DISCUSSION PAPER

Road Map for National and Sub-National VATs in India

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Road Map for National and Sub-National VATs in India

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1. Introduction

Value added tax (VAT) is a multi-point sales tax with set-off for tax paid on purchases. The tax is collected in instalments at each transaction in the production-distribution process. There is no cascading because of the system of deduction or credit mechanism for taxes paid. The tax is levied on consumption. The final and total burden of the tax is fully and exclusively borne by the domestic consumer. No VAT is charged on goods exported.

Beginning with the adoption of *Taxe sur la Valeur Adjoutee* by France in 1954, owing to its taxonomy, VAT has gained popularity in a large number of countries. Its adoption could be considered as the most important fiscal innovation of the century that has gone by. It has spread like a prairie fire through the world bringing the totai number of VAT countries to more than 115.

India's indirect tax system is unique in that under the Constitution, the Central government has the authority to impose a broad spectrum of excise duties on production or manufacture while the States are assigned the power to levy sales tax on consumption. In addition, States are empowered to levy tax on many other goods and services in the form of entry tax, octroi, entertainment tax, electricity duty, motor vehicles tax, passengers and goods tax and so on. Due to this dichotomy of authority under the Constitution, India has been rather slow in the adoption of VAT. Also, it has created an obstacle in introducing the European-style VAT in India, although over the years, tax reform committees have recommended that central excise duty, sales tax, and other domestic trade taxes be replaced by a comprehensive VAT that could tax all commodities and services.

2. CenVAT

At the federal level, at the time of Independence, India inherited a system of commodity taxes in which Union excise duties (UEDs) were levied on about a dozen articles yielding a small proportion of total tax revenue to the Centre. Following Independence, the rates were raised, the base was enlarged, and more and more items were

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brought into its net. Over time, there was a speedy extension of UEDs. It was not only levied on finished goods but also covered raw materials, intermediate goods and capital goods.

2.1 Structure of CenVAT

As of now, the Union government levies basic UEDs on all goods manufactured or produced in the country. The prevailing structure includes (i) CenVAT (also called UEDs), (ii) special excise duty (SED), (iii) additional excise duty in lieu of sales tax [AD(ST)]; (iv) additional duty of excise on textiles and textile articles [AD ($T_{\&}$TA), and (v) cesses on specified commodities.

The additional duty of excise in lieu of sales tax [AD(ST)] is levied on tobacco, textiles and sugar. This is a tax rental arrangement between the Union and the States. According to this arrangement the Union government levies additional excise duty in lieu of sales tax and the States refrain from levying sales tax on these items. The net proceeds of this duty were being distributed among the States until the recommendations of the Eleventh Finance Commission, which has recommended its inclusion under the sharable taxes.

Cesses on specified commodities and additional excise duty on textiles and textile articles are primarily meant to raise resources for the development of concerned industries. The revenue department administers it but some other departments also contribute in this endeavour.

CenVAT (i.e. UED) is levied on all goods manufactured or produced in the country. With effect from March 1, 1986 Modvat was introduced under the union excise duty as a system of giving credit for excise duty on inputs. Initially, it was introduced for a selected number of commodities. The coverage was limited to 37 chapters out of a total of 91. Over time, Modvat was extended and finally replaced by Central VAT, known as CenVAT in the Budget 2000-1. CenVAT has in general a single rate of 16% with some variations for select commodities. The coverage of CenVAT has been extended to all commodities except high speed diesel (HSD), motor spirit (petrol) and matches[2]. In addition to general rate, there are three rates of special excise duty (SED) of 8%, 16% and 24% on specified products. Most of the items under SED are final products but some of the items also fall in the category of intermediate goods.

The CenVAT Scheme allows instant credit for excise duty, special excise duty (SED), ADE and countervailing duty (CVD)[3] paid on inputs and capital goods received in a

[2] Under Rule 57AB a manufacturer or producer of final products is allowed to take CenVAT credit in respect of the duty of excise specified in Central Excise Tariff Act (CETA), 1985 and leviable under the Act. However, the CenVAT credit that is allowed to be taken is restricted to the actual duty that is paid on the inputs. In other words, if the Central Excise duty on the inputs is less than the tariff rate prescribed in the first Schedule to the CETA, 1985, through an exemption notification granting exemption, then CenVAT credit is limited to the actual duty paid on such inputs, in the light of the said exemption notification.

[3] This is levied as per the provisions of the Customs Act wherein this is referred to as Additional Duty of Customs. However, this is popularly known as CVD.

factory for the manufacture of any dutiable final products (except matches). The credit could be utilised to pay excise duty on any final products. That is, all raw materials or inputs are covered except high speed diesel and motor spirit[4]. Similarly, credit could be availed of on capital goods including pollution control equipment, components, spares, accessories, moulds and dyes and paints, packaging material and greases/coolants[5].

Through the introduction of CenVAT credit could be availed of by the manufacturer immediately on receipt of eligible and duty paid goods in the factory. There is no need for the manufacturer to file any declaration or obtain any permission[6] For capital goods, however, only 50% of the duty paid on the goods can be availed of in a financial year: the remaining credit can be availed of in the next financial year, provided the goods are still in use (except for spares and components)[7]. Further, no depreciation should be claimed by the manufacturer under Sec.32 of the Income Tax Act, 1961 on that part of the value of these capital goods which is equal to the duty paid on the goods[8]. A manufacturer who manufactures only exempt final products is not allowed to take this credit. However, the manufacturer producing both dutiable and exempted final products in the same factory is eligible to avail of its benefits. This is subject to certain conditions viz., maintenance of separate records in respect of inputs used to manufacture exempted products or payment of 8% of the total price (excluding taxes) of the exempted final products or in the case of a few specified items, on reversal of the credit availed. Similarly, credit can be availed of on capital goods if not used exclusively for the manufacture of exempted final products.

The Scheme, *interalia*, provides the following facilities:-

i. Removal of inputs or capital goods as such on payment of excise duty as if such goods had been manufactured in the factory[9];

ii. Removal of goods to job-workers for processing, testing, reconditioning or for any other purpose provided that the goods are received back within 180 days or are removed from the premises of the job worker if permitted by the Commissioner of Central Excise[10];

iii. Refund of credit accumulated due to export under bond of the final products is also permissible[11];

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[4] See Rule 57AB.

[5] See Rule 57AA.

[6] Rule 57AC.

[7] Rule 57AC (2).

[8] Rule 57AC (4).

[9] See *Explanation* to Rule 57AB (1) (b).

[10] See Rule 57AC (5) & (6).

[11] See Rule 57AC (7).

iv. Unutilised CenVAT credit can be transferred on account of shifting of a factory to another site or due to change in ownership by sale, merger, amalgamation, lease or transfer to a joint venture wherein liabilities are also transferred; and

v. A special dispensation has been made in the case of goods manufactured in specified areas of the North-East[12].

The manufacturer should take reasonable steps to ensure that the appropriate duty has been paid on inputs or capital goods on which credit is availed, as indicated in the documents accompanying the goods[13].

The structure and procedures under CenVAT, as given above indicates that the new procedure results in transparency of the tax burden under the Union excise duty. In addition, it reduces cascading effect of input taxation as well as the pyramiding effect of the tax. Also, it generates a mechanism to check evasion of tax through self-policing. The empirical studies on impact of introduction of CenVAT show that there is a definite positive effect. In fact, the industrial units have been able to save on interest (ranging between 0.5 and 1 percent of the total duty paid). Also, the overall effect has been revenue neutral and has not caused any price effect.

In addition, the reforms implemented under UEDs during last ten years have simplified its structure especially through CenVAT. While previously there were large number of rates, over the years it has been brought down considerably. As of today, the general rate of CenVAT is 16%. However, in many cases the actual duty paid on inputs could be less than tariff rate through exemption notifications. In addition, there are three rates category (viz., 8, 16, and 24 percent) of special excises. These also are given credit for tax paid on inputs[14]. Apart from rationalisation of rate structure, exemption notifications have also been curtailed and the specific rates are converted into *ad volrem* rates. Further, the rate structure of CenVAT is linked to the Harmonized System of Nomenclature (HSN), at present in vogue in more than 130 countries for providing help in international trade.

2.2 Administrative Controls under CenVAT

The administrative controls under the UEDs (or the CenVAT) fall in some categories, described below:

a. Physical Control: This is the oldest form of control under the Union excise duty. Under this control, there is an assessment of tax by the Central Excise Officer, posted at the factory, before the removal of goods. Thereafter, the goods are moved under his supervision and under the cover of an invoice countersigned by him. This system is now restricted to cigarettes only.

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[12] See Rule 57AJ.

[13] These documents are prescribed in Rule 57AE.

[14] Credit is also available for AD(ST) and AD ($T_{\&}AT$) and the component of CVD relating to AD(ST) and AD($T_{\&}TA$). Such credit, however, can be utilised only for payment of AD(ST) and AD($T_{\&}AT$).

b. Self-Assessment Procedure: This was previously known as self-removal procedure (SRP). Under this procedure, the assessee files a classification declaration for his goods in quadruplicate under Rule 173 B to inform the department of the claimed rate of duty applicable to his goods. If the rate of duty is *ad volrem* and the assessee sells goods to a related person or he has factories manufacturing similar goods in different Central Excise Divisions or Commissionerates or he removes goods for captive consumption etc., he should also file before the Assistant Commissioner a price declaration under Rule 173 C in the prescribed form in advance. The assessee himself assesses the duty due on the excisable goods intended to be removed and pays duty on a fortnightly basis.

c. The Compounded Levy Scheme: This is meant for small scale decentralized sector and at present covers embroidery, marble slabs, stainless steel Pattis/Pattas and aluminium circles. Under this scheme the duty for a specified period is fixed on the basis of the number and the type of machines. Payment of tax under the compounded levy absolves the manufacturer from observing day-to-day formalities of CenVAT regarding maintenance of accounts and removal of goods etc.

d. Collection of Duty at the Point of Consumption: This duty is confined to Khandsari Molasses going for manufacture of alcohol, whether for potable or industrial use. The duty is to be paid by the distilliers on the date of receipt of Khandsari Molasses. The CenVAT credit is admissible on Khandsari Molasses to the extent it is used for manufacture of dutiable excisable goods.

e. *Levy of Excise Duty on the Basis of Capacity of Production*: A new Section 3A introduced in the Central Excise Act through the Finance Act 1997 enables the Government of levy a duty at the notified rate on the notified commodity on the basis of production capacity as determined by an officer not below the rank of Assistant Commissioner of Central Excise, in place of actual production. The assessee, has however been given the right to represent on the basis of evidence of actual production being lower and in that case the proper office will determine the quantum of actual production to be taxed after observing the principles of natural justice. The scheme is now applicable to independent textile processors only.

