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**Turning The Tide**





## An Overview on Draft Value Added Tax Act 2011

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Value Added Tax (VAT) is a tax on value addition. It was introduced first in France in 1954 and so far more than 140 countries of the world have adopted it. Bangladesh introduced VAT in 1991 as a replacement of Sales Tax and Excise Duty. Initially VAT was imposed at manufacturing and import stage and has since been expanded to retail stage. This expansion of the VAT net caused many complications and reform of the law is urgently needed. Instead, the government has issued hundreds of General Orders, Special Orders and Statutory Regulatory Orders on an ad hoc basis. Consequently the law has become more complicated for regulatory authorities and taxpayer alike.

In view of this, the Government has formulated a draft VAT Act 2011 (draft Act) with the expectation that this will be implemented in 2012. A comparative commentary on the salient features of the proposed Act is given below:

### Structure

Value Added Tax Act 1991 comprises 73 sections and 43 rules. These sections and rules were not organized subject-wise. The draft Act has been expanded to 193 sections and structured into different chapters according to subject. The Rules

are expected to be published soon after the promulgation of the Act. This elaboration and re-organization has made the Act friendlier to all concerned.

### Language used

The VAT Act was formulated in Bangla in 1991. In view of globalization and to encourage Foreign Direct Investment, English is considered the appropriate language for a law related to trade and commerce. While most business laws have an authentic English version, in case of VAT laws this could not be completed even 20 years after promulgation. On the other hand, the draft VAT Act 2011 has been formulated in English – a move appreciated by the business community.

### Registration

The general rule under the existing law requires separate registration for each place of business activity operated by a person. The draft Act 2011 provides for a single registration for all economic activities, provided separately identifiable records and accounts are kept for the branches and divisions. This will reduce the inconvenience of taxpayers.

### Determination of price

Under the existing law, in case of



imported goods, the base value is ascertained by adding the amount of import duty, supplementary duty and all other duties and taxes (if any), except Advance Income Tax (AIT). In case of local supply of goods, VAT is leviable on the price to be realized from customers, inclusive of input cost, all expenses and profit of the taxpayers, discounts, commissions, fees and all duties and taxes, excluding VAT. There are provisions for tariff value, truncated value and VAT on retail price including VAT. In case of services, VAT is leviable on total receipt.

As per the draft Act, the VATable value of imported goods is the summation of assessment value, insurance, freight, cost of services ancillary or incidental to import, customs duty, supplementary duties and other taxes, levies, fees, or fiscal charges other than VAT and AIT payable on the import of the goods. In case of local supply of goods, immovable property and services, VAT is leviable on the consideration reduced by the amount of tax fraction. In case of the supply of imported services by a related person, VAT is leviable upon the fair market value and, in other cases, on consideration.

The changes in the draft law appear to be positive but the provision for fair market value may create confusion.

### Price declaration

Presently, price declaration with reference to the value base for VAT and the input-output co-efficient of the products are required to be submitted in prescribed format (Mushak 1, 1 Kha, 1Ga, 1 Gha), which the authorities are required to approve within 15 working days. Further, the tariff value and the truncated base system are distortions of the VAT system as

problems arise in the value chain for other stakeholders following the credit methodology. In the draft Act price declaration has been discarded. Instead, the taxpayers would notify the current price and input-output coefficient. The base for taxation has become the transaction price. Tariff Value and truncated base system have also been discarded. This would be great relief for taxpayers from procedural complexities.

### Deduction at source

Currently VAT deduction at source is applicable in case of services. Imported services, comprising royalty and technical know-how, are included in deduction at source. The explanation required to clear the ambiguity regarding the payee i.e. whether the service provider or recipient is to suffer the VAT is yet to be given. The net has been widened in the draft Act to include government entities, NGOs, banks, insurance companies and other financial institutions, limited companies and post secondary institutions and makes the following additional provisions.

Withholding would be mandatory in a supply under:

- an agreement by tender
- a supply under an ongoing supply agreement, or
- a supply or set of related supplies for which consideration exceeds Tk. 25,000.

Withholding entities would not be permitted to take supply unless:

- person is registered, and
- has a valid VAT honor card.

Obligation to withhold by a withholding entity:

- one third of the payable VAT amount to withheld
- to issue a certificate
- withheld amount to be accounted for in the VAT return.

“ THE VAT ACT WAS FORMULATED IN BANGLA IN 1991. IN VIEW OF GLOBALIZATION AND TO ENCOURAGE FOREIGN DIRECT INVESTMENT, ENGLISH IS CONSIDERED THE APPROPRIATE LANGUAGE FOR A LAW RELATED TO TRADE AND COMMERCE. WHILE MOST BUSINESS LAWS HAVE AN AUTHENTIC ENGLISH VERSION, IN CASE OF VAT LAWS THIS COULD NOT BE COMPLETED EVEN 20 YEARS AFTER PROMULGATION. ”





VAT is an output tax. Deduction of VAT from the suppliers of input is a distortion from the VAT principle. It is a woe for honest taxpayers which would be aggravated by the proposed law.

