

Curbing Fiscal Defecit through Enhancing the Agriculture Income Tax Collection in Punjab, Pakistan

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Abstract

Pakistan faces fiscal deficits, and the federal government struggles to increase revenue. Agriculture income is taxable by the provincial governments. Post the Eighteenth Amendment, the provinces have mainly relied on their share from Federal Consolidated Fund and have not diligently tried to increase agricultural income tax collection. There is a need to ascertain the impediments in enforcing the law for optimal tax collection in Punjab. This research is an attempt to fill this gap in the literature. Through a qualitative approach, this paper finds that the issues in the non-implementation of the Agricultural Income Tax Act 2001 in Punjab arise from socio-cultural and political considerations. These are then translated into administrative inefficiencies by the revenue authorities. Legal amendments, as well as administrative reforms, are needed to enhance the revenue collection according to its potential. Based on the analysis, this paper recommends conducting a district-level study to determine the true potential of agricultural income tax in Punjab, possibly using proxies for income estimation. It suggests changing the land-based tax assessment to a minimum tax to eliminate the incentive for tax avoidance and introducing a minimal turnover tax on agriculture income to broaden the tax base and enhance collection efficiency.

Keywords: agriculture, fiscal, income tax, tax base.

1. Introduction

Pakistan has been chronically facing fiscal deficits and a shortage of funds to spend on human and infrastructure development (Khan et al., [2023](#)). The federal government struggles to expand the net of both direct and indirect taxes while agriculture income is out of its ambit (Haq & Bukhari, [2020](#)). The exemption of agricultural income from income tax has long been a topic of discussion in Pakistan.

Pakistan's economy is heavily dependent on agriculture as it contributes about a fifth of the total GDP in a year (Jatoi, [2020](#)). Agriculture is also a source of over four-fifths of the country's total export earnings if the agro-based products that are exported are also counted (Agriculture Department, [n.d.](#)). In addition to that, a little less than half of the total labour force of the country is engaged in the agriculture sector (Arif

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et al., 2000). Agricultural income is the income derived from a piece of land by performing various types of agricultural activities, including any method to make agricultural produce fit for the market and any kind of rent received by the owner of agricultural land (Anriguez & Valdes, 2006). This income is taxable by the provincial government of the province where the land is situated, but it is exempt from taxation by the federal government.

Many people argue that the exemption provided to agricultural income is one of the leading causes of inequity of taxation which also results in inequality in the long run because it gives birth to a disparity between agriculturists and non-agriculturists (Kemal, 2006). It is also one of the primary reasons for the reduction in the government's revenue base. However, the opponents of this argument suggest that agriculture is the backbone of our national economy and the primary source of employment for the rural population; therefore, it should be supported by extending tax exemptions. The debate intriguingly skips the main factor that agriculture income is exempt from income tax at the federal level, but it is taxable under provincial laws, and provincial governments are responsible for collecting income tax. This is not a matter of national income tax policy anymore but an issue to be dealt with by provincial governments.

Post the Eighteenth amendment in the constitution of Pakistan, the provinces have been mainly relying on their share from Federal Consolidated Fund to run their affairs and have not been making diligent efforts to maximize their revenues. A glaring inaction on the provinces' part is failing to collect agricultural income tax equal to its potential, and Punjab is no exception.

Punjab is population-wise the largest province of Pakistan, housing more than a hundred million people on a land area of 20.6 million hectares (Agriculture Department, n.d.). The majority of the population in Punjab resides in rural areas and is involved in agriculture, cultivating more than half (53%) of the total land area of the province. The census of agriculture conducted in 2016-17 depicted that there were 5.3 million agriculture farms in Punjab (Agriculture Department, n.d.). Big farms, having an area over ten hectares (25 acres or more), are 22% of the total cropped area in Punjab, which is about 17 million hectares. The major crops sown in Punjab include wheat, rice, sugarcane, cotton, and maize (Agriculture Department, n.d.) and all these crops are termed cash crops which are a significant source of income for farmers in Punjab, and that income is taxable under the Punjab Agricultural Income Tax Act, 1997.

The agriculture income tax on their incomes is to be levied by the government of Punjab, and the law provides taxation of agriculture income both based on the area owned by a farmer, as well as on the income earned by a person through agricultural activities. If we take into account the scale of agriculture being conducted in the province of Punjab and the quantum of income earned, the revenue collected in the form of agricultural income tax per annum should be more than twenty times what is being collected (see section 1). The total AIT collection by the government of Punjab is reportedly 3-5% of its total potential, and there are various policy, administrative, political, and social reasons for this less-than-optimal collection of AIT in Punjab.

Annual rental value per acre in Punjab varies from Rs. 50,000 to 100,000 depending upon the location, irrigation status, and nature of the land (A. Hussain, personal communication, June 10, 2023). Farmers may earn much more than this amount per acre depending upon the cost of their inputs and the prices of produce they fetch (orchards and vegetables are more lucrative). Even if we take this annual letting value as a proxy for agriculture income and take the total cropped area in Punjab for the year 2016-17, which was about 17 million hectares (Agriculture Department, n.d.), the back-of-an-envelope calculation of agricultural income comes to Rs. 2 – 4 trillion. A tax at a meagre 1% of this value would have generated Rs. 21- 42 billion for the tax year 2016-17, but Punjab could not collect even Rs. 1 billion for that year (see table-1).

Other than big farms in Punjab, 2.2 million (42%) farms are small farms having less than 1 hectare (2.5

acres) area. If we take the threshold of small farms at having less than 3 hectares (7.5 acres) of farming area, then almost four-fifths of the total arable land constitutes small farms (Agriculture Department, [n.d.](#)). However, over half of the total farms have an area ranging from one to ten hectares (25 acres), and they occupy 69% of the total land area. This categorization indicates that the debate on agricultural income and official data is still biased in favor of the size of a farm whereas, these days, modern agriculture, including tunnel farming and greenhouse farming on even a small farm of one acre can yield agricultural income much more than income from conventional farming over twenty acres of land (P. A.Ditta, personal communication, May 15, 2023).

The debate on this topic is mainly focused on whether agricultural income should be exempted or taxed. However, the literature is mainly silent on the point that agriculture income is already taxable under the provincial income tax laws. It has not been researched and analyzed from this point of view how agricultural income tax is not being collected as per law or according to its potential. There is a dire need to ascertain the impediments in the implementation of the policy of agricultural income tax and the enforcement of the law for optimal collection of tax in Punjab. This research is an attempt to fill this gap in the literature.

