



# A study of key reforms with new taxation system (GST) in India

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## Abstract:

*GST is one of the most crucial tax reforms in India which has been long pending. It was supposed to be implemented from April 2010, but due to political issues and conflicting interests of various stakeholders it is still pending. It is a comprehensive tax system that will subsume all indirect taxes of states and central governments and unified economy into a seamless national market. It is expected to iron out wrinkles of existing indirect tax system and play a vital role in growth of India. This paper presents an overview of GST concept, explains its features along with its timeline of implementation in India. The paper is more focused on advantages of GST and challenges faced by India in execution.*

**Keywords:** GST; India; Indirect tax; Goods and Service Tax; export

## 1. Introduction

The proposed GST is likely to change the whole scenario of current indirect tax system. It is considered as biggest tax reform since 1947. Currently, in India complicated indirect tax system is followed with imbrications of taxes imposed by union and states separately. GST will unify all the indirect taxes under an umbrella and will create a smooth national market. Experts say that GST will help the economy to grow in more efficient manner by improving the tax collection as it will disrupt all the tax barriers between states and integrate country via single tax rate. GST was first introduced by France in 1954 and now it is followed by 140 countries. Most of the countries followed unified GST while some countries like Brazil, Canada follow a dual GST system where tax is imposed by central and state both. In India also dual system of GST is proposed including CGST and SGST

## 2. Objective of GST

One of the main objectives of GST would be to eliminate the cascading impact of taxes on production and distribution cost of goods and services. The exclusion of cascading effects i.e. tax on tax will significantly improve the competitiveness of original goods and services which leads to beneficial impact to the GDP growth. It is felt that the GST would serve a superior reason to achieve the objective of streamlining indirect tax regime in India which can remove cascading effects in supply chain till the level of final consumers only when all such above mentioned indirect taxes are completely included in GST. It is understood that alcohol, tobacco and petroleum products will not be enclosed by GST as alcohol and tobacco are considered as in Goods and governments do not like to allow free trade on these property.

## 3. Benefits of GST

1. GST provide comprehensive and wider coverage of input credit setoff, you can use service tax credit for the payment of tax on sale of goods etc.
2. CST will be removed and need not pay. At present there is no input tax credit available for CST.
3. Many indirect taxes in state and central level included by GST You need to pay a single GST instead of all.
4. Uniformity of tax rate across the states

#### 4. Disadvantage of GST

1. Some Economist say that GST in India would impact negatively on the real estate market. It would add up to 8 percent to the cost of new homes and reduce demand by about 12 percent.
2. Some Experts says that CGST (Central GST), SGST (State GST) are nothing but new names for Central Excise/Service Tax, VAT and CST. Hence, there is no major reduction in the number of tax layers.
3. Some retail products currently have only four percent tax on them. After GST, garments and clothes could become more expensive.
4. The aviation industry would be affected. Service taxes on airfares currently range from six to nine percent. With GST, this rate will surpass fifteen percent and effectively double the tax rate.

#### 5. Literature Review

- Agogo Mawuli (May 2014) studied, “Goods and Service Tax-An Appraisal” and found that GST is not good for low-income countries and does not provide broad based growth to poor countries. If still these countries want to implement GST then the rate of GST should be less than 10% for growth
- Dr. R. Vasantha gopal (2011)studied,“GST in India: A Big Leap in the Indirect Taxation System” and concluded that switching to seamless GST from current complicated indirect tax system in India will be a positive step in booming Indian economy. Success of GST will lead to its acceptance by more than 130 countries in world and a new preferred form of indirect tax system in As in also.
- Ehtisham Ahmed and Satya Poddar (2009)studied, “Goods and Service Tax Reforms and Intergovernmental Consideration in India” and found that GST introduction will provide simpler and transparent tax system with increase in output and productivity of economy in India. But the benefits of GST are critically dependent on rational design of GST.
- Nitin Kumar (2014) studied, “Goods and Service Tax- A Way Forward” and concluded that implementation of GST in India help in removing economic distortion by current indirect tax system and expected to encourage unbiased tax structure which is indifferent to geographical locations.
- Pinki, Supriya Kamma and Richa Verma (July 2014) studied, “Goods and Service Tax- Panacea For Indirect Tax System in India” and concluded that the new NDA government in India is positive towards implementation of GST and it is beneficial for central government, state government and as well as for consumers in long run if its implementation is backed by strong IT infrastructure.

#### 6. Title of the Study

A study of key reforms with new taxation system (GST) in India

#### 7. Objective of Study

The study has following objectives:

1. To cognize the concept of GST
2. To study the features of GST
3. To evaluate the advantages and challenges of GST
4. To furnish information for further research work on GST.

