# A STUDY ON GST AND IT's IMPACT ON SMALL BUSINESS ENTERPRISES

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***Abstract:*** ***The Goods and Services Tax (GST) has been heralded as the biggest indirect tax reform in India after Independence. After much deliberation, the GST bill has been passed in the Rajya Sabha and is set to be discussed in the state legislative assemblies in this winter session. With the ball set to roll for a unified country-wide tax reform, the market is filled with new found optimism amongst industry leaders and government officials. This sets the necessary momentum for the passage of the two Bills—Central GST (CGST) and Integrated GST (IGST) Bills—during the winter session along with the State GST Bill by different state assemblies. According to industry experts and government sources, the GST rollout date of April 1, 2017 is likely to be met. With this, enterprises, particularly SMEs, across a wide range of industries are caught in a state of flux. The comprehensive indirect tax GST will replace various other taxes such as Excise, Vat and Service Tax with a single tax structure. Driven by wide-ranging skepticism, several startups and SMEs are wary of the adverse impacts that may come into the picture with the GST rollout.***

***Keywords: Tax Slabs, Economy, Financial Reforms, Advantages, Enterprise.***

## I. Introduction

Goods and Services Tax(GST) is one of the most awaited tax reforms that is set to happen during the Financial Year 2017-18, improving the ease of doing business for many micro and small business Enterprises in India by reducing compliances. By incorporating multiple taxes into a single tax system, the complexities would be reduced while tax base would rise substantially. Under the new GST process, all entities that are involved in buying or selling of goods or providing any services or both are required to obtain GST registration compulsorily Entities without the registration of GST will not be permitted to collect GST from customer or claim the input tax credit of GST paid. Also, the GST registration is mandatory once an entity crosses the minimum threshold turnover. Under the GST bill, the Indian economy will see an economic integration. One will see all other taxes getting consolidated into one, it will restructure the indirect taxation, making the taxation process humbler. So, instead of paying, Octroi, Central Excise VAT i.e. the value added taxes etc., including few other indirect taxes, the taxpayers will only pay one amalgamated tax.

## II. History of GST

The word tax is derived from the Latin word taxare' meaning to estimate. A tax is not a voluntary payment or donation, but an enforced contribution, exacted pursuant to legislative authority" and is any contribution imposed by government whether under the name of levy, tribute, impost, duty, custom, excise, subsidy, aid, supply, or other name."1 The first known system of taxation was in Ancient Egypt around 3000 BC - 2800 BC in the first dynasty of the Old Kingdom. Records from that time show that the pharaoh would conduct a biennial tour of the kingdom, collecting tax revenues from the people. Other records are granary receipts on limestone flakes and papyrus. Early taxation is also described in the Bible. In Genesis2, it states "But when the crop comes in, gives a fifth of it to Pharaoh. The other four-fifths you may keep as seed for the fields and as food for yourselves and your households and your children." Joseph was telling the people of Egypt how to divide their crop, providing a portion to the Pharaoh. A share3 of the crop was the tax. In India, the tradition of taxation has been in force from ancient times. It finds its references in many ancient books like 'Manu Smriti'4 and 'Arthasastra'. The Islamic rulers imposed jizya5. It was later on abolished by Akbar. However, Aurangzeb, the last prominent Mughal Emperor, levied jizya on his mostly Hindu subjects in 1679. Reasons for this are cited to be financial stringency and personal inclination on the part of the emperor, and a petition by the ulema6. The period of British rule in India witnessed some remarkable change in the whole taxation system of India. Although, it was highly in favour of the British government and its exchequer but it incorporated modern and scientific method of taxation tools and systems. In 1922, the country witnessed a paradigm shift in the overall Indian taxation system. Setting up of administrative system and taxation system was first done by the Britishers. Broadly, there are two types of Taxes viz. Direct7 and Indirect taxes8. Taxes in India are levied by the Central Government and the State Governments.

