BANGLADESH CUSTOMS

# FISCAL FRONTIERS

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# *Fiscal Frontiers*

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## *Fiscal Frontiers*

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## *Contents*

## *Editor's Note*

It is about four years since the first collection of articles under the caption *Fiscal Frontiers* was published on the eve of the fortieth founding anniversary of the Customs Co-operation Council. The Council has since been renamed World Customs Organisation with a number of responsibilities and functions emanating from fresh international dialogues such as the Uruguay Round of talks. In the mean while, the global economic situation had also undergone some important alterations and so had the directions of international trade and finances. Simultaneously, there had been massive breakthrough in the field of the electronic data processing as well as gobal communications. On the national front, reform measures were claimed to have been pushed further forward. In such a context the second volume of *Fiscal frontiers* was brought out since when about two year have elapsed. It now seems appropriates to take a fresh took at the national taxation scene in the context of these changes that had taken place globally and locally. The focus in this publication is on indirect tax policy issues and its administration. If these few articles initiate the process of fresh thinking on these issues by those interested and involved in the theory and practice of Indirect Taxation, our efforts of bringing out the publication will have been richly rewarded.

Even though the original idea of bringing out the *Fiscal Frontiers* in shorter frequencies did not materialise due mainly to the limited spare time available to the organisers, it would appear that a longer frequency actually allowed time for the ideas to crystallise as well as the new developments to take place to which probing research could be directed. It is the hope of the Association and the Indirect Taxes Wing of the N.B.R. that the dialogue, if any, initiated by this modest publication would evente conclusion, but there are some physical manifestations of the effects in the real life situation. For example, we have been able to contribute 43% of our development expenditure from internal resources in FY 1994-95 due to the increase in the revenue with proportionate depletion of foreign aid on which we have been endemically dependent for the last three decades. On the otherhand the cost of living indices and consumer price index of the period indicates that there has not been any untoward escalation ually point towards some meaningful directions to which the policies and practices may re-orient themselves with consequent improvement in the administration and its benefits may hopefully emanate to the state.

**Saiful Islam Khan**
Member
National Board of Revenue, and
President
BCS (Customs & Excise) Association.



# *Value Added Tax Administration and Its Potential in Bangladesh*

DR. RAFIQUL ISLAM
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National Board of Revenue

### *Taxing Our Patience*

Communication is all about people being able to understand each other. Except when it comes to Government forms and directives. That's when middle brained civil servants are in a class of their own. The following is an example which arrived in employer's offices courtesy the Inland Revenue :

"Errors on form P38A (1992). Form P38A (1992) was enclosed with the form P35 (Employer's annual return) sent to you in late January / early February. We apologise for the fact that Form P38A contained the following two errors.

1. Question No. 1 of the check list on Form P35 says you should complete form P38A if you answer 'No' to this question. However, Form P38A itself asks you to complete it if you answered 'Yes' to Question 1 on the form P35.

2. On form P38A Question 3 asks 'Was the worker paid less than £100 in Total for that year?' This Question should say 'Was the worker paid less £100 in total for the year (leaving out those workers for whom a Form P46 is held)?"

----- "What does it mean? Search me" ---- asks the reporting newspaper.

[ Daily Star, April 13, 1992, P-9, London ].

### *Introduction*

The origin of Value Added Tax (VAT) can be traced as far back as the writings of F Von Siemens, who proposed it in 1918 as a substitute for the then newly established German turnover tax. Since then numerous economists have recommended it in different contexts. Also, various committees have examined the tax in great detail. However, for its rejuvenation, the tax owes much to Maurice Faure and Carl Shoup. The recent evolution of VAT can be considered as the most important fiscal innovation of the present century[1]. VAT

1 Mahesh C. Purohit, Principles and Practices of Value Added Tax, Gayatri Publications, Delhi, India. 1993. p.1.

was first introduced in France in 1954. With the imposition of *Taxe sur la Valeur Adjoutee*, France become the first European country to implement VAT on an extensive scale. It was not, however, at first a complete system of VAT, since it applied only to transactions entered into by manufacturers and wholesalers. It was supplemented by a separate tax on services *(Tax sur les Prestations de Services)*. In addition, there were special excises (Taxes uniques) which were levied on services and distribution in lieu of the *taxes sur les presentations de services*.

***Evolution of VAT***

Value Added Tax (VAT) was introduced in Bangladesh from the 1st of July, 1991. This tax is levied, as a substitute for excise duty, on most of the goods and services which were subjected to excise duty. It may be mentioned here, at the import stage, sales tax was abolished and VAT levied and collected in its place. However, for some initial administrative difficulties, a few selected commodities, such as, tobacco products, natural gas, petroleum products, etc., and also a few "services" remained within the purview of excise duty for some time. Now they are under VAT. Value Added Tax in Bangladesh is mainly confined to the import and manufacturing stages. In most of the countries of the world where there is VAT it is compulsory in both wholesale and retail distribution of goods and services.

At present the Turn Over Tax and the Cottage Industry exemptions are of the same limit. Cottage industries upto a turn over of Tk. 15 lakh are exempt. Small industries with a turn over of Tk. 15 lakh pay tax at the rate of 4%. There is a Turn Over Tax Determination Commission, which determines on a yearly basis the minimum tax payable by specific units and settles disputes between turnover units and VAT offices.

There were about four hundred and twenty six items of manufacture on which Supplementary Duty was leviable at various rates ranging from five per cent to 350%. Supplementary Duty was introduced to keep the total quantum of revenue intact, to discourage the importation of luxury goods and goods use of which were considered harmful on social, moral or religious grounds.

Though five years have elapsed by now, the system could not achieve a considerable dynamism because of the absence of strong measures and improved management. Indirect taxes collected from local sources viz. excise duty, VAT and supplementary duty now account

1 Turn over Tax rate was 2% from 1991 upto 1997 June. FY 96-97 has increased the rate to 4%.



for almost 26.32 percent of the total revenue collected by the National Board of Revenue. VAT has not been extended to cover all the economic sectors. One of the striking and pro-clientele features of VAT system is its credit mechanism. In order to ensure that trade sector benefits from this system it is essential that the VAT network is expanded, phase by phase, up to wholesale and retail levels. A legal provision for optional VAT registration by the wholesalers and retailers was introduced in FY 94-95, but no such registration was reported to have been taken. If VAT is introduced at all the levels of consumption- import, production, wholesale and retail- then the taxpayers themselves will be able to get credit on the input-taxes thus reducing the incidence of tax.

At present, excise duty is levied on bank deposits. In cases where the balance exceeded Taka five thousand and does not exceed Taka one lakh, the leviable duty till FY 96-97 was Taka one hundred and twenty; in other cases it was Taka two hundred. The depositors having small deposits would thus pay more taxes as compared to the depositors having big ones. Nominal amount of taxes was collected in cases where the balance exceeds crores of Taka. With a view to give relief to the small depositors, excise duty from the accounts were withdrawn where the balance does not exceed Taka ten thousand and having considered the financial capability, the rates of excise duty on bank services were made progressive in FY 96-97. Excise duty leviable on biri was Taka 22 per thousand sticks. The rate was Taka 19.25 in 1993-94. This was increased to Taka 25 in 96-97 FY. On cigarettes, at present the supplementary duty rates are 35 percent, 50 percent and 53 percent. Keeping the highest rate as it is, the lower rates were made progressive in FY 96-97.

Until July 1996, there were twentynine services on which VAT is leviable. During the last few years there has been a considerable expansion of different services. These have not, however, been brought under VAT network. Services like that of Shipping Agents, Audit and Accountancy firm, Consultancy and Supervisory firm, Leasing Deeds (Ijaradar) were brought under the network of Value Added Tax. Besides, the trading activities of luxury items like motor cars, airconditioners, dish antennas, etc. have been brought under the purview of VAT at the retail level.

A number of qualitative and important changes have been brought about in the VAT law. There were no incentive for the use of locally produced capital machinery in the export oriented industries.

Necessary provision in the VAT Rules were made in order to extend facility for the use of locally made capital machinery in the export oriented industries.

Timely realization of government revenue is very important. In many cases, persons and agencies empowered to collect VAT refrain from depositing the amount with the government exchequer, having collected it from the consumers. In order to encounter this tendency effectively, legal provision to take proper punitive measure has been incorporated in the Value Added Tax Act.

VAT officials inspect different VAT units but since the inspections were not carried out following predetermined methodology, there were hardly any follow-up actions taken. To make the inspection procedure systematic and result-oriented now a VAT unit can be inspected without giving any notice, but the inspecting officer will have to submit an inspection report within 48 hours of the completion of the inspection and for the sake of transparency, a copy of the report will be given to the unit owner within the same time frame.

VAT registered tax units were to submit return on monthly basis. Because of the uniqueness of business, production of many VAT units is seasonal. In view of this in cases of construction firms, export-oriented industries and brick manufacturers, now returns can be submitted quarterly.

Tax Identification Number (TIN) has to be mentioned in the application form for VAT registration and in the VAT registration certificate so that the exchange of information between taxation and VAT departments becomes easier than before.

Tax structure in Bangladesh is still heavily dependent on indirect taxes. Import duties during the fiscal years 1990-91, 91-92 and 92-93 constituted 51.57%, 55%, 54.34% respectively of the total revenue collection. The components were import duties, sales tax, VAT and supplementary duty at import stage. Indirect taxes from the domestic economy collected in the form of Excise, VAT and Supplementary Duty in the years 1990-91, 91-92 and 92-93 contributed 28.40%, 25.79% and 25.11% respectively of the total tax revenue. The share of direct taxes in those years was 20.03%, 19.21% and 20.55% respectively of the total revenue collected by the National Board of Revenue. About 88 per cent of VAT and Supplementary Duty on goods and services still comes from those sectors which were previously covered under Excise Duty and Sales



Tax. The goods and services which were included in the VAT for the first time contribute only 12 per cent of the domestic VAT. In 1992-93 there were 48,987 VAT registered units and in July 1996 this number was 1,06,022 out of which 73,011 units are from construction sector. VAT records show that there were 13,094 importers and 1,107 exporters registered in 92-93 FY. In the VAT administration work is under way to prepare VAT profiles for each VAT registered unit. The VAT administration will become transparent significantly when the job of computerization will be completed. Intra-sectoral analysis will be possible by indentifying the inputs, outputs, prices, VAT payable, VAT realised through treasury chalan and the rebates/refunds enjoyed by the VAT registered units. The VAT information bank will be useful to the client groups as well.

***Value Added Tax in Bangladesh***

The main features of VAT in Bangladesh are as follows:

(1) A single stage VAT for import cum manufacturing.

(2) A uniform rate of 15 per cent is applicable for both goods & services.

(3) VAT for whole salers/retailers is compulsory (for selected items).

(4) VAT is applicable for all items (except some of the unprocessed agricultural products) & thirty five listed services.

(5) Exports are zero rated.

(6) VAT is leviable at the time of supply of goods and services.

(7) Turnover tax @ 4 per cent is leviable where turnover amount is less than 1.5 million taka.

(8) Cottage industries are exempt from VAT.

(9) Tax paid on inputs are creditable against output tax.

(10) Tax returns are to be submitted on monthly or quarterly basis.

(11) Luxurious and socially undesirable goods are subject to supplementary duties at different rates ranging from 5 per cent to 350 per cent.

Cigarettes, natural gas and petroleum products which were the major sources of excise duties, initially were kept beyond VAT net work. In 1992-93 these items were brought under VAT. It may be mentioned that at present manually made cigarettes (known as Biri), part of textile items & services rendered by commercial banks are still under excise system.

The primary requirement under VAT system in Bangladesh is to have registration numbers by all taxable persons from the local VAT authorities. Such registrations are compulsory for each location of a business. The taxable persons are to apply in a specific form to the VAT authority if their annual turn over exceeds 1.5 million taka . The taxpayers are given a registration number through a specific certificate. The registration certificate contains alongwith other information the activity codes in which the person is related. The registration numbers are used by the taxpayers in their business transactions. Registrations are done free of cost and are not subject to renewal. Any person whose annual turnover is less than 1.5 million taka or any person outside VAT may also apply for registration voluntarily. Any registration may be cancelled if the person discontinues his business or if his annual turnover is found to be less than 1.5 million taka.

Under the VAT system in Bangladesh all tax payers are required to maintain books of accounts regarding purchases, sales,raw materials,finished products etc. They are also to maintain an account current book to help them to determine the amount of VAT due and the amount actually paid for taxable goods. Payment of taxes are made through adjustments in the account current book . Credit available for input taxes and refund against export can be used to settle the liability for output tax.

The value of imported goods for levy and collection of VAT is considered to be the assessable value for levy of custom duties plus other duties and taxes. While for domestic goods, this value is consideration (the money value) at which the goods are supplied by the manufacturer, this value includes all costs, charges, commission, duties and taxes except the VAT amount. On the other hand, the gross receipts is considered to be the basis for determineing the VAT liability for sevices in general. But in special cases,some narrow base values instead of gross value are taken into account for VAT calculation. Again in some cases, tariff values are fixed as base value for determining VAT.

Each tax payer is required to issue a tax invoice,as proof of payment of VAT, for each supply of goods or services. However, the importers are not required to issue any tax invoice. But when importers sell their goods they may issue a supplementary tax invoice to a VAT registered person. VAT on imported goods are to be paid by the



importers at the time when the customs duties on it are paid. In other words, VAT at import stage is paid before clearance of goods. But for the local manufactured goods VAT is payable at the time of supply of goods and services. Each registered supplier of goods or services is eligible to take instant credit of the VAT paid on inputs. The payment of VAT for goods (output tax) are made through adjustment in the account current book. Taxpayers are to keep sufficient balance in their credit in the current account book either through deposition of money to the Govt. treasury or through their input tax credit. System have also been introduced to collect taxes on certain services like Construction, Motor Garages & Workshops, Printing, Indentors, etc. at the source point of payment.

Each taxpayer is to submit a tax retrun for each tax period (each calendar month) within 20 days of a month following the tax period. The VAT authorities examine the returns, and enters the data into the computer.

All exports of goods & services are zero rated under VAT system. Moreover, all input taxes (VAT, Customs duty, Excise duty etc) paid on the inputs used for manufacturing the exported goods are refundable. Such input taxes against export are refunded either in actual or on a flat rate basis. Refund claims of input taxes are dealt with by a Duty Exemption and Drawback Office (DEDO).

Value added tax system in Bangladesh gives special treatment to the small firms. Under the system, small manufacturers and services whose annual turnover is less than 1.5 million taka is exempt from VAT but they are to pay turnover tax @ 4 per cent. Such turnover tax can be paid either at a time or on quarterly basis. But they are not entitled to get credit benefit of their input taxes. Moreover, small firms whose annual turnover is less than 1.5 million taka and whose investment in capital machineries only during a particular year does not exceed 300,000 taka are treated as a cottage industry and is fully exempt from VAT or turn over tax. They are also free from VAT formalities. It is easy to have the benefits of VAT in an economy where it is implemented in a comprehensive form covering all tiers of production and distribution as well as to all economic activities. The single stage VAT in Bangladesh has undoubtedly widened the tax base as compared to excise or sales tax system and has brought a favourable result in collection of taxes but it had limited further results due to some limitation and distortion in its application.

## ADVANTAGES OF VAT

### *Concept*

The rise of the value added tax (VAT) is a spectacular fiscal phenomenon. Within a rather short span, this tax has exploded from its rudimentary form to become the state-of-the-art tax on goods and services all around the globe. Today the VAT has come to be acclaimed more and more as the most efficient, broad based and revenue-productive system of indirect taxation. In recent times VAT has been increasingly adopted by many developing countries around the world, that share with Bangladesh the same policy objectives of development and socio-economic stability and are subject to the same constraints that may affect the efficiency of the tax administration.

VAT is a tax on the value added by a firm to the goods and services it buys from other firms. Operationally, the taxpayer adds VAT at a given rate to its sales and then deducts the amount already paid as VAT on its purchases before paying the net amount to the tax department. VAT thus avoids the taxation of inputs and its base is the final goods.

### *Problems of the previous system*

Bangladesh had a relatively complicated indirect tax system. It failed to provide the domestic resources needed for achieving the macro economic goals of the government. The system relied too heavily on the taxation of imports which essentially taxed the raw materials and intermediate goods. The import based taxation performed two related functions. It was both revenue raising and protective. The structure of protection again afforded unintended protection to industries, not justified on economic grounds. It thus led to inefficiencies in production and created an overwhelming antiexport bias. Since, around sixty percent of the total tax revenue is collected from the import based taxation, revenue collection in Bangladesh effectively became a hostage to the balance of payments situation. The system of excise taxation used for collecting revenue from domestic production and services was also badly flawed. The base was very narrow, there were too many rates and exemptions. In the absence of a credit mechanism substantial cascading was prevalent. There was also a lack of harmony in regard to the tax treatment of the imports and the domestically produced goods. The resultant effects of all these were that the tax-GDP ratio in Bangladesh was one of the lowest in the world and the system of taxation was inefficient, distortionary and inelastic.

### *Benefits of VAT*

The VAT avoids most of the negative features of the sales tax and excise taxes. It removes cascading, allowing the tax content of any



product to be known with greater degree of certainty and thus leading to better resource allocation decisions as the investment decisions can be taken independent of the tax policies. The self policing and cross checking properties of VAT as well as its collection in stages, leave less incentive for evasion. There is no frequent change in tax policies allowing investors to operate in a certain and stable tax environment. VAT simplifies tax administration and increases efficiency in resource allocation.

## PRICE EFFECT OF VAT

Price effect of VAT at the retail level is usually insignificant. In Bangladesh the effect of 15% VAT at retail level on sale of cars was calculated assuming a profit magin of 25% where the selling price was Tk. 287,500.00 and it was found that the price increase at the retail level was only 2.68%. Experiences of other countries are shown in following table:

Examples of Effects on Prices of Introduction of VAT

| Country | Date VAT Introduced | Immediate Price Change General[1] (In percent) | Attributed to VAT[2] (In percent) |
|---|---|---|---|
| Argentina | Jan. 1975 | 37.2 | Minor |
| Brazil | Jan. 1967- | 15.8 | Nil |
| Chile | Mar. 1975 | 146.7 | Minor |
| Denmark | July 1967 | 8.0 | 5.0 |
| France | Jan. 1968 | 2.1 | 1.0 |
| Indonesia | Apr. 1985 | 3.5 | Nil |
| Israel | July 1976 | 17.9 | (9.0) |
| Korea | July 1977 | 4.1 | Minor |
| Madagascar | Jan. 1969 | 3.2 | Nil |
| Morocco | Jan. 1962 | 2.4 | Nil |
| Netherlands | Jan. 1969 | 5.2 | 1.5 |
| Norway | Jan. 1970 | 7.8 | 5.8 |
| Spain | Jan. 1986 | 2.8 | 2.0 |

*Source: IMF data and various country reports.*

There are findings to the contrary also. As for example, the US Treasury Report (1984, Vol. 3, pp. 89-93) estimated that a 10 percent VAT would lead to an 8 percent increase in consumer prices.

1 The consumer price index for the quarter before VAT is deducted from that for the quarter after VAT and the difference expressed as a percentage increase.

2 Figure in parentheses represent broad estimates based on examination of the data; other figures are based on external and contemporary commentaries.

## POLICY ISSUES

### *Consumption type, destination principle and invoice or credit method*

The VAT that has been introduced in Bangladesh is of the consumption type (as opposed to the income or gross product type) under which the VAT shall amount to a tax on the consumer goods only leaving out capital goods. This has been done to ensure neutrality with regard to the choice of techniques. With regard to the regime for international trade, the destination principle (as opposed to the origin principle) has been adopted, under which a VAT taxes all value added, at home and abroad, in relation to goods that have as their destination the consumers of Bangladesh. Under this system exports are zero rated and imports are subject to VAT. The destination principle is compatible with the consumption type of VAT. The other reasons for adopting the destination principle are that it emphasizes employment more than consumption and ensures neutral treatment of imported and domestic goods by taxing imports and domestic goods going into domestic consumption at the same rate. In a country like Bangladesh where the exchange rate does not adjust quickly and the factor prices are also not flexible, the destination principle has to be favoured. In respect of the method by which a tax paying firm may compute its tax liability, the invoice or tax credit method (as opposed to the account based method) has been adopted in Bangladesh in view of its compatibility with a consumption destination type of VAT. The tax credit method avoids the direct calculation of value added, instead, the tax rate is applied to a component of value added (output and inputs) and the resultant tax liabilities are subtracted to get the final net tax payble. Its other advantages are that the tax liability is attached to the transaction and the invoice becomes the crucial documentary evidence and that it creates a good audit trail. Further, any tax period (monthly or quarterly) can be used under this method, while the account based VAT would focus on the annual profit and loss account.

### *Import-cum-manufacturing*

With regard to the tax on goods, the VAT in Bangladesh was restricted to the import and manufacturing stage since the accounting system at the other levels of operation is weak. This would mean relatively few registered traders, clearly indentifiable taxable commodities and a less complex administration. The disadvantages here are that the revenue base is relatively small implying a higher rate of tax and that firms in collusion with wholesalers or retailers might understate the true value of sales and



thus cause erosion of VAT revenue. In 1996-97 fiscal budget measures retail level has come under VAT and now only nine group of goods are VATable at retail sale. In future the retail level VAT will be expanding.

### *Services*

Certain selected services were brought under the VAT system in Bangladesh during the introduction of the system in 1991. A few more services have also been added to the list in 1992,1996 and in 1997. Since organized manufacturing accounts for only 15 percent of value added in Bangladesh, in order to have a meaningfully broad based VAT, it is essential to expand the VAT system to cover as large an area of services as possible. But although the total value added by services is quite high in Bangladesh (about 40 percent) only a small proportion of this value added could come under the potential VAT base. Services like education, public administration, and health would certainly remain outside the tax net leaving only 15-20 percent of total value added in service sectors that could be covered under VAT. The services however belong to the difficult tax area. It is difficult to define the service sector precisely and to measure its output. The location or time of supply or consumption of services is often elusive or even meaningless. Since the service sector is characterised by high value added than in the stage of production, it is immediately susceptible to evasion as well. Again, the predominance of labour intensive production in service limits economies of scale thus leading to the creation of a large number of difficult to tax small service renderers. Nevertheless, for distributional, efficiency and welfare reasons services should be brought under the VAT net as far as possible. Further efforts in base expansion would therefore lie principally in this direction.

### *Single rate*

The VAT in Bangladesh has a single rate of 15 percent, the exports being zero rated. A single rate has both administrative and accounting advantages and the multiple rates are to be avoided for many reasons. In a VAT system upto the manufacturing stage, multiple rates would distort producers choice. With multiple rates, the problems of classification and definition arise. Multiple rates are also an inefficient way to protect the poor as they protect the rich as well. Thus, instead of having multiple rates, the progressivity of the rate structure in respect of VAT in Bangladesh is designed to be brought about by the built-in exemptions and the imposition of supplementary duties in case of goods with high income elasticities of demand.

**Broader coverage**

The VAT in Bangladesh has a broader coverage compared with the bases of taxes it has replaced. All goods except those mentioned in the First Schedule to the VAT Act 1991 are subject to VAT (some more items have, however, been declared exempt by specific notifications). Theoretically, a tax that has consumption as its base has the desired property of being elastic. Since consumption is the largest component of GDP or value added, increase in revenue is expected to keep pace with the GDP growth. With regard to the services also, the VAT base is larger than the excise base it has replaced.

**Exemptions and exclusions**

To derive the maximum benifits from VAT as a non-cascading, efficient and buoyant revenue raising tax system, exemptions and exclusions should be kept at the minimum. Exemptions not only cause erosion of the tax base requiring imposition of higher rate to generate a given amount of revenue, they introduce cascading by bringing about breaks in the credit chains-something the VAT is designed precisely to avoid. Exemptions necessitate extra record keeping to separate the taxable from the exempt sales. Further, the distinction between what is exempt and what is taxed is often tenous or arbitraty. The use of exemptions can introduce ambiguity into the structure of tax rates by making the effective tax rate on a commodity a function of the structure of production, rendering the rate irrelevant. As a matter of principle, exemptions under VAT are not justified except onoverriding administrative expediency or equity grounds. In fact distributive goals would be better achieved if there exists necessary capacity to administer a comprehensive transfer system.

**Treatment of small firms**

For administrative and record keeping reasons, small firms have been kept outside the purview of the VAT in Bangladesh. There are two bases for exempting the small firms. Specified industries with installed capital machinery valued below Taka three lacs and with annual turnover below Taka fifteen lacs, are exempt from VAT. Secondly, all manufacturers or services rederers having turnover below Taka fifteen lacs are exempt from VAT. This way of exempting economic activities from the purview of VAT is not however free from problems. There is the protential danger of under reporting sales or understating the value of capital machineries. The borderline cases are also hard to deal with. This also creates competitive imbalance, since the exempted firms have artificial price advantage over the taxable firms leading to market distortions.





**Treatment of exports**

Exports are zero rated under the VAT system in Bangladesh. This implies that there would be no VAT on exports. In addition, all input taxes (VAT, customs duty, excise duty etc.) would be rebated. Under the VAT system, it would be possible to determine the hidden taxes with more confidence. As such, the rebate procedure would be more efficient and the amount rebated would approximate the actual input tax content of any export consignment.

## OTHER ISSUES

***Price effects of VAT***

The most sensitive aspect of VAT introduction is its effect on prices. It is bacause of this, the policy makers of different countries are often reluctant to introduce VAT in their countries. This fear is essentially groundless. VAT can lead to an once-for-all increase in prices if more revenues are desired. But there is nothing inherently inflationary about VAT. A study on international experience involving thirty nine countries shows that there was no price increase in twenty two countries. In the rest of the countries, there were one time price increases. Since VAT is a very big structural change, it often creates uncertainties in the minds of the businessmen and the consumers- the consumers anticipate inevitable price increase, while the businessmen use the across the board tax increase to widen profits. Prices could rise for reasons other than VAT as well, depending on the timing of VAT introduction. Although price increases were also apprehended in Bangladesh, the experience suggest that there has not been any significant rise in prices that could be attributed to VAT.

***Distribution effects***

It is usually argued that VAT is a regressive tax, as it is applied at uniform rate and there are few exemptions. But it can be made progressive if the items consumed by the rich are taxed more. In fact, the taxes replaced by the VAT were no less regressive. VAT is not designed to correct inequities. It is a part of the overall tax system in the country and as such the impact of VAT should be considered in the context of the overall tax system. In fact, tax system is not an efficient instrument for ensuring equity. If more revenues are available to the government, equity aspect could be better taken care of by increasing the supply of government services targeted to the poor-better housing, improved medical care and better education.

***Revenue effects***

In the developing countries, VAT has been acclaimed as a money machine. In India, revenue growth was twenty eight percent, in the first year of the introduction of MOD VAT compared with twelve percent in the year before. In Indonesia, revenue collection just doubled during the first year of introduction of the VAT. In Argentina, Chile, Costa Rica and Korea, the ratio of revenue to GDP grew by fifty percent during the first three years compared with revenue from indirect taxes replaced by the VAT. In Bangladesh, VAT has been found to be moderately revenue augmenting during the first years of introduction.

