

VAT AND CENTRAL SALES TAX

Question

Illustrate with an example, whether inter-State purchases liable to central sales tax are eligible for input credit and explain the effect of the same on inter-State transactions.

(4 Marks) (Nov 2008)

Answer

The inter-State purchases liable to central sales tax are **not eligible** for input tax credit. However, the liability to central sales tax can be set off against the input tax credit earned on other eligible purchases. By way of an example, a dealer in State K purchases goods from another dealer in State M. The dealer in State M charges CST at 2% on this sale against C Form produced by dealer in State K. The tax is deposited in State M. Though it is called CST, the Central Government does not get any share in this and it is a revenue receipt of the selling State. The dealer in State K sells these goods within the State K and collects VAT which is deposited in State K. The question is whether the dealer in State K can claim input tax credit of the central sales tax paid by him to be set off against the VAT liability in State K. This is not possible as State K will not permit the set off against the tax paid to another State M. This is because the same if permitted would result in loss of revenue to State K. This is the reason why CST is not vatable.

The effect on inter-State trade is that trade will be uncompetitive for the States that are net importers because in those States consumer prices will be high. **CST is origin based tax collected by the exporting State while VAT is a destination based consumption tax.** They both cannot go together and to that extent the objective behind the VAT regime in lowering of prices for consumers cannot be achieved.