

LEGAL, ADMINISTRATIVE AND INSTITUTIONAL REQUIREMENTS

Introduction of value added tax poses many challenges for policy-makers, tax administrators and the people. It involves, first, an appreciation of the need for basic reform of the existing tax system on the part of all the players and also the people at large, consensus on the approach to basic issues, and a readiness to adapt the system to new concepts and mode of operation. These reforms also have a profound impact on the economy and the society. Hence, implementation of VAT has been described as one of the most significant development projects undertaken by a country. Success in this as in any other major endeavour requires careful planning and management, while mismanagement can jeopardise the entire reforms programme.

Although the principles of VAT are operating in India through the excise system at the Centre and also have made their inroad into the sales tax system in some States (e.g., in Andhra Pradesh, Kerala and Tamil Nadu) VAT is a relatively new concept for most taxpayers and tax administrators in the country. Its extension at the Centre and, more so, introduction at the State level to replace the sales taxes will call for an overhaul of the legal and administrative systems governing the levy of trade taxes in the country. In many ways administrative reforms are a precondition for the full benefits of the new tax structure to be realised. Without them, the tax structure changes may amount to nothing more than a replacement of one set of books by another on the legislative shelves. Appropriate institutional infrastructure will also have to be evolved for launching and operating a harmonised, destination-based system of VAT at the State level independently of the Centre.

More thoroughgoing reform of administrative organisation and methods than has taken place so far would be needed for operating a fullblooded manufacturers' VAT at Centre too even though the MODVAT has been in operation in the Union excise system for some time. Problems of administration of

indirect taxes with reference to customs and Central excises have been examined at considerable length by the TRC and many valuable recommendations are contained in that Committee's Final Report (Part I, vide Chapter 7). The discussion of issues relating to legal, administrative and institutional requirements for the introduction of VAT in this chapter is focused on what would be needed at the State level.

9.1 Main Tasks

The tasks on the legal, administrative and institutional side for the introduction of State VATs may be considered under the following components:

1. Drafting of the law and regulations
2. Formulation of procedures and design of forms
3. Reform of administrative systems and organisation
4. Computerization and modernization of administrative methods
5. Training and reorientation of staff
6. Taxpayer education
7. Creation of institutional infrastructure.

Formulation of concrete proposals under each component would require much more detailed examination than was possible to undertake for this study. However, a few general observations on the possible approach and the essential requirements might be in order.

9.1.1 Legislation

Once a decision has been taken in principle to introduce VAT and broad agreement reached about its basic design features, steps would be needed to prepare the necessary legislation along with supporting regulations. As noted in Chapter 2, the sales tax systems of the States have evolved independently, each with its own laws. In many States the laws are dispersed over more than one legislation. These would have to be scrapped and a consolidated law governing the levy of a VAT would have to be

formulated to authorise the levy and provide the necessary legal framework for its enforcement.

Considering that uniformity of basic structure and procedures would be necessary for the harmonization and smooth operation of the system all over the country, a model law should be devised which the States can adopt with suitable changes but retaining the basic structure. The idea of a model sales tax law was mooted some time back and the NIPFP was asked to prepare a draft of a model law for sales taxation. Such a model was prepared and circulated but is still in the discussion stage. A VAT would have design features which would be quite different from those of a sales tax, although there are several common elements. A different model law would therefore be needed for a VAT, although the work done already could perhaps be drawn upon.

Drafting, being a specialised job, has to be undertaken by a team of experts. All major States in India have their law departments and also cells for drafting laws relating to sales tax, manned by experienced legal hands. Few of them would, however, have much familiarity with what legislation for VAT would involve. The States should jointly set up a team consisting of experts drawn from the law departments and legal cell of sales tax departments and officers with background of sales tax administration to undertake the task of drafting the law. Since VAT would be an unfamiliar concept and its rationale may not be apparent to legal experts, it would be necessary to include a fiscal economist in the team. As VAT has been operating in many countries now and there are experts who were associated with preparation of their laws, it may be useful to take the help of consultants from abroad to work with the team to be set up for the purpose. The tasks of the team should include, besides drafting the basic law, formulating regulations and resolving operational issues.