2.3 Obligations under CenVAT

As in the case of dealers under VAT in other countries, CenVAT has also introduced VAT procedures under the CenVAT. It has placed some obligations on the part of the dealers paying CenVAT. The declarative and accounting obligations are as follows:

Declarative Obligations:

The administration of CenVAT requires various declarative obligations as given below:

a. Tax Payer Registration: Every manufacturer of excisable goods (except small scale manufacturer) is required to get himself registered before the commencement of production. Registration is valid for the premises for which it is granted. That is, a manufacturer having more than one premises must obtain a separate registration for each of the premises from the respective Range Superintendent having jurisdiction over the premises, may it be a factory or a depot/branch office. If a manufacturer desires to start production of a new product he should get his registration duly endorsed to this effect. There is no fee for registration and there is no need for its renewal. In addition, to the manufacturer, since 1994, even wholesalers (i.e. dealers who intend to pass CenVAT credit to its buyers), could be registered. This system has been introduced to help small manufacturers.

b. Issue of Invoices: with effect from 1st April 1994, invoice has replaced the gate pass (GP-1) as the clearance document. It is prescribed that the invoices should be serially numbered for each financial year. An invoice must accompany the consignment, each time the goods are transported from the factory to the godown of the manufacturer. To keep track of the clearance of goods from the factory, each accompanying page of the invoice book should be pre-authenticated by an authorised officer of the assessee and be serial numbered in the book and the numbers intimated to the Assistant Commissioner in advance. Manufacturer paying duty exceeding Rs. 10 crore have been exempted from intimation and authentication. Invoices are required to be issued in quadruplicate. In the case of petroleum products, there is a provision for removal of dutiable goods from the factory to warehouse without payment of tax. In such cases subsidiary gate pass (GP-2) is required to be issued. The subsidiary Gate Pass called certificate in lieu of GP-1 is issued when the consignment of duty paid inputs moves first to another consignee or destination and thereafter a part of it is supplied to a manufacturer availing CenVAT. It is provided that the CenVAT credit could be taken through the invoices issued by the first and the second stage dealers of excisable goods only. The credit cannot be taken on the basis of the invoices that are issued by the third and the subsequent stage dealers. Thus, the scheme of invoices has the following features:

i. The first stage dealer is defined as one receiving the inputs directly from a manufacturer or his depot under the cover of an invoice issued under Rule 52A.

ii. The second stage dealer is one who purchases from the first stage dealer.

iii. No credit can be availed on the strength of an invoice issued by the second stage dealer unless the invoice is authenticated or countersigned by the proper officer having jurisdiction over the second stage dealer.

iv. Both the first stage and the second stage dealers should be registered with the central excise department.

c. Monthly Return: The manufacturer is required to pay CenVAT on fortnightly basis and submit a monthly return (RT12) to the Superintendent of the Central Excise by

the 10th of the month following the month during which duty was paid. Manufacturers availing of the small scale exemption, based on value or quantity of clearances during a financial year, need to file his return only on a quarterly basis. The return must contain:

- Particulars of goods manufactured and cleared and amount of excise duty paid:
- Particulars of inputs received during the month and the amount of duty taken as credit; and
- Information on total duty paid through PLA (account current) and CenVAT credit giving details of disposal of inputs and utilization of the credit.

d. Other Documentary Obligations: In addition to the monthly return, at the time of clearance the manufacturer is required to submit the extracts of PLA and CenVAT accounts to the Superintendent of the Range.

Accounting Obligations:

With the introduction of CenVAT, maintenance of statutory accounts has been done away with. That is, the manufacturer on his own shall maintain his records regarding receipt, disposal, consumption and inventory of the goods containing relevant information[15]. If CenVAT credit is taken or utilised wrongly, the same, along with interest, will be recovered and, if the same involves fraud, willful mis-statement, collusion, suppression of facts or contravention of the provisions of the Act or the Rules, mandatory penalty and interest will also be attracted[16].

For this purpose a Personal Ledger Account (PLA) is also maintained. The duty is paid fortnightly/monthly. The amount of duty payable is recorded in daily stock account under rule 53 before clearance.

The manufacturers to pay duty on the final products cleared by them could use PLA account or the CenVAT credit.

Special Audit: In addition to the already existing powers under section 14 of the Central Excise Act (to summon persons to give evidence and to produce documents), the excise department is empowered to go into the cost structure of the goods manufactured through a cost-audit so as to decide whether there is under-invoicing. The new sections 14A and 14AA make provision for special audit in certain cases. These sections envisage an audit within a limited period with some important conditions stipulated. As far as the department is concerned, the cost-audit report would prevail to determine the assessable value, notwithstanding any cost audit done in the unit under any law viz. the Companies Act, 1956. The expenses including the fee for the cost accountant would be borne by the

[15] The burden of proof regarding admissibility of the CenVAT credit lies upon the manufacturer. See Rule 57AE (2) & (3)].

[16] See Rule 57AH read with Sec.11A. 11AA, 11AB and 11AC.

department. It is important to note that the powers under section 14A and 14AA is exercised at a very high level. Power under section 14A is exercised by the Chief Commissioner of Central Excise and under 14AA is exercised by the Commissioner of Central Excise. In other words, the provisions of these two sections are invoked only under extraordinary circumstances and not as a matter of routine.

2.4 Weaknesses of the System under CenVAT

The existing structure of CenVAT (i.e. UED) and the procedures for its administration calling for specified obligations are characterised by the following weaknesses:

First, the existing procedures for physical controls are outmoded. In the context of the liberalized economy it is immaterial whether the tax is levied through UED or CenVAT, the physical control should have no place in the administrative system. It needs to be replaced by self-assessment procedure.

Second, the provision of registration of wholesalers has created plethora of loopholes in the system to avoid payment of tax. While it does help small dealers to claim set-off for the tax on their inputs, the practice has created additional work-load for the department to cross check their sales and purchases with the claim of set-off by the small manufacturers. The resulting cases of evasion are also large. Earlier, when Modvat provisions were liberalized and dealers in excisable goods were also permitted to register themselves under Rule 174 of the Central Excise Rules, 1944, any dealer of excisable goods could register himself with the Superintendent of Central Excise in charge of the Range in which he had premises. Under the liberalized procedure there was no distinction between a manufacturer, a first stage dealer, second stage dealer or a subsequent stage dealer. This led to fraud at a large scale when fictitious dealers were issuing modvatable invoices said to cover duty paid excisable goods, on the basis of which Modvat credit was being taken, fraudulently by various manufacturers. Detection of such fictitious invoices and fraudulent dealers became difficult, because cross verification could not be done either instantly through a computerized network or within a reasonable time through correspondence. As a result, a number of fictitious invoices said to cover duty paid excisable goods were floating in the system resulting in enormous amount of loss of revenue. When this was detected, the Modvat credit was restricted to the manufacturers, the first stage dealers and the second stage dealers. This has reduced fraud and issue of fictitious invoices to some extent. In fact, this could be further reduced if this facility is restricted to only the first-stage dealers and all the Central Excise Ranges and Divisions in the country are linked through a computer network.

Third, the coverage of CenVAT, as noted above, has not been extended to all the commodities. Initially, half the revenue was being derived through the commodities covered under it (initially under Modvat). Over the years the coverage has been expanded.

Now it accounts for approximately 92% of the revenue through commodities under CenVAT. The time is ripe to incorporate other excises also into the ambit of CenVAT.

Fourth, there is a special provision related to deemed credit. Under this facility a manufacturer takes CenVAT credit at specified rates for certain inputs without producing documents related to the payment of duty. Deemed credit is available only in respect of commodities where chain of various processes is broken due to some exempted goods that are used. For example, there is no duty on grey fabrics but CenVAT credit on yarn is allowed through deemed credit. Since in such cases, duty payment documents may not be available, it is felt that CenVAT credit at specified rates may be allowed. The inputs so specified are deemed to be duty paid unless they are clearly recognizable as non-duty paid. The deemed credit facility which was initially (i.e. in March 1986) given to the small manufacturers was extended to all the units after a month. Later on, it was restricted to items under the category of steel, ingots and re-rollables, certain flat products of steel. unwrought aluminum, copper, lead and zinc and waste/scraps of copper. However. with effect from 1st April 1994 it is applicable to iron and steel roller only. Also, it has of late been withdrawn on ingots and re-rollable materials of iron and steel when the clearances of the re-rollers exceed Rs. 7.5 million in a financial year. In the context of extension of CenVAT scheme to processed textile fabrics, through the Budget 1996-97 the government has declared final products in respect of which the deemed credit for the duty paid on inputs is available on such notified outputs.

Finally, while it is true that the declarative and accounting obligations, in general. have been reformed considerably, there is room for reforms in the procedures for PLA a/c.

3. State-VAT

At the State level, many taxes are levied on commodities and services. These include sales tax, state excise, motor vehicle tax and passenger and goods tax etc. Sales tax is the most important tax yielding almost two-thirds of the States' own tax revenue.

3.1 Structure of the Existing Sales Tax

All the States levy sales tax at the first-point of sale within the State under the State's sales tax laws[17]. Inter-State transactions are covered under the Central Sales Tax (CST) Act, 1956.

Under the CST Act, the tax is levied at the rate of 4 percent when sale takes place between the registered dealers of different States. The tax rate is 10 percent or higher (depending upon the local sales tax rate of the exporting State) when the sale is made to an unregistered dealer in another State.

