

# VARIOUS FACETS OF NEW TAX REFORM IN INDIA: THE GST

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## ABSTRACT

GST is one of the most sought reforms in Indian economy. Present paper is concerned with the opportunities and challenges related to GST in its way from parliament to people. Passage of the Constitution Amendment bill on the GST was a great moment for Indian democracy and federalism. First considered almost 30 years ago, GST once implemented, expected to do away with multiple indirect taxes, make the economy more effective and transform the country into single market, which at present divided into 30 different markets of 29 states and 1 center. However, there are various issues pertaining to the remaining gaps in the proposed structure as well as the consequences expected from those anomalies. Therefore, this paper is the study of both the sides of the coin.

The paper divided into three sections related to the introduction as first part, opportunities fostered as the seconds and the third part related to the challenges coming its way. Secondary data will be used for the purpose.

**KEY WORDS:** GST, Indirect tax, Business, Economy

## INTRODUCTION

The ongoing tax reforms on moving to a good and services tax would impact the national economy, international trade, firms and consumers. Make in India mission launched on September 24, 2014 under the visionary leadership of Prime Minister Narendra Modi, designed to transform India into a global manufacturing hub. This national program needs to meet the national requirements besides achieving the global standards. So, it becomes imperative to address the related issues and prescribe measures to facilitate “ease of doing business” in India. GST is one of the most desirable steps to be taken for making business doing more flexible and attractive. India must ready for a future where more literacy means more litigation. GST is as huge a political project as the European Union once was. India will face a similar challenge with GST, for it is a one-way street: easy to get in, but almost impossible to get out. It is the politics of GST implementation that is daunting. The mechanism of implementation – getting the GST Network up and running, training tax officials to handle the new system and nudging the companies to install the necessary software and hardware at their ends - will be hard enough. Even though the country has moved on the path of tax reforms since the mid-1980s yet there are various issues which need to be reconstructed so as to boost productivity and international competitiveness of Indian exporters.

## LITERATURE REVIEW

Empowered Committee of State Finance Ministers (2009) introduced their First Discussion Paper on Goods and Services Tax in India and discussed in detail the structure and loopholes if any in GST.

Ehtisham Ahmed and Satya Poddar (2009) studied, “Goods and Service Tax Reforms and Intergovernmental Consideration in India” and found that GST introduction will provide simplified and

transparent tax system leading to increase in output and productivity of economy in India. But the benefits of GST are critically dependent on rational design of GST.

Dr. R. Vasanthagopal (2011) in his study “GST in India: A Big Leap in the Indirect Taxation System” said 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 Asia also.

Girish Garg (2014) in his article “Basic Concepts and Features of Goods and Service Tax In India” gave the introduction, in general of GST and have tried to highlight the objectives the proposed GST is trying to achieve. Thereafter, he discussed the possible threats and opportunities that GST brings before us to strengthen our free market economy.

Pinki, Supriya Kamma and Richa Verma (2014) in their paper “Goods and Service Tax- Panacea For Indirect Tax System in India” 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.

Nitin Kumar (2014) in “Goods and Service Tax- A Way Forward” concluded that GST implementation 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.

Nishitha Gupta (2014) in her study pointed that implementation of GST in the Indian framework will lead to commercial benefits untouched by the VAT system and would essentially lead to economic development. Hence GST may usher in the possibility of a collective gain for industry, trade, agriculture and common consumers as well as for the Central Government and the State Government.

Jaiprakash (2014) in his research study mentioned that the GST at the Central and the State level are expected to give more relief to industry, trade, agriculture and consumers through a more comprehensive and wider coverage of input tax set-off and service tax setoff, subsuming of several taxes in the GST and phasing out of CST. Responses of industry and also of trade have been indeed encouraging.

Indirect Taxes Committee of Institute of Chartered Accountants of India (ICAI) (2015) submitted a PPT naming Goods and Service Tax (GST) which stated in brief details of the GST and its positive impact on economy and various stakeholders

Monika Sehrawat and Upasana Dhanda (2015) in their paper “GST IN INDIA: A KEY TAX REFORM” studied the GST concept, its features along with its timeline of implementation in India.

The Institute of Companies Secretaries of India (ICSI) (2015) published a Referencer on Goods and Service Tax to provide the information on the concept of GST in details

Parkhi (2015) in an article” Goods and Service Tax in India: the changing face of economy” through her exploratory research stated that implementation of GST is a changing face of India and the government is well equipped for that which is a symptom of fast paced economy.