In terms of complexity of development, demand for human resources and the impact it will have the soceity, the implemention of VAT in Bangladesh will rank as one of the most significant development projects ever undertakens in this country. The introduction of VAT in any country poses a gigantic management problem. The transitional issues need special attention which often span over 3-4 years. Once the transitional phase is over, and the base is consolidated, then the benefits of the system come into full play. It is, therefore, imperative to strive hard to lay the system firmly in place, initiate related changes and integrate the same into socio-economic mosaic of the country as surely and as smoothly as possible so that the tax induced and related distortions are removed, paving the way for industrial expansion along economically justified lines and at the same time enough revenues are generated to reduce external dependence and contribute to the building of a self-reliant Bangladesh.

***Tax Reform***

Introduction of value added tax (VAT) in July 1991 replacing sales tax on imports and many domestic excises, at a rate of 15 percent of the manufacturing-cum-import stage is a major tax reform in the country. It is argued that among others it will raise revenue yield by increasing the tax base and improving the elasticity of the tax structure of the country. Sales tax on import covered under VAT accounted for about 12.2 percent of the total tax estimates for 1991/92 and the commodities previously under excise coming under VAT, accounted for about 8.1 percent of the total tax yield. The major contributor to the excise taxes (about 70 percent), namely, tobacco, natural gas and petroleum were initially left out of the VAT net. Thus 60 percent of the VAT tax yield came from sales tax on import which was already the most efficient tax head since, once the import duty is paid, one cannot avoid paying sales tax. Given the tax



rate, tax yield under this head will be similar by whatever name it is collected. VAT replacing excises show that it still accounts for only around 8 percent of the total tax yield and as such the tax base remains very narrow. Unless VAT net is comprehensive it cannot achieve among other, the objectives of being a general tax covering, as far as practiable, all goods and services and be levied on all stages of production and distribution including the retail stage. A piece meal introduction of VAT negates its theoretical superiority over other tax handles because effect of an exemption prior to final stage is accumulation of tax caused by including previously paid VAT in the base upon which a later VAT is applied. Thus the cascading effect, which VAT was supposed to have avoided is reintroduced. In fact, almost all the attributes to VAT such as being neutral, non-discriminatory between products etc. on which it is theoretically justified to be superior to other tax systems are completely destroyed unless it is a comprehensive one.

Theoretically there is no reason as to why the tax structure of Bangladesh should not be elastic. Direct tax rates are very progressive while ad valorem tax rates imply proportional tax rates for indirect taxes. Therefore, as national income increases, yield from direct taxes should increase at a faster rate since higher proportion of increased income would be paid in taxes. Elasticity of tax bases should determine the overall income elasticity of indirect taxes. We have noted that all the major tax bases of indirect taxes are elastic. Hence there is no reason as to why even overall indirect tax yield should be inelastic. The problem was identified to lie primarily on administrative capability. The success of VAT, on the other hand, crucially depends on efficient administration and developed accounting system. One need not argue about the state of accounts keeping in ordinary transactions in Bangladesh while poor administration is the major weakness of our tax system. Thus poor tax administration and narrow tax base remain to be the crucial stumbling blocks in improving our tax revenue and elasticity of the tax structure.

Composition of indirect tax yield, on the other hand, still remains similar to what it was before the tax reform. Excise taxes still accounted for about a quarter of total tax revenue in 1991/92 and about 70 percent of it was contributed by tobacco, natural gas and petroleum which were left out of VAT net. VAT replacing excise show that it still accounts for only around 8 percent of total tax yield implying that the tax base under this head is still very narrow. To get full avantage of VAT it should be comprehensive covering both the production and distribution and upto the retail stage. The elasticity of the tax system can be ensured only if it covers all sales. If the tax is truly general, no matter what part of the economy is expanding, the VAT will respond at once to that activity.

During a transitional period, such as the one Bangladesh is passing through now, a zero rate of tax at the retail stage or to goods and services that are to be exempted from paying taxes may be imposed. This is a technical device to operate a complete VAT structure while still exempting some commodities entirely from tax.

The zero rate is an actual tax rate of the VAT, the same as 15 percent, 10 percent etc. Thus, the credit offset on purchases can be claimed against the liability i.e., zero. On the other hand, a good which is exempt cannot claim any credit and has no tax liability against which to offset it and thereby pays tax on input which must be wholly passed on or absorbed. In this way, the zero rate allows consumers complete exemption because, for instance, the retailer can claim full amount of tax he has paid on his input and, therefore, pays no tax, while all the previous stages have passed their tax liability fully forward. Initially it will involve the required cost of administration without yielding any revenue. But this will bring all economic activities under the VAT system which will help achieving the ultimate objective of having an elastic tax system for the country.

Inevitability of the imports as a tax base was reinforced when value added tax (VAT) was introduced in the country. In relation to the domestic production, excises, and in relation to the imports, sales tax and development surcharge were replaced by a very simple form of Value Added Taxes in 1991. Introduction of VAT was the result of global popularity of the system as a modern tax and the increasingly felt need for harmonisation of the tax systems across the world. It is interesting to note that the replacement of the sales taxes and the DSC at the import stage by the VAT resulted in a higher effective rate of duty, but went rather unnoticed for obvious reasons. However, the single flat rate of VAT is ideally simple in nature, but inconsistent with the broader policy of differential treatment of different commodities for obtaining non-revenue socio-economic goals of the nation. VAT at the import stage confirms the inescapability from the foreign trade bias of the prevailing tax-srtucture.

Starting with Caves who analysed Cananda's Tariff structure from a political decision making prespective, various alternative tax reform models have been developed for explaning the existing tax structures. On the face of it, the reform activities in Bangladesh illustrates an environmental dependency model where the changes



occur in response to the political and economic environment in the context of which the tax policy makers operate. But a deeper analysis reveals a Niskanian rational model where the individual bureaucrat is assumed to be rational actor seeking to maximise personal gain and self-intrerest in course of day to day activities. In this light, tax reform in Bangladesh, appears of to be mainly the product of bureaucratic polity who seeks to protect their position by minimising the political cost of tax programme while preventing a budget short-fall. They are constrained by the nexus of the political-government and the income-earners cum consumers as the interest groups. Any substantial reform would that the political government affords to break this nexus and comes forward with reform package purported to make a breakthrough in revenue mobilisation.

In a variant of this model, it has been suggested that minimisation of political cost may be considered an objective function of the governments. Political cost in essence is the untoward possibility of displacement from authority. Any political regime coming to power through an illegitimate way is destined to face significant level of threat. Given that the power regime is aware of it, it has been asserted that some political behaviour organized around the goal of risk reduction is quite likely to take place.

In the prevailing circumstances, the foremost target of any revenue augmenting reform would be to set up a long run pattern of revenue growth which is not lower than the growth of national income and in addition, commensurates with the annual growth of the expenditure budget. The long run trend should be at such a level that any minor fluctuation would not threaten with a budget deficit and would not call for ad hoc fiscal measures. This would require a linkage of the tax to its base and choosing a base which is well linked to the growth of national income. After a successful linking of the taxation mechanism with the growth of income, comes the second target of harmonising the tax programme with the broader socio-economic objectives of the country. Operationally this would require comprehensive rationalisation of the tax structure in conformity with the national plans for growth and development. This would demand an integration of the tax planning with the tax policy making. This integration would be required at the official level and would call for re-organisation of the entire tax policy sector. Unless such steps are taken, it is feared that the formulation of reform oriented tax policy would continue in the traditional incremental pattern and the source of the problem would continue to exist.

Finally, any major revenue augmenting tax reform is expected to raise the tax liability of the people in direct or indirect way. This would, therefore,require political will and capability of a stature that transcends the capacity of the bureaucratic polity. Consequently, unless there is a political leadership of the reform movement, it is unlikely that any worthwhile reform programme will materialise.



## WHY VAT

A striking feature of recent tax reforms world-wide has been the steadily growing number of countries adopting the Value Added Tax (VAT). Since the 1960s, more than 80 industrial and developing countries have embraced the VAT and it has become the main consumption tax across the globe.

Although the specific reasons for adopting the VAT differ from one country to another, the main argument is that properly designed VAT rasies more revenue with less administrative and economic cost than other broadly based taxes. VAT does not influence the methods of doing business, it ensures neutrality in international trade by freeing exports of tax, treats import and domestic goods the same, and is much harder to evade in comparison to other consumption taxes.

There can be no doubt about the significant advantages to be gained from the introduction of VAT. This is borne out by many of the studies carried out in countries which have introduced it, showing a growth in revenue yield and stimulation of the economy.

If a developing country needs to review its taxation strategy, the use of a VAT as a first step should be given serious consideration. The widespread use of this tax in highly industrialised and developing nations alike indicates that it has a basic effectiveness that cannot be ignored. However, it is not a simple tax, and needs care in its introduction and administration.

There is much to be said for making a virtue of necessity, and if it is decided to adopt a VAT then the opportunity should be taken to upgrade the government department which is being made responsible for its administration. The benefits of all the introductory work (improved procedures, forms design, computer systems, training, publicity campaigns, etc.) can then not only produce a better performance of the tax itself, but can also serve as a valuable guide and example to be used to carry out improvements in the working arrangements of other taxation regims in force in the country. Furthermore, an effective VAT can, in time, lead to improvements in record keeping and reporting by businesses which benefits the whole of the trading community.

In introducing a VAT many countries have encountered serious difficulties due to two main causes. The first is that the basic tax structure has been made too complex, e.g. too many rates of tax, too many exemptions from tax, etc. The second is that the administration has found itself unequal to the task of making the tax operate with a reasonable degree of success.

*VAT as an Instrument of Taxation Policy*

Taxation forms only one part of the economy of a country, and the proportion of gross domestic product (GDP) it absorbs will vary according to the requirements and dictates of the state. What is certain, however, is that an adequate and assured flow of revenue is essential to any government. This is perhaps particularly true in those cases where industrialisation remains limited, domestic savings are too small to provide sufficient investment for economic growth, and terms of trade are adverse with balance-of-payments difficulties arising. Such problems are often of concern to developing countries, and therein we examine the position of Value Added Tax (VAT) as a factor in their taxation strategies.

*A Gradual Approach to changes in Taxation Structure*

It would be inappropriate to review one tax in isolation,. An initial review of the total taxation structure (direct and indirect taxes, including customs tariffs and any relevant local or state taxes) is advisable. This does not mean, however, that action should be taken to change all the taxation regimes at the same time. A step by step approach is both safer and more certain of achieving the desired end result of improved revenue yield from an increasingly compliant taxpaying fraternity.

*The Advantages for Developing Countries*

In the case of developing countries, the approach recommended has many advantages. The likely outcome of the exercise can be more accurately assessed and, because the number of potential VAT taxpayers is likely to be fewer, the workload imposed on the administration is much reduced. As an introductory measure, the adoption of a VAT can be extremely valuable in carrying through subsequent changes in other areas of taxation.

## VAT AND THE TAX YIELD

*VAT as a Proportion of Total Taxation*

The revenues arising from the imposition of VAT can be considerable and, in those countries in which it has been introduced, it has provided a large proportion of the total tax yield. In the case of the European Community (EC), the percentage of total revenue provided by VAT in 1988 varied between member states from over 14% to over 24%. The tax also formed a considerable proportion of GDP, between over 5% and over 9% (ignoring Portugal and the Netherlands). In



Bangladesh VAT (local and import stage including supplementary duty) constituted about 44% of total tax revenue in 1995-96.

*The Importance of Indirect Taxation*

The position of VAT in the taxation systems of developing countries is not so clear, as separate figures for that tax are not readily available. Nevertheless, figures available, related to domestic taxes on goods and services, and taxes on general sales or on turnover, or VAT show wide variations, but clearly emphasise the importance of indirect taxation in the economies of developing nations. The indications are that the adopting of VAT could, in some instances, facilitate revision of certain excise-type taxes and also those imposed on particular types of services.

## THE ADVANTAGES OF VAT

*In widespread use*

VAT is in use in well over sixty countries throughout the world. In its usual form, it is a transaction-based consumer tax applicable to both goods and services, with the invoice (on which the VAT liability may be shown separately) acting as the basic evidential document. It is neutral in effect, the tax liability on sales (outputs) being offset by the tax paid on purchases (inputs). It thus avoids "cascading"; tax being paid again on goods which have already borne tax, which frequently occurs in the case of general sales taxes.

*Exports*

VAT frees exports from the burden of tax in that the tax paid on inputs can be identified and recovered by the exporter. Consequently, goods enter into international trade on an equal footing in this respect with those from other countries.

*VAT as an aid to Tax Reform*

A full VAT paid on importations and extending throughout manufacturing, wholesale/distribution and retail businesses - and including services - provides a wide tax base and, depending on the state of the economy, a buoyant source of revenue. Because of this revenue-generating capability, the introduction of a VAT can be used to reform or modify other taxation structures. For example, high customs tariffs may be lowered, a complex series of excise-type rates of tax simplified, or an unsatisfactory sales tax removed.

## OTHER BENEFITS OF VAT

### *Planning Skills*

In order to produce good results, the introduction of a VAT, whether a full or partial ("credit") system, needs to be carefully planned. This requires the setting up of a team dedicated to the work and allows new skills to be developed, possibly with the assistance of consultants who have been involved in such projects in other countries.

### Increased Administrative Capability

The introduction of a VAT will require the drafting of new law and new regulations. For the administration, this will involve the setting up of new organisational structures, the designing of new procedures and forms, writing of new instructions, arranging for the provision of better management information and statistics, etc. This gives the administration the opportunity to develop new skills and abilities which can subsequently be deployed right across the tax systems. A necessary feature of a VAT is the introduction of computer systems or the enhancement of those currently in operation. In-country experience may be limited in this area of work and the gradual approach to the taxation system can be of real benefit here.

### *New Relationship with Taxpayers*

In some developing countries, contacts between the administration and the taxpayers are limited to routine control duties and to enforcement and audit activities. Introducing a new tax allows a fresh approach to be made. Publicity campaigns can be designed with a view to improving the taxpayer's view of officialdom. Simple explanations as to why a new tax is required and how it will work may improve the image of the taxation authorities. Different approaches to the education of taxpayers can be adopted, and the use of explanatory leaflets in easily understood language and in eye-catching layout can help. Many steps can be taken to improve the administrator/taxpayer relationship which may lead in the longer term to improved trader compliance.

### *Better Record Keeping by the Business Community*

The control of VAT rests on the use of invoices and the keeping of records by the taxpayers. Larger companies in most countries generally keep adequate records, usually held on computers. Often it is the small companies, frequently sole proprietorships, that are not keeping proper records. It is these people that are the most difficult to control effectively for the purposes of taxation. In this connection, much will depend on the level of turnover at which businesses are required to register for tax. If the level is set too low, the cost of adequate control may become excessive. Good publicity aimed at the education of taxpayers in the requirements of the tax will facilitate its administration and can lead, in time, to a general improvement in business procedures.



### *Use of Unique Numeric Identifiers*

For a VAT it is essential that each business registered for the tax is identified by means of an identification number unique to that business. Where a suitable system of numbering already exists, it should be used for the VAT. Where it does not, a system of unique numbers (incorporating check digits) will have to be developed. Once established, the VAT system of unique numbers can be extened to other tax and associated areas. This can lead to each business using one number for most of its transactions with government.

### *Training : An Essential Element of Progress*

A neglected area in many administrations is training. Good training is expensive to design and carry into effect, but the rewards are great. Work is done better and complaints are fewer; there is greater flexibility in the use of staff whose morale and motivation are improved. As a result, costs are reduced. To introduce a new tax with any degree of success, staff at all levels must be well trained - from junior clerks to top management. This provides a further opportunity to improve on past performance. In the case of VAT, experience is gained in such matters as reviewing and re-designing training organisations, obtaining accommodation where this is currently inadequate, obtaining modern training equipment, preparing new course material, examining and improving training methods. Careful selection of a central core of trainers is essential since they will be responsible for training the staff, and some expert assistance may be necessary. Here again, much of the training experience and the strategies adopted for VAT can be used, after any necessary adaptation, to improve the situation in regard to other taxes.

## OBSTACLES AND OBJECTIVES

### *Obstacles facing the revenue administrations:*

- *inefficient management and organisational systems;*
- *weaknesses in revenue collection procedures;*

- *un-consolidated or inconsistent legislation;*
- *evasion and corruption;*
- *information systems handling risk profiling;*
- *inadequacy of staff incentives, and*
- *shortage of skills and training.*

***Objectives:***

- *strengthening the organisation and administration management;*
- *improving duties and tax collection;*
- *introducing information technology solutions;*
- *drafting laws and regulations;*
- *improving staff terms and condition, and*
- *facilitating the movement of goods.*

**Legislation**

Effectiveness of a revenue collection system is achieved by a clear understanding of, as well as, a consistent interpretation of the appropriate legislation. Proper legislation and legal drafting is necessary to ensure that revenue collection and enforcement officers have the necessary powers to perform their functions effectively. It is essential to have an implementation plan to improve the effectiveness and efficiency of a tax collection procedure. It is important to review and prepare administration, management and human resource strategies. Taxes and duty evasion, corruption and non-compliance severely reduce potential revenue yield and weaken the ability of governments to carry out their functions efficiently. To deal with such problems, and to strengthen enforcement and investigation measures following steps can be useful:

- *introducing new administrative, supervisory and auditing procedures;*
- *introducing risk analysis and profiling techniques;*
- *improving the co-ordination and exchange of information, both in-country and internationally;*
- *improving the quality of recruitment, remuneration packages, promotion and personnel practices;*
- *introducing improved collection systems;*
- *enhancing detection and investigative system and procedures, and*
- *designing and delivering appropriate training programmes.*



***Training***

Training is a fundamental component of capacity building, being a mechanism by which knowledge, experience, skills and technology is transferred; creating indigenous ability to take control and continue to develop functions independent of external help. For this reason a strong training component embracing a veriety of techniques from seminars, classroom learning, and distance learning packages, through to on-the-job training by the utilisation of counterpart staff during all stages of development is necessary.

**REVENUE ADMINISTRATION MODERNISATION AND REFORM PROGRAMME**

***Legislation***

To ensure that the revenue collection and administration legislation is adequate to enable the Income Tax, Sales Tax/Value Added Tax, and Customs and Excise Departments to undertake their delegated responsibilities effectively, and prepare amendments where shortcomings exist.

***Development Planning***

To define an administrative and operational framework for the organisation around which the programme of reform and modernisation will develop.

***Organisation & Structure***

An analysis and where necessary, modification of the structure and organisation to ensure that it can meet the requirements placed upon it.

***Business Process Re-engineering/Personnel/Instructional Manuals***

A thorough review of all operational and administrative issues designed to reflect the objectives of the Revenue Department to enable change to take place efficiently, effectively and with the support of staff at all levels within the organisation.

***Training***

Development of a comprehensive training programme for the whole organisation which will be designed to meet the objectives of the Department. Development of the staff will be monitored carefully against performance targets throughout.

***Automation***

Design, development and implementation of a programme of automation that will optimise the efficiency of the organisation and ensure that all relevant information is captured and utilised effectively.

***Anti Corruption Activities***

Implementation of specialist teams with the objective of targeting areas of abuse and ensuring that corrective action is implemented, and that revenue collection is enhanced in the short term.

***Investigation***

Development of an effective Investigation Division to operate within the organisational framework of the Revenue Department.

***Enforcement***

Implementation of effective enforcement procedures throughout the organisation.

***Publicity***

Development and implementation of publicity programme designed to inform. educate and demonstrate the transparency of the organisation.

***Internal Audit***

Creation and training of an Internal Audit Department designed to ensure that all procedures and controls are properly and correctly applied by all staff in the organisation.

## THE VAT MODULES

***The basic modules comprise:***

- Registration and De-registration
- Return Processing
- Automatic Processing of Penalties, Assessment and interest
- Trade Accounting
- Visits to Traders
- Control and Verification
- Enforcement
- Trader Credibility Checking and Risk Analysis
- Management Information System (MIS).



## FRAUD AND EVASION CONTROL

NBR must first consider whether the powers they have are sufficient to cope with VAT fraud and tackcing evasion. When fraud is suspected or discovered in VAT it is nearly always necessary to remove books, invoices, correspondences and subsidiary records from the tax payers premises. If this is not practical then it is necessary to have the power to make copies of the tax payers records.

Rules 43 and 47 of Value Added Tax Rule, 1991 give NBR and the Government respectvely the power "to summon and examine files and records" but this seems dangerously pedantic in the context of fraud. Incriminating evidence can so easily get lost in transit, it is often essential to remove documents and records as soon as fraud is suspected. NBR must be sure that Revenue Officers have the power to remove and/or copy books and records. Evidence obtained illegally will not be accepted in any court of law. It is better not to assume that the power is there in the law or rule but it is necessary to make sure before exercising save otherwise some very embarrassing situations may arise. When a fraud or suspected fraud case is to be transferred to the Investigation Directorate, all the documents and records should be photocopied and the photocopies sent to the Directorate with the Case Summary Form (F.C./01). The case officer who was responsible for the removal of the records should whenever possible retain the originals until required for court presentation. However one should remember that copying facilities are not always available at out-field offices and that original documents must be released to investigation staff and a detailed receipt obtained (Inventory Sheet Attached to Form F.C./01). A word of warning is appropriate here, when handing over tax payers records to investigation staff, that staff should be treated as an outside agency even if members are known personally. Nothing must be taken on trust, loss of a Tax Payers records is a very serious matter and it is the official who removed the records from the Trader's premises who will be responsible in Law. Form F.C./01 serves as a Transfer slip; case summary and receipt form. It should be prepared in triplicate, the top copy will be the investigation staff copy the duplicate will be retained by the Superintendent who will send the triplicate to the Head of Division. Obviously the Tax payer will ask for a receipt on the removal of his records and this must be given. However uplifting officials must show maximum care when issuing an official receipt and they must ensure documents, books etc., are securely and carefully stored while in official custody. There will be two types of fraud investigation, the local carried out by Circle Staff and the

Directorate of Investigation. It will be necessary to indentify these on the Computer from monitoring purposes through the medium of the location code. The Computer will have two direct inputs which will identify tax payers under investigation (i) the visit code and (ii) revenue rating compliance code . The location code will complete the picture by indentifying who is carrying out the investigation. It will be easy to remove the tax payers under investigation from the normal control visit selection routine. Tax payers will not be returned to the normal control visit selection programme until a notification is received from the Head of Division on From F.C./03. This Form will also show the outcome of the investigation in terms of underpaid Tax recovered and financial penalty imposed. It will be necessary to produce reports showing Annual Fraud Detection achievement by the VAT officies. When a fraud case is investigated in the first instance by the Investigation Department staff the above procedures are to be followed. This can be achieved by liaison with the Circle Superintendent and Head of Division.

Identification No. | | | | | | | | Circle Name ..............................

Circle Ref. No..............................

Division Code ..............................

Division Ref. No. ..............................



## INVENTORY OF DOCUMENTS - RECORDS

| Item No. | Description (e.g. Sales Day Book; Account Current, Purchase Invs. No. ..............................) |
|---|---|
| 1 | |
| 2 | |
| 3 | |
| 4 | |
| 5 | |
| 6 | |
| 7 | |
| 8 | |
| 9 | |
| 10 | |
| 11 | |
| 12 | |
| 13 | |
| 14 | |
| 15 | |
| 16 | |
| 17 | |
| 18 | |
| 19 | |
| 20 | |

Received as above lines .............................. to ..............................

.............................. Investigating Officer .............. Date

Directorate of Intelligence

& Investigation/ Audit/ Inspection

## INVESTIGATION CASE

Name : Circle .............................................. Name

Address : Circle .............................................. Ref. No.

Division .............................................. Code

Division .............................................. Ref. No.

Indentification No. [ | | | | | | | ]

Activity Code [ | | | | | | | ]

Location Code [ | | | | | ]

Suspect Period From .......... to ..........

Est. Tax Loss (T/000) ............. Taka

Summary of Case :-

............................ Date ................................ Inspector

[ | | | ] B. I. N.

............................ Date ........................Superintendent

Tear off

Superintendent ................ Circle Circle Ref. No..................

Case Accepted* Investigation Ref. No..................

Case Rejected* Papers as per Inventory Sheet returned herewith.

Reason for Rejection

..........................................................................................

..........................................................................................

..........................................................................................

Date ........................ Superintendent
for Director General





## INVESTIGATION CASE

Name : Investigation Ref. No.

..............................................

Circle Name

Address : ..............................................

Circle Ref. No.

..............................................

Division Code

..............................................

Division Ref. No.

Date Case Received

Date Case Cleared

Indentification No. [ | | | | | | | ]

Activity Code [ | | | | | | | ]

Location Code [ | | | | | ]

---

Dear

................................ Division

The Investigation of the above Tax Payer has been completed.

Summary of investigation

..........................................................................................

..........................................................................................

..........................................................................................

Tax Recoverable (Taka/000's) [ | | | | | | ]

Financial Penalty Imposed (Taka/000's) [ | | | | | | ]

............................ Date ................................ Director

F.C./03 To Collectorate Computer Cell ..........................................................

............................ Date ........................Initials

Form FC/03

## INVESTIGATION CASE

| | | | |
|---|---|---|---|
| Name : | Circle ........................................ | | Name |
| | Circle ........................................ | Ref. | No. |
| Address : | Division ........................................ | | Code |
| | Division ........................................ | Ref. | No. |
| | Date ........................................ | | Advised |

Indentification No. [ | | | | | | | ]

Activity Code [ | | | | | | ]

Location Code [ | | | | ]

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The Computer Cell

This case has been finalised. The Taxpayer should be returned to normal control visit selection with a scale of visiting set at:-

(a) No chance in visiting scale:*

(b) Changed to ........................ per year.*

(*Delete as appropriate)

---

Out of case :

Tax Recoverable (Taka/000's) [ | | | | | ]

Financial Penalty Imposed (Taka/000's) [ | | | | | ]

........................ Date ........................ Head of Division

---

Division..............................

Sir/Madam,

Input to Computer on..............................................................................

Date .............................. ........................................... For Commissioner



## COMBATTING EVASION

A sound knowledge of the mechanism of evasion is essential if any policy for fighting evasion is to be devised. Evasion necessarily depends on the opportunity of evasion and, for the vat, such an opportunity may be both a matter of discovery and planning. Planned evasion demands on the one hand good conversance with the vat laws, rules and current practice together with the loopholes therein, and the willingness and the courage to capitalise on such loopholes. Planned evasion is more possible for irregular VAT units than the regular established units. Unplanned evasion is the result of the units concern for reducing tax liability. But any opportunity of evasion, if it exists at all, has to be discovered by a competent person. Discovery of an opportunity may come from different sources. But in many cases where no scope of evasion is apparent, the VAT officer himself may come up with a novel plan. Usually this will be an evasion of a highly technical nature and may require stretching the legitimate discretionary authority vested in an officer. In the tax arena, officers who are capable of finding out loopholes in a seemingly `hopeless case' command special respect from the clients.

### *Modes of Evasion*

Choice of a mode of evasion is a limited domain. In reality a VAT unit does not have much discretion in choosing a mode of evasion in respect of his goods. Any person who is conversant with the VAT laws and practice is aware that the opportunity of evasion related to an item is usually situational and hence, rather invariable. Opportunity available with one item cannot be at will used for another item right away. Suitable opportunity is rather item specific and indeed depends on a large number of diverse factors such as the physical characters of the item, the intensity of legal enforcement prevailing at the time of clearance and manageability of the relevant officers and also visibility of the evasion mechanism.

It may be noted that popularity of a particular method of evasion differs with groups of commodities, and also between different stations. Such differences arise because of peculiarities of the local system of accountability, risk-taking attitude of the people involved, extent of physical surveillance, formal encoding of rules of conduct and procedural matters and the quality of record maintenance. Technological innovation also provides different opportunities of evasion.