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[17] See for details Purohit, Mahesh C (2001), *Sales Tax and VAT in India,* Gayatri Publications, Delhi-110052 (forthcoming).

A registered dealer collects the State sales tax in most of the States at the first-point of sale (or purchase). The rest of the dealers in the chain of transactions buy "tax paid goods". Delhi, Haryana, and Punjab levy tax, in general, on the last sale (or purchase) by the registered dealer. Even in these States, large number of commodities are taxable at the first-point of sale which yields more than half of sales tax revenue in respective States. Haryana levies tax at the first-point on 81 commodities yielding almost 60 percent of the revenue. However, when these commodities are bought by registered manufacturers a set-off could be claimed by them for the tax paid on input from their tax liability on sale of finished goods.

3.2 Weaknesses in the Existing Sales Tax System

Some reforms have been attempted in the field of sales tax. Notwithstanding these reforms, the existing sales tax suffers from a number of weaknesses.

The first and foremost deficiency relates to its cascading effect. At present the sales tax is levied on the gross value without allowing any credit or set-off for the taxes paid on inputs (i.e., tax is levied on gross value at the successive stage or stages).

Second, the existing system results in an uncontrolled incidence of the tax. The total effective incidence on any given final product at the end of the chain of production-distribution process would be fortuitous. This is, however, not very clearly seen by the consumers because the tax system lacks transparency.

Third, there is the problem of multiplicity of rates. Prior to the reforms in the sales tax system, all the States, in their attempt to have fine gradations of necessities and luxuries, provided for a plethora of rates. Quite a few States had as many as 17 rate categories. In recent months the States have attempted to adopt uniform floor rates that has checked the number of rate slabs considerably. However, a large number of rate-slabs are still in existence under the present sales tax system. The rate slabs range from 6 to 15 in many States (Table 1). It is useful to recall that the *Report of the Finance Ministers Committee (1995)* has presumed that by having floor rates, in the medium run, the *competition may be expected to lead to a convergence of rates*. It is expected that the rate categories would automatically be reduced to *four*. While the market forces might take some time, the concept of a few rate categories needs to be adhered to.

One of the reasons for the large number of rate-slabs is the differential treatment to the goods falling in the residuary entry (8% rate). While the *Report of the Finance Ministers Committee* has implied only one rate on all those goods "*not classified elsewhere*", the States have adopted "the existing rate" or "*any rate*" on the items not specified in the List. It might be useful if the Empowered Committee considers having one of the existing rate slabs for these commodities.

Another factor adding to this phenomenon is application of a higher rate than the floor rate. While in principle, the States have the legitimate right to introduce higher rate,

the number of rate categories need to be kept in mind. As these have to be as few as possible for the introduction of VAT, if the States want to have higher rate, it should be in the next rate-slab. Here it is important to bear in mind that the multiplicity of rates not only blunts the progressive effects that are intended to but also creates the need for additional calculations by the dealers.

Heterogeneity prevails in the structure of tax as well. In addition to general sales tax, most States levy an additional sales tax, turnover tax or a surcharge. Additional tax is based either on their total turnover or on the graduated turnover with different rates for different slabs of turnover. Similar practices prevail in regard to turnover tax as well as surcharge. Owing to heterogeneity in rates and structure of tax, there is an increase in the cost of compliance.

Fourth, economic consequence of widespread taxation of input leads to vertical integration of firms, i.e., the existing system of taxes militates against ancillary industries and encourages them to produce more and more of the inputs needed rather than purchase them from ancillary industries.

Finally, the existing system of sales taxes lacks neutrality. It interferes with the producers' choice of inputs and outputs as well as with the consumers' choice for consumption, thereby leading to severe economic distortions[18].

3.3 Efforts at Introducing State-VAT

In view of the above deficiencies in the existing structure of sales tax, it is important to replace this with VAT at the State level. Efforts in this context are being made for last many years. The Committees of States' Finance Ministers (in 1995 and 1998, respectively) and of the Chief Ministers (in 1999) have put forth recommendations to replace sales tax by VAT. This has now been ratified by the Conference of Chief Ministers and Finance Ministers on November 16,1999. This is in tune with the developments in all other countries, including developing countries, where VAT is a proven success. In this Conference, the Chief Ministers and Finance Ministers have resolved to introduce some major reforms.

The first reform relates to the adoption of a four-rate structure (i.e. zero, 4, 8 and 12 percent) in the existing sales tax. In addition, there are two special rates of 1 percent and 20 percent for a few specified items. The recommended rates are floor rates – the States have the freedom to adopt higher rate on any of the commodity from the list, but they cannot go below these rates. This checks the rate war and prevents diversion of trade. Here it is important to indicate that when the States started implementing the four-rate categories immediately after the Conference of the Chief Ministers held on 16th November 1999, many of them found it difficult to follow the floor rates in some commodities. Either the classification had some problem or there were administrative difficulties in

[18] See for details *Ibid*.

implementing the floor rates. Hence, the Standing Committee of Finance Ministers made a few changes in the items falling under exempt list. Some changes were made in the items falling in other categories as well. This was necessitated due to the fact that the *Report of the Finance Ministers Committee (1995)* had suggested that *"fine tuning of this classification would have to be done by a special group"*. As this was not done prior to the adoption of floor rates, it is of paramount importance that the same is attempted now. It is hoped that the existing Empowered Committee would attempt this exercise when the existing sales tax classificatory scheme is converted into HSN system. It is important to note that the Centre for Taxation Studies, Thiruvananthapuram (Kerala) is already putting efforts to complete this work. Once this is completed and the Report on HSN classification is available, another look would be given to the floor rate scheme. However, the list of floor rates of four-rate categories, as finalised by the Empowered Committee of State Finance Ministers is appended as Annexure I to this paper.

The second reform pertains to abolition of sales tax-related incentives. In the past, all the States granted such incentives to new industries. These were given in one or the other form of exemption from tax on the purchase of inputs as well as on the sale of finished goods. Incentives were also available in the form of sales tax loans and/or tax deferral. Various studies and committee reports[19] have already argued against such incentives. In terms of loss of revenue, all the States put together sacrifice about 25 percent of the sales tax base. In addition, the incentives take the form of tax competition (war) or *harmful tax practices*[20].

The States would find it convenient to adopt VAT without much difficulty once these reforms are implemented.

3.4 Experimenting with VAT in Indian States

The experience of introduction of VAT (in some or the other form) by some of the Indian States in the past is of great importance for the other States. Some of the States that have experimented with VAT, faced many problems of administrative or operational nature, in their efforts to introduce VAT.

Andhra Pradesh is one of the States that has introduced VAT on some select items with effect from April 1, 1995 for resellers only, with rate of tax of 4% on inputs

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[19] See especially the Report of the *Finance Ministers Committee to Chart a Time Path for the Introduction of VAT* (August 1998) and the Report of the *Committee of Finance Secretaries for Identification of Backward Areas* (November 1999).

[20] The empirical studies attempted for the NCR Region indicate that the concessions of sales tax do not affect the location of industry. The concession could be relevant, if at all, when given by one State alone. Similar results are seen from the other studies as well. When all the States give such concessions, such concessions result in zero sum game. No State benefits from these concessions. See for details, Purohit, Mahesh C *et. al.(1992),Fiscal Policy for the NCR Region*, Vikas Publishing House, New Delhi. In most countries of European Union or OECD some regional development incentives are offered only through income tax. These are akin to the backward area incentives already prevalent in the Indian income tax law. There are no schemes of incentives in place, which are related to sales tax (VAT-type) instruments.

applicable to all manufacturers. Prior to the introduction of VAT, Andhra Pradesh abolished the (then) existing surcharge and turnover tax. It also reduced the rate slabs to six only.

Kerala is another State that levied VAT on resellers on a few select commodities. While doing so, it did not grant set-off for the tax paid on inputs. No efforts were made to rationalize the structure of tax prior to the introduction of VAT. In addition, a graded surcharge was levied on dealers having different levels of turnover. However, with effect from April 1, 1997, Kerala has withdrawn VAT and replaced it by a double-point sales tax.

Maharashtra moved towards VAT from October 1, 1995. It attempted to simplify the existing structure prior to introduction of VAT. It abolished "additional tax" as well as "turnover tax". Also, it moved towards providing set-off on input-tax to manufacturers. Under the then prevailing rules, the input credit was available "for the tax paid above 4%". Taking into account the incidence of non-recoverable taxes such as "additional tax" and "turnover tax", the effective burden on inputs of the manufacturer was in excess of 6%. This burden was reduced to 4%. In addition, the rate slabs were drastically reduced from 20 to just seven. VAT was initially levied on all dealers having turnover above Rs. 1 crore. The coverage was extended to dealers with turnover above Rs. 50 lakh in 1996 and to Rs. 40 lakh from June 1, 1997. Also, the input credit was increased. Further, due to non-economic considerations the State has withdrawn VAT and replaced it by first-point sales tax with effect from April 1, 1999.

Madhya Pradesh followed the threshold approach and introduced VAT for dealers with turnover higher than Rs. 1 crore with effect from April 1, 1997. It brought down the threshold to Rs 50 lakh with effect from April 1, 1998. Also, it introduced one rate slab of 8 percent for all dealers falling under VAT. However, Madhya Pradesh has so far not given set-off for the tax on inputs in spite of the announcement made long back. Also tax on reseller is not in the true spirit of VAT. The most important aspect of VAT is to make it neutral and transparent system.

The experience of the States that experimented with some form of VAT indicates that except Maharashtra, no State has attempted introduction of a proper form of VAT so far[21]. It is misnomer to call a tax on resellers as VAT. The first and the foremost pre-requisite of VAT is to give input credit for all purchases. Also, there was no requisite preparedness on the part of tax department.

3.5 Reforms in Governance of State-VAT

The experiences from VAT experiments in different States indicate that the need of the hour is to have some reforms in the governance of State-VAT, when introduced. The first and foremost requirement relates to operating State-VAT through a single master file, based on unique tax identification number (TIN). The TIN should bear an economic activity

[21] Tamil Nadu announced introduction of VAT through this approach but so far it is in abeyance.

code based on International Standard Industrial Classification (ISIC). In addition, the TIN must have feasibility for comparison among different taxes such as State-VAT, CenVAT, and income tax (including tax on corporate income). The TIN would also aid in drawing a comparison of tax statistics with the national accounts. In addition, it would facilitate proper use of the database of various systems.

