

# Impact of Goods and Service Tax on Small and Medium Enterprises - Manufacturing Industry in Mumbai Region

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**Abstract :** It was in the year 2000 when our then PM Vajpayee had set up a committee to draft the Goods and Services Tax (GST) law which would transform the Indian economy into a single commercial market and ease out the tax structure which was considered problematic primarily due to the 'cascading effect of taxes' where an item was taxed more than once from the production to the final retail sales/consumption stage in the indirect tax regime. With the expectation to increase foreign investment inflows and improve the 'ease of doing business' rankings of India, GST debuted on 1<sup>st</sup> July 2017 after much deliberations in the parliament to simplify the multi-layered, federal, state and local indirect tax structure by subsuming at least 10 types of indirect taxes into one tax. At the same time, the cost of production was expected to fall thereby benefitting the manufacturing sector of our country and boost 'Make in India' initiative to transform India into a global design and manufacturing hub. Indian economy's facelift due to digitization and the paradigm shift to Goods and Service Tax (GST) has played an unavoidable impact on Micro, Small and Medium Enterprises (MSMEs) business model by largely affecting its labor and liquidity with an increase in compliance costs pooling a large number of small businesses into the tax net for the first time. Small and Medium Enterprises (SMEs) have had a tough time coping up with the compliance procedures and especially the different tax rates applicable on different raw materials which have affected their profitability and resulted in great ambiguity in deciding the final GST rate for the finished product. The objective of this paper is to find out the impact of GST on SMEs in manufacturing industry as there still exists a widespread anomaly with respect to the tax rates charged to different products of similar characteristics.

**Index Terms - Goods and Services Tax (GST), Compliance, Anomaly, SME, India**

## I. Introduction

Herald as the biggest indirect tax reform In India after independence, Goods and Service Tax (GST) debuted on 1<sup>st</sup> July 2017 after much deliberation to simplify the multi-layered, federal, state and local indirect tax structure. GST has subsumed at least 10 types of indirect taxes into one tax to be levied by the State and Centre levels. GST is based on the principle of destination-based consumption taxation as opposed to the earlier principle of origin-based taxation. Tax revenues are levied and collected by the consuming State. It is a dual GST model with the Centre and States levying it at a common base simultaneously.

The GST levied by the Centre is called CGST and the one levied by the State is known as SGST (including Union territories with legislature). Union Territories without legislature levy Union Territory GST (UTGST). An Integrated GST (IGST) is levied on Inter-State supply of goods and services including stock transfer which is collected by Centre hence not disrupting the credit chain. Imports of goods are treated as Inter-State supplies and are subject to IGST in addition to Custom duties whereas Exports are zero rated. Import of services are subject to IGST. 0%, 5%, 12%, 18% and 28% are the five GST rates imposed by the Government.

The Goods and Service Tax has completed a year and it is not a small milestone as it not only is the boldest effort in such a complex tax reform but has been there to achieve its main aim of economically unifying India. The GST has managed to take off and all the credit to the Union, State Governments and the three Union Territories but the compliance issues due to glitches arising from back end manned by the GST Network (GSTN) and the compliance issues arising due to new format of filing returns have proved to be a key concern for MSMEs in India. Indian economy's facelift due to digitization and the paradigm shift to Goods and Service Tax (GST) has played an unavoidable impact on MSMEs business model by largely affecting its labour and liquidity with an increase in compliance costs pooling a large number of small businesses into the tax net for the first time.

## Literature Review

**Mr. Prashant Deshpande and Ms. Mausumi Saikia of Deloitte Touche Tohmatsu India Private Limited in their report titled "Goods and Service Tax in India – Taking Stock and Setting Expectations" (2015)** said that with the roll-out of the Goods and Services Tax (GST), India has joined 160 countries globally in imposing a form of Value Added Tax (VAT). Acknowledged for being progressive and broadening tax base, these taxes decrease the cascading

effect of the multiple taxes and prevent revenue leakage. 33 of the 34-member countries of the Organization for Economic Co-operation and Development (OECD) have employed VAT as the preferred form of consumption tax and Malaysia was the recent foreign country to implement GST effective April 2015. Countries adopted the VAT/GST model after scrutinizing their existing tax structures and laws. European Union (EU) did it to replace the turnover taxes arising on account of the ease of handling cross-border transactions and to develop a common market thereby reducing trade and economic distortions. Countries even adopt VAT/GST to increase revenue from general consumption and bring down the rate of income tax. Revenue Neutral Approach was another reason as in the case of Norway and New Zealand while some did it to consolidate and modernize their existing tax structure which had multiple sales tax at different rates. Preserving neutrality by taxing the value added by each factor equally, large consumption tax and more stable source of revenue and potentially self-enforcing in nature are the key features of VAT/GST which has led to its increased adoption by a large number of countries. Economists Richard M. Bird and Pierre-Pascal Gendron noted in their book<sup>2</sup> IMF played a key role in this spread by consistently supporting and advocating this model of taxation system and facilitating its adoption by countries with less developed economic and administrative structures as well.