It will transpire from the detail account of the modes of evasion that any proper investigation of a detected or suspected case and even general auditing will demand on the part of inquiry-officer or the auditor profound specialised knowledge that transcends mere common sense. Unless this condition is fulfilled, it can not be expected that any inquiry, investigation or audit by the most honest and sincere officer will meet with any fruitful discovery.

### *Undervaluation*

Undervaluation is the most infamous way of evasion. Here the unit declares a lower price than the actual price. This may again be done in two ways. Usually the taxpayer gets into understanding with the receiver of goods and a lower price is declared in the documents. The taxpayer may decide to totally ignore his counterpart if he is daring enough to forge documents and replace the genuine ones.

### *Underassessment*

The most prevalent form of co-operation by the VAT office is the underassessment of the goods. Underappraisement usually implies hiding of actual price of the commodity and accepting the declared price as the assessable value. In practice, the most prevalent principle of assessment for the purpose of assessment is the "uniformity in taxation" in respect of the comparably similar commodities produced within a narrow range of time.

### *Misdeclaration of Quantity*

Misdeclaration of quantity is resorted to whenever there is little scope of under valuation and where counting or measurement of quantity is a prohibitively problematic task. The advantage is that (i) there is little scope of detection from documentary audit or scrutiny and so, (ii) once the consignment is cleared out there is virtually no way to establish that an evasion had been effected. Misdeclaration of quantity is a favourite form of evasion. Miscalculation, may also take place. Straightforward error of calculation either in calculating the assessable value or the tax liability may be restored to by the taxpayer. Another way to evade tax liability may through forging of payment receipts(know as treasury challan) for clearance.



## INVOLVING OFFICERS IN THE EVASION PROCESS

### *To involve or Not*

After having decided to evade, the immediate problem for the taxpayer is to decide whether the co-operation of the relevant officers will be unavoidable in effecting an evasion plan or not. Involvement of an officer will have cost implication for him, and so it is not necessary that he will approach the concerned officer for co-operation in all cases of evasion.

### *Who are to be involved*

Involvement of senior officers depends on the distribution of legal authority and also on assessment of the risk involved. In matters where a senior officer is the authority for approving such a case, his involvement is unavoidable.

### *Why negotiation ?*

The process of involving the officer in the evasion phenomenon includes negotiation between the taxpayer and the officers. Such negotiation demands open communication between the involved officers and the taxpayer. Communication may be direct or indirect.

### *Monetary Transaction*

The amount of money that has to be paid to the officer depends on many factors like the amount of risk involved and demand pattern of the officer. Many officers are there who try to exploit the taxpayers if they are new in the evasion process. Many are there who are rigorous in calculation of the amount of benefit they are offering the taxpayer in exchange for bribe. They calculate their entitlement based on the differential amount. Problem arises when the amount of benefit accruing to the taxpayer is not clear or negligible.

### *Attitude and Motives*

Why people evade taxes? Much of the answer lies in the definition of tax itself. A tax is a compulsory contribution to government made without reference to a particular benefit received by the tax-payer. The absence of a perceived direct benefit causes taxation to be regarded as burdensome in a way that prices, paid in exchange for goods and services, are not. While the essential role of the state in providing certain benefits and services are recognised, people often fail to establish a connection with the tax they pay to the government and the services rendered by the government. Absence of this linkage between the state's service and the charges payable to it, which has been termed as fiscal connection encourages people to rationally seek reduction of personal liability of taxes while wishing that the government's beneficient role is maintained. Similarly many people think that paying taxes to government is a wastage of money. Tax non-compliance is just one of the many forms of peoples behaviour flouting government as an institution.

***Different Factors***

While the fiscal psychological model purports to explain evasion in terms of peoples attitude and motives, the economic model considers some deterrent factors as the crucial determinate of attempts at evasion. The economic model assumes that people are rational being whose only objectives are maximisation of utility from evasion. Evasion provides utility by way of extra income or saving of expenditure subject to certain deterrent elements.Utility from any attempt at evasion is uncertain because there is the chance of detection and detection may lead to punishment which may plausibly be construed as a cost of evasion. It has been argued that deterrent theory of punishment is special version of the general economic principles that raising the price of something will reduce the amount purchased.

***Administrative corruption***

Further realism was infused into the tax evasion model by incorporating the role of venal officers in effecting evasion. Thus, bribe paid to the corrupt tax official was considered as a cost to the evader which reduced the net gain from evasion. It was also suggested that anti-corruption policy could be strengthened to increase the expected cost of accepting bribe, which would cause the tax officials ask for higher unit bribe that would discourage evasion. While instrumentality of administrative corruption was not altogether ignored, obviously, evasion was still viewed as a problem of a tax-payer non-compliance and a public employee perspective was lacking. It may be recalled that the problem of the evasion of VAT has been considered more as a problem of corruption by the officials than as a tax-payer non-compliance.

***A Model of VAT Evasion***

Evasion may be on two counts: undervaluation of goods and services, and underreporting of quantity. From this premise we can write the following equation which is good for expressing evasion relating it to the two basic causative factors:

$$E=(V-v)t+V(Q-q)t$$

where, v = Assessable value of the goods as declared by the taxpayer
V = Normal value
Q = Quantity actually removed
q = Quantity reported as removed
t = tax rate.



Costs of evasion may include at least two major elements. First, the taxpayer may have to purchase co-operation of the officers in the act of evasion. In such a case he may have to give as bribe share of the evaded amount to the relevant officer. Secondly, he may have to minimise risk by spreading money among some potentially threatening agencies or persons who may be directly involved with law enforcement or in a position to leak out the information which might call for intervention by other agencies.

***Policy Implications***

The principal policy implications that are evident on interpretation of the model are :

(i) Constant surveillance (phisical and paper work) is necessary ;

(ii) Discretion in the fixation of assessable value should be abolished.

(iii) Evasion would be lower with higher rate of penalty.

However, legal provisions to combat evasion are to be applied by VAT officials and their attitude is very important in order to curb evasion successfully.

Corruption[1] is a cause (or an effect ?) of evasion. The following simple framework provides a useful tool to both identify causes of corruption as well as combat corruption:

$$C = M + D - A - S$$

Where,

C - corruption, M - monopoly, D - discretion, A - accountability and S - public sector salaries.

Corruption thrives where there is discretion and monopoly, accountability is weak and public servants are poorly paid. The main causes of corruption are also - (a) nature of the regulatory environment, (b) the lack of transparency in government, (c) the influence of powerful business interests, (d) low salaries for public servants, (e) weaknesses in the legal framework, (f) the self-sustaining cycle of corruption, etc. One view of corruption is that it represents a disguised form of taxation, an earmarked tax, as only the actual users of services need to pay.

Frustration, including annoyance with the compliance costs, may tempt a trader to evade the VAT. Straightforward greed may also tempt him. All commemtators describe the theoretical self-checking mechanism of VAT and all go on to elaborate how this does not work. Estimates of VAT evasion range from 2-4 percent of revenue forgone (the United Kingdom) to 40 percent (Italy).[2] However, there may be frustrations within the VAT administration as well.

1. Government That Works, Reforming The Public Sector. The World Bank, Bangladesh, March 1996, P.60.
2. Alan A. Tait Value Added Tax, International practices and problems, IMF, washington, D.C. 1988, p. 304

In Bangladesh the main problems experienced by VAT administration is the resistance from the taxpayers to keep the prescribed VAT records. Every representative group of taxpayers under VAT complains that record keeping is time consuming and increases cost and hence almost every representative group prefers payment of a "lump sum" at the end of tax period instead of paying at the standard rate. Even fixation of narrow base for valuation is preferred to compromise with the credit mechanism. Enforcement is mainly dependent on 'consent' of the taxpayers and hence a number of deviations or distortions are allowed to perpetuate. Again, these 'distortions' or 'deviations' can be attributed to local peculiarities of the overall tax culture that exists in Bangladesh. On the other hand, the taxpayers allege that they can not pay the exact amount of 'tax due' due to the complicated and non-transparent tax administrative procedures that we have. In France, lumpsum tax liability of small firm with annual sales of goods and hotel services under 500,000 F, of other services 150,000 F and for the perfumes, 175,000 F, is estimated on the basis of a forfait (i.e., by mutual understanding between the firm and the administration, rather than by actual calculation of tax due on sales and tax paid on purchases).



# AUDITING

Auditing starts with examining/scrutinizing the following records :

a) Ledger and other related books of accounts and records,

b) Sales Invoices,

c) Purchase Invoices,

d) Subsidiary sales journal,

e) Subsidiary Purchase Journal,

f) General Journal,

g) Cash book,

h) Tax payment Receipts etc.

The steps followed during the audit are as follows :

i) The first step for auditor/examinar is to examine the VAT return for any defects or deficiency on the face of the return.

ii) To verify whether the taxpayer is registered under the VAT law and whether the taxpayer has valid registered VAT Invoices.

iii) Examining sales and purchase invoices and counter check the same information against sales book and purchase book.

iv) Checking the records of big suppliers for purposes of determining actual purchase for the stipulated period.

v) Checking purchase invoices, determine compliance with VAT regulations for purposes of claiming input tax credit on local purchases i.e.

- Vat registration number should be indicated on the face of the invoice.
- Purchase invoice invoiced/sold to cash are disallowed and it should be in the name of taxpayer.

vi) In checking the veracity of the amount of input tax credit claimed from importations, auditors secure the inportation papers : Import entry/ consumption entries and xerox copies of official receipts of payment.

vii) In examining sales invoices auditors likewise check the taxpayers compliance with VAT regulations. Special attention is given to deductions from output tax because of sales discounts.

viii) In certain cases access " to records " of selected clients of tax payer is secured to check for any underdeclaration in sales. A careful study of the " Cash accounts" is like wise very important in the audit process.

Any unexplained increase in cash receipts other than those coming from sales, advances, additional investment may indicate an underdeclaration of sales.

Any large cash disbursements are negative cash balance per month which the tax payer can not explain may also mean underdeclaration of sales. That's why the audit of cash account is very important.

ix) Bank statements are consulted as additional guides specially for checking the accuracy of input and output tax calculations.

x) Whether exempt and zero rated goods are properly recorded are also verified.

***Audit Management Activities***

Some would classify audits as (1) examinations, that is, the administrative check of returns at the district office; (2) verifications, which basically are field audits; and (3) in-depth audits, usually where a suspicion of fraud exists.

Audit management activities, which management should design, organize, monitor, evaluate, adopt, correct, and approve, include the following:

- Search for unregistered taxpayers.
- Indentifying the information needed by the taxpayers about VAT.
- Establishment of criteria to select audit cases.
- Selection of cases.
- Collection of information about trader practices.
- Preparation of VAT audits.
- Performance of office and field audits.
- Reporting on audits.
- Discussion and decisions about the outcome of audits.
- Processing of results for use in other audits and for management decision making.
- The quantity and quality of audit work.
- Training needs for audit.
- Staffing requirements.



## TAXPAYER TREATMENT AND ESTIMATION OF VAT POTENTIAL.

***Variations in treatment of different taxpayers is necessary***

In most countries, a relatively small group of taxpayers accounts for a substantial proportion of tax revenue (generally, 5 percent of taxpayers account for 75 percent or more of the revenue); this has prompted some countries, including the United States, to establish special systems and organizational units to monitor the largest taxpayers. There is increasingly widespread recognition of the idea that taxpayers should be treated differently with regard to collection and audit procedures, depending on their size. Many countries now monitor more closely the largest taxpayers, usually the top 10 percent of taxpayers. However, if none of the remaining 90 percent is monitored the tax administration will never be truly effective. In 1995-96 about 76% of domestic VAT was collected in the manufacturing sector from there items, viz., cigarette, biri and gas. Similarly in the service sector telephone, C&F agents, insurance, cinema and construction contributed 86% of the total collection from service sector in the same year.

It may be worth while to mention here that historically the trend of taxpayers composition even in land revenue in Bengal at the time of the decential settlement (1790) was of similar nature. The following table shows that only twelve zaminders paid 53.11% of the total land revenue of Bangal at that time:

**Table**
**Twelve Great Zamindars of Bengal**[1]

| Sl. No. | Names of the Zaminders | Decimal Jama (in thousand) | As Percentage to total land Revenue of Bangal |
|---|---|---|---|
| 01. | Burdwan Raj | 32,66 | 17.15 |
| 02. | Rajshahi Raj | 22,50 | 11.81 |
| 03. | Dinajpur Raj | 14,84 | 07.79 |
| 04. | Nadia Raj | 08,54 | 04.48 |
| 05. | Birbhum Raj | 06,30 | 03.31 |
| 06. | Bishuapur Raj | 04,00 | 02.10 |
| 07. | Eusufpur (Jessore) | 03,03 | 01.59 |
| 08. | Rajnagar (Dacca) | 03,00 | 01.57 |
| 09. | Lashkarpur (Rajshahi) | 01,89 | 00.99 |
| 10. | Idrikpur (Rangpur) | 01,60 | 00.84 |
| 11. | Roushnabod (Comilla) | 01,54 | 00.84 |
| 12. | Jahangirpur (Dinajpur) | 01,23 | 00.64 |
| | Total : Sicca Rs. | 10,113 | 53.11 |

(Total Government revenue demand on Bengal in 1790 was Sicca Rs. 1,90,40,000).

1. Sirajul Islam, The Permanent Settlement in Bangal, A study of its operation 1790-1819. Bangla Academy, Dhaka, 1979. (pp. 3-4).



Immediately below the great Zaminders were middle group of Zaminders whose annual gross incomes ranged from 20,000 to one lakh rupees. Next to this group were petty Zamindars and Chowdhuries, whose gross income were insignificantly low compared with that of the Zamindars and middle group of Zamindars. In 1787, the annual revenue demand on Chittagong was slightly above three thousand rupees shared by about two thousands of petty Zaminders. Vast majority of them were so tiny that their annual governmen revenue, was as low as 2 or 3 rupees and some less than one rupee. In 1790, 7327 villages of Sylhet were lend by an army of twenty five thousands of chowdhuries. Their combined dues to Government amounted to only four lakhs of rupees per annum. Though the above picture portrays a land revenue structure of more than two hundred years old, it has not lost its relevance when we relate the frame with the number of taxpayers in relation to the total amount of tax paid in any tax system.

Monitoring the large taxpayers will provide information that can be used to monitor small and medium size taxpayers. In addition to increasing revenue in the short term, In Uruguay, for example, some of the large taxpayers engaged in certain activities were added to provide details on their purchases; the supplier's records were then checked to see if they reported the sales. Similarly, to monitor the construction material (lumber) sales of wholesale vendors, large taxpayers engaged in the production of construction materials were asked to report their sales. In this case, the goal was to determine whether the purchases made by the (lumber)dealers were inconsistent with their reported sales. Both programs were facilitated by current information of economic activity and on large taxpayers purchases and sales available in the computer data base.

In Argentina, the monitoring of the large taxpayers played a significant role in increase in tax revenue. This began with a pilot system that monitored the 800 largest taxpayers. This system is now used throughout the country, and is capable of monitoring about 100,000 taxpayers.

### *Organizational Change*

The introduction of new technology will also have impact on the organizational structure of tax administrations. Organizations will be increasingly driven by data. Managers will have to help redesign the tax administrations, not just maintain the status quo. Managers should ask, how can the organization be stimulated to accept change? What will be the repercussions of changes in work methods? For example, what will be the impact on internal auditing of the elimination of paper as the data medium?

As regards organization, there are three foreseeable future trends : operational decentralization, the integration of functions, and administrative autonomy[1]. With the introduction of computer technology, many tax administrations were reorganized in the 1960s along functional lines. Typically, administrations were organized around *collection, auditing, appeals*, and *computing systems*. This specialization increased productivity. Again based on the concept that the taxpayer is a single entity and that the administration must therefore focus on the taxpayer. This requires that the collection, *auditiong*, and appeals functions be integrated. The taxpayer should be able to resolve all related issues at a single office. National Board of Revenue's General orders No. 16 dt. 19/9/95 and 17 dt. 26/10/96 issued from the VAT wing aim at this direction of change.

1. Jenkins, Glenn. Modernization of Tax Administrations : Revenue Boards and Privatization As Instruments For Change (Cambridge :Harvard Institute for International Development, April, 1993).



***Revenue productivity ratio***

A simple method for estimation compliance is to calculate the amount of VAT revenue collected as a proportion of gross domestic product (GDP) per point of the VAT rate. This ratio is commonly referred to as the revenue productivity ratio. According to this measure, high revenue productivity ratios are associated with high levels of compliance. Mathematically, the revenue productivity ratio is defined as follows:

RP= (VAT/GDP)/t

Here:
RP = Revenue productivity ratio
VAT = VAT revenue collected
GDP = Gross domestic product
t = Average VAT rate (weighted)

The main advantage to using this measure of compliance is that all of the components of the calculation are based on actual or observable data; no estimation is required. Because the data requirements for the revenue productivity ratio are mossiest and easily satisfied, the calculation can be made with a minimum of effort.

***ESTIMATING VAT BASE***

The idea to estimate potential VAT base in relation to the size of GDP emerged from a discussion with IMF supervision mission in Bangladesh in 1994. The main points were(can the following factors, i.e. (a) the size of the economy in terms of GDP, (b) the size of the formal economy, (c) the rate of the VAT, (d) the level or quantum of value addition in the economy, and (e) other factors cast any limitation on the volume of VAT collection? Is there any correlation amongst all these factors influencing the volume of VAT? Is it possible to overcome any constraint placed by any (or all) of these factors through administrative measures e.g. improvement in VAT administration by changing techniques of present administration of through introduction of technological elements like computerization. The author's search for a satisfactory answer to these basic questions and all efforts to this end resulted in the following.

The widest VAT base is all purchasable goods in the economy, that is, GDP plus imports minus exports. Thus the starting point is the national accounts. However, the estimate can be made either from the expenditure side or from the supply/production side. The expenditure side method could be summarized as follows. To total domestic expenditure (including imports), add net private expenditure from abroad, subtract nontaxed expenditure (typically, government expenditure on wages and salaries, fixed capital formation except private expenditure on new houses and change in inventories), to obtain taxable expenditure. Adjust for taxes on expenditure, to obtain adjusted taxable expenditure. Further, subtract exempted expenditures (typically, the financial sector, nonproft and social organizations, small businesses below a legally defined threshold, and gross rents paid) but add back taxable inputs and capital purchases of exempt sectors, to obtain the potential VAT base.

The VAT base calculation from the production side is quite similar, except that zero-rated exports have to be subtracted and imports added. In the expenditure side method, exports are already excluded from the domestic expenditure base. It is more convenient to use the production side method whenever the VAT contains many exemptions by economic sectors rather than by products for final sumption. Sectoral data are more amenable to production side estimates, while exemptions specified for particular products would be more amenable to expenditure side estimates. Further, given the nature of the VAT, that is, collection based on stages of production, sectoral data are again more amenable to base calculations.

Using the above mentioned methodologies, and IMF study has made some interesting inferences regarding the relationship between the VAT rate and the ratio of VAT revenue to GDP. For example, the concept of 'revenue productivity ratio means the amount of revenue raised per point of the VAT rate.' A country whose ratio approaches 0.5 percent could be said to be performing at a high VAT effort.

***Compliance coefficient***

Another measure of compliance is the compliance coefficient which is defined as the ratio of actual VAT revenue to potential VAT revenue. The compliance coefficient can be cumbersome to calculate because it requires making an estimation of potential revenue. Despite this limitation, the compliance coefficient will serve as the basis for the study because it accurately represents the definition of compliance discussed at the begining of this section. Mathematically, the



compliance coefficient is defined as follows:

cc = VAT/(txPB)

where,

cc = Compliance coefficient
VAT = VAT revenue collected
t = Average VAT rate (weighted)
PB = Potential VAT base

The key to making the compliance coefficient operational centers on estimating potential revenue which can be expressed as the product of the average VAT rate and the potential VAT base. The calculation of the average VAT tax rate is straightforward and only requires data on the amount of VAT revenue collected from each VAT rate.

***Number of rates.***

The relationship between the number of VAT tax rates and taxpayer compliance has been discussed in various studies. As Tait points out, the amount of information required to administer a VAT increases geometrically with the number of tax rates[1]. Multiple-rate VATs complicate compliance because firms are required to account separately for each different rate category when filling out tax returns[2].

***Potential base***

Exemptions reduce the size of the potential tax base. In doing so, exemptions have been observed to both increase the cost of compliance and provide additional opportunities for evasion. Exemptions increase compliance costs by complicating the record keeping required to complete the tax return. As in the case of multiple-rate VATs, exemptions provide an avenue for evasion by opening the door to intentional misclassification of goods by taxpayers.

1. Tait. Alan, Value Added Tax, International Practice and Problems, (Washington, D.C. IMF, 1988)
2. Choi, Kwang. 'Value Added Taxation: Experiences and Lessons of Korea,' In R.Bird and O. Oldman, Taxation in Developing countries, Fourth Edition, (Baltimore, MD. John Hopkins University Press, 1992)

### *Other factors*

A second broad group of variables relate to the structure of production (as measured by the agriculture to GDP and imports to GDP ratios) and the level of economic development (as measured by per capita income, literacy rates, and degree of urbanization). Compliance can be affected by the economy's structure of production because as the formal sector expands taxation tends to be increasingly determined by a more readily measurable and verifiable tax base, thereby reducing opportunities for non-compliance. The level of economic development can also be expected to influence compliance to the extent that tax administrations operating in wealthier countries have access to more advanced technological resources and more skilled staff to identify and control non-compliance.





### *Using the revenue productivity ratio to estimate VAT revenue*

In the Table VAT Data series the revenue productivity ratio is calculated for 20 countries which are separated into four groups based on each country's level of compliance and the size of its potential VAT base. An average revenue productivity ratio is then calculated for each group. These group averages can be used as a basis for predicting revenue by countries planning to introduce a VAT. For example, Table hereunder shows that a country planning to implement a 10 percent VAT, with a potential base of over 55 percent of GDP and anticipated compliance rate of under 70 percent, can expect to raise approximately 4 percent of GDP in tax revenue.

***VAT Revenue Productivity Averages (as a percent of GDP)***

| Compliance Coefficient | | |
|---|---|---|
| Potential VAT Base (as a percent of GDP) | Over 70 percent | Under 70 percent |
| Over 55 Percent | 0.58 | 0.40 |
| Under 55 Percent | 0.34 | 0.26 |

An attractive feature of the abovenoted table is that it concisely conveys a great deal of information on compliance, the potential base, and the level of the average rate which can be used to estimate VAT revenue.

**First,** the main lesson to emerge from this study is that a well-designed VAT is not always sufficient condition to ensure compliance. Many countries in the sample exhibited low levels of compliance even though they maintained VAT features that are administratively 'desirable' (i.e. a single, low VAT rate applied to a broad potential base). At the same time, many countries in the sample were able to achieve high levels of compliance despite possessing VAT features that complicate administration (i.e. multiple rates, high average rate, and narrow base). The latter set of countries hold out the prospect that good tax administration can overcome the constraints imposed by policy and vice versa.

**Second,** the study suggests that the structure of production and the level of economic development contribute significantly to the level of compliance. These results validate the assumption that shifts in the structure of production toward more easily measurable economic sectors leads to improvements in compliance. The results also confirm the notion that as countries increase in wealth they are able to achieve higher levels of compliance. This may occur because wealthier countries possess more sophisticated technology and skilled tax administration staff. It may also occur because increase in income are associated with other factors that promote compliance such as higher levels of literacy and urbanization.

**Third,** the variables included in the study accounted in the study accounted for less then half of the variance in the level of compliance. Other factors, excluded from the study, clearly play an important role in determining compliance. Tanzi and Shome summarize many potentially significant variables, such as attitudes and social ethics the structure of the business sector, the cost of compliance, and the effectiveness of the tax administration[1]. Although these factors are diffcult to measure, it is important nevertheless to recognize that compliance is affected by many varied and complex factors. This last point suggests that in designing strategies to improve compliance, policy makers should avoid blanket prescriptions and quick fix solutions. Instead, priority should be given to developing policies that are tailored to specific conditions facing each country.

1. Tanzi, Vito and Parthasarathi Shome, "A primer on Tax Evasion", WP/9321 (Washington, D.C. IMF, 1993).



***Summary of the Methodology to calculate VAT Compliance.***

Sales
+ gross production
+ imports
=Total supply
- exemptions
- exports
- change in inventories
= Taxables sales (1)

Purchases
+ total purchases (intermediate consumption)
- purchases of exempt inputs
- purchases of taxable inputs for production of exempt goods and services
= Net purchases (2)

Investments
+ total investments
- exempt investments
- taxable investments fot the production of exempt goods and services
= Net investments (3)

Potential taxables base (includes actual VAT revenue = (1) -(2) - (3) (4)

Actual VAT revenue (5)

Potential taxables base (net of VAT)= (4) - (5) (6)

Potential revenue = Average VAT rate x (6) (7)

Compliance Coefficient = (5) / (7)

## VAT Data Series

| Country | Year | Compliance Coefficient 1/ | Revenue Productivity | VAT Revenue GDP ratio | Number of VAT rates | Average VAT rate | Potential Base GDP ratio | Per Capital Income (US $) | Agriculture GDP ratio | Import GDP ratio | Year VAT |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Argentina | 1992 | - | 0.33 | 5.9 | 1 | 18.0 | 47.6 | 2790 | 15 | 8.0 | 17 |
| Bolivia | 1990 | - | 0.28 | 3.1 | 1 | 11.1 | 49.9 | 650 | 21 | 12.6 | 17 |
| Canada | 1991 | - | 0.32 | 2.2 | 1 | 7.0 | 41.3 | 20440 | 3 | 25.4 | 1.5 |
| Chile | 1991 | - | 0.49 | 8.8 | 1 | 18.0 | 59.8 | 2160 | 8 | 30.5 | 16 |
| Colombia | 1991 | - | 0.19 | 2.4 | 5 | 12.2 | 30.4 | 1260 | 17 | 15.2 | 16 |
| Ecuador | 1991 | - | 0.31 | 3.1 | 1 | 10.0 | 50.9 | 1000 | 15 | 24.9 | 21 |
| Guatemala | 1992 | - | 0.36 | 2.5 | 1 | 7.0 | 76.2 | 930 | 26 | 21.7 | 9 |
| Honduras | 1992 | - | 0.42 | 3.1 | 2 | 7.3 | 65.2 | 580 | 22 | 35.4 | 16 |
| Hungary | 1991 | - | 0.44 | 6.1 | 2 | 14.0 | 68.5 | 2720 | 10 | 33.4 | 3 |
| Israel | 1992 | - | 0.54 | 9.7 | 1 | 18.0 | 58.4 | 11950 | 3 | 46.0 | 17 |
| Mexico | 1992 | - | 0.30 | 3.0 | 1 | 10.0 | 48.3 | 3030 | 9 | 17.0 | 12 |
| New Zealand | 1992/93 | - | 0.67 | 8.4 | 1 | 12.5 | 70.7 | 12350 | 9 | 27.5 | 6.5 |
| Panama | 1991 | - | 0.36 | 1.8 | 1 | 5.0 | 76.4 | 2130 | 10 | 98.8 | 14 |
| Peru | 1992 | - | 0.17 | 3.1 | 1 | 18.0 | 53.3 | 1070 | 13 | 12.7 | 16 |
| Philippines | 1992 | - | 0.24 | 2.4 | 1 | 10.0 | 40.4 | 730 | 21 | 31.9 | 4 |
| Portugal | 1991 | - | 0.71 | 6.4 | 3 | 9.0 | 82.3 | 5930 | 9 | 45.0 | 5 |
| South Africa | 1992/93 | - | 0.52 | 5.2 | 1 | 10.0 | 61.3 | 2560 | 5 | 19.8 | 1.5 |
| Spain | 1989 | - | 0.52 | 5.4 | 4 | 10.5 | 69.6 | 12450 | 6 | 21.2 | 3 |
| Sweden | 1992 | - | 0.35 | 8.0 | 2 | 23.2 | 36.5 | 25110 | 3 | 27.0 | 23 |
| Uruguay | 1991 | - | 0.34 | 7.4 | 2 | 21.6 | 49.0 | 2840 | 10 | 20.1 | 23 |
| Average | | 69.2 | 0.4 | 4.9 | 1.7 | 12.6 | 56.8 | 5634 | 11.8 | 29.1 | 12.1 |
| Bangladesh | 1993-94 | 52 | 0.27 | 3.99 | 1 | 15 | 49.6 | 220 | 37 | 11.4 | 3 |

Notes: 1/Data omitted to preserve confidentiality.