This paper analyses the extant literature on this topic to understand the discourse and historical development of the agricultural income tax. Based on the examination of national and provincial tax laws, it is observed that the laws exist in every province to tax agricultural income. Through the official documents and figures reported in the national accounts, it is ascertained that the tax collected in Punjab is far less than the actual potential. Section 1 contains the data collected through primary and secondary sources and the figures on agricultural income tax. It also describes in detail the legal framework in Punjab and other provinces to tax agricultural income. Section 2 elaborates in detail on the legal mechanism, administrative framework and the impediments in the enforcement of these laws. Based on the analysis in the two sections, section 3 describes the policy and operational issues in the enforcement of the law and the political and social hindrances. The conclusion follows the policy and operational issues, and recommendations are made after the conclusion, followed by references.

1.1. Statement of Problem

Punjab, the most populated province of Pakistan, has a land area of about 21 million hectares, and more than half of it is cultivated to earn agricultural income in various ways (Agriculture Department, [n.d.](#)). Agriculture from Punjab contributes the bulk of the country's annual GDP, and the agricultural income so earned is taxable by the government of Punjab. The estimated potential for the annual collection of Agriculture Income Tax (AIT) in Punjab is Rs. 55-75 billion (Nasim, [2013](#)). However, the actual annual collection is less than Rs. 3 billion. A progressive AIT law has been in place for last over two decades, but still, there is a substantial agricultural tax gap.

1.2. Research Questions

1. What are the determinants of the gap in the potential and actual collection of AIT in Punjab?
2. How can the AIT collection be improved in Punjab to tap its true potential for revenue maximization?

1.3. Significance and Scope of Research

The scope of this research is to examine the determinants of the gap in agricultural income tax law and practice and to find ways to bridge the gap. It is essential to determine why tax collection is low even though progressive tax laws are in place. The research so far has focused on the exemption and not the gap. This research will be limited to the examination of the laws of agricultural taxation, data on the collection of tax



and implementation of the laws in the field, and to ascertain the reasons for the poor collection. The research suffers from the lack of meaningful data on the actual potential of the agricultural income tax based on the progressive income-based application of the law. The guesstimates are taken from the literature as there is no systematic study of actual potential.

2. Literature Review

Historically, in Pakistan, agricultural income has been based on the land revenue system. Chaudhary (2022) argues that there is a long-standing demand to replace this system with an agricultural income tax similar to the tax on other incomes. Among the researchers and academicians, there is a controversy on the nature and scope of agricultural income tax; while some believe in its transformation into income tax similar to the tax levied and collected on other types of incomes, others argue against the notion of changing its form from the historic land-based levy (Chaudhary, 2022). Those against the imposition of income tax on agriculture base their arguments on the stated facts that the agriculture sector is already burdened by indirect taxes and some kind of direct taxes and that there is not much potential therein. On the other hand, the researchers in favor of agricultural income tax rely on the notions of tax equity and fairness in a taxation system.

In Punjab, Pakistan, the challenge of low agricultural tax collection is deeply rooted in historical, administrative, and socio-political factors. The prevailing trend of minimal taxation in agriculture is a result of political influences and the considerable power held by landowning elites (Rehman, 2023). Furthermore, the absence of accurate land records and inefficient tax administration systems contribute to the underreporting and evasion of agricultural taxes. Additionally, there is a widespread perception among farmers that the taxes collected are not utilized effectively for their benefit, leading to resistance towards tax compliance (Sikandar et al., 2024). Addressing these challenges requires comprehensive reforms, including the digitization of land records, strengthening of tax administration, and enhancing transparency and accountability in tax collection processes. Efforts should also focus on educating and engaging farmers in the taxation process, highlighting the importance of their contribution to the economy and the need for fair and equitable tax policies (Aftab & Ali, 2023). In Pakistan, the agricultural income tax is a provincial subject, and the federal government cannot inflict agricultural income tax as provided in the Constitution of 1973, and this provision is inherited from the Government of India Act of 1935 (Azhar, 1991). Over the years, there has been a controversial debate on how to transform agricultural tax in Pakistan from a land-based to a progressive mechanism and multiple commissions were made for recommendations and only two out of the nine recommended for transformation (Chaudhary, 2022). The remaining seven favored the existing land-based system of taxation. However, Azhar (1991) asserts that the land-based system defies the fundamental logic of equity and fairness in the taxation system. The progressive taxation of agricultural income was introduced in the AIT Act of 1997 in Punjab, amended in 2001, but it exists alongside the land-based taxation and Bahl et al. (2008) maintain that one of the many reasons for poor collection and weak enforcement of the agricultural income tax is the duality provided in the law.

The extant literature on this topic of less than ideal collection of AIT and weak enforcement of progressive agricultural income tax in Punjab points towards the fact that this issue is marred by the political considerations of the political parties because of which its collection is far less than optimal. The issue of low collection of agricultural tax in Punjab has been in debate for a long time. As per the law, agricultural income includes income from crop farming, rental income from agricultural land, and income from livestock. He argues that more than a purely economic subject the agricultural income tax has become an issue of political economy in Punjab. Almost all of the major national political parties have their political bases in Punjab and they do not incline to alienate their political support in rural Punjab by taking up this issue. This is the primary reason that subsequent political governments in the province over the past many

decades have only made lacklustre efforts to increase tax collection under this head (Nasim, [2013](#)).

Comprehensive research on this topic indicates that there can be identified three main reasons for the failure of the provincial governments in enforcing AIT law: weak revenue administration, pressure from farming lobbies, and growing provincial shares in the NFC award that gives ample money to the province for their development budgets and diminishes the provincial government's proclivity to raise their revenues through AIT (Bahl et al., [2008](#)).

However, Rashid ([2012](#)) asserts that agriculture income tax on small-scale farmers will push them into poverty and that it should only be levied on big and medium farmers.

If we look at the national level, there is significant heterogeneity in the agriculture income tax rates in Pakistan and the agricultural revenue based on land is estimated at Rs. 5 billion in Punjab, Rs. 2.5 billion in Sindh, Rs. 1 billion in KPK, and Rs. 0.5 billion in Baluchistan (Salam, [2022](#)). Salam ([2022](#)) also argues that based on FBR rates, the estimated agriculture income tax collection in Punjab per annum will be Rs. 112-134 billion. This indicates that there is a vast potential for agriculture income tax in Punjab that needs to be tapped.

