



## THE EFFECTIVENESS OF VAT AND GST IMPLEMENTATION IN ENHANCING TAX REVENUE: A COMPARATIVE ANALYSIS

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### Abstract

This article evaluates the effectiveness of Value-Added Tax (VAT) and Goods and Services Tax (GST) implementation in enhancing national tax revenue. Through a systematic review and analysis of research studies from various countries that have adopted VAT/GST systems, this study demonstrates that both tax mechanisms significantly contribute to increasing tax revenue by expanding the tax base and reducing potential tax leakage. While their effectiveness varies across countries based on implemented policies, key factors such as taxpayer compliance rates, administrative complexity, and technological utilization in tax collection substantially impact implementation success. The findings emphasize the importance of well-designed policy formulation tailored to local economic contexts to ensure that VAT and GST can optimally contribute to national revenue. This research provides valuable insights for policymakers considering tax system reforms aimed at improving fiscal sustainability.

**Keywords:** Economic Growth, Fiscal Policy, Goods and Services Tax, Tax Revenue, Value-Added Tax

### Abstrak

Artikel ini mengevaluasi efektivitas penerapan Pajak Pertambahan Nilai (PPN) dan Pajak Barang dan Jasa (GST) dalam meningkatkan pendapatan pajak nasional. Melalui tinjauan sistematis dan analisis studi penelitian dari berbagai negara yang telah mengadopsi sistem PPN/GST, studi ini menunjukkan bahwa kedua mekanisme pajak tersebut berkontribusi secara signifikan terhadap peningkatan pendapatan pajak dengan memperluas basis pajak dan mengurangi potensi kebocoran pajak. Meskipun efektivitasnya bervariasi di berbagai negara berdasarkan kebijakan yang diterapkan, faktor-faktor utama seperti tingkat kepatuhan wajib pajak, kompleksitas administrasi, dan pemanfaatan teknologi dalam pemungutan pajak secara substansial memengaruhi keberhasilan implementasi. Temuan tersebut menekankan pentingnya formulasi kebijakan yang dirancang dengan baik yang disesuaikan dengan konteks ekonomi lokal untuk memastikan bahwa PPN dan GST dapat memberikan kontribusi optimal terhadap pendapatan nasional. Penelitian ini memberikan wawasan berharga bagi para pembuat kebijakan yang mempertimbangkan reformasi sistem pajak yang bertujuan untuk meningkatkan keberlanjutan fiskal.

**Kata Kunci:** Kebijakan Fiskal, Pajak Pertambahan Nilai, Pajak Barang dan Jasa, Pendapatan Pajak, Pertumbuhan Ekonomi

## INTRODUCTION

Taxation represents one of the most critical instruments in a nation's financial architecture. The primary objective of taxation is to mobilize funds to support public expenditure and development initiatives. Value Added Tax (VAT) and Goods and Services Tax (GST) are two widely adopted forms of indirect taxation implemented by countries worldwide. These taxation systems possess unique characteristics designed to minimize economic distortion and enhance the efficiency of tax collection mechanisms.

VAT was first introduced in France in 1954 and has since been adopted by numerous countries globally. Meanwhile, GST, a variation of VAT, has been implemented in various countries, including India since 2017. Both VAT and GST are applied with similar objectives: to increase tax revenue by imposing taxes at each stage of production and distribution of goods and services.



Empirical evidence demonstrates that VAT and GST implementation has significantly impacted government revenue. Research findings indicate that VAT revenue is substantially influenced by economic growth and inflation rates in ASEAN countries. Foreign Direct Investment (FDI) can either support or hinder the relationship between economic growth and VAT revenue, functioning as a moderating variable in this context.

VAT and GST enhance transparency and facilitate tax compliance. The input tax credit system incentivizes businesses to avoid tax evasion by allowing them to recover taxes paid at preparatory stages. These systems can be employed in tax administration to improve collection efficiency and minimize revenue leakages. More efficient and transparent taxation systems have proven to be major revenue sources for governments in numerous countries.

However, implementing VAT and GST faces various challenges, with one of the most significant being resistance from businesses and the public concerned about increased tax burdens. Additionally, effective and efficient tax system implementation requires the necessary technological infrastructure. While some research indicates that GST reduces administrative burdens and enhances tax transparency, its implementation requires thorough preparation.

GST was expected to make India's tax system simpler and more effective, improving tax compliance through digitalization and integration of tax management systems. This approach aimed not only to make tax administration more efficient but also to reduce tax waste and corruption prevalent in the previous system. Empirical studies conducted in ASEAN countries also demonstrate that value-added taxes can support economic growth and increase tax revenue. VAT and GST represent essential components of tax reforms aimed at enhancing tax collection effectiveness and efficiency.

This study examines in detail the effectiveness of VAT and GST implementation in increasing tax revenue, with an emphasis on the experiences of various countries and their potential application in Indonesia. The objective is to provide a better understanding of the advantages and disadvantages of different systems, ultimately leading to appropriate actions for improving the country's taxation system.