Parallel to the team envisaged above, each State would have to set up a standing legal cell of their own to adapt the model law to local conditions and needs, see the legislation through the State Assemblies,

answer queries on legal issues, process amendments whenever needed and get the regulations ratified.

The scheme of State VATs proposed in this study will call for some far reaching amendments in the Central Sales Tax Act of 1956 (e.g., to bring down the rate of CST to nil when the sale is between registered dealers, remove the ceiling on State sales taxes on declared goods and so on). The Sales Tax Cell in the Revenue Department of the Ministry of Finance may undertake the task of identifying the amendments required and draft them for consideration of Parliament in consultation with the Ministry of Law. The present cell may need to be strengthened with officers conversant with the State sales tax systems to undertake the job.

9.1.2 Procedures and forms

Implementation of any tax calls for prescribing operational procedures for

- . Registration of taxpayers
- . Filing of returns
- . Payment of tax
- . Assessment and reassessment
- . Appeals against assessment.

9.1.2.1 Registration

Under VAT, as in sales taxes, every trader having turnover exceeding a specified limit must be required to register with the tax authorities and obtain a registration number for his/her identification which can be quoted in all tax related documents. Ideally, a unique taxpayer identification number should be allotted to each trader which can be used for other taxes too like the Central VAT and income tax. Creation and maintenance of a central register of taxpayers, however, do not seem to be feasible in the present state of our information system and in the absence of effective coordination between Central and State tax departments. Hence, the task of registering VAT taxpayers and allotting their tax identification numbers (TIN) has to rest with the tax authorities of the States.

Under a system of destination-based VAT, inter-State movement of goods would

need to be monitored and transactions between registered dealers across States cross-checked from time to time, even though on a sample basis. Hence, it would be necessary to evolve an all-India coding system. As in the case of registration of motor vehicles, a particular series of registration numbers may be allotted to each State to which additions may be made to identify the district and the administrative division, tax ward/circle and number allotted to the taxpayer registered. The registration number may thus contain boxes to indicate the location of the taxpayer by State, district and identification number as shown below:

\$	#	@	*
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The first box (\$) would refer to the State, the second (#) to the district or administrative division, etc., the third (@) the ward or circle, and the fourth (*) would indicate the individual registration number of the dealer. Allotment of identification numbers to registered dealers in this way would help maintain a master file for all taxpayers in the State. The master file should be maintained on the computer accessible at the head office as well as in the administrative unit.

Information regarding dealers when they are registered and any changes therein should be regularly communicated to the computer centre at the head office as also the concerned administrative unit. The master file would serve to store information regarding every dealer (or at least large dealers) relating to filing of return, payment of taxes, etc. With a view to facilitating compliance under the new system of taxation, publicity should be given through the mass media and through free taxpayer education booklets about the obligations of various players in the system. Publicity material should include information on who should register for payment of tax, where and how to register, where to get the forms and so on.

The procedure for registration and allotment of identification number should be streamlined so that there is little scope for harassment. Since registration would confer certain benefits (such as claim for tax credit

for inputs) even while entailing liability to file returns and pay the tax, it would be necessary to make sure that registration is granted only to genuine traders. At the same time, there should be no harassment to applicants. Some simple checks (such as municipal bill, bank account number, telephone number, power connection number, etc.) should be adequate to make sure that the applicant is not a fictitious entity and can be located when required.

At present, registration procedure involves submission of an application by the dealer, along with deposit of a prescribed sum and/or some security. This is followed by departmental verification of the bonafide of the applicant. Verification, however, is not always carried out with the care needed. On the other hand, often there are complaints of harassment by the inquiring staff. This enables fictitious (Hawala) or bogus dealers to thrive. Also, at present, no educative pamphlets are supplied to dealers automatically at the time of registration.

VAT registration should follow a new procedure. The dealer should be required to submit an application in the prescribed form of which a specimen is given at Annex 1. On due verification and processing of the application, each registered dealer should be given a "registration kit" containing VAT Act and Rules along with copies of all the requisite forms and returns. It should also contain a guide to VAT-management explaining the Do's and Don'ts for dealers.