Source: Carlos Silvani, Unpublished Memorandum, Fiscal Affairs Department, IMF, September, 1992. Data on Bangladesh was calculated by Dr. Rafiqul Islam, First Secretary (VAT), National Board of Revenue, Govt. of Bangladesh.



# Brief Description for

# Currently available 19 Reports

# from

# "VSTAT"

## ( VAT- STATISTICS )

Currently VSTAT is able to generate 19 different reports. All reports are classified into three (3) categories:

A. Standalone Report --- 4 reports

B. Comparative --- 9 reports

C. Six Commissionerate Report --- 6 reports

### A. *Standalone Report :*

1. Standalone ***Total*** Report :

a) For ***Unique*** Commissionerate :

It provides statements of collection of taxes for a unique commissionerate for an specific period (e.g. 1 month, 2 months, 3 months, 4 months etc.) agains each item (e.g Biri, Cigarette, ---etc.) classifying them into taxpayer categories (e.g. Excise, VAT Production, VAT Service, .... etc.). It also provides group summary agains each taxpayer category. Finally it produces a summary report from which one can easily get collection figures of TOTAL VAT, TOTAL SD, TOTAL ED, TOTAL TT etc. On the other hand it provides figures for TOTAL COLLECTION from excisable items. TOTAL COLLECTION from Production. TOTAL COLLECTION from Serviceable items etc.

b) For *all* Commissionerate :

It provides statements of collection of taxes for all commissionerates for an specific period (e.g. 1 month, 2 months, 3 months, 4 months etc.) against each item (e.g. Biri, Cigarette, ----- etc.) classifying them into taxpayer categories (e.g. Excise, VAT Production, VAT Service, --- etc.). It also provides group summary against each taxpayer category. Finally it produce a summary report from which one can easily get collection figures of TOTAL VAT, TOTAL SD, TOTAL ED, TOTAL TT etc. On the other hand it provides figures for TOTAL COLLECTION from esciseable items. TOTAL COLLECTION from Production, TOTAL COLLECTION from Serviceable items etc.

2. Standalone **Monthly** Report:

a) For ***Unique*** Commissionerate :

It provides statements of collection of taxes for a unique commissionerate for a fiscal year of collection for any consecutive 12 months, against each item (e.g. Biri, Cigarette, ---- etc.) classifying them into taxpayer categories (e.g. Excise, VAT Production, VAT Service, ---- etc). This Report shows sum of first six months collection and that for second six months and 12 months total. By using this report 12 months collection can be inspected at a glance. It also provides group summary against each taxpayer category. Finally it produces summary report from which one can easily get collection figures of TOTAL VAT, TOTAL SD, TOTAL ED, TOTAL TT etc. On the other hand it provides figures for TOTAL COLLECTION from exciseable items, TOTAL COLLECTION from Production, TOTAL COLLECTION from Service items etc.

***B. Comparative Report :***

This report provides a comparative statement of collections against each item for two separate periods. For example one can compare collection of each item for Jan. 96-Mar. 96 with the collection of the same items for the period Jan. 95- Mar. 95. It is also possible to comapre collection of Jan. 96-Mar. 96 with that for Jul. 96-Sep. 96 (i.e. comparison between different quarters of the year or with different quarters of a different year. It also provides group summary against each taxpayer category for two periods, shows the absolute increase/decrease, percentage increase/decrease etc. Fianlly it produces a summary report from which one can easily get



collection figures of TOTAL VAT, TOTAL SD, TOTAL ED, TOTAL TT etc. for two periods and their increment/decrements etc.. On the other hand it provides figures for TOTAL COLLECTION from exciseable items, TOTAL COLLECTION from Production, TOTAL COLLECTION from Serviceable items etc. for two periods.

A total of 9 (nine) reports can be generated by adopting following combinations :

1. Comparison Between collection of unique commissionerate for two periods for–

   a) All Items
   b) Increasing Items
   c) Decreasing Items.

2. Comparison Between collection of two different commissionerates for two periods for–

   a) All Items
   b) Increasing Items
   c) Decreasing Items.

3. Comparison Between collection of all commissionerates for two periods for–

   a) All Items
   b) Increasing Items
   c) Decreasing Items.

***C. Six Commissionerate Report :***

This report provides collection reports of each item for a certain period (say Jan. 96-Mar. 96) for each commissionerate at a glance. Each commissionerate's figure is represented as a separate column. It also provides collection of that item for the same period of the previous year for each commissionerate also. The report contains sum of all commissionerate's figure for current period as well as for previous period. It also provides a comparison (increase/decrease) both in items of absolute value and percentage figure.

A total of 6 (six) reports can be generated by adopting following combinations :

1. Comparison Between collection of all comm. for two similar periods between two years for:

   a) All Items
   b) Increasing Items
   c) Decreasing Items.

2. Comparison Between collection of all comm. for two dissimilar periods between two years for:

   a) All Items
   b) Increasing Items
   c) Decreasing Items.

***Future development :***

All reports mentioned above are generated and used at NBR. All these reports provide statements in terms of the Commissionerate DATA. Each commissionerate may similarly need such 19 another report in terms of their divisional data. Each Division in turn may similarly need such 19 another report in terms of their circle data. Thus each organization will get statistical analysis for data generated from its lower level office. Thus in future VSTAT will be used in all Commissionerates, all Divisions as well as all Circles. Each office will use its own portion of the software and get its own set of reports. In future there will be not only compilation of statistical data for revenue collection, but also reports of evasion detection, penal actions, arrear collections, etc. to show the drive and activity of the Circles, Divisions and Commissionerates. It is also felt that the statistical revenue reports will be generated separately on the basis of H.S Code to compare data of customs & VAT. There is also a plan to generate statistical reports on the basis of VAT Registration number to show each VAT units performance over time. VAT data will also become interchangeable with Taxes Department by unifying VAT No. and TIN.



## Excise & Vat Registered Units and Revenue Collection

| | | | | | | | Collection (CR. Tk.) |
|---|---|---|---|---|---|---|---|
| Sl. No. | Description (Goods) | Number of Units Jan '96 | Collection FY: 91-92 | Collection FY: 92-93 | Colelction FY: 93-94 | Collection FY: 94-95 | Collection FY: 95-96 |
| 1 | Biri | 529 | 88.00 | 93.00 | 94.00 | 108.00 | 110.00 |
| 2 | Fabrics & Yarn (all sorts) | 341 | 0.07 | 14.00 | 13.00 | 13.00 | 13.00 |
| 3 | Cotton Yarn | 194 | -- | -- | -- | 8.00 | 9.00 |
| 4 | Cotton Fabrics | 149 | -- | -- | -- | 5.00 | 3.00 |
| 5 | Fabrics of M.M. Fibre | 97 | -- | -- | -- | 0.71 | 1.00 |
| 6 | Service by Bank | 32 | 43.00 | 45.00 | 49.00 | 56.00 | 58.00 |
| 7 | Miscellaneous | 7 | 3.00 | 7.00 | 1.00 | 1.00 | 0.96 |
| 8 | Cigarettes | 14 | 651.00 | 158.00 | 154.00 | 176.00 | 204.00 |
| 9 | Filter Rod | 4 | 0.15 | 0.41 | 0.36 | 0.04 | 0.65 |
| 10 | Petro. Gas & Other Gases | 8 | 531.00 | 290.00 | 150.00 | 184.00 | 185.00 |
| 11 | POL Products | 17 | 77.00 | 58.00 | 61.00 | 57.00 | 40.00 |
| 12 | Sugar | 16 | 57.00 | 57.00 | 52.00 | 49.00 | 70.00 |
| 13 | Jute & Jute Manufactures | 95 | 19.00 | 13.00 | 14.00 | 17.00 | 16.00 |
| 14 | Cement | 10 | 6.00 | 6.00 | 6.00 | 9.00 | 11.00 |
| 15 | paper all sorts | 50 | 25.00 | 22.00 | 27.00 | 19.00 | 19.00 |
| 16 | Paper Board all sorts | 13 | 3.00 | -- | -- | 5.00 | 4.00 |
| 17 | Medicine all sorts | 129 | 46.00 | 53.00 | 76.00 | 89.00 | 89.00 |
| 18 | M.S. Product | 191 | 20.00 | 12.00 | 21.00 | 28.00 | 20.00 |
| 19 | Steel/G.I. Pipe | 14 | 2.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 20 | P.V.C. Pipe | 56 | 0.14 | -- | 1.00 | 0.74 | 2.00 |

| Sl. No. | Description (Goods) | Number of Units Jan '96 | Collection FY: 91-92 | Collection FY: 92-93 | Colelction FY: 93-94 | Collection FY: 94-95 | Collection FY: 95-96 |
|---|---|---|---|---|---|---|---|
| 21 | Wireless Receiving Sets | 634 | 5.00 | 5.00 | 6.00 | 5.00 | 6.00 |
| 22 | Glass & Glassware | 25 | 4.00 | 5.00 | 4.00 | 5.00 | 5.00 |
| 23 | Soap | 104 | 16.00 | 32.00 | 19.00 | 19.00 | 20.00 |
| 24 | Detergents | 5 | -- | -- | -- | 1.00 | 1.00 |
| 25 | Electric Battery | 27 | 7.00 | 4.00 | 7.00 | 8.00 | 9.00 |
| 26 | Biscuits | 79 | 5.00 | 6.00 | 7.00 | 7.00 | 7.00 |
| 27 | Beverage | 10 | 5.00 | 5.00 | 8.00 | 7.00 | 8.00 |
| 28 | Purified Water | 13 | 0.29 | 0.13 | 0.03 | 0.13 | 0.17 |
| 29. | Vegetable Oil | 61 | 20.00 | 19.00 | 22.00 | 18.00 | 14.00 |
| 30 | Coconut Oil | 29 | 3.00 | 0.87 | 2.00 | 2.00 | 3.00 |
| 31 | Paints & Varnishes | 47 | 3.00 | 4.00 | 4.00 | 3.00 | 5.00 |
| 32 | Cosmetics Products | 25 | 9.00 | 4.00 | 7.00 | 10.00 | 9.00 |
| 33 | Mechanically Propelled Vehicles | 24 | 7.00 | 4.00 | 4.00 | 12.00 | 10.00 |
| 34 | Ceramic Products | 15 | 3.00 | 4.00 | 4.00 | 4.00 | 3.00 |
| 35 | Matches | 20 | 6.00 | 7.00 | 6.00 | 6.00 | 6.00 |
| 36 | Plastic Container | 25 | 0.91 | 1.00 | 0.67 | 0.69 | 1.00 |
| 37 | Metal Container | 18 | 2.00 | 2.00 | 2.00 | 3.00 | 2.00 |
| 38 | Plastic Product | 113 | 3.00 | 4.00 | 2.00 | 2.00 | 2.00 |
| 39 | Packaging Materials | 205 | 5.00 | 4.00 | 8.00 | 8.00 | 12.00 |
| 40 | Electric Bulbs all Sorts | 13 | 2.00 | 2.00 | 2.00 | 2.00 | 2.00 |
| 41 | Electric Tubes | 6 | 1.00 | 1.00 | 0.90 | 1.00 | 1.00 |
| 42 | Electrical Goods | 87 | 2.00 | 1.00 | 2.00 | 3.00 | 1.00 |



| Sl. No. | Description (Goods) | Number of Units Jan '96 | Collection FY: 91-92 | Collection FY: 92-93 | Colelction FY: 93-94 | Collection FY: 94-95 | Collection FY: 95-96 |
|---|---|---|---|---|---|---|---|
| 43 | Electric Fans | 67 | 1.00 | 1.00 | 2.00 | 2.00 | 2.00 |
| 44 | Wires & Cables | 23 | 1.00 | 3.00 | 5.00 | 6.00 | 4.00 |
| 45 | Oxygen/Carbon Dioxide | 10 | 2.00 | 4.00 | 4.00 | 5.00 | 5.00 |
| 46 | Antiseptics | 3 | 5.00 | 1.00 | 0.00 | 0.00 | 0.15 |
| 47 | Sodium Silicate | 21 | 0.82 | 0.61 | 0.71 | 0.93 | 1.00 |
| 48 | Glycerine | 1 | 0.65 | 0.01 | 0.94 | 1.00 | 1.00 |
| 49 | Plastic Bag | 98 | 1.00 | 0.95 | 2.00 | 2.00 | 2.00 |
| 50 | Rubber Products | 37 | 0.43 | 0.33 | 0.60 | 0.59 | 0.49 |
| 51 | Tyres & Tubes | 9 | 0.17 | 0.37 | 0.38 | 0.41 | 0.38 |
| 52 | Insulation Board | 4 | 0.11 | 0.21 | 0.63 | 0.51 | 0.31 |
| 53 | Nut, Bolt & Screw | 31 | 0.04 | 0.17 | 2.00 | 1.00 | 0.59 |
| 54 | Sanitary Ware | 6 | 3.00 | 2.00 | 7.00 | 4.00 | 5.00 |
| 55 | Aluminium Fittings | 11 | 0.44 | 0.23 | 0.33 | 0.42 | 0.41 |
| 56 | Foot Ware | 86 | 6.00 | 4.00 | 5.00 | 6.00 | 7.00 |
| 57 | Chemicals | 69 | 1.00 | 3.00 | 4.00 | 4.00 | 4.00 |
| 58 | Fruit Juice | 4 | 0.00 | 0.00 | 0.00 | 0.12 | 0.24 |
| 59 | Jam, Jelly | 5 | 0.00 | 0.00 | 0.00 | 0.02 | 0.03 |
| 60 | Other Food Products | 20 | 2.00 | 2.00 | 0.68 | 0.88 | 1.00 |
| 61 | Leather Products | 258 | 0.96 | 0.71 | 0.91 | 1.00 | 1.00 |
| 62 | Tea | 59 | 11.00 | 14.00 | 14.00 | 14.00 | 19.00 |
| 63 | Ceramic Bricks | 572 | -- | -- | -- | 1.00 | 1.00 |
| 64 | Non Ceramic Bricks | 2974 | 2.00 | 5.00 | 9.00 | 12.00 | 8.00 |
| 65 | Dextrose | 2 | 0.24 | 0.10 | 0.21 | 0.41 | 0.14 |

| Sl. No. | Description (Goods) | Number of Units Jan '96 | Collection FY: 91-92 | Collection FY: 92-93 | Colelction FY: 93-94 | Collection FY: 94-95 | Collection FY: 95-96 |
|---|---|---|---|---|---|---|---|
| 66 | Welding Electrods | 4 | 2.00 | 0.08 | 0.17 | 0.26 | 0.23 |
| 67 | Milk | 12 | 0.55 | 0.53 | 5.00 | 6.00 | 6.00 |
| 68 | Ice Cream | 6 | 0.00 | 0.00 | 0.00 | 0.53 | 0.65 |
| 69 | Other Milk Products | 3 | 0.00 | 0.00 | 0.00 | 0.30 | 1.00 |
| 70 | Asbestos | 1 | 0.82 | 0.00 | 0.56 | 0.87 | 1.00 |
| 71 | C.I. Sheet | 15 | 0.00 | 5.00 | 5.00 | 7.00 | 13.00 |
| 72 | G.P. Sheet | 13 | 0.00 | 0.00 | 8.00 | 7.00 | 4.00 |
| 73 | Carpet | 5 | 0.00 | 0.31 | 0.23 | 0.43 | 0.55 |
| 74 | Spare Parts all sorts | 22 | 0.43 | 1.00 | 3.00 | 2.00 | 2.00 |
| 75 | Stainless Steel | 8 | 0.41 | 0.36 | 0.06 | 0.11 | 0.10 |
| 76 | Steel Furniture | 286 | 0.35 | 0.25 | 0.28 | 0.35 | 0.32 |
| 77 | Wood & Articals of Wood | 263 | 1.00 | 2.00 | 1.00 | 2.00 | 2.00 |
| 78 | Wooden Furniture | 273 | 0.23 | 0.62 | 0.86 | 1.00 | 0.87 |
| 79 | Hard Board | 2 | 0.98 | 0.00 | 1.00 | 1.00 | 1.00 |
| 80 | Marble Stone | 46 | 0.16 | 0.10 | 0.16 | 0.26 | 0.19 |
| 81 | Melamine | 4 | 0.10 | 0.09 | 0.15 | 0.15 | 0.33 |
| 82 | Lever Spring | 3 | 0.13 | 0.13 | 0.13 | 0.23 | 2.00 |
| 83 | Telecommunication Equipments | 1 | 0.00 | 0.31 | 2.00 | 3.00 | 1.00 |
| 84 | Molasses | 2 | 0.06 | 0.33 | 0.58 | 0.99 | 1.00 |
| 85 | Aluminium Products | 4 | -- | 0.02 | 0.22 | 0.25 | 0.26 |
| 86 | Fishing Nets | 29 | 0.09 | 0.02 | 0.27 | 0.36 | 0.48 |
| 87 | Nylon Cord | 3 | 0.06 | 0.04 | 0.07 | 0.12 | 0.14 |
| 88 | China Clay | 1 | 0.02 | 0.02 | 0.02 | -- | -- |



| Sl. No. | Description (Goods) | Number of Units Jan '96 | Collection FY: 91-92 | Collection FY: 92-93 | Colelction FY: 93-94 | Collection FY: 94-95 | Collection FY: 95-96 |
|---|---|---|---|---|---|---|---|
| 89 | Scrap Vessels | 21 | 0.60 | 0.00 | 0.02 | 0.36 | 0.30 |
| 90 | Iron & Iron Products | 17 | 0.01 | 0.21 | 0.34 | 0.22 | 0.34 |
| 91 | G.I. Ware | 13 | 0.00 | 0.00 | 0.27 | 0.42 | 0.46 |
| 92 | Steel Ingot | 17 | 0.22 | 0.16 | 0.34 | 0.63 | 0.70 |
| 93 | Readymade Garments | 477 | 0.02 | -- | 0.05 | 0.03 | 0.14 |
| 94 | Socks | 36 | 0.01 | 0.03 | 0.07 | 0.15 | 0.13 |
| 95 | Misc. Products | 60 | 2.00 | 12.00 | 9.00 | 11.00 | 11.00 |

**VAT SERVICES**

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| 96 | Hotels | 324 | 13.00 | 13.00 | 18.00 | 16.00 | 15.00 |
| 97 | Restaurants | 299 | --- | --- | 1.00 | 2.00 | 2.00 |
| 98 | Decorators & Caterers | 18 | --- | 0.02 | 0.03 | 0.05 | 0.45 |
| 99 | Motor Garage Workshops, Dockyard | 37 | 0.49 | 0.39 | 0.79 | 1.00 | 1.00 |
| 100 | Construction Firms | 67365 | 0.00 | 3.00 | 90.00 | 181.00 | 191.00 |
| 101 | Warehouse & Storage | 5 | 0.00 | 0.00 | 0.29 | 1.00 | 2.00 |
| 102 | Advertising Agency | 74 | 0.02 | 5.00 | 7.00 | 8.00 | 8.00 |
| 103 | Printing Press & Binders | 151 | 0.28 | 0.48 | 2.00 | 2.00 | 2.00 |
| 104 | Land Development Agency | 80 | 0.00 | 0.00 | 0.71 | 1.00 | 0.88 |
| 105 | Video/Audio Cassette & Recording Shops | 9 | 0.02 | 0.07 | 0.30 | 0.07 | 0.01 |
| 106 | Telephone, Teleprinter, Telex & FAX | 13 | 54.00 | 76.00 | 64.00 | 70.00 | 72.00 |
| 107 | Laundry | 15 | 0.10 | 0.14 | 0.14 | 0.14 | 0.12 |

| Sl. No. | Description (Goods) | Number of Units Jan '96 | Collection FY: 91-92 | Collection FY: 92-93 | Colelction FY: 93-94 | Collection FY: 94-95 | Collection FY: 95-96 |
|---|---|---|---|---|---|---|---|
| 108 | Indenting Agency | 451 | 0.15 | 1.00 | 2.00 | 3.00 | 4.00 |
| 109 | FF/C&F Agency | 390 | 0.06 | --- | 3.00 | 16.00 | 23.00 |
| 110 | Community Center | 36 | 0.01 | 0.02 | 0.01 | 0.10 | 0.09 |
| 111 | Cinematographic Studio | 2 | 1.00 | 0.51 | 0.73 | 0.85 | 0.69 |
| 112 | Colour Photo Studio | 125 | 0.27 | 0.32 | 0.45 | 0.59 | 0.63 |
| 113 | Survey Organisation | 7 | 0.01 | 0.10 | 0.22 | 0.27 | 0.24 |
| 114 | Plant/Capital Machinery | 1 | 0.00 | 0.33 | 0.08 | 0.05 | 0.00 |
| 115 | Sweet Meat Shop | 325 | 0.00 | 1.00 | 2.00 | 2.00 | 2.00 |
| 116 | Cinema Hall | 813 | 2.00 | 4.00 | 5.00 | 4.00 | 4.00 |
| 117 | WASA | 2 | 5.00 | 3.00 | 11.00 | 11.00 | 11.00 |
| 118 | Gold/Silversmith | 936 | 0.35 | 0.31 | 0.67 | 0.70 | 0.59 |
| 119 | Courier Service | 42 | 0.00 | 0.19 | 0.46 | 1.00 | 2.00 |
| 120 | Insurance Service | 20 | 0.00 | 21.00 | 29.00 | 40.00 | 45.00 |
| 121 | Clinics & Hospitals | 246 | 0.00 | 0.06 | 0.35 | 0.47 | 0.50 |
| 122 | Beauty Perlour | 80 | 0.00 | 0.03 | 0.05 | 0.06 | 0.06 |
| 123 | Misc. serviceable Items | 4 | 27.00 | 0.00 | 1.00 | 1.00 | 0.64 |

**VAT at Retail Level (1996-97)**

1 Bath Tub & Jakuji (SPA)
2 Tiles
3 Air Conditioner
4 Gizzer
5 Microwave Oven
6 Compact Disk Player, Music System
7 Satellite Receiver & Dish Antena
8 Motor Car, Station Wagon, Jeep, Microbus
9 Chandelliers
10 Antics

**VAT able Services (1996-97)**

1 Consulting Firm & Supervisory Firm
2 Leasing Deeds
3 Audit & Accounting Firm
4 Shipping Agent



## Rate of Submission of Return

## For June-96

| Commissionerate | No of Total Units (3+5+7+8) | Mfg. Unit | Rate of Return of column 3 | Service Unit (Excl. Cons. firm) | Rate of Return of column 5 | Cons. firm | Importer, Exporter & EPZ |
|---|---|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
| Dhaka (South) | 31043 | 2511 | 72.16% | 2103 | 66.69% | 12808 | 13621 |
| Dhaka (North) | 16608 | 1501 | 50.16% | 901 | 57% | 11699 | 2507 |
| Chittagong | 30131 | 2543 | 57.10% | 2463 | 68% | 16803 | 8322 |
| Khulna | 18715 | * 881 | 18% | 441 | 56% | 15992 | 1401 |
| Jessore | 11091 | * 637 | 10.51% | 739 | 40% | 8461 | 1254 |
| Rajshahi | 16475 | * 558 | 25.63% | 472 | 60% | 12819 | 2626 |
| **Total** | **124,063** | **8631** | **50.77%(4382)** | **7119** | **62%(4434)** | **78582** | **29731** |

* As 85% of the manufacturing units are registered as Brick manufacturer and most of them are not operational throughout the year, so the return submission rate is low for manufacturing sector. It may be mentioned that because of seasonality of business, return submission for construction units, brickfields and 100% exporters has been made quarterly from FY 1996-97.

| | | Number | % of Return Submission |
|---|---|---|---|
| 1. | Total regd. units | 124,063 | 7.10% |
| 2. | All mfg. and service (Incl. cons) units | 94332 | 9.34% |
| 3. | All mfg. and service (Excl. cons) units | 15750 | 55.97% |
| 4. | All mfg. units | 8631 | 50.77% |
| 5. | All mfg. (Excl. bricks) units | | 63% |
| 6. | All service units | 85701 | 5.17% |
| 7. | All service units (Excl. cons. firm) | 7119 | 62% |

## Statistical Data of Registered VAT & Excise Units of Different Commissionerate (Upto May '96)

| Sl. No. | Commissionerate | Excise Unit | Manufacturing Item | Service Item (VAT) | Construction Firm (VAT) | Export/Import (VAT) | Total VAT | Grantd Total |
|---|---|---|---|---|---|---|---|---|
| 1. | Dhaka (South) | 325 | 2814 | 2854 | 5997 | 12481 | 24146 | 24471 |
| 2. | Dhaka (North) | 308 | 2589 | 866 | 11802 | 1517 | 16774 | 17082 |
| 3. | Rajshahi | 1099 | 876 | 433 | 15679 | 1291 | 18279 | 19378 |
| 4. | Chittagong | 167 | 2533 | 2435 | 16447 | 7772 | 29187 | 29354 |
| 5. | Jessore | 120 | 691 | 509 | 8363 | 1284 | 10847 | 10987 |
| 6. | Khulna | 69 | 532 | 449 | 12610 | 2593 | 16184 | 16253 |
| | **Total** | **2088** | **10035** | **7546** | **70899** | **26933** | **115417** | **117505** |

Total : Excise License : 2088
Total VAT Manufacturer : 10035
Total VAT Service (Excluding Construction Firm) : 7546
Total Construction Firms : 70899
Total Export Import : 26938

**Total Registered Unit Under Value Added Tax : 117505**



### Revenue Collection in Service Sector From 1991-96

| Sl. No. | Financial Year | Revenue Collection in service sector | % increase |
|---|---|---|---|
| 1. | 1991-92 | 117.54 | - |
| 2. | 1992-93 | 152.51 | 22.92% |
| 3. | 1993-94 | 273.72 | 44.28% |
| 4. | 1994-95 | 392.23 | 30.21% |
| 5. | 1995-96 | 413.34 | 5.1% |

### Arrear Revenue Statement of six Commissionerate

| Sl. No. | Commissionerate Name | Excise | VAT (Local) | SD (Local) | Total |
|---|---|---|---|---|---|
| 1. | Dhaka (South | 11.02 | 7.43 | 0.12 | 18.57 |
| 2. | Khulna | 0.97 | 3.19 | 0.082 | 4.25 |
| 3. | Dhaka (North) | 15.19 | 16.59 | 1.61 | 33.39 |
| 4. | Chittagong | 32.93 | 37.07 | 7.3 | 77.30 |
| 5. | Jessore | 3.3 | 0.61 | 0.03 | 3.94 |
| 6. | Rajshahi | 5.86 | 4.56 | 0.79 | 11.21 |
| | **Total** | **69.20** | **70.08** | **9.90** | **148.66** |