### European Union

The European Economic Community adopted VAT on a pan-Europe scale with the major focus on replacing the cascading multi-stage turnover tax and to ease the cross-border transaction which would help create a common marketplace. The VAT Directive has been entrusted with the responsibility of setting up the framework for the VAT structure in the EU but the national governments have been granted the freedom to set the number and level of rates accordingly. Supply of all goods and services in the course of business by a taxable person is subject to a standard VAT rate not below 15% unless exempt whereas one or two reduced rates not less than 5% on foodstuff, water supplies, pharmaceutical, books etc are applicable. Activities and supplies in public interest and intra-EU supplies are exempt from VAT.

### Canada

Canada has a federal government like in India and a federal GST was introduced in 1991 replacing the existing federal sales tax on manufacturers and licensed wholesalers at a rate of 13.5%. However, all provinces continued with the Provincial retail sales tax (PST) thereby having 2 levels of levy. Most goods and services supplied or imported in Canada are taxable at the rate of 5% harmonised sales tax (HST) in the range of 13-15%. A majority of goods and services including real property and intangible personal property attract GST in Canada.

### New Zealand

Designed as a comprehensive tax base by bringing in many difficult-to-tax goods and services under its ambit, the New Zealand GST became an international benchmark for indirect tax design and the Institute of Fiscal Studies of United Kingdom considered it as the benchmark for developing the European VAT Directives. A majority of indigenous and imported goods and services are taxed at a rate of 15% GST.

### India

The previous indirect tax structure in India levied taxes by both the Central and the State Government on manufacturing of goods and supply of services and at point of sale such as state VAT, Octroi duty respectively. Such multiple taxes and its division between Centre and the State government resulted in distortions for the effective working of the tax system and cascading effect of taxes which also had an adverse effect on the Gross Domestic Product (GDP) of our nation. GST was conceived by the Kelkar Committee back in 2004 while analysing the various Central and State level taxes then prevailing. The committee observed that a nationwide dual GST tax reform to be applied at the point of consumption will achieve the “nationwide common market” goal, widen the tax base and effectively improve the revenue stream arising through domestic indirect taxes which would eventually lead to welfare and efficient resource allocation of our nation.

**“Taking a Tumble” by Manu Kaushik of Business Today in the August 13<sup>th</sup> 2017 Issue** spoke about the downfall of Business Confidence Index (BCI) in the July-Sept 2017 after an increase in confidence level when Indian markets just recovered from the effect of demonetization. The downfall occurred as the surveyed business leaders turned pessimist due to anomaly surrounding the applicable GST rates on their products and the GST implementation process. Business leaders were worried about multiple factors like production levels, utilization capacity, investments and 40% of the respondents expected sales slowdown as investments in private businesses remained weak and were expected to see an uptick only if the manufacturing capacity reached a level of 85% which was hovering at 70% as the cycle of weak production, lower capacity utilization and less investment appetite had not passed by.

**“Teething Troubles” by Dipak Mondal of Business Today in the issue dated 13<sup>th</sup> August 2017** highlighted the issues faced by business houses on the Goods and Service Tax Network wherein GSTN chairman Navin Kumar said that they were not confident about the preparedness of the GST Suvidha Providers (GSP) which were facilitators of uploading invoices/returns on the GSTN portal. Admitting to the initial issues surrounding GSTN due to complexity and enormity, GSPs said that GSTN had neither provided them updated Application Programmed Interface (API) nor MPLS (Multiprotocol Label Switching) which were necessary to carry data from one network to another. GSTN suffered due to insufficient staff and lacked quality personnel. The prevailing view of smooth GST rollout was not true as the users faced issues due to technical glitches, understanding new laws and procedures and taxpayer’s reluctance and apprehensions where the transformation stage of shifting to new system involving start of invoice/return uploading, tax payments and refunds were yet to come. The most common complaints of users were that they were unable to login as they forgot their security passwords. Getting the digital signature right was also key issue as the user had to download additional software and then had to register it on the portal. A GSP executive pointed out that GSTN had not done the testing right and hence all the issues were cropping up as it was mandatory for companies and limited liability partnership (LLP) firms. There were even issues regarding PAN registration and people faced issues due to non-validation of PAN as they changed the ownership style of the business but didn’t change the PAN as it was based on the nature of the business. Traders and small businessmen’s major issue was to determine the HSN code and hence the tax rate of their commodities. These codes were crucial for levying the correct tax on a product and were to be mentioned in their invoices.