## **LITERATURE REVIEW**

### **Value Added Tax (VAT)**

Value Added Tax (VAT) is an indirect tax imposed on the consumption of goods and services at each stage of production and distribution, serving as a primary revenue source for many countries worldwide (Bird & Gendron, 2007; Keen & Lockwood, 2010). According to Law Number 42 of 2009 in Indonesia, VAT is a tax imposed on the consumption of taxable goods by individuals or legal entities and on taxable services within a customs area. VAT is levied incrementally during the production and distribution processes of goods or services (Riftiasari, 2019; Cnossen, 2020).

In its collection mechanism, VAT recognizes two principal approaches: the origin principle and the destination principle (Schenk et al., 2015; Ebrill et al., 2001). The origin principle dictates that VAT is collected at the place of origin of consumed goods or services. Currently, VAT is collected based on the destination principle, where tax is levied in the country where goods or services are consumed. These principles significantly impact VAT's status in international trade (Keen & Hellerstein, 2010). In the context of international commerce, the destination principle is adopted to maintain VAT neutrality. Under this principle, imported goods bear the same tax burden as domestically produced goods when consumed domestically (Ridho, 2021; Lamensch, 2018).

VAT represents an indirect tax imposed on final consumption, typically ranging from 15% to 20%. This tax is collected at various stages of the production chain and during sales to end consumers. Businesses can reclaim sales tax (input tax) paid during purchases by offsetting



it against sales tax (output tax) collected from sales, remitting the difference to tax authorities. Refunds can be utilized to settle future tax liabilities (Mascagni et al., 2022). VAT is considered a sales tax because consumers pay the tax when purchasing goods and services. This tax is efficient as it reduces the potential tax impact on inputs and accounts for the production supply chain process (Cevik et al., 2019; Crawford et al., 2010; James, 2015).

VAT adheres to sound taxation principles because it is transparent and easily collected, as well as efficient due to its generation throughout production and distribution processes. VAT effectively generates tax revenue while causing minimal economic distortion. Tax rates play a crucial role in determining the efficiency cost of taxation and can significantly impact relative prices (Erero, 2021).

VAT is globally recognized and currently implemented in over 150 countries (Brown & Gale, 2012). Research indicates that VAT represents a successful method for financing and modernizing taxation systems, explaining its widespread recognition and popularity worldwide (Ebrill et al., 2001). Despite its popularity among politicians and policymakers, VAT has limitations, and its revenue potential doesn't always meet expectations, creating a gap between actual VAT revenue generated during accounting periods (Kufanga & Mbewe, 2024).

As an indirect tax, VAT is imposed on consumers of goods and services but collected and remitted by sellers. According to Mgamal et al. (2023), VAT is one of the most influential and economical taxes for generating government revenue, provided it is well-managed by authorities. With comprehensive domestic VAT implementation, the potential for government revenue from VAT increases substantially, ultimately promoting national advancement (Asri & Suseno, 2023).

According to research published in the *International Tax and Public Finance* journal (2020), VAT implementation can enhance fairness and efficiency in taxation systems. This is because VAT is more difficult to avoid compared to other tax types, thereby minimizing tax avoidance practices.

Based on various scholarly definitions, Value Added Tax (VAT) can be understood as an indirect tax imposed at each stage of production and distribution of goods and services, serving as a primary revenue source for many countries. As stipulated in Law Number 42 of 2009 in Indonesia, VAT is levied on the consumption of taxable goods and services within a customs area. This tax is collected incrementally throughout production and distribution processes, with origin and destination principles being crucial in international trade to maintain tax neutrality. VAT rates typically range from 15% to 20%, with businesses able to claim input tax credits for taxes paid on purchases. Implemented in over 150 countries, VAT is considered efficient in minimizing tax impact on inputs and generating significant revenue. VAT enhances fairness and efficiency in taxation systems by being more difficult to avoid compared to other taxes. Despite occasional discrepancies between expected and actual revenue, VAT remains an influential and economical tax that supports government revenue and economic advancement when properly managed.

### **Goods and Services Tax (GST)**

Goods and Services Tax (GST) is an indirect tax imposed on individuals engaged in consumption activities across all business levels (Jain, 2018; Lourduathan & Xavier, 2017). Consequently, taxation doesn't require waiting until value is added to goods or services. According to World Bank information and taxation studies (Tait, 2022; Jenkins & Kuo, 2020), GST rates are typically lower than VAT rates, with the standard GST rate being 6%. Additionally, taxable goods obtained directly from sources in sectors like mining and extraction may also be subject to taxation. However, primary products such as those from micro, small, and medium enterprises (MSMEs), agricultural products, health products, education sector, and housing for low-income communities are exempted from taxation to provide incentives and



protect primary industries from economic shocks (Primacita & Khoirunurrofik, 2018; Vasanthagopal, 2011).

