AEC

Service Tax & VAT

IMP Key Point

For CS – Executive / CA – IPCC / CWA – Intermediate (AY 2011-12)

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CA – IPCC / CS – Executive

SERVICE TAX (AY 2011-12)

IMP KEY POINTS

Exemption from Service Tax

(A) Small service providers providing aggregate services up to ₹ 10 lakhs are exempt from paying Service Tax.

(B) Even if the service provider crosses turnover of ₹ 10 lakhs in current year, he will be liable to Service Tax only on turnover exceeding ₹ 10 lakhs and not on entire turnover. However, if taxable turnover in current exceeds ₹ 10 lakhs, there will be no exemption from Service Tax in next financial year.

(C) There is no Service Tax on export of services, if service is exported

(D) Services provided to United Nations & International Agencies is exempt from Service Tax.

(E) All services provided to foreign diplomatic missions or consular posts in India are fully exempt provided services are used for their official purposes.

(F) Exemption from Service Tax has been provided to all taxable services provided by Reserve Bank of India

(G) Sometimes the gross amount of contract shall include the amount charged for services as well as some other facilities provided. In such case Service Tax is payable at lower rates, i.e. partial abatement is available from gross value.

Registration under Service Tax

(A) No registration is required till turnover exceeds ₹ 9 lakhs.

(B) Time limit to apply for registration is 30 days from the levy of Service Tax or start of the business as the case may be.

(C) Registration is provided in 7 days and if not then deemed to have been provided after 7th day.

(D) No document except PAN issued by the income tax dept. is required.

(E) Service Tax registration no is 15 digits alphanumerical no.

(F) Rules for centralized registration and non-centralized registration exist.

(G) In case of more than 1 service, single registration covering all services is done.

Payment of Service Tax

(A) Service Tax is payable at the time of realization of the amount for services from the client.

(B) Service Tax is payable on the advance money received.

(C) Where there is short recovery of the billed amount, service provider should revise the bill otherwise he shall be liable to pay Service Tax on the full amount which has been billed to service receiver.

(D) Where there is excess recovery from a client or customer then such excess amount can be refunded to such client or customer

Due dates for the payment of Service Tax

(A) If the assessee is an individual or proprietary firm or partnership firm, the Service Tax shall be paid to the Central Government by the 5th of the next month immediately following the quarter in which the payments are received, towards the value of taxable services. **In case e-payment is made, due date is 6th.**

(B) In all other cases Service Tax received during any calendar month shall be paid to the Central Government by the 5th of the month immediately following the calendar month in which payments are received, towards value of taxable services. **In case e-payment is made, due date is 6th.**

(C) If the Service Tax on the value of taxable services is received during the month of March, or the quarter ending in March, as the case may be, shall be paid to the Government by the 31st day of March of the calendar year.

Service Tax To Be Paid Electronically: Where the assessee has paid Service Tax of ₹ 50 lakhs or more during the preceeding financial year or has already paid Service Tax of ₹ 50 lakhs in current financial year, he shall deposit the Service Tax liable to be paid by him electronically, through internet banking.

Special provision for the payment of Service Tax in case of life insurance business: An insurer carrying on life insurance business who is liable for paying Service Tax has the option to pay an amount calculated @ 1% + 2% EC + 1% SHEC of the gross amount of premium charged by him towards the discharge of his Service Tax liability instead of paying Service Tax @ 10% + 2% EC + 1% SHEC.

Special Rate for Payment of Service Tax:

- **Air Travel Agent – 0.618%** + 2% EC + 1% SHEC **of basic for domestic** & **1.236%** + 2% EC + 1% SHEC of **international fare**.
- **Money Changer – 0.25%** + 2% EC + 1% SHEC.
- **Works Contract Service – 4%** + 2% EC + 1% SHEC
- **Games of Chance Service - ₹ 6,000/₹ 9,000 on every ₹ 10 lakh or part thereof.**

Service Tax return shall be submitted on half yearly basis on 25th October and 25th April every year.

Service Tax return can be revised within 90 days from filling of original return.

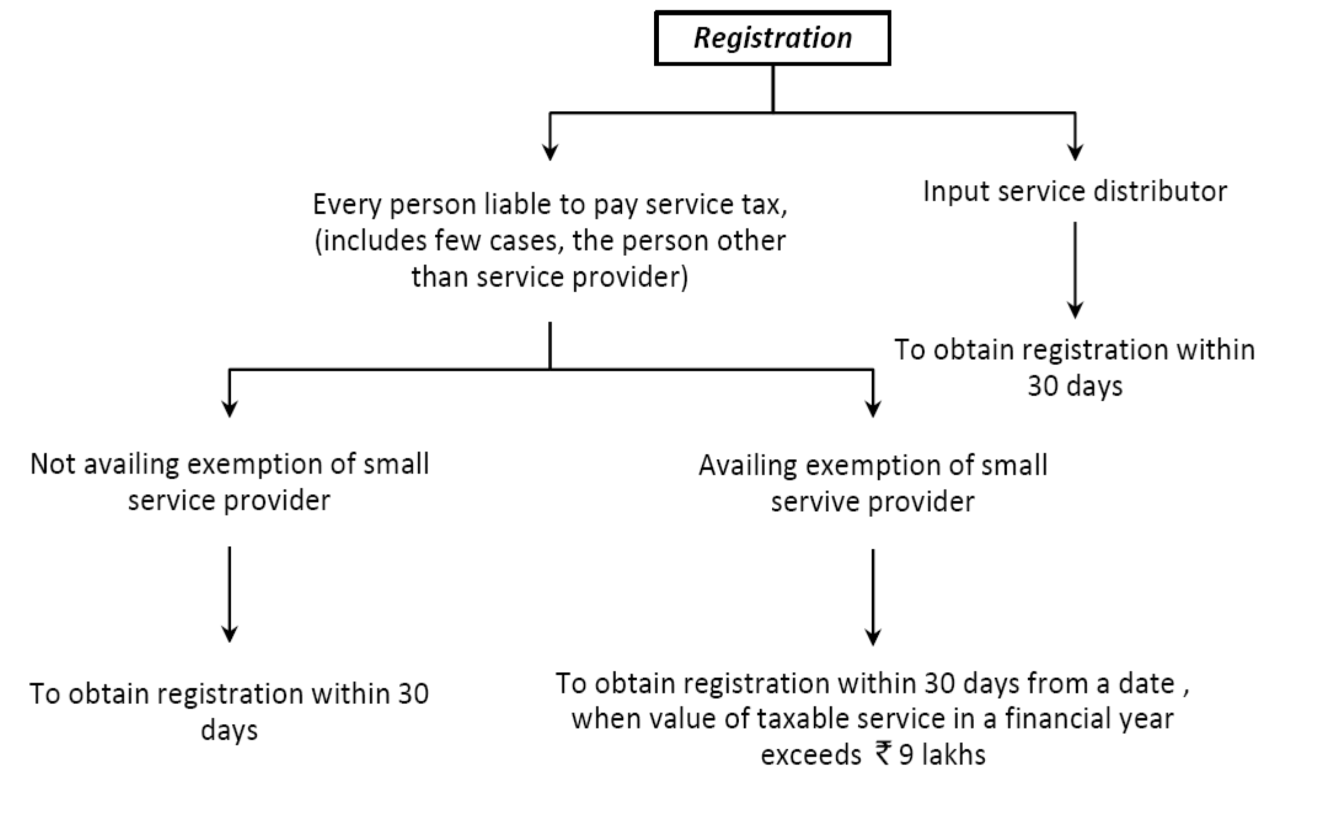
Belated Service Tax return is also allowed upon the payment of prescribed fees which is as follows:

1. If delay is up to 15 days from the due date of return: Fess of ₹ 500 is to be paid.
2. If delay is beyond 15 days but up to 30 days from due date: Fees of ₹ 1000 is to be paid.