## OBJECTIVES

- To study the history and need of GST in India
- To understand the process and working of GST
- To list out the various opportunities and challenges attached with the new reform

## RESEARCH METHODOLOGY

This paper is an explanatory and exploratory kind of research. Secondary data available through various government and non-government sites, papers and reports etc. is mainly used for the purpose. Keeping in mind 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 paper.

## SECTION: 1- INTRODUCTION

### 1.1 HISTORY: HOW IT STARTED

Table 3: Reforms in Indirect Taxation System Year Reforms

1974	Report of LK Jha Committee suggested VAT should be introduced
1986	Introduction of a restricted VAT called MODVAT
1994	Introduction of Service Tax @ 5%
1991	Report by the Chelliah Committee recommended either VAT or GST which was accepted by Government
1999	Formation of Empowered Committee on State VAT
2000	Implementation of uniform floor rate of tax for VAT at the rate 1%, 4% and 12.5%. and Abolition of tax related incentives granted by States
2003	VAT implemented in Haryana in April 2003
2004	Significant progress towards CENVAT, MODVAT was abolished and credit account was merged with service tax and excise to provide for cross utilization.
2005-06	VAT implemented in 26 more states
2007	<ul style="list-style-type: none"> <li>• First GST released By Mr. P. Shome in January</li> <li>• Finance Minister announces for GST in budget Speech and CST phase out starts in April 2007. Then, Joint Working Group formed and submitted report</li> </ul>
2008	EC finalizes the view on GST structure in April 2008
2009	First discussion paper on GST was released and commission submitted report proposing GST to be implemented from 1.4.2010
2010	Department of Revenue commented on GST discussion paper and Finance Minister suggested probable GST rate.
2011	Team was set up to lay down road map for GST and 115th Constitutional Amendment Bill for GST was laid down in Parliament
2012	Negative list regime for service tax was implemented
2013	Parliamentary Standing Committee submitted its report on the Bill
2014	115th Amendment Bill lapsed and was reintroduced in 122nd Constitutional Amendment Bill

### 1.2 GST NEED IN INDIA

In India, indirect taxes are levied by the Centre and the State Government as per the Constitutional provisions of Article 246, Seventh Schedule. India is having a federal finance system which requires financial independence and adequacy form the backbone. The essence of this form is that the Centre and the State Governments should be independent of each provided with the sources of raising adequate revenues to discharge the functions entrusted to it. At present tax laws in India are origin-based, structured to levy and collect at the point of happening of prescribed tax event, which ranges from point of manufacture or sale or provision of services or imports/exports.

The various tax laws are levied and collected as follows:

Tax	Taxable Event	Levied by	Collected by
Central Excise Duty	Manufacture of Goods in India (excluding goods manufactured in SEZ in India)	CG	CG
Service Tax	Provision of Service in Taxable Territory	CG	CG
Sales Tax/ VAT	Sale of goods within the State	SG	SG
Customs Duty	Import into India from a place outside India or Export from India to a place outside India	CG	CG
Central Sales Tax (CST)	Sale of goods Inter-State (i.e. from one State to another State)	CG	SG
Local Body Tax (Entry Tax/Octroi)	Entry of goods to a State from a place outside the State	SG	SG

Where, CG = Central Government; SG = State Government

Under the visionary leadership of Prime Minister Narendra Modi, “Make in India-mission” launched on 24<sup>th</sup> September, 2014, which is designed to transform India into global manufacturing hub besides achieving global standards. So it becomes imperative to address the related issues and also prescribe measures to facilitate “ease of doing business in India”.

A comparative statistical analysis representing the indicators for 'starting business in India' at a particular State is as follows:

Indicator	State in India ( name not mentioned)	South Asia	OECD
Procedures to be followed ( numbers)	13	7.9	4.8
Time required (in days)	30.0	16.0	9.2
Cost ( % of income per capita)	16.3	14.6	3.4
Paid-in minimum capital (% of income per capita)	111.2	14.2	8.8

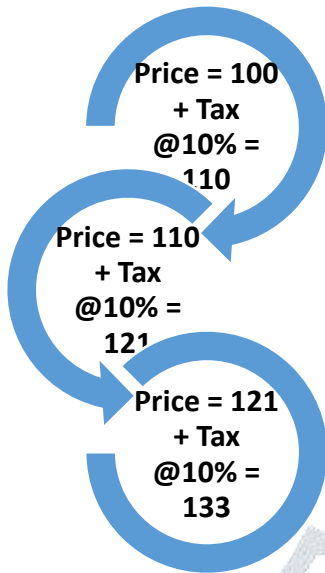
[Source: <http://www.doingbusiness.org/data/exploreeconomies/india>]

Statistics shows that Indian environment is not investor friendly, and hence probable investors may decide otherwise, as it hampers them economically.

