

REFORM IN CENTRAL SALES TAX IN THE CONTEXT OF VAT

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ABSTRACT

VAT is now a reality; whether we like it or not, we have to accept the reality. Since last decade, there has been a debate over implementation of VAT, but in his Budget speech of 8th July 2004, Finance Minister P. Chidambaram reiterated Government commitment to implementing value-added tax (VAT) by April 01, 2005 and gave a full stop to this debate. But this decision led to generate few other questions regarding VAT. First at all, it was asked that instead of existing tax systems and structure, why there should be another fear especially in the minds of the traders was that with the implementation of abolishing of other indirect and local taxes like sales tax, octroi etc.... Another doubt which was a cause of about the way of implementing the VAT. From the point of view of a common man, it was important whether the VAT regime would have to increase in the prices of goods. In the present paper, an attempt has been made to find answers to some of these questions on the basis of last 9 months experience.

Now most of the states in India have already started implementing VAT, but has thought been given to all the necessary technical and administrative preparations that need to be in place before VAT is introduced? There have been many agitations against VAT by the traders. Even though the idea and intention behind implementing VAT is good, still it would have been better if the people were educated and the myths and realities were explained before implementing VAT.

Keywords: VAT-Value Added Tax, WTO-World Trade Organisation, CST- Central Sales Tax, CGST- Central General Sales Tax, CENVAT- Central Value Added Tax, GST- General sales Tax, TIN- Tax Payers Identification Number.

INTRODUCTION TO VAT

VAT is a value Added Sales tax. It is the tax on value addition. To an assessee Vat is the excess of tax collected on total factory input or purchases. In other words VAT is a tax on the value added by business firm through its own activity to the goods and services it buys from other business firms.

This exercise seeks to assess the change in tax revenue that could result from the introduction of VAT by all states, following a uniform design. The key features of such design would be tax credit for inputs, extension of the base to include transactions. Beyond the first point sale and zero rating of interstate trade and international exports. The tax rates

proposed are 4 percent and 2.5 percent with the former rate being applicable mainly on inputs and some basic necessities the tax would however remain a tax on sale of goods alone.

India has for long debated on the issue of introduction VAT. Finally it has crystallized and industry, states are all set to move in to the new era by April 2003. However there have been serious doubts on the readiness of states for this transition. A recent World Bank study has found that none of the states are actually fully prepared for a VAT system. This raises doubts on the benefits that India would get by this tax regime. As pointed out earlier the benefits of a VAT system are huge. Hence India should accelerate its implementation schedule. Otherwise the true benefit of this system would start only after 2006 when the CST reforms are expected to be completed. Hence the Governments should work backward from that time and prepare for the new regime. Almost all the state governments have started having training sessions for the stakeholders including their officials and corporates. But the size of the effort may not be enough.

OBJECTIVES

The presence of different VAT rate, exemption, concessions and / or composition scheme distorts the flow of audit trail introduced by VAT system and may result in cascading effect of taxation.

- To increase the competitiveness of Indian Industry.
- To remove the multiple taxes.
- To ensure that all barriers of inter-state trade and commerce should be removed and a unified national market is created
- To also ensure that there is simplicity and transparency in the system.
- To bring revenue neutrality in the long run under VAT regime

LITERATURE REVIEW

The tax system is of universal nature involving the state, society, entire country and others part of universal as we under that the indirect tax system is prevalent in other part of world in some places it is called sales tax some where out put tax and some where VAT but his is toll in hand of state. That under the indirect tax system it is tool in the hand of state in some places it is called sales tax some where out put tax and some where VAT .The burden of this category of tax lies upon the ultimate payer. The ultimate payer of the tax is a consumer who ranks in one as the all the burden of tax is born by them. The time has come to let the policy maker imagine for those who pay this tax at least be honest to them. The study is basically aimed to problems in sales tax and its evils in tax administration.

METHODOLOGY

The decision to refer the introduction of value-added tax (vat) is no longer news though many reasons have been cited, including the unfortunate December 13 attack on Parliament and the events that followed, the various issues connected to ushering in vat remained unresolved. Also, experts felt that the preparations were far from satisfactory.

A VAT with many distortionary features and of a hybrid variety would be more harmful than the existing sales tax regime. The decision to defer and the time gained, among other things should help allay fears of industry and trade Industry was particularly skeptical about the

CST and its cascading effect on inputs purchased from other states. Trade too had its share of misgivings, particularly the small and medium business, on the likelihood of being pulled into the vat net and the attendant compliance burden. Tax department have also had reasons to welcome the decision as preparatory steps for law-making were not in place and many states did not even have the draft law ready. Besides, restructuring the departments-a major task on hand-was also not fully addressed.