9.1.2.2 Tax Return and other forms

Registration implies responsibility on the part of the trader to file returns and pay tax as required under the law.

Unlike under a sales tax with multiple levies and rates of tax, the VAT return form can be very simple, especially if the rate of tax is uniform. For with a uniform rate (and no exempt item) all that a trader is required to report is his total sales during a given tax period, his purchases and the tax paid. The tax payable can be computed simply on the return itself by multiplying the sales with the prescribed rate of tax and deducting the

Specimen Form of Application for Registration as a VAT Dealer

TIN (Taxpayer Identification Number)	01
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Affix a photograph of the signatory

SINGLE PROPRIETORSHIPS/FIRM/COMPANY/COOPERATIVE ETC.
PERSON TO BE REGISTERED

FAMILY NAME (for individual)	FIRST NAME	MIDDLE NAME
02 _____	03 _____	04 _____
05 Age: _____	06 Sex: _____	

NAME OF FIRM, COMPANY, COOPERATIVE, PUBLIC ENTERPRISE, SOCIETY ETC.
07 _____

ADDRESS	NO./STREET	CITY/MUNICIPALITY	PIN CODE
08 _____	_____	_____	_____

PARTNERS IN FIRM, CHIEF EXECUTIVE IN COMPANY, COOPERATIVE ETC.
09 _____

10 TELEPHONE	11 FAX
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ADDRESSES OF ALL BRANCH OFFICES
12 _____
13 _____

ECONOMIC ACTIVITY CODE	ECONOMIC ACTIVITY DESCRIPTION
14 _____	15 _____

SALES OF GOODS AND SERVICES

Last Quarter	16	_____
Last Year	17	_____
Expected for the next 12 months	18	_____

Date of first sale	19	D	M	Y
_____	_____	_____	_____	_____

I _____ (proprietor/director/secretary or other authorised person) hereby declare that the particulars given herein are correct and I hereby apply for registration for value-added tax.

Signature of Taxpayer or Authorised Officer

Introduced by: _____

(Bank official/Attorney/
Responsible person)

For official use only

Tax Office	20								
Date of registration	<table border="1" style="display: inline-table; border-collapse: collapse;"> <tr> <td style="width: 5%;">_____</td> <td style="width: 5%;">D</td> <td style="width: 5%;">M</td> <td style="width: 5%;">Y</td> </tr> <tr> <td>21</td> <td>_____</td> <td>_____</td> <td>_____</td> </tr> </table>	_____	D	M	Y	21	_____	_____	_____
_____	D	M	Y						
21	_____	_____	_____						
Registration refused (for reasons recorded on file)	22								
Received by:	_____								

Adapted from Casanegra de and Silvani (1991).

amount of tax paid on purchases. This is why in some countries where the VAT is in operation the return form is prescribed on a postcard (e.g., in Denmark). With more than one rate, space has to be provided in the return form for reporting sales and purchases under the different rate bands. Even so, the form should be simpler than those in vogue for sales taxes at present, if only the rate bands do not exceed two or three. A specimen VAT form is at Annex 2. This form as also the returns to be filed can be in the computerised format.

The periodicity of return filing and payment of tax would have to be determined in the light of the experience and requirement of each State. Some uniformity in this regard among all States is highly desirable.

9.1.2.3 Invoices and Accounts

Requirement of documents and forms to support a tax return should be kept to a minimum. The most important document for the operation of tax credit-based VAT is the invoice. Tax invoices are required to establish both the tax liability of the seller and the tax credit that can be claimed by the purchaser. Two types of invoices are used under VAT: (1) invoices to register sales and purchases among registered dealers and (2) invoices for final consumers or unregistered dealers.

Only VAT registered dealers should be legally authorised to issue a tax invoice. Such invoices should provide information regarding the particulars (i.e., name, address and TIN) of the seller, date of issue, serial number, particulars of goods sold (quantity, description and unit price), price excluding VAT, amount of VAT charged, and name, address and VAT registration number of the purchaser. The invoice should be prepared in three copies (in different colours): the original, for the buyer for his accounting records, first copy also for the buyer to be provided to the tax authorities, if required, to establish his claim for credit, and the second copy for the seller. A specimen of a VAT invoice is at Annex 3.