### VAT payment/ Treasury deposit

Under the existing system, advance deposit must be made to the Treasury and the output VAT is adjusted through the current account when products are supplied and services are provided. VAT payment is only possible through Treasury Challan. The system proposed in the draft Act would be an advancement towards global standards: treasury deposit will be completed at the time of Return submission and there is a provision for VAT payment through electronic bank transfer, credit card and certified bank cheques.

### Recovery of VAT from individuals leaving Bangladesh

Presently there is no provision to restrict a person from leaving Bangladesh while any tax payable by him remains unrecovered. As per the rules in the draft Act, the respective Commissioner may issue a certificate of non-compliance, stating the outstanding tax debt to the immigration officer, to prevent the defaulter from leaving the country. The new law sounds very tough for taxpayers. However, it would be rational to restrict the provision only to the amount of the agreed VAT liability.

### Offenses, penalties and punishments

As per existing laws, there are provisions for penalty for revenue loss of the Government and punishment in case of an offence of a criminal nature. Provisions in the draft Act allow for severe penalties and punishment for offences relating to registration, enlistment, submission of return, etc. The penalties and punishments appear to be drastic, particularly for SMEs.

### Tax Clearance Certificate (TCC) and Honor card

A person who submits all returns of the previous financial year are entitled to a VAT honor card. As per proposed Act, in addition to VAT honor card, Tax Clearance Certificate will also be issued to good taxpayers. This friendly move would be encouraging for honest taxpayers.

### Extension of VAT payment and VAT return deadlines at the time of natural disaster

In the event of natural disaster, there is no provision that allows extension of time for payment of VAT or submission of VAT Return. Provision has been made in the proposed Act to allow a registered person to pay VAT and submit Return even after the due time, in case of occurrence of natural disaster, subject to the permission of the Commissioner.

### Outsourcing

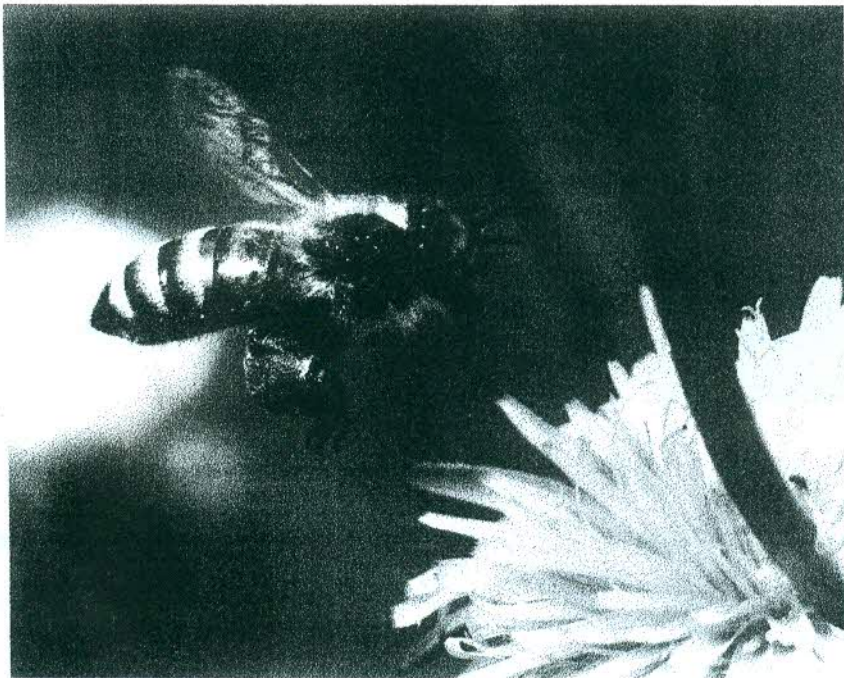
Outsourcing is a modern practice of managing business operations. In the existing Act there is clear and detailed provision regarding outsourcing. However, there is no clear explanation regarding outsourcing in the proposed Act. This may create complexity and confusion since outsourcing is a common practice. A clear explanation is required to ease tax payment.

### VAT refund

VAT refund is a multifaceted and compound system which has been simplified in the proposed Act. Excess amount of total decreasing adjustment over the total output and increasing adjustment in respect of:

- construction, building or





property development shall be carried forward indefinitely.

- an excess may be carried forward or be deducted over 6 (six) tax periods.

VAT paid in excess of payable amount will have decreasing adjustment instead of a refund. Turnover tax paid in excess is entitled to deduction instead of refund. This is an advancement towards standard practice.

### Appeal division and reference

Currently, an appeal to the Commissioner or to the Tribunal must be made within 90 (ninety) days of order. Reducing the scope of taxpayer for appeal, the draft Act allows for an appeal to be made to the Commissioner (Appeal or Tribunal) within 60 (sixty) days of the order.