### Turnover Tax Collection, FY: 1995-96

(Figure in Thousand Taka)

| Sl. No. | Commissionerate Name | Target | Revenue Collection |
|---|---|---|---|
| 1. | Chittagong | 15000 | 4833 |
| 2. | Dhaka (South) | 15000 | 7515 |
| 3. | Dhaka (North) | 10000 | 2467 |
| 4. | Khulna | 3400 | 2787 |
| 5. | Jessore | 3300 | 1774 |
| 6. | Rajshahi | 3300 | 2329 |
| | **Total** | **50,000** | **21,705** |

## List of Large Tax Payers of Dhaka (North)

Revenue Collection (in crore taka)

| Sl. No. | Name of the firm | Name of the Commission-erate | Item Name | Tax type | 1992-93 | 1993-94 | 1994-95 |
|---|---|---|---|---|---|---|---|
| 1 | Bangladesh Tobacco Co. | Dhaka (N) | Cigarette | VAT & SD | 639.12 | 611.20 | 685.23 |
| 2 | Dhaka Tobacco Co. | Dhaka (N) | Cigarette | VAT & SD | 50.23 | 103.02 | 133.40 |
| 3 | Asian Tobacco | Dhaka (N) | Cigarette | VAT & SD | 8.81 | 13.51 | 18.14 |
| 4 | Baximco Pharma | Dhaka (N) | Medicine | VAT | 7.80 | 8.44 | 12.72 |
| 5 | The Acme Laboratories | Dhaka (N) | Medicine | VAT | 3.80 | 5.59 | 7.56 |



## List of Large Tax Payers of Dhaka (South)

Revenue Collection (in crore taka)

| Sl. No. | Name of the firm | Name of the Commissionerate | Item Name | Tax type | 1992-93 | 1993-94 | 1994-95 |
|---|---|---|---|---|---|---|---|
| 1 | T & T Board | Dhaka (South)_ | T & T | VAT | 65.13 | 64.47 | 70.11 |
| 2 | Janata Bank Ltd. | Dhaka (South) | Bank Service | Excise | 8.06 | 9.41 | 10.14 |
| 3 | Agrani Bank Ltd. | Dhaka (South) | Bank Service | Excise | 7.76 | 8.03 | 8.57 |
| 4 | Sonali Bank Ltd. | Dhaka (South) | Bank Service | Excise | 12.21 | 13.37 | 14.22 |
| 5 | Sadaron Bima Corporation | Dhaka (South) | Insurance | VAT | 6.57 | 8.89 | 11.93 |
| 6 | Hotel Sonargaon | Dhaka (South) | Residence Hotel | VAT & SD | 8.15 | 8.87 | 9.42 |

## List of Large Tax Payers of Chittagong

Revenue Collection (in crore taka)

| Sl. No. | Name of the firm | Name of the Commission-erate | Item Name | Tax type | 1992-93 | 1993-94 | 1994-95 |
|---|---|---|---|---|---|---|---|
| 1 | Eastern Refinery Ltd. | Chittagong | Petroleum Oil & Crufe Oil | VAT & SD | 43.0301248 | 46.0776301 | 24.8921601 upto May '96 |
| 2 | Bangladesh Gas Field Co. Ltd. | Chittagong | Natural Gas | VAT & SD | 154.0658760 | 145.4991494 | 124.8480955 upto May '96 |
| 3 | Titas Gas Field | Chittagong | Natural Gas | VAT & SD | 208.0100000 | 293.7000000 | 254.1300000 upto 15th June '96 |
| 4 | Hobigonj Gas Field | Chittagong | Natural Gas | VAT & SD | 87.1500000 | 116.4000000 | 148.4800000 upto May '96 |
| 5 | Kailash Tilla Gas Field | Chittagong | Natural Gas | VAT & SD | 19.2472000 | 32.7782000 | 37.6941000 |
| 6 | Feni Gas Field | Chittagong | Natural Gas | VAT & SD | 17.6500737 | 19.9306200 | 22.7893116 upto May '96 |
| 7 | Rashidpur Gas Field | Chittagong | Natural Gas | VAT & SD | --- | --- | 73.1000000 upto May '96 |
| 8 | Karnaphuli Paper Mills Ltd. | Chittagong | Paper | VAT & SD | 9.0500000 | 10.5000000 | 5.4000000 upto Feb '96 |
| 9 | Lever Brothers (BD.) Ltd. | Chittagong | Cosmetics | VAT & SD | 18.2000000 | 19.7200000 | 13.8500000 upto May '96 |

## List of Large Tax Payers of Jessore

| Sl. No. | Name of the firm | Name of the Commissi-onerate | Item Name | Tax type | Revenue Collection (in crore taka) 1992-93 | 1993-94 | 1994-95 |
|---|---|---|---|---|---|---|---|
| 1 | Alpha Tobacco Manufacturing Company Ltd. | Jessore | Cigarette | VAT | 22.26 | 41.36 | 44.55 |
| 2 | Akiz Biri Factory Bheramara, Kustia | Jessore | Biri | Excise | 8.30 | 11.79 | 9.67 |
| 3 | Nasir Biri Factory Bheramara, Kustia | Jessore | Biri | Excise | 6.46 | 8.01 | 7.44 |

## List of Large Tax Payers of Khulna

| Sl. No. | Name of the firm | Name of the Commissionerate | Item Name | Tax type | Revenue Collection (in crore taka) 1992-93 | 1993-94 | 1994-95 |
|---|---|---|---|---|---|---|---|
| 1 | Opsonin Chemical | Khulna | Medicine | VAT | | | 8.00 |
| 2 | Karikor Biri | Khulna | Biri | Excise | | | 7.8973125 |

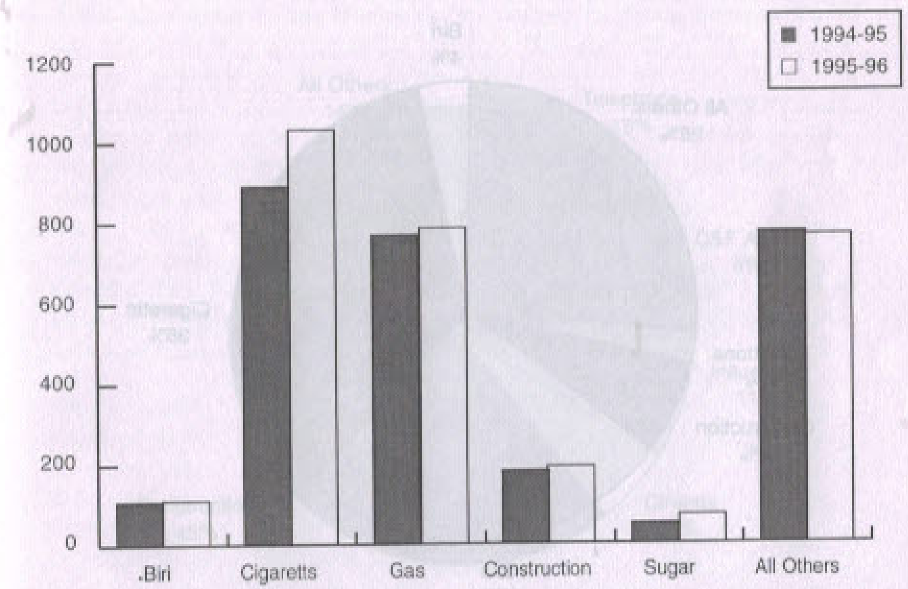
## Large Tax Payer of Rajshahi

| Sl. No. | Name of the firm | Name of the Commissionerate | Item Name | Tax type | Revenue Collection (in crore taka) 1992-93 | 1993-94 | 1994-95 |
|---|---|---|---|---|---|---|---|
| 1 | Square Pharmaceutical Ltd. | Rajshahi | Medicine | VAT | 8.67 | 10.03 | 10.95 |



## Comparative Revenue Position on Major Sectors 1994-95 to 1995-96

[Figure in Crore]



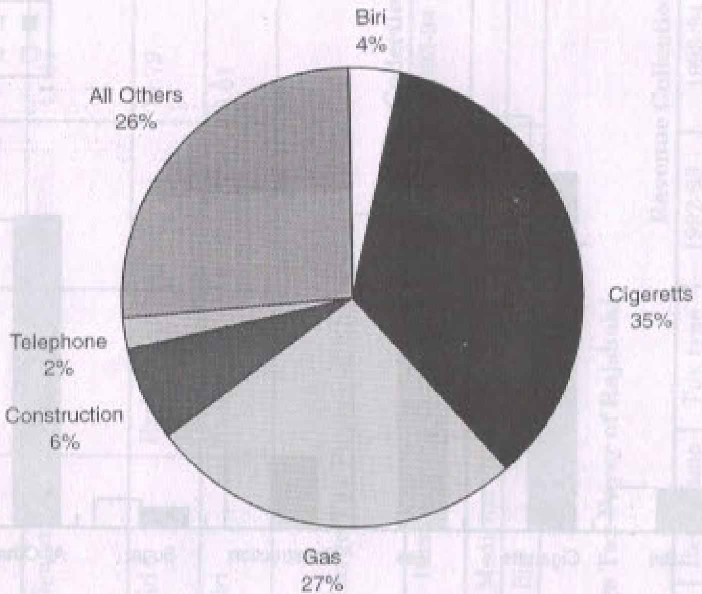

## Comparative Revenue Position on Major Sectors

(Figure in Crore)

| Item Name | Amount | Percentage |
|---|---|---|
| Biri | 107.63 | 110.37 |
| Cigaretts | 891.59 | 1030.26 |
| Gas | 768.95 | 785.63 |
| Construction | 180.84 | 191.13 |
| Sugar | 48.61 | 69.86 |
| All Others | 772.66 | 764.71 |

# Sector-Wise Revenue Collection (1995-96)

[Figure in Crore]



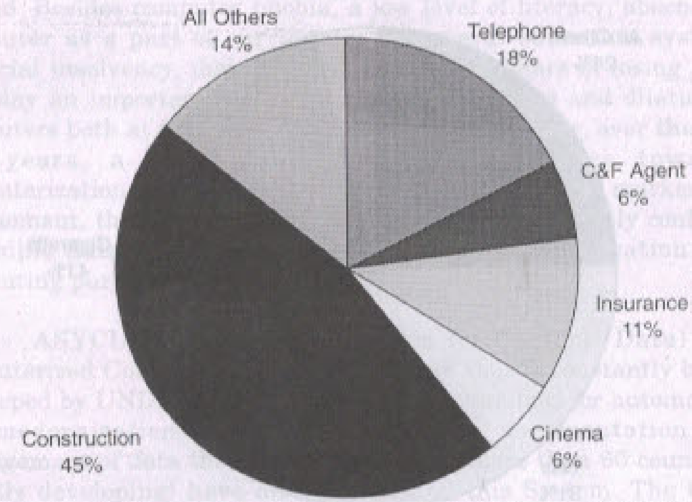

## Sector-Wise Revenue Collectin (1995-96)

| Item Name | Amount (Figure in Crore) | Percentage |
|---|---|---|
| Biri | 110.37 | 3.74% |
| Cigaretts | 1030.26 | 34.90% |
| Gas | 785.63 | 26.61% |
| Construction | 191.13 | 6.47% |
| Telephone | 72.65 | 2.37% |
| All Others | 761.92 | 25.90% |



# VAT : Services Sector (1995-96)

[Figure in Crore]

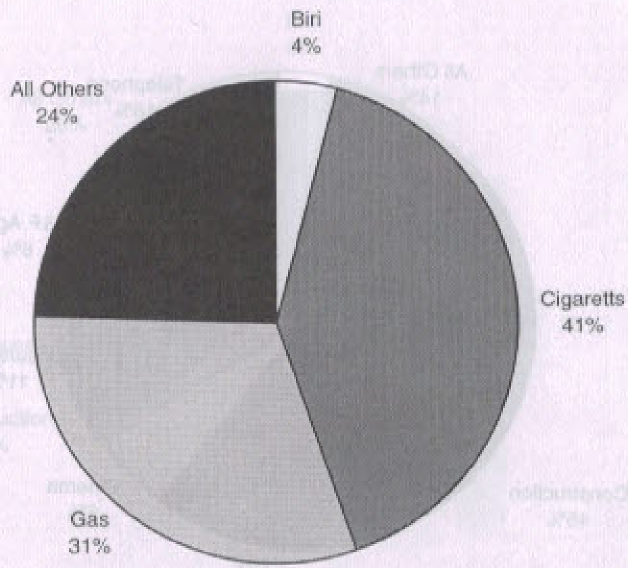



## Service Sector

| Item Name | Amount (Figure in Crore) | Percentage |
|---|---|---|
| Telephone | 72.65 | 17.62% |
| C & F Agent | 23.02 | 5.63% |
| Insurance | 44.61 | 10.82% |
| Cinema | 23.05 | 5.59% |
| Construction | 191.15 | 46.35% |
| All Others | 57.71 | 13.99% |

# VAT : Products Sector (1995-96)

[Figure in Crore]




## Product Sector

| Item Name | Amount (Figure in Crore) | Percentage |
|---|---|---|
| Biri | 110.37 | 4.30% |
| Cigaretts | 1030.26 | 40.60% |
| Gas | 785.63 | 30.90% |
| All Others | 613.97 | 24.20% |



# *Automation of Customs Clearance Procedure in Bangladesh*[1]

*- Md. Ghulam Hussain*[2]

Computer has become an integral phenomena of modern life. Although its use in the management system has long been accepted the world over, for a number reasons Bangladesh is still, lagging behind. Besides computer phobia, a low level of literacy, absence of computer as a part of curriculum in general education system, financial insolvency, disinclination to changes, fears of losing jobs, etc. play an important barrier to repudiate the use and dilation of computers both at public and private sectors. However, over the last few years, a remarkable change in attitudes towards computerization in both these sectors is ostensibly being marked. At the moment, the use of computers in Bangladesh is mostly confined to simple data storage and processing, report preparation and accounting purposes.

02. ASYCUDA (Automated System for Customs Data) is a computerized Customs management system that is constantly being developed by UNDP. It has become de-facto standard for automation and modernization of Customs procedures, documentation and management of data through out the world. More than 60 countries (mostly developing) have already adopted this System. The GOB (Government of Bangladesh) has taken a revolutionary step through the implementation of this System in Bangladesh.

03. In Bangladesh, ASYCUDA has been launched as a project of the National Board of Revenue (NBR), Ministry of Finance, GOB, in 1991 with the financial assistance from UNDP. The project is redesignated as SPEED (Special Processing of Electronically Entered Declarations) at its implementation stage. The project has gone live since August 01, 1994, in Custom House, Dhaka and since June 03, 1995, in Custom House, Chittagong.

### *Characteristics*

04. **ASYCUDA** has the following characteristics :

a. **a standard system** using the international codes and standards developed by ISO (International Organization for Standardization);

b. **an adaptive system** that can be configured to adapt to the operational requirements of each individual Customs Administration;

c. **fiscal flexibility** - all tariff regulations including exemptions are handled without changing the source codes;

d. **access to data** - different users within the administration are free to define the requirements and frequency of data output; and

e. **an EDI[3] system** that offers facility for the national administration to utilize Electronic Data Interchange (EDI) between traders and Customs based on UN/EDIFACT[4] (United Nations rules for Electronic Data Interchange for Administration, Commerce and Transport).[5]

***Objectives***

05. SPEED has been launched in Bangladesh with the following objectives:

a) to ensure faster processing of declarations;
b) to increase revenue through elimination of leakage;
c) to create a self data-base; and
d) to minimize the cost of clearances.

***System Benefits***

06. SPEED is introduced in Bangladesh for obtaining the following System benefits, namely;

a) accurate entries;
b) faster processing of entries;
c) accurate accounts;
d) greater revenue control;
e) improved management information;
f) up-to-date statistics on external trade;
g) low development cost;
h) targeting of control;
i) increasing revenue;
j) easier taxation changes; and
k) data interchange.



***System Modules***

07. The System (SPEED) has several modules. These are-
(i) manifest;
(ii) declarations processing;
(iii) licensing;
(iv) accounts;
(v) warehousing;
(vi) suspense procedure; and
(vii)statistics.

08. A brief explanation on the operation and utilities of these modules is provided below:-

(i) **The Manifest Module** - The acceptance of goods entering the country under Customs control is the first stage of the Customs process. This acceptance is undertaken through the input and verification processes controlled by the Manifest module. The Manifest module takes account of the traffic of goods automatically and is capable of establishing linkages with the custodians (Port Authorities or Civil Aviation Authority, as the case may be). This means, an account of the goods whether cleared or not, for how many days these are lying not cleared, legislative or regulatory actions to be taken against the defaulters, etc.- information on these aspects can be obtained at any time. To do these tasks properly, the System is capable of absorbing information on manifest number, name of the consignor/consignee, description and quantity of goods, weight, etc. In other words, the System is capable of writing off any manifest when the subject consignments are cleared out of Customs areas. Thus the services that can be obtained from this module must be of enormous use to Customs and custodians of goods. For this, an on-line system is to be established between them. Alternatively, a method of constant interchange of reports (using floppy diskettes) may be evolved. The ASYCUDA version 2.3 used in Bangladesh has some limitations (being relatively slow and time consuming compared with later versions) for which this module is not in use. The latest version **'ASYCUDA ++'** has overcome most of these limitations. Bangladesh Customs is yet to procure one of these versions. At present, Import General Manifests (IGM) are submitted to Customs and the task of writing off manifests is done manually as before. This system of submitting of IGM will have to be discontinued in consultation with the shippers (as soon as the latest version **'ASYCUDA ++'** is installed); and should be replaced with IGM in diskette for the effective functioning of the Manifest Module. The first and foremost task in this regard is to simplify and standardize the present IGM format.

(ii) **Declarations Processing Module** - To ensure speedy and accurate processing of Customs declarations is the principal responsibility of any Customs administration. In ASYCUDA, validation of declarations takes place during the data input process. Consultation of the Control Files and Tariff Files is always possible. At the end of the data input, a global validation is performed, only error free data are transmitted for registration, assessment and storage. It also provides a choice of amendment and cancellation of declarations and throughout its life, until it is archived, the system maintains records of all actions performed upon each declaration it generates, thus guaranteeing a full 'transaction trail'.

09. The processing of declarations includes verification of the genuineness of importers' identity (*VAT* registration number known as *BIN* or *Business Identification Number*) and C & F Agents' identity (*AIN* or *Agents' Identification Number*), *HS* (Harmonized System) *codes* and their corresponding descriptions of goods, valuation of goods (in cases having Tariff Values), and automatic calculation of duties and taxes and other charges. The System has built-in **Tariff** and **Control Files** that contain database on importers, exporters, C&F agents, National Tariffs, duty and tax rates and so on. The outcome of this module is generated in the form of an **Assessment Notice** showing the rates and amounts of duties and taxes payable. This means, the declarants are required to lodge an entry to be processed by Customs and then uplift an **Assessment Notice** to make payment. Upon payment of duties and taxes in the Treasury Bank, the C&F agent is also required to procure a computer generated **Out Pass or Release Order** of goods. Thus the System takes over many a functions and checks with exact precision and accuracy that were previously done manually. The time and energy (manpower) saved in this process are quite considerable. However, we shall elaborate this aspect more in detail while discussing **Declaration Processing Procedure** at a later stage.

(iii) **The Licensing Module** - The aim of this module is to automatically check and write off declarations for licensable goods against a computer record of licenses used. Periodical



reports can be produced showing the status of particular licenses and entries made against them. To operate properly, the license data from license issuing authorities must be got onto concerned Customs office through which the importer/exporter intends to operate and kept up-to-date. License data could be transferred from issuing authorities to the appropriate Customs offices on floppy disks on a regular basis. The Customs office, could, in turn, send back details of declarations processed to the licensing authorities. This, in turn, demands computerization of related activities in license issuing offices. ***Failure to develop a suitable mechanism for interchange of license-data between license issuing authorities and the Customs left this module unutilized.*** The module, however, is also found to be lengthy and time consuming.

(iv) **The Accounts Module** - This is the Cashier's office management system that caters for the payment of declarations. It also monitors the duties and taxes collected. This module provides, at the end of the day, a statement known as **Cashier's Day Book** showing the registration numbers of the declarations, names of the decalarants, HS codes and the amount of duties and taxes realized against each transaction. This means, the System is balanced daily and requires that the account be closed at the end of each day to maintain a reliable audit trail. Thus, it is a Single Entry Ledger Accounting System under which duties, taxes and other charges are automatically recorded. It also generates a **Payment Receipt** *and* **Release Order** *or* **Out Pass** for each declaration or entry. Declarations may be cleared against prepayment accounts or account currents (as in case of Bangladesh), credit accounts or cash.

(v) **The Statistical Module** - Data that have been entered into the System once may be used for several purposes. The data extracted as an **ASCII** (or American Standard Code for Information Interchange) can be used by various programmes, spreadsheets, databases etc. These programmes can be used for statistical and financial analysis and planning. At the moment, however, the extraction utilities are used as a powerful tool for the generation of routine reports, and the production of special reports, for control and enforcement purposes. Data held on the ASYCUDA / SPEED files is equally available by virtue of the extraction utilities, for use operationally on the valuation of specific commodities, or to obtain details of the pattern of imports by an importer. This module is functioning properly.

**However, a separate on line package (Supplementary database) is to be developed and be integrated with ASYCUDA system.** This will enable the Customs authority to monitor the value of goods imported/exported and extract necessary statistical reports that ASYCUDA can not generate directly.

(vi) **The warehousing Module** - The System maintains a warehouse account, writing off goods as they entered for home use or re-exported. The System requires the reference number of the **in to bond** declaration to be quoted on the **ex bound** declaration. However, this module requires more updating and configuration and so is not in use at this moment.

(vii) **The Suspense Procedure** - This module can take care of goods imported under Temporary Importation Rules. The functioning of this module is similar to the Warehousing module. This module is not in use in Bangladesh.

10. Given limitations of some of the modules mentioned above, all exports and imports for warehousing purposes are kept outside the arena of SPEED for the time being (in case of Chittagong Custom House).

CONTROL FILES AND TARIFF FILES

11. **Control Files** are created to verify the data entered into the system. These are classified under different functional groups taking into account of all international standards pertaining to the associated data elements. Thus the Control Files contain the numeric codes and other relevant information. Some numeric codes used in SPEED do not observe any international standard. For example, codes used to mean the bases of value, e.g., CIF, FOB, assessed value etc.; units of measurements, e.g., kilograms, litters etc., Customs station, Customs Procedure Codes (CPC) and so on. Other numeric codes do represent international standards (by the United Nations Statistical Office for the recording of statistics) like country codes and currency codes (both 3 digits), mode of transport (1 digit), and so on.

12. The ASYCUDA Tariff File is divided into two types- (a) Base Tariff and (b) National Tariff Files. The Base Tariff File contains the Harmonized System, commodity codes and nomenclature. This is the internationally agreed standard of classification. The National Tariff



File is the further development of the Base Tariff File. It offers the users scopes to add further precision to the HS classification according to fiscal or statistical requirements. It also holds taxation data, statistical units and supporting documents pertinent to the national classification. So, continuous amendment and updating of National Tariff Files showing the HS codes, description of goods, duty and tax rates and tariff values, etc. are to be done. In any case, the task of checking and updating of the National Tariff Files is very simple and easy.

***Training and Staffing***

13. Intensive training programmes were conducted for Customs officers and staff, and other related bodies like C & F Agents, shipping agents, Port Authorities, Civil Aviation Authority, banks and members of trade and commerce, etc. Training materials and guide books[6] are being published and made available to the users free of costs. The task of operating the computers is assigned to own ministerial staff and computer engineers (Assistant Programmers) are recruited to look into the technical/hardware side. The task of updating and configuration of files (since it requires adequate knowledge on both ASYCUDA System and Customs-classifications, etc.) is left to mid-level officers of Customs having training abroad or locally on ASYCUDA. The ministerial staff working as operators do not have access to the mother programme and as such cannot make any amendment to the data already inputted. In fact, the System is working under a **Local Area Network**[7] or **LAN** and as a part of the System, each operator is provided with a terminal for inputting data only. This means, their training is confined to particular aspects of System operation. This is very important from security point of view also.

***Manual System of Declaration Processing***

14. The Manual of System processing of Customs declarations has been often criticized as corruptive and evasive, lengthy, time wasting and cost inefficient. Under this Manual System, the declarants were required to prepare and submit seven (in some cases eight) sets of Entry / Declaration Forms along with related documents (some of these documents require authentication by the issuing authorities). The C&F agents are to move from one branch to another with the declarations and in the process, some 20 steps and 38 (approx.) signatures were required to obtain a ***Release Order*** or ***Out Pass***. This, however, does not include the formalities to be observed with

related organizations like Port Authorities, Shipping Companies and so on.

***Characteristics of The Asycuda Declaration Form***

15. The manual Declaration Form is a double-sized demy paper (22.5" x 17.5") with provisions to accommodate declaration information in one side and the back page is used for report writing purposes. Three different forms are in use for import, export and unaccompanied passenger baggage. To cater the requirements for computer processing, these Declaration Forms were needed to be redesigned and put into use with the introduction of ASYCUDA (see Appendix I). The new ASYCUDA Declaration Form has been designed to align with the standard UN layout. Thus the new Declaration Form is intended to be a Single Administrative Document. It is multi-functional and replaces existing three forms viz., Bill of Entry, Bill of Export or Shipping Bills and Baggage Entry Forms. Most of the information required to be furnished under the Manual System are being accommodated in the new Declaration Form.

***The Speed Declaration Form***

16. The SPEED Bill of Entry/Export or the Declaration Form (see Appendix I) is a A4-size pre-printed paper having 44 boxes to accommodate relevant information. It has three segments divided into dark and deep lines. Boxes 1 to 25 are treated as ***General Segment Information*** or ***Header Information*** containing information (e.g. importer, exporter, agent, mode of transport, name of carrier, manifest number, bill of lading number, and so on) which are proper to all goods being declared on the Entry Form irrespective of the number of items. The System has a built in mechanism to identify any wrong information related to ***Header Information Segment*** mentioned above. The second segment contains boxes from 26 to 44 usually known as ***Item Segment Information***. This segment contains information that relates to each separately classified product being declared (e.g. commodity codes, quantity, value, marks & numbers, number of packages and package types, country of origin, etc.). The third segment is called the ***Declarants' Segment*** meaning that the C&F Agent or the declarant is accepting responsibilities under law for :

a. the accuracy of the information in the Declaration;

b. the authenticity of the documents submitted with the Declaration; and



c. the observance of all the obligations necessary under the declared procedures.

***How to Prepare a Declaration***

17. Guide books for preparing a Declaration are published [8] by NBR and made available to the users. The decalarant is required to fill in only one copy of the Declaration Form using indelible ink. It should preferably be completed by use of type-writer or computer printer. It may also be filled in by hands. In any case, the writings or printings must be legible and in block letters. Mandatory boxes must be completed correctly and other boxes as and when necessary. Incorrect or inadequate information may lead to rejection of the Declaration by the System (and delay in processing) or even penal action. This is absolutely basic and vital for computer processing of the Declarations. Obviously, this responsibility lies with the C&F Agents as required under law.

