16-12-2014 VAT G.Vinay Bhargav kumar

Topic:- Concept of VAT and various meanings under VAT.

Concept of VAT :-

VAT works on the principle that when raw material passes through various manufacturing stages and manufactured product passes through various distribution stages, tax should be levied on the 'value Added' at each stage and not on the gross sales price. This ensures that same commodity does not get taxed again and again and there is no cascading effect. In simple terms, 'value Added' means difference between selling price and purchase price. VAT avoids cascading effect of a tax.

Basically, VAT is multi-point tax, with provision for granting setoff (Credit) of the tax paid at the earlier stage. Thus, tax burden is passed on when goods are sold. This process continues till goods are finally consumed. Hence, VAT is termed as 'Consumption type' tax. VAT works on the principle of 'tax Credit System'.

Meaning of Cascading effect:-

If a tax based on selling price of a product, the tax burden goes on increasing as raw material and final product passes from one stage to other. for Example,

$$A \xrightarrow[\text{i.e., } 100 + 10\% \text{ tax} = 110/-]{\text{supplies to 'B' at } 110/-} B \xrightarrow[\text{i.e., } 110+40 \text{ (conversion charges)}]{\text{supplies to 'C' at } 165/-} C$$

$= 150 + 10\%\ \text{tax} = 165/-$

In fact, 'value Added' by B is only 40/-, tax on which would have been only 4/-, while tax paid was 15/-. As stages of production and/or sales continues, each subsequent purchaser has to pay tax again and again on the material which has already suffered tax. This is called 'Cascading effect' or, snow ball effect'.

VAT avoids cascading effect of tax:-

System of VAT works on tax Credit method. In Tax Credit Method of VAT, the tax levied on full sale price, but Credit is given of tax paid on purchases. thus, effectively, tax levied only on 'value Added'.

In the said example, 'B' will purchase goods from 'A' @ 110/-, which is inclusive of tax of ₹10/-. Here, 'B' is going to get credit of tax of ₹10/-. He will charge conversion charges of ₹40/- and sells goods at ₹140/-. He will charge 10% tax and raise invoice of ₹154/- to 'C' (140/- + 10% tax). In the invoice prepared by 'B', the tax shown will be of ₹14/-. Thus, 'B' will be paid tax ₹4/- only i.e., 'B' is paying tax on the value added.

Principles for implementation of VAT

Principle of Origin / Source

- Country taxes only the value addition made to goods within its territory irrespective of the place in which or purpose for which such goods are consumed.

(Not accepted in India).

Principle of Destination / Consumption

→ Country taxes the value addition made to all those goods, which are consumed within its irrespective of the place in which such value addition was made.

(Accepted in India)

Variants of VAT

Gross product variant

Tax is levied on all sales
↓
Deduction allowed on all raw materials except capital goods.

Income variant

Tax is levied on all sales
↓
Deduction allowed on all raw materials and for Capital goods, only on the depreciation charged. ie, prorata basis.

Consumption variant

Tax is levied on all sales.
↓
Deduction allowed on all raw materials including capital goods.

Methods of Computation of VAT

Addition Method

Tax is levied on value addition only at every stage of sale.

Subtraction Method

Tax is levied at every stage of sale but tax is calculated only on value addition made.

ie, Taxable Turnover × $\frac{\text{Vat rate}}{100+\text{Vat}}$.

eg. (sales − purchases) × $\frac{5}{105}$

Invoice method / voucher method / Tax Credit method

Tax is levied at every stage of sale & tax is calculated on total sale value.

seller pay tax after deducting input.

ie,
a) Sale xxx
   VAT on sale xxx
b) Purchase xxx
   VAT on pur. xxx

(a − b) payment

Business:- Business includes –

→ any trade, commerce or, manufacture, or, any adventure or, concern in the natu of trade, commerce or, manufacture, whether or, not such trade, commerce ~~or~~ manufacture, adventure or, concern is carried on with a motive to gain or, profit and whether or, not any gain or, profit accrues from such trade, commerce, manufacture, adventure or, concern; and

→ any transaction in connection with or, incidental or, ancillary to, such trade, commerce, manufacture, adventure or, concern; and

→ any transaction in connection with the commencement or, incidental or, ancillar to the commencement or closure of such trade, commerce, manufacture, adventure or, concern;

Explanation: for the purpose of this clause:

i) the activities of raising of manmade forests or rearing of seedlings or plants shall be deemed to be business;

ii) any transaction of sale or purchase of capital goods pertaining to such trade, commerce, manufacture, adventure or concern shall be deemed to be business;

iii) A sale or, purchase whether by himself or through an agent of agricultural or horticultural produce grown by himself or, grown on any land whether as owner or tenant in the form not different from the one in which it was produced, save mere cleaning, grading or sorting does not constitute business.

Goods:- Goods defined as –

→ Goods means all kinds of movable property other than newspapers, actionable claims, stocks, shares and securities, and includes all materials, articles, commodities including the goods as goods or, in some other form, involved in execution of a works contract or those goods used or to be used in the construction, fitting out, improvement or repair of movable or immovable property and also includes all growing crops and things attached to or forming part of the land which are agreed to be servered before sale or under the contract of sale.

Different types of Goods

Future goods	Specific goods	Ascertained goods	Unascertained goods
Goods to be manufactured or produced or acquired by the seller after making the contract of sale.	Goods identified & agreed upon at the time of contract of sale are made.	Goods identified in accordance with the agreement after the time a contract of sale is made	Goods which are not identified & it is left to seller to apportion the goods out of his stock to the buyer

Sale:- 'sale' with all its grammatical variations and cognate expressions means every transfer of the property in goods (whether as such goods or in any other form in pursuance of a contract or otherwise) by one person to an other in course of trade or business, for cash, or for deferred payment, or for any other valuable consideration or in the supply or distribution of goods by a society (including co-operative society), club, firm or association to its members but does not include a mortgage, hypothecation or pledge of, or a charge on goods.

Dealer:- 'Dealer' means any person who carries on the business of buying, selling, supplying or distributing goods or delivering goods on hire purchase or on any system of payments by instalments, or carries on or executes any works contract involving supply or use of material directly or otherwise, whether for cash or for deferred payment, or for commission, remuneration or other valuable consideration, and includes:

→ a company, a HUF or any society including cooperative society, club, firm or association which carries on such business;

→ a society including a co-operative society, club, firm or association which buys goods from, or sells, supplies or distribute goods to its members;

→ a casual trader.

→ any person, who may, in the course of business of running a restaurant or an eating house or a hotel by whatever name called, sells or supplies by way of or as part of any service or in any other manner what so ever, of goods, being food or any other article for human consumption or any drink whether or not intoxicating;

→ any person, who may transfer the right to the use of any goods for any purpose whatsoever whether or not for a specified period in the Course of business to any other person;

→ a commission agent, a broker, a delcredere agent, an auctioneer or any other mercantile agent, by whatever name called, who carries on the busines of buying, selling or distributing goods on behalf of any principal or principal

TAX INVOICE :- A registered dealer, selling any goods, may issue to the purchaser a 'Tax invoice' containing the following particulars and retain a copy thereafter for three years from the end of the year in which sale took place:

→ 'TAX INVOICE' must appear in bold at top or, prominent place.
→ Name, address and registration number of selling dealer.
→ Name and address of the purchasing dealer.
→ Serial number and date.
→ Description, quantity and price of the goods sold.
→ The amount of tax charged is to be shown seperately.
→ Signed by the selling dealer or, a person authorised by him.

To claim input tax Credit, the purchaser must have tax invoice.