### Post-supply adjustments for adjustment events

There is no provision for

post-supply adjustments in the existing law. However, the input tax credit is allowed under certain conditions. To minimize the cascading effect, as per draft VAT Act, adjustment event occurs when the supply is cancelled, the consideration for supply is altered, the supplies are returned, the nature of the supply is fundamentally varied or altered, or VAT payable increases or decreases.

Adjustments increasing the amount payable include withheld amounts, bad debts, payments made outside banking channels, goods applied to private partners, VAT paid before registration, an increasing adjustment required on cancellation of registration, an increasing adjustment required where there is a change in the VAT rate, supplementary duty payable for the tax period, interest or a fine, penalty, fee or other sum imposed and payable.

Adjustments decreasing the amount payable include advance tax, adjustment relating to prepaid

telecommunication products, adjustment of withholding VAT, input tax credit amount, bad debts, adjustment on becoming registered, adjustment in relation to secondhand goods, adjustment in relation to indemnity payment under a policy of insurance, adjustment in relation to monetary price paid for a lottery, lucky draw, raffle or similar undertaking and refund of supplementary duty overpaid.

### Supplementary duty

As per existing laws, luxury goods, non-essential and socially undesirable goods, as specified in the 3rd schedule, are subject to imposition of supplementary duty. The draft Act proposes supplementary duty to be imposed and payable on import of dutiable goods, supply of dutiable goods manufactured in Bangladesh and supply of dutiable services made in Bangladesh. There will be no supplementary duty on export and zero rated goods and services. Supplementary duty is payable only once.

The provision for supplementary duty on locally manufactured goods and services should be withdrawn unless these are luxurious in nature or socially undesirable.

### Assessment

There is no provision of assessment of VAT under the existing law. As proposed in the draft Act the Commissioner may make an assessment of an amount payable by a person if he is not satisfied as to the accuracy of the information of the returns, if a person who fails to file a tax return, pays tax or has received a refund which he is not entitled to, or the person fails to pay the amount due, or a person



has been paid a refund which he was not entitled to. An original assessment may be amended within four years. This could be a major source of inconvenience for tax payers if this provision is recklessly used by the authorities.

**Duties of receivers/Directors**

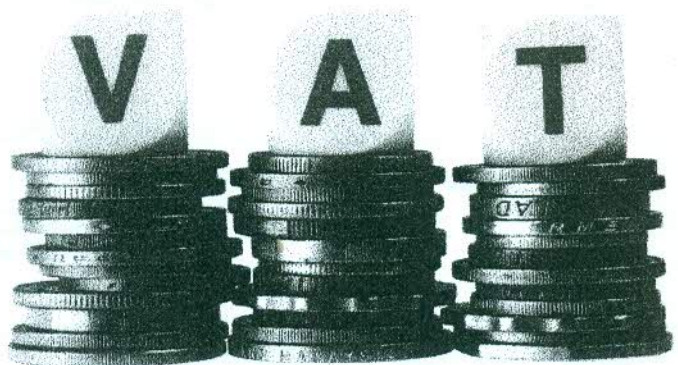
The draft Act defines the new concept of 'Receiver' as a person who, with respect to an asset in Bangladesh is:

- a liquidator of a company
- a receiver appointed out of court or by a court
- a trustee for a bankrupt person
- a mortgagee in possession
- an executor of the estate of a deceased person, or
- any other person conducting business on behalf of a person who is legally incapacitated.

A Receiver is required to notify the Commissioner in writing within 21 days, set aside the amounts notified by the Commissioner, and is liable to the extended amount set aside. He is personally liable to the extent of the said amount. The Directors of the Company are also jointly and severally liable depending on certain factors.

**Security deposit**

The draft Act has empowered the Commissioner to instruct taxpayers to make a security deposit to secure Government dues. This will create unwanted burden on working capital of taxpayers. There is also a risk of harassment of taxpayers.



**Default surcharge**

The draft Act introduces default surcharge @10% on taxpayers who fail to pay tax on due dates. On the top of 2% interest for non-payment of tax on the due date this provision appears unreasonable.

**VAT practitioner**

As per SRO 117-LAW-98/178-MUSHAK of 11 June 1998 issued under section 46 (2) of VAT Act 1991, even a qualified Chartered Accountant with long experience needs to pass a prescribed examination to get a VAT Consultant's license whereas an officer of Customs, Excise and VAT department who served a minimum of 15 years in the position of revenue officer and above, is exempted from this. Section 178 of the draft Act contains the provision for license of VAT Consultants. The qualification requirements are expected to be prescribed in the

Rules. Business experience, knowledge of VAT laws and accounting are essential criteria for a person to plead VAT issues. In consideration of the academic background and professional experience, Chartered Accountants and similar professionals deserve VAT Consultant licenses without any further examination. In this context, it should be noted that Chartered Accountants are eligible to practice Income Tax under ITO 1984.

Thus the draft VAT Act 2011 is an advancement towards global standards. It will enhance Government revenues and relieve the taxpayers from long outstanding problems if implemented with some modifications in consultation with different Chambers, Associations and Professional Bodies.

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