If delay is beyond 30 days from the due date: Fees of ₹ 1000 is to be paid + ₹ 100 for every day from the 31st day tills the date of furnishing of return but subject to the maximum of ₹ 2000.

INFORMATION CAN BE USEFUL FOR PRACTICAL QUESTIONS

Registration



Payment of Service Tax

Payment of Service Tax

- Individual, proprietory firms or Partnership firms
  - 5th of the month immediately after the said quarter.

    (1 day grace, in the case of e-payment)

    (In the last quarter due date is 31st March, No Grace)
- Others
  - 5th of the month immediately following the said calender month.

    (1 day grace, in the case of e-payment)

    (In the last quarter due date is 31st March, No Grace)

Note: *E-payment is compulsory for all persons, if service tax exceeds ₹ 50 lakhs in the previous year or in the current year.*

Value of Taxable Services

Value of Taxable Services

- Consideration is in money only.
  - Then, above amount is value ***[Section 67(1)(i)]***
- Consideration is not whole in money.
  - Then, value is money charged + other consideration ***[Section 67(1)(ii)]***
- Consideration is not ascertainable.
  - Valuation rules
    - Value of similar services to be determined by service provider ***[Rule 3(a)]***
    - Value of similar services is not available
      - Equivalent value of consideration to be determined by service provider on Costing Principal ***[Rule 3(b)]***

Note: *Rule 4 & 5 should be kept in mind while deciding the value*

PRACTICAL QUESTIONS

Q.1: (Based on registration) *Discuss whether the following person are liable to apply for registration under Service Tax law and if yes; by which date:*

(a) *A provider of taxable service, whose aggregate value of taxable services is ₹ 8, 80,000 upto 31-3-2010*

(b) *A provider of taxable service, whose aggregate value of taxable services is ₹ 9,10 000 upto 1-1 -2010*

(c) *A provider of taxable service, who has provided services as follows:*
Aggregate value of services upto 15-5-2009 (i.e. before the service became taxable) ₹ 5,00,000
Aggregate value of taxable services from 16-5-2009 to 31-3-2010 ₹ 8,95,000

(d) *An input service distributor who start his business w. e. f. 1-1-2010*

(e) *A provider of taxable service who starts his business w. e. f. 11-8-2009 and whose aggregate value of services as on 10-10-2009 becomes ₹ 9,02,000*

Solution:

(a) Not liable for registration, as aggregate value of taxable services doesn't exceed ₹ 9,00,000

(b) Liable for registration, application to be made up to 31-1-2010

(c) Not liable for registration, as aggregate value of taxable service doesn't exceed ₹ 9,00,000

(d) Liable for registration, application to be made up to 31-1-2010

(e) Liable for registration, application to be made up to 9-11-2009

Q.2: (Payment of Service Tax) *Mr. X, a Chartered Accountant, raised an invoice for ₹ 27,575 (25,000 + 2575 Service Tax) to a client on 20-1-2010. Client, however, as paid a lump sum of ₹ 26,000 on 28-4-2010 for full and final settlement-*

(a) *How much Service Tax Mr. X has to pay and when does this tax becomes due for payment?*

(b) *What will be his liability, if client refuse to pay Service Tax and pays only ₹ 25,000 in total?*

Solution:

(a) $\text{Service Tax} = 26{,}000 \times \frac{10.30}{110.30} = \boxed{₹\ 2{,}428}$ (approx.) which payable by 5th July 2010

(b) $\text{Liability} = 25{,}000 \times \frac{10.30}{110.30} = \boxed{₹\ 2.335}$

Q.3: (Due date of payment of Service Tax) *Mr. Y is consulting engineer raised a bill of ₹ 2,20,600 (including Service Tax) on his client for consulting services rendered by him in the month of June 2009. A partial payment of ₹ 1,65,450 was received by him in the month of March 2010. Compute the Service Tax amount payable by Mr. Y and due date by which Service Tax can be deposited.*

Solution:

Service Tax is payable only when the value thereof has been received. Since only part of the value has been received in March, 2010, the amount so received shall be deemed to include proportionate element of

$\text{Service Tax} = 1{,}65{,}450 \times \frac{10.30}{110.30} = \boxed{₹\ 15{,}450}$.

The amount of Service Tax is required to be deposited with central government by 31st March, 2010 for the month/quarter ending 31st March, 2010.

Q.4: (Payment of Service Tax/Due dates) *Give due dates for payment of Service Tax in following cases:*

(a) *M/s. Sanghvi & Co., a sole-proprietorship concern, receives payment of services provided in July 2009 partly on 8th August 2008, partly on 1st January and balance on 25th April 2009.*

(b) *M/s. Thakur-Macwan & Co., a partnership concern, receives a payment of services provided in April 2009 on 28th February 2010*

(c) *M/s. Shah Ltd., a company, receives payment of services provided in April 2009 on 28th February 2010*

Solution:

(a)

Payment Received on	Due Dated
8th August 2008	5th October 2008
1st January 2009	31st March 2009
25th April 2009	5th July 2009

(b) 31st March 2010

(c) 5th March 2010

Q.5: (Interest on delay in payment of Service Tax) *Macwan Engineering Ltd. deposited the Service Tax in the month of May, 2009 by cheque in the designated bank on 5th June 2009 and it is cleared on 8th June, 2009. The Service Tax has a notice to the company under Section 75 of Chapter V of Finance Act, 1994 demanding interest for the delayed period. Is demand justified?*

Solution:

Payment has been made by due date. Demand is unjustified.

Q.6: (Small service provider exemption) *The value of taxable services provided by Mr. Kamdar during the financial year 2008-09 was ₹ 9 lakhs. During the financial year 2009-10 (upto January 2010), Mr. Kamdar provides taxable services valuing ₹ 10 lakhs but receives payment towards taxable services valuing ₹ 11 lakhs. No taxable services provided during February to March 2010. Compute the amount of Service Tax payable by him. Will he get any exemption in the Financial Year 2010-11?*

Solution:

Since the value of taxable services provided in financial year 2008-09 was not exceeding ₹ 10 lakhs, Mr. Kamdar would get exemption in Financial Year 2009-10 in respect of aggregate value not exceeding ₹ 10 lakhs.

