

# THE ROLE OF VAT IN PUBLIC HEALTH FINANCING: LESSONS FROM GLOBAL HEALTH INITIATIVES

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## ABSTRACT

*This paper studies the role of Value Added Tax (VAT) in funding public health systems worldwide, especially in low- and middle income countries. VAT is now a dependable, effective source of revenue for health programs and projects. With rising demands on healthcare systems, VAT provides a lasting means to finance public health and fix resource gaps, notably in developing countries. By reading case studies from diverse global health projects, the paper shows both benefits and obstacles in using VAT for health finance and gives suggestions for policy changes to improve VAT support to health sectors.*

## INTRODUCTION

### **Background on VAT**

Value Added Tax (VAT) is a tax applied when goods or services gain value at each production or distribution stage. It provides key revenue for various governments worldwide, especially in Europe, Asia next to parts of Africa. VAT is a stable, efficient tax used on many goods and services. Authorities collect taxes at each production step to lower tax evasion.

Countries use VAT to pay for government spending. Many now use it to pay for public health systems. Healthcare needs rise because of aging populations, more non-communicable diseases and pandemics such as COVID-19. VAT supplies a steady source for health funding. It plays a key role in health financing.

### **Research Problem**

The state of the public health sector in any region largely depends on the financial strength of its government. This is particularly true for low- and middle-income countries (LMICs) where healthcare systems are severely underfunded. When there is a deficit of funds, it results in poor services,

inadequate healthcare systems, and low overall health standards. Moreover, as the demand for global healthcare continues to grow, there is a greater need to incorporate innovative financing strategies that would help achieve optimal funding. A critically important VAT, on the other hand, can be extremely useful for health care projects if employed effectively.

### **Research Objectives**

This paper aims to:

- Check at successful case studies from nations that have successfully financed health care through the use of VAT.
- Evaluate the benefits and drawbacks of utilising VAT as a funding source for public health.
- Offer suggestions for maximising VAT in health system funding.

## VAT AND PUBLIC HEALTH FINANCING – THEORETICAL FRAMEWORK

### **Understanding Public Health Financing**

The distribution of funds to support the delivery of medical treatment, illness prevention, and public health infrastructure is known as public health funding. The main sources of funding for health care are governments, commercial organisations, and international organizations. However, many governments find it difficult to provide sufficient funding due to the rising costs of healthcare.

There are primarily two models of public health financing:

- **Tax-based models:** Where the government funds public health systems using general tax revenues (e.g., income taxes, sales taxes, VAT).
- **Insurance-based models:** Where health funding is derived from premiums paid by citizens or employers.

VAT has emerged as one of the most dependable instruments for funding health systems in tax-based frameworks. VAT has the advantage of being a more predictable source of income than other taxes due to its wide base and application to almost all economic transactions.

### **How VAT Functions as a Source of Health Revenue**

When goods and services are sold, VAT is often applied at a set rate. The final customer is responsible for paying the tax, which is charged at every stage of production. VAT is effective because of the way it is set up: companies collect the tax from customers and send it to the government. Since it is difficult to avoid VAT once goods or services have reached the market, this approach lowers the likelihood of tax evasion.

The provision of universal health coverage (UHC), the building of medical facilities, and the funding of public health initiatives like immunization campaigns are all possible uses for VAT funds. In order to ensure that healthcare is sufficiently supported without solely depending on outside assistance or borrowing, several governments allocate certain percentages of VAT revenue to health-related projects.

### **Global Trends in VAT and Health Financing**

VAT is increasingly becoming a vital source of funding for healthcare on a global scale. Numerous nations have created VAT schemes especially to finance healthcare initiatives. For example, in several European nations, social welfare programs, such as healthcare, are funded in part by VAT revenues. In a similar vein, VAT is frequently employed as a cornerstone for funding necessary health care in developing countries.

## **CASE STUDIES OF VAT AND PUBLIC HEALTH FINANCING**

### **European Union: VAT and Health Systems**

VAT is utilized in the European Union (EU) to support public health systems in addition to general government spending. VAT income have long been used by nations like France and Germany to fund national healthcare programs that offer their citizens universal health coverage. With certain taxes intended expressly to finance health services, such as hospital development and medical care subsidies, VAT has been a reliable source of funding for France's healthcare system. To lessen the financial burden on citizens and guarantee that healthcare services continue to be available, the EU's VAT framework also provides reduced rates for necessary healthcare items and services, such as prescription drugs and medical devices.