#### 8. Research Methodology

Being an explanatory research it is based on secondary data of journals, articles, newspapers and magazines. Considering the objectives of study descriptive type research design is adopted to have more accuracy and rigorous analysis of research study. The accessible secondary data is intensively used for research study.

## 9. Timeline of GST in India

In 2000, an empowered committee was set up by NDA government under the chairmanship of Asim Das Gupta to design GST model. With UPA in power union finance minister, Mr. P.Chidambaram, proclaimed the implementation of GST from April 2010 in budget of 2007 and set up an empowered committee of state Finance ministers to work with center. Therefore, on 10 May 2007 Joint Working Group was set up by empowered committee of state finance ministers which submitted the report in Nov 2007. First detailed discussion paper on structure of GST was introduced by empowered committee in Nov 2009 with the objective of generating a debate and getting the inputs from all stakeholders. It suggested a dual GST Module along with a GST council and finally in March 2011, constitution 115<sup>th</sup> amendment bill was introduced to draw up laws for implementing GST. It includes the followings:

1. Setting up of GST COUNCIL by the president within 60 days of passage of bill. The council will be chaired by union finance minister and its members include MoS for revenue and finance ministers of states. It will work on GST rates, exemption limit etc.
2. Setting up of a GST Dispute Settlement Authority having three members to resolve dispute arising among states and take action against states.
3. GST Amendment Bill was referred to parliamentary committee on finance for evaluation.

In Aug 2013 the standing committee submitted the report and recommended that proposed Dispute Settlement Authority should be removed and its mechanism should be given to GST Council itself. It also recommended that GST Council should take decision by voting rather than consensus. The representation in the GST Council should be 1/3 from central and rest 2/3 from states. The decision in the council should be passed with more than 3/4 vote representatives present. The quorum of council is raised from proposed 1/3 to half by standing committee. But the proposed 115 amendment bill was lapsed with dissolution of 15<sup>th</sup> Lok Sabha. On 19 Dec 2014 after making slight changes in GST Bill, NDA government redefined it in 16<sup>th</sup> Lok Sabha as 122<sup>nd</sup> amendment of constitution. On 6 May 2015 it passed in lower house of government. Currently, the 122<sup>nd</sup> constitutional amendment is crag fasted in Rajya Sabha where it has to be passed with 2/3<sup>rd</sup> majority in order to be implemented from 1 April 2016

## 10. Features of Proposed GST

### 10.1 Ambit of GST

- It is applied to all taxable goods and services except the exempted goods and services and on transactions below the threshold limit.
- Exempted goods and services include alcohol for human consumption, electricity, custom duty, real estate. [Proposed article 366(12A)]
- Petroleum products [crude oil, HSD (high speed diesel), motor spirit (petrol), natural gas, ATF (aviation turbine fuel)] are initially exempted from GST till the GST Council announces date of their inclusion.
- Tobacco products are included in GST along with central excise tax.

### 10.2 Imposition and Collection of GST

- The power of making law on taxation of goods and services lies with both union and state legislative assemblies. A law made by union on GST will not overrule a state GST law. (proposed article 246A)
- GST has two components CGST and SGST as discussed above. CGST will be collected by central government whereas states governments will collect SGST.
- IGST is levied on supplies in the course of interstate trade including imports which is collected by central government exclusively and distributed to imported states as GST is destination based tax. The proportion of distribution between center and states is decided on recommendation of GST Council. (proposed article 269A).

**10.3 GST council**

1. It is set up by president under article 279-A. It is chaired by union finance minister.
2. It will constitute union minister of state in charge of revenue and minister in charge of finance or taxation or of any other field nominated by state governments. The 2/3<sup>rd</sup> representatives in council are from states and 1/3<sup>rd</sup> from union.
3. The decision of council is made by 3/4<sup>th</sup> majority of the votes cast and quorum of council is 50%.
4. It will make recommendations on
  - a) Taxes, surcharge, cess of central and states which will be integrated in GST.
  - b) Goods and services which may be exempted from GST
  - c) Interstate commerce – IGST- proportion of distribution between state and center
  - d) Registration threshold limit for GST
  - e) GST floor rates
  - f) Special rates during calamities
  - g) Provision with respect to special category states specially north east states
  - h) It may also work as Dispute Settlement Authority for GST.

**10.4 Additional 1% Tax**

1. Additional 1% tax on interstate taxable supply of goods which is levied by center and directly portioned to the exporter state (originstate).
2. This tax will be charged for two years or for longer time period recommended by GST Council.

