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**GET "READY  
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TO FACE THE  
CHALLENGES  
OF THE  
NEW MILLENNIUM**



## Vat on retail price: A forward step turned backward

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**V**alue Added Tax (VAT) a dynamic system of revenue collection was introduced in 1991. In spite of some procedural gap the system has proved it's worthiness eliminating long accumulated complicacies of former excise system.

Being an underdeveloped country we are largely dependent upon foreign loan and aids and consequently dominated by the donors formulating important national policies. To get rid of the situation, internal resource mobilisation has no alternative. Accordingly, VAT on some more products has been expanded upto retail price/level by recent fiscal measures. The attempt is progressive but due to certain regressive provisions of current fiscal measure and misinterpretation of the core issue "Retail Price" by local authorities, causing serious damage to local industry, it is now encouraging imports. To analyse the situation meaningfully, PAINTS sector the worst sufferer has been considered herein as a sample.

### HOW FISCAL MEASURE HAS PATRONISED IMPORTS

In view of the self-sufficiency in paints production, customs duty on imported paints was, at the highest level, 42.5%. Consequent upon reduction of highest slab of customs duty to 40%, Importers got a relief of 2.5%. In case of imported paints, VAT—leviable upon C & F value + import duty—represents at best 60% of MRP, while local Manufacturer pays on total

MRP at the time of delivery of their products from the place of production. Finally, the Manufacturer being a taxpayer with permanent establishment is paying income tax @40% of their income, while importers are paying only 3% AIT and subsequently, in many cases, instead of making additional contribution to National Exchequer has been claiming refund. Against all aforesaid adverse facts there is a reduction in the rate of customs duty, resulting in savings not exceeding 10% of the cost caused by them as revealed in a study conducted by the author to assess impact of current fiscal measure upon paints industry.

Now, it is clear that inspite of the commitment of government to ensure protection to local industry, current fiscal measures have weakened the competitiveness of some local industries like paints.

### MISINTERPRETATION AND EFFECTS

So far, paints manufacturer have been paying VAT in pursuance with Sec 5 (2) of VAT Act 1991, upon the value added by them. Now, consequent to the change in base they are to pay VAT under section 5(3) upon said value and the value to be added by their dealers in future. Considering national interest and infrastructure limitation of revenue department the manufacturer has obliged the new provision, inspite of the unjustified arrangement to collect VAT from someone against the value added by the others.

## Taxation

Accordingly, few leading company has submitted their price declaration immediately after the change, showing retail price as the base for computation of VAT to relevant authority. Such prompt response was appreciable but unfortunately was rejected by the authority with an instruction to add the amount of VAT with retail price in fixing base for computation of VAT.

Avoiding cascading effect, VAT system has created a business friendly environment and it's transparency is proactive to revenue. To take VAT + MRP in fixing base for computation of VAT, tantamounts to VAT on VAT which is against the fundamental principle of VAT, system "NO VAT ON VAT". Is it a step to return to the former complicated excise system? If so, who will compensate the nation for the huge costs incurred during the last 7-years while introducing and establishing the VAT system?

VAT is an indirect tax leviable upon consumers. Manufacturer are depositing VAT in advance in the Government Exchequer and collecting the same from their customers, long after delivery, during sale of the said goods. In fact, the stand of a manufacturer in the VAT-chain is that of a collector. Is it not unjust to penalise the collector by an additional VAT on the

amount collected by him, on behalf of the government? There may be a suggestion to increase price to realise additional VAT but that would be suicidal for the manufacturer in a situation where our market is open to foreign competitors.

The rate of VAT as noted in Sec 3(1) of said Act is 15%. Inclusion of VAT with MRP in fixing base for computation of VAT, produced an effective rate of  $V((15 \times 100), 85) = 17.65\%$ , which is contradictory to the provision of mother law and shall tarnished the relationship between taxpayers and the authority, locking them in a legal struggle.

In view of the said wonderful direction of local authority, leading taxpayers repeatedly met with the top brass of NBR including Finance Minister who assured that there would not be any "VAT on VAT". But unfortunately, three months have already passed and a circular in line with his assurance remains yet to be issued and in the absence of it, the sufferings of honest taxpayers are mounting-up.

Thus, immediate intervention of the government is now the crying need for existence of the concerned industries which are not only sources of government revenue but also provides the base for sustainable development of our country. ■