In line with this, according to Kour et al. (2016), GST is a combination of various state and federal indirect taxes such as value-added tax (VAT) and excise duties, along with various state taxes, central surcharges, entertainment taxes, luxury goods taxes, and others. GST is expected to transform the entire current indirect tax scenario by unifying all indirect taxes and helping create a more streamlined market. Experts suggest that GST will support a country's economic growth, potentially increasing economic growth by 0.9-1.7%. Exports are projected to drive economic growth by 3.2% to 6.3%, while imports are expected to increase by 2.4% to 4.7%.

GST resembles the VAT system, which is VAT on goods with an input tax credit (ITC) mechanism, but GST also encompasses services. Thus, compared to the current tax concept, GST applies to both goods and services provision. GST is a value-added tax on goods and services paid by the end consumer and allows retailers to deduct taxes paid when purchasing goods for retail sale. In this case, besides the actual price of manufactured goods, all services provided by retailers or networks behind them will be taxed. For example, if you have a network of manufacturers, wholesalers, and retailers, and GST is 10%, then GST is designed as a sales tax, where everyone from manufacturers, wholesalers, to retailers only pays tax on the value they add themselves (Madapana & Gupta, n.d.).

GST is imposed at the national level on the production, sale, and consumption of goods and services. This policy replaces all indirect taxes collected by central and state governments on goods and services (Shukla et al., 2022). GST is an excise tax collected as a value-added tax on a product and paid by the end-user or final consumer of the product. Businesses that purchase products and use them in business activities pay GST at the point of sale but receive refunds for the GST paid, known as "input credits" (Odhuno, 2016).

These additional transaction costs are transferred to the state as government revenue, specifically goods and services tax. GST, as its name suggests, is imposed on services in addition to goods. The service sector produces intangible goods, namely services rather than physical goods (Scott, 2022). According to Kotler (2009), services are actions or deeds performed by one party to another that are intangible and do not result in ownership transfer. Therefore, by providing a service to a party, that party only receives or enjoys benefits without owning the service. Unlike goods, when goods are delivered to a party, that party receives and owns them. The service sector can contribute to increasing a country's GDP, creating jobs, and reducing poverty (UGM, 2016; Prabowo & Wijaya, 2023).

GST also taxes consumed goods and services, but unlike VAT, this system is more centralized. Taxes are collected at each stage of production and distribution, but businesses only pay tax on the added value, not on the total amount of goods and services sold. This system reduces administrative burdens and minimizes tax avoidance activities. According to De Castro et al. (2016), GST is not a cost for sellers and is not displayed as an expense in financial statements. VAT is typically collected at various levels, with different rates applying to various categories of goods and services. Although GST can be applied with multiple tax rates, many GST systems attempt to allocate all goods and services to one tax rate or a limited number of tax rates. Additionally, GST coverage is broader because it tends to include almost all types of consumer goods and services, including luxury goods (Wahyuni & Wijaya, 2024).

From various research perspectives, Goods and Services Tax (GST) can be characterized as an indirect tax imposed on the consumption of goods and services across all business levels, without waiting for value addition. Standard GST rates are typically lower than VAT, approximately 6%. GST consolidates various federal and state indirect taxes, creating a more efficient marketplace and is projected to enhance economic growth. The tax encompasses



services, allowing retailers to deduct taxes paid when purchasing goods for retail sales. GST replaces all central and state indirect taxes, reducing administrative burdens and tax avoidance. With extensive coverage, GST encompasses almost all consumer goods and services, including luxury items.

### **Tax Revenue**

According to Indonesia's State Finance Law Number 17 of 2003, state revenue comprises three components: tax revenue, non-tax state revenue, and subsidies. Among these components, tax revenue constitutes the largest proportion of state revenue, accounting for 82% (Darussalam et al., 2019; Nurmantu, 2018). Various factors can influence government tax revenue, including (1) taxpayer compliance behavior (Desideria & Ngadiman, 2019; Alm, 2019); (2) factors that can reduce tax fraud levels (Afriyanti, 2012; Allingham & Sandmo, 1972; Slemrod & Yitzhaki, 2002); and (3) aggressive collection actions by tax authorities that may result in tax payment arrears (Saputri, 2015; Torgler, 2007).

Tax revenue represents the government's primary income source used to finance various programs and public services. Research indicates that both VAT and GST have significant potential to increase national tax revenue. Tax revenue encompasses all receipts derived from tax payments by individuals or business entities to the government. This includes various tax types such as income tax, value-added tax (VAT), goods and services tax (GST), and other taxes imposed by the government.

Tax revenue constitutes one of the main income sources for countries, used to finance government expenditures, including infrastructure development, education, healthcare, and other public services. The effectiveness of tax implementation depends on various factors, including tax rate policies, taxpayer compliance levels, tax administration complexity, and technology utilization in tax collection.

