization following cost-effective criteria.

including recruitment of international consultants and travel to Pakistan by Bank missions.

18. Among the identified risk factors with insufficient identification of mitigation measures, stiff resistance from vested interests against restructuring of FBR resulted in slow progress on the functional integration of income, sales, and excise taxes. Despite being recognized as a major risk factor at the outset, executive and staff resistance to restructuring proved to be a major disruptive element throughout implementation. A change management workshop promoted by FBR authorities during project preparation was foreseen as a mitigation measure at entry point, while similar events were advised in future stages of reform implementation¹⁸. However, the depth of the organizational reform embraced by the project, even if implemented gradually as advocated by the Bank, entailed a fundamental and complex change with highly unsettling potential consequences for an organization facing internal struggles to reform. The litigation and the Inspection Panel review, initiated by groups of FBR staff associations, have highlighted that additional mitigation measures should have been proposed at the outset to ensure a gradual but effective management of organizational change, while providing safeguards for an equitable and fair treatment of all staff along the reorganization process.

2.2 Implementation

19. Implementation was affected by the following factors:

Positive Factors in Project Implementation

- The Federal Board of Revenue Act, 2007 was approved by the Parliament, replacing the Central Board of Revenue with the new Federal Board of Revenue, in line with the tax administration reforms that had been agreed between GoP and the Bank, and set the stage for functional integration at FBR.
- The over four years' tenure of the first Chairman, FBR under TARP (March 12, 2004 to July 23, 2008) reflected GoP's strong commitment to tax administration reform and provided the continuity that had been envisaged at appraisal.
- Project restructuring, extension of the closing date, and the appointment of a committed PMU Chief/Project Director, helped the project to complete many critical activities related to physical and IT-related infrastructure.

Factors that Negatively Affected Project Implementation

- Overall lack of reform ownership by FBR rank and file officers, frequent changes of FBR leadership after 2008, and delays in formation of the PMU and readying procurement

¹⁸ Also, original project design embraced a "co-location" strategy towards FBR integration along functional lines from tax-by-type bases. According to this strategy, location of sales and income tax staff in the same physical space, without changing lines of authority, was expected to ease transition towards a new structure. Without additional measures to accelerate the restructuring process, the strategy increased entrenchment to maintain the traditional modus operandi across field formations.

packages before loan approval, undermined continuity of project management, weakened implementation monitoring, slowed procurement, and hindered financial management and disbursements.

- Inability of GoP to secure Parliamentary approval for the broad-based GST legislation - originally envisioned to be introduced by July 2010, but indefinitely postponed thereafter, limited the project's scope to achieve PDOs.
- Inspection Panel review, requested in January 2010 by officers of the Customs and Excise Association, slowed reform momentum, underlined divisions among staff from different service groups, delayed the restructuring process¹⁹, led to departures of key personnel from the PMU, and as a result further delayed processing of major IT procurement packages²⁰.
- Unfavorable economic circumstances on account of a deteriorating security situation, and the massive floods in 2010 and 2011, further eroded tax bases and compliance levels.
- Slow responsiveness of World Bank supervision teams before project restructuring to resolving implementation bottlenecks, and insufficient pro-activity to suggest timely corrective actions, which was partly affected by changes in TTLs.
- Weak monitoring and evaluation arrangements (see 2.3 below).

2.3 Monitoring and Evaluation (M&E) Design, Implementation and Utilization

20. FBR's PMU was initially responsible for establishing the M&E sub-component of TARP to monitor the original key performance indicators (KPIs). The project management team prepared a baseline scenario with qualitative and quantitative performance indicators. Following the approval of the project restructuring, TARP's performance was assessed against the revised KPIs. Especially since September 2008, FBR regularly provided data against the KPIs to Bank implementation review and TA missions.²¹ **However, FBR did not set up a specific M&E/Coordination unit with oversight at a Member level, to adequately monitor progress of, and follow up on, the reform action plan, detect deviations and propose short-term responsive actions.** This shortcoming had been consistently flagged in the Bank's supervision documents since 2009 as a major constraint to project implementation and follow up of actions agreed during supervision missions. The creation of an M&E/Coordination unit for TARP, with supervision at a Member level, remained an unfulfilled commitment by FBR management until the project's closing date.

¹⁹ Source: Restructuring Paper – August 19, 2010.

²⁰ The Bank initially agreed on only a 3-month extension (up to March 31, 2010). The PMU was unable to start major procurement processes in light of prevailing uncertainty.

²¹ Data on TARP performance was provided by various units of FBR to the Member for Strategic Planning and Statistics (SP&S), who was also the Project Director for TARP for most of 2009–2011. The office of Member, SP&S, served as the focal point for Bank supervision missions.

2.4 Safeguards and Fiduciary Compliance

21. Safeguards: At the restructuring, the project's environmental category was changed from "C" to "B" and OP/BP 4.01 (Environmental Assessment) was triggered owing to the construction of some housing facilities for FBR staff in different cities in Pakistan, financed by TARP²². GoP prepared an environmental management plan (EMP) with adequate institutional arrangements to address possible low-level, temporary environmental impacts. **The EMP compliance varied between different work sites, and is rated as moderately satisfactory.** One weak area was irregular preparation of the quarterly progress report - only three such reports for EMP compliance were prepared for six quarters. One of the construction sites had some moderate level of environmental sensitivity related to the need to avoid the cutting of several mature trees in a hilly terrain, which the project complied with.

22. Financial Management: The PMU was responsible for financial management (FM) aspects of TARP. The project had a disbursement flag (2008 and 2009) on account of long delays in implementation of large IT packages.²³ On account of delays in the hiring of FM specialists and the departure of the finance advisor from the PMU, the FM ratings in the ISRs were less than satisfactory until late 2009. During this period, the external auditors also highlighted a number of observations on poor FM practices. From 2010 onwards, a dedicated and strengthened team in the PMU was able to turn the performance around, address the pending audit queries, significantly increase the disbursement rate, and obtained a satisfactory FM rating from the Bank supervision mission in July 2011.

23. Procurement: The PMU handled the procurement function as well. As in the case of the FM function, procurement was slow in the early years on account of PMU's weak procurement capacity and protracted delays in the decisions on the procurement of major IT packages and finalization of bidding documents (see footnote 19). On account of relatively steady progress on contracts relating to the procurement of civil works and goods, the procurement rating in ISRs was maintained at satisfactory until December 2007, when it was changed to moderately unsatisfactory due to delays in procurement of IT packages. Again, because of new leadership at the PMU in early 2010 and intensive Bank supervision²⁴, a remarkable turn-around also took place in PMU's procurement-related performance. Between May 2010²⁵ and December 31, 2011, the PMU completed 8 ICBs, 13 NCBs, and 14 QCBS activities among a total of around 50 procurements for a total value of about US\$41.6 million.

²² For future operations, it is important that the safeguards rating should be based on project content.

²³ In 2007, FBR decided to proceed with a national customs computerized system through a public-private partnership and not utilize US\$28 million from TARP. Similarly, in February 2008, FBR decided to go for in-house development of ITMS through PRAL, using outside experts as needed, under the guidance of the international program manager. This was to be based on the Information Systems Plan, which was approved by FBR's Board and endorsed by the Bank.

²⁴ Starting from May 2010, the PMU developed an excellent working relationship with the Bank's core task team. The Bank's procurement specialist, responsible for TARP, was also moved from New Delhi to Islamabad. These developments had a very positive impact on project implementation in terms of matters relating to TARP's procurements, FM, disbursements, and safeguards.

²⁵ Date of TARP's restructuring mission.

2.5 Post-completion Operation/Next Phase

24. A DLI-based “Revenue Mobilization Project”²⁶ has been proposed by GoP as a follow-up operation to the TARP and is under preparation with a PPF advance (P128182). The objective is to consolidate the tax administration reform initiated under the TARP using a performance-based results framework. Activities are aimed at improving FBR's effectiveness, accountability, and transparency of tax administration through a results-based approach. The components/activities of the PPF will include (i) improving revenue forecasting; (ii) consolidating FBR tax administration functions (including HR, training, and strategic planning) supporting results-based management; (iii) enhancing the accountability of tax administration (M&E systems); and (iv) strengthening FBR automation to achieve a modern, performance-based (M&E oriented) tax administration. Lessons learned from the TARP will be incorporated into the new DLI project. In view of the fact that responsibility for administration of sales tax on services has been devolved to the provincial governments, the Sindh and Punjab Provinces have approached the Bank for technical assistance to set up provincial revenue authorities and support other capacity building measures for provincial tax administration.

3. Assessment of Outcomes

3.1 Relevance of Objectives, Design and Implementation

25. **Low revenue mobilization stands out as one of the long and most pressing development challenges in Pakistan**²⁷. This is the result of a combination of factors, such as inefficient tax administration, narrow and skewed tax structure, complex and obsolete legislation, non-transparent tax system, rent-seeking behavior and rampant tax evasion. As a consequence, the federal tax to GDP ratio has declined to 8.6 percent of GDP in 2010/11 from 9.3 percent of GDP a decade ago, with a steep drop during the last few years. At current levels, the tax ratio is not only the lowest in Pakistan for the last 35 years, but also one of the lowest in the world.

3.2 Achievement of Project Development Objectives

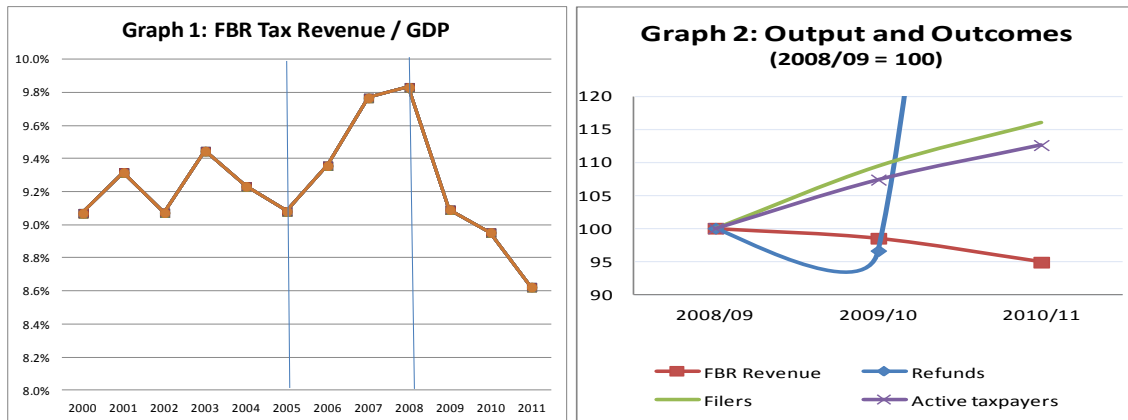
26. **The underlining development objective in terms of FBR tax-GDP ratio was not achieved, despite progress in key intermediate outputs and substantial investments in IT, physical and human infrastructure at FBR.** Notwithstanding moderate gains during 2004/05 to 2008/09, FBR tax-GDP collection has dropped substantially to reach 8.6 percent of GDP by the end of FY 2010/11, the lowest level in more than two decades.

27. During the first half of the 2000s, FBR's tax-GDP ratio followed a cyclical pattern within a narrow range of 9.1 to 9.4 percent of GDP (Graph 1). Despite sustained increases in economic growth, revenue collection from major taxes remained flat, reflecting low tax effort. In fact, the tax buoyancy coefficient reached only 0.93 during this period, meaning that revenue collection increased at a lower rate compared to overall economic growth. However, after project implementation started in 2005, two different and even opposite patterns in FBR tax-GDP ratio

²⁶ DLI stands for Disbursement Linked Indicator.

²⁷ According to the Country Partnership Strategy (CPS) for Pakistan for the period FY 2010-13, “*Weak revenue mobilization is the key challenge for addressing Pakistan's tight fiscal constraints*” (para 39).

were observed: an expansion during 2005-08 and a steep decline in 2008-11 (see Annex 3 for details).



Source: FBR, State Bank of Pakistan.

Source: FBR.

28. The economic crisis in 2008 prompted GoP to take immediate measures to increase tax revenues as part of an own-designed stabilization program, which was supported by the IMF through a Stand-By Arrangement. As a consequence, the reform program gained momentum and project implementation pace speeded up, allowing substantial investments in FBR’s physical and IT infrastructure and renewed efforts on technical assistance to implement FBR’s action plan. As a result, FBR maintained progress against some key outcome indicators. Positive results achieved from FY 2008/09 to FY 2010/11 included: (i) registered and active taxpayers increased by 12% from 3.345 million to 3.774 million; (ii) electronic return filers increased by 19% and 58% for sales tax and income tax filers, respectively; (iii) registered and active taxpayers for Income Tax and Sales Tax (e-enrolled, liable to e-file) increased by 29% and 13%, respectively, and (iv) the amounts of refunds to taxpayers as well as the efficiency for processing refunds increased substantially (Rs. 33 bn to Rs. 106 bn) as a result of efforts to clear the backlog of Sales Tax refunds pending for up to 10 years.

29. However, positive trends on some key outputs achieved during the final years of project implementation fell short of overcoming shrinking revenue performance (Graph 2). FBR’s lower than expected overall performance by end of the project life cycle is associated with three major shortcomings:

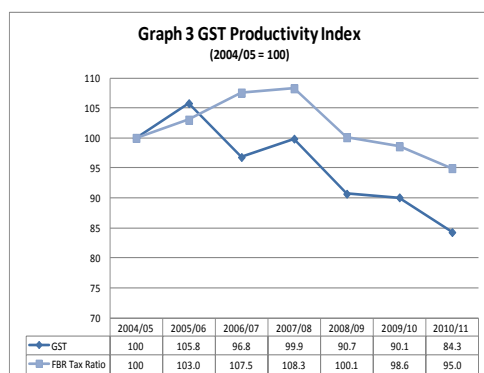
- (a) *Slow integration of FBR organization along functional lines*, because of resistance from staff of the Customs and Excise Group (CEG) and the Income Tax Group (ITG), lack of effective monitoring and evaluation mechanisms, and an unstable tenure at mid-management levels undermining the efficiency and effectiveness of FBR to implement its reform action plan.
- (b) *Underutilization of IT-related systems* due to poor integration of the new systems into re-engineered business processes, weak management follow up on implementation of systems, and opposition of FBR staff to adopt new business processes based on newly deployed systems at field formations; and
- (c) *Continued weakness of the audit function*, associated with lower than expected performance by the audit program delivered by private accounting firms during the outsourcing program,

lack of a centralized-based audit function in charge of planning, programming and monitoring of results, poor training, and unfavorable results to FBR on legal disputes from tax tribunals.

30. Break in the chain of reforms had consequences for the achievement of outcomes envisioned by the project. Without the reorganization of the FBR along functional lines, the redefinition of business processes was left in limbo. Without the implementation of new business processes, related IT investments were insufficiently incorporated into business routines. Without the new IT systems, training and change management investments were delayed. The shift from co-location of tax streams to actual functional integration of tax administration – along with the concomitant changes in business processes, IT systems and HR reforms – did not have consistent commitment and support from within the FBR. **At root of these problems was a lack of consistent political commitment to the major reorganization of tax administration initially envisioned in the GoP’s own strategy and supported by TARP (see Section 5.2)**

3.3 Efficiency

31. Productivity results from GST administration suggest an overall lackluster FBR performance under TARP implementation. Notwithstanding the VAT productivity ratio is typically used in cross-sectional analysis to assess VAT efficiency, the construction of a time series for a given country also serves as a diagnostic tool to gauge tax administration performance through time, when controlled for tax policy changes (see Annex 3 for complete description of GST productivity estimation methodology). During the economic crisis period and subsequent years (2008-11), the GST productivity index declined at a higher rate compared to FBR tax-GDP ratio despite a swift turnaround on project implementation and concomitant positive trends on some outputs by the last two years of project life (see Graph 3). Arguably, major external shocks experienced by the Pakistani economy during this period, with disrupting effects on economic activity - such as the floods during 2010/11 - further undermined weak compliance levels in Pakistan²⁸ beyond FBR capabilities to mitigate their effect. Nevertheless, dismal results in reform implementation described in the preceding section, especially those related to short-term actions aimed at curbing evasion through more effective enforcement actions by the final year of project implementation, strongly suggests a **weak FBR performance from 2008 onward, far from the project objectives envisioned at the outset.**



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3.4 Justification of Overall Outcome Rating

Rating: Moderately Unsatisfactory

32. From a thorough review of outcomes under each component by its closing date, the project only achieved moderately unsatisfactory (MU) achievements against the PDOs. As

²⁸ Economic downturns typically expose tax administrations to emerging challenges due to expected decline of tax file turnaround, increased accumulation of arrears stock, lower payment of withholding taxes, and increase in net operating losses.

discussed in Bank quarterly supervision reports after the restructuring, achievements on intermediate outcome and output indicators, such as increase in taxpayer registration, reduction in stop-filing population, and increasing the number of e-tax filers, have not yet resulted in increased net revenue collection levels in real terms (*see Annex 2 and Section 3.3*).

33. Failure to fully achieve project’s development objectives is partially explained by the lack of comprehensive tax reforms in Pakistan – especially the introduction of a broad based GST- as well as other powerful external and internal factors negatively affecting FBR collection targets, such as the economic slowdown due to domestic and external shocks. FBR management’s lack of success in delivering decisive change as originally envisioned by TARP only worsened the outcome (*see Section 3.2*).

3.5 Overarching Themes, Other Outcomes and Impacts

(a) Poverty Impacts, Gender Aspects, and Social Development

34. Exceptionally weak domestic resources mobilization in Pakistan reduce fiscal space to increase allocation of public expenditure on key social and physical infrastructure required to meet the Millennium Development Goals (MDGs), promote growth, and curb poverty levels.

(b) Institutional Change/Strengthening

35. Despite falling short in fully achieving envisioned PDOs, TARP was instrumental in establishing needed building blocks in terms of human, physical, and IT investment with the potential to strengthen institutional capacity at FBR in the mid and long term. Mostly during the second half of TARP, IDA and DFID financing facilitated massive improvements in FBR’s physical²⁹ and IT-related infrastructure³⁰ enabling the improvement of taxpayer services through refurbished facilities and the successful implementation of e-based services³¹. Also, FBR top management approved a new HRM policy framework in 2010, including guidelines for new job classifications, position descriptions, available training programs, compensation packages, and staff performance evaluation. Detailed job descriptions for positions at field formations reflecting the integrated structures of RTOs/LTUs have been prepared, and new guidelines were approved for mobility, postings, transfers, and career path. Finally, an intensive staff training program was supported by TARP during its final implementation leg, enabling a substantial investment in management and technical skills to a critical mass of FBR officers both at Headquarters (HQs) and field formations.

²⁹ Major refurbishments and development of: 21 Taxpayer Facilitation Centers (TFCs), 13 RTOs, 13 transit accommodations, 9 Model Customs Collectorates (MCCs), and one LTU were completed.

³⁰ Construction and configuration of two state-of-the-art data centers, installation of a video conferencing system linking FBR HQ and 28 other locations, procurement of licensed software, and investment in a critical mass of hardware equipment across field formations, were completed.