- This difficult regulatory burden is exemplified by India’s current rank of 142 among 189 nations in the World Bank’s Doing Business 2015 study.
- India does not feature in the top 100 countries on 8 of the study’s 10 indicators
- In Getting Credit and Protecting Minority Investors India is ranked 7th and 32nd respectively
- On Dealing with Construction Permits and Enforcing Contracts, India ranks among the bottom 10 economies in the world.



### Did VAT was a solution?



Suppose Mr. A sells goods to Mr. B and charges sales tax; then Mr. B re-sells those goods to Mr. C after charging sales tax. While Mr. B was computing his sales tax liability, he also included the sales tax paid on previous purchase, which is how it becomes a tax on tax.

This was the case with the sales tax few years ago. At that time, VAT was introduced whereby every next stage person gets credit of the tax paid at earlier stage. This means that when Mr. B pays tax of Rs. 11, he deducts Rs. 10 paid earlier.

Similar concept came in Excise Duty and Service Tax also, which is called Cenvat credit scheme. To a huge extent, the problem of **cascading effect of taxes** is resolved by these measures.

However, there are still problems with the system that have not been solved till date. We shall talk about these problems now.

- The credit of Input VAT is available against Output VAT. The credit of input excise/service tax is available against output

excise/service tax. However, the credit of VAT is not available against excise and vice versa.

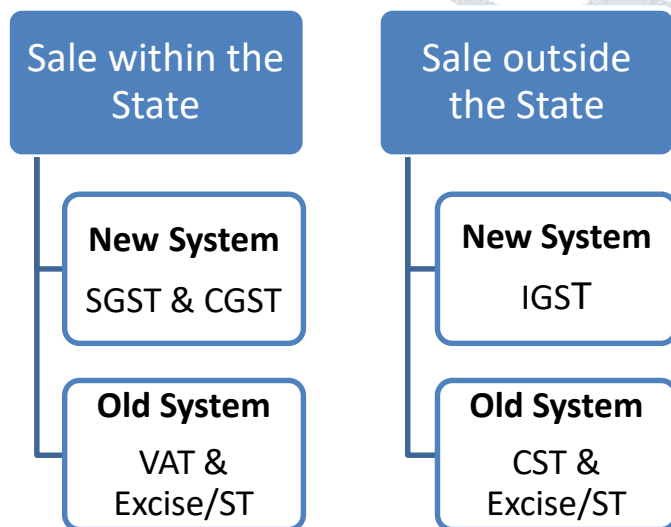
- VAT is computed on a value which includes excise duty. This shows that there is still a tax on tax! Thus the need of the day is reform, and the reforms must be led by the Government at both Central and State levels. GST will solve this problem. Let us see how.

### 1.3 GST: PROCESS & WORKING

GST is a destination based tax on consumption of goods and services. It is proposed to be levied at all stages right from manufacture up to final consumption with credit of taxes paid at previous stages available as setoff. In a nutshell, only value addition will be taxed and burden of tax is to be borne by the final consumer.

#### DUAL GST MODEL

We begin by stating the dual GST model and the taxes levied on each kind of transaction. See these abbreviations before we understand them-