Tax revenue can also be defined as income sources collected by governments from citizens and businesses to fund public services and economic development (Tanzi & Zee, 2000; Myles, 2000). Tax revenue reflects mandatory contributions from economic actors involved in production and consumption activities classified as taxable (Smith, 2020; Stiglitz & Rosengard, 2015). According to Smith and contemporary fiscal theorists (Musgrave & Musgrave, 1989; Feldstein, 2012), tax revenue is not only important for fiscal sustainability but also plays a role in wealth redistribution and achieving social justice.

Studies in the *European Journal of Taxation* (2022) comparing VAT revenue performance in European Union countries found that VAT collection effectiveness heavily depends on administrative structure and strong law enforcement. Effective tax revenue not only supports a country's fiscal sustainability but also plays an important role in wealth redistribution and social justice achievement. Therefore, good tax policy planning and implementation become crucial in national economic management.

### **METHODS**

This research employs a qualitative method with a descriptive-case study approach to analyze the effectiveness of Value Added Tax (VAT) and Goods and Services Tax (GST) implementation in enhancing tax revenue in Indonesia. The qualitative method was selected as it enables researchers to gain an in-depth understanding of the dynamics of VAT and GST implementation and their impact on tax revenue through comprehensive and holistic analysis. The descriptive-case study approach is used to provide a clear picture of the situations encountered in implementing these two tax types, focusing on the local and specific context in Indonesia.

Data collection was conducted through literature review and document analysis from various relevant sources, including research reports, journal articles, and official government



documents related to VAT and GST policies and implementation. Additionally, we examined in-depth perspectives from taxation experts, government officials, and relevant business actors to identify patterns, relationships, and trends relevant to the research topic. This technique aimed to identify challenges and opportunities in VAT and GST implementation and understand how these two tax types can be optimized to enhance tax revenue.

Data analysis was performed using thematic analysis techniques to identify the main themes emerging from the collected data. This process involved systematically coding data to group information based on specific themes, such as tax compliance, administrative transparency, and technology use in tax collection. The coded data was then analyzed in depth to discover patterns and relationships between relevant variables.

The analysis results are expected to provide a comprehensive understanding of the effectiveness of VAT and GST implementation in enhancing tax revenue in Indonesia. To increase research validity and reliability, data triangulation was conducted by comparing findings from various different data sources. This triangulation aimed to ensure that research results did not rely solely on one data source but were supported by consistent and reliable evidence. With this approach, this research is expected to make a meaningful contribution to taxation policy development in Indonesia, particularly in optimizing VAT and GST implementation to enhance national revenue.

## **RESULTS AND DISCUSSION**

### **Value Added Tax (VAT) and Goods and Services Tax (GST)**

Value Added Tax (VAT) and Goods and Services Tax (GST) are two types of indirect taxes applied to the consumption of goods and services (Baunsgaard & Keen, 2010; Cnossen, 2018). Value Added Tax is levied on the added value generated at each stage of production and distribution of goods or services (Charlet & Owens, 2010; Le, 2003). This tax is collected at each stage of the supply chain and paid by the final consumer. In other words, each business entity pays tax on the value added to their products before selling them to the next consumer in the supply chain (Tait, 1988; Mirrlees et al., 2011).

Conversely, according to World Bank reports, GST is a tax imposed at all stages of production and distribution of goods and services but is simpler in administration compared to VAT. Goods and Services Tax is directly levied on the consumption of goods and services at each business stage without waiting until goods or services have added value. GST rates are generally lower than VAT, with a standard example of 6%. GST (Goods and Services Tax) also covers goods taken directly from their sources, such as mining and extraction sectors, but there are tax exemptions for certain primary goods such as agricultural products and the education sector. According to research conducted by George et al. (2019), GST implementation can bring significant benefits in terms of enhancing administrative efficiency and reducing compliance burdens for businesses. GST enables a simpler and more transparent taxation system, which in turn can improve tax compliance and reduce tax avoidance. Additionally, GST can create a fairer market by eliminating price distortions caused by double taxation at each production and distribution stage.

Overall, VAT and GST play important roles in modern taxation systems with several key differences in their application and administration. VAT is more complex because it involves calculating added value at each production and distribution stage, while GST offers simplicity with direct taxation on consumption. Nevertheless, both tax types aim to optimize state revenue from the consumption sector and ensure fair contributions from each economic actor. Effective implementation of both taxes requires a deep understanding of each mechanism's functioning, as well as adaptation to economic conditions and regulations applicable in each country.



## **History of VAT and GST Implementation**

### ***VAT (Value Added Tax)***

VAT was first introduced in France in 1954. As a form of consumption tax, VAT was implemented to replace various existing sales taxes and production taxes. The main principle of VAT is that each stage of production and distribution of goods and services is taxed based on the added value generated at each stage. This tax was then expanded to various countries in Europe and beyond as a way to increase tax revenue more efficiently and fairly compared to traditional sales taxes.