A homogeneous vat is the need of the hour. Therefore, state governments, with the centre acting as guide, philosopher and friend, should aim at a common vat law procedures and administration mechanisms. That alone will fully sub serve the broader objective of fiscal reform. The decision to defer vat by a year is therefore, not a long delay. It is a certainly worth the wait when the reform is for more than a generation.

Reforms in Central Sales Tax in the Context of VAT, MODVAT & CENVAT

In order to make necessary improvement in VAT system the Indirect Taxation Committee headed by L.K. Jha made certain recommendations in 1976 and accordingly excise duties were converted into a VAT at manufacturing stage (MANVAT) Since then the government has been adopting the scheme of MODVAT in a phased manner.

Modified Value Added Tax (MODVAT) was introduced as a major step in respect of a major reforms in excise duties in India w.e.f. 1st March , 1986 through the Budget 1986 - 87 by the then Finance Minister Vishwanath Pratap Singh. Under MODVAT scheme, credit of excise duty was allowed in inputs which were used either for producing excisable finished products of intermediate products. Over time, the ambit of MODVAT has been extended to include more commodities and sectors.

The introduction of MODVAT in 1986 was considered as a major step in respect of reformation of indirect tax system. The MODVAT scheme allowed the manufacturers to obtain instant and complete reimbursement of the excise or counter vailing duty paid on the component and raw materials. It was extended to inputs for fibers and yarns in 1991 budget and only tobacco and petroleum products, textile inputs and matches were excluded from the MODVAT scheme.

The sales tax is indirect tax which means the burden is passed on to the ultimate consumer who pay for the goods and services. In free economic the consumer is king because the demand is based upon his behavior. It is stated for the consumer regulates the demand and thus decisive factor in creation of supply chain. The economic system also is depends upon the demand and supply.

Thus the burden on consumer because of the multipoint tax system and other evil of the sales tax administration are born by this consumer, who is a general citizen of this country The hike in price of the essential commodities and services directly effect the purchasing power of this segment, which generally effect the larger part of our country's population attributed by the sales tax and its administration in India .Thus the economic of the country is affected as this phenomena hamper the demand of the economy.

The CST Act provides for levy on Inter-State sales and also defines what is 'Inter-State Sale'. However, the concept that revenue from Sales Tax should be collected by States has been retained. Thus, though it is called Central Sales Tax Act, the tax collected under the Act in each State is kept by that State only. This is provided in Article 269(1) (g) of Constitution of India.CST in each State is administered by local sales tax authorities of each State.

Tax collected in the State where movement of goods commences - The scheme of CST Act is that Central Sales Tax is payable in the State from which movement of goods commences (i.e. from which goods are sold). The tax collected is retained by the State in which it is collected. CST Act is administered by Sales Tax authorities of each State. Thus, the State Government Sales Tax officer who collects and assesses local (State) sales tax also collects and assesses Central Sales Tax.

Implementation of VAT

We are living in the era of globalisation. Attempts are being made to globalise every thing. We have adopted new economic policy since July, 1991 though the developed countries in the world have adopted such policy since 1980. We are trying to integrate our economy with the world economy as a part of globalisation process started through GATT now converted into WTO. Taxation system of every member country of WTO is also to be integrated with the world taxation system. For this purpose almost all the member countries of WTO have accepted Value Added Tax System. Therefore, it is clear that uniform tax system all over the world is necessary for free trade of ' goods. Uniform tax system in the form of VAT has been accepted by the majority countries in the world. Therefore, VAT system may be called as the modern tax system.

Value added taxation has emerged as the most effective mechanism worldwide for levying and administering taxes on consumption. Most countries have adopted the value added tax structure of commodity taxation because of its non-distortionary impact on resource allocation and decision making by economic agents, self-policing nature, revenue productivity, ease of administration and compliance facility. A detailed presentation of the VAT mechanism and its several advantages has already been made in the first report of the Commission. In unitary countries, it is possible to effectively put in place an economically neutral VAT that is easy to administer and difficult to evade. Our study throws light on several core issues relevant to the concept and application of value added taxation in the country. It indicates the incentive-disincentive mechanism operating today in the origin-based, cascading commodity tax structure at the State level. It helps us to identify areas for decision and action and provides fairly reliable estimates of the likely revenue from different tax rates. It can be used as a guide for further similar studies by the department which could be eventually put together to construct a complete input-output table.