**S. Lakshmi in their paper “Impact of GST on Manufacturing Sector” published in International Journal of Innovative Research in Management Studies (IJIRMS) Volume 2, Issue 8, September 2017** wrote that a large proportion of textile industry welcomed the introduction of GST but were left working overtime to comply with its provisions. They harnessed their experience of work experience gained under the previous tax regime where online procedures were introduced a year before to comply with GST provisions. Even though working round the clock to comply with the norms with the help of chartered accountants, sections of the industry were struggling due to lack of clarity on certain aspects of the new applicable tax rates in the run up to the return filing deadlines.

**Dr.Laxmi Goritiyal and Mr. Gautam Rangras in their paper “Impact of Goods and Service Tax on Small and Medium Enterprises - Manufacturing Industry in Mumbai Region” (2018)** stated that the impact on Goods and Service tax on the Manufacturing industry in Mumbai city was positive and was yet to open more avenues for the manufacturers as they had not yet recorded their financials covering GST and the impact though being roughly positive, it had increased costs pertaining to compliance procedures of the tax regime. A majority of textile manufacturers were unhappy due to roll out of the new tax regime as there was a lot of anomaly around the tax structures and most importantly that their sector was largely operated through informal channels by circulating cash affording tiny profit margins.

## RESEARCH METHOD

### Objectives:

The objective of this paper is to find out the impact of GST on SMEs in manufacturing industry as there still exists a widespread anomaly with respect to the tax rates charged to different products of similar characteristics.

### Sources of data

The data collected was both primary and secondary. The primary data was based on questionnaire with a sample size of sixty. The secondary data was EBSCOHOST database and many other relevant websites and magazines such as Business Today

### Scope and Limitation

The research provides greater scope of successful implementation of Goods and Services Tax on Small and Medium Enterprises and making business easy. Few SMEs were reluctant to provide certain financial data of their business which was one of the limitations of this research. The collection of samples is limited to only to sixty.

### Hypothesis

#### Null Hypothesis:

Ho1 There is no insignificant impact of GST on SMEs in manufacturing industry

Ho2 SMEs have no significant difference of opinion in GST implementation

Ho3 There is a widespread anomaly with respect to the tax rates charged

**Alternative Hypothesis:**

Ha1 There is insignificant impact of GST on SMEs in manufacturing industry

Ha2 SMEs have significant difference of opinion in GST implementation

Ha3 There is no widespread anomaly with respect to the tax rates charged

**DATA ANALYSIS AND RESULTS****Data Analysis****Frequency****Age**

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1	41	43.6	43.6	43.6
2	44	46.8	46.8	90.4
3	8	8.5	8.5	98.9
4	1	1.1	1.1	100.0
Total	94	100.0	100.0	