Hence, Service Tax payable= ₹ (11 lakh-10 lakh) $\times$ 10.30% = $\boxed{\text{₹ 10,300}}$

He will be eligible for exemption in the financial year 2010-11, as the value of taxable services provided in the financial year 2009-10 does not exceed ₹ 10 lakhs.

Q.7: (Small service provider exemption) *Arihant Ltd. provided services valuing ₹ 8 lakhs during the financial year 2008-09. During financial year 2009-10, it has provided taxable services valuing ₹ 10 lakhs and has received payment towards taxable services ₹ 8.5 lakh. It also received services in the nature of transport of goods by road valuing ₹ 50,000, in respect of which it is the person liable to pay Service Tax. Compute the amount of Service Tax, of any, payable by Arihant Ltd. for financial year 2009-10. It is given that goods transport service is exempt to the extent of 75% of value thereof.*

Solution:

Arihant Ltd. is eligible for small service provider exemption during the financial year 2009-10 as the value of taxable services provided during financial year 2009-10 does not exceeds ₹ 10 lakhs.

For the value of taxable services received during the financial year 2009-10, no tax liability would arise, as payment received do not exceeds ₹ 10 lakhs. However, for goods transport agency services received, in respect of which Arihant Ltd. is the person to pay Service Tax, the company cannot claim small service provider exemption. Therefore, it will have to pay Service Tax payable= ₹ 50,000 $\times$ 25% $\times$ 10.30% = $\boxed{\text{₹ 1,288}}$

Q.8: (Value of taxable services) *M/s. Shah Consultant is a labour contractor of manpower to M/s. Sanghvi Creation. They charged to the principal employer for the wages of their labour which amounts to ₹ 1,20,000 plus their service charges of ₹ 12,000 for arranging the labour. The issue is whether service is taxable on the gross amount charged by them or only their charges for labour.*

Solution:

As per **Section 67**, the value of taxable service is the gross amount charged by the service provider for the provision of service. Hence, the value of taxable service in this case = ₹ 1,20,000 + ₹ 12,000 = $\boxed{\text{₹ 1,32,000}}$.

Q.9: (Value of taxable services) *Answer the following for services provided in January, 2010:*

(a) *Bhavin contracts with Mohit, a real estate agent to sell his house and thereupon Mohit gives an advertisement in television costing ₹ 5 lakhs. Mohit billed ₹ 15 lakhs to Bhavin including charges of television advertisement, showing separately in invoice. Mr. Mohit says that value of taxable services in his case is ₹ 10 lakhs only, as acted as pure agent of Mr. Bhavin while taking advertisement. Compute Service Tax to be billed.*

(b) *In the course of providing a taxable service, a service provider incurs cost such as travelling expences, postage, telephone, etc. to the tune of ₹ 20,000. He charged ₹ 80,000 for his services and indicates the said cost separately on the invoice issued to the recipient of service. Compute the amount of Service Tax to be billed by the service provider.*

(c) *Amit contracts with Burhan, an architect for building a house and Burhan's fees is fixed at ₹ 3,00,000. During the course of providing the taxable service, Burhan incurs expenses such as telephone charges, air travel tickets, hotel accommodation, etc. ₹ 50,000 to enable him to effectively perform the provision of service to Amit. Compute the Service Tax liability for Burhan.*

(d) *Anuj, a clearing and forwarding agent charges ₹ 50,000 for his services, which incurs octroi charges ₹10,000 paid on behalf of his client. Compute the Service Tax liability.*

(e) *A cable operator charges ₹ 10,000 for his services, which includes Entertainment Tax ₹ 2,000 paid on behalf of his client. Compute the value of taxable services and Service Tax liability.*

Solution:

(a) Since advertisement service is an input service for the estate agent in order to enable or facilitate him to perform his services as an estate agent. Hence, Mr. Mohit does not act as agent of Mr. Bhavin in taking advertisement. Hence, $\text{Service Tax} = ₹\ 15 \text{ lakhs} \times 25\% \times 10.30\% = \boxed{₹\ 1,54,500}$

(b) In this case, the service provider is not acting as an agent for recipient of service but procures such inputs or input service on his own account for providing taxable services. Such expenses do not become reimbursable expenditure merely because they are indicated separately in invoice issued by service provider to recipient of service.

Hence, $\text{Service Tax payable} = ₹\ (80,000 + 20,000) \times 10.30\% = \boxed{₹\ 1,288}$

(c) $\text{Value of taxable service} = ₹\ 3,00,000 + ₹\ 50,000 = ₹\ 3,50,000$ and $\text{Service Tax @10.30\%} = \boxed{₹\ 36,050}$

(d) Anuj (the clearing and forwarding agent) act as pure agent of the client while providing octroi charges.

Hence, $\text{Value of taxable service} = ₹\ (50,000 - 10,000) = ₹\ 40,000$ and $\text{Service Tax @10.30\%} = \boxed{₹\ 4,120}$

(e) A cable operator acts as pure agent to the client while paying Entertainment Tax.

Hence, $\text{Value of taxable service} = ₹\ (10,000 - 2,000) = ₹\ 8,000$ and $\text{Service Tax @10.30\%} = \boxed{₹\ 824}$

Q.10: (Pure agent) *Mr. Anvesh, a custom house agent, charges ₹ 1,00,000 from his client. This sum includes ₹ 10,000 towards payment of custom duty on behalf of the client. Compute the service tax to be charged from his client.*

Solution:

Expenses incurred by the service provider (here Mr. Anvesh) in his capacity as pure agent do not form part of the value of taxable services. Hence, Mr. Anvesh (custom house agent) has paid ₹ 10,000 towards custom duty on behalf of the client, while expenditure incurred by Mr. Anvesh in his capacity as 'Pure Agent'. Since, the sum of ₹ 10,000 does not include any element of profit, the same will not form part of the value of taxable service.

Hence, $\text{Value of taxable service} = ₹\ (1,00,000 - 10,000) = \boxed{₹\ 90,000}$

$\text{Service Tax to be charged} = ₹\ 90,000 \times 10.30\% = \boxed{₹\ 9,270}$

Q.11: (Gross amount charged and value of taxable service) *Hotel Nilkanth Palace charges 10% of amount as service charges and the Department has asked them to pay service tax on it. The assessee has submitted that the amount at 10% collected from the costumers is subsequently disbursed among the staff. Therefore, it is not part of their income and cannot be included in gross amount charged by them. Examine this care and advice.*

Solution:

As per **Section 67**, the value of taxable service is the gross amount charged by the service provider for the taxable services or to be provided by him. Since the assessee was charging service tax @ 10% of bill amount from its customers for providing the services, therefore the said amount was liable to be included in the gross amount charged.