**11. Compensation to States**

1. For maximum of 5 years union will compensate states for the revenue losses arising out of GST implementation.

This compensation will be made on the recommendation of GST Council

**12. Challenges of GST****12.1 High Revenue Neutral Rate (RNR)**

RNR is the rate which neutralize revenue effect of state and central government due to change in tax system, means, the rate of GST which will give at least the same level of revenue that is currently earned by state and central governments from indirect taxes is known as RNR. As per 13 finance commission the RNR should be 12% whereas state empowered committee demanding 26.68%. Union government is reckoning the rate band should be 15%-20% which is very high as compare to other countries. Hungary implemented GST from 1/4/2014 with 7% rate. Due to high RNR

- Competitive edge of India in Asian giants will decrease and domestic industry may be wrecking.
- Tax evasion and smuggling will increase.
- Regressive nature of indirect taxes will badly affect the purchasing power of poor people which will have negative impact on human development index.

So, before implementing GST, RNR should be minimized. This can be achieved by inclusion of petrol, liquor, land, electricity within the ambit of GST which will enhance the tax base and increase revenue of government.

**13. Compensation to States**

Currently, VAT is highest contributor in tax revenue of state governments. But after GST reform this will subsumed along with surcharge and cess into GST. Due to which state governments will occur revenue loss for sure and they will be more dependent on finance commission for tax devolution (currently 42%). To neutralize their revenue losses states are demanding compensation from union government. As per 14 finance commission union has to compensate states for maximum of five years with tapering effects. For first three years 100% compensation reduced to 75% and 50% in fourth and fifth year respectively. This compensation by union will lead to fiscal burden and may not fulfill the

fiscal deficit target of 3% by March 2017 announced by finance minister in 2015 budget. This fiscal target must be achieved for faster economy growth and full capital account convertibility in future.

Industrialized states will be at loss in GST regime due to its destination based feature. It will demotivate the manufacturing industry and incite states to import more in order to increase their tax revenue. It is not good for manufacturing industry as well as for India because boosted manufacturing sector is the main driver of our economic growth in future. For temporarily relief to industrialized states additional 1% tax for two years on interstate sale and supply of goods is proposed in GST. But with 1% additional tax, the main objective of GST to minimize cascading effect of taxes is fading out. So, to minimize cascading effect this additional tax at least should not be levied on supply of interstate goods.

#### **14. Registration Threshold Limit**

At present there are different threshold limits for VAT (5 lacs), service tax (10 lacs) and excise duty (1.5 crore). But for implementation of GST common threshold limit for all indirect taxes is required. It will turn into a conflict between state and center. States want to fix the limit as 10 lacs opposing 25 lacs limit suggested by union. The lower threshold limit will broaden the tax base and increase the revenue of government but it will also require a dandy IT infrastructure, to address the database of increased assess, which is presently missing out in Indian states. IT infrastructure will play a vital role in implementing IGST as union will electronically distribute IGST to states. To grapple the data base a strong network is required which is managed by GSTN (Goods and Service Tax Network) proposed in GST. GSTN has major responsibility to tackle biggest challenge of IT infrastructure in a time bound manner.

#### **15. Way forward for Implementation of GST**

1. The 122<sup>nd</sup> amendment bill to be passed by upper house with 2/3<sup>rd</sup> majority and then will be ratified by at least 50% state legislatures and will be followed by assent of president.
2. After the bill has been passed, GSTC (GST Council) to be established.
3. GSTC to advocate GST law and procedure.
4. GST law to be introduced in parliament.
5. GSTN (GST Network) a section- 25 company established to design IT infrastructure of GST

#### **16. Conclusion**

Due to dissilient environment of Indian economy, it is demand of time to implement GST. Consumption and productions of goods and services is undoubtedly increasing and because of multiplicity of taxes in current tax regime administration complexities and compliance cost is also accelerating. Thus, a simplify, user -friendly and transparent tax system is required which can be fulfilled by implementation of GST. Its implementation stands for a coherent tax system which will colligate most of current indirect taxes and in long term it will lead to higher output, more employment opportunities and flourish GDP by 1-1.5%. It can also be used as an effective tool for fiscal policy management if implemented successfully due to nation-wide same tax rate. It execution will also results in lower cost of doing business that will make the domestic products more competitive in local and international market. No doubt that GST will give India a world class tax system by grabbing different treatment to manufacturing and service sector. But all this will be subject to its rational design and timely implementation. There are various challenges in way of GST implementation as discussed above in paper. They need more analytical research to resolve the battling interest of various stake holders and accomplish the commitment for a cardinal reform of tax structure in India.

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