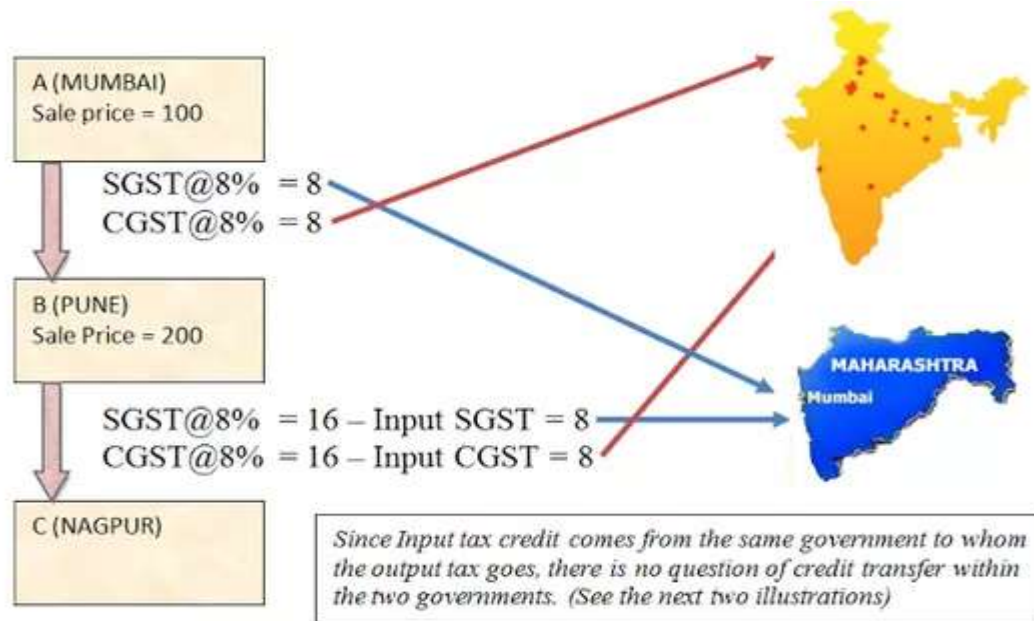
Now look at the chart that follows:

- ❖ SGST – State GST, collected by the State Govt.
- ❖ CGST – Central GST, collected by the Central Govt.
- ❖ IGST – Integrated GST, Collected by Central Govt.

### HOW GST OPERATES?

#### Case 1: Sale in one state, resale in the same state

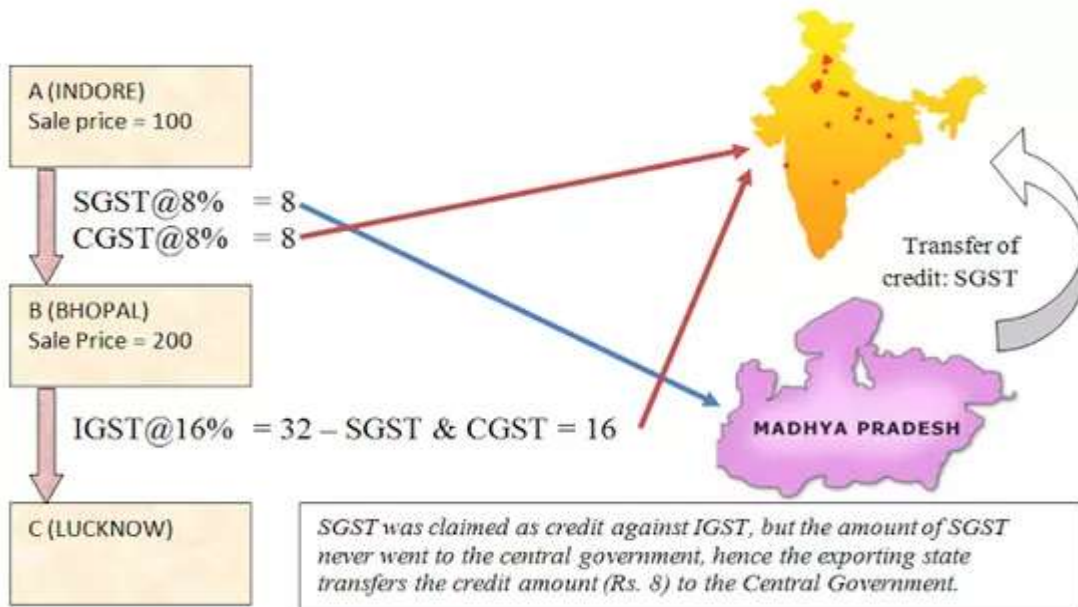
In the example illustrated below, goods are moving from Mumbai to Pune. Since it is a sale within a state, CGST and SGST will be levied. The collection goes to the Central Government and the State Government as pointed out in the diagram. Then the goods are resold from Pune to Nagpur. This is again a sale within a state, so CGST and SGST will be levied. Sale price is increased so tax liability will also increase. In the case of resale, the credit of input CGST and input SGST (Rs. 8) is claimed as shown; and the remaining taxes go to the respective governments.



#### Case 2: Sale in one state, resale in another state

In this case, goods are moving from Indore to Bhopal. Since it is a sale within a state, CGST and SGST will be levied. The collection goes to the Central Government and the State Government as pointed out in the diagram. Later the goods are resold from Bhopal to Lucknow (outside the state). Therefore, IGST will be levied. Whole IGST goes to the central government.