Therefore, service charges @ 10% of bill amount charged by Hotel Nilkanth Palace are included in gross amount charged by them and will be liable to service tax.

Q.12: (Value of taxable services) *A beauty parlour charges ₹ 1,00,000 from a client for providing beaut treatment service, the break-up of the bill is as follows:*

Labour and facility charges	*₹ 60,000*
Value of cosmetics and toilet preparations consumed in providing the services	*₹ 30,000*
Value of cosmetics and toilet preparations sold to the client	*₹ 10,000*
Total	*₹ 1,00,000*

Compute the amount of Service Tax to be charged from the client.

Solution:

The labour and facility charges are liable to Service Tax. The value of cosmetics and toilet preparations consumed in providing the services are forms intrinsic part of the value of service. The materials consumed during the provision of service form part of the cost of that service. Hence, the value of consumed materials will be included in the value of Service.

However, the value of cosmetics and toilet preparations sold to the client will be exempt.

$$\text{Hence, Value of taxable service} = ₹\ (60{,}000 + 30{,}000) = \boxed{₹\ 90{,}000}$$

$$\text{Service Tax to be charged} = ₹\ 90{,}000 \times 10.30\% = \boxed{₹\ 9{,}270}$$

Q.13: (Computation of taxable value and service tax – Exemption and Advance receipts)

B.I. Professionals, a partnership firm, gives the following particulars relating to the service provided to various clients by them for the half-year ended on 30-9-2009:

(1) Total bills raised for ₹ 8,75,000 out of which bill for ₹ 75,000 was raised on an approved international organization and payments of bills for ₹ 1,00,000 were not, received till 30-9-2009.

(2) Amount of ₹ 50,000 was received as an advance from MM Ltd. on 25-9-2009 to whom the services were to be provided in October, 2009

You are required to work out the:

(a) Taxable value of services

(b) Amount of service tax

Solution:

(a) Assume that bill amount is exclusive of service tax.

$$\begin{aligned}\text{Taxable vaue of services} = \ & \text{Bill amount} \\ & - \text{Exemption in respect of service provided to International Organization} \\ & - \text{Amount not received (not liable to service tax)} \\ & + \text{Amount recieved in advance (liable for Service tax)} \\ = \ & ₹\ (8{,}75{,}000 - 75{,}000 - 1{,}00{,}000 + 50{,}000) = \boxed{₹\ 7{,}50{,}000}\end{aligned}$$

(b) $\text{Accordingly, Service Tax to be charged} = ₹\ 7{,}50{,}000 \times 10.30\% = \boxed{₹\ 77{,}250}$

CA – IPCC / CS – Executive

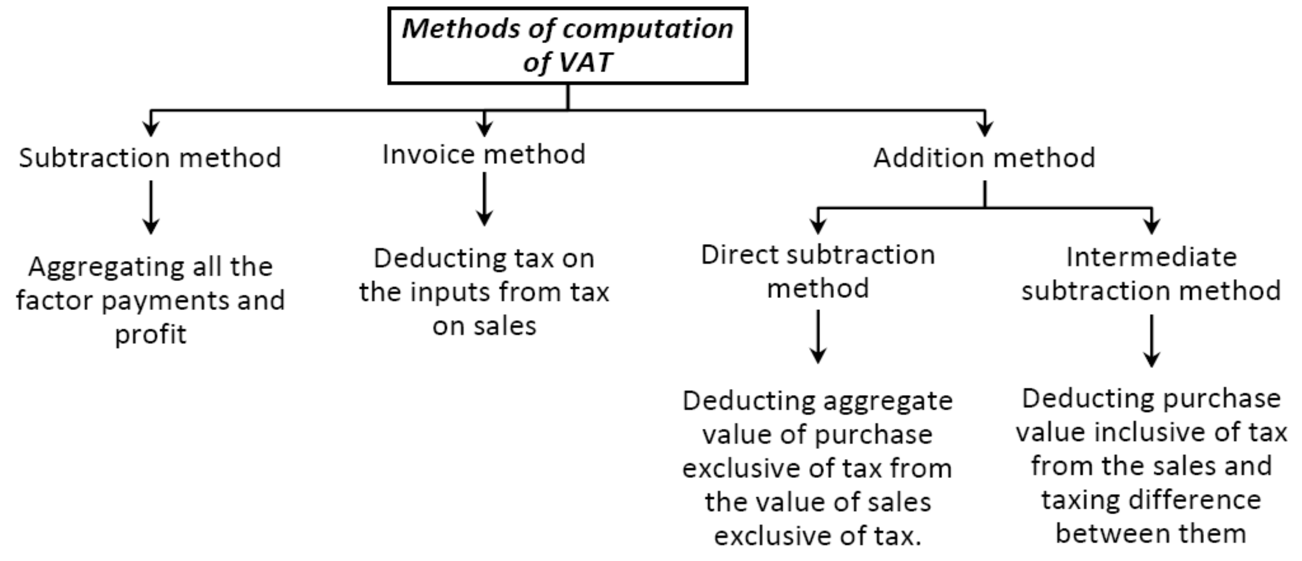
VAT (AY 2011-12)

IMP KEY POINTS

VAT- at a glance
1) Under the system of VAT the sales tax levied and collected at each stage of sale only the value added at every stage. 2) As commonly understood this is a method by which final consumer shall be taxed at different stages of production and distribution in various installments. For this difference between the sale price and purchase price is taken as value added and a tax is imposed at every level where there is some value addition. 3) **Need for VAT in India** ***(a)*** Avoids distortions in the economy due to uniformity all across the channel. ***(b)*** Prevents cascading effect (multiple-taxation) by providing credit of Input taxation. ***(c)*** VAT is just and logical way of taxing all dealers in equitable manner whereby all dealers share burden of tax. ***(d)*** This system leads to easy computation and compliance. ***(e)*** Credit of input taxation leads to cost efficiency. **4) Merits of VAT** ***(a)*** Eliminates multiple-taxation. ***(b)*** No tax evasion. ***(c)*** Simple method. ***(d)*** Lowering tax burden. ***(e)*** Transparency ***(f)*** Better revenue collection and stability. ***(g)*** Better accounting systems. **5) Demerits of VAT** ***(a)*** VAT does not cover services. ***(b)*** Non integration of central VAT with state-VAT. ***(c)*** Accounting burden. ***(d)*** Cost of administration for government. ***(e)*** Exemptions on goods. **6) Concept of input tax credit:** The main feature of system of VAT is that it provides the benefit of set off of input tax from the main output tax. The value added tax is based on the value addition to the goods, and the related VAT liability of the dealer is calculated by deducting input tax credit from the tax collected on sales during a particular period. 1) **Variants of VAT:** VAT could be levied under three variants. Gross product variant, Income variant, Consumption variant. These variants could be further distinguished according to their methods of calculation and they are addition method and subtraction method. The subtraction method could be further divided into direct subtraction method, intermediate subtraction method, and indirect subtraction method. **Methods for computation of VAT:** VAT is form of a sales tax and is charged at each stage on the 'Value Added' to the goods. 'Value Added' is the difference sales and purchases of the business. There are several methods to calculate the 'Value Added' to the goods for levy of tax. The three commonly used methods are addition method, invoice method (tax credit method) and subtraction method.