³¹ FBR’s website and e-portal currently allows for 100 percent e-filing and a substantial interaction between taxpayers and Facilitation and Tax payer Education (FATE) Wing.

(c) Other Unintended Outcomes and Impacts (positive or negative)

36. The process undertaken by FBR management to establish a new occupational group – the Inland Revenue Service (IRS) - resulted in bitter legal disputes by groups of staff who perceived that their career development had been adversely affected by the reform. The GoP took a series of administrative measures during 2009 to reorganize FBR along functional lines for the achievement of its reform objectives (*see Section 3*) by merging the administration of sales, income and excise taxes at LTUs/RTOs and integrating functions for collection, enforcement, audit and legal. FBR was, therefore, reorganized through the establishment of the IRS, allowing officers from the previously separated occupational groups – the Customs and Excise Group and the Income Tax Group - the option to transfer to the new service or remain in their existing groups.

37. Following allegations related to both substance and formal procedures,³² groups of officers from the Customs and Excise Group Association opposed the reform through different domestic and international legal instruments, triggering among others a review by Pakistan's High Court and a request for investigation to the Bank's Inspection Panel, alleging undue pressure on the GoP by the Bank to undertake the career service reorganization reform. While the Bank's Inspection Panel did not find sufficient grounds for an investigation based on an analysis of the facts presented by both inspection requesters and Bank's management³³, multiple and ongoing legal disputes instituted by groups of officers at field formations have been continuously disrupting FBR operations at some locations since the establishment of the IRS.

3.6 Summary of Findings of Beneficiary Survey and/or Stakeholder Workshops

38. Beneficiary surveys showed mixed results about the reform effectiveness with an overall moderate improvement in perceptions about FBR's transparency, tax facilitation, and service delivery by the end of the project.³⁴ Concomitant with wide deployment of IT solutions in FBR's internal management systems and service delivery to taxpayers after project's restructuring, stakeholders held moderately satisfactory views on the overall automation initiatives carried out by the project. Also, some improvements on stakeholders' perceptions about transparency in FBR operations were registered, mostly by legal experts, large taxpayers, and agents/intermediaries of FBR. These and other favorable perceptions on some aspects of reform were not equally shared by other stakeholders such as trade bodies and the medium and small taxpayer population, signaling the overall mixed and rather insufficient achievement of TARP's outcomes³⁵ (*see Section 3.2*).

³² Groups of staff voiced their concerns about alleged insufficiencies on the consultation process followed by FBR top management towards the creation of the IRS (reportedly, only 15 days were allowed), as well as on the short timeline allowed for the staff to decide upon the options presented.

³³ Request for inspection filed by claimants, Bank's management response and the Inspection Panel's eligibility report are publicly available at the Bank's external website.

³⁴ By request from FBR, representative surveys were carried out in 2007 and 2011 to monitor the stakeholder's perception toward the reform initiatives supported by TARP in terms of service delivery and integrity of the tax system. The surveys were financed by TARP and conducted by Gallup and Bearing Point Pakistan, respectively.

³⁵ Source: FBR-Stakeholders Perception Survey (TARP), BearingPoint, December 29, 2011.

39. From a brief snapshot of the Survey’s findings the following results are noteworthy:

- Overall, a significant majority of stakeholders feel that FBR has facilitated taxpayers to a large extent.
- Majority of respondents share the view that the Expeditious Refund System (ERS) has achieved its target to a large extent by the end of TARP.
- The FBR website has been rated higher than other automation initiatives.
- Alternate Dispute Resolution (ADR) mechanisms have been deteriorating.
- Overall, awareness level of TARP initiatives among stakeholders has been low.
- Tax filing procedures should be simplified.

A graphic summary of the 2011 Survey results are presented in Annex 5.

4. Assessment of Risk to Development Outcome

Rating: *High*

40. FBR’s efficiency gains expected from TARP’s investment on technical assistance, staff training, IT and physical infrastructure, depend on future strong political support and management drive in the context of an overall challenging institutional and security environment. Several of the reform actions achieved so far, such as the reorganization along functional lines, the reactivation of the audit function, and improvement on ITMS, are still faced by tangible opposition forces from within FBR, such as the partial reversal of the functional structure in February 2011.

41. A government dependent upon support from coalition partners in the context of a challenging external and internal environment, combined with an unstable tenure at top and mid-management levels at FBR³⁶, also threatens to undermine continuity of reform efforts. Full integration and utilization of IT systems require strong management drive to overcome lingering opposition of rank and file officers to adopt new business processes at field formations. Emerging internal pressures to adopt a new IT strategy, rather than consolidate the current one, further threatens reform objectives³⁷. The maturity of key reform initiatives introduced through TARP on FBR’s operations in terms of *inter alia* audit, enforcement, and the refund system; depend on a strong M&E system within FBR, which is yet to be consolidated. Finally, the introduction of critical tax policy reforms aimed at increasing revenue collection and introducing fairness and efficiency in the tax system, are unlikely to be introduced in the near term given impending elections and political tension between the Federal Government and some Provinces to agree on a stable and efficient GST-service taxation framework.

³⁶ The last Chairman, FBR under TARP retired on January 2012. Since then, two Chairmen have been appointed, with the one serving at the time of the completion of this evaluation retiring soon. For a complete inventory of number of acting Chairmen, see Section 5.2 (a) and Annex 4B.

³⁷ An external study conducted in 2011 recommended that FBR adopt a new IT strategy.

5. Assessment of Bank and Borrower Performance

5.1 Bank Performance

(a) Bank Performance in Ensuring Quality at Entry

Rating: *Unsatisfactory*

42. The quality at entry was affected by major shortcomings, such as insufficient identification of critical risk factors and mitigation measures, inadequate technical support on key reform areas, and misclassification of environmental category per OP/BP 4.01 (see Section 2.1 for details). In particular, failure in risk assessment by overestimating GoP's political will and institutional buy-in to the proposed reforms by relevant stakeholders within FBR, and inadequate provision for Bank technical assistance to support initial stages of project implementation (e.g. IT-related TA support), affected the quality at entry. On the other hand, the Bank and FBR teams worked closely to develop a project that was in line with GoP's tax administration reform agenda. Also, sufficient resources were provided for all the components at the design stage, particularly for information systems, physical infrastructure development, and for training/capacity building of staff.

(b) Quality of Supervision

Rating: *Moderately Satisfactory, based on MS during the beginning of the project, MU before project restructuring, and S after restructuring*³⁸.

43. Overall, the Bank's supervision was undertaken by adequate technical and operational skills mix³⁹, and Bank policies and procedures were properly applied and pursued, under a difficult implementation environment. The supervision/TA missions identified proper implementation bottlenecks and provided detailed action plans in aide memoires/technical reports to address them, especially in the wake of project's restructuring by mid-2010. Overall, during most of project life, the quality of Bank's supervision suffered on account of lack of coordination between the TA team (funded by a parallel grant) and the Task Team during 2008-09, as well as frequent changes in task team leaders (TTLs) and co-TTLs⁴⁰ (see Annex 4C). The Bank's supervision can be divided into two distinct periods: (i) January 2005 to December 2009 (5 years), during which seven implementation reviews were conducted. After moderately satisfactory supervision at the beginning of the project (2005-2006), the quality and intensity of Bank supervision wavered during 2007-2009, during which period TARP had become a problem project; and (ii) January 2010 to December 2011 (2 years) during which another seven implementation reviews were undertaken⁴¹. The latter intensity of Bank supervision took place in light of the Bank and DFID managements' decision to provide sufficient resources for regular and integrated supervision to move the project out of its problem

³⁸ According to the Borrower's assessment, Bank's quality of supervision after restructuring was rated as *Highly Satisfactory* (see Annex 7).

³⁹ Except that environmental aspects were not regularly covered until around mid-2010. This was essentially because the EMP was prepared only in April 2010, after the re-categorization of the project.

⁴⁰ TARP was approved by the Bank's Executive Directors on December 7, 2004. Between the project approval and December 2009, there were three TTLs and two different co-TTLs. From March 2010 onwards, the project was lead by one TTL responsible for both Bank's operational and TA teams.

⁴¹ The above reviews exclude some TA missions which were generally conducted on a quarterly basis, starting with September 2008.

status⁴². While the supervision effort in some of the earlier years suffered on account of changes in TTLs and inadequate management oversight, it was satisfactory in the last about two years, a period during which two restructurings⁴³ were undertaken and, remarkably, **procurements of about US\$41.6 million (58% of total disbursements under TARP) were completed during the last 18 months (July 2010 – December 2011)**. Also, during the last two years of project's implementation, sufficient attention was paid to fiduciary and safeguards issues.

(c) Justification of Rating for Overall Bank Performance
Rating: *Moderately Unsatisfactory*

44. Based on the *Unsatisfactory* rating under 5.1 (a), and *Moderately Satisfactory* rating under 5.1 (b), the overall Bank performance is rated as *Moderately Unsatisfactory*⁴⁴.

5.2 Borrower Performance

(a) Government Performance
Rating: *Unsatisfactory*

45. While recognizing the challenging country context prevailing during the TARP period, overall, GoP showed an inconsistent commitment to its own tax administration reform agenda, which significantly affected project's implementation. During the initial years of TARP⁴⁵, GoP took several steps to show its strong commitment to the project, including: (a) establishment of LTUs/MTUs; (b) confirming the Chairman, FBR for three years and renewing the terms of the Members responsible for functional areas; (c) granting FBR greater autonomy under the oversight of the Cabinet Committee on Finance and Revenue (CCFR); and (d) preparation of a rationalization plan for FBR staff. In line with GoP's commitment to the reform agenda, the FBR Act 2007 was enacted⁴⁶. The GoP also provided relatively adequate counterpart funds until the restructuring.

46. However, the Government's commitment to major tax policy and administration reforms wavered over time, especially during the boom years (2005-2008) when higher economic growth generated modest revenue gains, despite limited results on its tax administration reform program (see Sections 3.2 and 3.3). The security of tenure of key and senior FBR officials of at least three years was a desirable requirement to move the reform agenda forward. Yet, during the nearly seven years of project life, four Chairmen were appointed, with some of them coming from outside the Income Tax and Customs services⁴⁷ which did not go down well with some of FBR's

⁴² A technical assistance team on tax administration (referred to as the TA team in this report) started providing technical advice to FBR in September 2008. One joint implementation/TA teams' review was conducted in April 2009, while starting with May 2010 (Restructuring mission) Bank management instructed both teams to undertake joint reviews.

⁴³ A second restructuring paper was prepared in November 2011 to amend the DCA, based on a request from GoP.

⁴⁴ This rating is consistent with the MU rating for project outcome (see the *Ratings Summary* in the data sheet section).

⁴⁵ Including the preparation and implementation of PPF activities.

⁴⁶ The Federal Board of Revenue Act, 2007 replaced CBR with FBR and established CCFR. The CCFR was replaced with a Policy Board in the Federal Board of Revenue (Amendment) Act, 2011.

⁴⁷ Civil service in Pakistan includes several groups, such as: district management, foreign service, police service, customs, income tax, etc.

staff. FBR Board members and senior officials were transferred frequently. The CCFR also did not meet regularly to provide necessary oversight and guidance. Nor did GoP implement the plan for the rationalization of FBR staff (*see Annex 4B*).

47. The above major shortcomings impaired the achievement of the tax administration reforms. Subsequently, the GoP committed to a significant increase in tax revenues through *inter alia*: introduction of a broad-based Value Added Tax (VAT), or reformed General Sales Tax (RGST); reintroduction of tax audits; and strengthened enforcement measures. However, despite the critical need to implement these tax policy and tax administration reforms, which were required to address the macroeconomic imbalances in 2009/10 and onwards, GoP was unable to secure political consensus on the passage of the proposed VAT or RGST bill by the TARP closing date.

(b) Implementing Agency's Performance
Rating: *Moderately Unsatisfactory*

48. **Given the country context during TARP implementation, FBR achieved several positive outcomes, but insufficient to be translated into higher tax/GDP ratio by project's closing date** (*See Section 3.2*). Positive outcomes included *inter alia*: completion of several physical and IT infrastructure related sub-projects at several locations across Pakistan; introduction of the universal tax assessment scheme; significant increases in the number of registered and active taxpayers, electronic return filers for both income and sales taxes, and in the volume and timeliness of sales tax refunds, especially to exporters. **Notably, the PMU team showed a remarkable improvement in the last 18 months of project's life under the leadership of a dedicated and committed manager resulting in completed procurements for about US\$41.6 million – 58% of total disbursements under TARP⁴⁸.**

49. **However, FBR management contributed to the delays in TARP implementation and displayed an overall insufficient commitment to the reform agenda by not taking necessary decisions in its own domain in a timely manner.** Examples in this context include *inter alia*:

- i. Long delay in, or inattention to, the implementation of Bank missions' recommendations relating to the strengthening of the PMU⁴⁹, monitoring of the KPIs, ensuring coordination at FBR HQs and with field formations, and the enhancement of enforcement and audit actions;
- ii. Indecision of over two years on the IT strategy to be followed to procure the tax management system between off-the-shelf solutions or own design of systems through the Pakistan Revenue Automation Ltd (PRAL⁵⁰). Once a decision on the latter option was

⁴⁸ The performance of the PMU during the last 18 months of project implementation is considered highly satisfactory.

⁴⁹ FBR's experience with the hiring of private sector consultants for the PMU, rather than building internal capacity, proved to be unsuccessful (*see Annex 7, para 19*).

⁵⁰ PRAL is an FBR owned private limited company, set up in 1994, to provide IT services to FBR, empowered to hire competent and qualified IT professionals at market salaries.

made, FBR failed to mobilize resources to adequately monitor the internal development of ITMS by PRAL, resulting in non integrated tax management systems;

- iii. Failure to appoint a Member solely responsible for the coordination and monitoring function, both within FBR HQs Wings and between HQs and field offices, resulted in weak management of the reform action plan;
- iv. FBR's inability to carry out agreed actions based on its own action plan⁵¹ such as FBR's reversal of decisions agreed with the Bank on moving to a functionally integrated organization, a key pillar of the overall TARP reform plan;
- v. FBR's inability to provide security of tenure at mid-management level; and
- vi. Delays in implementation of the training program until the last year resulted in under-utilization of the IT systems. Because of the delays experienced in its early years of implementation, the project suffered from slow disbursements.

(c) Justification of Rating for Overall Borrower Performance

Rating: *Unsatisfactory*

50. The overall rating is based on the ratings under 5.2 (a) and 5.2 (b), considering major shortcomings described above which hampered project implementation, such as Borrower's inability to take decisive action on key tax policy reforms, frequent changes at senior management level at FBR HQs and PMU, and lack of adequate M&E arrangements.

6. Lessons Learned

51. The major lessons learned from the implementation and outcome of TARP are summarized below.

- i. Substantial enhancement of tax administration effectiveness requires fundamental organizational change.** Revenue administration reforms entail the implementation of substantial organizational reforms with the potential to disrupt operations at field formations and inflame staff's stiff resistance to change. Extensive consultations with stakeholders using a bottom-up participatory process, constructive dialogue, and adequate risk mitigation measures at the outset are needed. Reorganization action plans need to be phased carefully over a realistic period, while adequate safeguards and ongoing monitoring to facilitate stakeholders buy-in and to address perceived or real inequalities among staff, need to be actively undertaken through an effective communications and outreach program.
- ii. Revenue targets could be an unsuitable performance outcome indicator for revenue administration reform projects.** The use of revenue targets as major development outcome KPI makes it difficult to track pure revenue administration performance, dislocates the input-output-outcome result chain, and could introduce wrong incentives for revenue agency's managers to engage in ad-hoc and short-term revenue measures, rather than mid- and long-term institutional building reforms. Tax gap (difference

⁵¹ Serious ownership issues were detected among rank and file FBR's officers about the Action Plan agreed by the Bank's TA team and the FBR management team in September-October 2008.

between potential and observed outcome, both at the overall tax system level or by type of functions, taxpayers or taxes) is a measure better suited to gauge a tax agency's performance.

- iii. **Tax policy and other legal reforms must be identified and prepared in advance of project implementation if expected increases in tax administration effectiveness and tax collection are to be achieved.** In case tax policy reforms are not introduced in a timely and effective way, mitigating measures must be in place along with the needed political and institutional commitment to carry them out. Tax policy and other legal changes need to be taken in parallel with institutional capacity development to achieve full benefits from planned reforms.
- iv. **A broader and continued policy dialogue on tax reform is needed in parallel to increase likelihood of success of revenue administration reforms.** Supervision of investment projects can quickly get bogged down in the minutiae of implementation issues, diverting attention from a broader policy dialogue on fundamental tax reform that is critical to ensure that project outputs are converted into sustainable results.
- v. **To be effective, newly deployed IT systems must be accompanied by requisite operating business procedures and continuous training, following a solid strategy set out at preparation stage with a holistic view on both operational and institutional reform.** There also needs to be sufficient incentives for staff to adopt new procedures, through the development and implementation of new business processes that the staff can be trained in and evaluated against. As part of the project monitoring system, it is important to ensure that when new IT applications are introduced in the field: (a) they are field tested, (b) adequate training in new business processes is provided to users, (c) adopting the new procedures is identified in strategic plans, and (d) rewards or recognition of staff for adopting new processes are in place.
- vi. **The continuity of the Bank's Task Team, with the right mix of technical skills and Bank operational experience, is a necessary condition for successful supervision of revenue administration projects.** TARP implementation has demonstrated the need for Bank's Task Teams to maintain a continued, comprehensive and long term focus on the entire tax system with a strong operational support on Bank operations. To be effective, Bank's support on revenue administration reform needs to address institutional building, tax policy analysis, political economy/governance considerations, and emerging operational issues in an integrated way.
- vii. **Stand-alone investment loans may not be the most appropriate instrument for supporting major tax reform.** Effective support of high-risk/high return investment such as fundamental tax reform requires an array of Bank's instruments suited to tackle capacity building, tax policy, legislative reforms, and political economy analysis towards specific and long term maturing development objectives. Flexible and results-oriented lending instruments supporting a tax reform strategy with sensible sequencing of actions, greater recognition of political economy factors and the governance context, robust TA support, and continued policy dialogue, are best suited to bring sustained development objective results compared to the traditional, stand-alone investment lending approach.
- viii. **Technical assistance can be effective in supporting tax administration reform if the revenue agency has full ownership of the program, and the TA is well designed and provided in a timely manner.** Technical assistance support contributes to better dialog with counterparts, keeps track of project's ongoing activities, and helps in redirecting

assistance to meet capacity gaps and maintain commitment as needed, especially when implementation issues prove more challenging than anticipated. However, all sources of TA, including those provided by parallel instruments, need to be fully integrated under a single operation with fully coordinated Bank supervision.