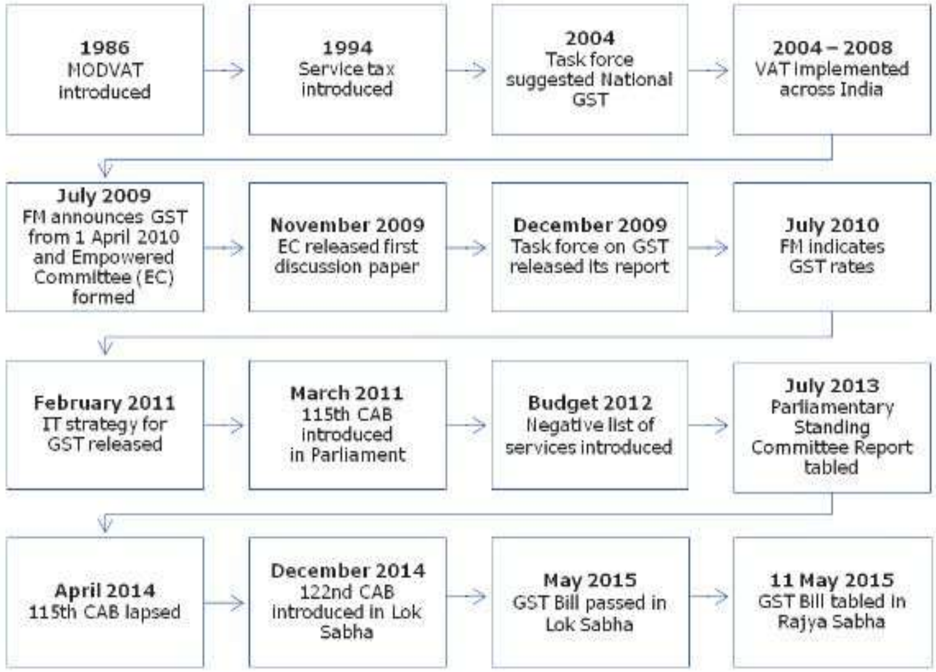



Fig 1: Taxes in India are levied by the Central Government and the State Governments

Some minor taxes are also levied by the local authorities such as Municipality or Local Council. The authority to levy tax is derived from the Constitution of India which allocates the power to levy various taxes between Centre and State.

**2. Major milestones in Indirect Tax reform**

1974 Report of LK Jha Committee suggested VAT1986 Introduction of a restricted VAT called MODVAT1991 Report of the Chelliah Committee recommends VAT/GST and recommendations accepted by Government1994 Introduction of Service Tax1999 Formation of Empowered Committee on State VAT2000 Implementation of uniform floor Sales tax rates Abolition of tax related incentives granted by States2003VAT implemented in Haryana in April 20032004 Significant progress towards CENVAT2005-06 VAT implemented in 26 more states2007 First GST stuffy released By Mr. P. Shome in January2007 F.M. Announces for GST in budget Speech2007 CST phase out starts in April 20072007 Joint Working Group formed and report submitted2008 EC finalises the view on GST structure in April 2008

**III. INTRODUCTION OF GST**:

Introduction of the Value Added Tax (VAT) at the Central and the State level has been considered to be a major step –an important step forward –in the globe of indirect tax reforms in India. If the VAT is a major improvement over the pre-existing Central excise duty at the national level and the sales tax system at the State level, then the Goods and Services Tax (GST) will indeed be an additional important perfection –the next logical step –towards a widespread indirect tax reforms in the country. Initially, it was conceptualized that there would be a national level goods and services tax, however, with the release of First Discussion Paper by the Empowered Committee of the State Finance Ministers on 10.11.2009, it has been made clear that there would be a “Dual GST” in India, taxation power –both by the Centre and the State to levy the taxes on the Goods and Services. Almost 150 countries have introduced GST in some form. While countries such as Singapore and New Zealand tax virtually everything at a single rate, Indonesia has five positive rates, a zero rate and over 30 categories of exemptions. In China, GST applies only to goods and the provision of repairs, replacement and processing services. GST rates of some countries are given below. Country Australia France Canada Germany Japan Singapore Sweden New Zealand Rate of GST 10% 19.6% 5% 19% 5% 7% 25% 15%World over in almost 150 countries there is GST or VAT, which means tax on goods and services. Under the GST scheme, no distinction is made between goods and services for levying of tax. In other words, goods and services attract the same rate of tax. GST is a multi-tier tax where ultimate burden of tax fall on the consumer of goods/ services. It is called as value added tax because at every stage, taxis being paid on the value addition. Under the GST scheme, a person who was liable to pay tax on his output, whether for provision of service or sale of goods, is entitled to get input tax credit(ITC) on the tax paid on its inputs.

**Objective of the study**

1) To study the GST impact on Indian Economy in General
2) To know positive impact of GST on SME
3) To study the negative impact on SME due to GST implementation.
4) Impact of GST on Small and Medium Enterprises (SMEs)

With only a few months left before the implementation of GST, small business owners are engrossed in understanding the potential effects of GST on their business. It’s a well-known fact that SMEs (Small and Medium Enterprises) are the primary growth drivers of the economy and major contributors to the GDP. While some business owners have lauded the Government of India for implementing GST, others are not very convinced. To comprehend the overall effect of GST on your business, let’s take a look at the pros and cons of the new regime from a small-business perspective.