The method of collection of tax from agricultural income in Punjab is obsolete (Ahmed & Naqvi, [2016](#)). Ahmed & Naqvi ([2016](#)) also argues that the method adopted for the calculation of the agricultural income tax liability in Punjab needs to be reformed. Under the law, the farmers are liable to pay higher acreage-based tax on their landholdings or the tax on their agricultural income, but since the law does not make it mandatory for the farmers to file their annual agricultural income tax returns, they can get away by paying only the acreage based tax which is always lower than their income tax liability on their actual income (Pakistan Institute of Legislative Development and Transparency, [2016](#)). The report also emphasizes that the laxity in the implementation of the law of agricultural income tax is due to the reason that the penalties for non-compliance provided in the law are not effective, nor are they imposed frequently on non-taxpayers. In addition to that, Ahmed & Naqvi ([2016](#)) asserts that there are severe issues with the capacity of the tax collection department i.e. the Board of Revenue Punjab. However, the lack of capacity cannot be taken as an excuse in this regard because agricultural income tax was being administered in the sub-continent as far back as the late nineteenth century (Azhar, [1991](#)). Azhar ([1991](#)) goes on to stress that if nothing else, then simple alternatives for determining and assessing agricultural income may be devised, like expressing net agricultural income as a function of rent for the land in that area.

3. Research Methodology

It was mainly qualitative research based on a single case study. Agricultural Income Tax is prevalent in all of the four provinces in Pakistan and the law and practices are more or less similar. However, this research is based and focused on the province of Punjab and relies on the case of Punjab as a single case study to understand the dynamics and deduce the answers to the research questions. The process tracing method was employed to focus on the clues in the study in search of plausible explanations. The descriptive method has been used to systematically understand and describe the situation from various angles and perspectives. The method of research is analytical to answer the research questions and answers have been found by the evaluation of facts and information relative to the subject of agricultural income tax in Punjab.

The data used for this research was collected through both primary and secondary sources. Mainly secondary sources of data were utilized including the internet and the library resources. Laws, regulations, and relevant rules were obtained from the websites of the concerned government departments, and international literature on the topic was accessed by consulting national and international journals, books and relevant records to get knowledge about the discourse on the topic. To ascertain the policy processes



in the making of laws in the province relevant documents and reports along with some grey material were utilized. The international literature on the general topic of taxation reforms was examined to develop an understanding of the philosophy of taxation and to have awareness of the historical evolution of taxation in this region.

The constitution of the Islamic Republic of Pakistan was consulted to determine how the right to taxation has been divided between the federation and the provinces. The Income Tax Ordinance, of 2001 showed how all other types of income, except agriculture income, are taxed by the Federation of Pakistan and how the law bars the federal government from taxing agricultural income. The Agricultural Income Tax Act of Punjab, 1997 was scrutinized to have an understanding of the mode and manner of taxation of agricultural income in the province. For the comparison's sake, the Khyber Pakhtunkhwa Land Tax and Agriculture Income Tax Ordinance, 2000 and the laws of other provinces were also examined in detail to develop an understanding of the agricultural taxation regime in the federating units of Pakistan and to learn lessons about the policy approach in other provinces. As it is also mentioned in the literature that all these laws are similar in every province, so reasonable conclusions can be made. The detailed examination of the agricultural income tax laws of all four provinces reveals that they were fundamentally amended to include the progressive agricultural income taxation regime at the same time in the year 2000 under the military regime of General Pervaiz Musharraf. It is also intriguing to note that all of these provincial statutes have similarities in rates and provisions. Therefore, the conclusions drawn in this study can be relevant to the policy processes in all four provinces.

Punjab Agricultural Income Tax Rules 2001 were also checked to understand how the law is administered by the administration. A thorough understanding of the law and procedure was developed by the author on this topic after consulting the above-mentioned literature.

The secondary literature mainly was obtained through the Internet, Google Scholar, Scopus, and also the NIM Library. The literature on this topic is mainly restricted to the quantum of the tax that is so far been collected and the potential of tax based on various estimation models. The author could not find any in-depth study or research that takes into account the stakeholder's views or revenues socio-political aspects of this issue. The articles on income taxation in Pakistan, specifically the sub-category of agricultural income tax in Punjab, were examined by the authors for and against this topic to understand the thinking pattern of the researchers on this topic and the evidence that they have utilized to reach conclusions. Many scholars have written on this topic from varied perspectives; some have approached it as an administrative issue, while others treat it as more relevant to equity of taxation among various types of income.

Trace evidence was obtained by examining the history of the evolution of the law of agriculture income tax in the province of Punjab. The grey literature also helped in this regard to build a chronicle account of the events. In addition to that, the judgments of the superior courts were also examined to understand the legal and judicial stance on the legislative or implementation issues of the law. The case law was retrieved from a website named eastlaw.com which contains a repository of the reported court cases covering all of the superior counts in the country. There are not many case laws on this issue, however, there are a few and those were examined in detail.

Although the central part of data for this research is secondary data, a minute portion of data is collected through primary sources. For that, two types of stakeholders were consulted to understand the ground realities and practices going on in the field. This information was gathered by conducting unstructured in-depth interviews with these resource persons either in person or on the telephone. These stakeholders included government officials who have worked in the field in various positions in several districts of Punjab as heads of tehsils as supervisors of *Patwaris* and *Qanungos* (both these officials administer the AIT law and are the first point of contact with the agricultural income earners to assess their incomes and tax

thereon), or in their capacity as Assistant Commissioners/Collectors in tehsils or Deputy Commissioners/Collectors in Districts.

The account evidence was collected by conducting seven in-depth unstructured interviews (four in-person and three telephonic interviews) from 15th May 2023 to 18th June 2023. Interview subjects also included three gentlemen farmers from district Gujranwala and One ex-member of the Punjab assembly who is also an agriculturist. A purposive sample of the respondents was chosen because only those officers in the revenue department could be of value to this research who had some experience working in the areas where they had administered agriculture income tax. Their availability was also an issue because not many of the chosen officers/officials were willing to respond at short notice, and some officials (Patwaris) were equally unaware of the legal intricacies involved as a layman.

