

Continued Struggle in Bangladesh

VAT is Regressive to Poor

1. VAT is regressive to poor

Value Added Tax (VAT) is an indirect tax on the consumption of goods and services. It is imposed on a product or service whenever value is added at a stage of production and at final sale. The amount of VAT that the user pays is the cost of the product, less any of the costs of materials used in the product that have already been taxed. So, the burden of VAT falls almost entirely on the ultimate consumers.

Tax performance in Revenue mobilization

Fiscal Year	% of total revenue	
	Direct Tax	Indirect Tax
2000-01	19.40	80.56
2004-05	19.49	80.51
2008-09	27.17	72.83
2009-10	28.09	71.90
2010-11	29.49	70.51
2011-12	24.42	75.58

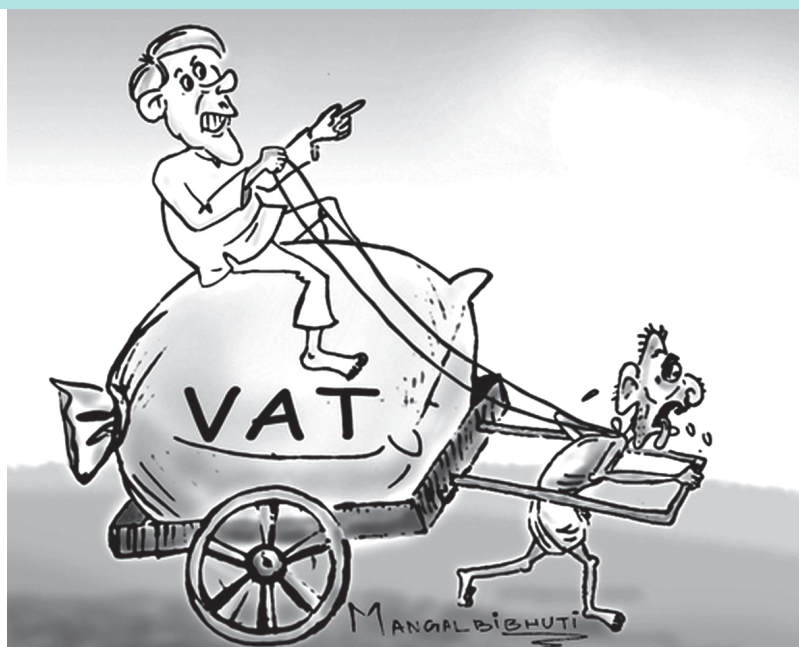
Source: National Board of Revenue, Annual Report 2011

The contribution of indirect tax in total revenue mobilization is 82% in FY91-92 and it is still as very slow pace (Stag at 75% in 2012) during last years despite bringing changes in taxation policy and system

In developing countries about two-thirds of the tax revenue comes from indirect taxes, mostly from VAT and others are from sales tax, excises and taxes on trade. The remaining one-third consists largely of corporate income tax. Tax revenue structure in Bangladesh can be divided into direct and indirect taxes. A direct tax is paid by a person to the revenue authority. Direct tax is borne by the tax payer and cannot be passed on to any person, whereas indirect tax is passed on by the tax payer so that the burden of the tax is ultimately borne by another. For example, Value Added Tax (VAT) which is passed on to the customers i.e. general people.

As per UNESCAP report "Economic and Social Survey of Asia and the Pacific 2014" the Tax-GDP ratio of Bangladesh should be 18% where at present it is 10.5%. This is how Bangladesh is losing more than one-third of the targeted revenue of amount is US\$ 10,641 million (BDT 830 billion) and it is the highest tax gap (more than 7.5%) percentage in the Asian countries. The tax gaps in other Asian countries are: Thailand-2%, Pakistan-1.8%, Nepal-0.9%, Malaysia-1.3%, Japan-2%, Indonesia-4.7% and China-1.8%.

VAT is regressive because it takes away a big portion of a poor person's income than that of a rich. Because low performance of income tax limits the asset transfer to the poor and on the other hand the high performance of VAT affects all sections of society equally and it creates a burden on the poor and ultimately causes income inequality between rich and poor in developing countries because of the high rate of inflation and caused by rapid government borrowing from different domestic sources.



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2. Preferring VAT: IMF and Government of Bangladesh

The heavy reliance on indirect taxation especially VAT has been treated as one of the main obstacles in attaining economic progress in developing countries. Presently more than 75% of total revenue collection (Revenue target FY2013-14: US\$ 17.70 billion) comes from the indirect tax where VAT is one of the major sources and easy to collect for revenue mobilization and the rest comes from personal and corporate income taxes. In fact, the government could not collect direct taxes i.e. personal and corporate taxes, due to their high skills of tax evasion. Recently a report says that four cell phone operators of Bangladesh evaded tax of amount US\$403 million in

Direct tax payers are few

The population of our country is about 150 million where the number of direct registered taxpayers is only 02 million even they don't pay their tax regularly. According to NBR (National Board of Revenue), only 0.8 million people are paying their tax on a regular basis.