### **Sub-Saharan Africa: VAT as a Financing Mechanism**

VAT is a crucial tool for funding public health systems in sub-Saharan Africa, including Tanzania and Kenya. In these nations, VAT is frequently used in conjunction with foreign financial assistance and donor money to pay for vital health services including HIV/AIDS prevention initiatives and maternity care. However, because tax fraud and informal economies are common in these areas, there are still issues with the effectiveness of VAT collection.

For example, in order to raise more money for health financing, Kenya imposed a value-added tax (VAT) on specific medical supplies, like medical equipment. Although the healthcare infrastructure has improved as a result of this action, issues with VAT enforcement and compliance still exist.

### **Latin America: VAT for Health Initiatives**

In Brazil, the Unified Health System (SUS), which offers millions of Brazilians free healthcare services, is mostly financed by VAT income. Primary care, hospital treatments, and emergency care are just a few of the health services that the government pays for with VAT money. Additionally, public health efforts like immunization programs and anti-smoking campaigns are funded by VAT. But issues like tax fraud and political opposition to higher VAT rates are problems for Brazil. However, despite economic difficulties, Brazil has been able to sustain a somewhat robust healthcare system thanks to the VAT's steady revenue generation.

### **Asia: VAT and Universal Health Coverage (UHC)**

In Asia, nations such as Thailand and Japan have made use of VAT as a key instrument to finance Universal Health Coverage (UHC). One of the most sophisticated healthcare systems in the world is found in Japan, and it is partially financed by VAT. In Thailand, health insurance programs that give the populace access to necessary medical treatment are financed by VAT. Both nations have effectively incorporated VAT into their larger health finance schemes, guaranteeing that the proceeds are used to improve access to care and fortify health systems.

## **BENEFITS OF VAT IN HEALTH FINANCING**

### **Stable and Predictable Revenue**

The stability of VAT as a health finance measure is one of its main benefits. VAT gives governments a steady and reliable stream of income because it is applied to a broad variety of goods and services. Long-term health funding depends on this stability,

particularly in developing nations where outside assistance may not always be dependable.

### **Equity and Inclusivity**

Despite being a regressive tax that disproportionately affects households with lower incomes, VAT can be made more egalitarian by lowering rates for health services and exempting necessities like medications. This guarantees that increased tax burdens won't prevent needy groups from getting the healthcare they need.

### **Efficiency in Revenue Collection**

VAT is regarded as one of the most effective tax structures. VAT is gathered gradually across the supply chain, in contrast to income taxes, which necessitate thorough reporting and compliance audits. By making it harder to evade, this approach increases government revenue and improves overall tax compliance.

## **CHALLENGES AND LIMITATIONS OF VAT IN HEALTH FINANCING**

### **Regressive Nature of VAT**

One of the main arguments against VAT is that it is regressive by nature, placing a greater relative cost on those with lower incomes who spend a greater percentage of their income on VAT-exempt products and services. This problem can be lessened by giving low-income families refunds or by exempting necessities like food and medical care.

### **VAT Evasion and Compliance Issues**

VAT evasion is a serious problem in many developing nations. Non-compliance with VAT is a result of informal economies, improper registration, and inadequate enforcement measures. To increase VAT income, governments must make investments in bolstering VAT collection mechanisms and shrinking the size of the unorganized sector.

### **Political and Institutional Barriers**

Implementing VAT as a health financing tool often faces political resistance. Some policymakers may

resist VAT rate increases, especially in countries with high poverty levels or weak public trust in government institutions. Institutional capacity is also a barrier, as effective VAT management requires strong administrative structures and skilled personnel.

## POLICY RECOMMENDATIONS

1. **Optimizing VAT for Health Financing**  
Governments ought to create VAT schemes that set aside a certain percentage of VAT income for financing healthcare. To lessen the burden on low-income groups, they should also think about lowering or exempting certain critical health products and services from VAT.
2. **Leveraging Technology to Improve VAT Collection**  
Governments ought to spend money on digital tools and platforms that improve the effectiveness of VAT collection. E-invoicing solutions, for instance, can increase the openness of VAT revenue management and lower the likelihood of tax evasion.
3. **International Cooperation and Capacity Building**  
Countries should get assistance from international organisations like the World Bank and the International Monetary Fund (IMF) in fortifying their VAT systems, especially in developing countries where tax fraud poses a serious problem.