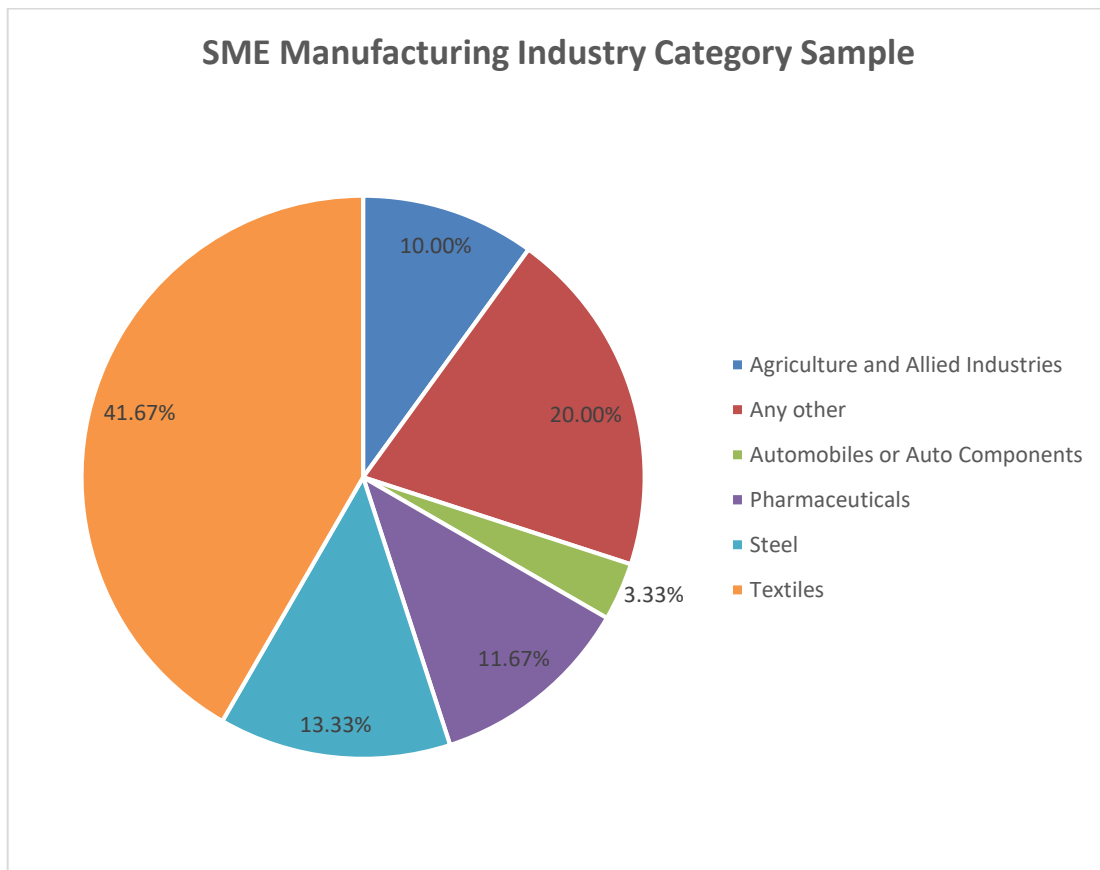
**Statistics****SME Samp**

N	Valid	60
	Missing	0

The sample size of data is 60. And there is no missing data.

**SME Manufacturing Industry Category Sample**

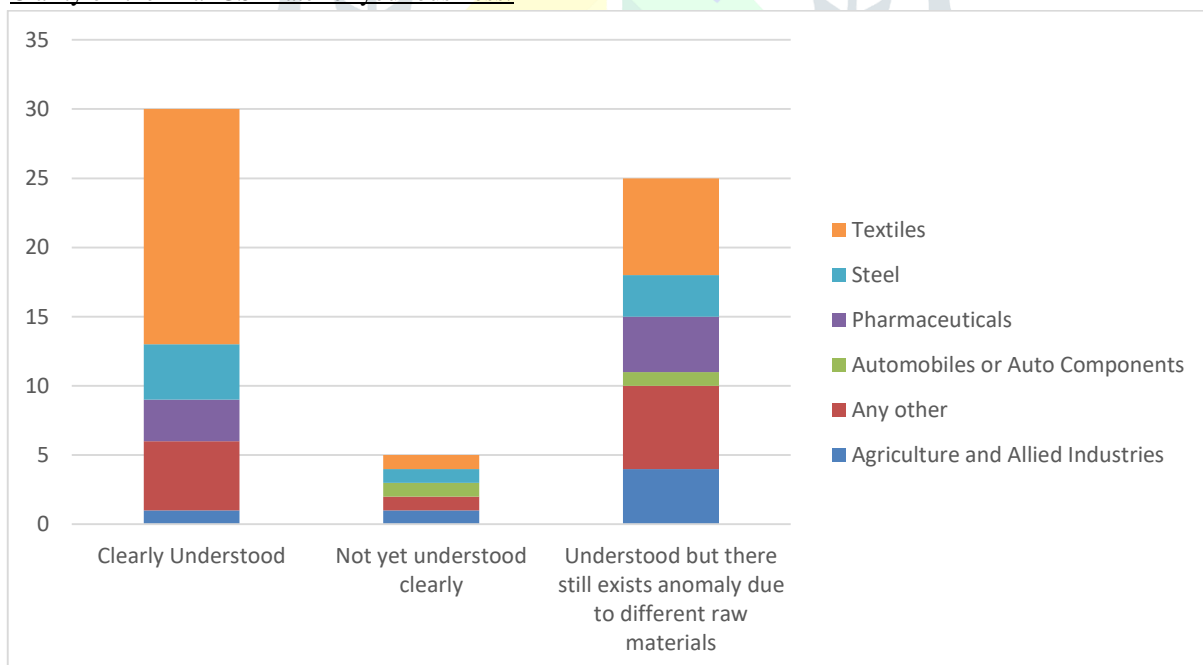
	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1	6	10.00%	10.00%	10.00%
2	12	20.00%	20.00%	30.00%
3	2	3.33%	3.33%	33.33%
4	7	11.67%	11.67%	45.00%
5	8	13.33%	13.33%	58.33%
6	25	41.67	41.67	100.00%
Total	94	100.0	100.0	