VAT (Value Added Tax) has become one of the main revenue sources for many countries. For instance, in Indonesia, VAT is the second-largest contributor to national tax revenue after income tax. However, despite its increasing contribution each year, VAT's impact on the tax-to-GDP ratio is still considered less significant.

### ***GST (Goods and Services Tax)***

GST is a further evolution of the VAT concept and is implemented in various countries to replace existing indirect tax systems, including VAT and sales taxes. GST is typically designed to be more efficient and reduce the negative impacts of multi-tiered taxation.

Several countries that have implemented GST include:

- **Singapore**

Singapore transitioned from sales tax to GST in 1994, aiming to increase tax revenue without hindering its business competitiveness. As Asia's largest cargo port, Singapore was able to maintain its tax revenue during this transition.

- **India**

India introduced GST in 2017, making it one of the first developing countries to implement GST. GST implementation in India aimed to simplify the tax structure by combining various state and central taxes into a single tax. Studies show that GST in India has successfully reduced the cascading effect of multi-tiered taxes and increased tax revenue as well as economic growth.

- **Australia**

Australia implemented GST in 2000 to enhance the country's export competitiveness. Studies indicate that the transition to GST did not cause significant changes in the consumer price index, showing that GST can be implemented without causing significant inflation.

- **Malaysia**

Malaysia implemented GST in 2015, aiming to strengthen the economy and improve its citizens' quality of life. Research shows that GST helps increase tax revenue without placing too much burden on the income of middle to lower-income communities.

- **Indonesia**

In Indonesia, there are considerations to replace VAT with GST. Studies show that GST has the potential to increase tax revenue higher than VAT. With GST, Indonesia can optimize tax revenue from the increasingly developing service and manufacturing sectors. Analysis indicates that GST is more efficient and can increase the tax revenue-to-GDP ratio, which is one of the main challenges of the current tax system in Indonesia.

Thus, the history of VAT and GST implementation shows that both tax systems have been adopted by various countries to increase tax collection efficiency and government revenue. While VAT has long been used and proven effective, GST offers additional advantages in terms of simplification and administrative efficiency, making it an attractive option for many countries, including Indonesia. GST implementation in Indonesia has the potential to provide higher tax revenue and fairer distribution across regions.



### **Working Principles of VAT and GST**

The collection principles of VAT (Value Added Tax) and GST (Goods and Services Tax) ensure that these tax systems function effectively, balancing government revenue needs with fairness and efficiency in administration. Revenue productivity becomes the main focus, with the aim of generating adequate revenue without imposing excessively high tax rates, as well as promoting economic growth through tax-financed expenditures. Administrative ease is an important sub-principle, ensuring certainty and convenience in tax collection and payment processes, as regulated in related regulations, such as PMK No. 48/PMK.03/2020 for VAT on digital services.

Meanwhile, GST's working principles are based on several key concepts to ensure effectiveness and fairness in tax collection. GST is imposed on the consumption of goods and services at each value addition stage in the distribution chain, ensuring that every business entity adds GST to their selling price, and that consumers purchasing goods or services can reclaim GST paid at previous stages. GST should also be neutral towards specific businesses and transactions, not influencing economic decisions and not providing preferences for certain business types. It is important to have high transparency in the GST system, with clear rules and efficient administration, as well as a strong law enforcement system to avoid tax avoidance practices and ensure high compliance from taxpayers. By applying these principles, GST is expected to be an effective instrument in generating government revenue while minimizing economic distortion and enhancing fairness in the overall tax system.

Neutrality of the tax system becomes another crucial principle, ensuring that there is no distortion to economic decisions, especially in the context of digital services that tend to be complex. These principles as a whole aim to create a balanced, effective, and fair tax environment that meets government revenue needs while minimizing burdens on taxpayers and ensuring good compliance.

### **Tariff Structure and Implementation Policies**

Tariff structures and implementation policies for VAT and GST have different characteristics across various countries. These rates are typically set by considering sales taxes, customs duties, VAT, etc. Countries like Singapore and Thailand have implemented a rate of 7%, while Indonesia, Australia, and the US impose a 10% tax on their consumers, and New Zealand sets a rate of 12.5%. VAT is applied at each stage of production and distribution of goods and services, with rates varying between 5% and 25% depending on the country. Some sectors such as local transportation, healthcare, education, and real estate may be subject to zero rates or certain exemptions. For example, in Saudi Arabia, the standard VAT rate is 5% with some exemptions for certain medical products and foods.

VAT implementation policies require each seller or producer to register and obtain a VAT registration number. Tax is imposed on each added value generated at each production and distribution stage, with input tax credits given for taxes paid at previous stages. This helps reduce the amount of tax payable at the next stage and supports tax collection at the point of origin of goods and services.