Value Added Tax 2009 (India)

VAT which ideally must be destination based. The Government had proposed CST Act only as a regulatory law with zero tax rates to ensure that inter-State sales are not taxed by the Origin State. This is the basis of VAT, which got defeated by the CST Act. Till early 1980's sales tax was a multipoint levy with no set off and this in turn, drove up the prices of goods on account of cascading effect of taxes. The States found it difficult to justify multipoint tax at the high rates of tax and secondly found it difficult to manage the increasing number of assesseees. It therefore, resorted to single point tax system at higher rates of tax to generate the required revenue. This was the second major step which created further distance/difficulty for introducing VAT in our country. Had the government introduced the concept of setoff to the existing multipoint tax system rather than going in for single point tax system, we would have had a major concept of VAT into our Sales Tax Law much earlier. The government has emphasized the need for buoyant revenues to satisfy the State's requirements of funds for its developmental activities. The system of sales tax is highly

saturated, addresses only limited resource mobilisation capabilities and does not lead to tax buoyancy except when tax rates are enhanced. In the event, the tax rates are enhanced the industry is adversely affected leading to flight of trade, evasion, suppression and unhealthy competition among States. States studied the impact of sales tax system and felt the need for reform to the sales tax system of taxation. Therefore, VAT was the answer.

VAT and Central Sales Tax

State level sales tax as a multi point tax was introduced first by Tamil Nadu way back in 1939. Many states thereafter resorted this form of taxation during and after World War II ofcourse, there were many anomalies within this structure of tax adopted by the states with no economic rational which then led to difficulties in administration of this tax. As the economic circumstances at state level were uneven, it led to trade diversion, opposition from trade organizations, problems of inter state trade and double taxation fared in many states across the country. Each state as a subject under its law the same transaction was taxed under the 'nexus doctrine' in different states based upon any stage of contract of sale use to get completed in more than one state. Each state relied on one or more such stages or elements of transactions as having a territorial nexus and brought the sales to tax. Supreme Court also held levy of taxes by different states on the basis of nexus theory. Some judgments later received, creating confusion resulted in refunds from state. This resulted in the introduction of Central Sales Tax Act in 1956, Concept of VAT simultaneously took away VAT as a 'Destination Based Tax' to origin based tax with introduction of CST. The original idea was that CST should act as a regulatory law with zero tax rates to ensure that inter state sales are not taxed by the state of origin. Sales tax as a multi-point levy with no set off increased the prices of goods and services due to cascading effects of taxes. States since were unable to justify multi-point tax at high rates with manageable volume of assesses shifted towards single-point tax system at higher rates to generate high revenue. This made VAT a distant reality.

SUMMARY, CONCLUSION AND SUGGESTION

The Need of the New Millennium By Mahesh C Purohit¹ Evolution of value added tax (VAT) is the most important fiscal innovation of the present century. Beginning with the adoption of Taxe sur la Valeur Ajoutee by France in 1954, it wash gradually been adopted by other countries. But in recent years it has spread like a prairie fire through out the world bringing the total number of VAT countries to more than 160 with acceptability of a large number of Latin American, Asian, African and Pacific countries. Such increasing popularity of VAT has primarily been due to its taxonomy and administrative expediency.

On the front of the state sales taxes, which account for approximately 60 percent of the states own tax revenue, no reforms have so far been attempted. The existing sales tax system of the states is confronted with many weaknesses.

To have effective and efficient governance of VAT, a prerequisite is to adopt suitable computational technology. It is absolutely necessary that a requisite system, suitable to the structure and administrative requirements of each state be selected. However, in adopting computer technology one must keep in mind the capacity of the computer system to be adopted. Indeed, it should not be too large creating under utilisation. At the same time in the selection of the system the principle of simplicity must be emphasised upon. More importantly, it is essential to have proper co-ordination among the states to adapt according

to their requirement of software. Pooling their resources for developing requisite software programmes could be cost effective.

A more important aspect for initiating reform process and to set the ball rolling relates to the central sales tax (CST). It is absolutely important that the central government provides leadership and takes a lead in reducing the rate of CST. It must immediately be brought down from 4 percent to 1 percent say by January 2002. The Union government must compensate the states for the loss of revenue; say a period of 3 to 5 years. Alternatively, the existing 'origin based' CST should be converted into a 'destination based' central purchase tax.

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