The SME Manufacturing Industry Category Sample is divided into six. Agriculture & allied, automobile, pharmaceutical, steel, textiles, any other. 10% from Agriculture & allied, 3.33% from automobile, 11.67% from pharmaceutical, 13.33% from steel, 41.67% from textiles and 20.00% from any other industry collected data.

**Data Analysis**

Clarity on the final GST rate for your business:



Anova: Single Factor

SUMMARY

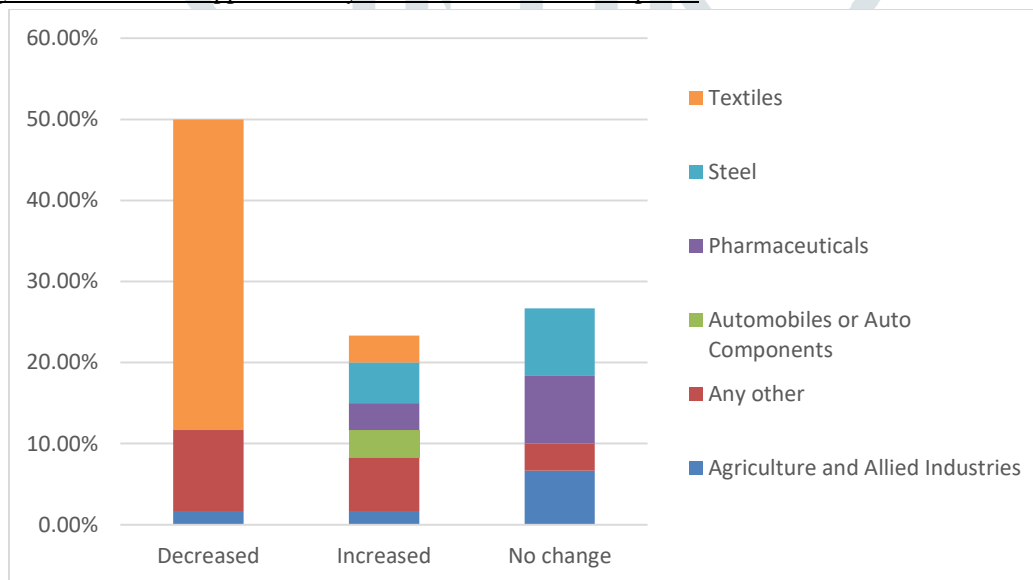
Groups	Count	Sum	Average	Variance
Column 1	3	6	2	3
Column 2	3	12	4	7
Column 3	2	2	1	0
Column 4	2	7	3.5	0.5
Column 5	3	8	2.67	2.33
Column 6	3	25	8.33	65.33

ANOVA

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	91.17	5	18.23	1.17	0.39	3.33
Within Groups	155.83	10	15.58			
Total	247	15				

As per ANOVA Single factor tool the F value i.e., 1.17 is less than F critical value i.e., 3.33. And the P-value is 0.39 which is more than the 0.05. Null hypothesis is accepted. Hence SMEs have no significant difference of opinion in GST implementation.