## DISCUSSION

A vast range of issues and ramifications for companies, governments, and consumers are made apparent by the implementation of Value Added Tax (VAT) in the manufacturing, services, and agricultural sectors. VAT is a vital and effective source of funding for governments, but because of sector-specific factors including supply chains, market structures, and production methods, its effects on particular industries vary greatly. The wider effects of VAT on these sectors are covered in this part, along with the

important problems that arise and the ways in which policy changes might help.

When it comes to VAT implementation, the agriculture industry poses a special set of difficulties, especially with regard to input tax recovery and exclusions. A large number of agricultural goods, especially food items, are either VAT-free or subject to lower taxes. These policies protect vulnerable groups and keep consumer prices low, but they also lead to systemic inefficiencies. The inability of farmers to recoup VAT paid on inputs such as machinery, seeds, and fertilizer is one of the biggest obstacles they face. This implies that farmers essentially pay the input VAT, which might raise their total production costs and lower their profitability. Farmers are discouraged from investing in inputs that increase production, including new technology or better seeds, in contrast to VAT-registered manufacturers who can claim input VAT through tax credits. The agriculture industry is still quite unorganized in many developing nations, and small farmers might not have access to official VAT registration, which makes tax collection and compliance even more difficult.

Moreover, cross-border transactions are frequently a part of agricultural trade, and export VAT handling might present serious difficulties. Although many nations return VAT on exported goods, the procedure is frequently complicated by bureaucratic procedures and prone to delays. These delays can hinder the competitiveness of agricultural products on global markets and have a negative effect on farmers' cash flow, especially for smallholders. Cross-border agricultural trade may become more difficult as a result of variations in VAT laws and rates among trading nations.

**Policy Considerations:** In order to overcome these obstacles, legislators should think about making sure that agricultural inputs are eligible for VAT credits and streamlining VAT exemptions. To promote greater formalization in the industry, governments might also fund VAT education initiatives. In order to expedite export procedures and minimize VAT refund delays, cross-border VAT systems ought to be standardized.

Because of its intricate supply networks and dependence on intermediate goods and raw resources, the manufacturing sector is particularly impacted by VAT. Manufacturers can typically recover VAT spent on inputs, unlike agricultural farmers, although the intricacy of global supply chains makes recovery more difficult. A complex web of national and international VAT regulations must frequently be negotiated by manufacturers, which can raise administrative expenses and decrease the effectiveness of tax collection. The problem of VAT refunds on exports is one of the biggest obstacles facing manufacturers. The procedure for requesting and obtaining a VAT refund can be difficult, even though many nations exclude exports from VAT in order to preserve their ability to compete globally. Manufacturers may experience severe cash flow issues as a result of refund delays, particularly small and medium-sized businesses (SMEs) who lack the finances to wait for payment. Additionally, manufacturers involved in cross-border trade frequently face a tangle of varying VAT regulations due to the intricacy of VAT systems in many nations. Increased transaction costs are the outcome, which may make firms less competitive in terms of pricing.

VAT compliance in the domestic supply chain presents another difficulty. Many suppliers, some of whom might not be VAT-registered, provide inputs to manufacturers. Manufacturers are unable to claim VAT credits on such inputs in these situations, which may result in increased effective manufacturing costs. This issue is most noticeable in nations with sizable informal sectors, which results in ineffective VAT collection and an unlevel playing field for companies.

**Policy Considerations:** To ensure faster and more transparent reimbursement processes, governments should streamline the VAT refund procedures for exporters. To enable more seamless cross-border transactions, there is also a need for increased cross-border harmonization of VAT regulations, particularly under regional trade agreements. Additionally, promoting digital VAT reporting and using technology to automate VAT

collection could increase compliance rates and lessen administrative responsibilities for producers.

Because services are intangible and different service categories have different VAT regulations, the service sector poses a particularly challenging environment for VAT implementation. In contrast to tangible and easily valuable items, services are intangible, and it is frequently challenging to identify their value-added component. Because of this, there is uncertainty about the proper application of VAT, which results in disparities in the tax treatment of different service sectors.

In the service industry, cross-border VAT concerns are much more noticeable. Applying VAT to services from overseas suppliers has become more difficult as a result of the growth of digital services like software, e-commerce, and digital media. Since service providers frequently operate in numerous jurisdictions with varying VAT laws and rates, the global character of the digital economy makes VAT compliance more difficult. The problem of "place of supply," which establishes which nation has the authority to impose taxes on a specific service, further complicates the application of VAT on cross-border services. This raises the price of compliance for firms, especially SMEs, and causes uncertainty.

