TAXATION AND GOOD GOVERNANCE:
THE CASE OF VALUE-ADDED TAX IN BANGLADESH

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Thesis submitted in fulfilment of the requirements for the Degree of Doctor of Philosophy

Department of Politics and Public Policy, School of Social and Policy Studies, Flinders University, Australia, June 2013
Dedicated to

My Father—(Late) A.B. Muslehuddin Ahmed whom I lost when I was two years old and yet whose ethereal presence has always been a source of guidance and

My Mother—(Late) Hazera Khatoon whose indomitable spirits shaped me to become what I am.
PAPERS DRAWN FROM THE THESIS

The following papers have been drawn from the thesis:

International VAT Monitor 23(5):316-321

International Journal of Public Administration 36(6): 381-396

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Inspired by the new fiscal sociological approach which sees taxation as binding a contract between the state and its citizens and engaging the latter in a revenue bargain, this study explores the extent a tax system works as a tool for good governance in a social milieu characterized both by a poor state of governance and poor tax to GDP ratio. This is one of the first empirical studies of VAT from an interdisciplinary approach with special focus on a political science perspective. The context is Bangladesh which adopted a sophisticated modern consumption tax – VAT- in 1991 to maximize internal resources by broadening the tax base and simplifying the tax structure.

In contrast to the traditional role of revenue which has dominated the tax literature until the 1980s, the role of taxation in state-building has captured the attention of political scientists who consider taxation as a political process through which citizens can demand more accountability and responsiveness from the state. Stemming from this premise good governance, taxation and development become interdependent. Participation, transparency and accountability improve mutual trust between taxpayers and the government, and ensure better control and enforcement by the tax authority. The combined impact of these two aspects contributes to more and better voluntary tax compliance. Maximization of tax revenue is enhanced by the degree of voluntary tax compliance, which, in turn, contributes to development. This relationship is dynamic rather than linear as development generally ensures improved governance. This thesis attempts to contribute to that understanding.

Based on this conceptual framework, this qualitative case study research has employed a variety of research methods such as interview and focus group discussion and questionnaire survey involving 214 respondents representing the different segments of stakeholders. The quantitative method of survey questionnaire for a number of respondents has been used to triangulate the qualitative data.

The present study argues that the poor tax-to GDP ratio in Bangladesh, generally attributed to administrative inefficiencies and a narrow tax base, in fact reflects the
poor state of good governance. Although the introduction of the VAT by replacing the excise system in 1991 was mainly prompted by the desire to maximize revenue, the tax reform to introduce a self-assessed tax was also partly inspired by the urgency of making the tax system more transparent, more accountable and more participatory. But while the design features, drawing heavily on the excise system and deviating from the best international practice, undermine the fundamental features of self-assessment, transparency and accountability, many of the practices are also not favourable to the promotion of good governance values. Though more efficient, more transparent, more accountable and more participatory than the tax it replaced, the Bangladesh VAT has been able to utilize only a modicum of its huge potential in promoting good governance.

The contribution of the thesis to the literature lies not only in empirically exploring and evaluating a tax system from a new perspective, but also in identifying policy implications for making the VAT more effective and efficient in Bangladesh. These implications are equally relevant to other developing countries with a similar socio-economic milieu in making their tax system more effective in terms of social contract and revenue bargain through which people can demand more accountability and responsiveness from their governments.
DECLARATION

I certify that this thesis does not incorporate without acknowledgment any material previously submitted for a degree or diploma in any university; and that to the best of my knowledge and belief it does not contain any material previously published or written by another person except where due reference is made in the text.

Signature:

(Ahmed Munirus Saleheen)
ACKNOWLEDGMENTS

Although a PhD journey is generally a lonely one with a great many vicissitudes, the thesis would not have been completed without enormous support from a number of people and institutions. In doing this research my supervisors - Dr. Noore Alam Siddiquee and Dr. Craig Matheson, have been sources of unflagging support and inspiration. Their comments, suggestions and useful guidance have been invaluable inputs that have improved the quality of my research. I remain ever grateful and thankful to them.

I am greatly indebted to the Australian Government’s Endeavour Awards for granting me the scholarship for pursuing the higher degree research and also the Faculty of Social and Behavioural Sciences of Flinders University for financial assistance in the later part of my studies. I am grateful to the Government of Bangladesh for generously granting me deputation for the period of the study. My thanks are due to Jane Horgan of Flinders’ International Students Service Unit (ISSU) for extending support and providing invaluable advice at some critical junctures of my PhD journey.

I would like to take the opportunity to thank the officials of the National Board of Revenue (NBR) in Bangladesh for the help they extended to me in data collection. I am particularly thankful to Hafizur Rahman, Zakir Hussain and Zahurul Al Mamun for helping me in arranging a Focus Group Discussion in Dhaka. I am also thankful to all in-depth interviewees, FGD participants and other respondents who spent their valuable time in sharing their opinions and experiences with me during my field visit.

I would like to express sincere gratitude to my family members for their continuous support and encouragement. Particularly, my wife, Dalia Parveen, as always, stood beside me as a spring of inspiration in the moments of emotional ups and downs. My son Rafid and daughter Zareen have their undeniable share in this effort as they constantly infused inspiration in me.

Although many people and institutions have contributed to this thesis, I alone bear responsibility for its contents, and for all the errors and lack of judgment, if any.
ACRONYMS

ACR: Annual Confidential Report
ADB: Asian Development Bank
ADR: Alternative Dispute Resolution
ARO: Assistant Revenue Officer
ATO: Australian Tax Office
ATV: Advance Trade VAT
BDT: Bangladesh Taka
CAGB: Comptroller and Auditor General of Bangladesh
CD: Customs Duty
CPD: Centre for Policy Dialogue
CSO: Civil Society Organization
DCCI: Dhaka Chamber of Commerce and Industries
EU: European Union
FAD: Fiscal Affairs Department
FBCCI: Federation of Bangladesh Chambers of Commerce and Industries
FGD: Focus Group Discussion
GDP: Gross Domestic Product
GATT: General Agreement on Tariff and Trade
GTZ: Gesellschaft für Technische Zusammenarbeit
IDS: Institute of Development Studies
IMF: International Monetary Fund
ITD: International Tax Dialogue
LARD: Local and Revenue Audit Directorate
LTU: Large Taxpayers Unit
MDG: Millennium Development Goal
NBR: National Board of Revenue
NPM: New Public Management
NGO: Non-Government Organization
OECD: Organization for Economic Cooperation and Development
PRSP: Poverty Reduction Strategy Paper
RIRA: Reforms in Revenue Administration
RRC: Revenue Reform Commission
RTI: Right to Information
SAARC: South Asian Association for Regional Cooperation
SAI: Supreme Audit Institution
SD: Supplementary Duty
SRO: Statutory Regulatory Order
TIB: Transparency International Bangladesh
TT: Turnover Tax
UNDP: United Nations Development Programme
UO: Unnoyan Onneshan
VAT: Value-Added Tax
WGI: Worldwide Governance Indicators
WTO: World Trade Organization