- ix. To increase likelihood of tax reform success, a thorough and systematic political economy analysis (PEA) should not only be seen as a desirable feature, but rather as a key component of project design and implementation.** As taxation proves to be a development area with increasing interaction between economics and politics, investment on PEA analytic work could result in a better design, timing, and sequencing of Bank supported reform plans. PEA may also provide teams with a better understanding of the likely reform outcomes to be expected from the interaction of multiple stakeholders, within imperfect political markets, weak institutions, and uncertain economic conditions.

7. Comments on Issues Raised by Borrower/Implementing Agencies/Partners

(a) Borrower/implementing agencies:

52. The Borrower noted in their Project Completion Report (PCR) that the Bank's supervision was strong at the beginning of the project but over time became weaker, suggesting that feedback and requests for clearances took longer, leading to many procurement delays. However, it was stated that after TARP's restructuring, feedback and support was excellent. The Borrower cites as evidence that 58 percent of expenditure occurred after restructuring; moreover, during the first five and a half years of the project, total expenditure was PKR 2.1 billion (US\$ 30.8m), while after restructuring (18 months) it was PKR 3.4 billion (US\$41.6m). The Bank's overall performance after restructuring was rated as "highly satisfactory" by the Borrower.

53. The Borrower's PCR has highlighted a number of lessons learned including: (i) the provision for technical assistance should be driven by the demand of the implementing agency (only 22% of funds allocated for TA-consultancies were used by FBR); (ii) business process reengineering and related automated applications must be fully integrated throughout the tax administration with appropriate management and training aspects; (iii) competent officials should be identified from within the organization, and adequately trained for positions within the PMU for the entire length of the project, is a better option than relying on private sector consultants; and, (iv) SOPs/Manuals should be prepared prior to commencement of the project to facilitate implementation. Also, the Borrower made several suggestions for improving the Bank's procurement processes. The above lessons have been reflected in the main section on lessons learned (*see Section 6*).

54. The Borrower has observed that: (i) the overall rating was downgraded from moderately satisfactory to moderately unsatisfactory on account of non-implementation of 15 of the 22 priority measures agreed in April 2011, (ii) of the FBR's 2008 Action Plan, which was the blueprint for the restructuring, 100 activities and their subtasks were completely implemented, (iii) substantial improvements under the project have established the foundation of future and deeper reforms, and (iv) the full extent of the reforms cannot be fully captured quantitatively by the KPIs and that in that context, from the Borrower's perspective, the PDOs were basically achieved under the restructured TARP.

55. This difference in perception between the Bank and the Borrower on the achievement of project PDOs and impact of activities may be due to an emphasis on an array of quantitative indicators that the counterpart suggests do not accurately capture the overall benefits of the

project accruing to FBR. This may be due to FBR's perception that the institution building that took place was not subject to equal weight in assessing project outcomes. In the Bank's view, substantial investments under TARP have contributed to improvement in physical and IT related infrastructure, but these investments are yet to be translated into sustained outcomes to achieve the reform objectives (*see Annex 7*).

56. The implementing agency's comments on the draft ICR have been included in Annex 7. In terms of some of the comments raised on the number of staff trained, status of HRM policy and strengthening of appeals function, these have been reflected in the ICR.

(b) Cofinanciers:

57. According to DFID's PCR, given that much of the progress achieved by TARP occurred during the last two years of implementation in the midst of an overall deteriorating political and macro-economic environment, **it is important to have a thorough understanding of the political context when engaging in institutional reform.** Within a challenging implementation environment, DFID recognizes that a more active oversight was required to keep track on implementation progress and maintain a continued policy dialogue on issues affecting project's performance (*see Annex 8 for a summary of DFID's PCR*).

58. In hindsight, the Bank recognizes that for most part of project implementation, a more active and productive policy dialogue between the Bank and DFID with GoP, on fundamental decisions affecting revenue mobilization and institution building at FBR, was required to address timely implementation insufficiencies within a highly complex and changing environment. Also, the Bank acknowledges the importance of conducting timely political economy analysis (PEA) and social /stakeholder assessments when engaged on institutional reform projects like TARP (*see Section 6- ix*).

(c) Other partners and stakeholders

N/A

Annex 1. Project Costs and Financing

(a) Revised Project Costs (USD million)

	Original Estimate at Appraisal				Revised Cost Estimate			
	IDA	IBRD	DFID	Total	IDA	IBRD	DFID	Total
Works	18.00		-	18.00	31.04	-	-	31.04
IT Systems: Software and hardware	41.60	24.40	10.00	76.00	6.86	-	16.85	23.71
Consultant Services	6.10		8.00	14.10	5.11	-	2.16	7.27
Training	5.00		5.00	10.00	2.37	-	3.99	6.36
Vehicles	2.40	-	-	2.40	2.11	-	-	2.11
Incremental Administrative and Operational Costs	2.50	-	-	2.50	3.29		-	3.29
Front End Fee						0.12		0.12
Total	75.60	24.40	23.00	123.00	50.78	0.12	23.00	73.90

Notes:

- 1) The original estimate included the refund for the Project Preparation Advance of US\$2.9 million, bringing IDA financing to US\$78.5 million and donor funding to US\$125.9 million.
- 2) The Front End Fee of US\$0.122 million, which has already been charged, has been included in the project cost above.

(b) As per TARP PC-I estimates and Restructuring Paper (excludes USD\$0.122m from IBRD)

No.	Description	Cost Estimates (Rupees)	GOP Component (Rupees)	Foreign Component (Rupees)	Foreign Component (Equivalent US\$)
1	Technical Assistance	629,916,174	71,010,450	558,905,724	7,265,212
2	ICT- Software	312,370,000	6,247,400	306,122,600	3,826,533
3	ICT-Hardware	1,686,000,000	168,600,000	1,517,400,000	19,886,400
4	Infrastructure Development	2,880,648,216	687,220,174	2,193,428,042	31,036,510
5	Vehicles	178,864,000	35,772,800	143,091,200	2,113,600
6	Training	493,417,000	14,802,510	478,614,490	6,365,140
7	Program Management	291,601,974	55,404,375	236,197,599	3,289,941
	Total	6,472,817,364	1,039,057,709	5,433,759,655	73,783,336

(c) Project Cost by Component (in US \$ Million) prior to Restructuring

Components		Appraisal Estimate (US\$ millions)	Actual Expenditure (US\$ millions)	Percentage of Appraisal
1	Management & Institutional Development	9.29	1.643	17.68
2	Improving Revenue Operation	93.17	1.569	1.68
3	Strengthening Revenue Services	6.62	1.286	19.42
4	Tax Compliance Culture	6.27	0.147	2.34
5	Adopting Responsive IT System	3.65	6.284	172
6	Infrastructure Up-gradation	24.00	18.136	75.56
7	Program Management	3.10	1.743	58.26
Total Project Costs		149.00	30.813^{1/}	20.68

^{1/} PPF disbursement of US\$1.946m is not included.

(d) Project Cost by Component (in US \$ Million) after Restructuring

Components		Expenditure (US \$ millions) ^{1/}
1	Enforcement Including Audit	3.032
2	Organization & Management	20.275
3	Information Technology	16.671
4	Program Management & Implementation	1.622
Total Project Costs		41.600

Source: PMU

^{1/}These figures are still provisional because reconciliation with the World Bank, State Bank of Pakistan and National Bank of Pakistan remains to be done in due course of time.

(e) Financing

Source of Funds		Type of Co-financing	Appraisal Estimate (US \$ million) ^{1/}	Revised Cost Estimate at Restructuring	Expenditure (US\$ million) ^{2/}
1	IDA	Credit	75.60	50.78	45.627
2	DFID	Grant	23.00	23.00	18.539
3	IBRD	Loan	24.40	0.12	0.122
4	Local	Local	23.10	0	8.247
Total			146.10	73.90	72.535

Source: PMU

Note: Because of fluctuations of the SDR exchange rates against the US dollar and Pound Sterling during the implementation period, the DFID grant of GBP 12.152m did not translate into US\$23m. It resulted in about US\$18.539m (as shown above) which was fully utilized. The shortfall in the DFID grant was offset by the IDA Credit on account of the depreciation of the US dollar against the SDR.

1/ Excludes IDA PPF amount of US\$2.9m.

2/ Provisional figures as reconciliation with the World Bank, State Bank of Pakistan and National Bank of Pakistan remains to be done. IDA amount excludes PPF disbursement of US\$1.946m, per Bank's client connection system. The actual expenditure under IDA, DFID, and IBRD amounts to US\$64.288 million. This is reflected in the ICR's Data Sheet.

Annex 2(A): Project Outcome Indicators

Indicator	Outcome
<p>1. FBR gross and net revenue collection as percentage of tax revenue target.- Baseline 2009/10 (net revenue collection) Rs. 1,327.4 bn.</p>	<ul style="list-style-type: none"> FBR net revenue collection for FY 2010/11 was Rs 1,558 bn, against a (post-floods) target of Rs 1,604 bn, for an achievement ratio of 97.1%. Hence, FY 2010/11 revenue collection felt slightly short of target. For the period July-December 2011 (end of project) FBR revenue collection was Rs.840.7 bn, slightly above the target of Rs. 839.7 bn.
<p>2. FBR total tax collection/GDP (<i>annual</i>) - Baseline 2009/10- 9.4%; Est. target end project-9.8%.</p>	<ul style="list-style-type: none"> FBR tax collection /GDP for FY 2010/11 was 8.6%. Target was not achieved
<p>3. Survey-based user ratings for FBR- Baseline survey conducted in 2007; Next survey planned in FY'11.</p>	<ul style="list-style-type: none"> CY 2011 Beneficiary survey showed mixed results about the reform effectiveness with moderate improvements on perceptions about FBR's transparency, tax facilitation and service delivery (<i>see section 3.6 and Annex 5</i>)
<p>4. Stop-filers as percentage of registered active taxpayers (total, type of tax, taxpayer size)- Baseline 2008/09 – Companies 54%; Individuals 40%; end project target - Companies 53%; Individuals 39%.</p>	<ul style="list-style-type: none"> By end of project, FBR reported filing figures by tax type only. Stop-filers base line for FY 2008/09 was: Income tax 67%; and Sales tax 4%. By end of project life: Income tax: 28%, and Sales Tax 8%. Overall, the outcome achieved seems satisfactory as total stop-filers fell to 23% in FY 2011/12 from 47% in FY 2008/09.
<p>5. Additional tax paid after audit as percentage of total collection of domestic taxes — Baseline 2009/10 Rs. 7,560m (0.56% of total tax collection); est. target end project-Rs. 7,700m.</p>	<ul style="list-style-type: none"> By end of FY 2010/11, additional tax collected after audits is Rs 6,231m (0.39% of total tax collection), hence the outcome was not achieved.
<p>6. Modernized FBR organizational structure fully functional.</p>	<ul style="list-style-type: none"> Moderately Satisfactory (<i>see Appendix 2c below for details on implementation ratings for Component 2 – Organization and Management</i>)

Annex 2(B): Intermediate Outcome Indicators

Outputs	Intermediate Outcomes	Intermediate Outcome Indicators	Project Outcomes
Organization and management:			
<ul style="list-style-type: none"> FBR structure integrated and function based A new HRM policy and rules for staff evaluation and mobility based on merit implemented Training program for mid-level staff 	<ul style="list-style-type: none"> Improved organizational efficiency and effectiveness of revenue administration 	<ul style="list-style-type: none"> Administrative cost of collection as % of total tax revenues (<i>annual</i>) – maintain below 1% A large number of mid-level staff trained (<i>annual</i>) – estimate 5,000 p.a. 	<p>By FY 10/11, the figure was 0.87%, therefore the target was achieved.</p> <p>2,694 officers were trained; hence the target was not achieved.</p>
<ul style="list-style-type: none"> An action plan to improve staff integrity implemented 		<ul style="list-style-type: none"> User ratings for Taxpayer Facilitation Centers through periodic taxpayer surveys (actual experience and perceptions) (<i>annual</i>) 	<p>A beneficiary survey was conducted in 2011 (<i>see section 3.6 and Annex 5 for results discussion</i>)</p>
<ul style="list-style-type: none"> A new set of performance indicators with specific benchmarks covering taxpayer registration, filing, audit, enforcement of arrears payment, and appeals – e.g. e-filing and e-payment extended to most income tax taxpayers Periodic reports on FBR performance to the FBR management, Board, and the public (<i>annual</i>) 		<ul style="list-style-type: none"> Per cent of tax returns filed electronically (by type of tax) (<i>annual</i>) – Baseline 2008/09 - 36% <p>End project target – 45%</p>	<p>e-filing for Sales Tax and Income Tax (corporations) reached 100% by the end of project. Yet, e-filing for Income Tax (AOP, individual business and salary) is 32% on average</p> <p>Overall, the target was achieved.</p>
Enforcement including audit:			
<ul style="list-style-type: none"> Implementation of the new taxpayer ledger 	<ul style="list-style-type: none"> Improved compliance and enforcement, including audit 	<ul style="list-style-type: none"> Percentage reduction of tax arrears (<i>annual</i>) <ol style="list-style-type: none"> Less than 6 months More than 6 months – Baseline (2009/10) – less than 6 months – 73,335; more than 6 months – 35,164 	<p>No figures were available by the end of project to assess the achievement of this target.</p>
<ul style="list-style-type: none"> GST operations adapted to VAT/reformed GST⁵² 			
<ul style="list-style-type: none"> VAT/reformed GST enforcement and compliance 			<p>FY'11 stock of arrears increased</p>

Outputs	Intermediate Outcomes	Intermediate Outcome Indicators	Project Outcomes
activities implemented ¹			by 15.6% compared to FY' 10, hence the target was not achieved
<ul style="list-style-type: none"> Electronic Refund System implemented 		<ul style="list-style-type: none"> Reduction of stock of arrears as percent of stock of arrears for previous year (<i>annual</i>) 	
<ul style="list-style-type: none"> Expanded use of third-party information 		<ul style="list-style-type: none"> Number of registered active taxpayers (total and by type of main taxes) (<i>annual</i>) – Baseline 2008/09 – 3.34m; Target – 10% <i>annual increase</i> 	FY'10 – 3.59 M FY'11- 3.77 M Annual increase has been 7.4% and 5.1%, respectively, so the annual target was not achieved by end of project.
<ul style="list-style-type: none"> Enforcement programs using single NTN as taxpayer identification number and targeting taxpayers with high revenue potential 		<ul style="list-style-type: none"> Reduction in the percentage of non filers, tax arrears, and returns with errors (<i>biannual</i>) 	Stop filing outcome is reported in Annex 2(a), item 4. No data was available for tax arrears and returns with errors by the end of the project.
<ul style="list-style-type: none"> Improved taxpayer registration 			
<ul style="list-style-type: none"> Risk-based audits conducted by FBR staff 		<ul style="list-style-type: none"> Reduction of the tax gap (<i>annual</i>) 	The evidence available from tax gap studies is not conclusive to make an accurate assessment of this KPI.
<ul style="list-style-type: none"> Action plan to strengthen the appeals function implemented 		<ul style="list-style-type: none"> Reduction on average number of days to complete administrative appeals process (<i>annual</i>) – Baseline 2009/10 – 60 days 	First Appellate Stage – 120 days allowed. Most cases are decided within 60 days.
Information Technology:			
<ul style="list-style-type: none"> IT applications integrated under a single structure 	<ul style="list-style-type: none"> Improved integrity and fairness of tax administration 	<ul style="list-style-type: none"> Strengthened FBR information systems and their management operational (<i>by Dec. 2011</i>) Effective use of the IT systems by FBR field offices (<i>by Dec. 2011</i>) 	See Annex 2(c) for a complete assessment and rating of this component.
<ul style="list-style-type: none"> Action plan for IT systems in field offices implemented 			
<ul style="list-style-type: none"> An integrated taxpayer/tax type accounting adopted 			
<ul style="list-style-type: none"> ISP 2011-2012 prepared 			
<ul style="list-style-type: none"> Regular business process reviews and adjustments 			
<ul style="list-style-type: none"> A disaster recovery data center implemented 			
Project Management:			
<ul style="list-style-type: none"> Quarterly/Annual progress reports 	<ul style="list-style-type: none"> Project management and implementation on track 	<ul style="list-style-type: none"> Timely project implementation, including adherence to procurement schedules 	The outcome was fully satisfactory (<i>see sections 2.4 and 5.2(b) for a complete discussion and assessment</i>)

Annex 2 (C): Assessment by Components

Revised Components	Achievements/Outputs	Not achieved	IP Rating
1. Enforcement (including audit)			
Carrying out measures to ensure compliance with registration, filing and payment requirements i. Registration/e-registration ii. E-filing and e-payment	Control of unregistered taxpayers <ul style="list-style-type: none"> • Introduction of a single TRN • Important increase in registered taxpayers Control of non-filers <ul style="list-style-type: none"> • Introduction of e-filing • Improved control of non-filing • Introduction of the active taxpayer list (ATL) 		MS
Implementation of the reformed GST /VAT	Some zero rated and exempt items were brought into the GST at transitional rates (e.g.: tractors, fertilizer, domestic sale of textiles)	Implementation of a reformed VAT/GST system. The authorities decided not to implement it for political reasons.	U
Extension of the automated refund system to other LTUs/RTOs for GST, Income Tax and proposed VAT / reformed GST	Control of ST refund <ul style="list-style-type: none"> • Implementation of a modern refund system, which has improved considerably the payment of refunds. The system is implemented in all LTU/RTO for GST. 	Only GST manufacturers cum exporters are participating	MS
Carrying out of audits (post, targeted, composite and desk) including annual audit plans; third-party matching; risk-based prioritization of cases (e.g. audit, follow-up, compliance); detecting tax fraud	Reduction of evasion/audit <ul style="list-style-type: none"> • Introduction of self-assessment particularly for income tax • Introduction of information crosschecking with invoice data • Introduction of a risk management system Control of underground/cash economy <ul style="list-style-type: none"> • Requirement of payment by checks for amounts above a certain amount to qualify for ST input credit • Expansion of the withholding system 	High occurrence of successful appeals by taxpayers indicates poor quality audits being undertaken.	MU
Carrying out of a workflow review and automation of the appeals/disputes process.	FBR is starting to review the appeals process	Not achieved. FBR is focusing on enforcement, audit first.	HU
Collection of arrears (outstanding debt)	Control of arrears <ul style="list-style-type: none"> • Introduction of the enforcement plan • Prioritization of enforcement actions (according to the arrears size) • Introduction of e-payment 	It is necessary to proceed to populate the ledger with current payments/charges as they occur. Also it is necessary to charge Core Business Domain Team and Enforcement staff to develop the	MS

Revised Components	Achievements/Outputs	Not achieved	IP Rating
		arrears recovery officer's application	
Carrying out of studies to determine the tax gap	A study was prepared for ST gap in 2009 for tax year 2006-07.	No methodology was designed or group established to measure the tax gap in a continuous way. This is due to lack of resources and lack of management decision. No funding was allocated for this activity.	N/A
Training staff on risk-based audits and skills update	Currently FBR audit is based on risk analysis. The refund system is based on risk analysis as well	No training specifically provided for risk based auditing.	HU
Carrying out of measures for taxpayer facilitation and education on fulfillment of tax obligations.	Taxpayer service <ul style="list-style-type: none"> Development of a strong taxpayer service system Creation of an online tax portal for e-filing and communicating with FBR 		MS
Carrying out of business process review for the enforcement function.		Not completed yet. This is due to delays in establishing a business owners group to conduct the review	HU