To have an effective and efficient governance of State-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.

In most States training of personnel needs prioritisation. The staff to administer existing sales tax is not adequately trained. The training is all the more crucial when it comes to administering VAT. Hence, it is extremely important that the staff must be trained adequately at all levels.

The officers of the commercial tax department are generally drawn from the State finance services. In some States this service is not even in existence. It is remarkable that at no stage of recruitment or promotions are these officers sent for appropriate training for the work they are required to do for the assessment of taxes. In some States, these persons do not even belong to the taxation department. It is, therefore, of paramount importance that those who are posted at the commercial taxes department are imparted proper training at the beginning of their career. The State should think of having personnel well trained in taxation services to serve better. The training now given to the officers directly recruited to the finance service of the State is, by all standards, inadequate. The course is for too short a period and the vital components of economics or accountancy do not appear much in the course contents. It is important that the new recruits earmarked for the taxation services be given intensive training for a period of not less than six months.

An important aspect of reform relates to procedures and the governance. One such aspect concerns assessment. At present all the dealers are called into the office of the sales tax with books of accounts. This procedure is not cost-effective. It is important that we switch over to a system of selective assessment. Selection of cases for assessment has to be made in accordance with various criteria, such as, size, turnover, and risk evaluation. It might indeed be useful to cull out a fixed proportion of large and medium sized dealers for assessment on a regular basis. Further, the assessment of VAT dealers should be supplemented by cross-checking of invoices. The most important aspect relates to use of Discriminate Function System for audit selection. This function could use other relevant sources such as names of suppliers, number of taxpayer deviating from the normal trend,

data on imports supplied by the customs department, and the information on the fast growing sectors of the economy.

A decision about the size of the firm under VAT is of critical importance. In fact, it is impracticable to include all the small dealers under VAT. Given their large number and low level of maintenance of records, learning from different country experiences[22], the States should have a threshold of Rs 5 lakh for registration. The dealers having turnover between Rs. 5 lakh and Rs. 25 lakh could be assessed on the basis of one percent tax on their turnover. The rest of the dealers, having higher turnover, would fall in the actual system of VAT. However, dealers dealing mainly in exports requiring refund could always go in for proper system of VAT irrespective of their size. This would enable them to claim full refund of tax involved in exports[23].

The above steps would gear the tax machinery in such a way that the administrative cost of VAT would be low and the compliance cost as well as the harassment to the taxpayers minimum.

The existing practice of monitoring of inflow of goods at the check-posts is an archaic method of tax administration. The introduction of VAT should be able to do away with such posts. As is known, this would reduce corruption and save considerable national truck time spent at these check-posts. It would also facilitate the country to have free flow of goods.

An important step in the introduction of VAT, however, is the need for all taxpayers to understand that VAT will be levied on their value added only and not on the gross turnover. Such an understanding will not cause any resistance and compliance problems from taxpayers. This requires that the government should vigorously campaign for the case of VAT. It should take the help of various national and regional Chamber of Commerce and Industry. The role of daily newspapers, TV and radio and other mass media is significant in the dissemination of knowledge to the users. There could be series of articles, question and answer sessions, feature stories and lectures discussing the need for adopting VAT. Various pamphlets on VAT could be printed and distributed through out the country.

While sufficient lead-in-time is required to prepare for the introduction of VAT, we should take note of the fact that the States have got good experience of administering a turnover tax and a first-point sales tax. The reform process to reduce the rate categories and computerising the system of administration has already begun in many of the States. The National Institute of Public Finance and Policy (NIPFP) has already prepared a *Model VAT Law* for the implementation of VAT. It is useful to note that while many countries took two to three years in introducing VAT, Chile was able to reduce the lead-in time to a few

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[22] See for details Purohit, Mahesh C (2001), *Value Added Tax: Experiences in India and Other Countries*, Gayatri Publications, Delhi-110052, *op. cit.*

[23] See NIPFP, (1998), *Model Statute for Value Added Sales Tax in India*, New Delhi.

months because of its prior experience with a turnover tax. Given the experience of Indian States in sales tax system, 18 months is a sufficient lead-in time for the government to anticipate the transitory problems associated with VAT reform and to implement policies and measures to effect a smooth transition.

3.6 Schedule of Activities for Introduction of State-VAT

Keeping the above aspects in view and also the decision to introduce VAT in all States from April 1, 2002, the following time schedule of activities has been approved by the Empowered Committee of State Finance Ministers. All the States/Union Territories are expected to follow the schedule given below:

- *Time to be spent 1 month – balance time 16 months*: Finalising design of VAT for inter-State transactions (i.e. the decision on rates path of CST) and intra-State transactions (i.e. whether to follow a single-rate VAT or three-rate structure). It should also include coverage of VAT (whether including services) and issues related to transitional measures (about tax paid inventories, continuing contracts etc.).

- *Time to be spent 3 months – balance time 14 months*: Preparation of Draft Legislation of VAT and passing of the same by the State Assembly. Finalisation of procedures for VAT administration including registration of VAT payers, collection procedures, processing of returns, and audit for VAT, design of VAT Return Forms, VAT Payment Form (chalan), Registration Form (a Model VAT Law has already been prepared and circulated to all the States by the NIPFP. The law prepared by Madhya Pradesh could also be circulated to the States) The Empowered Committee must decide on the design of all forms for the sake of uniformity.

- *Time to be spent 6 months – balance time 11 months*: Organise workshop on business process and computerisation for VAT administration, determining system's design and identifying resource requirements.

- *Time to be spent 8 months – balance time 9 months*: Starting preparation for extensive information campaign and publicity literature. Training of officials at the State level.

- *Time to be spent 9 months – balance time 8 months*: General campaign added with articles, brochures, advertisements and publicity through media. Publishing detailed procedures for VAT including business process model. Designing criteria for selection of cases for assessment.

- *Time to be spent 13 months – balance time 4 months*: Test the computer software and hardware for VAT. Start registration process with new TIN for VAT. Interact with banks on procedures for receiving returns and VAT payment.

- *Time to be spent 15 months – balance time 2 months*: Complete allocation of new registration numbers.

The above steps indicate that most of the activities are to be attempted on a continuing basis. In addition, the Empowered Committee would have a regular review of the progress in regard to the above activities. These steps would gear up the tax machinery in such a way that the administrative cost of VAT would be lower and compliance cost as well as the harassment to the taxpayers minimum.

3.7 Reforms in CST

Along with reforms of sales tax on intra-state transactions (i.e. GST), it is important to have reforms in sales tax on inter-State transactions (i.e. CST).

Historically, CST was introduced to (i) maintain competitive conditions between local dealers and out of State dealers; (ii) ensure that the exporting States get a small share of the total tax that is leviable on a given commodity and (iii) regulate and monitor inter-State trade. Accordingly, it prescribed two different rates of tax: (i) one percent on inter-State sales to registered dealers; and (ii) 10 percent on inter-State sales to unregistered dealers. The higher rate is charged on sales to unregistered dealers because the State sales tax (GST) is also charged on the sales made by registered dealers in the consuming State but no tax is charged by that State on sales made by unregistered dealers[24] The higher rate of tax on the unregistered dealer prevents him from entering into inter-State trade for any competitive advantage. By the same logic, the low rate (of one percent) is charged from registered dealers because the same commodity is taxed by the importing State also. The rate differential brings about equity of treatment of registered and unregistered dealers.

Over time, the Central government has abandoned the regulatory objective of the tax and raised the tax rate from one percent in 1956 to two percent in 1963, to three percent in 1966 and to four percent in 1975.

While the CST has served the purpose of regulating the flow of inter-State movement of goods within the country, it is important to recognise that CST is economically irrational and harmful tax. It has caused following deleterious effects on the economy of the country:

First, the high rate of tax under CST has caused severe obstruction to the formation of a common market within the Indian federation. In contrast to the principle of unified market, it encourages consumers to buy locally produced goods at the expense of the national economy and economic unity of the country. With the opening up of the economy, this may also encourage import of goods from other countries at the expense of the national economy.

Second, the existing high rate of CST has created conflict with the principle of inter-jurisdictional equity and caused horizontal imbalance among States. The high incidence of CST discriminates against the consuming States. The States dispatching raw materials first

[24] If the local sales tax rate in the exporting State is higher than 10 percent, the unregistered dealer in importing State has to pay the higher rate.

levy CST on inputs. The States manufacturing commodities and exporting for consumption again levy it. That is, the incidence of the tax both on inputs and on finished goods is borne by the consumers of the importing State. At the same time, industrialised States collect the bulk of sales tax revenue[25].

Third, the CST levied on inputs and on finished goods at early stages of transaction causes cascading effect. This results in higher prices when inputs are sold from one State to another and manufactured goods are sent from one State to another bearing CST. Cascading increases further if CST is levied twice on finished goods due to movement of goods in more than one State.

Fourth, to the extent the tax is passed on to the buyers, the CST is used as a measure to 'export' the tax of producing States to the consumers in other States. It, therefore, puts a higher burden on consumers situated in the importing States than the producing State on all commodities not produced therein. This is to the detriment of States that happen to be net importers.

Finally, the tax on inter-State trade puts a burden on exports. While in principle, the CST provides for exemption of tax on exports, the exemption is available provided the last sale takes place after and is for the purpose of complying with the agreement, or order for, or in relation to such exports. In practice, it is difficult for the exporters to purchase commodities against confirmed orders. Purchases made in anticipation do not qualify for exemption. Such conditions give rise to disputes as to whether a given sale can be regarded as a penultimate sale. The tax treatment of inputs among the States being heterogeneous, exports bear the burden of tax to the extent the tax is levied on raw materials or at an early stage of its manufacture. The Indian manufacturers are thus put to a competitive disadvantage in the international market.

