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Goods & Services Tax

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1 Introduction

- India's biggest indirect tax reform since 1947 looks like it has finally arrived – the Goods and Service Tax. From its first official mention in 2009 when a discussion paper was introduced by the previous government to the point when the current government tabled the Constitution Amendment Bill in Parliament, building consensus on the GST hasn't been easy.
- The most prominent hurdle in introducing this new tax structure has been the struggle between the states and the Centre on the loss of revenue. It's taken years to resolve, but even now it is an issue that isn't completely fixed.
- The GST is being introduced not only to get rid of the current patchwork of indirect taxes that are partial and suffer from infirmities, mainly exemptions and multiple rates, but also to improve tax compliances.

2 Proposal of Current GST Bill in the Parliament

The Constitution (122 Amendment) Bill, 2014 seeks to amend the Constitution to introduce the goods and services tax (GST). The GST subsumes various central indirect taxes including the Central Excise Duty, Countervailing Duty, Service Tax, etc. It also subsumes state value added tax, octroi and entry tax, luxury tax, etc.

- **Concurrent powers for GST-:** The Bill inserts a new Article in the Constitution to give the central and state governments the concurrent power to make laws on the taxation of goods and services.
- **Integrated GST (IGST)-**: However, only the centre may levy and collect GST on supplies in the course of inter-state trade or commerce. The tax collected would be divided between the centre and the states in a manner to be provided by Parliament, by law, on the recommendations of the GST Council.
- **GST Council-:** The GST Council will recommend rates of tax, period of levy of additional tax, principles of supply, special provisions to certain states etc. The GST Council will consist of the Union Finance Minister, Union Minister of State for Revenue, and state Finance Ministers.
- **Resolution of disputes-:** The GST Council may decide upon the modalities for the resolution of disputes arising out of its recommendations.
- **Restrictions on imposition of tax-:** The Constitution imposes certain restrictions on states on the imposition of tax on the sale or purchase of goods. The Bill amends this provision to restrict the imposition of tax on the supply of goods and services and not on its sale.
- **Additional Tax on supply of goods**-: An additional tax (not to exceed 1%) on the supply of goods in the course of inter-state trade or commerce would be levied and collected by the centre. Such additional tax shall be assigned to the states for two years, or as recommended by the GST Council.
- **Compensation to states-:** Parliament may, by law, provide for compensation to states for revenue losses arising out of the implementation of the GST, on the GST Council's recommendations. This would be up to a five year period.
- **Goods exempt-:** Alcoholic liquor for human consumption is exempted from the purview of the GST. Further, the GST Council is to decide when GST would be levied on petroleum crude, high speed diesel, motor spirit (petrol), natural gas and aviation turbine fuel.

3 Current Deadlock

For the GST to be reality constitutional amendment is must. To pass constitutional amendment ruling coalition needs support of 2/3rd members in the Rajya Sabha. The Opposition holds key to pass any constitutional amendment. Following are the apprehensions to the current bill that led to deadlock.

- A major sticking point that needs to be resolved concerns the 1% additional levy provided for manufacturing states for two years. The Congress has opposed the additional levy — which will mainly benefit states such as Gujarat and Maharashtra — arguing that it will be market distorting.
- In addition, it wants a GST rate of about 18% to be included in the bill itself.

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- Globally, the GST rate ranges from 16% to 20%. But a subcommittee in November last year suggested a revenue neutral rate (RNR) of 27%, raising concerns that it would, instead of helping industry, end up crippling it. The RNR is supposed to be such as to not cause a revenue loss to states after implementation of GST.
- 13th Finance Commission recommended a rate below 20% so that compliance is higher and tax evasion is lower.
- With its 68 members, the Congress, which originally mooted the idea of GST, is in a better bargaining position to facilitate the passage of the Bill in Rajya Sabha.
- Government has to work on these apprehensions so as to pass the GST bill in coming winter session.

