A brief on VAT (Value Added Tax)

What is VAT?

VAT is a multi-stage tax levied at each stage of the value addition chain, with a provision to allow input tax credit (ITC) on tax paid at an earlier stage, which can be appropriated against the VAT liability on subsequent sale.

VAT is intended to tax every stage of sale where some value is added to raw materials, but taxpayers will receive credit for tax already paid on procurement stages. Thus, VAT will be without the problem of double taxation as prevalent in the earlier Sales tax laws.

Presently VAT is followed in over 160 countries. The proposed Indian model of VAT will be different from VAT, as it exists in most parts of the world. In India, VAT has replaced the earier State sales tax system.

One of the many reasons underlying the shift to VAT is to do away with the distortions in our earier tax structure that carve up the country into a large number of small markets rather than one big common market. In the earlier sales tax structure tax is not levied on all the stages of value addition or sales and distribution channel which means the margins of distributors/ dealers/ retailers at large not subject to sales tax earlier.

Thus, the sales tax pricing structure needs to factor only the single-point levy component of sales tax and the margins of manufacturers and dealers/ retailers etc, are worked out accordingly.

internal trade and impeded development of a common market.

prices by an amount higher than what accrues to the exchequer by way of revenues from it.

Also, there was the problem of multiplicity of rates. All the states, provided for plethora of rates. These range from one to 25 per cent. This multiplicity of rates increases the cost of compliance while not really benefiting revenue.

Heterogeneity prevailed in the structure of tax as well. Apart from general sales tax, most states used to levy an additional sales tax or a surcharge. In addition, the states levied luxury tax as also an entry tax on the sale of imported goods.

All these practices of heterogeneity in structure as well as rates cause diversion of trade as well as shifting of manufacturing activity from one State to another. Further, widespread taxation of inputs relates to vertical integration of firms, i.e., the earlier system of taxes militated against ancillary industries and encourages them to produce more and more of the inputs needed rather than purchase them from ancillary industries.

The earlier system of commodity taxes is non-neutral. It interferes with the producers' choice of inputs as well as with the consumers' choice of consumption, thereby leading to severe economic distortions.

How can VAT address these issues:

Under the VAT regime, due to multi-point levy on the price including value additions at each and every resale, the margins of either the re-seller or the manufacturer would be reduced unless the ultimate price is increased.

VAT would not cause cascading, nor would it cause vertical integration of firms. Also, it provides total transparency of the incidence of tax. This is because, VAT is a multi-stage sales tax levied as a proportion of the value added. It is collected at each stage of the production and distribution process, and in principle, its burden falls on the final consumer.

Another feature of VAT regime is discontinuation of the sales tax based incentives to new industrial units. Until now, all the states were granting such incentives to new industries in the form of exemption from tax on the purchase of inputs as well as on the sale of finished goods, sales tax loans and/or tax deferral. However for the new industrial units to whom the incentive by way of exemption/ or tax deferrals are already sanctioned under the Sales Tax Act are continued in the form of refund.

Rebating, returns & billing under VAT

IN CASE OF MANUFACTURER

(a) Input tax rebate is available only on the purchases made in the State of Karnataka and on the basis of 'Tax invoice' issued by the dealers selling goods to the manufacturers. Taxes or duties paid on other types of purchases namely: interstate purchases, interstate consignment receipt and International imports are not eligible for input tax rebate.

(b) Output tax is to be charged and collected on the sales made in the State of Karnataka. However, on the interstate sales taxes under CST Act could be collected separately or it could be included in the sale price also. In both these cases of sales, input tax rebate is available only on the purchases made in the State of Karnataka. On consignment transfer both in the State of Karnataka and interstate there is no levy of VAT or CST as there is no transaction of sale in either of them. (For interstate consignment of manufactured goods and the goods purchased from Karnataka and despatched to outside the State the dealer would be entitled for input rebate paid in excess of 2% on the local purchase). In case of export of the goods (both direct and indirect) the output tax is zero and input tax rebate is available only on the purchases made in the State of Karnataka.

(c) In the monthly return prescribed under VAT Rules namely Form VAT 100, the above types of purchases and sales are itemized. The dealer has to extract the details from the books of account and fill the return form.

(d) The input tax rebate is taken while filing the VAT monthly return by reducing the output tax. For example: For a given month the input tax paid by a dealer is say Rs.10,000/- and the output tax payable is say Rs.20,000/-, then net-tax payable would be Rs.10,000/- (20,000 - 10,000). Please note that in the tax invoice, VAT is charged and collected on the entire output value. And in the bill of sale issued under interstate sales, CST could be collected separately or it could be included in the sale price also. In case of direct and indirect exports no taxes are collected but the VAT paid on the locally purchased inputs is fully rebatable.

IN CASE OF DISTRIBUTOR

In case of distributors / wholesaler the conditions noted in para 1(a), (b), (c) &(d) above applies with the following modifications: Under para 1(b) the ''For interstate consignment of goods distributors / wholesaler would be entitled for input rebate paid in excess of 2% on the local purchase.''

