

Speeding up trade

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Trade is now easier in Pakistan, with customs clearance at the Karachi international container terminal dropping from 10 days in 2004 to 4 hours in 2007. Customs revenues are also up, from 115 billion rupees to 138 billion, despite a reduction in tariffs.

Failures of earlier reforms

Customs reforms are not new in Pakistan. Indeed, computerizing the customs services started in 1979. More recent initiatives include an Express Lane Facility (1998) to simplify the examination procedure, an Electronic Assessment System (2000) to automate assessment, and a Risk Indicated Selective Examination (2002) to assess risk in the examination procedure. Other customs-related reforms include outsourcing customs valuation functions to pre-shipment inspection companies, simplifying and enhancing the institutional setup for the duty drawbacks, and bringing customs valuation into conformity with General Agreement on Tariffs and Trade Article 7.

Despite the good intentions, customs clearance continued to be cumbersome and slow. Clearing an import cargo required 62–113 steps and 26–34 customs officials. Clearing an export cargo required 31–46 steps and 17–20 handling officials. Not surprisingly, this left traders in Pakistan at a competitive disadvantage.

Why the inability of the earlier efforts to ease customs clearance?

- The reforms were piecemeal. Clearing goods often required a chain of processes (declaration, valuation, examination, payment, and release). So tackling 1 link in the chain, even if effective, did little to shorten clearance times without attending to the other links.
- Key stakeholders were reluctant to participate. Traders expected that simplifying the duty drawback system would be less advantageous to them. Customs authorities expected that a new valuation scheme would mean large revenue losses.
- Political instability meant that in the 10 years to 2002, the average tenure of the chairman of the Central Bureau of Revenue, a political appointee, was less than a year.
- The turnover of key customs staff was high, hampering continuity.
- Customs operations lacked funds. Indeed, a fiscal crisis in 2001 prompted the reform of the Central Bureau of Revenue (CBR), the umbrella organization for Pakistan customs.

When President Pervez Musharraf came to power in October 1999, he appointed a reform-minded finance minister, Shaukat Aziz. Together, they pushed for reforms in several areas of the economy, with revenue administration being one of the most challenging. In 2000 the budget deficit was 6.4% of GDP, tax receipts were insufficient to service debt, and there were hardly any funds remaining for development. Further, the ability of the government to effectively deliver essential public services was under threat, and hyperinflation was looming. Reforming the tax administration was the single most important economic task facing the new government. It was not an option—it was a necessity.

A task force to review and recommend

President Musharraf set up an independent task force in June 2000 to review the tax administration and recommend how best to improve it. Headed by Syed Shahid Husain, a retired World Bank executive, the task force consulted widely within the CBR and among various trade associations. It looked at all aspects of CBR operations, including sales tax, income tax, excise tax, and customs, and presented its findings in May 2001.

In a big departure from the past, the task force viewed customs not merely as a revenue generation agency, but as an integral part of economic development. It saw the major benefit from improving customs services in an improved trading environment, with reduced trading times, costs, and documents. Increased trading would create jobs, spur economic growth, and enlarge the revenue base.

The task force also confirmed the inadequacy of the piecemeal approach to earlier customs reforms. And flagging corruption, it identified serious problems in business processes and organization, human resources, and information management.

A reform unit set up

The chairman of the CBR, Riaz Malik, was given the task of coming up with a reform program. The CBR reform cell had to grapple with several issues. Should the tax collection system be privatized, turning the CBR into a corporation? What should be the time frame for achieving the overall objectives? How should salaries be addressed? Should experts from the private sector be hired for specific assignments?

The reform unit received input on initial drafts of the reform agenda from the World Bank, International Monetary Fund, UN Conference on Trade and Development, and a foreign consulting firm (Maxwell Stamp). These consultations enabled it to assemble a comprehensive program to reform the CBR, approved in March 2003.

As part of the program the CBR's Customs Administration Reform (CARE) set out to redesign processes in customs operations and modernize customs services—through round-the-clock clearance, self-assessments, risk management, a paperless single-window environment, and reduced opportunities for discreet interaction between importers and customs officials.

As with the failed Public Revenue Authority Bill in 1998, the 2003 reform faced hurdles. Staff resisted change, fearing job losses from the rationalization of a bloated workforce. Staff also had interests vested in a corrupt and badly managed customs administration. Government rules and procedures reduced the flexibility that the CBR needed to hire private sector experts and offer higher salaries to CBR staff than to other public servants. Also needed was a legal basis for re-engineering the customs business processes through an electronic data interchange. That's not all. Possible political changes could remove government support. And several aspects of the reform agenda were expensive, requiring external funding.