On the other hand, GST implementation policies in India combine various indirect taxes into one comprehensive tax system. The GST system is fully online, covering registration, filing returns, and tax payments through the GSTN (Goods and Services Network) portal. Destination-based GST implementation means taxes are collected at the place of final consumption of goods and services, not at their place of origin. Companies with turnover exceeding certain thresholds, for example, Rs. 20 lakh, are required to register for GST. These clear and efficient tariff structures and implementation policies help in more transparent tax collection and reduce the possibility of tax avoidance, as well as simplify tax administration for governments and businesses.



### **Influence of VAT and GST on the Economy**

The influence of Value Added Tax (VAT) and Goods and Services Tax (GST) on the economy can be very significant, depending on how they are implemented and managed in various economic contexts.

In many countries, VAT becomes a stable and important revenue source for governments. For example, in South Africa, increasing the VAT rate from 14% to 15% in the 2018/2019 fiscal year resulted in a significant revenue increase and helped stabilize the country's tax revenue system. This is because VAT is a broad-based tax that tends to be more stable compared to income tax during business cycles. VAT increases directly affect goods and services prices, which can impact consumption and public welfare.

Meanwhile, for GST in certain countries like India, it is considered the biggest tax reform that creates a more integrated and efficient market. Nevertheless, complex GST implementation and high rates can negatively impact some sectors such as real estate and SMEs (Small and Medium Enterprises), which play important roles in India's GDP.

In general, both VAT and GST have the potential to increase government revenue and provide fiscal stability. However, both can also have different impacts on consumption and economic growth. Increasing VAT rates can reduce consumer purchasing power if companies are unable to absorb additional costs through operational efficiency. Conversely, GST can simplify the taxation process and reduce compliance costs, but complexity in its implementation and high rates can limit these benefits.

Thus, it is important for governments to balance between increasing revenue through consumption taxes and ensuring that tax rates do not hamper economic growth or burden consumers and important sectors in the economy.

### **Benefits of VAT and GST Implementation**

VAT and GST implementation has a number of significant benefits that not only impact increasing national revenue but also contribute to the efficiency and transparency of the taxation system, elimination of double taxation, and promotion of economic growth. Through simpler and fairer tax collection mechanisms, VAT and GST can provide benefits for governments, businesses, and society as a whole.

Experts have identified various benefits of GST implementation as follows. First, GST will introduce a one-country-one-tax two-level tax regime, which simplifies the overall taxation system. Second, GST will combine all indirect taxes at the central and state levels, thus creating uniformity in tax imposition. Third, GST will not only expand the tax regime by covering goods and services but also increase transparency in the taxation system. Additionally, GST will free the manufacturing sector from the cascading effect of taxes, which in turn will increase the cost competitiveness of goods and services. With GST implementation, prices of goods and services are predicted to decrease, thus encouraging increased consumption. Furthermore, GST will create a business-friendly environment, which is expected to increase the tax-to-GDP ratio. Lastly, GST implementation will improve the ease of doing business, providing a positive boost to the country's economic growth.

### **Challenges and Obstacles in VAT and GST Implementation**

The implementation of Value Added Tax (VAT) and Goods and Services Tax (GST) represents an important step in tax reforms adopted by many countries worldwide. These taxes are designed to enhance the efficiency of the taxation system, expand the tax base, and increase government revenue. However, VAT and GST implementation doesn't always proceed smoothly and often faces various challenges and obstacles. From administrative complexity to resistance from businesses, various factors can affect the effectiveness and success of these tax implementations. Below are the challenges that must be faced in implementing VAT and GST.



- Approval from all states or local governments is very important in enacting GST legislation, given its broad implications for national tax and financial structures.
- To ensure successful GST implementation, the importance of achieving a Revenue Neutral Rate (RNR) becomes crucial. RNR aims to maintain stable government revenue despite the tax credit system given to businesses. This requires careful planning and management from the government to avoid unexpected revenue deficits.
- Determining GST thresholds that not only avoid excessive tax burdens for small businesses but also encourage broader economic participation in the tax system. Meanwhile, the need for a strong information technology network, such as GSTN, to support registration, tax filing, and other administration should not be neglected. This requires reliable IT infrastructure to effectively support GST operations.
- Extensive training for tax administration staff to fully understand the concepts, regulations, and procedures related to GST. By strengthening tax administration capacity, it is expected to reduce potential errors or misuse in managing this new system.
- In the context of additional compensation or levies on GST, this becomes crucial to compensate states that may experience revenue declines when switching to the new GST system. This is important to maintain economic balance between central and regional governments within the integrated GST framework.

With proper handling of these challenges, GST can become an important instrument in stimulating national economic and financial development.

#### **Influence of VAT and GST on Consumers**

Value Added Tax (VAT) and Goods and Services Tax (GST) are two forms of indirect taxes applied to the consumption of goods and services in various countries. These tax systems are designed to effectively increase government revenue without burdening a particular sector. However, although the main purpose is to support development and provide public services, VAT and GST have a significant influence on consumers. The influence of VAT and GST on consumers can vary depending on economic structure, income levels, and consumption patterns in each country.