Against IGST, both the input taxes are taken as credit. But we see that SGST never went to the central government, still the credit is claimed. **This is the crux of GST.** Since this amounts to a loss to the Central Government, the state government compensates the central government by transferring the credit to the central government.



**Case 3: Sale outside the state, resale in that state**

In this case, goods are moving from Delhi to Jaipur. Since it is an interstate sale, IGST will be levied. The collection goes to the Central Government. Later the goods are resold from Jaipur to Jodhpur (within the state). Therefore, CGST and SGST will be levied.

Against CGST and SGST, 50% of the IGST that is Rs. 8 is taken as a credit. But we see that IGST never went to the state government, still the credit is claimed against SGST. Since this amounts to a loss to the State Government, the Central government compensates the State government by transferring the credit to the State government.

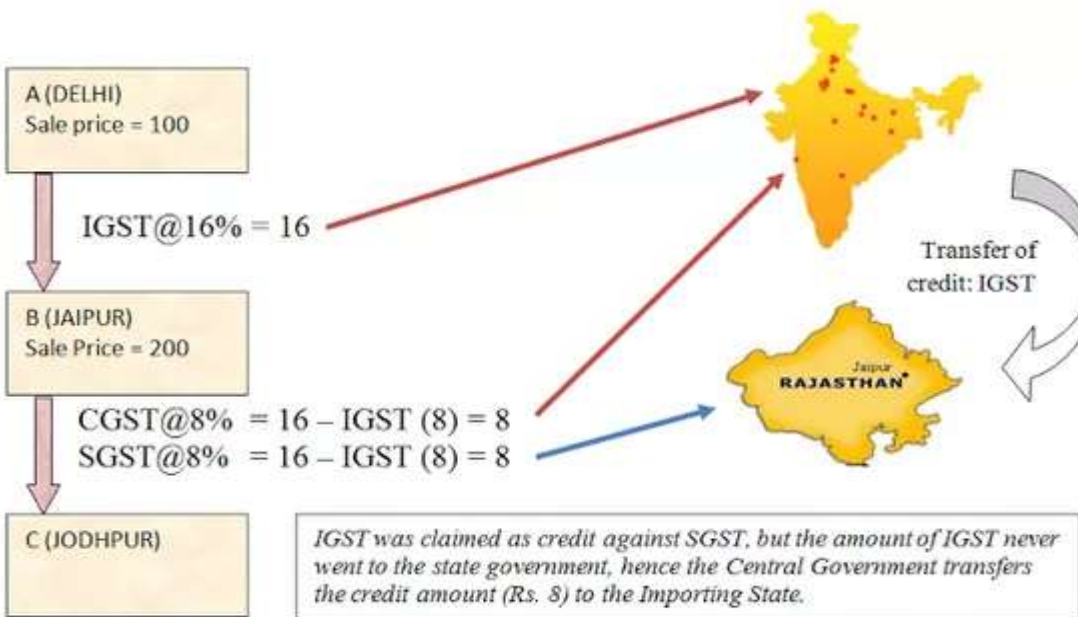


Table 1: Rate of GST (Some Countries)

Country	Rate of GST
Australia	10%
France	19.6%
Canada	5%
Germany	19%

Japan	5%
Singapore	7%
Sweden	25%
New Zealand	15%

Let us first understand the various indirect taxes that are presently being levied by the Central & State Governments.

Ref.	Tax	Levy by	Nature (Levied on) -	Can be Set-off against	Covered by GST
1	Central Excise	Centre	Manufacture	1,2	Yes
2	Service Tax	Centre	Providing services	1,2	Yes
3	Customs	Centre	Import	-	No
4	CVD* under Customs	Centre	Additional Import duty (compensating Excise)	1,2	Yes
5	SAD* under Customs	Centre	Additional Import duty (compensating Sales Tax)	1,2	Yes
6	CST	Centre	Inter-State sales	-	Yes
7	VAT	State	Sales within a state	7	Yes

(\*CVD – Countervailing Duty; SAD – Special Additional Duty)

- The GST shall subsume all the above taxes, except the Basic Customs Duty that will continue to be charged even after the introduction of GST.
- India shall adopt a Dual GST model, meaning that the GST would be administered *both by the Central and the State Governments*.

## SECTION: 2- OPPORTUNITIES

### 2.1 An end to cascading effects

This will be the major contribution of GST for the business and commerce. At present, there are different state level and center level indirect tax levies that are compulsory one after another on the supply chain till the time of its utilization.