4 Analysis of the Impact of GST Regime

- **<u>Positive Impact:</u>**

    - A unified GST is an economically efficient solution even for the multinationals, which have to compete with the companies in the unorganized sector, as it simplifies the indirect tax structure to one general rate that can be paid by all companies.
    - It will result in substantial reduction in logistics costs and consolidation of warehousing facilities. An inefficient logistics network created using smaller warehouses to save on state taxes has resulted in higher costs and increased inventory levels.
    - GST by subsuming an array of indirect taxes under one rubric, will simplify tax administration, improve compliance, and eliminate economic distortions in production, trade, and consumption.
    - By giving credit for taxes paid on inputs at every stage of the supply chain and taxing only the final consumer, it avoids the 'cascading' of taxes, thereby cutting production costs, and making exports more competitive.

- **<u>Apprehensions:</u>**

    - Article 246A in proposed bill now confers power on Parliament and every state legislature to levy goods and service tax. Thus, we are likely to have one parliamentary law and about 28 state laws that levy GST.
    - The GST Council can only "recommend" a model law but nothing prevents each state from going its own way. The VAT experience is testimony to this. Such multiple levies by Parliament and the states, if not in harmony, will have disastrous consequences.
    - The uncertainty about the final GST rate or rates. While the states want a rate of 26 per cent, the Centre is seeking a cap of 16-18 per cent.
    - A GST levy of even 16 per cent is bound to result in large scale tax evasion at the retail level. It is going to be very difficult to expect a consumer to pay 26 or even 16 per cent on the purchase of a refrigerator costing Rs 50,000.
    - There is also no clarity on the basic threshold exemption and the GST can easily be derailed by multiple rates and numerous exemptions/ concessions.
    - It is argued that the GST regime leads to substantial erosion of the state power to manage its taxing power and resource generation.
    - In a diverse country like India the needs of states like Maharashtra and Gujarat are completely different from states like Jharkhand and Assam. The GST is bound to lead to serious difficulties, and could possibly fail, because it seeks to treat unequal states equally. It will be practically impossible for the Centre to compensate states that are likely to lose tax revenue for the next several years.
    - Some experts have hinted at scraping of the GST regime. Instead it is recommended to subsume all central taxes into a single Central Tax. It is best not to curb the taxing power of the states.

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5 Arvind Subramaniam Panel Report

- A panel under chief economic adviser Arvind Subramanian, constituted by the government to decide on goods and services tax (GST) rates, has recommended a revenue-neutral rate of 15-15.5%, with a standard rate of 17-18% which will be levied on most goods and all services.
- The panel has recommended a three-tier rate structure wherein some essential goods will be taxed at a lower rate of 12%; so-called demerit goods such as luxury cars, aerated beverages, pan masala and tobacco products at a higher rate of 40%; and all remaining goods at a standard rate of 17-18%.
- The committee has recommended doing away with the additional 1% tax to be levied on supply of goods over and above GST.
- It has also recommended broadening the GST base by including petroleum, electricity and real estate.

6 Conclusion

- The indirect taxes are considered regressive compared to direct taxes, which are typically proportional to the ability to pay. It's because the poor and the working classes spend a greater proportion of their income on essential consumption compared to the classes that are better off.
- In light of such scenario government needs to strengthen the social protection measures to neutralize the effects of regressive tax regime.
- Based on the experience of tax reform and the complexities involved, it is important to underline three important issues. First, given that there are 32 actors in the negotiations (29 states, two Union Territories with legislatures and the central government), it would take considerable time to finalize the structure and operational aspects of the tax.
- It would be unrealistic to expect a "flawless" GST. In fact, such a GST structure does not exist in any country where both the centre and states are empowered to levy the tax.
- Every country has to adopt the structure it can administer. The structure that would emerge would be based on the consensus reached and it is necessary to ensure that the fundamental, sound features of the tax are not compromised.
- Finally, for the above reason, it is important to consider the GST reform as a process rather than an event. Once the basic features of the tax are implemented, it would be necessary to improve the structure and operational aspects of the tax over time.
- Arvin Subramaniam Panel has addressed the main concerns raised by the opposition to GST regime. With this acceptance its likely that GST bill wil be passed in the Parliament in Budget Session of 2016.

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