INFORMATION CAN BE USEFUL FOR PRACTICAL QUESTIONS

Methods of computation of VAT



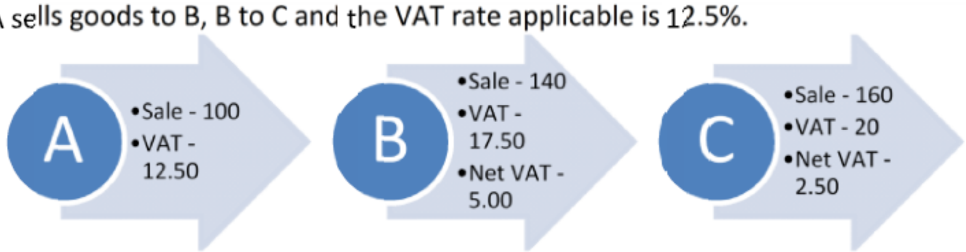
VAT – Concept and General Principles

Basic Concepts

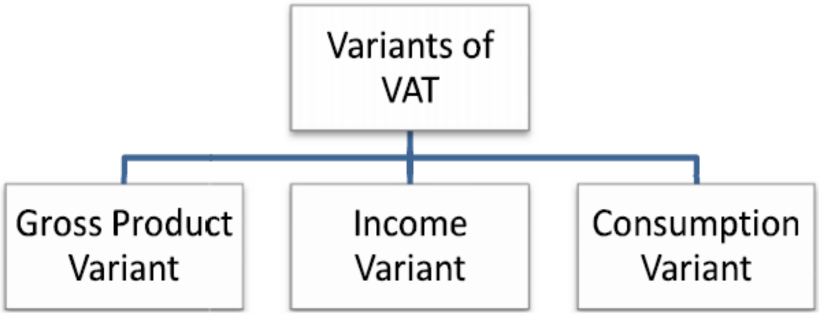
- Value-Added-Tax or VAT is multi-stage indirect tax levied on sale of goods.
- The concept of VAT is taxing only the value addition on goods.
- VAT was first introduced in 1954 in France on wholesale goods and by 1994, the concept was implemented in most of the European and Asian countries.
- India introduced VAT in excise by the name of modified VAT (MODVAT) in 1986 on selected commodities. Thereafter, concept of credit of tax was introduced in service tax in 2002. In year 2004, inter-sectoral credit was introduced whereby credit of duty paid on inputs including capital goods was allowed for payment of service tax and vice-versa. In 2005, VAT was introduced as a replacement of existing sales tax law by almost all the states.
- VAT structure has been evolved on the basis of consensus amongst States. In order to bring in uniformity in VAT a committee of State Finance Ministers was formed. The committee brought out a White Paper and recognized that VAT is a state subject. The states have the freedom to prepare rules for VAT for their respective states but they shall be consistent with the overall structure and recommendations of the committee.

Multi-Stage Taxation

- VAT is a tax levied on the value added to any product at every stage of production or distribution.
- However, provision is made for input tax credit tax in respect of tax paid at the previous point of purchase.
- The total tax charged at various stages is ultimately borne by the end-customer.
- ***Example*** – A sells goods to B, B to C and the VAT rate applicable is 12.5%.



Variants of VAT



Gross Product Variant

- The gross product variant allows deductions for taxes on all purchases of raw materials and components, but no deduction is allowed for taxes on capital inputs. That is, taxes on capital goods such as plant and machinery are not deductible from the tax base in the year of purchase and tax on the depreciated part of the plant and machinery is not deductible in the subsequent years. Capital goods carry a heavier tax burden as they are taxed twice. Modernization and upgrading of plant and machinery is delayed due to this double tax treatment.

Income Variant

- Income variant of VAT on the other hand allows for deductions on purchases of raw materials and components as well as depreciation on capital goods. This method provides incentives to classify purchases as current expenditure to claim set-off. In practice, however, there are many difficulties connected with the specification of any method of measuring depreciation, which basically depends on the life of an asset as well as on the rate of inflation.

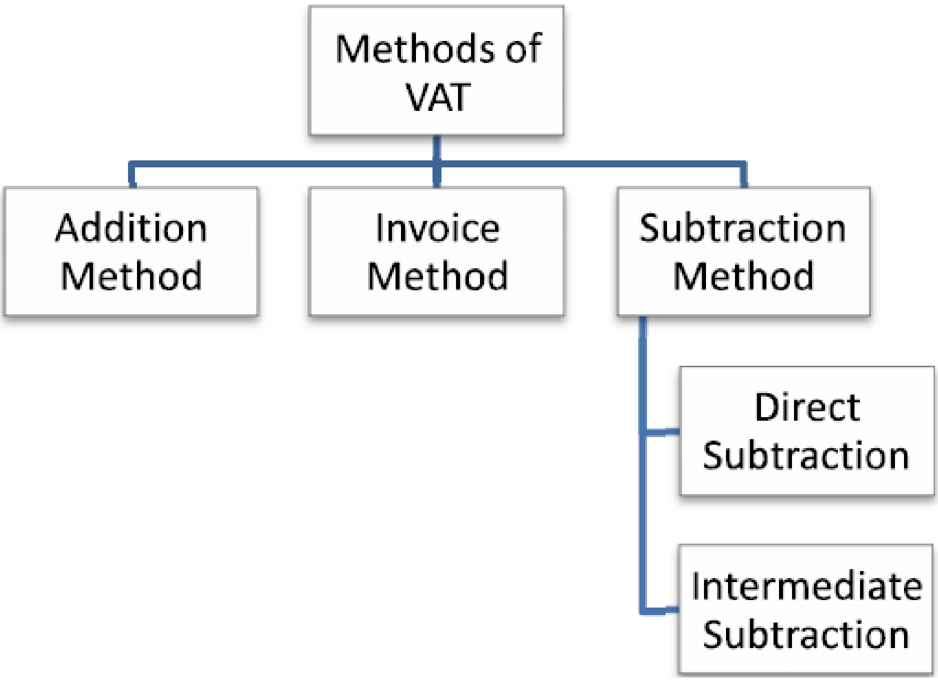
Consumption Variant

- Consumption of VAT allows for deduction on all business purchases including capital assets. Thus, gross investment is deductible in calculating value added. It neither distinguishes between capital and current expenditures nor specifies the life of assets or depreciation allowances for different assets. This form is neutral between the methods of production; there will be no effect on tax liability due to the method of production (i.e. substituting capital for labour or vice versa). The tax is also neutral between the decision to save or consume.