***More Than Two Items' Cases***

18. For consignments with two commodities or less, the new Entry Form as shown in Appendix I is sufficient. When the number of commodities is more than two, the continuation sheet (as shown in Appendix II) should be used. When the number of commodities in one consignment exceeds 99, two Declarations are to be submitted. This means, the System can accommodate a maximum of 99 items under one Declaration Form.

***Colours of The Entry Forms***

19. For easy identification, the Declaration Forms are assigned to five colours; namely,

(1) **Blue** for general imports;
(2) **White** for unaccompanied passenger baggage;
(3) **Pink** for general exports;
(4) **Yellow** for warehousing (in to bonds); and
(5) **Green** for warehousing (ex-bond).

***Declaration Processing Procedure***

20. A lot of functions and checks are done by computers under this System which were previously performed manually. This demands processing of the Declarations in a certain sequence. In the following paragraphs, a brief explanation of the main activities to be

undertaken within each functional area is provided. Appendix III provides a diagrammatic path of processing of Declarations under this System (following discussion is confined to the procedures to be followed for imported goods only).

21. **Step 1 : *Lodgment of Declaration*** - Presentation of the Declaration and its final acceptance by the System involves three sub-steps within the network. The functional area is known as **Lodgment Hall**. The three sub-steps are discussed in brief as follows-

(a) **Pre-Entry Check Counter** - A properly completed Declaration is to be presented to the Customs at the Pre-Entry Check Counter. Following checks are done at this desk:-
   (i) that all relevant documents are attached;
   (ii) that all mandatory boxes in the form have been completed;
   (iii) that the entry is legible;
   (iv) that it is properly signed; and
   (v) that a Lodgment Slip in duplicate is tendered.

22. The Declaration is accepted only when it is found correct on preliminary check or face vet as mentioned above. If accepted, the Declaration and the accompanied documents are placed in a numbered folder and then sent to the next step - **Data Entry Counter**. The C&F Agent's copy of the Lodgment Slip noting the date and time of presentation of the Declaration and the folder number of the Declaration is returned to them. If not accepted, Customs mark with a highlighter pen the boxes on the Declaration that are incomplete or incorrect and return the same to the C&F agents.

(b) **Data Entry Counter** - Declarations are received in this counter for input of the data into the System. As the information is being keyed into the computer, various checks are applied automatically to ensure that such information is both valid and in agreement with other information stored within the System (Control Files). If the input is successful, the computer automatically generates a print out (3 copies set) of the Declaration which is called **Entry Registration Advice** bearing a continuous number of registration. All papers are then put in the folder and sent to **Lodgment Counter** for acceptance of the Declaration.

(c) **Lodgment Counter** - Declarations are formally accepted at this counter. Customs notify the C&F agents that the Declaration is



ready to be lodged by displaying the folder number of the Declaration on the **Display Board** in the **Lodgment Room**. Customs make entry of the registration number, date and time on both copies of the **Lodgment Slip** and return the copy of the **Lodgment Slip** to the C&F agents. All other documents are retained for subsequent checking and assessment.

23. **Step 2 : *Appraisement Groups*** - The functions of the Appraisement Groups are concerned with ensuring that the information as declared on the Declaration Form are correct and in accordance with supporting documents. Followings are the main jobs to be done at this stage:
   (a) a full document check against the Declaration;
   (b) the correct classification of goods;
   (c) ensuring the declared values are correct;
   (d) ensuring use of the correct **Customs Procedure Code** (CPC - relating to duty & tax rates); and
   (e) the importability status of the goods.

24. At this stage, the Declarations are also identified for the type of physical examinations to be done depending on importer's status, type and quantity of goods imported and so on. **Three separate categories** have been built into the entry process, designed to enhance the quicker delivery of goods from the Customs control. These are :-

   (i) **delivery without examination;**
   (ii) **delivery after examination**; and
   (iii) **examine and report.**

25. The process of assessment of the Declarations varies considerably in respect of the above three categories. In relation to 24(i) above, appraisement and assessment are done without physical examination of goods. The C&F agents are advised through a display board to uplift the **Assessment Notice** from **Folder Exit Center** for making payments of duties and taxes (if any) in the Treasury Banks. During delivery time, the **Jetty Customs** conducts inspections of containers. In respect of 24(ii) above, duties and taxes are paid in the same process as mentioned under 24(i) above. However, goods are examined during delivery times. **Release Order** or **Out Pass** is issued only when no discrepancy is reported in the examination of goods. In regard to category 24(iii) above, assessment takes place after the goods have been examined. To ensure quick clearance of goods, categories 24(i) and 24(ii) are encouraged

covering about 70% of the consignments (in terms of value). The Government has also enacted some laws (like **Pre-Shipment Inspection law**[9] or **PSI**) that prohibits tall order examination of goods (third category).

26. Any error detected during the appraisement check or physical examination of goods or both, is advised to the C&F agents using the **Advice Notes** (Appendix IV) on the reverse of the Declaration through **Folder Exit Center**.

27. <u>Step 3</u> : ***The Assessment Counter/Room*** - The display board kept in the C&F agents' waiting room is controlled from this counter. Under the following circumstances, a **C&F** agent may be notified or advised to contact the **Folder Exit Center**-

a. to raise the documents requiring for conducting examination of goods[10];

b. to procure an **Advice Note**;

c. to raise the **Assessment Notice** for making payment; and

d. to appear on interviews for further explanation on the Declaration.

28. **Assessment Notices** (3 copies) are printed in this room on the basis of the final recommendation given by the **Appraisement Groups**. These notices show the amount of duties and taxes payable. The amount due for payment is calculated automatically since data on duty and tax rates are put in advance in the System. So there is no scope for wrong assessment as per as duty and tax rates are concerned. The **Assessment Notices** are then sent to the **Folder Exit Center** for distribution among the C&F agents.

29. <u>Step 4</u> : ***Folder Exit Center*** - The Folder Exit Center is the epicenter for the uplifting of **Advice Notes**, collecting of documents, and making contacts with the Customs officers. This center receives folders and or **Advice Notes** from **Appraisement Groups** through **Assessment Room** or from **Jetty Customs**. It also receives notices from C&F agents soliciting interviews with any Customs officer. An Advice Note is issued to the C&F agents when-

a. further information is required to process the Declaration;

b. an interview of the C&F agent or importer is required;

c. the goods are to be sent for testing; and

d. the goods are to be examined before final assessment.



30. Thus the primary responsibility of the **Folder Exit Center** is to ensure security and control traffic of folders from Appraisement Groups to Jetty Customs and vice versa, arrange appointments for the C&F agents with the Customs officers and distribution of documents among the C&F agents. It also receives left over Customs documents (known as Customs copies) from the Jetty Customs and sends them to respective branches for post clearance audit or writing off manifests.

31. <u>Step 5</u> : ***Examination of Goods*** - ASYCUDA provides facilities for automatic selection of Examining Officers. Thus it ensures a degree of protection against collusion between a Examining Officer and a trader or a broker. The task of physical examination of goods is performed in accordance with departmental standing instructions. Normally physical examination of goods before appraisement [category 24(iii)] is discouraged. The **Selectivity Criteria** is in use to some extent, though the method in practice is not scientific. The Appraisement Groups maintain personal profile of big or frequent importers or exporters and C&F agents. Besides, other considerations like country of origin or shipment of goods, nature and type of goods, value declared, quantity imported, etc. are also in practice. The Customs Vigilance Team is also providing continuous information.

32. For writing of Examination Reports, a separate form known as **'Examination Report'** is in use. The C&F agents are informed of the decisions for examination of goods through an Advice Note to be obtained from the **Folder Exit Center** as mentioned above. All relevant documents (folder) are directly sent to the **Jetty Customs** [in case of category 24(iii) above], under Customs custody. However, the C&F agents are provided with only those documents that are necessary for the identification and production of goods for examination. This is done before sending the folder to **Jetty Customs** so that in the mean time, the C&F agents can make suitable arrangements for the examination with the custodians of goods and report to the concerned Customs Examining Officers deputed to conduct the physical examination.

33. In case of category 24(ii) above (delivery after examination), folders are sent directly to Jetty Customs and the C&F agents are to follow the same procedure for making arrangements for examination of goods as mentioned under category 24(iii) above. If no discrepancy is found during examination, the C&F agents are advised to go on with relevant documents to make payments and obtain **Release**

**Orders** or **Out Pass** of goods. If discrepancies are found, the examination reports are noted accordingly and all papers are retained and then sent back to the Appraisement Groups.

34. In case of category 24(i) above, appraisement and assessment tasks are done and relevant papers and delivery of goods provided to the C&F agents without examination.

35. The **Selectivity Criteria**, as mentioned above, is used for the selection of goods for examination on the basis of a set of pre-determined criteria. On the basis of these criteria, the declarations are allocated with different status such as **Green, Yellow** and **Red.** A similar method is evolved in Bangladesh, but practiced manually as follows-

a) 24(i) - **Green - Delivery without Examination** :- imports against CRF (Clean reports of Findings or PSI), government imports, bulk imports, items having nil or nominal rates of duties etc.;

b) 24(ii) - **Yellow - Delivery after Examination** :- capital machinery, renowned importers, etc.;

c) 24(iii) - **Red - Examine and Report** :- all other imports.

36. Examination of goods is a manual job and as such remains outside the purview of the automation System.

37. <u>**Step- 6**</u> : ***Treasury Bank***- The Treasury Bank is responsible for the collection and receipt of duty payable. Once duty is paid, the bank authority authenticates the payment , and the papers are sent to the Customs officers' desks, a **Payment Receipt** in duplicate is generated by the System. The Customs officer signs and stamps it and the original is handed over to the C&F agents. Meanwhile, the System is instructed to generate a **Release Order** or **Out Pass** against this that is to be obtained from the Custom Treasury Branch situated to the next door.

38. <u>**Step -7**</u> : ***Customs Treasury***- The **Release Order** or the **Out Pass** is to be collected from this branch. This order is issued in triplicate, the original being used for taking delivery of goods and it is known as 'importer's copy'; the duplicate is sent back from the **Jetty Customs** to the Custom House (Folder Exit Center which in turn to Manifest Branch) confirming the physical delivery of goods from the Custodians and the triplicate is retained for onward transmission to the Manifest Branch.



39. <u>**Step 8**</u> : ***Gate Check*** - This is the final stage to check the documents against delivered goods. During actual delivery of goods, the Preventive Staff stationed at this stage is to ensure that the number of containers, packages, marks and numbers , etc. do correspond to those of the Declarations. Any discrepancy found at this stage leads to temporary stoppage of clearance of goods and the matter is brought to the knowledge of the concerned Appraisement Groups through Jetty Customs for legal action.

***Manual System Vs. Automated System***

40. Computerization and rationalization of Customs clearance procedure should have quickened the clearance of goods and reduced delays in deliveries to the clients. The requirement of preparing seven sets of Declarations is replaced by one set of Declaration. The number of steps involved in the processing of a Declaration has gone down to seven (exc. Examination which is in fact not a part of the System. This subject is explained earlier.) and approximately ten signatures are now required to get the goods cleared against 38 signatures under the Manual System. As a result, the associated overhead costs that affect the price of imports and exports are being greatly diminished. The System reinforces Customs control and monitors the collection of customs duties and taxes. It generates trade data that are used for statistical analyses which in turn results in more coherent information being available for the formulation of realistic economic plans and forecasts. Thus data generated by this System is now available for many purposes of national requirements. Following is a comparative scenario of Manual System and the Automated System:-

***Manual vs. Automated System of Processing of Declarations***

<u>**Manual System**</u>
<u>**Automated System**</u>

| | | | |
|---|---|---|---|
| 1. | 9 steps | 1. | 7 steps |
| 2. | about 38 signatures required | 2. | only 10 signatures are required |
| 3. | 7 sets of declarations & allied allied papers | 3. | single declaration & one set of papers |
| 4. | different forms for X, M, B | 4. | single declaration form |
| 5. | double demy size form | 5. | A4 size form |
| 6. | manual calculation of CD VAT & charges- no mistake | 6. | automatic calculation of CD VAT & other charges - mistakes |
| 7. | 95% consignments examined | 7. | examination before assessment |

| | | | |
|---|---|---|---|
| | | | is discouraged |
| 8. | chasing of declaration by C&F agents | 8. | Closed Loop System |
| 9. | discrepancy in daily reports | 9. | automatic generation of reports- no discrepancy |
| 10. | manpower shortage | 10. | surplus manpower utilized on vigilance jobs, data input & examination |
| 11. | high administrative costs | 11. | low administrative costs |
| 12. | almost no control | 12. | better control- automatic identification of risk cargoes |
| 13. | slow and lengthy procedure | 13. | quick & time saving procedure |
| 14. | difficult to monitor collections | 14. | easy to monitor collections |
| 15. | manual preparation of reports | 15. | automatic generation of reports |
| 16. | difficult to transfer data | 16. | easy to interchange data |
| 17. | manual writing off of manifests & license data. | 17. | automatic writing off of manifests & license data |

### *Measures to Guard Misdeclarations and Revenue Leakage*

41. It has been mentioned earlier that the task of examination of goods is left out of the System, though some sort of **Selectivity Criteria** is also in use. However, to ensure speedy clearance of goods on the one hand, and to guard any possible leakage of revenue on the other, several administrative and fiscal measures are being undertaken. Some of these are- encouragement of examination or inspection of goods at the time of delivery (as mentioned earlier), use of VTR (**Valid Test Reports** made acceptable if the test is conducted not before six months) for chemical products, rationalization of Tariff structures and introduction of **Pre-Shipment Inspection** (voluntary), and so on. But these are not enough. **Some more administrative and fiscal measures are in immediate need such as - deployment of more officers for conducting examination works, strengthening of intelligence network, maintain dossiers of importers, exporters and C&F agents having bad records, statutory provisions to take exemplary penal actions against the offenders, creation of a Supplementary database to prevent over or underinvoicing of goods** (more specifically, to monitor values of goods and generation of statistical reports as required, since the System can generate some specific reports only that may be found not enough from policy formulation and planning point of view), **and finally, reintroduction of the Closed Loop System** (also discussed later).



### *Problems Encountered at the Configuration Stage*

42. It is stated in the ASYCUDA documents published by the UNCTAD that the package runs under a variety of configurations and encompasses the majority of a country's international trade procedures. The configuration facilitates the definition of mandatory and conditional data elements, the structure and format that such data should take (numeric and alpha-numeric), and the specification of validation checks that will be performed against it. The package contains indexed master tables that are user friendly and ensures efficient management of large volumes of reference data which can potentially be related to a given transaction. For example, country codes and currency codes, means of payments, exchange rates, means of transportation, etc. provide all the information which may relate to a Declaration. In other words, **ASYCUDA allows the national Customs administration to adapt the system to its own needs and national regulations.** But in reality, a good number of divergent requirements of the Bangladesh Customs could not be fully satisfied. Our following discussion aims at highlighting some of these problems in brief:

### *Configuration Problems*

43. At the configuration stage, the SPEED team has faced a lot of problems (causing delay in implementing of the project) that may be attributed to the presence of a cumbersome Tariff Structure (such as existence of so many exemption notifications, more than one duty rate for a single HS code, notifications using commodity trade names instead of Tariff descriptions, etc.), presence of Tariff Values on items using trade names and country of origins, more than one Tariff Values for a single item, non-availability of standard information for the creation of Control Files, development of procedures and the like. Moreover, problems have been created by statutory restrictions on valuation[11], such as-

a. between **Tariff Values** and **invoice values**, the higher one is to be accepted for assessment purposes; and,

b. mandatory acceptance of **Pre-Shipment Inspection Certificate** (CRF-Clean Reports of Findings) values though the item in question may have Tariff Value.

*Lack of Commitment*

44. There is no denying the fact that implementation of a package like ASYCUDA (perhaps equally applicable to any sort of automation) presupposes simplification of national rules and regulations. It is very crucial that all parties involved in the System be committed to its success and there is a strong political commitment (because such automation may lead to loss of jobs) at the appropriate level. This is also required because the System reinforces control leading to transparency and minimization of tax evasion scopes and monitors the collection of public revenue so vital for a country like Bangladesh. In any case, solutions of the problems cited above were not easy and simple. In many a cases, it was found very difficult, if not impossible. However, a solution was arrived at for each of these problems, though often, these solutions are found to be very lengthy and error-prone (manual recalculation of adjustment coefficient as discussed below) that may result into loss of revenue.

*System Bottlenecks*

45. The ASYCUDA Declaration Form is actually the EC Declaration Form that does not accommodate all the information relating to the clearance of exports and imports in Bangladesh. Because of inherent non-flexibility characteristics of this form, and presence of some cumbersome System modules (like manifest and license), Bangladesh had to implement it leaving these problems unresolved. Let us discuss some of these limitations as follows:

a. ***Carriers' Name*** - There is no provision to accommodate the 'Carriers' Names' in the ASYCUDA Declaration Form. As a result, the computer generated Declarations do not contain this information. But Shipping Agents need this particular for issuance of NOCs (No Objection Certificates) requiring for taking physical delivery of goods from the custodians. Information like Cargo Lading Numbers, Rotation Numbers should suffice (shown on the computer generated Declarations and Assessment Notices) for virtual writing off of shipping documents or for simple official records at that end, but some Shipping Agents were found hesitant to issue these NOCs. This compelled the Customs authority to write down manually the 'Carriers' Names' on the **Release Orders** whenever asked for;

b. ***Cargo Lading Numbers*** - Cargo Lading Numbers are not globally standardized like Air Way Bills. These can be of any



number of characters or digits. But ASYCUDA System can accommodate a maximum of fourteen characters or digits starting from the left. This means, numbers beyond this limit cannot be inputted in the System. This creates problems in time of examination and delivery of goods and writing off manifests (manually). At the moment, the left over digits/characters (if any) are written down on the **Release Orders** manually by the Customs. But this practice leaves the database incomplete and virtual non-functioning of the Manifest Module. This kind of manual manipulation is not desirable in a computer environment;

c. ***Letter of Credit Numbers*** - The non-functioning of the License Module leaves no provision for inputting letter of credit numbers and the related bank's name in the System. So the computer generated statistical reports do not show license numbers and bank names. Under such circumstances, the license issuing authorities or the Bangladesh Bank cannot link up monthly statement particulars sent by the Customs authorities to their database;

d. ***CRF Numbers*** - There is no scope of accommodating CRF (Clean Reports of Findings) numbers in the System and as such, the Customs authority does not have any means to monitor these CRFs and generate reports accordingly;

e. ***Trade Names of Goods*** - Computer generated documents (like Declarations and statistical reports) provide goods description on the basis of Base Tariff Files (Harmonized Nomenclature) of ASYCUDA. But most goods are traded under trade or generic names. These names though can be accommodated in the National Tariff Files of ASYCUDA (and seen on the screen while inputting) but are not shown on the Declarations and standard reports generated. These create problems in time of examination and delivery of goods on the one hand and monitoring of goods traffic, on the other;

f. ***Adjustment Coefficients*** - For the purpose of ascertaining the assessable value, the 'adjustment coefficient' is fixed at '1' which is equivalent to CIF value plus landing cost. If the item in question bears a declared value lees than the Tariff Value, the System picks up the higher value (whichever higher) for assessment purposes. But if the assessable value is fixed at a level higher than the declared value or Tariff Value, the adjustment coefficient is to be refixed manually at more than one. An opposite position may arise in cases where goods are imported against CRF having a value less than the Tariff Value (adjustment coefficient is to be refixed at less than one). This kind of manipulation may result into unintentional errors and thus causes loss of revenue.

*Closed Loop System*

46. It appears from our foregoing discussion that the ASYCUDA or SPEED entails many changes to the processing path of Declarations. To ensure that the Declarations follow the correct path they routed through the System by means of functional areas and in each of these areas, a specific activity is performed. Once a Declaration is lodged, it remains in the custody of Customs through out the process. There is no direct interface between C&F agents and Customs officers unless queries arise, or further information is required.

47. Ideally, this should be the working atmosphere in both the Custom Houses where ASYCUDA is in operation. Unfortunately, none of the two Custom Houses could as yet proceed with the introduction of this **Closed Loop System** in its desired form. Custom House, Chittagong, has tried to introduce this, efforts in this direction went in vain due to strong resistance from the C&F agents and their employees (sirkers). It may be mentioned at this stage that the **Customs authority will not be able to ensure security of Customs documents and revenue if everybody and anybody has access to the restricted areas. This, also, is in contrast to a computer environment**.

*The Management Issue*

48. It should be noted that ASYCUDA is not merely a technical know-how to process the Declarations. Unfortunately, the managerial responsibility of the project in both the Custom Houses is left with mid-level officers having either no training on computer or are not trained on ASYCUDA locally or abroad. The System Manager and the Assistant System Managers should be ASYCUDA trained personnel. The technical manpower is also awfully inadequate to run such a big System. At the moment, both Custom Houses have only one Assistant Programmer each. There should be at least one Programmer and two Assistant Programmers in each station. None of the Custom Houses could as yet build a



Supplementary database and then integrate it with ASYCUDA for lack of technical manpower.

*Standardization of Relevant Documents*

49. For the purposes of facilitation of international trade, standardization of all relevant documents is a pre-requisite. This means, standardization of Customs Declaration Forms is not enough. Other forms like invoices, bills of lading or airway bills, licenses, etc. are also to be standardized (at least in terms of digits to be used for their numbering). At the moment, Custom House, Chittagong, is facing a serious problem with numbers used in the bills of lading. For example, ASYCUDA can accommodate a maximum of 14 digits as the number of the bill of lading. But in practice, in many a cases, this number is found beyond the above mentioned limit. The System accepts the first 14 digits beginning from the left and remaining digits (if any) are left non captured. This creates unwarranted delay in the processing of Declarations and ultimate delay in delivery of goods and virtual non-functioning of the Manifest Module (as it fails to write off the manifest number automatically). In other words, this problem alone is sufficient to frustrate the very objectives of ensuring faster processing of Declarations and the creation of a self database. The database created by the Customs becomes incomplete and distorted[12].

*Pilot Implementation*

50. It is very important to carry out a Pilot Implementation prior to introducing the System in big stations. Unfortunately this was not done. Instead, the project was introduced in big stations like Dhaka and Chittagong Custom Houses with a couple of months so called '**trial running**'. Should the project team stationed at the NBR select ICD, Kamalapur, Dhaka (the workload in this station is relatively low), it could have monitor the functioning of the project very closely. Once satisfied, then the project could be implemented in other stations. Given the present circumstances, it would be very difficult to introduce a Closed Loop ASYCUDA in ICD, Kamalapur. Only a strong political commitment and administrative will can ensure reintroduction of the Closed Loop Systems in Dhaka and Chittagong Custom Houses.

## *Evaluation of the Project*

51. Both the Custom Houses have more than one year's experiences of running the System. In the meantime, there should have been some appraisals of the performances of the System. In any case, a study should be carried out preferably by individual Custom House administrations (or centrally by the Board) covering the following aspects, for example:

a. What are the costs of introducing the System?
b. What are the benefits that it should have provided?
c. What are the benefits derived out of it in terms of revenue augmentation, cost minimization, elimination of revenue leakage possibilities, and so on?
d. Is it running at its desired level?
e. What is the opinion of its clients towards it?
f. Do we have the right environment for smooth running of this automated System?
g. What are the reasons for non-functioning of the Closed Loop System?
h. Is it desirable to run the System under an Open environment like the present one (following the breakdown of the Closed Loop System, it is being in an Open environment)?
i. What is the level of commitment among the Customs officers for its eventual success?
j. What steps should be taken to make it a complete success?
k. Do the clients have the same ideal and goals towards it as the Customs have?
l. Did it simplify the clearance procedure?
m. What is the impact on revenue?
n. Does it ensure quick clearance?
o. and so on.

52. Experiences in Mauritius and Zimbabwe reveal that the transit time of goods through Customs has been decreased from one week to one day since the installation of the System. In Sri Lanka, for an investment of less than 2 million US$, the revenue has increased by some 8 million US$ monthly, or about 10% of Customs revenue[13].



## *Conclusion*

53. The benefits of Customs Automated Systems are often intangible and even where they can be measured it is frequently the case that they do not accrue to the Customs authority itself but to other members of the trading community e.g. carriers, agents or brokers, importers or exporters. The Customs Administration of Bangladesh is yet to make an evaluation of the benefits derived from Customs automation. However, introduction of ASYCUDA has brought about many procedural changes - most important one is being the C&F agents' are no longer carrying the Declarations through the System but is lodging a Declaration to be processed by the Customs and uplift ***Release Order*** for the goods after a check has been undertaken and the duty-taxes have been paid. The automated System ensures quick clearance of goods, minimizes mistakes in classifying goods and calculation of duties and taxes, ensures security of Customs documents, helps creation of a self data-base, generation of statistical reports and interchange of external trade statistics, etc. All these, in turn, surely minimizes revenue evasion possibilities and corruption and finally, the administrative costs of clearance of goods. There was no loss of jobs, inter-branch transfer of manpower has been made and some new jobs were created to look into the hardware and technical side.

54. As we move towards the Twenty First century, Customs perception of its role is changing dramatically. Gone are the days when Customs could carry out their tasks with little or no regard for the effect on other trade participants. Todays Customs authority is there to provide a service. A service to the economy through the collection of taxes and duties, the application of economic measures such as quotas and restrictions and the collection and compilation of the statistical information so vital for proper economic planning; a service to the trading community by being as unobtrusive as possible and facilitating trade to the maximum extent possible; and a service to the community in general by its role in combating drug smuggling, terrorism, etc.

55. Customs has a dual role of trade facilitation and control and a balance between these two aspects is very difficult. There is no denying of the fact that automation has accelerated the processing of imports and exports and the same time helped to identify risk cargo for intensive scrutiny. Despite these, there is still pressure for greater facilitation; and growing drugs problems around the world has asked for intensification of controls. The automation of Customs

clearance procedure in Bangladesh may thus be treated as an inception of a new era to encounter all these challenges.

**References:-**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02. How to Prepare a Bill of Export, SPEED publication series-3, National Board of Revenue.

03. What Happens to the Bill of Entry, SPEED publication series-4, National Board of Revenue.

04. What Happens to the Bill of Export, SPEED publication series-5, National Board of Revenue.

05. SR.O. No. 226-AIN/94/1560/SHULKA, dated June, 1994, National Board of Revenue, Internal Resources Division, GOB.

06. ASYCUDA ++, UNCTAD, October 1994.

07. Standing Orders issued by Bangladesh Customs Administration.

08. S.R.O No. 316-AIN/94/1568/SHULKA, dated November 03, 19904, National Board of Revenue, Internal Resources Division, GOB.

09. An Introduction to Electronic Data Interchange (EDI) in Customs, World Customs Organization (WCO), Rue de l'Indutrie 26-38, 1040 Brussels, Belgium.




**Transperancy-1**

CHARACTERISTCS

a. a standard system using the international codes and standards developed by ISO (International Organization for Standardization);

b. an adaptive system that can be configured to adapt to the operational requirements of each individual Customs Administration;

c. fiscal flexibility - all tariff regulations including exemptions are handled without need to change the source codes;

d. access to data - different users within the administration are free to define the equirements and frequency of data output; and

e. an EDI System which offers facility for the administration to utilize Electronic Data Interchange (EDI) between traders and Customs based on EDIFACT (Electronic Data Interchange for Administration, Commerce and Transport).

**Transperancy-2**

OBJECTIVES

- to ensure faster processing of declarations;
- to increase revenue through elimination of leakage;
- to create a self data-base; and
- to minimize cost of clearances.