**A. Positive impacts of GST on SMEs:**

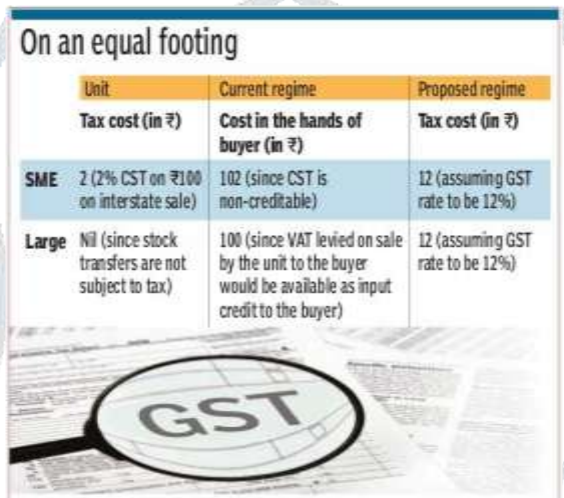
*1. Launching a new business becomes easier*

Under the previous tax regime, if your business had operations across multiple states, you would need to register for VAT with each state's sales tax department in order to carry out business activities there. The fact that every state had different tax rules complicated the entire process, and business owners had to pay multiple procedural fees for VAT registration. Under GST, the registration is centralized and the rules are uniform for all the states across the country. All you have to do is complete and submit an online form to obtain a GSTIN (GST Identification Number). Launching a new business, and subsequently expanding it, will be comparatively easier under the GST regime.

*2. The entire process of taxation becomes simpler*

The prime reason GST is implemented is to remove cascading taxation. It reduces the complications caused by the overlap between Central taxes (Excise duty, customs duty, service tax, etc.) and State taxes (VAT, purchase tax, luxury tax, etc.), because it levies a uniform tax on goods and services all over India. The taxes on goods and services levied under VAT, purchase tax, and luxury tax will now be merged into one single tax with one common return. If you've spent a large portion of your time on managing multiple taxes, you can relax under the new regime because filing and paying taxes is easier with the GSTN portal.

A combined tax also means dealing with fewer tax authorities. Previously, business owners had to deal with many different tax authorities depending on the nature of their business and transactions. Under GST, you can be sure that the relevant authority is always either the Centre or the State government. As per the current tax structure, businesses with a turnover of more than rupees 5 Lakh need to pay a VAT registration fee. The government mulls the exemption limit under GST to twenty five Lakh giving relief to over 60% of small dealers and traders.



On an equal footing

| | Unit | Current regime | Proposed regime |
|---|---|---|---|
| | Tax cost (in ₹) | Cost in the hands of buyer (in ₹) | Tax cost (in ₹) |
| SME | 2 (2% CST on ₹100 on interstate sale) | 102 (since CST is non-creditable) | 12 (assuming GST rate to be 12%) |
| Large | Nil (since stock transfers are not subject to tax) | 100 (since VAT levied on sale by the unit to the buyer would be available as input credit to the buyer) | 12 (assuming GST rate to be 12%) |



*Fig 2: Source: Jaswal (2014)*

***3. Reduced cost of logistics***

The current tax regime has created a lot of hassles for the transportation sector. The long queues at checkpoints and inter-state entry points have caused vehicles to stand idle for long periods of time, adding to labor and fuel costs. Businesses transporting goods to other states have had a hard time filing paperwork and paying entry taxes at the inter-state borders, further delaying the delivery of goods.

Under GST, the current Central Sales Tax (CST) on interstate sales will be replaced with a combined tax called IGST, which is composed of CGST and SGST and collected by the Central Government. As the removal of border and check-post taxes makes state boundaries less significant under the GST regime, both the delay and the transportation cost will be reduced. This will increase inter-state business, facilitate faster movement of goods, and reduce maintenance costs. Under the GST bill, no entry tax will be charged for goods manufactured or sold in any part of India. As a result, delivery of goods at interstate points and toll check posts will be expedited. According to an estimate by CRISIL, the logistics cost for manufacturers of bulk goods will get reduced significantly—by about 20%. This is expected to boost ecommerce across the nation.