The purposive snowball sampling technique was employed by requesting the first participants of the survey to identify or refer to some other resource person who contains knowledge on this topic. In more than fifty per cent of cases, the initial contacts referred to other junior in-rank officials or to those who had served before them in the field and were now either not holding any charge or were undergoing training. The interviews conducted with them were not only unstructured but informal as well to get their true feelings on the subject and their knowledge of both legal and political issues attached to this topic. The resource persons were also requested to allow for interview recordings on the phone which all of them denied and not even one agreed to mention their actual names in the research. They preferred to disclose their rank and place of posting where they have been implementing this law. This is also the severe weakness of this research as it cannot be declared with surety as to whether the responses are based on the general conditions or whether there is an element of bias or subjectivity.

Another stakeholder identified for this research was landowners or farmers who have been earning agricultural income through farming practices or obtaining rent on their agricultural land. They were also consulted to take their point of view on the issue of agriculture income tax in Punjab and how they feel would the proper implementation of agriculture income tax laws would affect them. For purposeful research and conclusion, it would be proper to select a sample of agriculturists based on their land holdings, nature of farming, and futures so that the issue could be examined from multiple angles this is a constraint on this research, and domestic research can include this aspect. Due to the paucity of time and other constraints, this research was limited to the sample of one district, i.e. District Gujranwala and a limited sample of two landlords and two tenants. This is a limitation of this research that the sample is not truly representative and the data gathered from the sample may not reflect the holistic and comprehensive approach to identifying the real issues and might have overlooked some clues to explain the situation.

The third stakeholder in this equation is the legislative assembly of the Punjab province as the legislation is done by the legislature. An ex-member of the Punjab assembly who also happens to be a landlord in a district of central Punjab was also interviewed. He had returned to the Punjab Assembly as a member of the most popular political party, the one which has been in power in Punjab for most of the time in the last thirty years. Since the assembly stands dissolved and the elections have not been scheduled as yet, it was a significant challenge to take a truly representative sample of the legislators.

Another primary source of data for this research was a panel discussion held during the 33rd SMC on 15th May 2023 on the topic, "Taxation Structure in Pakistan". One of the two resource persons was Mr Zain-ul-Abideen, who served five years as Chairman Punjab Revenue Authority. His discourse included the taxation structure of Punjab, and he dilated upon the agriculture income tax policy and implementation in Punjab. In response to the author's query on impediments and policy suggestions on the AIT in Punjab, the resource person gave a detailed insight into the topic from all perspectives. He was also interviewed on the telephone



later on.

Finally, after the data collection, the data analysis was carried out to generate a better understanding and to find answers to the research questions. Since the central part of the data was secondary data which included documents, legal procedures, journal articles, and reports, the method of data analysis chosen was thematic analysis. The general themes derived from the data initially included the impediments in the implementation of AIT law, suggestions for improvement in the collection of AIT in Punjab, and the history and context of legal development in the past. The analysis was then narrowed to the two key themes in this regard, which included the impediments or hindrances in the implementation of AIT laws. These main themes included the policy impediments that were due to the historical background of the law and policy and its acceptability amongst the public along with the enforcement by the district administration.

The primary data were analyzed during the process of collection. Since recording was not an option, taking notes during the telephonic discussion was resorted to, and the two central themes mentioned above were adhered to in those discussions. The responses of the resource persons to every question were clubbed under the same question type, and a central theme was extracted to ascertain the issues and analyses the problem.

4. Section 1 - Punjab's Agricultural Economy: Contribution to GDP and Revenues

Punjab is population-wise the largest province of Pakistan. It has a land area of 20.6 million hectares of which 53% is cultivated. The census of agriculture conducted in 2016-17 depicted 5,249,800 agriculture farms in Punjab with 22% big farms (25 acres or more) (Agriculture Department, [n.d.](#)). Usually, two crops are sown on arable land in Punjab, with some exceptions where farmers take three crops a year. The major crops include wheat, rice, sugarcane, cotton, and maize (Agriculture Department, [n.d.](#)). All these crops are termed cash crops, and excluding those small-scale farmers who own less than 5 acres of farmland, and indulge in subsistence farming, all other farmers earn income by sowing these crops. Punjab provides the largest share of the national agricultural production including significant quantities of raw materials for the industrial base of Pakistan (Agriculture Department, [n.d.](#)).

4.1. Legal Frame Work for Agriculture Income Taxation

4.1.1. The Constitution

The 1973 constitution of the Islamic Republic of Pakistan defines Agricultural Income in Article 260(1) as; *"income as defined for the law relating to income tax."* The reference to income tax was initially for the tax chargeable under the Income Tax Act of 1922, which was the law of the land for income tax at the time of the promulgation of the 1973 constitution. Later on, this was meant for the Income Tax Ordinance of 1979, which remained in vogue till the year 2001, and presently it refers to income tax administered under the Income Tax Ordinance of 2001 (ITO).

4.1.2. The Income Tax Ordinance 2001

The definition of agricultural income under the ITO is quite elaborate and covers many ways and means of earning agricultural income. As per sub-section (2) of Section 41 of the ITO anything emanating from and attached to agricultural activities is covered under agricultural income including revenue received or derived as well as the rent received by a person from land located anywhere in Pakistan, if that land is used for agricultural purposes. It also uses the term income derived from a piece of land by performing various types of agricultural activities, including any method to make agricultural produce fit for the market. So, it includes the whole chain of agricultural activities from farm to market. This way, the law is clear and delineates the categories of income not to be taxed under the ITO. It is noticeable that the base of agriculture tax for provincial governments is not narrow because it covers almost everything related to agricultural activities.

4.1.3. Punjab Agricultural Income Tax Act, 1997 AITA

In Punjab, the tax on agricultural income is levied under AITA and the same definition of agricultural income has been adopted under Sub-section (2) of Section 2 of the Act *ibid.* as is provided in ITO. The tax is chargeable under Section 3 of the AITA which states as under;

“Charge of Agricultural Income Tax.—(1) Subject to the other provisions of this Act, there shall be levied, assessed and collected each year a tax in respect of agricultural income of a tax year of an owner at the rate specified in the First Schedule to this Act.”

This legal provision contains a term that limits the scope of the charge of tax and has been misused to avoid agriculture income tax in Punjab in the past (M. Hamza, personal communication, June 10, 2023). It says that; “...in respect of agricultural income of a tax year on **an owner at**” (*bold and emphasis supplied*).