2. Organization and Management for Efficiency

Implementation of organizational change management <ul style="list-style-type: none"> i. Management practices 	There are several critical problems with management practices that are negatively impacting FBR's effectiveness. These are: <u>Follow-up:</u> There is limited active follow-up on important initiatives. <u>Coordination:</u> Ineffective coordination among Operations, Enforcement, Audit, PRAL and RTOs/LTUs is seriously undermining the effective implementation of instructions from HQs by field formations resulting in ineffective operations. <u>Accountability:</u> Relevant staff are not held accountable for implementing instructions from HQ, which in turn is not exercising effective sanctions against non-performance.		U
ii. Structure-functional integration	The FBR moved first into co-location of staff as part of its strategy for integration. Some of the measures to make integration possible were: <ul style="list-style-type: none"> In January 2009 an integrated organizational structure was approved, which eliminated Sales Tax and Income Tax 	The list of actions taken is a reflection of the legal, administrative and judicial difficulties found in putting in place an integrated organization.	MS

Revised Components	Achievements/Outputs	Not achieved	IP Rating
	<p>wings and included a single operational Wing for supervising the work of RTOs and LTUs. This first approach was insufficient given the legal limitations and the judicial challenges against that model.</p> <ul style="list-style-type: none"> • In May 2009 it was decided to implement a new organization based on integration of core tax administration functions and cross-delegation of power by Commissioners/Collectors in the regional offices. • On June 30, 2009 the authorities decided to establish a <i>revised</i> functionally-integrated organization at senior management level and in RTOS and LTUs, and to establish new occupational groups. • Legal complaints during 2009 delayed substantially the implementation of the organizational structure approved early that year. • Once the judicial process is resolved, the integration process can be considered accomplished in terms of the basic structure of organization. 	<p><u>Partial Reversal</u>: The new FBR organization, in place since March 2011, appears to depart from the model along functionally based and integrated organization supported by TARP by downgrading functional areas at field formations. It is too early to assess its impact on effectiveness, and additional time is needed before assessing its real impact on overall FBR performance. A holistic assessment at the national level based on KPIs is needed to gauge performance progress of core functions for tax administration (audit, enforcement and legal) before reaching solid conclusions.</p>	
iii. Planning and coordination	<p>A formal planning process has not been implemented in FBR. However, since October 2008, FBR started to use a detailed Action Plan to serve as a monitoring framework to follow up progress in the reform process, including an enhanced focus on the integrated administration of sales, income and excise taxes. This instrument has been put in practice as a management tool by the Chairman and the Board to keep control on a regular basis of the status of implementation and identification of results for the mid-term management of FBR.</p>	<p>Coordination and monitoring at the management level remains a problem. An initiative agreed between the FBR and the Bank to create a Wing and appoint a member exclusively dedicated to coordination and monitoring of the Action Plan was not done.</p>	U
Upgrading of human resource policies and management	<p>In 2010, FBR approved a “Human Resources Management Policy Paper.”</p>		S
	<p><u>Job descriptions</u>: Job descriptions for positions at field formations reflecting the integrated structure of RTOs/LTUs have been completed.</p>		MS
	<p><u>Mobility</u>: New guidelines were approved in December 2010 for</p>	<p>Not completed yet.</p>	MS

Revised Components	Achievements/Outputs	Not achieved	IP Rating
	<p>internal job postings (IJP). These guidelines establish rules for the payment of a special allowance to employees that have been selected by the IJP process, including technical and computer proficiency requirements for grades BS5 to BS16. A more comprehensive approach to establish competency requirements for all grades should be prepared after job descriptions are updated. Implementation in progress.</p>		
	<p><u>Staff evaluation system:</u> The current system based on the Establishment Division rules provides room to include specific consideration of objective performance indicators as part of the annual evaluation exercise. The use of objective indicators to assess the employee's contribution to achieve the annual targets established for his/her unit is being considered for the future. FBR requested the MoF authorization for using a set of key performance indicators (KPI) to monitor field units' performance linking both the individual and units performances. The use of KPI for the implementation of the performance-based bonus that will be paid in 2011-12 and for the annual performance evaluation report will require training for supervisors to ensure that a homogeneous procedure is used.</p>	<p>The assignment of staff to each position according to new job descriptions is also a pending task. The number of cases (taxpayers) assigned to Zone Commissioners vary considerably among different RTOs. Even though five new RTOs have been created in the last year (there are 18 in total), there are significant differences in the workload that they carry. To enhance the efficiency of RTOs/LTUs requires that redeployment of staff be completed</p>	<p>MU</p>
	<p><u>Staff training:</u> FBR is implementing during the period September-December 2011 a very intensive program of staff training for several groups of employees focusing on distinct areas and various modalities. In addition to activities with TARP funding, there is also an ITMS training program which started with a pilot program in RTO Islamabad and is planned to extend to all field formations. Training program focuses on management and technical issues that correspond to priorities of the FBR operations and have strategic relevance in the modernization of the agency. Activities that will be conducted during the rest of the program are:</p>	<p>The original plan to train almost 5,000 officers and officials at various levels in FBR has been significantly reduced with the purpose of a substantial improvement in focus with respect to the initial plan and to avoid interference in FBR operations.</p>	<p>MS</p>

Revised Components	Achievements/Outputs	Not achieved	IP Rating
	<p>Events Participants Taxpayers Facilitation 500 Job-Related Management – Foreign 50 Job-Related Management - Local 250 Job-Related Technical – Local 200 Job-Related Technical Staff 800 Management Training for BS 19 350</p> <p>The training offered on technical issues focused on two aspects: audit and information technology (IT). This allocation of effort reflects the importance of both dimensions for the work of FBR and the challenges for modernization of tax administration.</p>		
Upgrading infrastructure and adoption of responsive IT systems to improve efficiency	Infrastructure (buildings and equipment) are significantly improved; ITMS is operational and offering a suite of tools to allow staff to perform their job – training in use of the system is still in progress.		S
Diagnostic study and independent assessment of mid-term modernization requirements for Customs, including IT systems.		Study was not done as funding was not allocated to it. As a result, this is not rated.	Unrated

3. Information Technology

Adopting responsive IT systems	<p>Partially done. The Integrated Tax Management System (ITMS) developed by FBR and PRAL has been made available to the field formations and is being rolled out with a training package. The current ITMS provides the following core functions: taxpayer registration, tax obligation registration, return processing, automated sales tax refunds, enforcement of non-filing and of delinquent payments, tracking for audits including identifying the investigation areas for the audit along with the auditors assigned to the audit and its results, bank payment reconciliation and a data warehousing function for matching and detection of potential new taxpayers along with feeding the risk management profiling of taxpayers. Some components are in national use (e.g.: the audit modules</p>	<p>Debt collection functions are not currently available in ITMS – their design is being undertaken and this sub-system should be available in early FY2012. Different components of ITMS are currently under review in a process carried out by the Core Business Domain Team and PRAL, to design a complete instruction program for field formation workforce and to identify opportunities for a better flow of information in support of tax administration functions. Training in</p>	MU
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Revised Components	Achievements/Outputs	Not achieved	IP Rating
	TAMS). New modules and refinement of functions are an ongoing process.	the use of ITMS is ongoing in the field formations. New SOP's are being introduced along with the training.	

4. Program Management and Implementation			
Change management, communications, outreach – internal and external	Based on a MU rating for the first 5 years of project implementation and an S rating on the last about 2 years.		MU
Surveys of taxpayers (companies and individuals) and publication/ dissemination of results	The activity was completed.		MS

Annex 2(D): Link between Original and Revised Components

Original Components	Revised Components
<p>1. Management and Institutional Development</p> <ul style="list-style-type: none"> i. Organization and Policy ii. Human Resource Development iii. Internal Audit iv. Internal Affairs and Vigilance Units v. Change Management <p>2. Improving Revenue Operations</p> <ul style="list-style-type: none"> i. Direct Tax ii. Sales Tax and Central Excise iii. Customs <p>3. Strengthening Revenue Services</p> <ul style="list-style-type: none"> i. Audit ii. Voluntary and Enforced Collection Appeals and Dispute Resolution iii. National Intelligence and Risk Management iv. Customs and Tax Frauds <p>4. Creating a Tax Compliant Culture</p> <ul style="list-style-type: none"> i. Taxpayer Education and Facilitation (communications, internet facilities, call centers) ii. Taxpayer Identification and Registration <p>5. Adopting Responsive IT Systems. (Note: This has been merged within the revised components).</p> <p>6. Infrastructure Up-gradation and Development (Note: This has been</p>	<p>1. Enforcement (including audit)</p> <ul style="list-style-type: none"> – Carrying out measures to ensure compliance with registration, filing and payment requirements <ul style="list-style-type: none"> i. Registration/e-registration ii. E-filing and e-payment – Implementation of the reformed GST /VAT – Extension of the automated refund system to other LTUs/RTOs for GST, Income Tax and proposed VAT / reformed GST – Carrying out of audits (post, targeted, composite and desk) including annual audit plans; third-party matching; risk-based prioritization of cases (e.g. audit, follow-up, compliance); detecting tax fraud – Carrying out of a workflow review and automation of the appeals/disputes process. – Collection of arrears (outstanding debt) – Carrying out of studies to determine the tax gap – Training staff on risk-based audits and skills update – Carrying out of measures for taxpayer facilitation and education on fulfillment of tax obligations. – Carrying out of business process review for the enforcement function.

<p>merged within the revised components).</p> <p>7. Program Management and Implementation</p>	<p>2. Organization and Management for Efficiency</p> <ul style="list-style-type: none"> - Implementation of organizational change management - Upgrading of human resource policies and management - Upgrading of infrastructure and adoption of responsive IT systems to improve efficiency - Diagnostic study and independent assessment of mid-term modernization requirements for Customs, including IT systems. <p>3. Information Technology</p> <ul style="list-style-type: none"> - Adopting responsive IT systems <p>4. Program Management and Implementation</p> <ul style="list-style-type: none"> - Change management, communications, outreach – internal and external - Surveys of taxpayers (companies and individuals) and publication/ dissemination of results - Incremental operating costs
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Annex 2(E): Activities Planned to be Financed by Components

Components and sub-components	Activities Planned
1. Management and Institutional Development:	
- Organization and Policy	Move from a tax-type to functional structure within FBR, consolidate field offices into 12 RTOs ⁵³ , strengthen planning, legal framework for taxation and tax capacity, and design and implementation of an integrity strategy for FBR.
- Human Resource Development	Workforce rationalization, new job descriptions, development of a human resource management policy framework, adoption of new pay and benefits regime, training, and development of a code of conduct and ethics.
- Internal Audit	Establish an internal audit unit.
- Internal Affairs and Vigilance Units	Establish an internal affairs and vigilance unit.
- Change Management	Explain rationale and potential impact of planned changes to all FBR staff, taxpayers and other stakeholders.
2. Improving Revenue Operations	
- Direct Tax	Improve the identification and registration process, create LTUs and 12 RTOs, establish a tax-payer self-assessment scheme, maintain a taxpayer database, establish capability to quickly detect taxpayer non-filing and non-payment, and finance development of supporting software systems.
- Sales Tax and Central Excise	Broaden tax base, review number of goods and services that are exempt to bring ST in line with international practice, and streamline ST refunds system through use of supporting software.
- Customs	Support long-term goal of modernizing import and export clearance procedures and related trade facilitation procedures to international standards, apply risk

⁵³ The functional program areas to be carried out at each of 12 future RTOs were: taxpayer facilitation, taxpayer audit, collection and enforcement, investigation of tax fraud/evasion, information processing, human resources, information technology, and legal (Source: PAD).

	management principles, and develop a system that enables electronic submission of declarations and assessments/release.
3. Strengthening Revenue Services	
- Audit	Support establishment of a tax audit function as a separate functional stream, develop automated approach to audit case selection based on risk management and audit parameters imbedded in the information management system.
- Voluntary and Enforced Collection Appeals and Dispute Resolution	Establish an effective collection and enforcement function at FBR head office together with a computer system and tax database that will facilitate collection of taxes; develop systems, procedures and processes to improve fairness and transparency in the resolution of appeals and disputes, initially through pilot efforts.
- National Intelligence and Risk Management	Create a national intelligence-gathering unit to support all operational areas, co-located with a risk-management function to provide similar support to field operations.
- Customs and Tax Frauds	Create an integrated tax and customs fraud function.
4. Creating a Tax Compliant Culture	
- Taxpayer Education and facilitation (communications, internet facilities, call centers)	Strengthen tax facilitation and education through a well coordinated communication program (internet and call centers) promoting greater compliance and a user friendly, supportive interface between FBR and taxpayers; introduce easy forms for electronic filing, and have an accurate taxpayer registration system for all tax purposes and taxpayers.
- Taxpayer Identification and Registration	
5. Adopting Responsive IT Systems	Formulate an IT strategy that will help transform FBR business processes from a highly manual to an automated environment, to improve management control and increase transparency of tax administration; strengthen data management, and create a central information depository system to provide easy online access to relevant acts, SROs, rules, etc.
6. Infrastructure Up-gradation and Development	Support office modernization through a comprehensive accommodation modernization plan in line with roll-out of the

	functional organization.
7. Program Management and Implementation	Establish a project management unit (PMU) for the overall coordination of project activities including M&E, disbursement, procurement and financial management.

Annex 3. Economic and Financial Analysis

Economic Analysis

The main economic benefits identified at project appraisal were: “(i) increase in government revenues as a result of a widening of the tax base in terms of more taxpayers and transactions coming into the tax net; (ii) improvement in customs procedures aim to reduce the average time to clear customs; (iii) improvement in voluntary tax compliance rates implying early revenue generation for the government; (iv) reduction in taxpayers’ costs associated with tax compliance; (v) economic-wide gains to the private sector as an increasing number of economic agents operate under the same set of rules and taxes; (vi) reduction in taxpayers’ costs associated with tax compliance; and, (vi) greater predictability of tax liability and lower costs of doing business for the private sector”. Acknowledging that not all economic benefits associated with tax administration performance are measurable, only economic benefits (i) to (iv) were estimated at appraisal. Assuming a set of assumptions in terms of macroeconomic and financial variables, the relevant economic rate of return (ERR) for the project was 119.7 %⁵⁴.

A re-estimation of the ERR at completion was carried out under different variables and assumptions; hence the results are not comparable. From the economic benefits identified at appraisal, the economic appraisal at completion dropped variables (i) to (iii) above on account of the following factors: (a) the flow of project’s benefits in terms of government revenues is not considered as an economic benefit since taxes and subsidies are usually removed from project’s appraisal from the economic point of view as they relate only to transfers between government and the private sector⁵⁵; (b) there is no way to link savings in terms of administrative costs to FBR as a result of changes in compliance rates; and, (c) the restructured project dropped the trade facilitation component related to customs administration.

Therefore, the estimation of the ERR at completion included only the reduction in taxpayers’ costs associated with tax compliance as the sole variable. Considering its major contribution towards this end, the economic benefits associated with savings for taxpayers using FBR’s e-filing capabilities deployed through TARP were estimated. For this purpose, the ERR estimation was carried out under the following key information and assumptions: (a) On average, taxpayers in Pakistan took 599 hours per year to pay taxes in 2007⁵⁶; (b) e-filing contributes, on average, savings of up to 15 percent of total taxpayers time⁵⁷; and (c) e-filers total population reached 366,159 to FY 2010/11; (d) opportunity costs associated with major tax filing in Pakistan, such as hiring of tax accountants, was estimated based in information from local sources. Based on this, the ERR associated with the project is estimated to be 624%.⁵⁸

⁵⁴ Variant 3 in PAD estimation.

⁵⁵ For a complete discussion on this topic see: Jenkins, G. and A.C. Harberger, 1992, *Manual: Cost Benefit Analysis of Investment Decisions*, Harvard Institute for International Development (HIID), Harvard University, 1992.

⁵⁶ Source: *Doing Business in Pakistan*, IFC and World Bank, 2010.

⁵⁷ Savings are expected to increase through time as taxpayers become more familiar and confident with e filing procedures.

⁵⁸ While there is not yet much empirical evidence on similar estimations, savings associated with the use of e-filing and e-payment are expected to be substantial according to the *Handbook for Tax Simplification*, Investment Climate Advisory Services, World Bank Group, 2009.

Financial Analysis

At appraisal, the estimation of project's financial analysis was carried out under the assumption that the underlining financial benefits would be expected from increased federal tax receipts. For this purpose, revenue collections were estimated through regression analysis by using the buoyancy coefficient of tax revenue with respect to GDP growth under different scenarios. Assuming a buoyancy coefficient of 1.2 and other macro variables projections (e.g. GDP growth, exchange rate, discount rate and inflation), a stream of financial benefits was estimated through the project life. The estimated project cost at appraisal was also used as input in the financial analysis. As a result of the financial analysis, the estimated financial rate of return (FRR) for the project at appraisal ranged from 302.3% to 522%, depending on the assumptions used under different scenarios.

The FRR at completion was not re-estimated considering that the assumptions used to estimate the financial rate of return of the project at appraisal seem unsustainable in hindsight for the following reasons:

(i) The very nature of tax administration reform projects makes it extremely difficult to quantify the change on revenue collection due to change in tax administration performance, so that it could be isolated from other variables affecting receipts, such as tax policy changes (e.g. reforms on GST, or income tax structure), and changing economic conditions on underlining variables affecting tax bases (e.g. nominal GDP growth, inflation, exchange rates). The association of total tax revenue to revenue administration performance could be assessed under stable economic conditions, different from the highly evolving economic conditions observed in Pakistan during the project's life.

(ii) The identification of financial benefits for project appraisal purposes in the case of on-going operations - such as FBR's - entails the need to identify the flow of marginal (rather than total) benefits and costs during project life. At appraisal, the flow of estimated total federal revenue collection for the upcoming five years was assumed as project's financial benefits, notwithstanding the fact that most of this flow would have been received by FBR anyway had the project not been implemented. The lack of use of alternative parameters to adequately gauge project's marginal benefits at the outset makes unviable the re-estimation of a comparable FRR at project's completion.

(iii) At appraisal, the buoyancy coefficient (defined as the ratio of change of federal tax revenue collection to change in GDP or other underlining macro variable) was used to estimate revenue collection, and hence project's financial benefits, through project life. However, for an adequate revenue forecasting exercise, the tax elasticity coefficient (same as buoyancy, except that tax revenue series is adjusted to eliminate the impact of discretionary policy reforms introduced through time) represents a more accurate tool of analysis. So even under the assumption of total identification of financial benefits to revenue collection, the replication of the FRR at completion using the tax buoyancy coefficient would have produced a rather distorted picture of project's outcomes from the financial point of view, especially considering the volatile economic conditions in Pakistan during the project life.