Best Variant

- Among the three variants of VAT, the consumption variant is widely used.
- The reasons for preference of this variant are:-
  - (i) The consumption variant is a tax-neutral system and it does not affect decisions regarding investment (labour intensive or capital intensive) because the tax on capital goods is also set-off against the VAT liability.
  - (ii) The consumption variant is convenient from the point of administrative expediency as it simplifies tax administration by obviating the need to distinguish between purchases of intermediate and capital goods on the one hand and consumption goods on the other hand.
  - (iii) Consumption variance does not distinguish between goods and services. Since the business gets set-off for the tax on services, it does not cause any cascading effect.

Methods of VAT



Input and Output Tax

Meaning of Input Tax and Output Tax

- **Input Tax** – Input tax is the tax paid or payable in the course of business on purchases of any goods made from a registered dealer within the State.
- In simple words input tax is the tax a dealer pays on his local purchases of business inputs, which include the goods that he purchases for resale, raw materials, capital goods as well as other inputs for use directly or indirectly in his business i.e. consumables.
- **Output Tax –** Output tax means the tax charged or chargeable under the Act, by a registered dealer for the sale of goods in the course of business.
- Output tax is the tax that a dealer charges on his sales that are subject to tax.

Input Tax Credit or VAT Credit

- Input tax credit means, credit available on the purchases made by dealer. Credit of VAT paid will be available only on purchases made within the State.
- Input tax credit is available only to VAT registered dealer on purchases made from another VAT registered dealer against a valid VAT invoice.
- Purchases include raw material, consumables, packing material and capital goods.
- Input tax credit is available to both manufacturers and traders for purchase of inputs/supplies meant for both sales within the State as well as to other States.
- In certain cases, it is possible that the output tax rate is zero either because the final product is either exempted or subject to 'zero rate' of tax. It may be noted that while input tax credit is not available if the final product is exempted. However, in case of 'zero rated sale', credit is available on tax paid on inputs.
- For example, sales tax is not payable on export sales, credit will be available of tax paid on inputs.

Utilization of VAT Credit

- Input tax credit of VAT is utilized as follows:-
  (i) VAT payable on Finished Goods
  (ii) CST payable on Inter State Sales
  (iii) Any interest or penalty under VAT
- Therefore, VAT payable = Output tax – Input Tax credit.
- In other words, out of the tax charged on sales, a deduction shall be first made in respect of tax charged on purchases and only the balance is payable to Government.

Input Tax Credit on Capital goods

- Input tax credit is available on Capital goods and the same is to be adjusted over a period of 36 monthly instalments (3 years).
- The States may at their option reduce this number of instalments.
- For example, Maharashtra has decided to give full input tax credit in the month of purchases only. However, if the capital asset is sold within the period of 36 months proportionate input credit will be withdrawn.
- There is a negative list for capital goods (on the basis of principles already decided by the Empowered Committee) not eligible for input tax credit.

Example – 1

X purchases input worth Rs. 1,00,000 in a month and his sales are worth Rs. 2,00,000 in the same month. All purchases and sales are made within the same state. The purchases are subject to input tax rate @ 4% and the sales are subject to output tax rate @ 12.5%. The input tax credit/set-off and calculation of VAT will be as shown below:-

(a) Input purchased within the month : Rs. 1,00,000/-
(b) Output sold in the month : Rs. 2,00,000/-
(c) Input tax credit = Input tax paid : Rs. 4,000/-
(d) Output tax payable : Rs. 25,000/-
(e) VAT payable during the month after set-off/input tax credit [(d) – (c)]: Rs. 21,000/-

Example – 2

X purchases input worth Rs. 80,000 in a month from registered dealers within the same State and the same are subject to VAT rate of 12.50%. He makes total sales of Rs. 4,87,500 out of which Rs. 1,12,500 is made within the same state, the rest being inter-state sales. The sales are subject to 4% CST as well as 4% VAT.
The input tax credit/set-off and calculation of VAT will be as shown below:-

(a) Input tax credit = Input tax paid : Rs. 10,000/-
(b) Output tax payable : Rs. 4,500/-
(c) CST payable: Rs. 15,000/-
(d) VAT payable during the month after set-off/input tax credit [(b) – (a)]: 4,500 – 4,500 = NIL
(e) Excess credit available = Rs. 5,500/-
(f) CST payable after set-off of excess credit = 15,000 – 5,500 = Rs. 9,500/-

Example – 3

Assume in Example – 2, X only makes a sale of Rs. 1,00,000 and that too within the State only which is subject to VAT @ 4%.
The input tax credit/set-off and calculation of VAT will be as shown below:-

(a) Input tax credit = Input tax paid : Rs. 10,000/-
(b) Output tax payable : Rs. 4,000/-
(c) VAT payable during the month after set-off/input tax credit [(b) – (a)]: 4,000 – 4,000 = NIL
(d) Excess credit available = Rs. 6,000/-

This excess credit is eligible to be carried forward and adjusted against the VAT payable of subsequent months.

Purchases eligible for availing Input Tax Credit

Purpose of purchase of goods

For the purpose of claiming input tax credit, the taxable goods should be purchased for any one of the following purposes:

(i) For sale/resale with in state or outside state;
(ii) As raw material or packing material or consumables for manufacture/packing of goods for sale inside state or outside state;
(iii) For being used in execution of works contract;
(iv) As capital goods required for the purpose of manufacture or resale of taxable goods;
(v) As raw material or capital goods or packing material or consumables for manufacture/packing of goods for sale outside India (Exports)

VAT Procedures

Registration

- Any dealer, who intends to carry on the business of purchase and sale of goods in the State and is liable to pay tax, cannot carry on the business unless he is registered and holds a valid registration certificate under the state VAT Act.
- Registration is the process of obtaining certificate of registration (RC) from VAT authorities.
- A dealer registered under the VAT Acts is called a registered dealer.
- All existing dealers who are registered under existing state tax laws are automatically registered under VAT.
- New dealers are required to register after VAT is implemented immediately on crossing the basic threshold limit.

Eligibility for registration

Threshold Limits for registration under VAT:-

(i) Turnover upto Rs. 10 lakh – No VAT registration required.
(ii) Turnover Rs. 5-50 lakh – Registration required but can opt for composition at lower rate up to 0.25% (Only for retailers).
(iii) Turnover above Rs. 50 lakh – Mandatory registration

Compulsory registration

- If an assessee fails to obtain registration under the VAT Act, he may be registered compulsorily by the Commissioner.
- The Commissioner may assess the tax due from such person on the basis of evidence available with him. In this event the assessee shall have to forthwith pay such amount of tax.
- Further, failure to get registered shall result in attracting default penalty and forfeiture of eligibility to set off all input tax credit related to the period prior to the compulsory registration.

Voluntary registration

- A dealer otherwise not eligible for registration may also obtain registration if the Commissioner is satisfied that the business of the applicant requires registration.
- The Commissioner may also impose any terms or conditions that he thinks fit.