The term “owner” in the charging section provides a significant loophole for tax avoiders in a way that those who do not own agricultural land but earn agricultural income by performing farming on leased land have often misused this provision to evade tax. This problem is discussed in detail in section 2.2.

The agricultural income of a person is to be taken as annual income earned for a tax year which is again defined in the law under clause (j) of section 2 of the AITA as an “*agricultural year as defined in the Punjab Land Revenue Act of 1967.*” Moreover, an agricultural year is defined under sub-section (1) of section 4 of the Punjab Land Revenue Act of 1967 as, a “*year commencing on the first day of July, or on such other date as the Board of Revenue, with the previous approval of Government, may by notification, appoint for any specified area.*”

So a tax year for the agricultural income coincides with the financial year from the 1st of July in a year to the 30th of June next year unless otherwise provided by the Government of Punjab through a notification for a specific area.

There are three different legal provisions in the AITA to capture the tax base for a specific tax year. Firstly, land-based tax, which is provided in sub-section (1) of Section 3. This is simply the tax on the measurement of cultivated land during a tax year at the rates provided in the First Schedule to AITA. The exemption threshold under this provision is 12.5 acres of land below which there is no tax, and the highest rate is Rs. 600 per acre for exceeding 50 acres of irrigated land.

Secondly, as provided in subsection (3) of Section 3, to be charged at the rates provided in the Second Schedule to AITA. This captures the base of agriculture income earned during a tax year instead of the land cultivated in that period. This subsection was inserted through amendment in the year 2001, and since then, the law of agricultural income tax in Punjab has become progressive and caters to the income earned by a farmer instead of the land cultivated. The minimum threshold for exemption from tax in this scheme is Rs. 400,000. Income earned by a farmer can vary on the same measurement of cultivable land depending on various factors, including the nature of crops, agriculture techniques used, and the quality of inputs. Therefore, limiting the scope of tax only to the measurement of land cultivated was keeping a lot of the tax base out of the tax net.

Thirdly, Section 3B was inserted in AITA in the year 2013, and this provides for the taxation of any agricultural income that is declared by a person in their income tax return filed under the ITO, 2001.

4.2. Agriculture Income Tax Laws in Other Provinces



4.2.1. Khyber Pakhtunkhwa (KPK)

Agriculture Income Tax in KPK is governed through the Khyber Pakhtunkhwa Land Tax and Agriculture Income Tax Ordinance, 2000 (Khyber Pakhtunkhwa Ordinance No. IV of 2000) and is almost the same as AIT in Punjab as it is both land tax and based on income (Bahl et al., 2008). One of the similarities in both tax laws is regarding the progressive rates provided for an income tax. The minimum tax threshold for exemption from tax, when the tax is calculated based on income and not on land in the case of KPK, is Rs. 600,000. This has been enhanced from Rs. 400,000 (which is still the threshold in Punjab) vide Finance Act 2021. Through this Finance Act, not only the minimum threshold has increased the charge of tax for the whole tax year 2020-21 was waived off due to floods. The definition of agricultural income is the same in both provincial laws and is inclusive, containing all forms of agricultural activities.

However, when the income and tax thereon are calculated based on land, then in Punjab, there is an exemption in case of land less than 12.5 acres if the land is irrigated and 25 acres if the land is unirrigated. The exemption in KPK, when the income is calculated based on land, is only one acre, and the tax rates are also slightly higher than those in Punjab.

4.2.2. Sindh

In the case of Sindh, the agricultural income tax is governed through the Sindh Agricultural Income Tax Ordinance 2000, amended vide the Finance Act of 2018. Before this amendment, the land and income-based tax provisions were similar to those in the Punjab and KPK laws. However, through these amendments, the law of agricultural income tax in Sindh has been made different and better. The land-based tax has been abolished in Sindh and has been replaced with a minimum agriculture income tax. It means that the tax to be calculated and collected based on measurement of land shall be now considered as an advance tax to be adjusted against the final liability to be calculated at the end of a tax year. However, at the same time, this advance income tax has been made a minimum tax. This shall be the minimum amount of tax a farmer will have to pay. This is a significant step by the government of Sindh towards modernizing the agricultural income tax law. Since there are longstanding urgings by the researchers to change the land-based tax into a progressive income tax. The minimum threshold for exemption from progressive agricultural income tax has also been increased in Sindh to Rs. 1,200,000.

4.2.3. Balochistan

The Balochistan Tax on Land and Agricultural Income Ordinance, 2000 also provides similar provisions as are provided in the Punjab Agricultural Income Tax Act of 1997. The same two types of charges are there in the form of a land-based tax (with no exemption) and an income-based tax with progressive rates. The minimum threshold for exemption has also been brought equal to that in Punjab (Rs. 400,000) through the Baluchistan Finance Act, 2018.

4.3. Section 2 - Structure of Collection of AIT in Punjab

4.3.1. Authorities and Mode

4.3.1.1. Board of Revenue

The Revenue Department under the Board of Revenue Punjab carries out revenue administration in the headquarters and regional offices located in divisions, districts, and tehsils (Board of Revenue, [n.d.](#)). The revenue administration is carried out through the field officers starting from the lowest in rank, closest to the farms, namely *Patwaris*, upwards to Tehsildars, District Collectors, Divisional Commissioners, and finally Member Board of Revenue. These functionaries have to perform various functions including; survey of land, preparation and maintenance of land records, appointment of Lambardars, recovery of government dues, and administration of ten provincial laws and rules made thereunder (Board of Revenue, [n.d.](#)).

4.3.1.2. The Procedure

The procedure for assessment and collection provided in the law. Section 4 of the AIT Act provides a detailed mechanism that the tax shall be assessed and collected by the Collector as prescribed. Sub-section (3) of section 4 provides that if a person whose income is more than the exemption threshold or the land he cultivated in a year exceeds fifty acres (irrigated) or hundred acres (non-irrigated), then that person has to file his agricultural income tax return. The time limitation for assessment of the income by a collector has been provided at two years from the year to which the income belongs. Section 4A provides the mechanism of calculation of the income in a manner that aligns with the normal way of calculation of any income i.e. receipts minus all kinds of business expenses incurred by the person earning that income.