Lack of adequate data⁵⁹ at project's completion severely constrains the elaboration of an alternative financial analysis set out for traditional Bank's economic and financial evaluation. Nevertheless, an overview of FBR's tax collection, the expected impact of TARP's outcomes, and a discussion of GST productivity as a proxy of revenue administration performance is elaborated below (*Section 3.2 includes a summary of this analysis*).

Assessment of relevance and achievement of Project Development Outcomes

Low revenue mobilization stands out as one of the long and most pressing development challenges in Pakistan. This is the result of a combination of factors, such as inefficient tax administration, narrow and skewed tax structure, complex and obsolete legislation, non-transparent tax system, rent seeking behavior, and rampant tax evasion. As a consequence, the federal tax to GDP ratio has declined to 8.6 percent of GDP in 2010/11 from 9.3 percent of GDP a decade ago (Table 1), after a steady decline during the last few years. At current levels, the tax ratio is not only the lowest in Pakistan for the last 35 years, but also one of the lowest in the world.

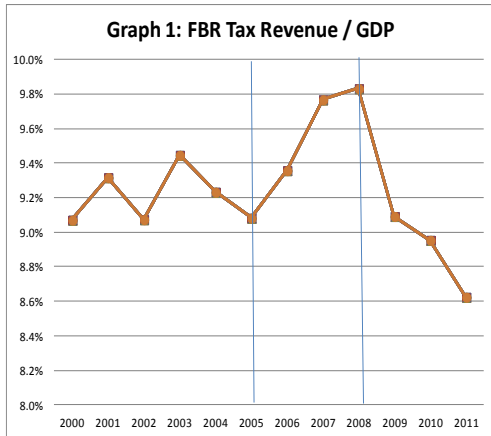
		2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
FBR Revenues	Rs Billions	392.3	404.1	460.6	520.8	590.4	713.4	847.2	1,007.2	1,157.0	1,328.6	1,558.0
	% real growth	4.7%	0.5%	9.2%	4.9%	5.9%	10.6%	10.2%	4.7%	-6.0%	2.2%	-1.4%
	as % of GDP	9.3%	9.1%	9.4%	9.2%	9.1%	9.4%	9.8%	9.8%	9.1%	9.0%	8.6%

Sources: FBR, National Bank of Pakistan and own calculations

Exceptionally weak domestic sources of revenue in Pakistan reduce fiscal space to increase allocation of public expenditure on key social and physical infrastructure required to meet the MDGs, promote growth and curb poverty levels. Also, the low and unstable source of revenues threatens macroeconomic stability, exposing Pakistan to higher levels of vulnerabilities during economic downturns. Finally, insufficient domestic revenue mobilization strains debt sustainability (debt to GDP ratio currently reaches 60 percent of GDP, one of the highest in the region), increases dependency on foreign aid and inflationary sources of revenue, and promotes crowding out of private sector investment through higher public deficits. As a result, revenue mobilization will continue to be a fundamental challenge to address fiscal constraints and core development objectives in the years to come.

The underlining development objective in terms of FBR tax-GDP ratio was not achieved, despite progress in key intermediate outputs and substantial investments in IT, physical and human infrastructure at FBR. Notwithstanding moderate gains during 2004/05 to 2008/09, FBR tax-GDP collection has dropped substantially to reach 8.6 percent of GDP by the end of FY 2010/11, the lowest level in more than two decades.

⁵⁹ Needed parameters not available at completion include, among others, estimation of tax gaps and a time series of the impact of discretionary changes introduced into tax legislation.



During the first half of the 2000s, FBR’s tax-GDP ratio followed a cyclical pattern within a narrow range of 9.1 to 9.4 percent of GDP (Graph 1). Despite sustained increases in economic growth, revenue collection from major taxes remained flat reflecting low tax effort. In fact, the tax buoyancy coefficient reached only 0.93 during this period, meaning that revenue collection increased at a lower rate compared to overall economic growth. However, after project implementation in 2005, two different and even opposite patterns in FBR tax-GDP ratio were observed: an expansion during 2005-08 and a steep decline in 2008-11

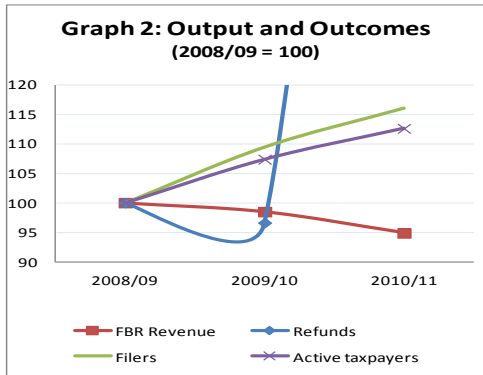
- **Period 2005-08: Economic boom, combined with slow implementation of TARP**

Overall economic performance maintained the expansionary trend started in 2001, mainly driven by external financial flows and loose monetary policy. As a result, FBR tax-GDP ratio increased at a sustained pace reaching 9.8 percent of GDP by 2007/08. Notwithstanding TARP’s effectiveness in early 2005, increased levels of tax collection are explained by modest improvements in income tax buoyancy, rather than enhanced operation efforts from FBR. Project implementation delays during the first years of TARP restricted the scope for any substantial improvement in tax administration efficiency.⁶⁰ In fact, the momentum for tax administration reform weakened during this economic expansion period, as modest increases in tax buoyancy reduced the urgency for fundamental changes in tax administration performance.

- **Period 2008-11: Economic crisis and natural disasters, combined with turnaround of TARP implementation**

The steep decline in tax-GDP ratio during this period is partly explained by the negative effect on economic activity by natural disasters, and an overall unfavorable external and domestic environment, including deteriorating security situation. Unparalleled devastation caused by two major floods during 2010-11 had a significant and long lasting effect on economic activity, further deteriorating eroded tax bases and tax compliance levels. On the other hand, the lack of a diversified export base and the need to import oil and food induced the economy to increased vulnerability during a period of high fluctuations in international commodity prices. Finally, an increasingly adverse political climate derailed the proposal to implement a new broad-based RGST – the cornerstone of the tax policy strategy to enhance revenue collection and support the tax administration reform program.

⁶⁰ According to a Quality Enhancement Review carried out in May 2008, despite an adequate design of project in terms of needs and activities, the results in terms of development objectives as well as on disbursements were perceived as weak.



The economic crisis in 2008 urged GoP to take immediate measures to increase tax revenues as part of a self-designed stabilization program, which was supported by the IMF through a Stand-By Arrangement. As a consequence, the reform program gained momentum and project implementation pace speeded up, allowing substantial investments in FBR's physical and ICT infrastructure and renewed efforts on technical assistance to implement FBR's action plan. As a result, FBR maintained progress against some key outcome indicators. Positive results by 2010/11 included: (i) registered and active taxpayers increased

by 6.2% from 2.984 million to 3.167 million; (ii) electronic return filers increased by 6% for sales tax, with income tax filers registering a 27% increase in FY10 (FY11 returns have yet to be filed⁶¹); (iii) registered and active taxpayers for Income Tax and Sales Tax (e-enrolled, liable to e-file) increased by 29% and 13%, respectively, and (iv) the amounts of refunds to taxpayers as well as the efficiency for processing refunds increased substantially as a result of efforts to clear the backlog of Sales Tax refunds pending for up to 10 years.

However, positive trends in some key outputs achieved during the final years of project implementation fell short of overcoming shrinking revenue performance (Graph 2). FBR's lower than expected overall performance by end of project life is associated with three major shortcomings:

(a) Slow integration of FBR organization along functional lines, because of resistance from staff of the Customs and Excise Group (CEG) and the Income Tax Group (ITG), lack of monitoring and evaluation mechanisms and an unstable tenure at mid-management levels undermining the efficiency and effectiveness of FBR to implement its reform action plan.

(b) Underutilization of IT-related systems due to poor integration of the new systems into re-engineered business processes, weak management follow up on implementation of systems, and opposition of FBR staff to adopt new business processes based on newly deployed systems at field formations; and

(c) Continued weakness of the audit function, associated with lower than expected performance by the audit program delivered by private accounting firms during the outsourcing program, lack of a centralized-based audit function in charge of planning, programming and monitoring of results, poor training, and unfavorable results for FBR on legal disputes from tax tribunals.

Break in the chain of reforms had consequences for the achievement of outcomes envisioned by the project. Without the reorganization of the FBR along functional lines, the redefinition of business processes was left in limbo. Without the implementation of new business processes, related IT investments were insufficiently incorporated into business routines. Without the new IT systems, training and change management investments were delayed. The shift from co-location of tax streams to actual functional integration of tax administration – along with the concomitant changes in business processes, IT systems and HR reforms – did not have consistent commitment and support from within the FBR. At root of the problems was a lack of consistent

⁶¹ Data from filing of income tax returns is not available until the first quarter of the following calendar year.

political commitment to the major reorganization of tax administration initially envisioned in the GoP's own strategy and supported by TARP (see Section 5.2).

Productivity assessment

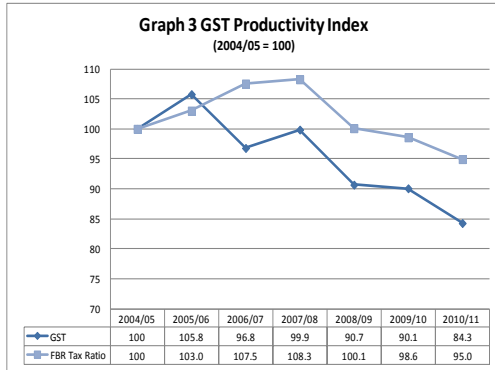
The GST productivity ratio represents a useful diagnostic tool to assess revenue efficiency and FBR performance during project's lifespan. Defined as the ratio of VAT revenues to GDP divided by the statutory rate, productivity ratio approximates the ability of the tax system to raise revenues by each percentage point of standard rate under a given policy and enforcement environment. Although the VAT productivity ratio is typically used in cross sectional analysis to assess VAT revenue performance worldwide, the construction of a time series for a given country also serves as a diagnostic tool to gauge tax administration performance through time, when controlled for tax policy changes.

In the case of Pakistan, the construction of a time series for the GST productivity ratio provides a useful insight of FBR's performance trends throughout the project's life. In general, VAT/GST productivity depends on two factors: (i) structural features of tax design, such as the scope of the base, exemption threshold and number of tax rates; and (ii) level of compliance enforced by tax administration efforts. By controlling the tax rate and the coverage of the tax base, GST productivity ratio gauges the extent to which FBR overall performs, considering the following factors:

- A. GST structure in Pakistan has not suffered major changes during project's life other than the general statutory rate, which is inherently controlled by the computation of the productivity ratio. Despite efforts to overhaul the indirect taxation structure by introducing a reformed GST featured with few exemptions and wide coverage of goods and services, the current narrow-based GST in Pakistan has remained almost entirely unchanged throughout 2005-2012 yielding rather low buoyancy gains (tax buoyancy coefficient of only 0.47). Therefore, lack of major policy changes allows the GST productivity index to isolate the pure FBR performance effort during the reform period.
- B. Different from other sources of tax revenue in Pakistan, administration of GST entails a full fledged operation of major FBR functionalities, including: registration, monthly tax return processing, collection, refunds, audit and enforcement. GST operation also integrates joint effort from both internal revenue administration and customs since GST import tax is collected at the borders and zero-rating is targeted for export operations, besides other activities. Hence, FBR's performance on GST administration represents a fair indicator to gauge its overall corporate effort during project's life.

To estimate GST performance for Pakistan, a time series was constructed using nominal GST collection, GDP and general GST tax rate. **As a result of this computation, GST productivity in Pakistan turns out to be only 23 percent, compared with an average ratio of 34 percent worldwide⁶².**

⁶² See "The Modern VAT", Ebrill, Keen, Bodin and Summers, International Monetary Fund, 2001. In the case of Pakistan, a one percent of GST standard rate is associated with a collection of only about 0.23 percent of GDP in Pakistan, while the rest of the world raises an average of 0.34 percent of GDP.



In terms of GST productivity used as a proxy for FBR performance, the estimation covering the project life reflects an overall decreasing trend during 2005/06 – 2010/11 suggesting feeble tax administration efforts throughout the reform period. Considering 2004/05 as the base year, a GST productivity index was constructed and compared with FBR’s tax-GDP ratio behavior during the same period to infer the extent to which tax administration performance is associated with low tax ratio (Graph 3).

Overall, FBR’s tax-GDP ratio and GST productivity index followed a similar pattern throughout reform implementation, signaling declining performance in both tax policy and administration. Nevertheless during the economic boom period (2005-08) GST productivity index showed a rather declining trend despite modest buoyancy gains in FBR revenue collection, signaling relatively poor tax administration performance amidst relatively favorable overall economic conditions. This trend supports earlier assumptions described above related to low urgency for tax administration reform perceived by GoP/FBR during the economic boom period. Slow implementation of TARP during this period, especially related to IT deployment and functional integration, isolates any association between tax administration performance and project implementation during this period.

During the economic crisis period and subsequent years (2008-11), GST productivity index declined at a higher rate compared to FBR tax-GDP despite a swift turnaround in project implementation and concomitant positive trends in some outputs by the last two years of project life (see section above). Arguably, major external shocks experienced by the Pakistani economy during this period with disrupting effects on economic activity - such as the major floods during 2010/11 - further undermined weak compliance levels in Pakistan⁶³ beyond FBR capabilities to mitigate its effects. Nevertheless, lackluster results in reform implementation described in the precedent section, especially those related to short term actions aimed at curbing evasion through more effective enforcement actions by the final year of project implementation, strongly suggests a weak FBR performance from 2008 onwards, far from the project’s objectives envisioned at the outset.

⁶³ Economic downturns typically expose tax administrations to emerging challenges due to expected decline of tax file turnaround, increased accumulation of arrears stock, lower payment of withholding taxes, and increase in net operating losses.

Annex 4(A). Bank Lending and Implementation Support/Supervision Processes

(a) Task Team members

Names	Title	Unit	Responsibility/ Specialty
Lending			
Mudassir Khan	TTL at Appraisal	SASFP	
Michael Engelschalk	Sr. Private Sector Development Specialist (Tax expert)	CICTI	
William V. Mayville	Consultant/HR & Training	SASGP	
Arturo A. Jacobs	Consultant/Tax expert	SASFP	
Zubair Khan	Tax Economist		
Erik Puskar	Consultant/ Tax IT Systems	CICTI	
Haseeb Ahmed	Consultant/IT Systems	SASFP	
Michel Zarnowiecki	Consultant/Customs expert	ECSP1	
Amer Durrani	Sr. Transport Specialist	SASDT	
Asya Akhlaque	Senior Economist (PSD & Trade)	AFTFE	
Zia Al Jalaly	Senior Social Development Specialist	SARDE	
Asif Ali	Senior Procurement Specialist	SARPS	
Martyn Gordon Ambury	Consultant	SASEP	
Anwar Ali Bhatti	Financial Analyst	SACPK	
Michael Engelschalk	Sr. Private Sector Development Specialist	CICTI	
Carlos D. C. Ferreira	Consultant	ECSPE	
Shabana Khawar	Senior Investment Officer	CMEPI	
Riaz Mahmood	FM Analyst	SARFM	
Amir Munir	Senior Business Partnership Officer	ISGOS	
Akhtar Hamid	Lead Counsel	N/A	
Ali Awais	Legal	N/A	
Chau-Ching Shen	Sr. Finance Officer	CTRLN	
Hasan Saqib	Sr. FM Specialist	SARFM	
Rubina Geizla Quamber	Program Assistant	SASHD	
Kadija Jama	Program Assistant	ENVCF	
Supervision/ICR			
Daniel Alvarez Estrada	Senior Public Sector Specialist/Task Team Leader	SASGP	
Mohammed Taqi Sharif	Consultant/Operations Specialist	SASGP	
William V. Mayville	Consultant/Member ICR Team	SASGP	
Carlos Silvani	Consultant/Tax expert/TA team head	SASGP	
Paulo dos Santos	Consultant/Tax expert/Member TA	SASGP	

	team		
Wyatt Grant	Consultant/IT expert/Member TA team	SASGP	
Orlando Reos	Consultant/HR specialist/Member TA team	SASGP	
C. Janyna Rhor	Sr. Procurement Specialist	SARPS	
Khalid Bin Anjum	Procurement Specialist	SARPS	
Rehan Hyder	Sr. Procurement Specialist	SARPS	
S. Waseem Abbas Kazmi	Financial Management Specialist	SARFM	
Saeeda Sabah Rashid	Sr. FM Specialist	SARFM	
Javaid Afzal	Sr. Environment Specialist	SASDI	
Mohammad Omar Khalid	Consultant	SASDI	
Amitabha Mukherjee	Lead Public Sector Specialist	ECSP4	
Mudassir Khan	Task Team Leader, SASFP	N/A	
Erik Puskar	Consultant/ Tax IT Systems	CICTI	
Shamsuddin Ahmad	Sr. Financial Sector Specialist (former TTL)	SASFP	
Esperanza Lasagabaster	Service Line Manager (former TTL)	FIEEI	
Anjum Ahmad	Senior Energy Specialist	SASDE	
Haseeb Ahmed	Consultant	SASFP	
Asya Akhlaque	Senior Economist	AFTFE	
Zia Al Jalaly	Senior Social Development Spec	SARDE	
Asif Ali	Senior Procurement Specialist	SARPS	
Martyn Gordon Ambury	Consultant	SASEP	
Anwar Ali Bhatti	Financial Analyst	SACPK	
Michael Engelschalk	Senior Private Sector Development	CICTI	
Carlos D. C. Ferreira	Consultant	ECSPE	
Arturo A. Jacobs	Consultant	SASFP	
Shabana Khawar	Senior Investment Officer	CMEPI	
Amir Munir	Senior Business Partnership Officer	ISGOS	
Michel Zarnowiecki	Consultant/Customs expert	ECSP1	
Kaspar Richter	Senior Economist	ECSP2	
Furqan Ahmad Saleem	Sr. Financial Management Specialist	AFTFM	
Hasan Saqib	Sr Financial Management Specialist	SARFM	
Imtiaz Ahmad Sheikh	Program Assistant	SASFP	
Shafqat M. Mirza	Program Assistant	SASEP	
Shabnam Naz	Program Assistant	SASEP	

(b) Staff Time and Cost

Stage of Project Cycle	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
Lending:		
FY02	3.89	2.82
FY03	11.62	64.36
FY04	25.17	235.45
FY05	10.16	34.47
FY06		0.00
FY07		0.00
FY08		0.00
Total:	50.84	337.10
Supervision/ICR:		
FY02		0.00
FY03		0.04
FY04		0.00
FY05	9.83	29.07
FY06	29.61	245.51
FY07	36.33	143.83
FY08	46.24	127.25
FY09	42.90	158.98
FY10	70.99	453.45
FY11	45.46	240.88
FY12	21.39	121.16 ¹
Total:	302.75	1,520.17