Cancellation of registration

- The registration can be cancelled on:
  (i) discontinuance of business; or
  (ii) disposal of business; or
  (iii) transfer of business to a new location; or
  (iv) annual turnover of a manufacturer or a trader dealing in designated goods or services falling below the specified amount.
- The dealer is required to inform the Commissioner regarding cancellation of registration, surrender the original Registration Certificate and pay taxes due till the date of cancellation.

Tax Payers Identification Number (TIN)

- TIN will be allotted all registered dealers.
- It will be a 11 digit numerical code.
- First two digits will indicate State Code.

Questions from Previous Examinations

Concept and General Principles of VAT

1. Which is the most popular and common method for computing VAT liability and at what stage is the tax imposed? (2 Marks) (**May, 2007**)
2. Is it correct to state that VAT usually increases the retail price, as the tax is payable on the first sale price? (2 Marks) (**May, 2007**)
3. Briefly explain the invoice method of computing tax liability under the VAT system. What are its other names? (3 Marks) (**Nov, 2007**)
4. What are the different variants of VAT and how is deduction available for tax paid on inputs including capital inputs? (3 Marks) (**Nov, 2007**)
5. Does the VAT system bring certainty to a great extent? (2 Marks) (**Nov, 2007**)
6. Can VAT be said to be non-beneficial as compared to single stage-last point system? (2 Marks) (**Nov, 2007**)
7. Briefly explain the income variant of VAT. (2 Marks) (**May, 2008**)
8. What is the demerit of VAT from the view point that it is a form of consumption tax? (2 Marks) (**May, 2008**)
9. What are the different stages of VAT? Can it be said that the entire burden falls on the final consumer? (3 Marks) (**May, 2008**)
10. Briefly explain how VAT helps in checking tax evasion and in achieving neutrality. (3 Marks) (**May, 2008**)
11. Can we say that levy of VAT will have effect on retail price of goods? (2 Marks) (**Nov, 2008**)
12. Discuss the word "transparency" in the context of VAT system. (2 Marks) (**June, 2009**)
13. How can an auditor play a role to ensure that the tax payers discharge their tax liability properly under the VAT system? (3 Marks) (**June, 2009**)
14. Discuss the 'subtraction method' for computation of VAT. (3 Marks) (**June, 2009**)
15. VAT would increase the working capital requirements and the interest burden. Discuss. (3 Marks) (**Nov, 2009**)
16. What are the different stages of VAT? Can it be said that entire burden falls on the final consumer? (3 Marks) (**Nov, 2009**)
17. Briefly explain the income variant of VAT. (2 Marks) (**Nov, 2009**)
18. What are three variants of VAT? Which of these methods is most widely used and why? (3 Marks) (**May, 2010**)
19. Do you agree with the statement that 'Tax cannot be evaded under VAT system'? (2 Marks)(**May, 2010**)
20. What are the items aggregated in the Addition method to calculate the VAT payable? When is this method mainly used? (2 marks)(**May, 2010**)
21. Can it be said that VAT brings about certainty to a great extent in the matter of interpretational issues? If so, how? (2 marks)(**May, 2010**)
22. What are the merits of VAT in the context of tax evasion, neutrality and transparency? (3 marks)(**May, 2010**)

PRACTICAL QUESTIONS

Q.1: *Vishal, a manufacturer sells goods to Vinit, a distributor for ₹ 2,000 (excluding of VAT). Vinit sells goods to Samkit, a wholesale dealer for ₹ 2,400. Samkit, the wholesale dealer sells the goods to Bhavin, a retailer for ₹ 3,000, who ultimately sells to the consumers for ₹ 4,000. Compute the tax liability, input credit availed and tax payable by manufacturer, distributor, wholesale dealer and retailer under invoice method assuming VAT rate @ 12.50%.* ***(IPCC, Nov. 2009, 8 marks)***

Solution:

Computation of tax liability, input tax credit availed and tax payable under invoice method:

Stage	Particulars	VAT Liability (a)	*Less* VAT Credit (b)	Tax payable to Government (c)=(a)–(b)
1.	Vishal, the manufacturer, sells to Vinit, the distributor, for ₹2,000. Therefore his tax liability will be ₹ 250 (₹ 2,000 @ 12.5%). He will not have any VAT credit.	250	-	250
2.	Vinit, the distributor, sells goods to Samkit, the wholesale dealer, for ₹ 2,400. Vinit's tax liability will be ₹ 300 (₹ 2,400 @ 12.5%). He will get set off of tax paid at earlier stage of ₹ 250. Thus, tax payable by him will be ₹ 50.	300	(250)	50
3.	Samkit, the wholesaler dealer, sells to Bhavin, the retailer at ₹ 3,000. Samkit's tax liability will be ₹ 375 (₹ 3,000 @ 12.5%). He will get set off of tax paid at earlier stage of ₹ 300. Thus, tax payable by him will be ₹ 75.	375	(300)	75
4.	Bhavin, the retailer sells goods to consumers at ₹ 4,000. His tax liability will be ₹ 500 (₹ 4,000 @ 12.5%). He will get set off of tax paid at earlier stage of ₹ 375. Thus, tax payable by him will be ₹ 125/-	500	(375)	125

Note: *It has been assumed that sales made by the distributor, the wholesale dealer and the retailer are also exclusive of VAT.*

Q.2: *Compute the VAT amount payable by Ankit who purchase goods from a manufacturer on payment of ₹2,25,000 (including VAT) and earn 10% profit on sale to retailer? VAT rate on purchase and sale is 12.50%.* ***(IPCC, June 2009, 3 marks)***

Solution:

Computation of VAT payable by Ankit:

	Particulars	₹
	Payment made by manufacturer	2,25,000
Less:	VAT paid $\left(\frac{(2,25,000 \times 12.50)}{112.50}\right)$	(25,000)
	Purchase price	2,00,000
Add:	Profit margin	20,000
	Sales price before VAT	2,20,000
Add:	VAT @ 12.50% on ₹ 2,20,000	27,500
	Invoice value after 10% profit margin	2,47,500
	VAT charged in invoice	27,500
Less:	VAT input credit $\left(\frac{(2,25,000 \times 12.50)}{112.50}\right)$	(25,000)
	VAT payable by Ankit	2,500

Note: *Profit has been computed as 10% of the cost price of the goods.*

Q.3: *Compute the VAT amount payable by Rahul who purchase goods from a manufacturer on payment of ₹1,20,000 and after adding for expense of ₹ 10,000 and profit ₹ 15,000 had sold the same. VAT rate on purchase and sale is 12.50%.* ***(IPCC, Nov. 2007, 3 marks)***

Solution:

Computation of Invoice Value:

	Particulars	₹	₹
	Cost of goods purchased		1,20,000
Add:	Expenses	10,000	
	Profit margin	15,000	25,000
	Product sale value		1,45,000
Add:	VAT @ 12.50%		18,125
		Invoice Value	1,63,125

Computation of tax payable under VAT:			₹
	VAT charged on sale		18,125
Less:	Input credit of VAT on purchase @ 12.50% on ₹ 1,20,000		(15,000)
		Tax payable under VAT	3,125

Note: It has been assumed that the purchase price of ₹ 1,20,000 is exclusive of VAT.