IN CASE OF RETAILERS

In case of retailers the conditions noted in para 1(a), (b), (c) &(d) above applies with the following modifications: Further the retailers within the turnover limit between 2-15 lakhs could opt for composition tax of 1% on their sales. The condition prescribed to remain under composition scheme is apart from turnover limit, such dealer must not effect any interstate purchases (except a dealer executing works contract with certain conditions), must not claim any input tax rebate and must not collect output tax.

Composition scheme under VAT Act

Registration and payment of taxes under VAT Act can be of two types. First type is the registration and payment of taxes under full VAT and second type is the registration and payment of taxes under composition.

The option should be exercised by a dealer, while applying for registration in the prescribed VAT Form 1. A dealer who is already registered under full VAT could also opt for composition subjected to certain condition mentioned hereunder:

Conditions prescribed for registration under composition:-

A dealer applying for registration under composition should fulfill the following conditions:

1) Dealer should either be a registered dealer under the Act or shall be making an application for registration under the Act.

2) The stock of the dealer shall not comprise of goods purchased from outside the state.

3) Dealer shall not be purchasing goods from outside the state.

4) Dealer should not have claimed input tax rebate on the transition stock.

5) Dealer shall not be selling liquor.

6) Dealer shall not make interstate sales (except a dealer executing works contract with certain conditions)

7) Dealer shall not effect export sales.

8) Dealer shall not be a casual trader.

9) Dealer shall not be a dealer who has taken voluntary registration under section 23 of the VAT Act.

In order to avoid frequent changes from full VAT to composition there is a restriction of a minimum retention of 12 months as a registered dealer under full VAT; before exercising the option to go in for registration under composition scheme.

Category of dealers eligible for composition scheme:

Subject to the condition laid above, only the following dealers are eligible for composition scheme:

1) Dealer whose annual total turnover is between 2 lakh and 15 lakh.

2) Dealer who executes Works Contract.

3) Dealer who is either a hotelier or restaurateur or a caterer and or a dealer running a sweatmeat stall or an ice cream parlour or a bakery

4) Dealer producing granite metal and other than granite metal by using stone crushing machinery.

The applicable rate of tax for the dealers under composition scheme and the ceiling of the turnover prescribed along with periodicity for filing the returns are indicated in the table below.

Features to be noted by composition dealer:

1) The Composition dealer will be provided with a certificate of composition called Form VAT 8. The dealer applying for Composition Scheme shall be collecting regular rate of tax under section 4 till he gets the certificate.

2) After service of 'Certificate of Registration' under composition such a dealer is barred from collecting the tax. This is clearly mentioned in the said certificate.

3) No 'tax invoice' meant for full VAT dealers can be raised by dealer under composition. They should raise sales invoice as prescribed under the VAT Rules.

4) The Composition dealer is barred from taking input tax credit. The input tax credit even on transition stock is also not allowed.

5) Dealer exceeding the turnover limit of Rs. 15 lakhs in a year [except dealers executing in Works Contract], Hotelier, restaurateur or caterers or a dealer running a sweatmeat stall or an ice cream parlour or a bakery and dealer producing granite metal by using stone crushing machinery], shall automatically enter into full VAT from the first day of the month succeeding the month in which he exceeds the threshold.

In such cases, the dealer shall file the final return under Composition Scheme upto the end of that month and shall start charging regular rate from the first of next month.

6) The dealer coming under the Composition Scheme becomes ineligible for the Scheme if he purchases goods from outside the state or if he imports the goods from outside the territory of India(except for a dealer executing works contract with certain conditions) and he shall start paying at regular rate of tax from the first day of the month in which he has made such purchases.

7) The dealer under Composition Scheme, other than a hotelier, restaurateur or caterer and a dealer producing granite metal by using stone crushing machine, shall be filing his returns in the Form VAT 120 once in a quarter which will have to be filed by 15th of the month following the relevant quarter. This filing of return every quarter is compulsory even if the tax payable is nil.

Quarter is defined as the period ending on final day of months of March, June, September and December. For others, filing of returns is monthly in Form VAT 120 within fifteen days after the end of the relevant month. Revised return can also be filed in Form VAT 120 only.

8) While moving from Composition to full VAT Scheme, he shall surrender his Form VAT 8 certificate file a final return in Form VAT 120 with full payment of tax.

9) For the dealers who have opted for full VAT or composition during 2002-03 and they have been allotted TIN during that period, have been given the option to modify the option from 1st April. The relevant Rule is extracted hereunder:

Rule 181: Transitional provisions:- Subject to these rules, any application made by a dealer for registration under the Act before the commencement of these rules shall be deemed to be an application made under rule 4 and such dealer shall be permitted to make any modification in the application made by submitting an application in Form VAT 1.