Final sale invoices would only serve to

register sales to a unregistered purchaser or final consumer for purposes of VAT. This invoice may show only the price including VAT. No extra copy of the invoice apart from one for the seller's accounts would be needed. Use of cash registers in place of invoices may also be permissible provided it records the description of the goods sold and VAT charged, with daily totaling and transfer to a permanent record.

A thorough review of forms in force in sales tax should be undertaken and only those which are absolutely necessary retained, with suitable modifications. All forms should, however, be standardised to facilitate transfer of information without delay.

Dealers registered for VAT (other than those coming within the "small dealers" category) must maintain record of all tax invoices issued and received by them indicating their serial number, date, price charged and the VAT. The records should help to check the accuracy of the return by the tax authorities. The books of accounts usually maintained for running businesses may have to be adapted for the purpose. The manner in which such adaptation may be carried out with the least disruption of the existing practices may be worked out in consultation with the accounting and traders' bodies. Since it may not be possible for tax administration to verify or check the authenticity of all tax credit claims, reliance would necessarily have to be placed on accredited accountants. That would cast a special responsibility on the accounting profession. Tax authorities should, however, have the powers to check any claim that they may feel necessary.

9.1.2.4 Filing of Returns and Tax Payment

Assessees often undergo hassles in filing return and paying their due taxes because of shortage of necessary forms, limited number of tax payment receiving counters, etc. It would simplify life if banks were authorised to receive returns along with taxes with the responsibility to pass on the returns to the tax authorities. Such a system is in vogue in many other countries. A similar system has been introduced in Maharashtra and could be

State of.....

VAT RETURN

[01] For the Month of..... [02] Registration No..... [03] Telephone No..... [04] Fax No..... [05] Economic activity code (Manufacturing/Whole- saling/Retailing)..... [06] Name and address of registered person:	For Office Use	
	S.no	Date Stamp
	Tax due and payable Rs.....	
	Penalty/Fine Rs.....	
	Tax Paid Rs.....	
	Receipt No.....	
Date.....Initial.....		

Purchases	Value (excluding VAT) (Rs)	Tax credit (Rs)
[07] Exempt or non-creditable purchases ¹NIL.....
Purchases from domestic suppliers:²		
[08] at low rate
[09] at standard rate
[10] at high rate (where creditable)
[11] Total [07] to [10]

Sales	Value (excluding VAT) (Rs)	Tax due (Rs)
[12] Exempt salesNIL.....
[13] Inter-State sales/consignment transfers supported by advance tax payment by dealers in importing StateNIL.....
[14] International exportsNIL.....
Sales taxable at		
[15] low rate
[16] standard rate
[17] high rate
[18] Total [12] to [17]

1. Non-creditable purchases include those for which no rebate is available under the law.
 2. Including suppliers in other States for which advance tax is paid.

Contd.

VAT Account	Tax due and payable (Rs)
[19] Tax due on account of sales in the current month (18)
[20] Add: Tax/penalty due from the previous month
[21] Less: Tax Credit for purchases in the current month (11)
[22] Less: Tax Credit carried forward from previous month
[23] Tax payable to the government (+)/ tax credit carried forward (-)
Declaration	
I (full name of signatory in BLOCK LETTERS) *MR/MRS/MISS.....	
.....	
.....	
(a) declare that the information and particulars given in this return in respect of the taxable period shown herein are true and complete and include details for all places where business has been carried on by the registered person named in Part I above, and	
(b)* tender the sum of Rs..... representing the tax due and payable shown at item No. 23 above.	
(c)* request that the excess amount of tax credit shown at item No. 23 above be carried forward to the next return.	
[24] Date.....	Signature.....
Capacity in which acting.....	
*Delete whichever is not applicable.	
For Official Use	
Assessment Order	
[25] Tax due:	
[26] Tax underpaid:	
[27] Penalty/Fine:	
[28] Total due:	
[29] Notified by letter dated:	
(Signature of Assessing Officer)	

Specimen of a VAT Invoice

INVOICE

ORIGINAL: To be submitted with the return to claim tax credit by the buyer.