^{1/} As of March 31, 2012

**Annex 4(B)– List of Key FBR Officials under TARP
(as of April 30, 2012)**

No.	Designation/Name	Tenure	Remarks
	Chairman/Acting Chairman		
1	Mr. Mumtaz Haider Rizvi	Feb. 13, 2012 – to date	Acting Chairman/Member Customs
2	Mr. Mehmood Alam (Member SP&S)	Jan. 25 – Feb. 13, 2012	Transferred
3	Mr. Salman Siddique	Dec. 24, 2010 – Jan. 21, 2012	Retired
4	Mr. Sohail Ahmad	May 18, 2009 – Dec. 24, 2010	Transferred
5	Mr. Ahmad Waqar	July 23, 2008 – May 18, 2009	Retired
6	Mr. M. Abdullah Yusuf	March 12, 2004 – July 23, 2008	Retired
	Member (SP&S)/TP&R*		
1	Mrs. Azra Mujtaba	Feb. 17, 2012 – to date	
2	Mr. Mehmood Alam	Jan. 27, 2011 – Feb. 13, 2012	Transferred
3	Mr. Abrar Ahmad Khan	Sept. 6, 2010 – Jan. 26, 2011	Retired
4	Mr. Zafar-ul-Majeed	June 27, 2009 – Aug. 1, 2009	Retired
5	Mr. Afzal Naubahar Kayani*	Aug. 1, 2008 – June 26, 2009	Transferred
6	Mr. Habib Fakharuddin*	Feb. 23, 2007 – July 31, 2008	End of contract
7	Mr. Khwaja Tanvir Ahmad*	May 15, 2005 – Jan. 26, 2007	Transferred
8	Mr. M.S. Lal*	July 31, 2001 – May 12, 2005	Resigned
	Member (Inland Revenue)/Direct Taxes*		
1	Mr. Shahid Hussain Asad	Sept. 9, 2011 – to date	
2	Mr. Khawar Khurshid Butt	Feb. 2 – Sept 9, 2011	Transferred
3	Mr. Asrar Raouf*	Aug. 26, 2009 – Feb. 1, 2011	Transferred
4	Mr. Khalid Aziz Banth*	June 30 – Aug. 26, 2008	Transferred
5	Mr. Irfan Nadeem Sayeed	July 29, 2008 – June 20, 2009	Transferred
6	Mr. Usman Khalid Mirza*	Aug. 30, 2007 – July 29, 2008	Transferred
No.	Designation/Name	Tenure	Remarks
7	Mr. Salman Nabi*	June 24, 2004 – Aug. 30, 2007	Transferred

	Project Director, TARP		
1	Mr. Muhammad Saleem	Oct. 15, 2011 – to date	
2	Dr. Amna Saeed Khalifa	April 28 – Oct. 15, 2011	Resigned
3	Mr. Abrar Ahmad Khan*	Sept. 6, 2010 - Apr. 27, 2011	Retired/end of Contract
4	Mr. Zafar-ul-Majeed*	June 27, 2009 – Aug. 1, 2010	Retired
5	Mr. Afzal Naubahar Kayani*	Aug. 1, 2008 – June 26, 2009	Transferred
6	Mr. Habib Fakhruddin*	Feb. 23, 2007 – July 31, 2008	End of contract
7	Mr. Khwaja Tanvir Ahmad*	May 15, 2005 – Jan. 26, 2007	Transferred
8	Mr. M.S. Lal*	July 31, 2001- May 12, 2005	Resigned

Note: Project Directors marked with an asterisk (*) were at Member level.

Annex 4(C): List of Bank Task Team Leaders (TTLs) and co-TTLs

No.	Name of TTL	Name of Co-TTL	Period
1	Mudassir Khan, SASFP	N/A	July 2003 – Sept. 2005 ^{1/}
2	Ms. Esperanza Lagabaster, SASFP	Ms. Shabana Khawar	Oct. 2005 – Sept. 2006
		Anjum Ahmad	Sept. 2006 – April 2007
3	Shamsuddin Ahmad, SASFP	Anjum Ahmad	May 2007/ mid-March 2010
4	Daniel Alvarez Estrada, ^{2/} SASGP	N/A	Mid-March 2010 – to date

^{1/} Based on the PCD review meeting held in August 2003.

^{2/} Messrs. Shamsuddin Ahmad and Daniel Alvarez Estrada overlapped during the period December 2009 to mid-March 2010. Mr. Alvarez Estrada was tasked with the responsibility of preparing TARP's Restructuring Paper from November 2009.

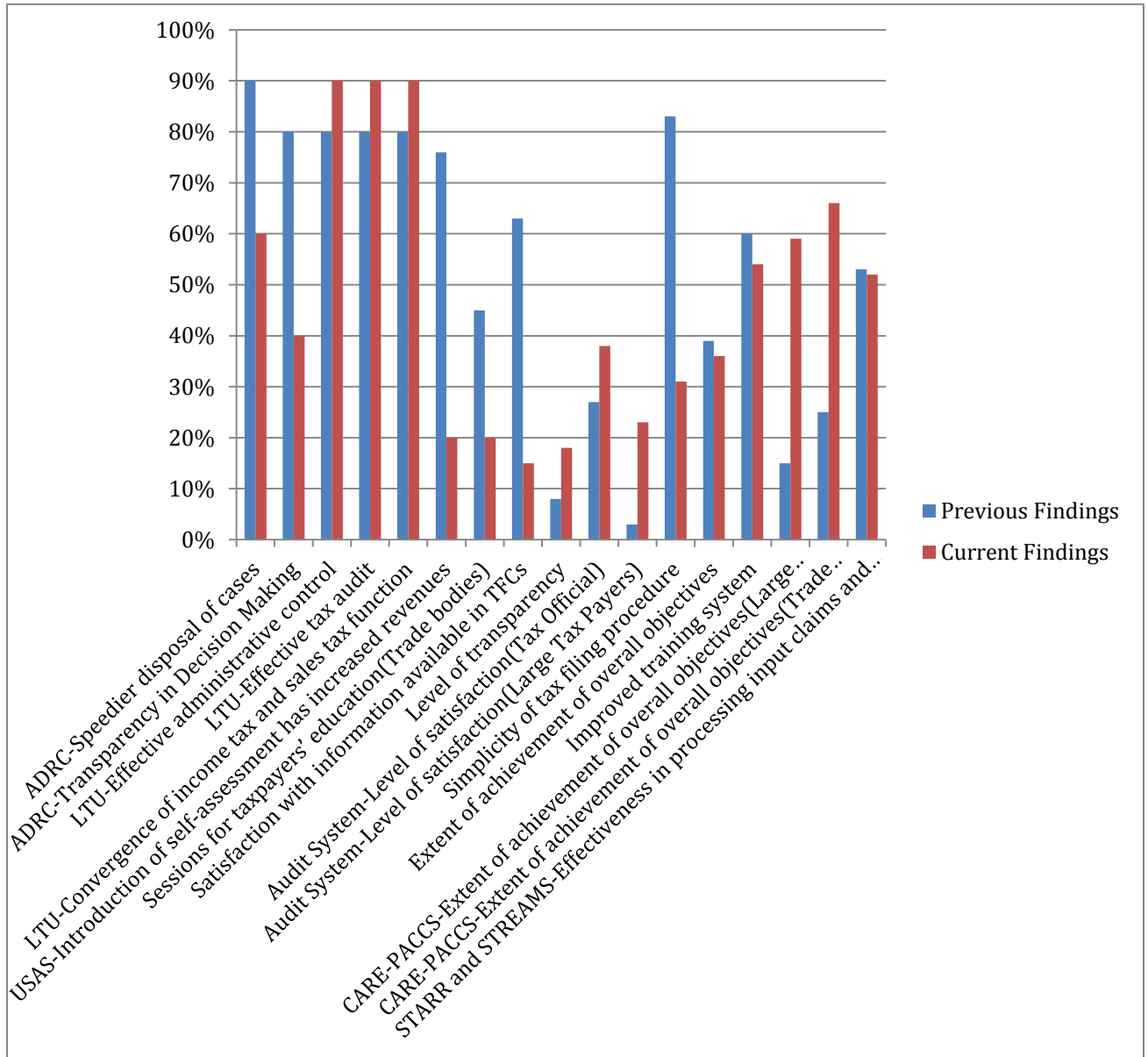
Annex 5. Beneficiary Survey Results⁶⁴ (Summary)

In order to monitor the Tax Administration Reform Program (TARP), stakeholders' perception periodic survey was an integral part of the reform initiatives. The first round of a country wide stakeholders' perception survey was conducted in the year 2007. FBR contracted M/S BearingPoint for second round of perception survey in 2011. BearingPoint carried out a nationally representative survey of the stakeholders to determine the degree of improvements between the two surveys. Following is a brief summary and a graph of the survey findings:

- i. Overall, awareness level of TARP initiatives among stakeholders has been low. However, it is on higher side for large taxpayers and legal experts.
- ii. Overall user ratings (scale 1-5); FBR Employees and Large Tax Payers assigned above 3.0, while the user rating given by all other stakeholders is 2.64.
- iii. Focusing on the aspect of whether FBR supports taxpayers who want to do the right things, the trend indicates that majority is in agreement.
- iv. The perception about transparency in FBR has also improved, as the current results indicate significant increase in high level of transparency in comparison to previous study.
- v. Higher level of transparency is observed by the legal experts, large tax payers and agents/intermediaries in FBR. However, individuals, small businesses and opinion makers perceive low level of transparency.
- vi. There are more positive responses concerning understanding about functions of FBR and awareness of certain rights related to the tax system.
- vii. Tax filing procedures have become more complex for the stakeholders.
- viii. According to the satisfaction levels of all stakeholders, the overall automation initiatives of FBR are regarded as being moderately satisfactory.
- ix. The FBR website has been rated higher than other automation initiatives.
- x. Overall, a significant majority of stakeholders feel that e.FBR has facilitated tax payers to a large extent.
- xi. Alternate Dispute Resolution (ADR) negative trend has been observed from the previous study.
- xii. Stakeholders are very positive about the objectives of Tax Administration Reform Project (TARP) for facilitating the Large Taxpayers and almost all the aspects of LTUs.
- xiii. Majority of respondents share the view that the Expedious Refund System has achieved its target of quicker refund claim processing to a large extent.
- xiv. Most of the stakeholders perceive that RTO/Model Customs Collectorate (MCC) officials are performing their duties to a large extent, however opinion of trade bodies indicate a lower level of performance.
- xv. Tax audit is an important component of TARP. Improvement in the tax audit system has been observed by large tax payers, tax authorities and trade bodies in most of the aspects during the past few years. This positive perception, however, is not shared by small and medium businesses.

⁶⁴ Source: FBR-Stakeholders Perception Survey (TARP), BearingPoint, December 29, 2011

xvi. Significant increase in positive perception has been observed in large tax payers about the overall objectives of the CARE-PACCS (Customs project).



Annex 6. Stakeholder Workshop Report and Results

Not Applicable (N/A)

Annex 7. Summary of Borrower's PCR and/or Comments on Draft ICR

Summary of Borrower's PCR

Ground work for tax reforms in FBR occurred between 1999-2000. First detailed report, commonly known as Shahid Hussain Report, was produced on April 14, 2001. Pilots were run from 2002 – 2004. Thus, extensive work was done prior to launching main TARP from January 2005. Despite a pre-project preparation spread over five years, overall implementation performance remained just 'moderately satisfactory'. This has necessitated identifying the lessons learned in this process, which include both successes and failures. The risk classification for TARP was 'substantial risk' and it has fully met that classification. Suggested mitigation measures were largely unsuccessful in reducing the risk of the project. The Bank performance was highly productive in the start, but with the passage of time the Bank supervision became weaker. The performance of the Bank's team after TARP restructuring in 2010 was highly satisfactory.

Lessons learned have been classified under broad categories for convenience of consultation.

Ownership

1. Reform can only succeed with strong ownership and commitment. Importance of ownership, change management and incremental reforms in public sector institutional modernization need to be kept alive and consistent. At the time of start of the project in January 2005, there was a vibrant ownership of the project which with the passage of time weakened due to multiple variables. Momentum for tax administration reform could not be maintained during the economic 'boom' years as increases in tax collections compromised the urgency for maintaining tempo in tax reforms. By 2007, the project had landed into problem area.
2. Continuity in the leadership of the tax agency provides an important contribution to successful implementation of the reform process. During TARP implementation command at Chairman FBR level was changed four (4) times. During seven years' project life, seven (7) Project Directors had to step in and out.
3. Concerned wings of FBR rarely remained proactive in reform processes; therefore, this lacked ownership under a misconception that the same was a job of TARP Wing. Whereas, the reforms were primarily their area for achieving results. TARP wing was just an implementing arm. In future there is a need to create a small and smart forum like reforms monitoring Steering Committee with representation of the concerned Wings.
4. Integration of different IT systems is a process, which involves a multitude of stakeholders. It is important to involve these stakeholders actively in the design, monitoring and active management of the reform process. There has to be an overall supervisory body to control the scattered development and introduction of different IT systems. This has to be constant feature for ensuring ownership and success of reforms.
5. A lesson has been learned that complete caution should be exercised while identifying the activities to be included in the project. In TARP, off the shelf procurement of IT systems for Customs, ITMS and HRIS were among major activities. After launching the project, lot of efforts and resources were spent for acquisition of these systems but after wastage of more than two years this had to be scrapped. Hence, for any related project an in-depth review/study may be required.

6. In revised PC-I, major consultancy activities like Organization and Management, Compliance Management, Adopting Responsive IT System, TARP Implementation could not be initiated because the concerned wings regretted to take their ownership. It was experienced during project implementation that concerned Wings of the Board were reluctant to go for availing any consultancy service. Technical Assistance (Consultancies) is the only major area under TARP where utilization remained extremely on lower side. In PC-I an amount of Rs.629.9 million was earmarked which was equivalent to US\$ 8.188 million. Against this allocation, total utilization at the end of the project was Rs.142 million only equivalent to US\$ 2.728 million. In percentage terms, utilization in Pak rupees was just 22.5%. For any future program, lessons already learned may be kept in view to ensure the ownership of the activity.

Human Resource (HR)

7. Any change that affects field workers and the way they do their job has the potential to be disruptive. There has to be a plan to ensure that all the staff is at least informed and understands as to what changes are being made and there is a mechanism to address the concerns of rank and seniority. There should be an ongoing monitoring mechanism to ensure buy-in or to find a way to address perceived set-backs in the transition. Corrective actions need senior management participation and a contingency plan should be in place if any resistance comes to the notice.

Requirement of Pragmatic Approach

8. At one point of time, it was decided to go for a completely new VAT Law. Lot of efforts and resources were spent for this purpose but ultimately it could not succeed. A new service group was created in haste which delayed project implementation process. There was a need for in-depth analysis of the related issues. In both these cases, stakeholders were required to be taken on board to address the risk involved in the decisions. Workable mitigating measures were to be put in place.

Design

9. Project design is the basic building block for entire structure. For successful completion of any project and to achieve the desired objectives, project identification/preparation plays an important role and contribute a lot. This requires extra efforts at the time of identification and preparation of the project and its components. At this stage, all stakeholders should be taken on board for ensuring ownership of the activity.
10. Design of the TARP project with an original cost estimate of US\$ 149 million to be implemented in five years time span vis-à-vis capacity of the implementing agency was over ambitious. Consequently, in pursuance of review of the implementation progress in 2008, an amount of US\$ 49 million was determined to be surrendered to the World Bank. At the end, another US\$ 7 million plus will be surrendered. This needs to be taken care of for any identical project.

Business Process Re-engineering (BPR)

11. Business process re-engineering and related automated applications must be fully integrated throughout the tax administration with appropriate management of the organizational transition including human resource and training aspects as central part of the process.

Information Technology (IT)

12. Information Technology is the backbone of all the processes in reformed structure. Entire structure of functional distribution of work is to be based on formidable ITMS. Efforts for the purpose lacked direction. IT systems including ITMS and TAMS, etc. have been introduced. New IT systems are ineffective unless they are complemented with new operating procedures and continued strength. Changing old ways of doing business requires that the staff understands what is being changed and why in addition to being trained in the procedures. Any new introduction of IT system should be through the development and implementation of new SOPs for the purpose.
13. During implementation, especially at the initial stage, FBR faced certain difficulties in IT related procurement especially for ITMS and HRIS. In this process, more than two years were lost. So it is always important to adopt the right path to achieve the desired objective. All IT procurements are complex in nature which needs to be planned with caution. These procurements are always time consuming.
14. Moving to an e-Tax system is an essential process for reducing the compliance and administrative burden and the risk of corruption. Increasing the use of electronic tools, in particularly e-filing, by taxpayers therefore is important. This requires in addition to providing incentives for e-filing to eliminate obstacles and create a workable platform for use of e-tax.
15. Different IT systems developed by the FBR's field formations required integration. There was no integration management in place which could have catered for alignment of the components.
16. IT procurements and particularly procurement of software systems are highly complex in nature. ICT Hardware was procured which required focus on 'sizing' and 'hardware optimization'. These activities were not dove tailed in a logical manner resulting in impediments to project execution within the procurement portfolio.

Project Management Unit (PMU)

17. TARP typically consisted of new project designed towards the achievement of common PDOs. It had all the enumerators of a complex program and therefore required, in totality, a well trained and focused management team to cover the entire ambit of the program. There were unnecessary interruptions The Bank has commended the Project Management Unit (PMU) for having made extra ordinary efforts since restructuring in September, 2010 to put in place robust business processes and infrastructure related to enforcement, IT, organization and HR, laying down the foundation for future reforms. It is pertinent to highlight that before restructuring (w.e.f 14.9.2010) TARP was only able to spend Rs.2.8 billion only in six (6) years, whereas after restructuring and during around one year, Rs.2.7 billion have been spent on procurement of works, goods, training and technical assistance. Thus, at expenditure front, around 50% of the entire progress was achieved during ending year of the project. Entire grant amount was exhausted. Savings have mostly occurred on account of depreciation in rupee value vis-à-vis dollar and ensuring efficiency gains and transparency in procurements. A great lesson was learned that once there is strong commitment, then unprecedented result become achievable.