In view of the above weaknesses of the existing system of tax on inter-State trade, its reform is of paramount importance. It attains urgency in view of India's acceptance of the agreement to create a free trade area comprising the SAARC countries by 2001. In the event of our being part of SAARC free trade zone, phasing out CST and having destination based system would be the only way to face competition from the SAARC countries on a level playing field. It is, therefore, 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 3 percent. The union government must compensate the States for the loss of revenue due to rate reduction. Theoretically, this should mean a loss to the extent of 25 percent in the revenue from CST to each of the States. The total amount of CST collected by all the States together being under Rs 9,000 crore, 25 percent of it would be about Rs

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[25] Five States in high-income group (Gujarat, Maharashtra, Andhra Pradesh, Karnataka and Tamil Nadu) collect the bulk of CST revenue (60.9 percent in 1997-98). Six high income States with 36 percent of the country's population account for 45 percent of the total revenue of CST, while the low income States with 41 percent of the population get only 13 percent of the CST revenue.

2250 crore, with varying amount to each State. The union government could compensate the States for this loss, say for a period of 3 to 5 years.

In the next 2 to 3 years, the CST could be further reduced to 1 percent or brought down to zero percent. Giving the power to levy tax on some select services could compensate the States.

4. Further Reforms in Harmonisation

The current phase of tax reforms is an important step forward. It is linked to the on going structural reforms. All these attempts are important and are likely to have far reaching implications for the reforms of the overall structure of the commodity taxes in the country. With proper procedures adopted in the CenVAT and States converting their sales tax into a State-VAT, India would have a system of dual VAT: a CenVAT levied by the union government (to replace the Union excise duties) and a State-VAT (to replace the existing sales tax) by the States. Even for such a system to be implemented we need to make special efforts.

First, a smooth implementation of VAT requires a mechanism to oversee its operation. Failing this, the problem of harmonisation crops up. The experiences of other counties including European Union and Brazil indicate the need for such machinery. India requires two-tier machinery *viz.* an apex body dealing with policy issues and a functional body overseeing the operations. Such regulatory bodies have already been set up. A regulatory body in the form of a *VAT Council of States*[26] comprising Finance Ministers has already been appointed by the Union Finance Minister to provide policy guidance and to over see the implementation of these decisions. Also, a *Standing Council of Commissioners*[27] has been set up to oversee the operational problems of VAT implementation.

Second, the management of VAT in India calls for separation of duties of different functionaries of VAT department. For example, the work related to revenue receipts and follow up action of the defaulters is an important component of VAT management. It requires special attention on delinquents. In some countries this is taken care of by contacting dealers on phone, sending them reminders and visiting them personally. Auditors on the other hand are specialised officers trained to look into the accounts of the dealers. They have also the experience of attempting risk analysis and working in verification and enforcement branch. It is important to note that many of the countries appoint departmental officers with a general qualification (say, the first degree) and train them in special functional areas such as audit or electronic commerce. We have also to attempt functional re-organisation of the department to provide for separation of duties of different officers. This is essential to have efficiency in the working of department.

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[26] See Resolution No. F.No. 31/11/99-ST dated 24th February 2000, Department of Revenue, Ministry of Finance, Government of India, New Delhi.

[27] See Resolution No. F.No. 31/11/99-ST dated 24th February 2000, Department of Revenue, Ministry of Finance, Government of India, New Delhi.

Third, the integrated management information system (MIS) is a prerequisite for obtaining all the information from tax returns of individuals and of corporations. This would enable the tax department to have access to necessary data for 'risk management'. In fact, the coordination of VAT department with all the tax departments is extremely useful. In India, at present the administration of federal taxes such as income tax and CenVAT is quite independent. This is equally true of sales tax. In the context of introduction of VAT, it is important to develop procedures that would have complete coordination among all the tax departments.

Fourth, the most important component being risk management, the tax department has to make use of the information collected through registration, submission of VAT return, claim for input credit, refunds and information flowing from income tax returns etc. This information is used to classify dealers into small, medium and large categories. 'Risk management' is attempted for selecting dealers from different size groups to perform thorough audit of these dealers. In the Indian context, it is important to evolve procedures to undertake 'risk management' prior to introduction of VAT.

Finally, it is of paramount importance that we concentrate on this activity to reduce interaction of dealers with the department. Availability of authentic information should be a matter of right for the dealers. Requisite publicity of their rights and duties with do's and don'ts and use of telephone and electronic means would help developing proper provisions for introducing VAT in India.

5. Towards a Comprehensive State-VAT

Even when India adopts a system of dual VAT, as discussed above, the cascading effect of CenVAT on State-VAT and *vice versa* would continue to be there. The ultimate solution for reducing cascading altogether lies in the adoption of a full State-VAT. This could be possible if the Centre withdraws from the field of VAT (leaving aside a few sumptuary excises), and the States have the full commodity tax regime to implement a comprehensive State-VAT. This could as well be an agenda of second-generation reforms.

Keeping in view the federal considerations and to have a harmonised system of VAT at the State level, we could consider a scheme of tax devolution based on criteria that takes care of fiscal balance and provide for rational tax structure in the country[28]. Basic to the proposal are the following:

First, the resources from VAT are primarily meant for the States only. However, for the administrative reasons, the Centre could also collect the tax for the use of the States. In effect the VAT would belong to the States only.

Secondly, notwithstanding the allocation of existing powers, the revenue from the taxes is distributed between the Centre and the State governments in such a way that in

[28] See, "Assignment of Taxing Powers for Fiscal Balance" in Srivastava, D K (ed.) (2000), Fiscal Federalism in India: Contemporary Challenges - Issues Before the XI Finance Commission, NIPFP, New Delhi.

effect the power to levy and use revenue for VAT rests with the States. It may be mutually exclusive as well.

Similar to other federations[29], in India too, the States would levy a comprehensive State-VAT[30]. European Union, which could also be considered as a federation, has successfully introduced and practised a system of State-VAT. Over the years, the Commission of the European Union has harmonised the system - each member State has its own VAT with floor rates imposed by the Commission[31]. The experience, therefore, suggests that State-VAT is not only desirable but also the only long run reform feasible under the Indian Constitution.

Under the proposed system of assignment of taxing powers, the Centre would divide the existing system of UEDs into two:

First, sumptuary excises (SEs) would be levied by the Central government on a few select commodities only. These would at the most be a dozen in number. The Centre would retain the revenue generated from the SEs. The SEs would yield to the Centre approximately the same revenue from the UEDs (Table 2), which used to be retained by it (i.e. 52.5%) for its own use on the basis of the recommendations of the Tenth Finance Commission. While considering devolution of 37.5% of the revenue of all the taxes, as per the later Finance Commissions, the central kitty would have to take note of this.

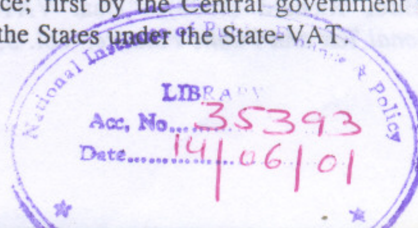
The second component of UEDs (i.e. excluding those brought under SEs), called CenVAT, would continue to be collected as is being done today. However, it would not be treated as Central revenue for the purpose of Finance Commission devolution. It is in fact to be treated as a State tax being collected by the Centre. Accordingly, its yield would be distributed among the States on the basis of collection. This would allow the States to give set-off for the tax paid to the Centre at the manufacturing level. The manufacturers under the proposed system would be taxed twice: once by the Centre under the CenVAT[32] and the second time by the States under the State-VAT. However, the States would give set-off if the taxpayer has already paid CenVAT. That is, the Centre would follow the scheme of VAT for the whole of the manufacturing sector avoiding cascading effect and offering attendant advantages of the system. This reform would warrant the Finance Commission to continue playing its part but with some difference.

[29] See Purohit, Mahesh C. (1995), *VAT in Brazil*, NIPFP, New Delhi. Also, see Purohit, Mahesh C. (2001), *Value Added Tax, op. Cit.*

[30] Such a proposal is given in many studies. See for example, Purohit, Mahesh C. (1993), "Adoption of State-VAT in India: Problems and Prospects", *Economic and Political Weekly*, March 6, pp.393-404: Burgess, Howes and Stern in Purohit, Mahesh C. and Vishnu Kanta Purohit (1995), *Commodity Taxes in India*, Gayatri Publications, Delhi.

[31] See for details, Purohit, Mahesh C. (2001), *Value Added Tax, op.cit.*

[32] Under the concurrent VAT the manufacturers are taxed twice; first by the Central government under the Central-VAT and next time on the CenVAT-inclusive price by the States under the State-VAT.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- In doing so the Finance Commission has to adopt two different approaches: one for those States that would introduce VAT and another for the rest of the States. The existing State revenues for all the States, as shown in Table 3, would then change considerably. The change has to be different for those adopting VAT and those continuing to levy sales tax.

- As regards States introducing VAT, the yield from the tax would be distributed to the States on the basis of collection. This principle would be necessary for the States that adopt a system of VAT and grant set-off for the tax paid by the manufacturers to the Centre. The effect of devolution of CenVAT on the basis of collection is given in Table 4.

- For the rest of the States the distribution would be made on the basis of criteria such as population and, index of backwardness as recommended by the Finance Commission.

- The empirical estimates of the fiscal impact on the States due to the adoption of State-VAT are presented in Tables 5 and 6. The data indicate that: (i) The States' own tax revenue (SOTR) increases because of the inclusion of the yield of the CenVAT (which is now given to the States on the basis of collection) which yields larger resources to producing States. However, it is important to note that there would be considerable amount of set-off of the taxes already being collected. The yield of the tax on inputs (accounting for approximately one-fourth of the total) and on goods entering into inter-State trade would also not be available to the States; (ii) The State-VAT being based on destination principle requires restructuring of CST, as discussed earlier. This would result in considerable decline in the SOTR in many States[33]; and (iii) The distribution of the proceeds of the CenVAT is based on collection. This enables the States to give complete set-off for the tax already collected by the Centre at the manufacturers' level. The set-off would be based on the invoice with the manufacturer. If a manufacturer is not within the purview of the CenVAT, the States could levy VAT on that dealer. In addition, the State-VAT would now be levied giving set-off for the tax paid at the earlier stage. That is, both the CenVAT and the State-VAT would be based on the destination principle.