Sl.No.	**Type of dealer**	**Turnover limit**	**Rate of taxes**	**Period for filing return**
1.	Regular Composition dealer Trader/Manufacturer	Upto 15 lakh	1%	Quarterly
2.	Dealer executing works contract	No turnover limit	4%	Monthly
3.	Hotelier, restaurateur or caterer	No turnover limit	4%	Monthly

In respect of a dealer being a mechanised crushing unit producing granite metals, at the following rates,

Sl. No.	Capacity	Rates	Period for filing return
(1)	(2)	(3)	
(i)	For each mechanized crushing machine of size exceeding 16"x 9"	Rs. 16,500 per month	Monthly
(ii)	For each mechanized crushing machine of size exceeding 12"x	Rs. 8,250 per month	Monthly

(iii)	For each crushing machine of size upto 12"x 9"	Rs. 4,000 per month	Monthly

(4) In respect of a dealer being a mechanised crushing unit producing metals other than granite metals, at the following rates,

Sl. No.	Capacity	Rates	Period for filing retrurn
(1)	(2)	(3)	(4)
(i)	For each mechanized crushing machine of size exceeding 16"x 9"	Rs. 10,000 per month	Monthly
(ii)	For each mechanized crushing machine of size exceeding 12"x 9" but not exceeding 16"x9"	Rs. 5,000 per month	Monthly
(iii)	For each crushing machine of size upto 12"x 9"	Rs. 3,000 per month	Monthly

How to calculate VAT

Formula for calculating net sale price on which VAT @12.5% has to be charged:

Net Sale Price= 88.89 X MRP / 100

VAT @12.5% on net sale price = 11.11 X MRP / 100

P.price: Purchase price; T.R: Transition Rebate

Under KST regime the retailer used to absorb the RST of 1.5% or collect it separately without exceeding the MRP. This can be achieved even under VAT without exceeding MRP as indicated below.

Sl. No	Name of the item	P.price incl of KST	MRP	Margin under KST Sales	Net margin after RST	Net Sale Price	VAT @ 12.5%	90% of Purchase price	Transition rebate @ 12.5%	Net VAT payable= (Column 7 Minus Column 9)	Net margin after Transition Rebate
	1	2	3	4	5	6	7	8	9	10	11
1	Old Spice	45.50	50.00	4.50	3.75	44.44	5.56	40.95	4.55	1.01	3.49
2	Old Spice	136.50	150.00	13.50	11.25	133.33	16.67	122.85	13.65	3.02	10.48
3	Sweetex Pallets	28.15	32.00	3.85	3.37	28.44	3.58	25.34	2.81	0.74	3.11
4	Setwet hair-styling gel	73.50	80.00	6.50	5.30	71.11	8.89	66.15	7.35	1.54	4.96
5	Krack-SR	25.00	29.00	4.00	3.57	25.78	3.22	22.50	2.50	0.72	3.28
6	IG Dermicool-LAV	38.85	45.00	6.15	5.48	40.00	5.00	34.97	3.88	1.12	5.03
7	Livon silky potion	71.90	79.00	7.10	5.91	70.22	8.78	64.71	7.19	1.59	5.51
8	Dr.Lips	12.15	14.00	1.85	1.64	12.44	1.56	10.94	1.21	0.34	1.51
9	CDM 24.G	9.10	10.00	0.90	0.75	8.89	1.11	8.19	0.91	0.20	0.70
10	Fruit and nut 44.G	21.50	24.00	2.50	2.14	21.33	2.67	19.35	2.15	0.52	1.98
11	Cherry 40.G Black	22.32	25.00	2.68	2.31	22.22	2.78	20.09	2.23	0.55	2.13
12	Cherry liq tan 75ml	31.35	36.00	3.65	3.13	31.11	3.89	28.22	3.13	0.75	2.90
13	Quick wax black	27.25	30.00	2.75	2.30	26.67	3.33	24.53	2.72	0.61	2.14
14	Dettol	12.90	14.00	1.10	0.89	12.44	1.56	11.61	1.29	0.27	0.83

	soap										
15	D/liq soap pump	50.00	55.00	5.00	4.18	48.89	6.11	45.00	5.00	1.11	3.89
16	Dettol 200ml	24.50	25.37	0.87	0.49	22.55	2.82	22.05	2.45	0.37	0.50
17	Dispirin tablets	30.98	31.56	0.58	0.11	28.05	3.51	27.88	3.10	0.41	0.17
18	Mortein Rat killer	18.20	20.00	1.80	1.50	17.78	2.22	16.38	1.82	0.40	1.40
19	Harpic twin	71.45	80.00	8.55	7.35	71.11	8.89	64.31	7.14	1.74	6.81
20	Harpic 200ml	18.00	20.00	2.00	1.70	17.78	2.22	16.20	1.80	0.42	1.58
21	Lizol power-500ml	17.30	19.00	1.70	1.42	16.89	2.11	15.57	1.73	0.38	1.32
22	Whisper	102.68	115.00	12.32	10.60	102.22	12.78	92.41	10.27	2.51	9.81
23	Whisper Ultra	53.57	60.00	6.43	5.53	53.33	6.67	48.21	5.36	1.31	5.12

(By the Commissioner of Commercial Taxes, Government of Karnataka).