

VAT: Composition Schemes

What is a composition scheme?

In order to relieve some businesses of the need to keep detailed records, the law makes provision for a simpler method of accounting for VAT. The method of calculating how much VAT is due to be paid is also made easier.

Such a method is called a composition scheme.

Who may join a composition scheme?

The alternative method of calculating VAT is available to dealers who:

- are reselling goods at retail.
- run a restaurant, eating house, club, hotel (other than star hotels), refreshment rooms or boarding establishment,
- are caterers and serve food with non-alcoholic drinks
- run bakeries
- are dealers in second hand passenger motor vehicles
- are engaged in executing works contracts.

Please note that if you are involved in works contract, leaflet MVAT 109 provides full details about the composition scheme available for you.

A composition scheme is not available to:

- manufacturers
- importers
- dealers who purchase any goods from a registered dealer on high seas basis.
- dealers who sell in retail Foreign Liquor and Country Liquor.
- dealers who sell in retail Drugs covered by Entry C-29
- dealers who sell in retail notified Motor Spirits

What are the advantages of joining the scheme?

That will be for you to decide. Much will depend on how the new value added tax will affect your business.

But it essentially saves a lot of labour of keeping transactions wise sales side records including tax recovery. It simplifies calculations of tax liability of the dealer.

What are the disadvantages of joining the scheme?

Again, it will be a matter for you to decide based on the nature of your business.

But, you will not be able to claim set-off of any VAT you may pay on your business purchases, nor will you be able to issue tax invoices to your customers. For dealers who are engaged in executing works contracts or dealers in second hand passenger motor vehicles and opting for composition option, special provisions for claim of set off and tax invoice would apply. (Refer leaflet MVAT 109 and MVAT 108)

How is retail selling defined?

In order to qualify as a retailer, at least 90% of your sales must be made to people who are not dealers.

Is there a limit to the size of the business that can apply for a composition system?

No. There is no turnover limit or any other conditions – other than those already outlined.

Under a composition scheme, how is the value added tax calculated?

This will depend on which composition scheme applies to your business. For each scheme, there is a different method for calculating the tax.

1) Retailers

A retailer calculates the gross profit for a six-months' period, that is:

	Value of turnover of sales, other than sales of goods excluded
Less:	Value of turnover of purchases effected from a registered dealer, including the amount of tax collected separately by his vendors other than turnover of purchases of goods excluded
Balance	= Profit element

The tax payable is 8% of the profit element.

2) Restaurants, Hotels etc

- a) Dealer registered under the Act is required to pay tax @ 8% of the total turnover of sales
- b) Dealer not registered under the Act is required to pay tax @ 10% of the total turnover of sales

3) Caterers

- a) Dealer registered under the Act is required to pay tax @ 6% of the total turnover of sales
- b) Dealer not registered under the Act is required to pay tax @ 8% of the total turnover of sales

4) Bakeries

a) The bakery owner who is a registered dealer and who had an annual turnover of sales of bakery products including bread in loaf, rolls or slices, toasted or otherwise, of not more than Rs.30 lakh in the previous year is required to pay tax @ 4% of his turnover of sales. For a newly registered bakery owner, the current year's sales turnover shall be reckoned as the relevant sales turnover for the purpose of levy of tax on him.

b) The bakery owner who is not a registered dealer is required to pay tax @ 6% of the turnover of sales of goods including bread in loaf, rolls or slices, toasted or otherwise, if his annual sales turnover does not exceed Rs. 30 lakh.

Note : Bakeries with an annual turnover of sales in excess of Rs. 30 lakh is taxable at the applicable VAT rate.

4) Second-hand passenger motor vehicle dealers

The second hand passenger motor vehicle dealers is required to pay tax @ 4% of the turnover of sales and he is entitled to avail of set-off of the tax paid on purchases of materials used for re-furbishing and re-conditioning of vehicles before sale.

Please note that details of the works contract calculations can be found in leaflet MVAT 109.

How do I join a composition scheme?

If you are a dealer applying for a new VAT registration, you can opt to join the composition scheme by indicating this at question no. 7 of the VAT registration application form 101.

If you are already registered for VAT, you must opt to join the composition scheme. You can do this using prescribed form which is available from your Sales Tax Office. You should return the duly completed form to the Sales Tax Office.

What is the deadline to join?

If you wish to join the scheme with effect from 1 April 2005, you must apply before 30 April 2005.

You can apply to join the scheme at any time after 30 April 2005 but your application will then only become effective from the beginning of the next financial year, that is the following 1st April. Until that time, you must continue to account for VAT under the normal rules.

What VAT return form do I use to pay VAT under a composition scheme?

There are different return forms for different composition schemes and you must use the correct one as follows:

Type of Dealer	VAT Return Form Number
Retailer	204
Restaurant, eating house, etc	205
Bakery	206
Second-hand car dealer	207

How often do I file a return?

If you are a **retailer**, you will make a return for a six month period. The periods are 1st April to 30th September and 1st October to 31st March each year.

For **other composition dealers**, you will file returns as follows:

- If your total net tax liability including CST, BST and VAT in the previous year was more than Rs. 1 lakh, you must file your returns monthly
- If your total net tax liability including CST, BST and VAT in the previous year exceeded Rs. 12,000/- but was not more than Rs. 1 lakh, you should file your returns quarterly for the quarters ending on 30th June, 30th September, 31st December and 31st March.
- If your total net tax liability including CST, BST and VAT in the previous year was Rs.12,000 or less, you should file your returns every six months for the periods 1st April to 30th September and 1st October to 31st March.

What is the deadline for filing returns?

Your returns for the periods ending 31st December and 31st January must be filed by the 20th day of the following month, that is 20th January and 20th February respectively.

Your returns for all other periods must be filed by the 25th day of the following month. For example, your return for the period ending 30th September must be filed by the following 25th October.

Can I switch from normal VAT to a composition scheme or vice versa?

Yes, if otherwise eligible. But you must notify your local Sales Tax Office of the change in writing the change to or from normal VAT accounting will only be effective from the beginning of the next financial year, that is the following 1st April. Until that time, you must continue to account for VAT under the normal VAT or composition scheme as the case may be.

There is a new series of leaflets, written in simple language, to explain the value added sales tax system.

The range of leaflets will each cover a single topic, and the topics covered will gradually be expanded over the next few months.

You will be able to get copies of the leaflets from your local Sales Tax Office.

Other leaflets that you may find useful are:

- MVAT 101 - What is VAT?
- MVAT 102 - Should I be registered for VAT?
- MVAT 103 - How to register for VAT
- MVAT 104 - Keeping records for VAT
- MVAT 105 - Tax invoices for VAT
- MVAT 107 - How to file a VAT Return
- MVAT 108 - Claiming set-off for VAT
- MVAT 109 - Accounting for VAT on Works Contracts
- MVAT 110 - Incentives under VAT
- MVAT 111 - VAT Advisory Visits

These notes are for guidance only. They reflect the tax position at the time of publication. They do not replace the legislation or affect your rights of appeal about your own tax position. If in doubt, contact your local Sales Tax Office for assistance.

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