VAT and GST implementation typically causes price increases for goods and services, which can affect purchasing power and consumer welfare. In some countries, consumers may feel a greater tax burden on basic needs, while in other countries, these policies may be designed to protect consumers from adverse impacts through tax exemptions or reductions on essential goods. Below is a summary of the influence of VAT and GST implementation in various countries on consumer behavior.

- **Malaysia**  
Describes the impact of GST implementation on respondents' consumption behavior in Malaysia, where most respondents did not change their consumption behavior, some considered purchases more carefully, and others reduced purchases according to their income.
- **New Zealand**  
New Zealand's experience in GST implementation shows that consumer fear of price increases due to GST can lead to irrational purchasing decisions. When GST was first introduced, many consumers made large purchases because they thought prices would rise by 10%. However, GST implementation actually caused price decreases for these goods, so some consumers experienced losses.
- **Australia**  
The Australian government took several initiatives when introducing GST, including establishing penalties for price exploitation or misleading and deceptive actions. The government also conducted a national consumer awareness campaign regarding GST's



impact on prices. There was also a view that the government should not regulate prices and let entities make pricing decisions based on market supply and demand balance.

- **India**

When introducing VAT, the Indian government faced harsh criticism from the public and industry. Prices of some commodities decreased, but others increased. The government needs to pay attention that prices of goods currently exempt from sales tax may increase, while prices of goods currently subject to sales tax may decrease depending on the reduction in retail markup and passing benefits to consumers. Service prices may increase because the proposed GST rate is higher than the current service tax rate.

Overall, VAT and GST policies not only affect consumption patterns but also market transparency and efficiency, which can significantly impact consumer welfare and economic stability.

### **Influence of VAT and GST on Producers and Businesses**

In the business context, VAT and GST implementation affects various operational aspects, from production processes to product selling price determination (Barbone et al., 2012; Harrison & Krelove, 2005). Producers and companies must adjust their accounting systems to comply with tax regulations, which can increase administrative and operational burdens (Krever, 2014; Evans, 2003). Additionally, VAT and GST can affect company cash flow because taxes must be collected and deposited to the government periodically (Pope, 2001; Lignier & Evans, 2012). Nevertheless, this system also offers advantages in the form of input tax refunds that can reduce the overall tax burden for producers (Joshi et al., 2014; Fullerton & Metcalf, 2002). VAT and GST implementation can encourage companies to increase efficiency and transparency in their operations (Feria & Krever, 2013; Swain, 2015).

According to industry experts, small-scale businesses and new startups will be greatly affected by GST introduction, but the impact will be positive in many ways. Some ways in which GST encourages most sectors and startups are as follows:

- VAT registration is required for businesses operating in various states. People face complications due to different tax regulations in each state and large procedural costs. Through GST, a centralized registration process has been established so people can start businesses more easily than before.
- In the old tax structure methodology, companies with turnover exceeding 5 lakh rupees had to pay VAT registration fees. But now, the government plans to change the exemption limit to 20 lakh rupees, providing benefits to more than 60% of small traders and readers.
- In the current GST system, input tax is not imposed on goods that are produced or sold. So goods shipment at interstate points and toll gates will be expedited. According to estimates made by CRISIL agency, logistics costs and other supply chain costs for mass goods producers will be reduced significantly—about 20%. This will encourage e-commerce throughout the country.
- GST reduces ambiguity between goods and services. Various legal procedures related to packaging products become simpler. Finally, there will be no more differences between material components and services, which will greatly reduce tax smuggling.
- GST has brought fundamental changes to the taxation system by introducing an input tax credit mechanism, which reduces the tax burden imposed at each stage of the supply chain. This is expected to drive overall economic growth by increasing efficiency and transparency in business processes.

However, negative impacts are also clearly visible, especially for SMEs with turnover below the 20 lakh rupee threshold and therefore not required to pay GST. This causes small



companies to continue operating under the old taxation structure such as paying excise and VAT, which may impose a higher tax burden in the short term. Additionally, small unorganized sectors may lose their competitiveness as they cannot adapt to the new tax changes, facing challenges to maintain their operations and possibly being forced to implement layoffs to reduce costs.

Information technology readiness is also a major concern, especially for small companies that often face constraints in implementing the technology required to comply with GST requirements. The need for a strong IT network to facilitate GST filing indicates the need for additional investment and education for SMEs to maximize the benefits of the new tax system.

Therefore, although GST brings potential to enhance economic efficiency and reduce corruption through taxation system simplification, the challenges faced by SMEs and small sectors indicate the need for a careful approach and ongoing support to ensure that GST benefits can be felt equitably across all economic sectors.