Section 10 provides for penalties to be levied by the collector on a defaulter of tax and the upper limit of penalty is fifty per cent of the total tax liability. Under this law, as provided in section 11, the government of Punjab has made rules to operationalize the law these rules are called Punjab Agricultural Income Tax Rules, 2001. These rules provide the prescribed forms of returns and the mode and method of filing a return of income, self-assessment scheme, assessment by a collector, and the mechanism for recovery of tax.

The land revenue staff in Punjab determines the average yield per acre for the crops cultivated on any land, *Jhar Paidawar* is the document that contains this information. The formula so developed becomes operative after it is endorsed by the district collector. Practically, *patwari* who is the revenue official closest to land farmers prepares *khasra gardawari* which is a register prepared based on crop inspection. However, the main factor that *Patwari* takes into account while doing so is land tenure instead of crop valuation (J. Hussain, personal communication, June 15, 2023). This is a substantial shortcoming that results in creating less than optimal tax liability for the farmers. Land area-based taxation has, therefore, become a leading source and method of taxation.

4.4. Annual Collection of AIT

The data on the collection of AIT in Punjab in the last ten years, along with the projected targets for those years, is as under

Table 1

Annual Collection of AIT in Punjab

Financial Year	Budget Estimate	Revised Estimate	Land-Based AIT Collection	Income-Based AIT Collection	Total AIT Collection
2012-13	721	864	759	68	827
2013-14	2019	830	759	175	934
2014-15	2019	1000	759	269	1028
2015-16	2300	1550	759	630	1389
2016-17	2300	1280	759	117	876
2017-18	1530	775	759	154	913
2018-19	1650	1100	759	815	1574
2019-20	2074	2074	1410	679	2089
2020-21	2500	2500	1410	956	2366



Financial Year	Budget Estimate	Revised Estimate	Land-Based AIT Collection	Income-Based AIT Collection	Total Collection	AIT
2021-22	2500		1410	704	2114	

Note: Deputy Secretary Recovery, Board of Revenue. ([n.d.](#)) Punjab, Rs. in Millions

The above-mentioned data indicates how over the years, the collection of AIT in Punjab has been made on land-based assessments. The third column shows clearly that a fixed amount has been levied and collected over the years, and income-based tax has been less than 40% of the total collection. This income-based collection is also not based on assessments carried out in the field by the *Patwaris* who are supposed to do this, instead, it was based on the data transferred from FBR to the Board of Revenue Punjab regarding those individuals who had declared their agricultural income in their income tax returns (J. Hussain, personal communication, June 15, 2023). On the other hand, the potential tax revenue that can be collected from this source is much more than the actual annual collection as the following table shows.

Table 2

Potential Tax Revenue

Sector	Current Tax Revenue	Potential Tax Revenue	Incremental Tax Revenue
Agriculture	3	375	372
Property Taxes	20	400	380
Total	23	775	752

Note: Dr Ishrat Hussain, The News August 12, ([2022](#)), PBC/CDPR, Rs. in Billions

The above data indicates that there is a huge potential gap in the agriculture income tax being collected in the country and what can be collected (Rupees Two Trillion, [2022](#)). A potential gap in the agricultural income tax in Punjab, according to some estimates is up to Rs. 75 billion, whereas, others put the amount higher than Rs. 100 billion per annum (Nasim, [2013](#)).

4.5. Reasons for low AIT collection in Punjab

There are various reasons for the low collection of AIT in Punjab, however, three reasons can be termed most important.

4.5.1. Land Based Assessment

Almost all land is taxed on a flat rate on acreage in Punjab. Therefore, it has become a norm and tradition such that the farmers are not inclined to graduate towards income-based progressive taxation. Moreover, in the case of land-based taxation above the exemption level, there is no progressive taxation structure; instead, when the threshold is achieved beyond that, all land is taxable at the same rate. This may provide a disincentive to the farmers to declare actual ownership or tenure of their land instead, they tend to declare less than actual ownership which is not caught by the land revenue authorities.

The law enjoins every farmer, who has to pay AIT based on income, to furnish a tax return declaring their actual income (sales minus expenses) on which they have to pay tax, but farmers usually do not file their

returns. It is also generally considered that the land revenue staff in the field, the *Patwaris* and *Tehsildars*, do not have the capacity to assess the AIT based on the incomes as provided in the schedule of the AIT Act (A. Buksh, personal communication, May 29, 2023). This phenomenon is explained in section 1.1 while describing the legal framework for charging and collecting tax.

4.5.2. Legal Lacunae

One of the reasons for the lower collection of the tax is that many farmers use the loophole provided in the law in the form of the charge of the tax on an “owner”. This author interviewed a tax lawyer in a famous income tax case that was decided by the Appellate Tribunal Inland Revenue (ATIR) in the favor of a taxpayer and the income tax charged on an annual income of Rs. 1 billion was deleted. The view of the tax officer who charged income tax on that taxpayer was also taken to ascertain the fact of the case.

In that particular case, a taxpayer had claimed exemption from Federal Income Tax on the premise that he had earned income for that particular tax year by cultivating sugar cane and selling the produce to his sugar mill. Since the income from farming activities is exempt under the ITO, as explained above, the tax under ITO could only be charged if the taxpayer had not paid income tax under the AITA of Punjab, which he did not (W. Bajwa, personal communication, June 12, 2023). On inquiry, it came to the fore that the taxpayer had exploited this loophole to avoid tax over an income of Rs. 1 billion in a year and neither paid tax in the province where he claimed to have earned the income through agriculture nor did he pay the federal income tax (W. Bajwa, personal communication, June 12, 2023).. This loophole is often used by many to avoid their tax liabilities both in the province where they are supposed to pay agricultural income tax and the federal income tax (M. Hamza, personal communication, June 10, 2023).

4.5.3. Improper Application of the Law

Sub-section (3) of Section 2 provides the mode of collection of agricultural income tax. For an assessment year, which coincides with a financial year, the tax on a person’s agricultural income is to be assessed and collected as per the rates specified in the Second Schedule. Now there are two charging subsections in this section, sub-section (1) and (3). The first sub-section provides that the tax will be charged as per the first schedule, whereas the sub-section (3) provides that the same shall be charged as per the second schedule. Furthermore, subsection (4) of the same section says that an assessee shall be liable to pay the higher of these two taxes. It can be understood from this scheme of the law that for an assessment year, an assessee liability shall be calculated under both these provisions and the higher one shall be charged.