The *modus operandi* of this implementation would be as follows:

Assume that the collection of the VAT at the Central level from different States is denoted by $X_{1,} X_{2,} X_{3,} X_4, \ldots X_n$ where the total tax collection equals

$$X = \sum_{i=1}^{n} X_i$$

[33] See Bird, Richard (1998), "Dual VAT and Cross Border Trade: Two Problems, One Solution". *International Tax and Public Finance,* Vol. 5, No. 3, July, 429-442.

Similarly, collection of State-VAT for n States is denoted as $S_1, S_2, S_3, S_4, \ldots S_n$. When a State has to give set-off for the tax under CenVAT, the State would have reduced collection from State-VAT indicated as $S_1', S_2', S_3', S_4', \ldots S_n'$ where $S_1' < S_1$, etc.

Let

$F_i = S_1 - S_1'$ denote fall in revenue from State-VAT due to set-off[34].

The effect of the set-off by the manufacturing sector could be calculated by employing input-output model where the inter-industry demand (IID) is given as:

$$IID = \sum_{i=1}^{n} a_{ij} X_j$$

where

a_{ij} = the input-output coefficient indicating the input of ith commodity per unit of output of the jth product; and

X_j = the total output of the jth product.

In matrix form it can be expressed as

$$IID = AX$$

i.e. the coefficient matrix A is post multiplied by the vector X to obtain the IID for the State.

For the rest of the transactions (such as wholesalers and retailers), the value addition could be estimated on the basis of data available from the *Directory of Trade Establishments*[35]. In general, the likely additional revenue due to value added or due to better administration caused by self-policing mechanism of VAT might cancel out against loss of revenue due to set-off for the inputs. Hence, while estimating the yield of SOTR any additional revenues have not been claimed; although in the long run it ought to generate additional yield. The empirical calculations given in Tables 5 and 6 illustrate the changed scenario in SOTR before and after sharing of CenVAT.

Estimates presented in the paper suggest that the State-VAT would not only give more revenues to the developed States but would also benefit others. This would be possible due to the fact that the yield of the tax would now be distributed among the States on the basis of consumption and on destination principle. In the context of the 73rd and 74th

[34] In addition, the Centre would also deduct its cost of collection on an actual basis. This would however be less than the cost of collection by the States.

[35] See Government of India (1989), *Directory of Trade Establishment Survey- Report on Trade Sector*, Central Statistical Organisation, New Delhi.

Constitutional Amendments, the States could raise further resources for the local self-governments by way of surcharges on State-VAT as a piggyback system.

6. Integrating other State Taxes under State-VAT

With the withdrawal of the Centre from the field of commodity taxes, there would be no dichotomy of taxing powers between the Centre and the States. States would be able to levy a comprehensive State-VAT. As a next step, it should be useful to combine all the taxes on commodities and services levied by the States. In addition to sales tax, the State Governments are levying the following taxes under this category.

1. excise on alcoholic liquor for human consumption, opium, Indian hemp and other narcotic drugs
2. taxes on the entry of goods into local areas for consumption, use or sale therein (octroi levied and collected by local authorities through delegated power)
3. tax on the consumption or sale of electricity
4. tax on goods and passengers carried by road or inland waterways
5. tax on vehicles suitable for use on roads
6. tax on animals and boats.
7. tolls
8. tax on luxuries including tax on entertainment, amusements, betting and gambling .

When sales tax is converted into a State-VAT, some of the taxes mentioned above namely electricity duty, entertainment tax, and luxury tax on hotels could be integrated in the State-VAT.

Taxes on motor vehicles, passengers and goods tax are in the nature of regulatory taxes. In addition, many of the States have compounded these taxes. Some of the States have merged the taxes into one. In addition these taxes have inter-State ramifications. These are also used to control vehicular pollution, else these could still be retrained as separate taxes. Entry tax, octroi, tax on animals and boats and hotel tax could be integrated into the State-VAT. Tolls could, however, be levied in respect of new bridges for the maintenance of the roads.

Finally, as already recommended by the Empowered Committee of State Finance Ministers, when the State Governments are authorized by the Centre to levy tax on some of the localised services, including sales tax related services (such as service component of works contract), these also could be integrated in to the State-VAT.

Table 1: Rate Slabs of Sales Tax in Different States

States	Rate-Slabs															No. of Rate Slabs
Andhra Pradesh	0%	1%	4%	8%	10%	12%	16%	19.33%	20%	70%*						10
Assam	0%	1%	4%	8%	12%	20%										6
Delhi	0%	1%	4%	6%	8%	12%	20%									7
Gujarat	0%	1%	2%	4%	6%	8%	12%	14%	15%	20%	22%	54%*				12
Haryana	0%	1%	2%	4%	5%	8%	10%	12%	20%							9
Himachal Pradesh	0%	1%	1.5%	3%	3.5%	4%	8%	10%	12%	15%	30%**					11
Jammu and Kashmir	1%	4%	8%	12%	20%	30%										6
Karnataka	0%	0.25%	1%	2%	4%	8%	10%	12%	15%	20%	60%*					11
Kerala(#)	1%	4%	8%	12%	17%	20%	24%	25%	27%	30%	37%	55%	85%			13
Madhya Pradesh	0%	1%	2%	4%	8%	12%	20%	25%(a)								8
Maharashtra $	0%	0.5%	2%	4%	8%	10%	12%	13%	20%	24%	25%	27%	30%	33%		14
Meghalaya	0%	1%	4%	8%	12%	20%	25% (b)									7
Nagaland	0%	1%	4%	8%	12%	20%										6
Orissa	0%	1%	2%	4%	6%	8%	10%	12%	16%	18%	20%					11
Punjab	0%	1%	2%	3%	4%	5%	6%	8%	10%	12%	20%					11
Rajasthan	0%	2%	4%	5%	6%	8%	10%	12%	16%	20%	22% (a)	43%*				12
Sikkim	0%	1%	4%	8%	10%	12%	20%									7
Tamil Nadu	0%	1%	2%	4%	8%	10%	11%	12%	16%	18%	20%	24% (a)	30% (d)	50%*	70%*	15
Tripura	0%	2%	4%	5%	6%	7%	8%	10%	12%	13%	14%	15%	20%			13
Uttar Pradesh	0%	1%	2%	2.5%	4%	5%	6.5%	7.5%	8%	10%	12%	12.5%	15%	20%	32.5% (e)	15
West Bengal	0%	1%	2%	3%	4%	4.55%	5%	7%	7.5%	8%	10%	12%	15%	17%	20%	15

* Tax on liquor.

** Tax on firewood, timber and liquor.

a. Tax on motor spirit.

b. Tax on lime.

$ All rates greater than 20% are for motor spirit including aviation turbine fuel.

(d) Tax on molasses.

(e) This applies to liquor, narcotics and rectified spirit.

(#) 24% on lubricating oil and other petroleum products not mentioned in the 2nd Schedule. 25% on non alcoholic drinks, 27% on HSDO, 30% on petrol other than naphtha and aviation turbine fuel, 55% on beer & wine, 85% on other than beer & wine.

Table 2: Items to be brought under Sumptuary Excises under UEDs

(Rs crore)

Sl. No.	Items	Yield (1997-98)
1	Petroleum Products	8206.6
2	Tobacco & its products	3648.7
3	Motor Cars, etc.	1659.8
4	Cement Clinkers, etc.	2375.3
5	Chemicals & Dyes	1926.4
6	Tyres & Tubes	1442.9
7	Plastics & articles thereof	1776.2
8	Arms & Ammunitions, etc.	25.4
9	Precious Stones, etc.	5.2
	Total	**21066.5**

Source: Government of India, Receipts Budget, 1998-99

Table 3: State Revenue as per the Existing System (1996-97 RE)

(Rs lakh)

	States	SOTR	Shared Taxes	Grants in Aid	Total Cols. 2+3+4	Percent Share to Total Revenue		
						SOTR	Shared Taxes	Grants in Aid
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
A. HIGH	1.GOA	30,013	9,055	6,615	45,683	65.70	19.82	14.48
INCOME	2.GUJARAT	630,432	133,206	73,017	836,655	75.35	15.92	8.73
STATES	3.HARYANA	216,641	42,300	48,658	307,599	70.43	13.75	15.82
	4.MAHARASHTRA	1,199,980	214,592	176,314	1,590,886	75.43	13.49	11.08
	5.PUNJAB	280,679	52,835	59,384	392,898	71.44	13.45	15.11
	TOTAL(1)	**2,357,745**	**451,988**	**363,988**	**3,173,721**	**74.29**	**14.24**	**11.47**
B. MIDDLE	6.ANDHRA PRADESH	498,851	288,360	174,260	961,471	51.88	29.99	18.12
INCOME	7.KARNATAKA	604,442	172,980	121,159	898,581	67.27	19.25	13.48
STATES	8.KERALA	394,885	121,770	74,693	591,348	66.78	20.59	12.63
	9.TAMIL NADU	777,580	212,229	97,014	1,086,823	71.55	19.53	8.93
	10.WEST BENGAL	460,925	242,015	122,848	825,788	55.82	29.31	14.88
	TOTAL(2)	**2,736,683**	**1,037,354**	**589,974**	**4,364,011**	**62.71**	**23.77**	**13.52**
C. LOW	11.BIHAR	236,544	394,411	86,779	717,734	32.96	54.95	12.09
INCOME	12.MADHYA PRADESH	400,136	258,290	189,799	848,225	47.17	30.45	22.38
STATES	13.ORISSA	143,306	157,284	114,409	414,999	34.53	37.90	27.57
	14.RAJASTHAN	328,429	176,583	139,409	644,421	50.96	27.40	21.63
	15.UTTAR PRADESH	607,965	586,485	281,540	1,475,990	41.19	39.74	19.07
	TOTAL(3)	**1,716,380**	**1,573,053**	**811,936**	**4,101,369**	**41.85**	**38.35**	**19.80**
	TOTAL(15 MAJOR STATES)	**6,810,808**	**3,062,395**	**1,765,898**	**11,639,101**	**58.52**	**26.31**	**15.17**
D. SPECIAL	16.ARUNACHAL PRADESH	954	17,905	58,067	76,926	1.24	23.28	75.48
CATEGORY	17.ASSAM	83,810	117,556	187,855	389,221	21.53	30.20	48.26
STATES	18.HIMACHAL PRADESH	37,386	53,008	86,804	177,198	21.10	29.91	48.99
	19.JAMMU AND KASHMIR	28,927	82,146	242,447	353,520	8.18	23.24	68.58
	20.MANIPUR	3,240	22,951	49,750	75,941	4.27	30.22	65.51
	21.MEGHALAYA	7,652	21,754	44,918	74,324	10.30	29.27	60.44
	22.MIZORAM	633	18,178	43,952	62,763	1.01	28.96	70.03
	23.NAGALAND	3,135	27,475	52,684	83,294	3.76	32.99	63.25
	24.SIKKIM	2,211	7,357	26,955	36,523	6.05	20.14	73.80
	25.TRIPURA	5,962	31,878	62,673	100,513	5.93	31.72	62.35
	TOTAL(4)	**173,910**	**400,208**	**856,105**	**1,430,223**	**12.16**	**27.98**	**59.86**
	TOTAL(ALL STATES)	**6,984,718**	**3,462,603**	**2,622,003**	**13,069,324**	**53.44**	**26.49**	**20.06**

