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Practical Session:

Indirect taxes

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Edris Seid,
TaxDev Country
Adviser, IFS

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from the British people

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Trade TE

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Computing Trade TE using both approaches

Country A levies customs duty (on the CIF value of imports) and VAT (on the sum of the CIF value of imports and the customs duty payable).

- Demo data is provided.
  - contains detailed information on the CIF value, the actual collection of customs duty and VAT, and the statutory customs duty rate and VAT at the commodity category level
  - assume that import VAT TE is reported as part of the import TE.

Computing Trade TE using both approaches

Question I:

1) Calculate the TE under approach I

- ❑ Customs TE
- ❑ VAT Tax expenditure
- ❑ Summarize the results by 'SECTORS'

Approach 1: *Hint*

Direct VAT TE + IE of customs through VAT = VAT TE

- $\boldsymbol{VAT\ TE = Benchmark_{VAT} - Actual_{VAT}}$
- $Benchmark_{VAT} = VAT_{Rb} * (CIF + CIF * DUTY_b)$
- $Actual_{VAT} = VAT_{Ra} * (CIF + CIF * DUTY_a)$
- $Direct\ VAT = (VAT_{Rb} - VAT_{Ra}) * (CIF + Actual_{Duty})$

Computing Trade TE using both approaches

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Question 2:

1) Calculate the TE under approach II
   - ❑ Customs TE (both the direct and indirect tax TE)
   - ❑ VAT Tax expenditure
   - ❑ Summarize the results by 'SECTORS'
2) Compare the results under the two approaches

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Approach II: *Hint*

- The **DIRECT** customs duty TE arising from *customs duty exemptions* or *rate reduction* is given as:

$$Direct\ Customs\ duty\ TE = (DUTY_b - DUTY_a) * CIF\ Value$$

- The **INDIRECT** customs TEs arising through VAT is ;

$$IE\_Customs_{VAT} = VAT_{R_b}(Direct\ Customs\ duty\ TE)$$

- Similarly, VAT TE is

$$\boldsymbol{Direct\ VAT = (VAT_{Rb} - VAT_{Ra}) * (CIF + Actual_{Duty})}$$

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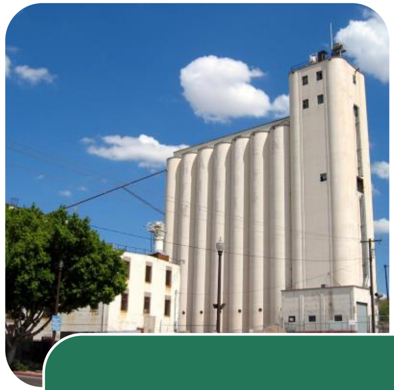
VAT TE

VAT TE

Suppose we have this simple VAT supply chain with a standard 15% VAT rate but wheat is VAT exempt

Farmer

produces wheat & sells it to the 'miller'



Miller

purchases the wheat and produces flour

Bakery

purchases the flour & produces bread

Consumer

buys the bread from the bakery

Practical Session II: *VAT TE*

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Question I

Farmer’s produce is VAT-exempt.

- *What does this imply for VAT collections across the supply chain?*

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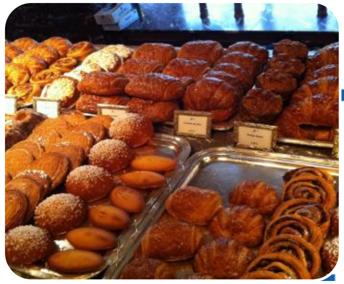
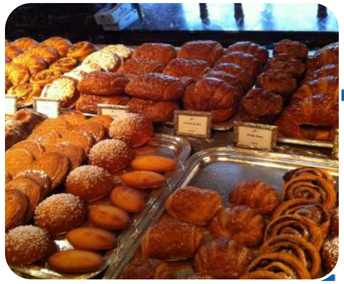
Wheat is VAT exempt



SALES	200	500	600
VAT charged on sales	0	75	90
VAT reclaimed by buyer	0	75	0
Net VAT on transaction	0	0	90

Wheat is VAT exempt



SALES	200	500	600
VAT charged on sales	0	75	90
VAT reclaimed by buyer	0	75	0
Net VAT on transaction	0	0	90

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Practical Session II: *VAT TE*

Question II

What is the key difference between exemption and zero rating?

- *Scenario a– Flour being VAT exempt*
- *Scenario b– Flour being zero-rated instead*

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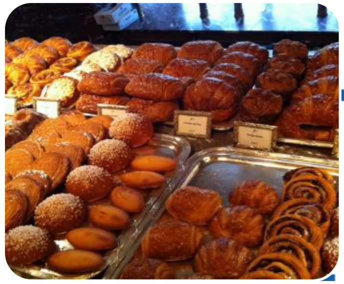
VAT across a supply chain – *flour being VAT-exempted*

SALES	200	500	600
VAT charged on sales	**30**	0	90
VAT reclaimed by buyer	0	0	0
Net VAT on transaction	30	0	90

The Centre for Tax Analysis in Developing Countries (TaxDev)
LinkedIn: @taxdev
Twitter: #TaxDev

www.taxdev.org

The Institute for Fiscal Studies
7 Ridgmount Street
London
WC1E 7AE

www.ifs.org.uk

The Overseas Development Institute
203 Blackfriars Road
London
SE1 8NJ

www.odi.org

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