Type of Taxpayers	Number of Taxpayers	%
Corporate	61,998	2.98
Other Taxpayers	778,750	37.53
Minimum Taxpayers	390,964	18.83
Only Tax File Holder	843,548	40.66
Total Tax Payer	2,075,260	100

Source: NBR Annual Report 2011

the name of SIM replacement where the British American Tobacco Bangladesh (BATB) evaded taxes of US\$ 250 million by false declaration of raw material import. Another study said that only 8 million people of the country out of the total 160 million are the owner of 40% of the country's total resource. But their contribution to the national revenue is only 11.15 per cent. The rest is provided by the general people, especially by the poor, through the indirect tax like VAT (Value Added Tax) imposed on almost all the items of everyday essential commodities.

The government of Bangladesh finalizes the new VAT Act 2012 to be applicable from FY2015 forced by IMF as a condition of a loan of about US\$1 billion under ECF (Extended Credit Facility). The new law proposes only one flat rate i.e. 15% will be added as VAT in every steps of the production of a commodity. The current range of VAT in Bangladesh is from 2% to 15%, which is already quite higher than that of other countries. In many countries some essential goods are exempted from VAT as it goes out of buying capacity of poor but the scenario is opposite in Bangladesh. Our government has imposed VAT even on all sorts of essential goods like rice, wheat, oil and also planned to expand the VAT at the retail level in rural areas which ultimately will create a hardship on the rural poor people.

3. VAT Impact on Income

Bangladesh is a poor developing country where 40% of people are living below the poverty line (earn less than \$2 a day according UN-MDG standard) and income inequality is high (0.36 according to gene-coefficient). The present exercise of VAT in absolute consumption level already has been creating burden over poor people and limiting the access in essential services related to human development and poverty reduction. Institute of Fiscal Studies-UK (IFS) has conducted a study on the price effect of VAT where they said that the VAT is always regressive for poor because this type of indirect tax impinges the poor and their livelihood as they have to spend most of their income for the essential goods than rich. The study also showed that the poor people are paying VAT (almost 20% of income) as double than the riches (almost 10% of their come) in UK due to the imposed VAT.

Other study showed that the VAT burden in the lowest income range is 6.92%, which is quite higher than that of highest income group, that is only 4.56%. The average effect of VAT rate is 6.01%, which is higher than that of the highest fourth income group. The higher income groups are enjoying fewer burdens than the lower.

Christian Aid in their report, "One size fits all-2009" mentioned that the Sub-Saharan countries in Africa had introduced VAT prescribed by MF that by next 20 years their Tax-GDP ratio will be boost up to 18%. But unfortunately most of the countries did not achiev this target which in turn did not change any livelihood of the countries rather increased the income inequality between poor and rich.

4. VAT in Bangladesh and Other countries

Bangladesh government has initiated Structural Adjustment Program (SAP) in 1985. Under this program, government has adopted the Tax Reform Program and the then VAT act was designed and approved in 1991 in the national parliament. The objective of introducing VAT system in Bangladesh was ensuring transparency in revenue system, stopping tax pilferage in the different layer of relevant production sectors and ensuring economic growth through mobilizing internal resources and finally increasing rate of tax-GDP. In the very beginning, VAT were introduced especially on some imported products and some businessmen having a turn-over of

more than 1.5 million BDT every year. Although in 1991, VAT was applied only on 21 products but now it covered almost all sort of products and services. Because, the main objective of VAT is to increase government's revenue by imposing VAT at imported goods, production and also in wholesale to retail level.

In Bangladesh VAT is being levied at the rate of 2-15% and is being imposed on different level of production, sale, import, retail and wholesale. The existing rate of VAT is quite higher comparing to the other developing countries. In Singapore, it is maximum 5%, Thailand 7%, Indonesia, Myanmar, Lebanon, Vietnam and south Korea have 10%, New Zealand 12%, and in Nepal it is 13%.

Conclusion

The world is now talking about post 2015 development on the basis of redistribution and justice. But there is no doubt, a tool like VAT for increasing inequality in the society will never let us to meet the target of development, nor to reduce the poverty.

EquityBD protest events on VAT and alternative recommendations for Internal Resource Mobilization

Sl	Title of the event	Date
1	Press conference on proposed budget FY2014-15, title: "Anti Poor Tax Policy in Budget 2014-15 denies Redistributive Justice"	22 June 2014
2	Human chain on "VAT is regressive to the poor: Demand pro poor internal revenue mobilization on next budget FY2014-15"	03 May 2014
3	Conducted Seminar at 07 divisions on "VAT is regressive to the Poor"	July-August 2013
4	National Seminar on "Domestic Resource VS Pro-Poor Revenue Mobilization"	October 2012
5	Conducted Seminar at 06 divisions on "Domestic Resource VS Pro-Poor Revenue Mobilization"	Oct-Nov 2012
6	Seminar on national budget 2012-13, National budget shouldn't use a revenue increasing tool ignoring the poverty reduction target : Emphasis on the direct tax and withdrawal stress creating new proposed VAT in national budget 2012-13	27 June 2012
7	Seminar on "internal Resource Mobilization and Pro-poor collection strategies"	6 June 2011
8	Seminar on "Taxation in Bangladesh: A Critical Look at VAT"	12 Jan 2011



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