Notes: SOTR = State Own Tax Revenue
RE = Revised Estimates

Table 4: Effects of Devolution of UED on the basis of Collection (1997-98)

(Rs crore)

	States	Estimated UED Collected	UED Received*	Difference Between Cols. 2&3
	1	2	3	4
A. HIGH	1.GOA	348.6	69.9	278.7
INCOME	2.GUJARAT	7145.4	711.5	6433.9
STATES	3.HARYANA	1576.3	217.7	1358.6
	4.MAHARASHTRA	12049.3	1077.2	10972.1
	5.PUNJAB	2078.8	256.9	1821.9
	TOTAL (1)	**23198.4**	**2333.2**	**20865.2**
B. MIDDLE	6.ANDHRA PRADESH	3455.0	1488.5	1966.5
INCOME	7.KARNATAKA	3456.7	938.8	2517.9
STATES	8.KERALA	1273.4	681.4	592.0
	9.TAMIL NADU	3707.2	1167.1	2540.1
	10.WEST BENGAL	2441.6	1313.7	1127.9
	TOTAL (2)	**14333.9**	**5589.5**	**8744.4**
C. LOW	11.BIHAR	2409.6	2261.5	148.1
INCOME	12.MADHYA PRADESH	2694.9	1457.7	1237.2
STATES	13.ORISSA	732.3	953.1	-220.8
	14.RAJASTHAN	1179.6	976.1	203.5
	15.UTTAR PRADESH	3896.0	3131.9	764.1
	TOTAL (3)	**10912.4**	**8780.3**	**2132.1**
	TOTAL (15 MAJOR STATES)	48444.7	16703.0	31741.7
D. SPECIAL	16.ARUNACHAL PRADESH	-	223.5	-223.5
CATEGORY	17.ASSAM	709.0	880.2	-171.2
STATES	18.HIMACHAL PRADESH	191.1	587.3	-396.2
	19.JAMMU AND KASHMIR	70.7	917.8	-847.1
	20.MANIPUR	3.0	267.3	-264.3
	21.MEGHALAYA	14.9	241.5	-226.6
	22.MIZORAM	-	233.2	-233.2
	23.NAGALAND	18.5	369.7	-351.2
	24.SIKKIM	-	86.1	-86.1
	25.TRIPURA	18.7	371.9	-353.2
	TOTAL (4)	**1025.9**	**4178.5**	**-3152.6**
	TOTAL (ALL STATES)	**49470.6**	**20881.5**	**28589.1**

Notes: UED = Union Excise Duty

* This refers to collection of UED under State-VAT.

Table 5: State Revenue as perceived under State-VAT (1996-97 RE)

(Rs lakh)

	States	SOTR	Shared Taxes	Grants in Aid	Total Cols. 2+3+4	Percent Share to Total Revenue		
						SOTR	Shared Taxes	Grants in Aid
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
A. HIGH	1.GOA	30,052	9,016	6,615	45,683	65.78	19.74	14.48
INCOME	2.GUJARAT	631,304	132,334	73.017	836,655	75.46	15.82	8.73
STATES	3.HARYANA	216,917	42,024	48,658	307,599	70.52	13.66	15.82
	4.MAHARASHTRA	1,201,300	213,272	176,314	1,590,886	75.51	13.41	11.08
	5.PUNJAB	280,994	52,520	59,384	392,898	71.52	13.37	15.11
	TOTAL(1)	**2,360,567**	**449,166**	**363,988**	**3,173,721**	**74.38**	**14.15**	**11.47**
B. MIDDLE	6.ANDHRA PRADESH	500,675	286,536	174,260	961,471	52.07	29.80	18.12
INCOME	7.KARNATAKA	605,592	171,830	121,159	898,581	67.39	19.12	13.48
STATES	8.KERALA	395,720	120,935	74,693	591,348	66.92	20.45	12.63
	9.TAMIL NADU	779,010	210,799	97,014	1,086,823	71.68	19.40	8.93
	10.WEST BENGAL	462,535	240,405	122,848	825,788	56.01	29.11	14.88
	TOTAL(2)	**2,743,532**	**1,030,505**	**589,974**	**4,364,011**	**62.87**	**23.61**	**13.52**
C. LOW	11.BIHAR	239,315	391,640	86,779	717,734	33.34	54.57	12.09
INCOME	12.MADHYA PRADESH	401,922	256,504	189,799	848,225	47.38	30.24	22.38
STATES	13.ORISSA	144,274	156,316	114,409	414,999	34.76	37.67	27.57
	14.RAJASTHAN	329,625	175,387	139,409	644,421	51.15	27.22	21.63
	15.UTTAR PRADESH	611,802	582,648	281,540	1,475,990	41.45	39.48	19.07
	TOTAL(3)	**1,726,938**	**1,562,495**	**811,936**	**4,101,369**	**42.11**	**38.10**	**19.80**
	TOTAL (15 MAJOR STATES)	**6,831,037**	**3,042,166**	**1,765,898**	**11,639,101**	**58.69**	**26.14**	**15.17**
D. SPECIAL	16.ARUNACHAL PRADESH	991	17,868	58,067	76,926	1.29	23.23	75.48
CATEGORY	17.ASSAM	84,410	116,956	187,855	389,221	21.69	30.05	48.26
STATES	18.HIMACHAL PRADESH	37,538	52,856	86,804	177,198	21.18	29.83	48.99
	19.JAMMU AND KASHMIR	29,163	81,910	242,447	353,520	8.25	23.17	68.58
	20.MANIPUR	3,301	22,890	49,750	75,941	4.35	30.14	65.51
	21.MEGHALAYA	7,713	21,693	44,918	74,324	10.38	29.19	60.44
	22.MIZORAM	665	18,146	43,952	62,763	1.06	28.91	70.03
	23.NAGALAND	3,174	27,436	52,684	83,294	3.81	32.94	63.25
	24.SIKKIM	2,238	7,330	26,955	36,523	6.13	20.07	73.80
	25.TRIPURA	6,043	31,797	62,673	100,513	6.01	31.63	62.35
	TOTAL(4)	**175,236**	**398,882**	**856,105**	**1,430,223**	**12.25**	**27.89**	**59.86**
	TOTAL(ALL STATES)	**7,006,273**	**3.441,048**	**2,622,003**	**13,069,324**	**53.61**	**26.33**	**20.06**

Notes: SOTR = State Own Tax Revenue – Central Sales Tax + Union Excise Duty. RE = Revised Estimates

Table 6: Net Result of Adjustments in UEDs and CST

(Rs. Crore)

	States	Net Results of UED (1997-98 Actuals)	CST(@ 3%) (1996-97 RE)	CST(@ 2%) (1996-97 RE)	CST(@ 1%) (1996-97 RE)	Net Results		
						CST (@ 3%)	CST (@ 2%)	CST (@ 1%)
A. HIGH	1.GOA	278.7	14.0	9.3	4.7	274.0	269.4	264.7
INCOME	2.GUJARAT	6433.9	497.0	331.3	165.7	6268.2	6102.6	5936.9
STATES	3.HARYANA	1358.6	352.5	235.0	117.5	1241.1	1123.6	1006.1
	4.MAHARASHTRA	10972.1	948.0	632.0	316.0	10656.1	10340.1	10024.1
	5.PUNJAB	1821.9	197.6	131.7	65.9	1756.0	1690.2	1624.3
	TOTAL (1)	20865.2	2009.1	1339.4	669.7	20195.5	19525.8	18856.1
B. MIDDLE	6.ANDHRA PRADESH	1966.5	515.0	343.3	171.7	1794.8	1623.2	1451.5
INCOME	7.KARNATAKA	2517.9	425.6	283.7	141.9	2376.0	2234.2	2092.3
STATES	8.KERALA	592.0	195.0	130.0	65.0	527.0	462.0	397.0
	9.TAMIL NADU	2540.1	567.8	378.5	189.3	2350.8	2161.6	1972.3
	10.WEST BENGAL	1127.9	524.6	349.7	174.9	953.0	778.2	603.3
	TOTAL (2)	8744.4	2228.0	1485.3	742.7	8001.7	7259.1	6516.4
C. LOW	11.BIHAR	148.1	276.2	184.1	92.1	56.0	-36.0	-128.1
INCOME	12.MADHYA PRADESH	1237.2	294.8	196.5	98.3	1138.9	1040.7	942.4
STATES	13.ORISSA	-220.8	168.2	112.1	56.1	-276.9	-332.9	-389.0
	14.RAJASTHAN	203.5	74.6	49.7	24.9	178.6	153.8	128.9
	15.UTTAR PRADESH	764.1	131.3	87.5	43.8	720.3	676.6	632.8
	TOTAL (3)	2132.1	945.1	630.1	315.0	1817.1	1502.0	1187.0
	TOTAL (15 MAJOR STATES)	31741.7	5182.2	3454.8	1727.4	30014.3	28286.9	26559.5
D. SPECIAL	16.ARUNACHAL PRADESH	-223.5	-	-	-	-223.5	-223.5	-223.5
CATEGORY	17.ASSAM	-171.2	75.0	50.0	25.0	-196.2	-221.2	-246.2
STATES	18.HIMACHAL PRADESH	-396.2	14.6	9.7	4.9	-401.1	-405.9	-410.8
	19.JAMMU AND KASHMIR	-847.1	-	-	-	-847.1	-847.1	-847.1
	20.MANIPUR	-264.3	-	-	-	-264.3	-264.3	-264.3
	21.MEGHALAYA	-226.6	12.3	8.2	4.1	-230.7	-234.8	-238.9
	22.MIZORAM	-233.2	-	-	-	-233.2	-233.2	-233.2
	23.NAGALAND	-351.2	-	-	-	-351.2	-351.2	-351.2
	24.SIKKIM	-86.1	-	-	-	-86.1	-86.1	-86.1
	25.TRIPURA	-353.2	-	-	-	-353.2	-353.2	-353.2
	TOTAL (4)	-3152.6	101.9	67.9	34.0	-3186.6	-3220.5	-3254.5
	TOTAL (ALL STATES)	28589.1	5284.1	3522.7	1761.4	26827.7	25066.4	23305.0