### 2.2 Growth of Revenue in States and Union

It is expected that the introduction of GST will increase the tax base but lowers down the tax rates and also removes the multiple point. This will lead to higher amount of revenue to both the states and the union.

### 2.3 Reduces transaction costs and unnecessary wastages

If government works in an efficient mode, it may be also possible that a single registration and single compliance will suffice for both SGST and CGST provided government produces effective IT infrastructure and integration of such infrastructure of states level with the union.

### 2.4 Eliminates the multiplicity of taxation

One of the great advantages that a taxpayer can expect from GST is elimination of multiplicity of taxation. The reduction in the number of taxation applicable in a chain of transaction will help to clean up the current mess that is brought by existing indirect tax laws.

### 2.5 One Point Single Tax

Another feature that GST must hold is it should be 'one point taxation'. This also gives a lot of comforts and confidence to business community that they would focus on business rather than worrying about other taxation that may crop at later stage. This will help the business community to decide their supply chain, pricing modalities and in the long run helps the consumers being goods competitive as price will no longer be the function of tax components but function of sheer business intelligence and innovation.

### 2.6 Reduces average tax burdens

Under GST mechanism, the cost of tax that consumers have to bear will be certain, and GST would reduce the average tax burdens on the consumers.



## 2.7 Reduces the corruption

It is one of the major problems that India is overwhelmed with. We cannot expect anything substantial unless there exists a political will to root it out. This will be a step towards corruption free Indian Revenue Service.

## SECTION: 3- CHALLENGES

Consensus GST reflects that socio-economic conditions of countries differ; hence, a GST framework successful in any particular country may not necessarily be successful in other countries. Though GST has a number of administrative, compliance and other benefits, to what extent such a tax regime would be suitable in the socio-economic context of the Indian economy, is a matter of debate. From country experiences, it can be observed that GST is particularly suitable for countries with homogeneous commercial and demographic features. The success of GST model will depend on effective credit mechanism to avoid cascading effect of multi-stage taxation in supply chain. The challenge for the government to introduce a seamless mechanism of credit across India:

### 3.1 With respect to Tax Threshold

The threshold limit for turnover above which GST would be levied will be one area which would have to be strictly looked at. First of all, the threshold limit should not be so low to bother small scale traders and service providers. It also increases the allocation of government resources for such a petty amount of revenue which may be much more costly than the amount of revenue collected. The first impact of setting higher tax threshold would naturally lead to less revenue to the government as the margin of tax base shrinks, second it may have on such small and not so developed states which have set low threshold limit under current VAT regime.

### 3.2 With respect to nature of taxes

The taxes that are generally included in GST would be excise duty, countervailing duty, cess, service tax, and state level VATs among others. Interestingly, there are numerous other states and union taxes that would be still out of GST.

### 3.3 With respect to number of enactments of statutes

There will two types of GST laws, one at a center level called 'Central GST (CGST)' and the other one at the state level - 'State GST (SGST)'. As there seems to have different tax rates for goods and services at the Central Level and at the State Level, and further division based on necessary and other property based on the need, location, geography and resources of each state.

### 3.4 With respect to Rates of taxation

It is true that a tax rate should be devised in accordance with the state's necessity of funds. Whenever states feel that they need to raise greater revenues to fund the increased expenditure, then, ideally, they should have power to decide how to increase the revenue.

### 3.5 With respect to tax management and Infrastructure

It depends on the states and the union how they are going to make GST a simple one. Success of any tax reform policy or managerial measures depends on the inherent simplifications of the system, which leads to the high conformity with the administrative measures and policies.

## CONCLUSION

The introduction of GST at the Central level will not only include comprehensively more indirect Central taxes and integrate goods and service taxes for the purpose of set-off relief, but may also lead to revenue gain for the Centre through widening of the dealer base by capturing value addition in the distributive trade and increased compliance. In the GST, both the cascading effects of CENVAT and service tax are removed with set-off, and a constant chain of set-off from the original producer's point and service provider's point upto the retailer's level is established which reduces the burden of all cascading effects. This is the real meaning of GST, and this is why GST is not simply VAT plus service tax but an improvement over the previous system of VAT and disjointed service tax. Moreover, with the introduction of GST, burden of Central Sales Tax (CST) will also be removed. The GST at the State-level is, therefore, justified for- (a)

Additional power of levy of taxation of services for the States, (b) System of comprehensive set-off relief, (c) Subsuming of several taxes in the GST & (d) Removal of burden of CST.

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