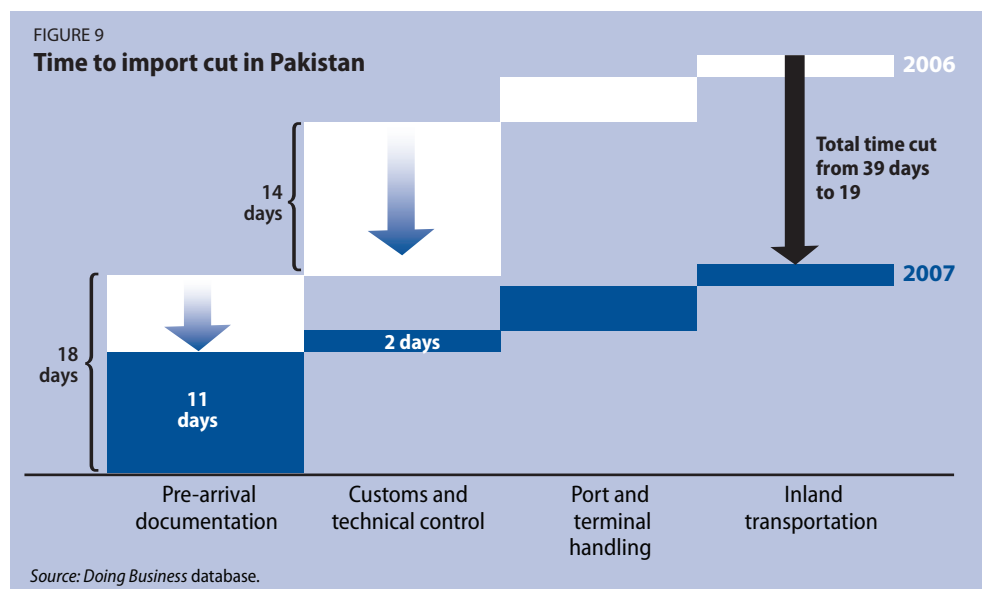
Start with quick wins

The reform cell strategy was to implement the short-term, less costly, quick-win reforms immediately while preparing the ground for the medium- to long-term reforms, perhaps more complex and costly.

Among the quick wins was simplifying the documents required for trading—a simple administrative decision with very powerful consequences for the ease of trading. Traders needed to submit only 1 document, the Pakistan Goods Declaration. Other reforms followed:

- The CBR reduced the maximum tariff rates and the number of tariff bands, simplifying the valuation of customs duties.
- The CBR published a new professional code of ethics and conduct, signalling to staff the intent to eliminate corruption.
- To sustain the reforms, the Cabinet Committee for Finance and Revenue, headed by the minister of finance, and the CBR Board, were given fixed 5-year terms. The committee oversaw the CBR reform and reported directly to the president, thereby bringing considerable political clout to the reform.
- The legal basis for several of the medium- to long-term measures was sought from the Ministry of Finance and the legislature. These included the CBR's ability to formulate its budget and administrative policies in specific areas, to have flexibility in spending its budget, to decide its compensation structure, and to adopt its own human resource recruitment and development strategy. Given the strong backing for reform, the necessary approvals were granted.

Envisaging resistance to costlier long-term reforms, the CBR adopted a proactive change management strategy, seeking to involve staff in the reform process by defining expectations, building consensus, and articulating a clear vision. Workers



fearing job losses were assured that they would not be forced out of their jobs and that all workers departing voluntarily would get a “golden handshake.” This helped reduce early resistance to reform.

Costlier long-term reform

FINANCE. While implementing the quick win measures, a medium to long-term reform was also being prepared. The International Monetary Fund (IMF) approved a Poverty Reduction and Growth Facility with Pakistan in 2001, including tax policy changes and the CBR reform. The World Bank approved a project dealing with the CBR’s medium- to longer term reform program in December 2004, with modernizing customs being a significant component. The \$149 million project, co-financed by the government of Pakistan and the U.K. Department for International Development, is to be under implementation until 2009.

HUMAN RESOURCES. A major long-term goal is to rationalize the workforce. The CBR is known to be overstaffed, particularly at lower grades. With a move to modern revenue administration, lower skills would be in even less demand. An improved compensation package for the reorganized CBR has been agreed upon. All staff are expected to apply for vacancies and those recruited will have a more lucrative package. New staff are expected to have higher qualifications, and the staff training program has been improved to build capacity. For staff not recruited the strategy to reduce the workforce is voluntary and spaced over 5 years (2005–09). CBR officers with 25 years of service are expected to retire. And any surplus staff, particularly at lower grades, would be offered career counseling and retraining.

MODERNIZING CUSTOMS SERVICES. Customs procedures are being modernized through the Pakistan Customs Computerized System (PACCS). Unlike previous standalone modules, the PACCS is a comprehensive integrated information technology system to implement user management, carrier declaration, goods declaration, risk management, assessment, examination, payments, management information systems, transshipment management, status notification, clearance management, adjudication management, security management, bonded warehouse management, and a tax node. The new system streamlines the clearance process (allowing for pre-arrival lodging of declarations, electronic payment, and signatures) and applies risk management.

PACCS was piloted in April 2005, and the electronic submission of documents was fully implemented at the Karachi International Container Terminal by January 2006. Traders can now lodge documents before goods arrive at the port, avoiding customs disputes because the system automatically determines the duty. Thanks to risk profiling (green, yellow, and red lanes), customs officials do much less physical inspection of goods.

The success chalked up so far is mainly at Karachi International Container Terminal, it is currently being rolled out to 11 other customs collectorates.

FIGURE 10

Timeline of trade law reform in Pakistan*Source: Doing Business database.*