In addition, the service sector is often subject to a wide range of exemptions and reduced VAT rates, which can create distortions and inefficiencies. For example, healthcare and educational services are often exempt from VAT to ensure affordability, but this can create inconsistencies when compared to other sectors. While exemptions can promote equity, they can also complicate the VAT system by creating "grey areas" where services with similar characteristics are treated differently for tax purposes.

**Policy Considerations:** Governments need to establish clear and consistent VAT rules for services, especially digital services, to avoid ambiguity and increase compliance. Simplifying VAT treatment across different service sectors could reduce inefficiencies and ensure fair competition.

Furthermore, countries could consider implementing VAT rules that better account for the realities of the global digital economy, such as harmonizing VAT rates for cross-border digital services and simplifying tax collection mechanisms for international e-commerce.

Across all three sectors—agriculture, manufacturing, and services—there are common themes in the challenges posed by VAT. These include the complexity of cross-border trade, the potential for VAT evasion and non-compliance, and the regressive nature of VAT. The regressive nature of VAT, particularly in sectors like agriculture and services, may disproportionately affect low-income households that spend a larger proportion of their income on VAT-taxed goods and services. While governments can mitigate this through exemptions and rebates, these measures can create inefficiencies in the system.

Moreover, VAT is often less effective in informal sectors, where businesses operate outside the formal tax system. Informal enterprises, which are common in agriculture and services, may not register for VAT or may evade VAT payments entirely, undermining the potential for VAT to be a reliable source of revenue. Strengthening VAT compliance in informal sectors and encouraging formalization is a critical challenge for governments, particularly in developing countries.

In summary, VAT presents both opportunities and challenges for different industries. The agricultural, manufacturing, and service sectors each face unique hurdles, but common themes such as the need for simplified VAT rules, improved cross-border cooperation, and better VAT collection systems emerge across all three. By addressing these sector-specific challenges, governments can optimize VAT systems to ensure that they support economic growth while ensuring fairness, efficiency, and sustainability. Comprehensive policy reforms, improved digital systems, and greater international cooperation will be crucial in adapting VAT systems to the evolving needs of businesses in these sectors. Ultimately, the goal should be to create a VAT framework that balances the need for efficient

revenue generation with the need to support industry-specific growth and competitiveness.

## RESULTS

The results of this analysis highlight that VAT has proven to be an effective and sustainable source of revenue for financing public health systems in diverse global contexts. In high-income regions like the European Union, VAT has been successfully integrated into national health financing models, with specific allocations earmarked for health services. Countries like France and Germany demonstrate the advantages of using VAT to maintain universal health coverage, ensuring steady funding for public health infrastructure, services, and programs. In sub-Saharan Africa, despite challenges related to tax evasion and informal economies, nations like Kenya and Tanzania have effectively utilized VAT to support essential health services such as maternal care and HIV/AIDS prevention. However, issues such as inadequate compliance mechanisms and reliance on external aid continue to present challenges in these regions. In Latin America, Brazil's use of VAT for financing its Unified Health System (SUS) has been pivotal in providing free healthcare services to a large portion of the population. However, political resistance to VAT rate increases and tax evasion remain barriers to fully maximizing its potential. In Asia, countries like Japan and Thailand have integrated VAT into their strategies for funding universal health coverage (UHC), ensuring broader access to healthcare services. These countries demonstrate how VAT can support the expansion and sustainability of health systems, especially when paired with well-managed collection mechanisms. Overall, VAT has shown to be a reliable tool for health financing across different global regions, though its effectiveness is contingent upon addressing challenges related to compliance, equity, and political support.

## CONCLUSION

Value Added Tax (VAT) plays an increasingly important role in financing public health systems

worldwide. It provides governments with a stable and reliable source of revenue, which can be directed toward improving healthcare infrastructure, expanding health coverage, and funding essential health programs. However, challenges such as VAT evasion, the regressive nature of the tax, and political resistance must be addressed to fully realize the potential of VAT as a tool for health financing. By adopting best practices from successful case studies and strengthening VAT collection mechanisms, governments can ensure that VAT continues to play a pivotal role in the sustainable financing of public health systems globally.

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