Although the intent of the law is clear that the higher of the two has to be levied and collected but both the taxpayers and the tax collector have settled on the lower of the two. In practice, the patwaris rely primarily on the land holdings and consequential tax liabilities in the First Schedule to the AIT. They conveniently ignore the progressive taxation provided under the Second Schedule to the AIT (A. Hussain, personal communication, June 10, 2023).

4.6. Section 3 - Challenges in Taxing Agriculture Income in Punjab

4.6.1. Policy Challenges

Agricultural income tax policy in Punjab is devised through the AIT Act of 1997, and historically it was based on the land tax principle. Since the creation of Pakistan, the land tax policy has been in vogue. This policy was not optimal on two counts: One the land tax has no potential to grow with time as the land ownership has been reducing with time as the population grows the land is inherited and the chunks of land get smaller and smaller finally getting into the exempt bracket (A.A. Tiwana, lecture discussion, May 18, 2023). From the beginning of the AIT law, the minimum exempt threshold for land tax has been provided



at 12.5 acres of land and Eighty per cent of farms in Punjab are small farms (less than 10 acres) (Agriculture Department, [n.d.](#)). The policy of taxing agriculture income based on land-based tax would practically exclude four-fifths of the tax base from the tax net. This policy would rely overly on the remaining twenty per cent of the farms of the province, which are owned mainly by the rich and influential landlords who can easily influence the system to avoid taxes. There is also a firm reliance and bias in calculating and assessing the AIT based on the land measurement. This has been a big reason for poor enforcement and low collection of AIT in Punjab, as the tax is being collected based on a sub-optimal policy.

In the year 2000, there was a policy shift towards progressive agricultural income tax to be assessed based on income with a minimum threshold for exemption. This shift is visible in the four provinces simultaneously as all four provincial agricultural income tax laws were amended in 2000. However, there is a strange co-existence of this land base tax policy alongside the progressive income-based tax policy for decades now. The land-based tax was not removed from the statute books and this duality has been used as a loophole by the taxpayers to avoid income-based taxation and by the tax collectors to make less than desired efforts for tax collection. The data indicates that in Punjab, this duality of tax policy has been a significant cause of the low agricultural income tax collection.

This anomaly has been removed in Sindh through the Finance Act, 2018 and the land-based assessment and collection of tax has now been converted into a minimum tax to be adjusted against the final liability to be calculated based on income-based assessment. In this way, the loophole to be exploited by the taxpayers earning higher agricultural income to minimize their tax liability has been plugged.

The second policy-level challenge in Punjab for maximization of AIT collection is the continuation of assigning the function of agricultural tax collection to the district administration. Historically this function has been performed by the district administration when a *Patwari* at a local level used to maintain records of land ownership called *Khasra* and the record of crops cultivated on a farm called *Gardawari*. However, in the olden times, agriculture in Punjab was not as intense and widespread as it is now. In most parts of the province, agriculture is non-irrigated and occasionally land was cultivated once or twice a year. After the advent of modern agriculture techniques in the 1960s including tube-well irrigation, and industrial inputs in the form of modern seeds, fertilizers and pesticides, the scale and form of agriculture have changed and the old system of revenue collection limited to land-based assessment is not feasible anymore. More so, since the law now provides progressive income tax rates based on the income earned from agriculture and not only the land-based levy, the techniques of assessment based on the calculation of income after debiting allowable expenses is something that requires a skill set that *Patwaris* trained for the land-based system are lacking (Zain-ul-Abideen, panel discussion, May 15, 2023) (A. Buksh, personal communication, May 29, 2023).

4.6.2. Operational Challenges

To determine whether the low collection is due to some field operations or shortcomings on the part of the departments responsible for the collection of AIT the author conducted in-depth interviews of the officers having vast experience in the field as Deputy District Officers, Revenue, Assistant Commissioners (acting as Assistant Collectors), and Deputy Collectors. Their names have not been revealed because they are still in service, and they desired that their identities not be disclosed.

The main reason for the low collection of AIT in Punjab is that this is the lowest priority area of the district administration (Ex. D.C. Lodhran, personal communication, June 12, 2023). Although this is their primary duty to assess and collect AIT as per law properly, district administrations are busy doing other duties including but not limited to protocol duties, municipal functions, and firefighting exercises in case of any eventuality (Ex. D.C. Lodhran, personal communication, June 12, 2023).

The big landlords in every district or tehsil are mostly the politicians of that area too. They have affiliations with the leading political parties in the country and they can influence the district administration through their political powers. They are also used to paying meagre amounts of agriculture income tax on their lands since times immemorial and do not let the district administration assess their tax on their incomes at progressive rates (Ex. D.C. Bahawalpur, personal communication, June 10, 2023). Even if in some cases the district administration succeeds in assessing the actual tax liability based on agricultural income, the same is not recovered for years again because of the political influence and power of the defaulter landlords in an area (J. Hussain, personal communication, June 15, 2023) (Ex. D.C. Lodhran, personal communication, June 12, 2023). The following table shows the state of arrears for one district Gujranwala;

Table 3*Agricultural Income Tax Arrears in District Gujranwala*

Sr. No.	Tax Year	Tax Recoverable (Rupees)
1	2012	1,121,428
2	2013	1,070,605
3	2014	367,310
4	2015	81,200
5	2016	23,000
6	2017	65,250
7	2018	35,500
8	2019	1,444,013
	Total	4,208,296

Note: Board of Revenue Punjab, Board of Revenue ([n.d.](#)) Punjab

The above data indicates that even if in some tax years the demand is created it remains uncollected and then for subsequent years the landlords manage the system so that the demand is not created in the first place the situation is even worse in the southern districts where billion of rupees of arrears are still pending against the big landlords for years (Ex. D.C. Lodhran, personal communication, June 12, 2023).

4.7. Political and Social Will to Enforce AIT in Punjab

The analysis done by the author based on the primary and secondary data indicates that there is an absence of strong political as well as social will in Punjab to enhance the collection of agricultural income tax in the province.

On the political front, since the eighteenth amendment to the constitution, the share of provinces in the Federal Consolidated Fund has increased and the province of Punjab gets a higher share to run its affairs than it used to do before the amendment. This easy receipt of money from the federation has left the successive provincial governments least interested in making efforts to increase their tax collection through efficient enforcement of provincial levies. The biggest of these are two taxes that the provincial government can tap into to increase revenues Urban Immovable Property Tax (UIPT) and agriculture income tax.