18. In recent two years, highly useful lesson was learned that in case there is uniformity in approach between PMU/FBR and its counterpart team in the Bank then there can be wonderful results. Both the teams had a strong intention to deliver and all delaying slip shots were addressed with focus, speed and success. Response from the Bank's side was marvelously quick and productive. Procurements starting from preparation of bidding documents, invitation for bids, evaluations, award of contracts and complete implementation and management thereof within 7 – 8 months was par excellent. Once TARP (PMU) was working day in and day out then performance was overly visible. Organization is the ultimate beneficiary.
19. Despite unprecedented performance of TARP (PMU) during recent two years, its previous performance has also suffered due to multiple vulnerabilities within the given environment. PMU was constituted even prior to launch of TARP in January 2005 which was operating under a Member as Project Director (PD) reporting direct to the Chairman. PMU was required, as given in the Project Appraisal Document (PAD) to hire full time outside consultants to assist in implementation of the respective project components. In pursuance of advice given in PAD, consultants from private sector were hired as Procurement Specialist, Director (PMU) and Advisor on Finance, etc. Almost all of them failed to deliver except one Director PMU. Persons hired from private sector have competing priorities. Whenever, they got better alternate options from any other source then they simply opt to move out. In this case, ownership assumption in the project fades away. During TARP implementation, it was also experienced that some of them were found interested in perpetuating their own stay rather than expediting the project work. Consequently, contracts of two Financial Advisors were not renewed. Contract of one Director (PMU) had to be terminated. This cost a lot to the project.
20. TARP involved procurement of works, goods and services. PMU with required level of competence, dedication and capacity to handle the gigantic task was required to be put in place right at the outset of the project. Before start of implementation, a well trained team of officials particularly for procurement, financial management and project monitoring and evaluation had to be put in place. The lesson learned is that instead of relying on hiring from private sector, competent officials may be identified from within the organization who should extensively be trained and posted in PMU.
21. During the execution of project PMU faced multiple administrative problems that badly affected the project progress. These included frequent transfer of PDs (7 PDs changed hands), frequent changes in the PMU team, capacity building and training issues, lack of interest/involvement of major stake holders and end users, delay in completion of works and timely availability of funds, etc. Persons posted in PMU should be kept there for entire life of the project. This should be known to the concerned officials, who should be asked to opt for it so that there is no disruption during implementation phase.
22. Proper job description should be prepared for persons involved in procurements, monitoring & evaluation. In TARP (PMU) this was lacking.
23. SOPs / Manuals should be prepared prior to introduction of the project. Persons working in PMU should fully be aware of the procedures and processes for doing the related job. This was not done for TARP (PMU).

24. During project implementation it was required to appoint Project Directors (PDs) at respective site scattered throughout the country. However, comprehensive training for PDs was not imparted to equip them as to what they were supposed to do. They were almost unaware of required monitoring and evaluation mechanism. Therefore, before posting of any PD for undertaking implementation of any sub-activity, his/her training should be ensured before expecting productive feedback/output.
25. Transparency, strict adherence to the rules, quick complaint redressal mechanism and meeting the deadlines are the great lessons learned during project implementation which may be replicated for future projects. In such a voluminous work not a serious single complaint was lodged against tendering thereof.
26. An integral part of the PMU responsibilities was to establish `monitoring and evaluation` mechanism for the project. It had to establish performance indicators as explained in the Project Implementation Plan (PIP) to monitor impact of the project and measure its success. There was no effective monitoring & evaluation (M&E) framework based upon MIS for the project, so management could not get the real time progress of scores of projects spread throughout the country and was also unable to make mid-course corrections where required.

Policy assumptions should be carefully evaluated

27. It should be ensured that policy assumptions worked out at the time of preparation of project are well documented and that effective mitigation strategies are in place to identify when one of these assumptions is proven incorrect. Suggested corrective actions may be used to provide some guidance on how to minimize the impact of the change in the project's environment.
28. The project expected that as taxpayers became more compliant due to the changes in FBR as a result of TARP, revenue would increase. However, the complexity of the tax system imposes severe restrictions on tax administration, which are a major obstacle to improve its effectiveness, e.g. the existence of widespread exemptions and zero rates in the ST complicates its administration. Tax policy reforms are indispensable to increase tax administration effectiveness and tax revenue.

Training

29. Major component of the project was procurement of hardware/software; it went fairly well and proved to be a success story in the entire project portfolio. Nevertheless, soft side of the project which was a corner stone for building the individual's capacities remained at a slower pace which was accelerated in 2009-10. Capacity Building Projects involve enhancement in capacity of institution, individuals through trainings, restructuring of organizations and business process re-engineering, hence, the capacity of FBR as revenue collecting agency remained deficient, and resultantly FBR relied much on presumptive taxation to make up the revenue losses, which created distortion in distribution of economic gains in the country.

Consultant (infrastructure)

30. Services of M/s NESPAK were hired through QCBS procurement methodology. This organization has scattered set ups located in Islamabad, Lahore and Karachi. Its Electrical Division is based in Lahore and IT Division in Karachi. NESPAK was also a Project Manager for FBR's infrastructure related activities. At times, bidding documents prepared by NESPAK were found deficient in specifications, incorrect determination of Bill of Quantities

(BOQs), etc. It could not even address construction related requirements of the concerned local governments/municipalities. Timelines could not be followed. It's monitoring & evaluation mechanism was not based on sound techniques covering design model, tracking tables and work breakdown structures (WBS), etc. Many delays had occurred due to faulty feedback/preparation of NESPAK. Thus, working experience with NESPAK was not a success story.

31. In case of any major project like TARP, instead of hiring services of external consultants like NESPAK for preparation of design layouts, procurement support and supervision of works at sites, organization should evaluate the possibility to engage their own engineers (civil/electrical), architect and quantity surveyors for the said jobs.
32. The decision to separate Public Works Department (PWD) from TARP refurbishment and construction activities was found to be a success. This helped to complete the projects smoothly and within the given timelines.

Contract Management

33. Before award of contracts for construction works/renovations, supply of goods and services, real ground checks regarding the capacity of the contractors/suppliers should also be evaluated. In theory or on paper, profile of prospective suppliers/contractors may be attractive but market feedback from previous clients should be obtained. Lessons were learned that some of the successful evaluated bidders were not able to abide by their commitments for contract executions.
34. Vendors who depend upon their financing sources through their head offices based in Middle East faced serious constraints. Release of required financing was delayed unnecessarily, which made the local vendors unable to pay for even small activities. During contract implementation, this results into avoidable complications. Effective strings are required to be attached for this type of vendors/suppliers.
35. Performance Security should be 10% for entire warranty period and that should not be reduced to 2.5% after operationalization. Some vendors simply tend to forego 2.5% Performance Security rather than abiding by 3 years warranty. In any case, for foreign vendors warranty threshold should not be less than 10%.
36. Instead of planning complex procurements in one go, it would be advisable to breakdown these procurements into smaller chunks. Proper sequencing is advisable.
37. Default penalty for delays, etc. was normally prescribed to the extent of 10%. In order to force the vendors/contractors to complete the project within the given timelines penalty threshold may be fixed at 20% of the contract value.

Bidders Qualifications

Interior Development & Construction Works:

38. Tender documents are required to be prepared with complete clarity. Bid data, contract data sheet are required to be drafted with complete care and caution to avoid subsequent mis-

interpretations and litigations. Likewise, each special condition of contract given in the tender document needs to be drafted with complete clarity.

39. In certain construction and refurbishment projects the qualifying firm, which emerged as the lowest evaluated responsive bidder, could not deliver the project on time. A deeper analysis into the problem revealed that the firm had submitted satisfactory statistics information in terms of its past experience while qualifying technically but had subsequently/simultaneously involved in so many other projects that its cash flow went under pressure and stuck-up in other project(s). Hence, TARP activity badly suffered in terms of physical progress as adequate funds were not available with the firm for executing its activities on the Critical Path Method (CPM). This created difficult situation when TARP was nearing its closure and contract cancellation was not a viable option. Even available penal provisions were not helpful in resolving the issue. Bidding Documents prepared by NESPAK did not contain the Financial Capability Analysis Clause, which could have calculated the current financial strength of the firm, thereby alerting the Client of its weak financial position in terms of project execution.
40. The Client Risk Tolerance in terms of financial variation in project cost should have been incorporated at the very outset in the bidding documents through Special Conditions of Contract. This Risk Tolerance typically prohibits the client to allow project scope creep and relating expenses to go beyond a certain percentage. In some construction and interior development activities, the contract was awarded to the lowest evaluated responsive bidder at a project cost which escalated more than 50% of the original cost. The lowest evaluated bidder won the contract but as he could not complete the project within the evaluated bid price, he resorted to cost variation claims, which if added originally, would have qualified the second or third lowest bidder. This may sometimes create transparency issues for the client. The Client therefore needs to establish a maximum and minimum threshold of Risk Tolerance in terms of contract price beyond which either the contract is not awarded or the contractor is not paid the variation in the activity closing phase.

Supply of Goods:

41. L/C Clauses for supply of goods should have been clearly spelt-out in bid data sheet for both the foreign and local suppliers. Absence of standard INCOTERM terminology for each category of supplier and its relation to the buyer resulted in audit objections which wasted lot of time and efforts for settlement thereof.

IT Goods Acquisition

42. Certain IT firms submitted bids which, *prima facie*, at the time of bid opening looked as lowest bidders and their products duly conformed to the specifications but their bids contained avoidable infirmities which rendered them non-responsive during bid evaluation process. These infirmities occurred due to incorrect filling of various bid forms in the tender documents by inexperienced managers who could not understand the sensitivity attached to it. Project would have benefited from better prices, had the firms been educated. Presence of IT Bid Managers should be made mandatory in the Pre-Bid Conference and it should be made part of evaluation process by assigning specified marks to it.

Project Financing

43. During execution of Project and especially during negotiations for extension from 5 to 7 years, DFID stopped its financing through freezing its accounts. DFID was financing three (3) important components of TARP, namely; procurement of ICT hardware/software, training and technical assistance (consultancies). Due to this stoppage, no process relating to procurement for these activities could be started and consequently around a year was lost. Hence, need for timely availability of financing is highly important. In order to address this situation mitigating measures are required to be put in place.
44. It was experienced during implementation of the project that required PSDP allocation for the year was not timely available. Besides this, timely release of counterpart financing also suffered delays. Consequently, project activities suffered. For any smooth implementation, timely PSDP allocation and release will render great help to the project.

Legal constraints

45. Tax administration reform frequently requires changes in the legal framework. These changes must be initiated as early as possible in order to ensure a clear and sufficient legal basis for the reform. It is important to know ahead of time what constraints are in the law that would affect the anticipated changes.

Technical Assistance (TA) - Consultancy Services:

46. The Expression of Interest (EOIs) submitted by the consulting firms generally do not furnish necessary data required for their preliminary evaluation leading to their short-listing. The firms had to be contacted time and again to provide the missing information. This resulted into undue delay. Furthermore, the firms used to give requisite information in a jumbled-up manner. The consulting firms should have been given the short-listing templates and evaluation benchmarks by providing them in the Request For Expression of Interest (REoI). Earlier this has not been included in the REoI approved by the World Bank.
47. The Request For Proposal (RFP) should have contained a clause showing contract price with and without taxes. The contract price exclusive of taxes should be used for evaluation and the contract price inclusive of taxes should be got approved from the Contract Award Recommendation Committee (CARC). This would result in payment of consultancy fee which the consultant originally envisaged for his services. Absence of this feature resulted in bickering by both the local and foreign consultants when the consultancy fee indicated by them in their RFP was taxed.
48. Quality & Cost Based Selection (QCBS) does not allow dissemination of information about the cost estimates of the activity. Indication of base price should have been a regular feature in the Pre-Proposal Conference with the approval of the World Bank. Many consultancy activities either had to be re-tendered or dropped altogether in the wake of exorbitant prices offered by the consultants. This wasted valuable resources in terms of project time and effort consumed in evaluating their proposals.

Assessment of Bank's Performance:

49. The Bank performance was highly productive in the start, but with the passage of time the Bank supervision became weaker. The performance of the Bank's team after TARP restructuring in 2010 was highly satisfactory.

Comments on Draft ICR

Quality at entry:

50. Draft report has highlighted policy indecision on an IT modernization strategy (See first bullet of para 15). Two issues have been clubbed and focused, (a) out-sourcing of customs automation as a Public Private Partnership activity and resultant taking out of US\$ 28 million which were intended to be disbursement on this count; and, (b) non-agreement of internal IT group to acquire-off-the-shelf integrated solution vs in-house development of an Integrated Tax Management System (ITMS) which led to a delay of more than two years. This needs elaboration to see it in proper context. Instead of policy indecision, there were other factors which cannot be overlooked. In the project design, a decision was already there to go for off-the-shelf integrated ITMS, therefore, no new decision was needed. In order to have a strengthened and working application of this solution, a team of FBR officials, on the suggestions of the World Bank, had visited identified developing as well as developed countries to see the actual implementation and operations of ITMS over there. Initially, in pursuance of clearance of the Bank, procurement of ITMS under single stage bidding methodology was undertaken which could not succeed. In view of this outcome, the Bank advised to go for two stage bidding process. After completion of the related processes under two stage bidding methodology, RFPs were received which were found deficient on two counts; (i) the proposed solution/product did not serve ITMS purpose of the organization; and, (ii) financial quotes were in excess of the available envelope for the purpose. This process right from single stage bidding to arrive at end of two stage bidding had taken around two and half years but without a success. Per force, organization was left with no option but to go for an alternate venture for in-house development through PRAL which could perhaps provide required flexibility and convenience for getting the required solution. Besides this, it will be more appropriate to say that IT procurement being complex in nature demanded proper expertise and capacity to do it which remained lacking both in the implementing agency as well as in the Bank during the relevant time period. Just to pin down 'indecision' may not be a true reflection of factual position.

Identification of risk factors and mitigation measures:

51. The project was implemented in seven (7) years. Most of the time, implementation environment was difficult. Risk factors were said to be identified at project design stage along with mitigating measures (See paras 16 & 17). For success of any project, risk factors and mitigating measures are required to be continuously updated even risk register may be required to be updated on daily or weekly basis. During the implementation, new risks crop up which are required to be addressed through adequate mitigating measures. In case of TARP, this did not happen. New risk factors were neither properly identified nor adequate mitigating measures were worked out and triggered, therefore, this resulted into avoidable wastage of time, resources and energies. This remained one of the major infirmities in this project.

52. Draft report has talked about stiff resistance from vested interest groups against restructuring as well as reforms (See para 18). Instead of saying resistance from executive and staff, it will be more appropriate to say that they were less receptive to go for accelerated reforms. Here, two issues may be seen separately, (i) creation of a new service group and (ii) adaption to reforms. Legal and administrative problems had occurred after creation of a new service group. The staff which had gone into litigation had clearly and unequivocally stated at each forum that they were not against reforms in the organization rather they were seeking protection of their rights/privileges as well as legitimate expectations for career progression. Other than this, there was hardly any evidence where FBR staff was strongly resisting reforms. This needed to be appreciated in a context where there was aging manpower (more than 80%) with hardly any previous exposure to reforms / computerization and automations, etc., whose automated outcome was slashing of discretionary powers/authority. Since 1994, all recruitments in the organization are banned, therefore, no fresh blood (excluding intake at BS-17 level where an annual batch of officials ranging 30 – 50) enters in service after qualifying through national competitive examination/selection process with latest IT/management related education is available. TARP reforms were designed and targeted for a manpower of around 12 – 13 thousands against a working strength of 25 thousands. In the national context, it is highly difficult to bring down the level of manpower by around a 50% which has a direct relationship with creation of unemployment rather than providing jobs. Politically, this hardly remained a viable option. In the reform process, no effective mechanism could be adopted to address this volatile issue. In such an environment to go for robust reforms will always be difficult. An effective ownership of the program was not only required to be created rather that had to be kept alive.

Monitoring and Evaluation (M&E):

53. Creation and putting in place of a dynamic monitoring and evaluation (M&E) system was required right from day one (See para 20). This remained lacking on the part of the implementing agency but at the same time this could not be effectively highlighted and focused on the part of the Bank as well. Had there been an effective M&E mechanism in place right from the start, then many deviations from the original implementation plan could have been avoided. This unit had to keep the project on track while monitoring the implementation plan and introduction of corrective measure as and when those were required.

Bank's supervision technical and operational skills mix:

54. It has been highlighted in the report that supervision/TA missions identified proper implementation bottlenecks and provided detailed action plans in Aide Memoires/ Technical Reports to address them (See para 43). It has also been pointed out that during most of project life, the quality of Bank's supervision suffered on account of lack of coordination between the TA team and the task team. It may not be proper to doubt the technical knowledge and expertise of the TA team members but perhaps some of them were not fully conversant with the local operational, legal, economic and political environment, therefore, their technical advices could not yield the desired results rather at times those were found counter-productive. Following can be quoted as examples:-

55. An agreement was signed between the World Bank and FBR on Tax Administration Reforms on July 10, 2009 (see Appendix I – Follow up on Tax Administration Reform July 2009). This agreement vide para 8 prescribed certain timelines for creation of new occupational group with necessary changes in laws and rules, etc. It was required under this agreement

that Revenue Division will move the Establishment Division to prepare a proposal for the creation of two new occupational groups. The staff had to be given a two week period to decide whether to be transferred to a new occupational group. As cited, agreement was signed on July 10 and all related actions were mandated to be completed by September 30, 2009. This timeline was followed and the outcomes of these decisions have elaborately been highlighted in ICR at paras 14, 18, 19, 36, 37 and 51. Before going for a major structural decision for creation of a new occupational group, it was required to undertake detailed discussions with all stakeholders to address their perceptions or concerns about new arrangement. GOP had introduced occupation groups in 1973 and to make any structural change within 15 days and that too without addressing concerns of the concerned, its outcome could well be imagined. This decision had far reaching implications for the staff who had put in decades of service. In country like Pakistan, there is a different culture attached to permanence in job and any change in already laid down terms and conditions or withdrawal thereof is prone to be counter-productive. At the moment, scores of litigation are pending at different forums filed both by Customs and IR officials relating to different service matters. Customs has ended up with surplus officers. Presently, total sanctioned cadre strength of Pakistan Customs from BS-17 - 22 is 379 and against this, working strength is 472. This situation is leading to a kind of stalemate in the promotion prospects and de-motivated workforce which is not only counter-productive rather contrary and detrimental to reforms with inherent potential disruptions. This shows the level of over-crowding and administrative problems for the organization. FBR management is doing its best to address these administrative issues but there are hardly any short cuts and workable quick solutions.

56. Customs reforms were integral part of this project. There was no customs expert in TA team. An amount of US\$ 28 million was earmarked for IT side of customs reforms. In 2007, FBR had floated an idea of doing customs reforms on Public Private Partnership (PPP) basis instead of planned under the project. This was the time where a forceful, correct and productive advice was required for the organization from customs expert in TA whether PPP was workable or not. There was no mention of any best practice in the world where customs was being run on PPP basis. The TA team simply agreed to the proposal/decision of FBR and reported in the Aide Memoire of Mid Term Review: August 20 – September 13, 2007 that in view of the PPP approach being adopted by CBR (now FBR) for Computerized Customs System, the funds earmarked should be surrendered by CBR. This deviation from the strategic objectives resulted in non-realization of reform objectives envisaged for Customs. Due to lack of focus on customs reforms, not only the strategic objectives were not achieved, the workforce of customs suffered badly because of lack of focus on their HR issues. Now, it has been proved that FBR's PPP approach for customs was not a viable venture which ended in void. The benefit from the available financial resources could not be availed which were surrendered to the Bank and simultaneously lot of precious time was wasted. Practically, reforms in customs have fallen back by many years.
57. TARP was a 'program' under 'program and project management' definition. Different activities under this program had to be done under project management methodology. TA team members, though experts in their own fields, were not well versed with the requirements of program and project management. Whenever, new proposals / advices were rendered which had important structural impacts, were not based upon program and project management methodologies. For example, when it was advised to go for creation of a new service group, then the underlying risk factors were not identified and likewise required mitigating measures were neither identified nor put in place. Almost same was the case when customs reforms were agreed to be run on PPP basis. Procurement of certain training related sub-activities were also delayed in absence of clarity during discussions of TA members with

the concerned officials of the Board. It will always be useful if procurement expert remains part of the discussions which involve any types of procurement being discussed with the TA team.

