

VALUE ADDED TAX IN INDIA (VAT)

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In one of the most large scale reforms of the country's public finances in over past 50 years, India has finally agreed the launch of its much-delayed Value Added Tax (VAT) from 1st April 2005. At a rate of 12.5%, VAT will come in on April 1, 2005. The tax, agreed after state finance ministers met in New Delhi, is designed to make accounting more transparent, cut trade barriers and boost tax revenues.

The system had been postponed many times, mainly because of opposition from the powerful trading lobby. Ashim Dasgupta, who heads a panel overseeing the implementation of VAT, said: "We are very happy to announce that a broad consensus among states was arrived at the meeting to introduce VAT on April 1, 2005." The Congress-led new left-leaning United Progressive Alliance (UPA) government has made implementing VAT one of its key priorities. According to analysts VAT is essential in tackling the problem of tax evasion. In India, all the state governments collect over Rs 85,000 crore (Rs 850 billion) by way of sales tax and further over 20,000 crore (Rs 200 billion) by way of Central Sales Tax. This is what officially comes mostly from petroleum, liquor, iron and steel and cement companies. Rough estimates suggest that these industries account for over 50 per cent sales tax for the states and the Centre. Majority of the officials in sales tax departments believe that what they actually collect is less than 50 per cent of the revenue that should otherwise accrue to them if all transactions are accounted for by the businessmen.

India has a large un-organised market, especially agro-based industries and here a large number of transactions go unrecorded. The menace of stock transfers adds to the problem of tax evasion. In India, introduction of VAT will only change the collection methods for sales tax rather than reform the indirect tax system.

VAT is nothing but sales tax at source. Instead of collecting it after five months or so, the state governments would collect the same in advance and then allow set-offs to the businessmen. All tax paid on inputs, subject to rules made, shall be allowed to set-off against the tax on output. There would be exceptions like CST not allowed to be set off if sales are made locally in some other state; octroi not to be set off against output tax, etc.

References

1. *Actioned: Where Does It Hurt?*, Report from Action Aid, London, March 2005