

Value Added Tax (VAT)- Replacement of Sales Tax System



* Akhil Sharma

A B S T R A C T

Research Paper- Commerce

Value added tax (VAT) is modern, logical and progressive form of sales tax. It is multi staged sales tax levied on value added to a product by each selling dealer with the provision of credit of tax paid by the dealer to the previous person on purchase of goods. Basically Vat implementation seeks to broaden the tax base, providing neutrality, equity and fairness in the current system for the development of the country. Now the State level Vat has been introduced as a replacement of State level Sales Tax. It is collected by the government of state in which the final consumer is located.

Keywords: Progressive Tax, Multi-staged Tax, Replacement Of Erstwhile Sales Tax System.

Introduction:

VAT is a system of indirect taxation, which has been introduced in lieu of sales tax. It is the tax paid by the producers, manufactures, retailers or any other dealer who add value to the goods and that is ultimately passed on to the consumer. VAT has been introduced in India to ensure a fair and uniform system of taxation. It is an efficient, transparent, revenue-neutral, globally acceptable and easy to administer taxation system. It benefits the common man (consumer), businessman and the government. Vat is levied as a percentage of sales prices. Unlike Indian sales tax, VAT is an intra-state multi-point tax system and is levied on the value added at every stage.

Under the VAT regime, the VAT paid by registered persons on goods (including capital goods) purchased from within the state is available for input tax credit. The input tax credit can be used to offset periodic liability either under VAT or the CST. This ensures that the cascading effect of taxes is avoided and that only the value addition is taxed. Currently, there is no VAT on imports into India and exports are zero-rated. This means that while exports are not charged with VAT, VAT charged on inputs purchased and used in the manufacture of export goods or goods purchased for export, is available to the purchaser as a refund.

Objectives of Vat:

- To avoid the problem of under valuing as all stages are subject to tax.
- To keep proper records of sales and purchases.
- To avoid Tax evasion
- To abolish unhealthy sales tax war among the states.
- By giving tax credits, the manufacturing cost will be less.
- To ensure simplicity and transparency in the system
- To help in fiscal consolidation for the country in bringing a steady source of revenue reducing the debt Burdon.

Origin and Chronology of VAT:

The VAT was first introduced in France in 1885 and was known as "Taxe Surlo Valeur Adjoutee" Later on it spread to other countries. At present almost all the developed countries have adopted the VAT in some form or the other. A brief account of introduction of VAT in some countries is given below.

Countries	Year
France	1954
Brazil	1967
European Countries In Mid	1970's
Pakistan	1990
Bangladesh	1991
China	1994
Sri-lanka	1995
Nepal	2000
India	2005 (Haryana2003)

General Terminologies Used in VAT:

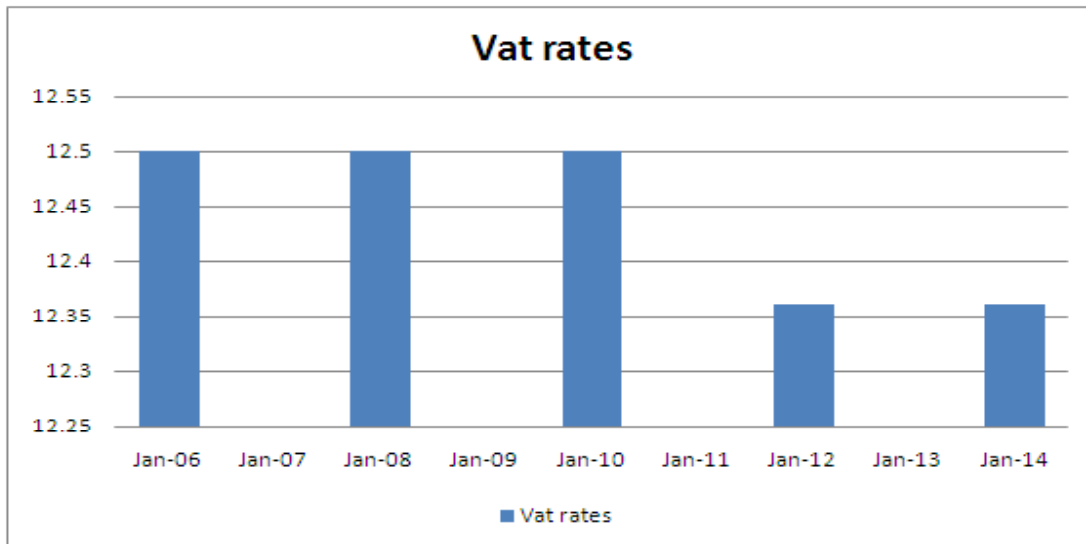
1. Input VAT: This is a tax paid on purchases
2. Output VAT: This is a tax charged on sales.
3. Input credit: The amount of Input tax that permitted to be set off against output tax.
According to white paper, there are 550 categories of goods under the VAT system. They are classified into the following four groups, depending upon VAT rate:

- VAT@1%
This is for specific category of goods like gold, silver etc.
- VAT@4%
The largest number of goods (270) comprising of basic necessity items such as drugs and medicines, agricultural and industrial inputs, capital goods are under 4% VAT.
- VAT@12.5%

The remaining commodities are under the general VAT rate of 12.5%.

Note: Few goods that are outside VAT as a matter of policy would include liquor, lottery tickets, petroleum products as the prices of these items are not fully market determined. These items will continue to be taxed under the sales tax act of the respective states.

VAT Rates From 2006-2014



Methods of Charging VAT:

Subtraction Method:

Tax rate is applied to the value added on the difference between the value of output and the cost of input.

Addition Method:

By summation of all elements of value added (profits, rent, wages etc).

Invoice or Tax Credit Method:

Difference between the tax paid on purchase and the tax payable on sales as per the invoice is VAT. India opted for this method.

Concept of VAT Example:

- **'A'- Raw Material Producer**
Sales value- Rs 100/-
Gross VAT @ 10%- Rs 10/-
NET VAT- Rs 10
- **'B'- Manufacturer**
Sales value- Rs 140/-

Gross VAT@10%- Rs 14/-
NET VAT- Rs 14- Rs 10= Rs 4/-

• **'C' Wholesaler**

Sales value- Rs 170/-
Gross NET@10- Rs 17/-
NET VAT- Rs 17- Rs 14= Rs 3/-

• **'D' Retailor**

Sales value- Rs 200/-
Gross VAT@10%- Rs 20/-
NET VAT- Rs 20- Rs 17= Rs 3/-

How VAT Utmatelley Works??

VAT is levied on every stage in supply chain along with credit of tax paid at earlier stage on input Tax credit. Thus

VAT payable= VAT on sale of output - VAT on input

Illustration:

Input worth Rs 1,00,000 are purchased and sold at Rs 2,00,000 after adding value (including profits). The rate of VAT applicable on inputs is 4% and VAT rate on sale of output is 12.5%. The calculation of VAT will be as follows:

Input purchased- Rs 1,00,000
Output sold- Rs 2,00,000
Input tax paid- Rs 4000
Output tax payable- Rs 20,000
VAT payable- Rs 16,000

Under Sales Tax System

Particulars	Cost
Input Purchased From A	1,00,000
Add: Sales Tax Paid @4%	4,000
Total Purchase Cost For B	1,04,000
Add: Value Addition By B	96,000
Total Sales Price	2,00,000
Add: Sales Tax Payable @ 12.5%	25,000
Total Selling Price To Consumer	2,25,000

Under VAT System

Particulars Cost	VAT
Input Purchased From A	1,00,000
Vat Paid @4%	4,000
Total Purchase Cost To B	1,00,000
Add: Value Addition By B	96,000
Total Sale Price By Seller	1,96,000
Add: Vat @ 12.5%	24,500
Total Selling Price To Customer	2,20,500
Vat Payable By B (24500-4000)	20,500

Conclusion:

From the above ILLUSTRATION it is clear that due to VAT the price of goods has come down by Rs 2,25,000-2,20,000=Rs 4500. Therefore one can say it reduces the cost for the consumer. VAT is the replacement over erstwhile sales tax system, which has featured by narrow base, multiple rated, cascading effects, tax evasion etc. It is an tax which has widen the tax base, has no exemption of tax, tax evasion is not possible as it is well administered.

REFERENCE

1 <http://www.tradingeconomics.com>
2 Gaur,v.p., &puri.rajiv.(2012).value added tax, planning and management of co-operative taxation(ninth edition),504-508