Seller's Name _____	
Address _____	

Telephone No. _____	Fax No. _____
Taxpayer Identification No. _____	

Date _____
Serial No. _____

Buyer's Name _____
Address _____

Taxpayer Identification No. _____

Terms of Sale

Quantity	Description of goods or services	Unit Price	Value (Rs)	VAT Rate (%)	Amount of VAT (Rs)
	Total				

Signature of Seller

INVOICE

DUPLICATE: Record copy of the buyer. This copy does not entitle the holder to a tax credit.

Seller's Name _____	
Address _____	

Telephone No. _____	Fax No. _____
Taxpayer Identification No. _____	

Date _____
Serial No. _____

Buyer's Name _____	
Address _____	

Taxpayer Identification No. _____	

Terms of Sale

Quantity	Description of goods or services	Unit Price	Value (Rs)	VAT Rate (%)	Amount of VAT (Rs)
	Total				

Signature of Seller

emulated profitably by other States.

9.1.2.5 Assessment

Procedure for assessment should also be standardised.

Tax administration all over the world is now moving towards a system in which returns filed by the assesseees are accepted and thorough scrutiny or audit of only a few cases is taken up on a sample basis. The basis of selection and the proportion of cases to be taken up for audit have to be decided keeping in view the costs and the likely results. It would not be appropriate to indicate any norms *a priori* for this purpose. However, the following suggestions might be of some help.

Returns of large taxpayers that is those with turnover exceeding a certain limit (say Rs 20 lakh or carrying a tax limit exceeding, say Rs 10,000) should be processed with some care. For others, that is those with turnover or tax payable (or paid) below a certain limit - the small traders - the returns may be accepted with only a small sample of cases audited every year. The assessments of small traders may be completed under a simplified procedure with no requirement for the taxpayer to appear in person or produce accounts. A simple acknowledgement after routine checks should signify completion of assessment. It should, however, be open to tax authorities to reopen a case within a reasonable period of time if concealment of any material particular is detected or reported subsequently.

The verification of zero-rating ought to be undertaken promptly, and for this it is imperative to complete the checking of returns which might be taken up for audit, expeditiously, say, within a year.

9.1.2.6 Appeals

The structure of appellate authorities and procedure also should be standardised. With standardisation and harmonization of the system it would be helpful to set up appellate courts having regional jurisdictions, that is

covering three or four States. To ensure speedy settlement the appellate machinery should not consist of too many tiers.

9.1.3 Administrative System and Organisation

The current excise and sales tax systems rely more on physical controls and attention to legal detail than accounts-based control and attention to the maintenance of proper books of accounts and their verification. Success in the implementation of VAT hinges critically on financial or accounts-based controls supplemented by physical controls such as field visits by authorised officers. Hence, with the introduction of VAT, tax officers will have to orient their approaches towards examination of accounts instead of relying heavily on physical controls. This would call for reassessment of staff needs, staffing pattern, and retraining and redeployment of the existing staff. It would also require a reorganisation of the tax departments.

9.1.3.1 Staff requirement

Proposals for VAT in India may give rise to apprehensions on the administrative front on two contradictory counts. Many may tend to think that the number of taxpayers would multiply unmanageably when the single point sales taxes are converted into a multi-stage tax on value added while another view could be that with simplification of the laws and administration and more so, with modernisation, a large proportion of the staff in the sales tax departments of many States would be rendered redundant. There may be misgivings also about the promotional prospects of officers, as under the new system, there would be no rationale for having a multi-tier distribution of assessment work with senior officers being entrusted with cases of the higher categories. None of these apprehensions seem to be well-founded. Similar misgivings might arise among tax practitioners too. However, the opposition to reform has to be countered frontally, pointing to the gain that the reforms would confer on the community if litigation was reduced and the tax practice ceased to be as profitable as it seems to be now.