The weak social and political will to enforce the law and enhance AIT collection in Punjab can be inferred from the fact that for many years even the parliamentarians of Punjab who had agricultural income were not paying AIT as per law. This weak enforcement of the law by the Punjab government was misused even to avoid the federal income tax on the taxable income under the Income Tax Ordinance, 2001. In their federal income tax returns many people, including parliamentarians, used to declare ‘exempt’ agricultural incomes to evade taxes. The federal government, in its effort to plug this loophole, persuaded the Punjab legislature and through the Finance Act 2013 an amendment was made to the Punjab AIT Act 1997 to introduce section 3B. This section provides that if a person declares agricultural income in his federal income tax return and he has not paid the AIT on that income then the declared income is taxable as per progressive tax rates provided in the provincial tax law. This was a significant step in the legislative history of the AIT law in Punjab and the law was implemented before the national and provincial elections and the nomination papers of all such persons who had declared agricultural income in their federal income tax returns but had not paid tax thereon were not accepted until they paid the due tax. Still because of the absence of a political and social will, this process was challenged before the Lahore High Court and the court decided the case in favor of the landlords on technical grounds. Fortunately, the decision was then overturned by the apex court of the country (2019 SCMR 446, [2019](#)).

Table 4

PESTL Analysis

Political Factors	Economic Factors	Social Factors	Technological Factors	Legal Factors
<p>Political Factors</p> <ul style="list-style-type: none"> • Power of big Landlords • Lack of political will • Corruption 	<ul style="list-style-type: none"> • Undocumented sector • Economy of subsistence agriculture 	<ul style="list-style-type: none"> • Social behavior against taxation • Narratives – Underdeveloped Sector 	<ul style="list-style-type: none"> • Manual records. • Lack of automation and technology in assessment 	<ul style="list-style-type: none"> • Historic legal legacies • Lacunae in the charging section

5. Conclusion

Agricultural income is exempt under the Federal Income Tax law, but it is taxable under the provincial tax laws. Provinces can tax agricultural income based on land holdings or progressive rates depending on the income earned. The debate on this topic has been whether agricultural income is taxable or not and missed the critical fact that taxation is not being implemented as per law. Punjab also suffers from poor implementation of law and less than optimal collection of agricultural income tax. Based on primary and secondary data analysis, this paper argues that multiple policy and operational issues impede the proper enforcement of agricultural income tax law and the collection of tax accordingly. The primary policy issue is that the law provides for both land-based as well as income-based tax and this loophole is frequently exploited by the farmers to avoid taxes. Another policy issue is that the enforcement of this law is assigned to the Board of Revenue Punjab which in turn administers it through the district administration framework which is not well equipped to do so.

At the operational level there are capacity issues in the administration, and the staff responsible for

assessment and collection resorts to land-based assessment and collection which is easier than complicated income-based taxation. Even if farmers file their income tax returns based on income earned through agriculture, the district administration does not assess their income correctly. Finally, there is a severe problem of lack of political and social will in Punjab to enforce this law in letter and spirit. Majority of legislators are involved in agriculture in one way or the other and they quell any attempt to enforce this law. The farmers also resort to the courts against any demand raised against them and avoid paying taxes for years.

There is a dire need to revamp the tax policy to make it optimal. The current tax policy is trite and caters only to land-based taxation of old times when land holdings were large and agricultural incomes paltry. In the current scenario where land holdings are small and incomes higher, a relevant agricultural income tax policy based on incomes needs to be formed and implemented. Reform in the tax administration is also required as the current administration faces operational challenges in implementing the law and collecting the tax. Finally, the political and social will in Punjab to maximize the revenue from agricultural income is also missing since a large number of members of the Punjab assembly are land owners and agriculturists. This is a major impediment to reforming the legal regime and enforcement of the law in letter and spirit.

The following policy recommendations are based on the analysis carried out in this research and the conclusion drawn therein. These are made keeping in view the ground realities as well as the policy gaps identified.

6. Recommendations

Based on the analysis and conclusion above this paper recommends the following policy measures;

Firstly, a systematic study should be conducted at a district level to ascertain the true potential of agricultural income tax in the province of Punjab. There is no such reliable data available in any department as the Board of Revenue Punjab maintains the lists of collection of agricultural income tax and arrears as sent by the district administrations and most of the district administrations apply the law only on land-based assessments. Assessment of tax based on the area of land is neither the true way of applying the law, nor it gives the exact potential of the tax due. For an informed policy decision on this issue, solid evidence is needed in the form of the calculation of the true potential of tax. Since the progressive taxation method, based on agriculture income has never been applied across the board in the districts of Punjab, it is difficult to ascertain the total potential of tax. If agriculture income earned in a year cannot be determined, then this can be done by taking a proxy for agriculture income. For example, as highlighted in this paper, the annual rent value of a unit of land in an area can be determined to the nearest value, and then, based on this the estimate of the total annual agricultural income for the whole of the province can be estimated.

Secondly, the land-based provision of assessment and tax in the law should be changed into minimum tax as has been done in Sindh in 2018. Section 3 of the Punjab Agricultural Income Tax Act, 1997 should be amended to change the land-based assessment into minimum tax and tax so calculated and paid should be made adjustable against the final tax liability to be calculated at the end of a tax year. This would remove the incentive for avoiding actual tax liability by just relying on the land-based tax provision.

Thirdly, to assess tax on agriculture income in a simplified manner, the concept of turnover tax should be introduced on a similar pattern as is available in the Income Tax Ordinance, 2001. It is easy to manage the expenses in any business, as is the case with agriculture, but a majority of farmers sell their cash crops to government departments at support prices, so it is difficult for them to hide their turnover. A minimal rate of tax, e.g. 1% of turnover, should be introduced to broaden the tax base and increase tax collection.



Finally, the administration of agricultural income tax should be transferred from the Board of Revenue (BOR) Punjab to the Punjab Revenue Authority (PRA) as the authority has delivered in GST collection on services by increasing the tax collection through efficient administration and using modern technologies like Information Technology. Compared to patwaris, the human resource of PRA is capable to assess progressive income tax efficiently based on return filing and assessments for which they are trained.

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9. Data availability

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