Notes: UEDs = Union Excise Duties
CST = Central Sales Tax
RE = Revised Estimates

Floor Rates of Sales Tax

Zero Floor Rate or Exempted Goods:

1. Unprocessed cereals, including rice and wheat
2. Pulses
3. Fresh vegetables & fruits
4. Fresh meat, fish and livestock
5. Salt (processed and unprocessed)
6. Fresh milk and pasteurised milk
7. Eggs
8. Plain water
9. Books, periodicals and journals
10. Bread (branded and unbranded)
11. Fresh flowers
12. Gur and jaggery
13. Handlooms
14. Betel leaves
15. Khandasari
16. Condoms and contraceptives
17. Curd, *Lussi* and butter milk
18. Seeds
19. Organic manure
20. Electrical energy
21. Glass bangles
22. Kumkum
23. Wheel chairs and crutches used by handicapped persons
24. Artificial limbs
25. Rice flour, *Atta, Maida and Suji*
26. Charcoal
27. Poultry feed, cattle feed and aquatic feed
28. Garlic and ginger
29. Renewable energy devices and spare parts
30. Handmade safety matches
31. Firewood
32. Agricultural implements
33. Hand pump and spare parts
34. Aluminium utensils
35. *Agarbatti*
36. Educational writing instruments
37. Raw silk
38. Life saving drugs
39. Rubber/plastic footwear with MRP of Rs.200 or less
40. Turmeric

41. Tamarind
42. Chillies
43. PDS kerosene
44. Indigenous handmade musical instruments
45. Raw wool
46. Silk Fabrics

Goods with 4% Floor Rate:

1. Declared goods
2. Edible oils and oil cake
3. Vegetables, fish and meat sold in sealed containers
4. Bulk drugs
5. Cumin seed
6. Kerosene (excluding PDS kerosene)
7. Dry fruits
8. Bicycles
9. Vanaspati
10. Readymade garments
10. Utensils and kitchenware (excluding aluminium utensils)
11. Bone meal
12. Industrial inputs
    a) Non ferrous metal viz. sulphur, zinc and aluminium
    b) Belting
    c) Bearing
    d) All types of chemicals and intermediate chemicals including barytes, hydrogen peroxide, silicon carbide, lime, caustic soda and ferro silicon
    e) Dyes
    f) Ferro-alloy and super-alloy
    g) Transformer
    h) Polystyrene
14. IT products are as follows:
    84.69 Word Processing Machines and Electronic Typewriters
    84.70 Electronic Calculators
    84.71 Computer Systems and Peripherals, Electronic Diaries
    84.73 Parts and Accessories of HSN 84.69, 84.70 and 84.71 for items listed above.
    85.01 DC Micromotors/Stepper motors of an output not exceeding 37.5 Watts
    85.03 Parts of HSN 85.01 for items listed above.
    85.04 Uninterrupted Power Supplies (UPS) and their parts
    85.05 Permanent magnets and articles intended to become permanent magnets (Ferrites)
    85.17 Electrical Apparatus for line telephony or line telegraphy, including line telephone sets with cordless handsets and telecommunication apparatus for carries-current line systems or for digital line systems; videophones.
    85.18 Microphones, Multimedia Speakers, Headphones, Earphones and Combines Microphone/Speaker Sets and their parts
    85.20 Telephone answering machines
    85.22 Parts of Telephone answering machines

85.23 Prepared unrecorded media for sound recording or similar recording of other phenomena
85.24 IT software on any media
85.25 Transmission apparatus other than apparatus for radio broadcasting or TV broadcasting, transmission apparatus incorporating reception apparatus, digital still image video cameras.
85.27 Radio communication receivers, Radio pagers
85.29 (i) Aerials, antennas and their parts
(ii) Parts of items at 85.25 and 85.27 listed above
85.31 LCD Panels, LED Panels and parts thereof
85.32 Electrical capacitors, fixed, variable or adjustable (Pre-set) and parts thereof
85.33 Electrical resistors (including rheostats and potentiometers), other than heating resistors
85.34 Printed circuits
85.36 Switches, Connectors and Relays for upto 5 Amps at voltage not exceeding 250 Volts, Electronic fuses
85.40 Data/Graphic Display tubes, other than TV Picture tubes and parts thereof
85.41 Diodes, transistors and similar semi-conductor devices; Photosensitive semi-conductor devices, including photovoltaic cells whether or not assembled I modules or made up into panels; Light emitting diodes; Mounted piezo-electric crystals.
85.42 Electronic Integrated Circuits and Micro-assemblies
85.43 Signal generators and parts thereof
85.44 Optical fibre cables
90.01 Optical fibre and optical fibre bundles and cables
90.13 Liquid Crystal Devices, Flat Panel display devices and parts thereof
90.30 Cathode ray oscilloscopes, Spectrum Analysers, Cross-talk meters, Gain measuring instruments, Distortion factor meters, Psophometers, Network & Logic analyser and Signal analyser.

15. Tractors, harvesters and attachments
16. *Kirana* items
17. Chemical fertilisers, pesticides, weedicides and insecticides
18. Ores and minerals
19. Ice
20. All types of yarn
21. Sewing thread
22. Beedi leaves
23. Packing materials, including gunny bags, HDPE bags, corrugated boxes and containers
24. Hosiery goods
25. Gingili oil
26. Bran oil
27. Sponge iron
28. De-oiled cake
29. Vegetable oil
30. Solvent oils other than organic solvent oil
31. G.I. pipes
32. Starch

33. Maize products
34. Safety matches (excluding handmade matches)
35. Ship (including ship building)
36. Water pump and oil engines
37. All kinds of bricks including refractory bricks and asphaltic roofing
38. PVC pipes
39. Stainless steel
40. Calculators
41. Typewriters

Goods with 8% Floor Rate:

1. R.C.C. sleepers
2. Cooked food
3. Filters
4. Tiles
5. Electronic goods except those specified in category II and IV
6. Ceramics
7. Suitcases
8. Surgicals
9. All electrical goods including fans and air circulators but excluding transformers
10. Diesel locomotive
11. Photographic goods
12. Paper
13. Napa slabs
14. Tyres and tubes
15. Printing ink
16. Electrodes
17. Sanitaryware
18. Milk food and milk products
19. Sewing machines
20. Foam
21. Butter and ghee
22. Arecanut powder
23. Flasks
24. Earth moving machinery
25. Pulp
26. Explosives
27. Blades and razors
28. Timber
29. Drugs and medicines (excluding life saving and bulk drugs)
30. Footwear (excluding those exempted)
31. Magnets
32. Electric motors
33. Nutrition food
34. Hose pipes
35. Cooking gas (LPG)
36. Machinery of all kinds except earth moving machinery and agricultural implements

37. Tea and coffee
38. Toffees, chocolates, biscuits and confectionery
39. Cakes, pastries etc.
40. Tooth pastes
41. Building materials such as wood, bamboo and plywood including cement
42. Electric bulbs and tube lights
43. Paints and colours
44. All types of furniture
45. Batteries and parts thereof
46. All types of cables and electrical wires
47. Plastic and PVC items excluding PVC pipes given in category II
48. Electronic musical instruments (excluding indigenous handmade musical instruments)
49. Auto parts
50. Items not specified elsewhere

Goods with 12% Floor Rate:

1. Weather proofing compounds
2. Fire works
3. Furs and skins with fur
4. Lifts and elevators
5. Diesel oil
6. Marble and marble tiles
6. Sandalwood and oil
8. Cutlery
9. Preserved food articles
10. Vacuum cleaner
11. TVs and VCRs
12. Transmission towers
13. Voltage stabilizers
13. Washing machines
15. Air conditioners
16. Arms and ammunition
17. Articles of stainless steel
18. Carpets
19. Cushions and mattresses
20. Electronic toys
21. Fancy leather goods
22. Aerated drinks
23. Hair oils
24. Cigarette cases and lighters
25. Cinematographic equipment
26. Glassware, other than bangles
27. Naphtha
28. Rubber goods
29. Cosmetics and soaps
30. Adhesives

31. Motor vehicles, except tractors
32. Laminated sheets
33. Oxygen and gas
34. Aeronautics
35. Watches and clocks
36. ACSR conductors
37. Refrigerators

Goods with Floor Rate of 20%:

i. Motor spirit including aviation turbine fuel
ii. Liquor
iii. Narcotics
iv. Molasses
v. Rectified spirit

Goods with Floor Rate of 1%:

i. Bullion
ii. Gold articles
iii. Precious stones including synthetic gems
iv. Silver articles

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