### **Effectiveness of VAT and GST in Enhancing Tax Revenue**

Value Added Tax (VAT) and Goods and Services Tax (GST) are important instruments in fiscal policy implemented in many countries to increase tax revenue (Keen & Lockwood, 2010; Auerbach & Gordon, 2002). Both tax types are imposed on the added value of goods and services at each production and distribution stage, making them more effective in reaching various economic sectors compared to direct taxes (Bird, 2010; Hines & Summers, 2009). VAT and GST implementation is expected to address challenges in tax collection, such as tax avoidance and taxpayer non-compliance (Keen & Smith, 2006; de Paula & Scheinkman, 2010). The effectiveness of VAT and GST in enhancing tax revenue can be seen from several aspects:

- First, this system provides a stable and predictable revenue source for governments, which is essential for budget planning and public program financing.
- Second, VAT and GST minimize economic distortion because they are applied broadly and evenly, thus not excessively burdening one sector or economic group.
- Additionally, VAT and GST implementation encourages increased transparency and accountability in economic transactions, which in turn can strengthen the tax base and reduce tax avoidance practices.

### **Policy Recommendations to Enhance VAT and GST Effectiveness**

To enhance the effectiveness of Value Added Tax (VAT) and Goods and Services Tax (GST), several actions can be implemented:

- There needs to be a simplification of tax rates and exemptions to reduce administrative complexity and compliance.
- Enhancement of technology and tax administration systems, such as using online platforms for registration, filing, and tax payments, can increase efficiency and transparency.
- Governments should conduct broader education and socialization to taxpayers regarding benefits and obligations related to VAT and GST, to raise awareness and compliance.

By implementing these recommendations, governments can ensure that VAT and GST function optimally as stable and fair revenue sources, while supporting sustainable economic growth.

### **CONCLUSION**

The implementation of Value-Added Tax (VAT) and Goods and Services Tax (GST) has proven effective in enhancing tax revenue across various countries (Keen & Lockwood, 2010; Cnossen, 2018). Despite differences in management and operations, both share a common



characteristic of pursuing fairness and efficiency in taxation systems (Bird & Gendron, 2007; James, 2015).

VAT operates on the principle of taxing goods and services at each stage of production and distribution, proving effective in reducing tax avoidance and increasing government revenue. However, administrative complexity and the need for high taxpayer compliance represent challenges that governments must address to ensure successful implementation.

Conversely, GST offers administrative simplicity and broader coverage, encompassing nearly all types of goods and services. This system enables the reduction of price distortions resulting from cascading taxes across production and distribution stages. Although the standard GST rate is lower than VAT, it still significantly contributes to tax revenue by expanding the tax base and reducing tax leakages.

Both tax types can maximize contributions to government revenue when properly managed and supported by appropriate technology. Governments must continually adapt to local economic conditions and develop effective measures to maximize the potential of VAT and GST. With careful policy planning and proper implementation, these taxes can not only serve as crucial revenue sources but also become instruments for achieving economic equity and enhancing societal welfare.

### **Recommendations**

Based on the findings of this study, several recommendations can be proposed to enhance the effectiveness of VAT and GST implementation:

#### **1. Policy Simplification**

- Governments should simplify tax rates and exemptions to reduce administrative complexity and compliance costs.
- The adoption of a single or limited number of tax rates would minimize distortions and enhance taxpayer compliance (Kowal & Przekota, 2021).

#### **2. Technological Enhancement**

- Investment in robust digital infrastructure is essential for efficient tax administration.
- Implementation of integrated electronic systems for registration, filing, and payment would reduce administrative burdens and minimize tax evasion (Mascagni et al., 2022).

#### **3. Educational Initiatives**

- Comprehensive taxpayer education programs should be developed to increase awareness about VAT/GST benefits and obligations.
- Regular training for tax officials would ensure consistent application of tax regulations and improve service delivery (Bhalla et al., 2023).

#### **4. Transitional Support for SMEs**

- Special assistance programs should be established for small and medium enterprises during the implementation phase.
- Simplified compliance procedures and temporary concessions could help SMEs adapt to new tax requirements (Darmayasa et al., 2020).

#### **5. Regular Evaluation**

- Governments should conduct periodic assessments of VAT/GST impact on different economic sectors.
- Data-driven evaluations would help identify areas for improvement and ensure the tax system remains efficient and equitable (Erero, 2021).

#### **6. International Cooperation**

- Enhanced collaboration between countries can help address cross-border VAT/GST challenges.



- Sharing best practices and harmonizing tax approaches would facilitate international trade and reduce compliance complexities (Lamensch, 2018).

#### 7. Targeted Exemptions

- Essential goods and services used primarily by lower-income households should receive carefully designed exemptions or reduced rates.
- This approach would maintain the progressivity of the tax system while preserving revenue generation capabilities (Crawford et al., 2010).

These recommendations aim to balance revenue generation objectives with economic growth considerations, ensuring that VAT and GST systems serve as effective fiscal tools while minimizing potential negative impacts on businesses and consumers.

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