Apprehensions about staff redundancy fail to take into account the increase in the workload that may occur under VAT. At present under the sales taxes, there is a practice of carrying out assessment of all the dealers for every assessment year. But the actual assessment under sales taxes is attempted for dealers dealing in first sale of the goods (by manufacturer or wholesaler) in the State. The other dealers (who deal in tax-paid goods) are only assessed perfunctorily or not at all. Under the system of VAT all dealers will come within the tax-paying category requiring proper assessment of everyone. Thus the introduction of VAT which may necessitate carrying out checks or assessment upto the retail level or final point of sale, should cause an increase in the number of assessing officers as well as the other supporting staff. In general, it would be reasonable to suppose that there would be an overall increase rather than any reduction in staffing requirement.

Data on distribution of dealers according to turnover suggests that under VAT, by and large, full auditing may have to be done only for one-fifth of the dealers; a sample audit would be required for two-fifths; and a system of self-assessment could be adequate for the rest. If such a system is followed, staff requirement would go up even though marginally or at least not decline.

No doubt, in most countries of the world where VAT is in operation, the ratio of staff to taxpayer is quite low, as the following figures would show:

Table 9.1

Staff/Taxpayers Ratio for VAT

Country	Ratio
Belgium	1:123
France	1:173
Ireland	1:130
Italy	1:726
Korea	1:360
Netherlands	1:280
New Zealand	1:350
Portugal	1:215
Sweden	1:250
United Kingdom	1:149

In India, for Central excise the total strength is about 35,000 to handle about 150,000 taxable entities. Of these, about 7500 are on assessment work. The ratio thus works out 1:20 or so. However, the number of dealers per assessing officer is higher for sales taxes and several States compare favourably with other countries in this respect, as may be seen from Table 9.2. However, the ratio (number of dealers per tax staff) goes down sharply if the supporting staff in addition to assessors are also included. With the change in the system of assessment and audit and, what is more, with computerisation, the requirement of staff per taxpayer should decline or at least need not increase. However, as argued above, there should be no fear of any retrenchment with VAT. Only some reallocation of functions and redeployment with emphasis on examination of accounts might be needed.

Reform in any sphere calls for restructuring of administrative organisation. It should not be difficult for governments to work out schemes of organisation keeping in view the need to provide adequate promotional avenues. Given the uneven quality of tax administration among the States and the constraints likely to be faced in many States in switching over to an accounts based system of taxation such as VAT, consideration may be given to the creation of a unified independent Value Added Tax Administration or authority with All India and State Services eventually. This authority should take care of the needs of VAT administration of States and provide assistance by lending the services of officers belonging to the unified service. Besides strengthening the tax administration of the States that would also help to create new promotional avenues and challenges for the officers engaged in tax administration.

9.1.4 Computerisation and modernisation of administrative methods

Modernization of administration with extensive use of computers is a crucial element of reform. Computers provide an extremely powerful and at the same time affordable instrument for administration of taxes and are particularly useful in the

Table 9.2

**Ratio of Sales Tax Staff to the
Number of Registered Dealers**

State	Staff	Number of Regd. dealers under GST	Ratio
1	2	3	4
1. Kerala (1993-94)			
Total Staff	4231	104113	1:25
Support Staff	2925		
Officers	1306		1:80
2. Maharashtra (1990-91)			
Total Staff	8975	374830	1:42
Support Staff	5736		
Officers	3239		1:116
3. Punjab (1991-92)			
Total Staff	2722	130929	1:48
Support Staff	2097		
Officers	625		1:209
4. Rajasthan (1993)			
Total Staff	4314	161642	1:37
Support Staff	3453		
Officers	861		1:188
5. Tamil Nadu (1991-92)			
Total Staff	9907	303000	1:31
Support Staff	7596		
Officers	2311		1:131
6. Uttar Pradesh (1992)			
Total Staff	11649	319000	1:28
Support Staff	10136		
Officers	1513		1:211
7. West Bengal (1991-92)			
Total Staff	5514	114738	1:21
Support Staff	3698		
Officers	1816		1:63

operation of a tax like the VAT which calls for monitoring of tax payments and credits availed of continuously and also cross-verification of tax-credit claims even if selectively. EDP can help VAT enforcement in a variety of ways such as in creating VAT register, preparing tax return form and identification labels, validating batches of return received from say the depositors' banks, processing refund claims, maintaining a current ledger account of VAT assessees, selecting dealers for scrutiny, providing support for investigation and following up appeals.