**Transperancy-3**

SYSTEM BENEFITS

- accurate entries;
- faster processing of entries;
- accurate accounts;
- greater revenue control;
- improved management information;
- up-to-date statistics on external trade;
- low development cost;

- targeting of control;
- increasing revenue;
- easier taxation changes; and
- data interchange.

**Transperancy-4**

SYSTEM MODULES

1. manifest;
2. declaration processing;
3. licensing;
4. accounts;
5. warehousing;
6. suspense procedure; and
7. statistics.

**Transperancy-5**

MANUAL SYSTEM OF DECLARATION PROCESSING

01 Preparation of Entry Forms or declarations
02 Submission to Import BR for making entry- number & date stamping by ministerial staff
03 Appeasement Groups- PA to distribute among Appraisers or AOs
04 Examination requisitions - AOs
05 Jetty Customs - noting & distribution among PAs by A C / D C Jetty
06 Distribution among Examining Officers- PAs
07 Requisition to Port Authorities for examination
08 Physical examination - PAs, EOs, agents & port authorities
09 Report of Examination to PAs- EOs
10 Countersigned by PAs
11 AC/DC Jetty- forwarding to appr. groups
12 Back to Appr. Groups- AOs proposals for report writing
13 PA decides- 80% cases- for approval
14 AC/DC/JC/Commissioner- 20 % cases only-for approval
15 Back to AOs- to assess CD VAT/TAX etc.
16 PAs for confirmation of assessment
17 Treasury Banks for making payments
18 Customs Treasury- for payment authentication
19 APR [illegible]ups- for out pass



20 Jetty- Port authority for delivery
21 Jetty Preventive- Gate Checks by Preventive Staff
22 Physical Delivery of Goods

**Notes-** PA- Principal Appraiser; AO- Appraising Officer; EO- Examining Officer; AC- Assistant Commissioner; DC- Deputy Commissioner; JC- Joint Commissioner; CD- Customs Duty; VAT- Value Added Tax

**Transperancy-6**

SYSTEM FUNCTIONS- DECLARATIONS

Checks Input Data

Eliminates Errors

Records Each Entry

Calculates Duty and Taxes

Controls payments

Allows data to be interrogated

Produces copies of Customs Entries

MANIFEST MODULE

Captures Manifest Data

Links Manifests to Goods declared

Writes off Declarations against manifests

Produces Control Reports

LICENSES MODULE

Processes Licenses Data

Checks Licenses against Declarations input

Writes Off Declarations against Licenses

Links license issuing Authorities Records to Customs

ACCOUNTS MODULE

Records Accounts Paid and Outstanding

Checks Credit Status

Produces Assessment Notices

Produces Payment Receipts

Produces Release Order

STATISTICS MODULE

Data Captured only once

Sorts and Analyses declarations

Produces Statistics by-

a. Type of Goods;

b. Revenue; and

c. Traders

COLORS OF DECLARATION FORMS

| | |
|---|---|
| Blue | for General Imports |
| White | for Unaccompanied baggage |
| Pink | for General Exports |
| Yellow | for Into-bond Warehousing |
| Green | for Ex-bond Warehousing |

1 This paper was first presented in a seminar jointly organized by the Shipping Ministry, GOB, ESCAP and IMO on the Facilitation of Maritime Traffic held in July, 1996, at Hotel Purbani. For obvious reasons, the weaknesses of the ASYCUDA system were not discussed at this seminar. Since the present seminar is confined to the representation of the departmental delegates, the author finds it his duty to let every participant be informed of the inherent bottlenecks of the version 2.3 of ASYCUDA used in Bangladesh. The paper is being modified and revised accordingly. This paper is for distribution among official delegates only. This revised paper was presented at a seminar on Customs Automation & EDI Techniques jointly organized by the National Board of Revenue and the Bangladesh Customs, Excise & VAT Training Academy, Chittagong, on Sept. 19, 1996.



2 The author is a Joint Commissioner of Customs, Excise & VAT, Chittagong. Views expressed in this paper are his own.

3 Electronic Data Interchange (EDI) is the inter-organizational, computer to computer exchange of business documentation in a standard, machine processable format.

4 UN/EDIFACT comprises a set of internationally agreed standards, directories and guidelines for the electronic interchange of structured data, and in particular that related to trade in goods and services, between independent computerized information systems.

5 ASYCUDA ++, UNCTAD, October, 1994. The ASYCUDA version 2.3 used by the Bangladesh Customs does not have such facility. 'ASYCUDA ++' is the latest version having this facility.

6 Two brochures on 'How to Complete a Bill of Entry/Export' and two other on 'What Happens to the Bill of Entry/Export', Bangladesh Customs Operative Tariff (BCOT) on HS codes, operative splits, Customs Procedure Codes (CPC), duty and tax rates, tariff values, etc. and Standing or Office Orders issued by the Custom House Administration.

7 A local Area Network, or LAN, is a system of computer communication that links together a number of personal computers, usually within a single building, so that various computer users can easily transfer information back and forth.

8 Two brochures namely, 'How to Prepare a Bill of Entry' and 'How to Prepare a Bill of Export', and Bangladesh Customs Operative Tariff showing the HS codes, description of goods, operative splits, Customs Procedure Codes, duty and tax rates, tariff values, etc. are published by the NBR. The first two brochures are available at free of cost in all Custom Houses.

9 S.R.O. No. 316-AIN/1568/SHULKA, dated November 03, 1994, National Board of Revenue, Internal Resources Division, GOB.

10 Documents needed for identification and production of goods at the Jetty are handed over to the C&F agents and the folder with remaining papers are directly sent to Jetty Customs.

11 S.R.O. 316-AIN/94/1568/SHULKA, dated - November 03, 1994, National Board revenue, Internal Resources Division, GOB.

12 ASYCUDA ++, UNCTAD, October 1994, p-5.

13 ASYCUDA ++, UNCTAD, October 1994, p-5.

# *Uruguay Round Agreements and Bangladesh*

Dr. M. Zahid Hossain

***Introduction:***

The Uruguay Round (UR) of the multilateral trade negotiations (MTN) took place on the initiative of the GATT, which is the custodian of MTN, based on equal treatment of all trading nations. Before the UR, seven similar rounds of trade negotiations took place. These were the following:

1. Geneva Negotiations, 1947
2. Annecy Negotiations, 1949
3. Torquay Negotiations, 1950-51
4. Geneva Negotiations, 1955-56
5. Dillon Round, 1959-62
6. Kennedy Round, 1963-67
7. Tokyo Round, 1973-79

Of all the MTNs, the UR was the most ambitious in terms of scope, coverage and implications. Starting in the Uruguayan city of Punte Del Este in September, 1986 it took seven years of protracted and often, difficult negotiations to complete the UR. The UR sought to-

(i) further liberalize trade

(ii) strengthen the role of the GATT

(iii) improve GATT's responsiveness to the evolving international economic environment and

(iv) foster cooperative action with a view to strengthening trade and other macroeconomic policies that impinge on growth.

All the above rounds had similar goals : (i). promoting growth through removing trade as well as domestic policy distortions and (ii). developing an open, transparent and predictable global trading system. The belief that has motivated these painstaking and sometimes stormy negotiations is that freer trade is conducive to specialization based on comparative advantage, which directly translates into higher productivity and growth. In terms of their principal focus, the first six rounds dealt with tariff reduction while the Tokyo Round was concerned with the elimination of non-tariff barriers. The UR went far beyond these traditional concerns and covered new areas such as agriculture, textiles and clothing and services. It also embraced important issues such as intellectual



property rights and trade related investment measures. In addition, it sought to place greater emphasis on the links between trade and other general economic policies and also on the systematic issues related to the functioning of the GATT.

For conducting the negotiations, a Trade Negotiations Committee was set up with two subordinate bodies: the Group of Negotiations on Goods (GNG) and the Group of Negotiations on Services (GNS). While, the GNS was exclusively devoted to dealing with the issues on services, the GNG was divided into 14 negotiating groups as follows:

1. Tariffs
2. Non-tariff measures
3. Natural resource based products
4. Textiles and clothing
5. Agriculture
6. Tropical products
7. GATT Articles
8. MTN agreements and arrangements
9. Safeguards
10. Subsidies and countervailing measures
11. TRIPs
12. TRIMs
13. Dispute settlement
14. Functioning of the GATT

The negotiations culminated in 28 different agreements. In addition, there were numerous understandings and ministerial decisions and declarations. The Final Act embodying them was signed by 124 countries (the membership of WTO has since risen to 128 as of December, 1996) in the Moroccan city of Marrakesh on the 15th of April, 1994 and the agreement establishing the World Trade Organization (WTO) entered into force and, was accepted as a whole on the 1st of January, 1995. The ministers signing the Final Act expressed the view that the conclusion of UR would strengthen the world economy, lead to more trade, investment, employment and income growth throughout the world. It was also hoped that rule of law would prevail in international economic and trade relations.

The UR provides the basis for the removal of direct trade barriers through lowering tariffs and quantitative restrictions (QRs) for both manufacturing and agriculture, enhances market access and integrates trade in textiles, clothing and agriculture into established GATT rules and disciplines. In addition, it clarifies rules and regulations with regard to safeguards, subsidies and antidumping actions, customs valuation, state trading enterprises and technical barriers to trade and strengthens measures taken on balance of payments grounds and the dispute settlement mechanism.

The Final Act of the UR is fully binding on the signatory countries and any violation of its provisions could attract retaliatory actions by affected trading partners. The UR constitutes a single indivisible undertaking in that all the agreements have to be complied with by the signatories. The results of UR have been pieced together under GATT 1994, consisting mainly of the provisions of GATT 1947, as rectified, amended or modified, as well as the Marrakesh Protocol to GATT 1994. The results of the UR will be overseen by the newly set up WTO.

This paper would seek to analyze the effects of the UR on the economy of Bangladesh by looking at —

(i). the impact of the UR on the country's revenue earnings and protection of domestic industries as a result of the reduction of tariff and non-tariff barriers by Bangladesh;

(ii). the possible increase in market access for Bangladeshi products in other countries following the reduction of tariffs and non-tariff barriers by the latter;

(iii) the possible increase in Bangladesh's import bills consequent upon the reduction or elimination of production and export subsidies in the advanced countries and

(iv). the impact on domestic policies relating to investment, intellectual properties and services and their implications in terms of cost of production, output, employment and the country's trade balance.

This paper would analyze the implications of those key UR agreements which are considered important for Bangladesh. The paper would also discuss the opportunities as well as the challenges an risks posed by the UR for Bangladesh and other less developed countries.



***Tariff Reduction:***

The emphasis on tariff reduction was lower in the UR compared with the previous rounds of MTN as the average tariffs on manufactures in developed countries were already reduced to very low levels in the previous rounds with relatively higher tariffs concentrated in sensitive areas only. The UR provides for enhanced and more certain market access through greater tariff bindings. By binding a tariff rate at a specific level, a country commits to keep the tariff rate within that level. Bindings contribute to certainty and predictability of a county's trade regime. This is thus expected to facilitate greater stability to trade and investment decisions.

The UR provides for a major increase in market access security through higher levels of tariff bindings i.e., from 78 percent to 99 percent for the developed and from 22 percent to 72 percent for the developing countries. The developed countries have committed to reduce tariffs by 38 percent from 6.3 percent to 3.9 percent. The value of imported industrial products that receive duty free treatment in developed countries increased from 20 percent to 43 percent and the proportion of imports into the developed countries, subject to peak tariffs is expected to decline from 7 percent to 5 percent. Considerable progress has also been made towards reducing tariff escalation, thus creating enhanced scope for the export of more processed primary products.

Under the UR, Bangladesh has bound the tariff rates on certain industrial goods. As the operative rates in these cases are lower, this will neither reduce the level of protection nor revenue for Bangladesh. As a matter of fact, in recent years, in the context of its unilateral liberalization efforts Bangladesh has both reduced its tariff rates and removed non-tariff barriers quite significantly. Since in all probability such actions are irreversible, it seems that Bangladesh could even think of binding its tariffs at their respective operative levels without in any way jeopardizing its interests of revenue and protection. Such actions would not only impart stability and predictability with regard to the country's trade policy regime, these would also give a more positive signal to the outside world with regard to Bangladesh's preparedness to more fully integrate into the global trading system.

***Agriculture:***

Agriculture has always been considered special for socio-economic and strategic reasons. Historically, the performance of agriculture has been seriously affected by massive economic distortions. In some cases farmers have been artificially encouraged to produce more while, in other cases they have been rewarded not to produce at all or produce less. These resulted in the ballooning of production subsidies, increase of import barriers and rapid expansion of export subsidies. In general, agricultural protection has been an extremely costly business. Moves to reform agriculture faced serious obstacles as the subsidies spawned powerful vested interests. The concerned negotiating countries therefore began to seek long term reform in agricultural trade and domestic policies in terms of large reductions in export subsidies and commitments to reduce internal price supports and import barriers.The agreement on agriculture involves (i) tariffication (ii) tariff reduction and (iii) market access in general.

Under tariffication, all QRs are required to be eliminated and replaced by tariffs. Like other developing countries, Bangladesh bound the tariff rates for most of the agricultural products at 200 percent, except for a handful of items where tariff bindings were set at 50 percent. In addition, Bangladesh set another rate of 30 percent as other duties and charges for all agricultural products. The above tariffication would no doubt enhance transparency to some extent but there is no question of increasing any market access as the operative rates are already set at much lower levels.

Like other LDCs, Bangladesh is not obliged to reduce tariffs and production or export subsidies for agriculture. Thus there is no loss of protection or revenue or reduction of export potentials for Bangladesh on these accounts. It is however apprehended that the reduction in subsidy on agricultural products in other countries would lead to an increase in food prices for a net food importing country like Bangladesh .

In agriculture, the developed countries are required to reduce over six years, their (i) tariffs by an average of 36 percent with a minimum of 15 percent for individual products (ii) domestic support by 20 percent (iii) value of direct export support by 36 percent below 1986-90 base period level and (iv) volume of subsidized exports by 21 percent. The developing countries will reduce over 10 years, by 2/3rd of those for the developed countries.

***Textiles and Clothing:***

Trade in textiles and clothing, has been subject to special restrictions imposed by the main importers, for protecting their own domestic industries from 'market disruption' by lower cost suppliers from the



developing countries. As a result , the Multi fibre Arrangement (MFA ) came into existence in 1974, under which around 50 percent of textiles and clothing trade came to be regulated through bilateral quotas. This managed trade has however been a major derogation from the GATT principle of non-discrimination.

Under the agreement on textiles and clothing, which was an extremely hard fought out package of agreement, the MFA quotas would be eliminated in phases over a 10 year period. After 2005, for all signatories to the UR, textile trade rules would revert to the general GATT rules applicable to trade in goods. The phasing out of MFA would follow the schedule shown below:

| Schedule | Total import value of 1990 calculated by H.S. codes |
|---|---|
| On 01 January 1995 | 16 percent |
| On 01 January 1998 | 17 percent |
| On 01 January 2002 | 18 percent |
| On 01 January 2005 | 49 percent |

In the intervening period the remaining quotas would be expanded in the following manner:

| | |
|---|---|
| First 3 years | Quota will grow by 16 percent |
| Next 4 years | Quota will grow by 25 percent |
| Next 3 years | Quota will grow by 27 percent |

It is well known that a sizable garments industry has developed in Bangladesh over the past 15 years in response to the MFA. Garments exports from Bangladesh to North America face MFA quota. But there are no such quotas for Bangladesh in the European Union (EU) although quota is applicable to garments exports from other countries to the EU. Exports of garments accounted for 64 percent of total exports in 1994-95.Thus, the Agreement on Textiles and Clothing will have important impact on Bangladesh's overall export performance.

An examination of the schedule of quota elimination shows that bulk of the quota would be eliminated towards the end of the 10 year period. In addition, the growth of the quota during the intervening period would mean that Bangladesh's market share into North America would increase progressively up to the year 2005. As there is no quota for Bangladesh's garments exports to the EU, the gradual elimination and growth of MFA quota will mean that the market share in EU of other countries may increase leading to a corresponding shrinkage of Bangladesh's share in EU market up to the year 2005. Overall, Bangladesh's exports of garments are however expected to increase up to 2005. For the period beyond, the price of garments in the importing countries would decline with the removal of quota leading to increase in demand. This will probably reduce per unit price received by the exporters as there will be no quota rents, but the market will widen although there will be more competition. Bangladesh will thus have to maintain its price competitiveness by containing the costs of production and enhance its supply capacity especially through developing backward linkages if it has to maintain its exports of garments at high levels. Conducive environment will have to be created for producing fabrics and other materials used in the garments industry at reasonably low costs because, in the absence of the MFA quota, it would not be cost effective to compete with other producers if Bangladesh has to rely on imported fabrics and other materials. Since Bangladesh has virtually the lowest unit labor costs in garments among the South Asian countries, it does not seem to be a difficult proposition if a supportive policy environment is available to the Bangladeshi garments exporters.

On the other hand, the phenomenal growth of RMG (under the MFA) in Bangladesh has served a very important purpose for the country. It has provided the country with a large pool of efficient entrepreneurs, well trained in running export industries and conducting international trade. This is certain to have a positive spillover effect in the country's efforts to diversify its exports. Should the prospects for RMG exports of the country become any less promising in the post MFA era, at least a part of these dynamic entrepreneurs could branch out into other areas of export activities and contribute in a major way in increasing the export earnings of the country.

***New Areas:***

The UR has extended the agreements to include new issues such as trade in services (GATS), trade related investment measures (TRIMs) and trade related aspects of intellectual property rights (TRIPs). The important factors that have generated the demand for GATT disciplines in these areas are: internationalization of economic activities, linkage of domestic policies and global competitiveness, rapid increase in foreign direct investment and the globalization of services.



***General Agreement on Trade in Services (GATS):***

GATS provides for a set of multilateral rules for the conduct of trade in services like banking, insurance, telecommunications, tourism, transportation, hotel, restaurant, cinema, television etc. GATS in fact seeks to expand market access for trade in the above and other services. Services could be delivered internationally by supplying services from across the border (e.g. television), supplying services in the territory of one country to the consumers of other countries (e.g., tourism), providing services through the presence of a commercial entity of one country in the territory of any other country (e.g. banking) and providing services by nationals of one country in the territory of another country (e.g. construction projects). The national treatment rule (non-discrimination between local and foreign service renderers) and the MFN (non-discrimination between two trading partners) will apply in case of GATS for all signatories.

Trade in services has grown very fast over the last decade. Thus the share of services in global trade grew from 17 percent in 1980 to 22 percent in 1992. In case of Bangladesh however, trade in services relative to total trade decreased in the recent years.

It is important to make specific commitments on market access in respect of GATS. According to a study on GATS, Bangladesh has made specific commitments in respect of 4 out of 620 possible commitments. The number of commitments made by Bangladesh is 0.7 percent of total possible commitments compared with 21 percent by India and 17 percent by Pakistan. Since opening up of the service sector under GATS seems to be potentially beneficial to the domestic service export sector, Bangladesh could examine the possibility of greater liberalization of its service sector with a view to enhancing its service capacity and improving efficiency and competitiveness in the provision of services.

***Trade Related Investment Measures (TRIMs):***

The agreement on TRIMs relates to the avoidance of trade restrictive or distorting effects of investment measures. It aims at facilitating investment across international frontiers for increasing economic growth of all trading partners. The TRIMs are regarded as a form of protection that artificially reduces imports, encourages inefficient domestic production and thus adversely affects the balance of payments of the countries of the potential investors. Examples of such TRIMs are local content requirement, trade balancing requirement and export performance requirement. The developing countries quite often employ stringent foreign investment restrictions mainly on developmental grounds. The TRIMs agreement was therefore of vital concern to them.

Under the TRIMs agreement no member can impose any measure which is inconsistent with the provisions of Article III (national treatment) or Article XI (elimination of QRs). Thus, a member country shall not make any discrimination between a local and a foreign company i.e. between local and foreign capital. The foreign investors will not be under any compulsion to buy raw materials from local sources. There will also be no QRs on the import of raw materials from other countries by them and this shall not be related to their levels of exports. In addition, the foreign investors will be under no obligation to employ local nationals and they can remit the entire amount of profits after tax. The ownership of foreign companies may also be fully controlled by them.

As an LDC, Bangladesh will have a moratorium of 7 years with regard to the application of TRIMs compared with 5 years for the developing and 2 years for the developed countries. Like other LDCs, Bangladesh will enjoy certain exemptions from the application of national treatment and elimination of QRs specified in the previous paragraph. These would include the imposition of trade restrictions for balance of payment purposes or for the protection of infant industries. However Bangladesh has already introduced a series of measures for liberalizing foreign investment. The TRIMs may, in the ultimate analysis contribute to increase in investment by removing existing bottlenecks in the country's investment regime.

***Trade Related Aspects of Intellectual Property Rights (TRIPs):***

The agreement on TRIPs relates to the establishment of rules for protecting patents, trade marks, copyright, geographical indicators, industrial designs, trade secrets and lay out designs of integrated circuits. The UR put in place new regulations and disciplines in the GATT for setting higher standard of protection of intellectual property rights by underscoring the link between trade measures and the enforcement of these rights. It has long been argued by the holders of these rights that because of the absence of effective and adequate protection, they are losing huge amounts of money in terms of foregone income i.e., the balance of payments positions of their countries would improve considerably if they received their due fees, royalties and charges on the use of their intellectual properties in



other countries and also if the import of the right protected products into other countries were not reduced because of right piracies in these countries.

The agreement on TRIPs also covers importation of counterfeit trade mark or copy right pirated goods. The TRIPs will provide protection to intellectual properties in the following way:

***Patent :*** Protection of both product and process patents will be extended to 20 years from the date of filing. The patent holder will thus reserve the rights to the use of patented process or product, for that long a period.

***Copyright :*** Items like computer software and books would be protected under the copyright law. The producers of sound recordings and films will receive protection under the rental rights.

Trade marks: These will be protected up to 7 years. The protection will be renewable after every 7 years at the option of the holder of rights.

***Industrial design :*** Protection will be available up to 10 years.

***Geographical indicators :*** Protection of goods against misleading origin will be available.

***Trade secrets :*** Misappropriation and unauthorized use of trade secrets would be protected.

Impact of the changes under the TRIPs may be unfavorable to Bangladesh. Since, on balance, Bangladesh is an importer of technology and knowledge based products, it will have to pay higher prices for the protected products. Access to modern technology will obviously become costly. The effects may be particularly pronounced in case of medicines, agricultural seeds, insecticides, computer software etc. The TRIPs may particularly constrain the productivity of domestic agriculture. As at present we do not have the right to any knowledge based product or process, there is no way we could derive rents on their uses by others. In order to be able to do so, it would thus be essential to invest heavily on indigenous R&D activities in the country.

As an LDC, Bangladesh has 10 years moratorium on the application of TRIPs. The developing countries will have 5 years to give effect to the TRIPs. The national treatment (non- discrimination between a local and foreign rights) and MFN provisions (treatment extended to one trading partner to be extended to all other trading partners) shall however be implemented by January 01, 1996.

***Other relevant agreements for Bangladesh:***

In addition to the agreements discussed above, the following agreements are also important for Bangladesh:

Agreement on Valuation of Imported Goods: This agreement envisaged the abolition of the concept of normal value (Brussels Definition of Value) presently employed by Bangladesh Customs for the valuation of imported goods and the introduction of the concept of transactions value (GATT Definition of Value) by the year 1999. It also requires the elimination of the tariff value system presently in force. Both these measures have Important revenue significance for Bangladesh at least in the medium run.

**Trade Policy Review Mechanism:** This is designed to contribute to improved adherence to rules, disciplines and commitments made under the MTN for achieving greater transparency and understanding of the trade policies and practices of the signatories. The most important function of the review mechanism is to examine the impact of a member country's trade policies and practices on the multilateral trading system. As a member country, Bangladesh is also mandated to carry out regular Periodic eview of its trade policies.

**Agreement on Dispute Settlement:** This would provide for setting up of panels, adoption of rulings by the panels and the authorization of corrective measures. For the settlement of trade a simplified procedure would be followed in case of Bangladesh and other LDCs.

**Agreement on Antidumping:** The agreement provides for the protection of domestic producers against predatorily priced imports. Clearer rules have been framed to prevent unpredictability and avoid abuse of antidump- ing measures. An agreed methodology for calculating dumping margins has been worked out and strict time limits have been defined between initiation and final determination.

**Agreement on subsidies:** Like other LDCs, Bangladesh is exempt from the prohibition of export subsidies. But Bangladesh (and other LDCs) is required to phase out subsidies on the use of domestic inputs over imported inputs within 8 years.



***Market Access of Bangladesh Goods in Trading Partners***

***Tariff Reduction:*** According to a study on market access, tariffs in developed countries will reduce by more than 2 (affecting 81 percent of total exports to developed countries) percentage points and those in selected developing countries by 6.1 (affecting 20 percent of total exports to selected developing countries) percentage points for the exports from Bangladesh. The reduction of tariff rates for Bangladesh's exports of agricultural products to developed and developing countries will be 3.5 (affecting 58 percent of agricultural exports) percent and 6.2 (affecting 33 percent of agricultural exports) percent respectively. For textiles and clothing, rate reduction will be respectively 3.9 (affecting 64 percent of garments exports) percent and 6.0 (affecting 26 percent of garments exports) percent. The decline in tariffs will help Bangladesh expand its exports. But the reduction may also mean some trade dislocation because of increased global competition.

The reductions of Most Favored Nation (MFN) tariffs will reduce prices in the importing markets and increase total import demand. However, for markets where Bangladesh already faces zero tariffs the reduction will not have any trade creation effects. The MFN reduction of tariffs in importing countries will mean erosion of GSP (Generalized System of Preference) margin on Bangladesh's exports (if it enjoys this facility there) , leading to a possible loss of market share and consequent loss of exports.

***Removal of QRs:*** Before the UR, Bangladesh faced quite high QRs in the developed countries, compared with its South Asian neighbours. With the conclusion of UR, the situation is going to improve quite significantly. Thus, according to the above study, the coverage under QRs for all exports from Bangladesh will reduce from 58 percent to 11 percent. For manufactured goods, the coverage will reduce from 74 percent to 13 percent. Thus, UR will create a good opportunity for Bangladesh to expand its exports to the developed countries. In order to exploit this opportunity, Bangladesh would need to expand its supply capacity, improve competitiveness and enhance productivity in respect of different export items.

The barriers to exports from LDCs like Bangladesh to the developed countries are still high in many cases. For enhancing market access possibilities, it is essential to promote export diversification and strengthen export base in Bangladesh. It is also essential to improve both human resource and institutional capabilities of the country for the promotion of exports. This would require both technical and financial support from the developed countries at least for some years to come. It is also necessary to improve labor skills and infra structural facilities in the country.

***LDCs' prospects under UR:***

In recognition of the plight and the special needs of the LDCs, the developed countries reaffirmed their commitments on differential and more favorable treatment of the LDCs in the UR negotiations. A separate decision in the UR was made on measures in favor of the LDCs. This decision provided that although the LDCs would be required to comply with the general rules set out in the different UR agreements, they would only be required to undertake commitments and concessions to the extent consistent with their individual development, financial and trade needs, or their administrative and institutional capabilities.

***It was also agreed in the UR that :***

I. all special and differential measures taken in favor of the LDCs would be expeditiously implemented;

II. as far as possible, agreed MFN concessions on tariff and non-tariff measures on products of export interest to the LDCs would be implemented autonomously and without staging.

III. considerations would be given to further improve GSP and other schemes for products of particular export interests to LDCs.