58. TA team had advised to go for complete redrafted VAT law, though, other proposals were also offered during discussions. Lot of resources and energies were invested. A new redrafted law was submitted before the Parliament but that could not be approved. The TA team vide 'Follow up on Tax Administration Reform – October, 2009' had suggested an alternate option for approval of set of legal instruments, that instead of sending the package of legal reforms to Parliament which may subject it to changes with undesirable consequences an 'Ordinance' may be submitted for President's signatures and enforcement. This advice was negatively flashed by the local media. Title of one such press clipping on referred to suggestion of the TA team is quoted, "Bypass Parliament, World Bank advises Government of Pakistan". This type of approach made the job of FBR/GOP more difficult for getting the law approved by the competent forum/authority.
59. At certain times, TA team adopted top-down approach while rendering advice on different issues which when subsequently came up for implementation then those were not found doable. In reform related activities, where no policy decision is required, then bottom-up approach through discussions and agreements with the concerned functionaries will be more meaningful and result oriented (See para 3.2 of PCR).

Government's performance:

60. Government's performance rating has been determined in the report as 'unsatisfactory' and rationale for this finding is explained at paras 45 – 47. Government's commitment to Tax Policy Reforms could not bring intended results due to multiple vulnerabilities. There were changes at top leadership level but most of these changes had resulted due to retirement of the officials after completing the prescribed tenure of service. During this time period there were four Chairman FBR. Three of them had retired after completion of their service tenure i.e. 60 years. Besides this, out of eight PDs, four had again either retired or contract duration had ended. After promulgation of FBR Act 2007, CCFR was replaced with the Board-in-Council consisting of Members of FBR. Thus, meeting of CCFR after constitution of Board-in-Council was not required. Chairman FBR has regularly been convening meetings of the Board-in-Council to take important decisions. In the draft report, it has been highlighted that GOP had committed for increase in tax revenue through introduction of broad based value added tax (VAT) or reformed general sales tax (RGST), etc. but the GOP was unable to secure political consensus on the passage of the proposed VAT or RGST bill by the TARP closing date. Concerted efforts rendered by the GOP for introduction of VAT/RGST are needed to be acknowledged which is missing in the report. Lot of efforts were invested for drafting of VAT/RGST law. An international conference was convened in Islamabad in 2009, and later on, two workshops were convened in Dubai, UAE where international experts in the field had also participated for assistance in drafting the law. After doing lot of work, draft law, after clearance by the Ministry of Law, was submitted before the Parliament for consideration and approval. Here again, numerous meetings were held at Parliamentary Committees level where GOP officials appeared and made all out efforts to convince the parliamentarians for approving it. Despite all these sincere efforts stretched over many months, the Parliament did not approve the law. To say, the Government was unable to secure political consensus for approval of the law may not be a fair comment. Government is subservient to the Parliament and if any law, in its wisdom is not approvable then the Government cannot be blamed for this happening because sovereign decision of the people's

representatives has to be respected by all, including the Government. With this explanation, rating of the Government performance needs to be upgraded to 'moderately satisfactory' rather than 'moderately unsatisfactory'.

Implementing agency's performance:

61. In the report, implementing agency's performance has been rated as 'moderately unsatisfactory'. Justification for this rating has been summarized at paras 48 – 49. Both positive as well as negative outcomes have been focused. It has been highlighted that positive outcomes include completion of several physical and IT infrastructure related sub-projects at several locations across Pakistan, etc. This is to be highlighted that not several rather all procurement related activities consisting of ICT hardware/software, refurbishment of existing infrastructure, construction of Transit Accommodations were completed with exception of only two activities; (i) TFC Guru Mandir –litigation issue, and (ii) FBR Call Center. Hence, there could be no better performance than this one. FBR recognizes that certain suggestions of the Bank could not be implemented as per given timelines but most of the recommendations were followed and implemented. Position relating to indecision on IT strategy as discussed in para 49 has already been discussed in these comments. Instead of indecision, there were certain factors which were beyond the control of both FBR and the World Bank and ultimately it had to be reconciled with the situation. It was not in the domain of the FBR to provide security of tenure to the leadership because as explained at preceding paras, if an official had attained the age limit prescribed for retirement then that had to be followed. This has happened in many cases. There were many policy related decisions which had to be taken by the Government and FBR could only provide its input. Example includes the creation of consensus with the Provincial Governments for levy of VAT/ Sales Tax on Services after passage of 18th Constitutional Amendment. FBR's efforts were there but at times those could not yield the intended results due to inherent limitations. While taking into account overall level of efforts made by the implementing agency for undertaking these reforms in an environment which was saddled with many vulnerabilities, the rating should not be less than 'satisfactory'.

Lessons learned:

62. Lessons learned during implementation of TARP have been summarized at para 51 of the report. FBR had also identified lessons learned during implementation of this program which are shown at Annex-7 to the draft ICR. Another lesson has also been learned during this process that composition of the TA team is very important. A TA team having complete professional competence, receptive in approach, accommodative to workable views and with a problem solving approach can be more productive and supportive to the project. In the TA team for TARP, professional competence of IT expert was par excellent, likewise, there was no doubt about the competence of the HRM expert. Other experts of TA team who had to address VAT/RGST drafting and implementation, etc., or making changes /amendments in rules/regulations or administrative laws were required to be fully aware of the local dynamics. For complete success of a program/project, it will be more appropriate that before making selection of a TA team member his/her extensive knowledge of that country/environment is evaluated objectively. An example can be cited from the TARP procurement scenario where problem solving approach was overly visible. There were difficult and complex procurements. Most of the procurement processes were started during 2005 – 2009 but could not succeed due to multiple reasons. There were delays both on the part of the implementing agency as well as delays in response from the Bank's side. After TARP restructuring, both the teams i.e. TARP (PMU) and the Bank's TTL team sat together

and devised a strategy for a way forward. Both the teams landed on the same page and remained there till completion of the job. Bank's TTL team was found to be highly receptive, accommodative to any workable and convincing proposal and the TARP (PMU) team has always been addressing the observations /suggestions made from the Bank's side. There were lot of meetings, face to face discussions as well as extensive telephonic discussions on the issues and both the teams agreed to implementable methodologies. All types of differences were sorted out in productive manners. The end result was that all procurements enlisted in TARP PC-I were completed in totality with exception of only two. To say the least, problem solving approach and clarity in objectives while staying on the same page gave the dividend.

63. In Annex 2(B) Intermediate Outcome Indicators, under the "Project Outcomes" heading it has been stated that 5,000 mid level officers were to be trained annually. As against this 2,150 were trained so the target was not achieved. This statement needs correction. A total of 2,200 officers were trained in 2011 under different training activities undertaken through procurement and 494 officers were sent on short courses abroad on regularly offered courses in universities/institutions abroad. Thus, a total of 2,694 officers were trained. Further the number of officers to be trained was reduced after consultation with the Bank, with the purpose of substantial improvement in focus on technical and IT areas and to avoid disrupting revenue collection efforts.
64. In the same annexure under Organization and Management for Efficiency it has been mentioned regarding upgrading of human resource policies and management under the column "not achieved" that implementation of several aspects of policy paper is still incomplete and some components have not evolved as desired. The spade work at level of HRM in all areas of HRM policy has been done and solid proposals and concept papers with complete working have been submitted for final approvals of the competent authorities so nothing is pending at HRM Wing's end.
65. In Annex-2(B), it has been shown against the output 'Action Plan to strengthen the appeals function implement' that no information was available by end of the Project. The Legal Wing of the Board has explained that at the 1st Appellate Stage, time period to decide the appeal is 120 days. However, in most of the cases, these appeals are decided within 60 days. Reasonable time has been provided in the statutes to facilitate taxpayers and to improve fairness and transparency in the resolution of appeals.
66. In Annex 2(D), it has been pointed out against the original component 'strengthening revenue services – voluntary and enforce collection appeals and dispute resolution to carry out workflow review and automation of the appeals/dispute processes. The Legal Wing of the Board has explained the related position that at present, at 1st appellate stage Appeal Management and Processing System is in place and operational and similar kind of system needs to be implemented at the stage of both the Appellate Tribunals of Inland Revenue and Customs to enhance the collaboration and better representation of appeal cases.

Annex 8. Comments of Cofinanciers and Other Partners/Stakeholders

Summary of DFID's PCR:

TARP has made significant progress in some areas, but the nature of shortcomings limit the effectiveness to achieve final outcomes. Major achievements include the reorganization of the Federal Bureau of Revenues (FBR) into an integrated functional organization, the reactivation of tax audits based on a risk-management system, improvement in enforcement and the Integrated Tax Management System (ITMS) developed by FBR and PRAL which is now available to field formations.

Project's implementation shortcomings have a common characteristic: the continuation of discretionary procedures at FBR. Delays in the rolling out of the ITMS, staff training on its use, reorganization at zonal level which weakens monitoring of the audit at the field level, contributed to the continuation of traditional methods for tax assessment, collection, audit and enforcement. In retrospect, it seems the donors were the most enthusiastic supporters of TARP although the benefits are clearly of national nature. It is understandable that the implementation of a reform where accountability is poor and there is no culture to pay taxes, there would be resistance to make tax administration more efficient and effective.

A key question for DFID is whether it should have been prepared to walk away. This is a difficult call. The enabling environment for this project deteriorated in its last two years as the political and macroeconomic context evolved. And yet, much of the progress achieved by TARP occurred during the last two years after project extension. This underscores the importance of DFID maintaining a thorough understanding of the political context when engaging in institutional reform projects like TARP. The analysis should be regularly updated as the project progresses, and DFID should stay actively engaged in maintaining its investments, tracking progress, and maintaining a policy dialogue on issues affecting implementation.

DFID's contributions to developing FBR's IT systems have been critical. The effectiveness of the development and availability of ITMS throughout FBR has been reduced by delays in the training of staff to use the system pending validation from the Core Business Domain Team (CBDT) and PRAL. The effectiveness of the development and availability of ITMS throughout FBR has been reduced by delays in the training of staff, with the result that field formations are using informal mechanisms to learn the new system. Although the use of IT is pivotal to many components of TARP, the use of ITMS is still not universal in FBR seven years into the reforms. The reluctance to fully operationalize ITMS could also reflect the unfamiliarity of senior management with the IT system.

Potential benefits could include higher government revenues for years to come which, if well targeted, could support poverty eradication programs many times over through multiplier effects. But while all the key building blocks are in place, shortcomings in implementation, which still leave scope for discretion, mean these benefits are not yet secured. The value for money of DFID's contribution may prove to be substantial if the outstanding steps are completed swiftly by the government, but this remains in doubt. Renewed support to tax administration reform would help maintain momentum to complete the remaining components, especially as internal resistance continues and the government's attention is distracted by impending elections. Donors should stay engaged in this crucial policy area.

DFID largely tracked TARP through World Bank missions, and its engagement with FBR was limited in between. Management of TARP also changed hands within DFID several times during

the last few years of the programme, reducing the quality and consistency of DFID's oversight and leaving DFID a little over-reliant on the World Bank policy analysis. Given the ambition of the programme, and the challenging context, a more active policy engagement from DFID may have been helpful, particularly as the World Bank was unable to deliver an Islamabad-based staffer to manage TARP. However, this would have an investment of significant more DFID staff time, impacting other work areas.

Further donor support is likely to be critical to completing the parts which are institutionally and politically most difficult and where resistance is still tangible. Time is of the essence; the reform efforts will come to naught if the remaining essential components are not completed soon. Already major reversals have taken place; without further donor support (training or technical assistance) the whole process can be setback fatally.

The main benefits of TARP so far are not the hardware but the gradual built-up of momentum for change. If support for the TARP does not continue, the non-tangible benefits will not take long to evaporate. The lack of government focus on this vital reform, vital not just for better governance, but for revenues to stabilize the economy, reduce inflation, and finance a large development agenda, makes a strong case for donors to continue support for an important neglected reform.

Annex 9. List of Supporting Documents

Preparation documents

Project Concept Document and meeting minutes
Preparation mission aide memoire
PAD (November 5, 2004), appraisal meeting minutes, Appraisal mission aide memoire
Development Credit Agreement
Pakistan Country Assistance/Partnership Strategy

Supervision documents

All aide memoires and ISRs
Mid term review aide memoire
Project Implementation Plan
Procurement Plans and Bank evaluations of post-procurement reviews
FM review documents, including copies of TARP's audit reports
TA team's quarterly mission reports (starting with Sept. 2008)
Progress Reports against FBR's Action Plan
Restructuring mission aide memoire (May 2010)
Main Restructuring Paper dated August 19, 2010
Amendment of DCA after Project Restructuring, including cancellation of IBRD and IDA funds, reallocation, and extension of Closing Date
Second Restructuring Paper (December 2011) and related amendment of DCA

Special reports

“Pakistan's Tax Gap: Estimates by Tax Calculation and Methodology” - prepared jointly by the World Bank, the Pakistan Federal Board of Revenue, and Georgia State University, July 2008 (Robina Ather Ahmed & Mark Rider).
Bank Management Response to the Request for Inspection Panel Review of the Islamic Republic of Pakistan Tax Administration Reform Project (IBRD Loan No. 72640-PAK: IDA Credit No. 4007-PAK), February 19, 2010.
“Revenue Analysis and Forecasting Sectoral and Tax-Gap Analyses.” Ather Maqsood Ahmed in collaboration with Robina A, Ahmed and Ashfaque H. Khan - Pakistan Federal Board of Revenue, USAID, and CSF Tax Assistance Program, May-November 2011.
Federal Board of Revenue Stakeholders Perception Survey (BearingPoint), Dec.29, 2011
FBR Automation Review by CEO, PRAL – April 9, 2012

Evaluations

“Second Structural Adjustment Credit for the Islamic Republic of Pakistan”, Implementation Completion Report (ICR), The World Bank, June 23, 2003.

“Poverty Reduction Support Credit for the Islamic Republic of Pakistan”,
Simplified Implementation Completion Report (ICR), The World Bank, June 20,
2005.

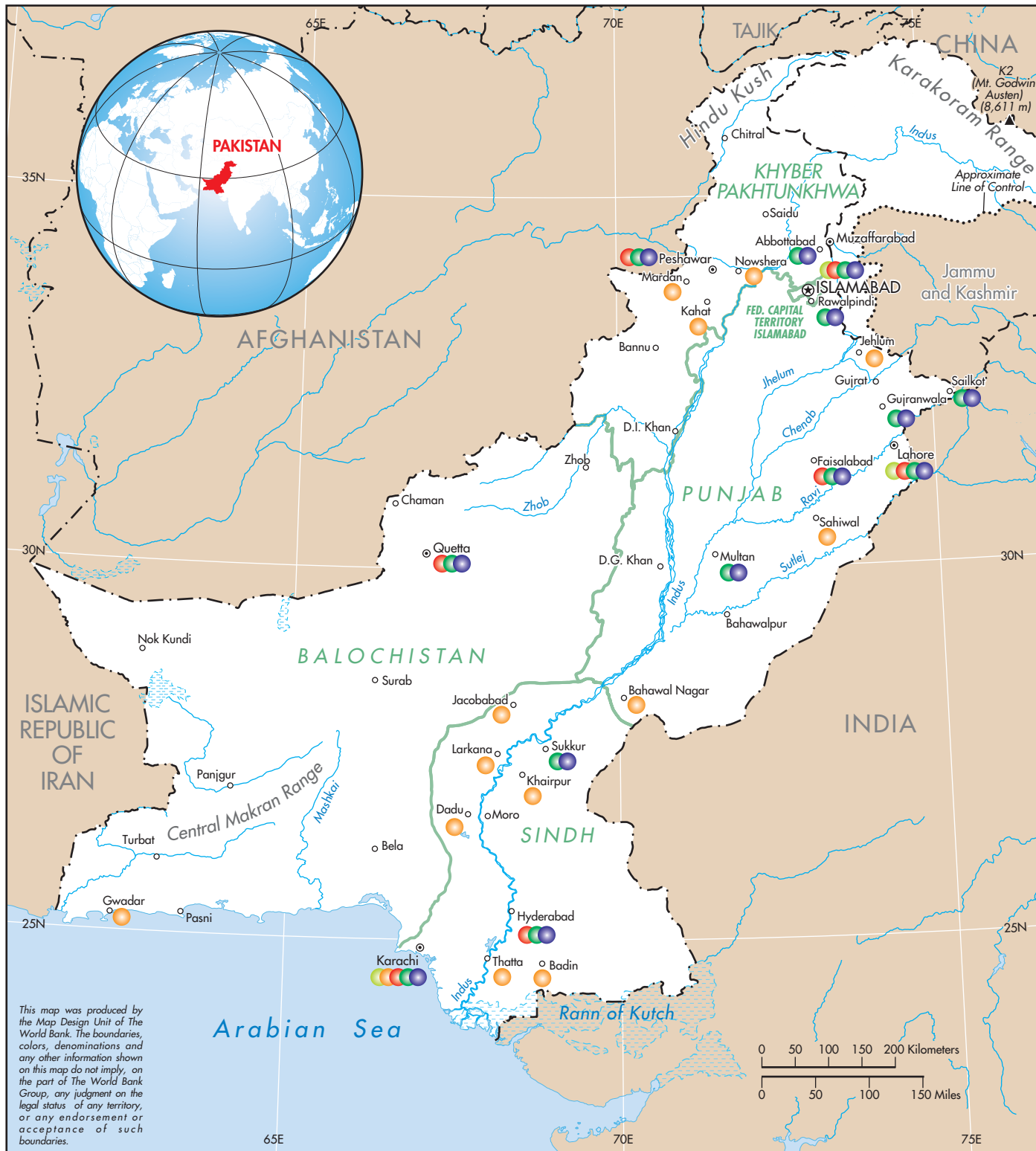
Quality Enhancement Review: TARP IT Delays, CITE, 2007

DFID: TARP – Project Completion Report (January 31, 2012)

Government of Pakistan - Revenue Division/FBR – Project Completion Report
(PCR) on Tax Administration Reform Project (2005 – 2011) – March 2012
(updated June 22, 2012).

PAKISTAN TAX ADMINISTRATION REFORM PROJECT

- FBR OFFICES:**
- TAs
 - RTOs
 - MCCs
 - TFCs
 - LTUs
 - CITIES AND TOWNS
 - PROVINCE CAPITALS
 - ⊗ NATIONAL CAPITAL
 - RIVERS
 - PROVINCE BOUNDARIES
 - - - INTERNATIONAL BOUNDARIES



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