The approach of tax administration towards enforcement also has to undergo a transformation and rely more on gathering information from various sources and processing them promptly minimising the need for any contact with taxpayers. Modern information technology with its capacity for storing data and networking across vast regions has revolutionised tax administration throughout the world with dramatic results. The system of zero-rating of sales between registered dealers among member countries of the EEC operates principally through a computerised information system. While that might be a goal a little too far for India, with the talent available in the country, States in India can make rapid strides towards modernisation of tax administration given the will and some support.

Several States in India have initiated programmes for introducing computer in their tax administration. However, progress has been halting and tardy. Use of computers for enforcement on a significant scale is yet to begin. It is absolutely necessary to draw up plans for computerising tax administration in all States in a time bound programme. The Central government and multilateral aid agencies could perhaps help in this task in a big way by providing the necessary funds to acquire the hardware and software and hiring experts from within or outside the country to set them up. Administration of Central excise department also needs to be modernized for the MODVAT to be expanded and operated efficiently. It is understood that the Department has already embarked on an ambitious programme of computerisation. The programme needs to be speeded up.

9.2 Training

An important pre-condition for the introduction of VAT is intensive training of the tax staff and a proper recruitment policy for the departmental personnel.

Officers of both the Union excise duties and of the sales tax departments are trained to administer, audit, and verify documents related to trade taxes, both single-point as well as multi-point. Their principal emphasis has, however, been physical checks and controls. Under a regime of VAT which is in fact a multi-point sales tax with set-off, the system of administration of the tax will undergo a radical change. Officers meant for auditing of VAT would, therefore, have to be trained afresh. All States would have to organise training programmes to induct them to their new tasks. It would also be necessary to update the skills of the personnel already trained periodically. The VAT Council proposed below may take the initiative to set up training institutions and secure the support they may require in terms of resources.

9.3 Institutional Set-up : Need for a VAT Council of States

Implementation of the reforms will require consultation and discussion among the State governments on a continuing basis. Involvement of the States would be needed for steering the implementation of VAT in the initial stages and also later for overseeing its operation. The process should be initiated as soon as the Central and the State governments agree on the whole package.

Article 307 of the Constitution envisages the creation of statutory authority by the Parliament for the purpose of ensuring free flow of trade, commerce and intercourse within the territory of India. The VAT Council of States can be one such body. To facilitate consultation and chalk out lines of action it would be advisable to set up an All-India VAT Council of the States. This Council will provide the mechanism for bringing all States together and ensuring their active participation. It will concentrate expertise, prepare the draft of a common tax base (like the Sixth Directive of the EEC) and common procedures, play a major role in

educating and guiding State VAT officials, provide for review and continuity of the VAT adoption process, integrate policy/analysis with legal drafting, etc. Consultation may take time but is essential if the States are not to drift apart further. The need for a statutory body for inter-State consultation was stressed by the Sarkaria Commission too. Introduction of State VATs would lend urgency to this need.

It would be helpful to set up the permanent statutory institution for consultation among States and overseeing the introduction and the operation of VAT in two tiers: one, the apex body (VAT Council) and another, a functional one below it.

The apex body should be constituted with finance ministers of all the States. Ministerial involvement would be needed to lend the necessary authority for implementing the decisions reached. The major policy issues will have to go to the apex body, that is, the VAT Council for resolution. The Council should be constituted at the earliest to initiate the process of planning for the VAT reform and draw up the agenda. Since the reforms are predicated on an agreement being reached on the basic approaches and adherence to the system of harmonisation, there has to be some mechanism enforceable sanctions against infringement by any State. The Council itself should evolve such sanctions and the mode of enforcement.