IV. the rules set out in the various agreements, instruments and transitional provisions in the UR would be applied in a flexible and supportive manner for the LDCs. To this effect, sympathetic consideration would be given to specific and motivated concerns raised by the LDCs in the appropriate councils and committees for the different agreements and

V. LDCs shall be accorded substantially increased technical assistance in the development strengthening and diversification of their production and export base including those of services as well as in trade promotion, to enable them to maximize the benefits from liberalized access to markets.



It was expected that the progressive implementation of the results of the UR as a whole would generate increasing opportunities for trade expansion and economic growth for the benefit of all participants . However, in the UR negotiations, it was recognized that the greater liberalization of the trade in agriculture might have negative effects in terms of the availability of adequate supplies of basic foodstuff from external sources, including difficulties in normal levels of commercial imports of basic foodstuffs for certain countries. Under the circumstances, it was agreed to develop mechanism to maintain the availability of food aid at a level sufficient to finance the food needs of the developing countries, especially the LDCs and the net food importing countries . It was also agreed to establish institutional financial facilities (if they did not exist already) to alleviate the short-term difficulties of the developing countries in financing their normal levels of commercial imports.

The UR required the LDCs only to make symbolic commitments so as to register a sense of belonging to the UR negotiations, although they were accorded notable concessions under different UR agreements (one might however note the overwhelmingly qualitative nature of these concessions, implying difficulties in their compliance). The UR provided considerable flexibility in case of some, and longer transitional periods, in case of a number of agreements in respect of their application to LDCs. This is designed to let the LDCs develop their capacity for eventually enabling them to compete globally.

The UR has thrown up both tremendous challenge and opportunities as well as generated a lot of anxieties for the LDCs. It has also exposed the countries with weak domestic policies to considerable risks. At the current state of affairs, these countries are not well posed to derive any meaningful benefit from the UR, because of their limited capacity to participate in the global trade with their very limited range of tradable products and difficult constraints on the supply side. These countries also have poorly developed administrative and institutional capabilities. As in the case of sustaining the countries own development efforts, these capabilities are not strong enough to ensure due observance of the new rules and disciplines introduced by the UR. Even the administrative costs of fulfilling the obligations under the UR might prove burdensome for some of the LDCs.

In general, the LDCs are expected to suffer in the immediate future, in respect of erosion of preference margins, higher import prices for food, pharmaceuticals and machinery. According to different estimates, the collective short run annual losses for the LDCs are expected to be quite large. It has been argued that for protecting them from being marginalized, these countries would need financial support from the developed countries at least up to the medium run. But in this context it has to be borne in mind that the capabilities (and willingness!) to provide financial support to the LDCs are fast on the decline. There are also more candidates now for a much reduced sum of external assistance. Thus the conclusion of the UR negotiations might also have served an important message to the LDCs that time has finally come for them to take full charge of themselves.

In fact, in the first WTO ministerial conference held in Singapore during 9-13 December, 1996, it was argued that the LDCs are already having serious problems of integration into the multilateral trading system. It was pointed out that the developed countries are paying only lip service to the need to help out the LDCs while failing to follow up their words with action. It has also been pointed out that although trade preferences of these countries are eroding, promised compensations for the adverse effects of liberalization have not been forthcoming. The view of the WTO that benefits of trade will trickle down to the LDCs as they open up their economies and adopt market oriented policies has also come in for criticism. Thus, the eleventh hour decision on the part of the developed countries to boost the world's 48 poorest countries has generated limited optimism, at best. In fact, the action plan adopted in this context only proposes (but does not require!) that the developed countries explore ways for giving preferential market access to the LDCs. Thus, the plans to help these nations by giving them duty free access to developed countries were also watered down.

During the above conference, certain Non Government Organizations (NGOs) based in the developing countries have stated, in the same vein, that it was a myth that trade liberalization was good for everybody. They argued that poverty was spreading despite trade liberalization and demanded fairness in the world trade rules. They also argued that the poorer countries should be given more flexibility in time and policies to enable them to adjust to the rapidly changing global trading environment. They were also severely critical of the developed countries' attempt to add new items (like labor standards, investment and competition policies and government procurement), onto the WTO agenda as this would needlessly overload the trade system. They argued that the WTO



should instead concentrate on resolving problems liberalization has caused for the poorer countries. They called for prompt and effective remedial measures for redressing the imbalances of the UR. To their dismay however, the developing countries noticed that during the above conference, far too much time was spent on the so called new issues and too little on the problems of implementation of UR agreements.

Since the UR has left the LDCs virtually to fend for themselves, they have no choice but to work harder, design well thought out reform programmes, restructure their economies, reduce their wastage and leakages and quickly improve efficiency, both in the public and the private sectors. The transitional period has provided some respite for them, however. The LDCs could try to best utilize this period to rapidly develop their capabilities and abandon their undignified status of being LDCs. For, UR or no UR, these countries need to develop quickly in their own interest. This would no doubt involve making hard decisions on their part, specially that of their governments: in many cases, this might require reaching difficult political consensus to push through the desired reforms and balancing conflicting interest groups.

Looked at from another angle however, the UR has thrust upon the LDCs an opportunity to interlock their own development efforts needed to improve upon the present highly dismal living standards of their peoples, on the one hand and the reforms mandated by the UR, on the other. One could identify many points of intersections between them. These countries could thus utilize this opportunity to carry through long pending reforms in the areas of land ownership, finance, privatization, private sector development and downsizing the government. The UR could as well give them an opportunity to mobilize opinion and support to implement difficult reforms. For this, the LDCs could also endeavor to make the full implications of UR agreements transparent to their peoples. Rather than remaining in the dark, it would be much better if the people knew these implications. That way, the UR could be looked upon as a blessing in disguise for the peoples of these countries.

### *Conclusion:*

Studies by the GATT economists indicate that world income would grow by US$ 235 billion annually and there would be a trade gain of $755 billion annually, by 2002. The gains would be directly proportional to the degrees of liberalization of different countries.

Studies also show that developed countries would be the biggest gainers followed by the relatively advanced developing countries. For the LDCs, some may gain or lose a little more than the others depending on the relative change in opportunities for them in the wake of the UR.

The post UR life may be very different for the peoples of the LDCs. The full implementation of UR will have profound influence on their lives, their thinking patterns and their ways of doing things. For better or worse, the UR is going to expose the LDCs to a more difficult and challenging life. If the LDCs can live up to this challenge, they can surely survive in the assembly of nations with more dignity and honor. If not, they might gradually slip back into the primitive age, through a reverse process (also built into the UR?) of underdevelopment! The message therefore is: hard work, self reliance — and progress.



# *Value Added Tax in Operation : A Bangladesh Perspective*

SAIFUL ISLAM KHAN

### *The Questions We Face*

It is fashionable these days to talk about, and even to pass judgments on a topical subject the Value Added Tax. But what, in fact, is Value Added Tax or VAT? How does it affect us - the general public and the trader - in our day to day life? What effect is it going to have on the economy and the revenue earning of the state? Is it at all desirable to continue to keep alive the VAT statute in our context ? Have we been subjected to it at the right time and at the right stage of our development? All these questions continually agitate us. Answers to most of these questions can be found in the vast wealth of literature on the subject which, however, is not easily accessible to the general public who are ultimately affected by it. But the answers can also be found in the real world functioning of the system locally and globally.

The global situation testify clearly to the acceptability and efficacy of the system in a variety of cultures so much so that beginning in France some time in the early sixties VAT is now the major taxation system in 80 countries across 7 continents. More and more countries in the developing world are adopting the system as an ideal tool for internal resource mobilization to meet the ever increasing demands of development. It was introduced in Bangladesh in 1991 FY and was made operative at the importation and manufacturing levels only. Is it VAT at all or VAT proper? Should we keep it at this level for some more time or move forward to distriof prices other than the effect of normal inflation owing to growth and expansion of the economy. As far as the prices of food are concerned, the rise does not reflect the effect of Value Added Tax because the entire agricultural sector is outside the tax net.

### *The Real Picture*

However, if we take a closer look at the composition of Value Added Tax yield in the domestic sector, we find a rather dismal picture . Of the total tax yield from VAT/SD the cigerettes contribute 35%, Gas 28%, construction 7%, telephone bills 3%, and all other 27% . The dynamics of composition of VAT/SD since FY91-92 reflect a rather static situation and confirms the existence of an extremely narrow-based VAT so much so that more than two-thirds of the economy is outside its jurisdiction and, of the one -third within it, the full potential is still not properly tapped. Most of the services, for example, are outside its scope. One of the fastest and largest growing sectors ( transportation ( is totally outside the VAT net . Most of the professions are still not Vatable . And, even worse, there are allegations of large scale evasion within the existing system. In this country the market is still a seller's market and the consumers are neither organized nor is there a law to protect their interests. The burden of indirect taxes, VAT being one, are ultimately borne by the consumers and yet it is the sellers who put out the loudest protests against any move to expand the Tax base. Why?

### *The Problems*

The overt objections mainly centre round the alleged propensity to rent seeking of not only the tax officials but also other agents of the law enforcing and service providing systems of the Government. There are on the other hand, clear evidences of large-scale, and sometimes, organized evasion by businesses in general. The covert objection, from one kind of the business emanate from a fear of paying proper income taxes as a result of accepted standardised record keeping in an imperfect market mechanism where the honest tax payer is more often than not subjected to all kinds of harassments and forced rent seeking. The other kind among the tax payers take advantage of enforcement of weak situation and seek to evade tax with impunity. This locks the entire system into a torpor and its net result is much lower than optimal collection of revenue. This does not benefit either the producers of goods or services or the consumers in the long run. This is due to the fact that lesser revenue means lesser infrastructural allocation resulting in lesser and qualitatively inferior products for the consumers which pressurise the prices of local manufactures to go up. One of the fallouts of this situation, especially in the bankdrop of the geopolitical realities that we live with, is a strong upward swing of smuggling and undervaluation of imports affecting the entire economy adversely decelerating growth in general. So there has to be a collective decision as to whether we want the situation to change. The essential pre requisite of it is, of course, a political will. But that certainly is not enough. It also requires a public consensus on the issues involved and the responsibility of it has to be shouldered by the leaders of the trade and industry and the leaders of the civil society. There cannot be any progress and development unless we come face to face with the fundamental decision as to whether we need a clear transparent tax administration and transparent clientele i.e. tax payers. We are now in a situation where the tax



payers are accusing the tax administration of rent seeking and tax administration is accusing the tax payers of blatant evasion. The cycle goes on and on and no reform can take place in such an atmosphere. Our national saving is deplorably meagre even in the context of a developing economy and tax effort is one of the lowest in the world which means that were are one of the least taxed countries also. Over and above that due to the rising expendeture of the government there is a continuious increase in the borrowing of the government from the banking and private sectors. If the pace of development is to improve and to reach a sustainable level then there is no option but to raise our tax revenues substantially and quickly. Luckily we have already opted for the VAT system. If we now want to jump start considerable improvement in the direct taxes an expanded VAT base is the answer. This contention is validated by the experiences in such South East Asian countries as the Philippines and Indonesia and now, notably, China where direct taxes have registered substantial growth following the introduction VAT upto the retail level. VAT is a Taxation system that hovers between the direct and indirect taxes in a way that it uses the techniques which are common to both. Particularly the type (subtractive-indirect) that we have adopted, if expanded upto the distributions, will invariably result in boosting up the direct tax yield as a profitable offshort.

### *The System*

If we decide that there is in fact a need to improve the situation we must diligently implement a proper VAT system without delay. VAT is considered to be the most ideal system of taxation. From the resource-allocation perspective, it is an optimal form of tax system which is trade-neutral and which generally avoids tax on tax i.e, the cascade effect. Its operation is also comparatively simple a may be illustrated with an example.

Let us consider the case of a an imported car. If its price inclusive of customs duty is Taka 2,00,000, then the amount of VAT paid at the importation stage is Taka 30,000 making the total duty and VAT inclusive price Taka.2,30,000. It may be recalled that in Bangladesh VAT is charged at a flat rate of 15 % ad valorem. Now the local sale price is supposed to be fixed in a way so that the entire import VAT is passed on to the next stage in the distribution system which continues until the entire tax liability is shifted to the consumer. If the importer of a car is a dealer he has to first decide what price to charge to his customers. Needless to say the selling price will have to be competitive in relation to that charged by other dealers so that the margin for adjustment is limited.

The second factor to be quite clear about is how the VAT due on the sale is to be determined. A car dealer who is registered for VAT knows that the VAT system will enable credit to be taken for the VAT paid at the time of importation. He also knows that, as a VAT-registered trader, he must account for VAT on the full price charged to the customer for the car.

So how does the dealer set about deciding what his selling price should be to leave him with a profit margin of Tk. 50,000 (which happens to be 25% of the VAT - exclusive price of the car at importation)? There are two ways of doing this.

First of all by using tax-exclusive price eg. ;-

| | |
|---|---|
| Price at importation (without VAT) | TK. 2,00,000 |
| Gross Profit margin | TK. 50,000 |
| Tax-exclusive selling price | TK. 2,50,000 |
| To which VAT @ 15% must be added | TK. 37,500 |
| Total price to customer | TK. 2,87,500 |

The total amount of VAT due on the sale to the customer is Tk. 37,500 of which Tk. 30,000 has already been paid at importation. The dealer then pays over the remaining Tk. 7,500 (Tk. 37,500 less the Tk. 30,000 paid at importation) when the car is sold.

The second way is to look at the tax-inclusive prices as follow :-

| | |
|---|---|
| The dealer paid at importation, including VAT | TK. 2,30,000 |
| If a gross profit of 25% is added | TK. 57,500 |
| The tax-inclusive selling price will become | Tk. 2,87,500 |

To work out the amount of VAT included in Tk. 2,87,500 a factor of 3/23 is used (this will be explained later) which produces an amount of VAT due on the sale of Tk. 37,500.

In this case also the dealer is able to take credit of the Tk. 30,000 paid at the time of importation and remit only Tk. 7,500 to the Government when the car is sold to a customer.

It will be noted that, in both cases, the resultant selling price is the same - as is the VAT due. In both cases the Government receives Tk. 30,000 at the point of importation and a further Tk. 7,500 when the car is sold. It should also be noted that the Tk. 7,500 represents 15% VAT on the profit margin of Tk. 50,000 (the added value). In the



second example the profit margin is still Tk. 50,000 because Tk. 57,500 includes the VAT.

The only difference in the two cases is the method of calculation and it is very important that a business man or woman does not mix VAT - inclusive and VAT - exclusive amounts.

One may ask why the VAT factor is 3/23. It is 3/23 because, as we have already noted, the rate of VAT in Bangladesh is 15 %. It is explained below:

$$\text{VAT factor} = \frac{(\text{VAT inclusive price} - \text{cost price})}{\text{VAT inclusive price}} \text{ or } \frac{\text{rate of tax}}{100+\text{rate of tax}}$$

$$= \frac{\text{Taka } 115 - \text{Taka } 100}{\text{Taka } 115}$$

$$= \frac{3}{23}$$

7-66

For example, if you sell something for Taka 100 and the rate of VAT is 15% the selling price becomes Taka 115, the amount of VAT being Taka 15. But Taka 15 is not 15% of 115, it is 3/23 of 115.

For the trader, it is convenient to calculate the VAT payable in the direct method illustrated above. For direct sale to the consumer our advice is that it is better to show the VAT inclusive price in the cash memo or the invoice so that the VAT factor may be applied. However, in the case of the car the amount of VAT may be shown separately if it is sold to another trader instead of a consumer. The assumption here is, of course, that VAT system and its innate adjustment mechanism is fully operational in a closed lap situation i.e. the entire cycle from importation to distribution must be completed

***What in fact is Value added Tax ?***

Value Added is the value that a businessman or a producer - whether a manufacturer, a hairdresser, an advertising agent or a restauranteer - has added to his raw materials or other purchases by the time he sells the product or the service .This means that he purchases things to operate his business , pays wages to workers who work on the inputs and when he sells the final product or service there must also be a profit left to him. All this adds up to become the added value. Therefore , Value Added can be shown in two different ways:- 1. wages and other operating costs + profits 2. output - inputs. The former is obviously the additive method and the latter is subtractive.

We can thus express the Value Added as follows :

**Value Added = Wages and other operating costs + Profits**
**= Output - inputs**

Now if a tax rate i.e. (t) is levied on the value added, it may be expressed in four different ways to arrive at the same tax yield. These are the following :

1. **t (wages etc. + profits )** : this is the additive , direct or accounts method;

2. **t (wages etc.) + t ( profits )** : this is additive-indirect method ; Here the Value Added itself is not calculated but only the tax liability on the components of value added i.e. liability on wages and profits is calculated ;

3. **t (output - inputs)** : this is the subtractive - direct method which is also called an accounts method and some country calls it business turnover tax ;

4. **t (output ) - t (inputs )** : this is called subtractive - indirect method or invoice or credit method;

The last one or the method four is now the most popular in the world. There are a number of reasons for that preference.

Most taxes are calculated by first determining the tax base wheather it is income, sales, wealth and property values etc. giving any statutory allounces and then applying a tax rate to that value. This is how the income tax is calculated .It may seem appropriate for calculating Value Added Tax as well .But in practice, the method 4 referred to above, the Indirect-subtractive method or the Invoice method has been found to be the most convenient for the consumption tax purposes, because consumption taxes actually tax goods and services.

The foremost convenience of the invoice method is that it attaches the tax liability to the specific transaction. Thus the invoice becomes the crucial evidence for tax liability unlike the other taxes in which case wages, profits etc. are calculated at a later date than the date of the actual transaction. This renders it technically far superior to other consumption tax, because it instantaneously taxes the goods and services consumed. In some countries therefore it is called Goods and Services Tax. This subtractive-indirect or Invoice Method also creates an excellent audit trail which starts with the



invoice itself.Thus the invoice becomes the crucial evidence for the transaction as well as for the tax liability.

In the account based method profits need to be identified. Company accounts do not usually divide sales by different product categories. They do not also divide inputs by differential tax liabilities . Thus in the additive method , one is necessarily restricted to a single rate tax. This method cannot handle multiple rates which some countries prefer or are necessitated to prefer at some stage of their economic history.

It may, therefore, appear that the easiest way to calculate a VAT using a subtractive methods would be the calculation of the value added (output - inputs ) and then to apply the tax rate to arrive at the tax liability. In actual practice, firms do not find it convenient to calculate their value added in this way month by month as purchases,sales and inventories can fluctuate greatly during the tax period. In the method 4 i.e. a invoice method the tax liability can be calculated week by week, month by month, quarterly or annually. It is, therefore, the method that allows the most uptodate assessments. It is also the clearest and the easiest method to calculate the VAT liability on each transaction.

***VAT Structure***

In an ideal situation, in its purest form, a VAT system should embrace the entire economy including all the service sectors and the agricultural sector as well. But in various cultures, in the real world situations, this ideal system does not really exist except, perhaps, in one country-New Zealand. Ideally there should be no exemptions and no multiple rates in order that the elimination of cascade effect can be ensured in its totality. In real world working of the system, the ideal situation is impaired due to various factors which are generally those other then economic. On social justice or equity grounds, many countries have to keep various sectors of economy outside the tax net. Thus in our country, the agricultural sector is completely exempted. Since this is a local consumption tax, for the sake of competitiveness of local products in the foreign countries, exported products are zero rated in order to remove the burden of local taxes and make exports more competetive. In many countries multiple rates are applied which again is distortive and does not allow full benefit to be reaped from the credit mechanism. Thus elements of tax on tax remain to some extent in very many cases. In spite of these distortions, Value Added Tax has proved to be the most trade-neutral and industry-friendly consumption tax if a credit method and a single rate is applied all along. Value Added Tax works on the principle that it starts from importation and runs through manufacturing to finally the distribution of goods and services. It has to start from import because from the time a good lands at the port jetty, the build-up of value added starts .And the import must be taxed in order to create the base from where to start. The build up of the value added from importation to distribution is demonstrated in the following simple example:

***Example of the operation of the VAT system from importation to the retail stage***

Importer

| | |
|---|---|
| Importers goods at duty -paid price of | Tk . 6,00,000.00 |
| pays VAT at import of 15% | Tk. 90, 000.00 |
| Tax -inclusive purchase price | Tk. 6,90,000.00 |
| At importation the government receives | Tk. 90,000.00 |

However the importer needs to make a profit. So he adds a 10% mark -up (Tk. 60,000)

| | |
|---|---|
| Before selling to a dealer (wholesaler) at which he adds VAT @ 15% | Tk . 660,000<br>Tk. 99,000 |
| Making his tax-inclusive selling prise | Tk.759,000 |

On his VAT return the importer shows VAT due as Tk 99,000 but can deduct the VAT already paid at import (Tk. 90,000) and he pays Tk. 9,000.

It will be noted that the Tk. 9,000 remitted by the importer at the time of sale to the dealer is equal to 15% on the mark-up of Tk. 60,000

Dealer (or wholesaler)
(Registered for VAT)

| | |
|---|---|
| Purchases the goods and adds a 10% mark-up to the tax -exclusive purchase price to cover the cost of running his business and to give him a profit. | Tk. 66,000.00 |
| So the tax-exclusive selling price is now | Tk. 7,26,000.00 |



| | |
|---|---|
| to which he adds VAT at @ 15% | Tk. 1,08,900.00 |
| Making the tax inclusive selling price | Tk. 8,34,900.00 |
| on his tax return the dealer shows VAT due | Tk. 1,08,900.00 |
| but can deduct the VAT paid to the importer which was | Tk. 99,000.00 |
| And remits to the Government | Tk. 9,000.00 |

It will be noted that the VAT actually paid by the dealer, TK.. 9,900/= is equal to 15% of the mark-up which was Tk. 66,000.00

Retailer (registered for VAT)

| | |
|---|---|
| Purchases the goods from the dealer and adds | (TK. 1,08,900.00) |
| a 15% mark-up to the tax-exclusive purchase price of the goods to cover the cost of running his business and to give him a profit. | TK. 8,34,900.00 |
| So the tax-exclusive selling price is now, to which he adds VAT @15% | TK. 1,25,235.00 |
| Marking the retailer's tax inclusive selling price to the consumer | TK. 9,60,135.00 |
| On his tax return the retailer shows VAT due but can deduct the VAT paid to the | TK. 1,25,235.00 |
| dealer/wholesaler which was | TK. 1,08,900.00 |
| And pays to the Government | TK. 16,335.00 |

It will be noted that the VAT actually remitted by the retailer, Tk. 16,335/= is equal to 15% of his mark-up which was tk. 108,900.00

In this example the Government has collected the full amount of the tax paid by the consumer (Tk. 1,25,235.00) in three stages.
Tk. 90,000.00 at the time of importation
Tk. 9,000.00 at the time of sale to the dealer
Tk. 9,900.00 at the time of sale to the retailer
and
Tk 16,335.00 at the time of sale to the final consumer.

This arithmetic clearly shows how at every subsequent stage the input tax paid previously by either the manufacturer or the wholesaler or the retailer is subtracted resulting in avoiding the cascade effect i.e, tax on tax. As would be easily perceived the Value Added Tax that now operates in Bangladesh is a rather truncated one since it has not been applied to the distribution or to sales by importers levels. It is only during fiscal 96-97 that some attempts have been made to expand VAT coverage by including a mumber of goods and services at a time in order that the entire sector of wholesale and retail levels of distribution is brought under it in a graduated manner over the next few years. This principle has been followed up in fiscal 97-98 as well.

***Effects of VAT on the Economy***

There have been a number of schools of thought with regard to the introduction of VAT system in a developing country like Bangladesh. It has sometimes been argued that being poor and culturally shy of keeping accounts /records the system is not really suitable for Bangladesh. The other side of argument is clearly to hold a position of static economy. In the backdrop of globalisation of the economy no nation can lag too far behind in creating a viable and rational economic system. It is bad argument to say that record keeping is too bothersome and should not be prescribed for businesses at distribution level. In reality even a small businessman has to keep some sort of records in order to run his business. It has also to be remembered that in every country there is a minimum threshold below which VAT is not applicable. Thus in Thailand, hawkers and wayside temporary small businesses upto a certain turnover are exempt.

If VAT has come before its time in Bangladesh, we might as well try to reap its benefits well so that it would be a progressive argument to say that the economy of the country may move forward in order to catch up with the outside world or at least the immediate neighbours. The introduction of VAT may very well be the beginning of evolving starting point for a transparent economy which we all know how badly we need. When the businesses get used to the transparency of the system , there will not only be a larger take of revenues from VAT alone, its immediate effect will also be reflected in the increased yield of income taxes making it difficult to avoid. There will thus be more stability and less fluctuations in the consumer market. With transparency in the system it will be possible to minimise rent seeking as well as propensity to evade. But is order to oftain that result we have to start somewhere.

That auspicious beginning was willy-nilly made in the year 1991. It now remains to complete the cycle by gradually moving towards the



logical completion of the system. The second significant break through has been consciously and boldly made during the fiscal 96-97 by extending it to the distribution levels, albeit, in a modest way which has been almost equally modestly followed up in fiscal 97-98 by including a few more items at the distribution levels. But in any journey in the path of a reform you can not afford to apply break abruptly in the midway particularly when it is an uphill path. This may very well spell disaster for the entire economic system of the country. In the context of ever increasing pressure of globalisation and shaking off the bondage of command economy it now remains with the people of Bangladesh to move forward with courage, determination and with faith in the future and the inherent resilience of the genious of the masses. In a situation where there is tremendous dearth of national savings, proper implementation of VAT system of taxation may very well work as a catalyst for bringing Bangladesh into the brave new world of the twenty first century.

## *Notes on Authors*

**Mr. Saiful Islam Khan** is a member of the Customs and Excise cadre of Bangladesh Civil Servicess. Born in 1942, he served as a teacher for about 3 years during the mid-sixties before being inducted into the Finance Services in 1968 of the then Pakistan Superior Services. He is one of the seniormost officers of the cadre and is now working as a Member of National Board of Revenue. Mr Khan is a widely published author on literary and technical subjects. He is considered as one of the most powerful literary personalities of the sixties and a serious literary and art critic.

**Dr. Zahid Hossain** has done his Masters and Ph.D. from the school of Economics, University of the Philippines. His specialized area of research was International Trade. Born in 1953, Dr. Hossain now works in the Ministry of Finince as an Advisor of the Asian Development Bank. He is a member of the Bangladesh Customs and Excise Cadre. He has widely published and attended a number of Seminars on fiscal policy and issues.

**Dr. Rafiqul Islam**, First Secretary (VAT Policy), National Board of Revenue, joined Bangladesh Civil Service: Customs & Excise in 1981. He earned his Master's Degree in Economics from the USSR in 1977. He taught economics at Dhaka University from 1978 to 1981. He earned his Ph.D. in economics from Holland in 1982. He also earned ITP certificate from Harvard Law School in 1987. He attended 'Information Technology' course jointly organised bythe Harvard University and Lincoln Institute on Land Policy in 1994. He attended a seminar on EDI jointly organised by Japan Customs and Tariff Bureau and World Customs Organisation in Nov-Dec, 1994. He held positions as Deputy Director, Training Academy; Deputy Director Research & Statistics, NBR and also Director of President's Secretariat.

**Mr. Gholam Hossain** is a member of the B.C.S. (Customs & Excixe) cadre and worked at various posts both in customs and excise and VAT. He has been the manager of the Automated Data Processing in Chittagong Custom House and a member of the team that implemented the automated system. He is now working as Director in the PM's secretariat on deputation.