***4. The distinction between goods and services will be eliminated***

Previously, businesses providing both goods and services had to calculate the VAT and service taxes individually. GST eases the process by removing the distinction between goods and services; tax will be calculated for the final total, not individual products or services. This will help SMEs take advantage of the tax incentives for payment on the procurement of input goods and services (like import, interstate and local purchases, and telephone services).

Currently, every invoice contains a long and confusing list of taxes levied on the goods and services involved in the transaction. GST will make invoicing simpler, as only one tax rate will need to be mentioned.

***5. Increased threshold limits for new businesses***

Under the current regime, businesses with a moderate annual turnover (Rs.5 lakh in some states and Rs.10 lakh in other states) are supposed to register and make payments for VAT. Under GST, this burden is eliminated for many businesses, since a business does not have to register or pay if its annual turnover is less than Rs.20 Lakh (Rs.10 Lakh in North Eastern states). Also, under the composition scheme, businesses with turnover between Rs.20-Rs.50 Lakh will pay GST at a lower rate. This should have a positive effect on startups and other small businesses by relieving them from tax burdens.

**B. Limitations of GST:**

Though there are a lot of advantages to GST, SMEs may have reservations about transitioning to GST and getting used to the new tax regime within a short period of time. Their concerns might include increased compliance costs and numerous returns. Here are a few negative effects of GST that are likely to affect SMEs.

**Negative impact of GST on SMEs:**

***1. Multiple registrations for Pan-India businesses***

Under the new regime, a business will have to register online for GST in every state involved in its sales process. If your business delivers goods across 5 states, then you'll have to register for GST in those 5 states to carry out your business activities. Since the entire registration process takes place online, small business owners who are not used to working online might not find the transition easy.

***2. Returns must be filed on a monthly basis***

Under GST, there will be around 36 returns in a fiscal year. GST returns will also require you to close your books on a monthly basis, which, realistically, will take a lot of time. The time that business owners spend filing these returns could instead be spent on other productive activities, like developing their business and acquiring clients.

To top it off, until you've filed the relevant returns, you cannot claim refunds and your customers cannot claim tax credit for the goods they bought from you. Should you miss a single return, you'll be penalized Rs.100/- a day and your compliance rating on the GSTN portal will be reduced.

***3. Cost of tax compliance is likely to increase***

As mentioned above, consistently filing 3 returns a month, periodically reconciling your transactions, and uploading invoices regularly will give rise to the need for an accountant with technical expertise. Hiring an accountant and paying them, adds to the burden on small businesses. It's tedious to maintain separate books of accounts for every state involved in the supply of goods/services and assess the records of various entities involved in every single transaction. To cope with the system, small businesses might use the services of licensed third parties that help firms comply with the GST regime. For this convenience, small businesses will have to dish out a sum ranging from Rs.1000-Rs.5000, depending on the kind of service that is rendered to them.

***4. Registration will be mandatory for e-commerce suppliers and operators***

Businesses carrying out activities related to e-commerce should register under GST irrespective of their annual turnover rate. Unlike other types of businesses, e-commerce firms will not be eligible for threshold exemptions or for the Composition Scheme (which allows firms to file their tax returns on a quarterly basis instead of 3 times a year and pay taxes at a much lower rate).Also, e-commerce firms should register for GST in every single state where they supply goods. Overall, GST simplifies the entire process of filing and paying taxes. It will also increase the competition between SMEs by unifying the Indian market. If you're proactive and take care of your GST compliance measures beforehand, you can minimize the potential negative effects of the new regime on your business. In the long term, GST is expected to have a positive impact on SMEs and the Indian economy as a whole.

## IV. CONCLUSION

India's paradigm shift to the Goods and Services Tax (GST) regime brought majority of MSME's into the indirect tax net for the first time and thereby increased compliance costs for MSME's. Complying with GST is bit complex for MSME's at present. SMEs will have to opt for electronic compliance system, starting from registering to filing online returns. This will primarily cause teething problems and will also increase the cost of compliance. GST would improve demand and competitiveness of 'Made in India' products. It is most likely that the burden of indirect tax will reduce both for the producer of goods and the ultimate end user except in some cases, as the producer or manufacturer of goods will get the advantage of input tax credits (ITC) and the consumer will have to bear only the indirect tax charged by the last retailer or dealer in the supply chain. Under the Goods and Service Tax system, self-supplies or interstate stock transfer will fall under the scanner of GST. This will have a certain impact on the working capital requirements resulting in higher interest cost and eventually impact pricing policies.

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