Q.4: *Sandeep, a trader selling raw materials to manufacturer of finished products. He imports his stock in trade as well as purchase the same from the local markets. Following transaction took place during the financial year 2009-10. Calculate the VAT and invoice charges by him to a manufacturer. Assume the rate of VAT @ 12.50%.*

Cost of imported materials (from other state) including VAT	*₹ 2,00,000*
Cost of local material including VAT	*₹ 4,50,000*
Other expenditure including storage, transport, interest and profit earned by him	*₹ 1,00,000*

Solution:

The facts of the question may be taken to be that of the financial year 2009-10

Sale Price of goods:

	Particulars	₹	₹
	Imported material cost		2,00,000
	VAT @ 12.50%		25,000
	[Since, this is not a VAT levied inside the State, it will form part of cost of input]		
Add:	Cost of local materials	4,50,000	
Less:	VAT @ 12.50% $\left(\frac{(4{,}50{,}000 \times 12.50)}{112.50}\right)$	(50,000)	4,00,000
	[Since, credit of Rs. 50,000 would be available, it will not be included in cost of input]		
Add:	Other expenses and profit		1,00,000
	Sale price of goods		7,25,000
Add:	VAT on the above @ 12.50%		90,625
	Invoice value charged by Mr. Sandeep to the manufacturer		8,15,625

Q.5: *Mercy, a trader selling raw materials to manufacturer of finished products. He imports his stock in trade as well as purchases the same from the local markets. Following transaction took place during the financial year 2009-10. Calculate the VAT and invoice charges by him to a manufacturer. Assume the rate of VAT @ 4%*

Cost of imported materials (from other state) including VAT	*₹ 1,50,000*
Cost of local material including VAT	*₹ 6,24,000*
Other expenditure including storage, transport, interest and profit earned by him	*₹ 3,25,000*

Solution:

The facts of the question may be taken to be that of the financial year 2009-10

Sale Price of goods:

	Particulars	₹	₹
	Imported material cost		1,50,000
	VAT @ 4%		6,000
	[Since, this is not a VAT levied inside the State, it will form part of cost of input]		
Add:	Cost of local materials	6,24,000	
Less:	VAT @ 4% $\left(\frac{6,24,000\times4}{104}\right)$	(24,000)	6,00,000
	[Since, credit of Rs. 50,000 would be available, it will not be included in cost of input]		
Add:	Other expenses and profit		3,25,000
	Sale price of goods		10,81,000
Add:	VAT on the above @ 4%		43,240
	Invoice value charged by Mr. Sandeep to the manufacturer		11,24,240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Monthly Income with Grant Rs. 50,000/-
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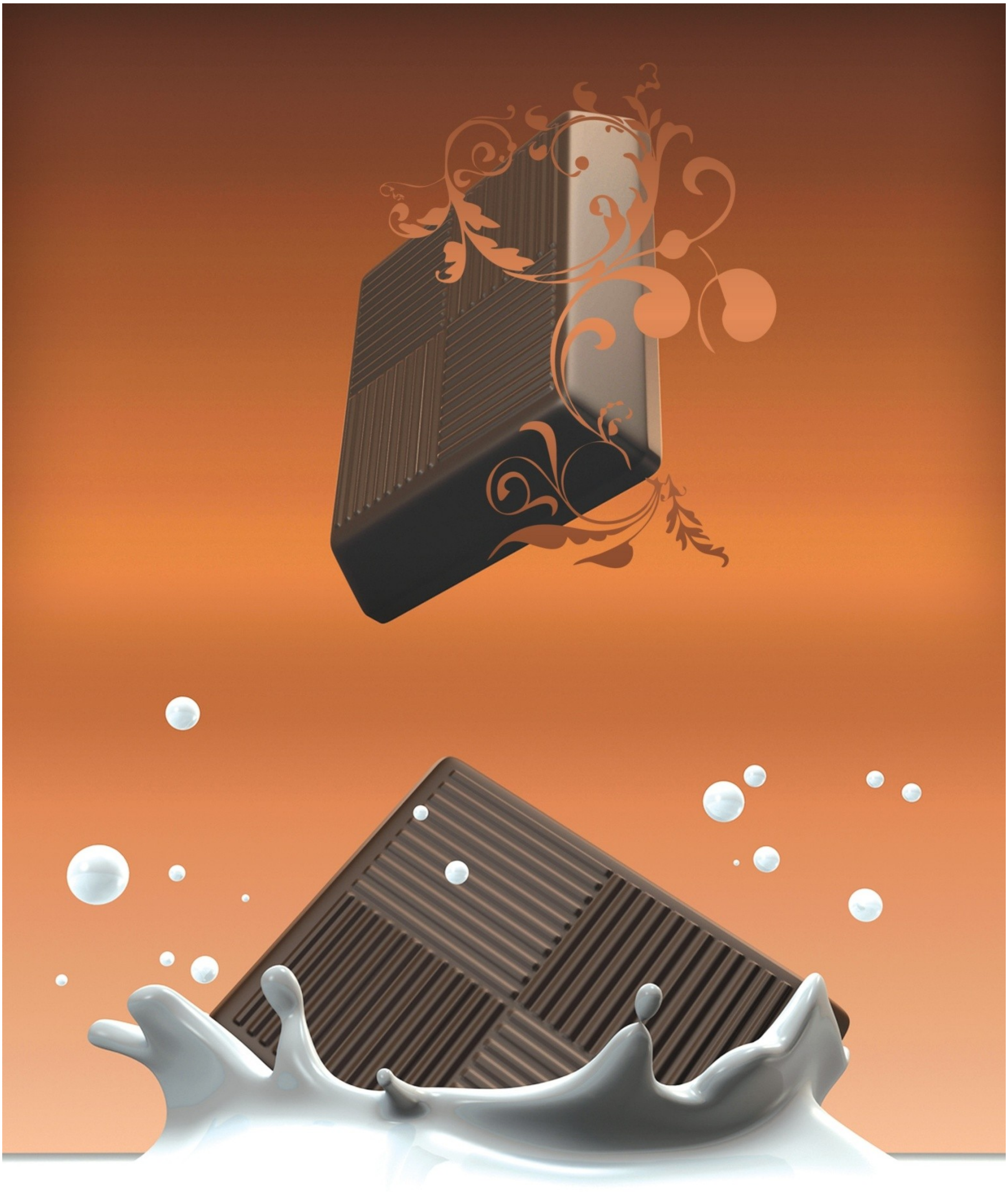

All

The Best