The mode of functioning of the Council, whether unanimity should be required for any decision to be effective or whether the convention followed in the National Development Council (NDC) should be adopted, needs further consideration. The NDC would perhaps be the best forum for taking a decision on and recommending to Parliament the creation of a VAT Council and the decision rules. It may only be added that the unanimity condition has been a stumbling block in the reform of the system in Brazil.

At the second tier which would function under the umbrella of the VAT Council, there should be a Standing Committee of officials (Commissioners of Commercial Taxes) who would meet regularly to identify issues and propose solutions. Needless to say, there

should be a secretariat to service these bodies.

Disputes between States or taxpayers located in different States may be referred to the Commissioners' Committee first. Inter-State disputes which remain unresolved may, however, have to go to the Supreme Court under our Constitution.

9.4 Taxpayer Education and Publicity

Apart from opposition born out of fears of the unknown, VAT arouses suspicions and misgivings among large sections, often based on misconception about its mode of operation and likely impact and ignorance about its merits. Dissemination of information regarding VAT and the case for reform is thus crucial for the success of any scheme for replacing the present system with a scheme of VAT. Before embarking on the reform, it is necessary to launch a programme of public discussion about the ills of the present system, how VAT could remedy them as well as its weaknesses and the benefits likely to be derived by the community from its introduction. Active participation of the key players, viz., traders and tax administrators in this programme would be necessary. Traders and trade/industry organisations should be consulted in resolving both structural as well as operational issues. That would help avoid pitfalls and needless complexities in law and procedures and advance the acceptability of the entire programme. Publication of pamphlets, open discussion in seminars and on the television and radio with leading intellectuals, politicians and administrators as well as representatives of trade and industry should be on the agenda for reform.

In Korea, before launching the reforms, the government vigorously campaigned for the case of VAT. It took the help of chambers of commerce and industry, daily newspapers, TV and radio and other mass media. A series of articles, question and answer sessions, feature stories and lectures for the need of adopting VAT were mounted. A movie was also made about the VAT and shown in all the theatres in the country. About 30 different kinds of pamphlets on VAT were printed and millions of copies distributed. In addition, three preliminary exercises on filing tax returns were conducted before the actual

implementation of the tax. In the latter two programmes most of the potential taxpayers participated. These exercises not only helped the taxpayers understand the new tax but also gave valuable feed back to the government for its improvement.

Along same lines, Taiwan also assiduously campaigned to educate the public on VAT. In addition to seminars, exercises in filing returns, and use of mass media, tax enforcers did a lot of field work by visiting firms and demonstrating the use of VAT forms and the computation of VAT.

9.5 Lead time

With a view to enabling the taxpayer, the public and tax departments to prepare themselves for VAT, adequate lead time would be required. Although no hard and fast rule can be laid down in this regard, preparing the legislation and rules, prescribing the systems of registration, prescription of requisite forms, modernisation of administration, reorganisation and training of staff would all require time.

Experience of several developing countries suggests that a lead time of two to three years is necessary to prepare for VAT. Chile was the only country to reduce the lead time to a few months because of its prior experience with a turnover tax. Also, a

sufficient lead time allows governments to anticipate transitory problems associated with reforms and to implement policies and measures to effect a smooth transition.

India has a fairly long experience of trade taxes. Even so, the tasks involved and the creation of necessary institutional infrastructure will take time to accomplish. However, as noted at the beginning, introduction of VAT without adequate preparation or institutional backing can be disastrous. A lead time of two to three years, therefore, is perhaps unavoidable in moving towards a system of VAT in the States.

9.6 Concluding observations

It needs to be stressed that reform of this magnitude cannot be carried through without strong political will and real interest on the part of the Central and State governments and support from the people. Further, because many parties would be involved, a package reform with inter-dependent gains and losses would be preferable to incremental change which is favoured by some on practical grounds. Incremental reform may soon get bogged down and lead to nowhere. Obviously the task will be arduous but, as stressed at the outset, needs to be addressed boldly if the Indian economy is to get free of the shackles of its present irrational and inimical tax system and move forward fast.