There is a change on the GST rate applicable to your business since its inception:



Anova: Single Factor

SUMMARY

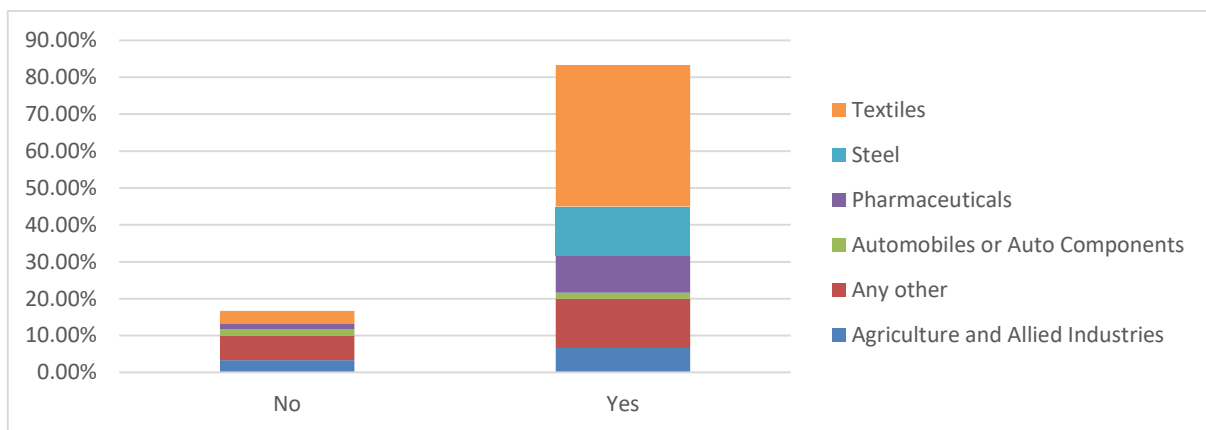
Groups	Count	Sum	Average	Variance
Column 1	3	6	2	3
Column 2	3	12	4	4
Column 3	1	2	2	0
Column 4	2	7	3.5	4.5
Column 5	2	8	4	2
Column 6	2	25	12.5	220.5

ANOVA

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	156.08	5	31.22	0.91	0.53	3.97
Within Groups	241	7	34.43			
Total	397.08	12				

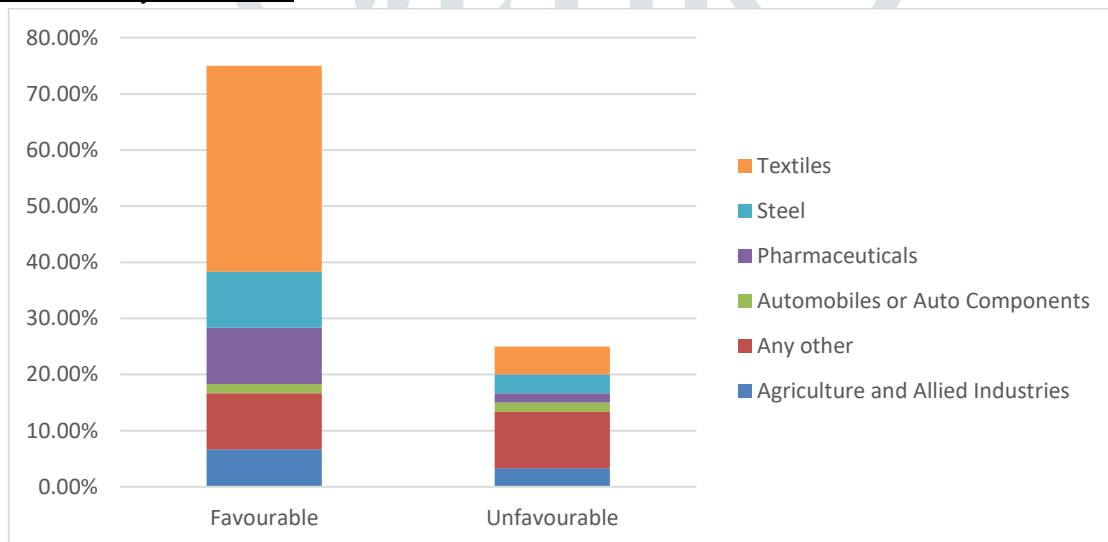
As per ANOVA Single factor tool the F value i.e., 0.91 is less than F critical value i.e., 3.97. And the P-value is 0.53 which is more than the 0.05. Null hypothesis is accepted. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

Favour of GST:



The SME Manufacturing Industry Category Sample is divided into six. Agriculture & allied, automobile, pharmaceutical, steel, textiles, any other. And majority of them are in favour of GST. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

The transition to GST on your business:



Anova: Single Factor

**SUMMARY**

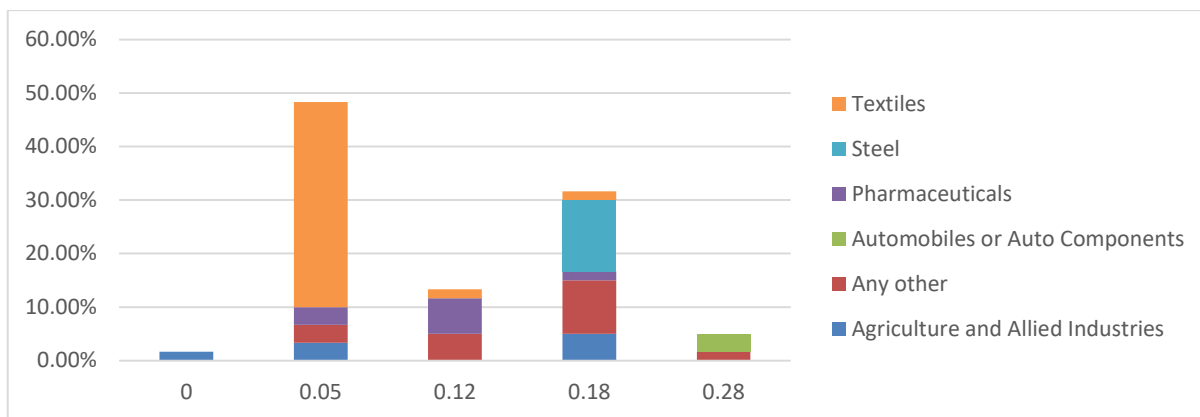
Groups	Count	Sum	Average	Variance
Column 1	2	6	3	2
Column 2	2	12	6	0
Column 3	2	2	1	0
Column 4	2	7	3.5	12.5
Column 5	2	8	4	8
Column 6	2	25	12.5	180.5

**ANOVA**

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	161	5	32.2	0.95	0.51	4.39
Within Groups	203	6	33.83			
Total	364	11				

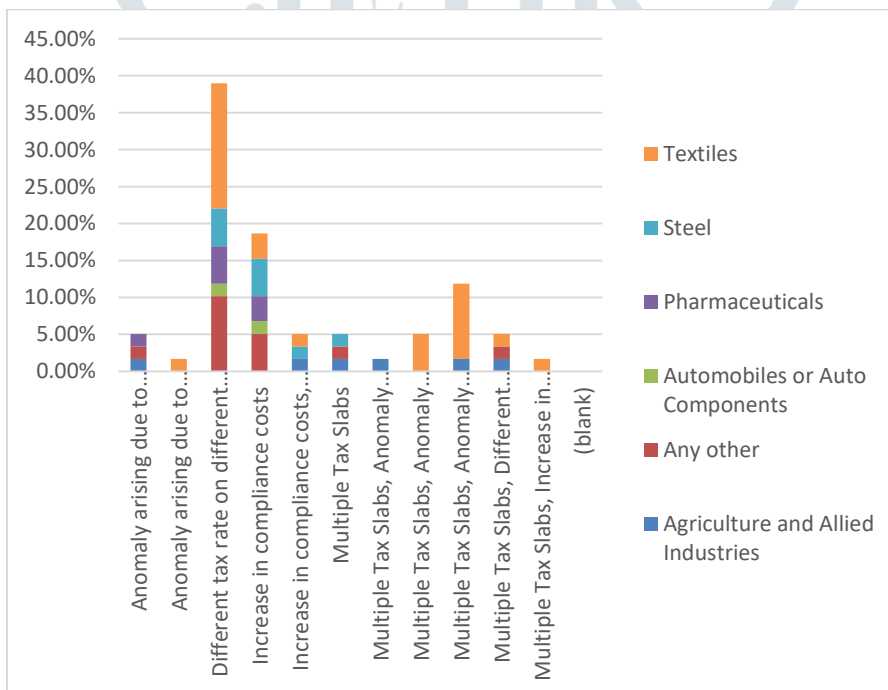
As per ANOVA Single factor tool the F value i.e., 0.95 is less than F critical value i.e., 4.39. And the P-value is 0.51 which is more than the 0.05. Null hypothesis is accepted. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

GST rate applicable to your business:



The SME Manufacturing Industry Category Sample is divided into six. Agriculture & allied, automobile, pharmaceutical, steel, textiles, any other. And industries been charged 5%, 12%, 18% & 28% GST rates which are applicable to their business. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

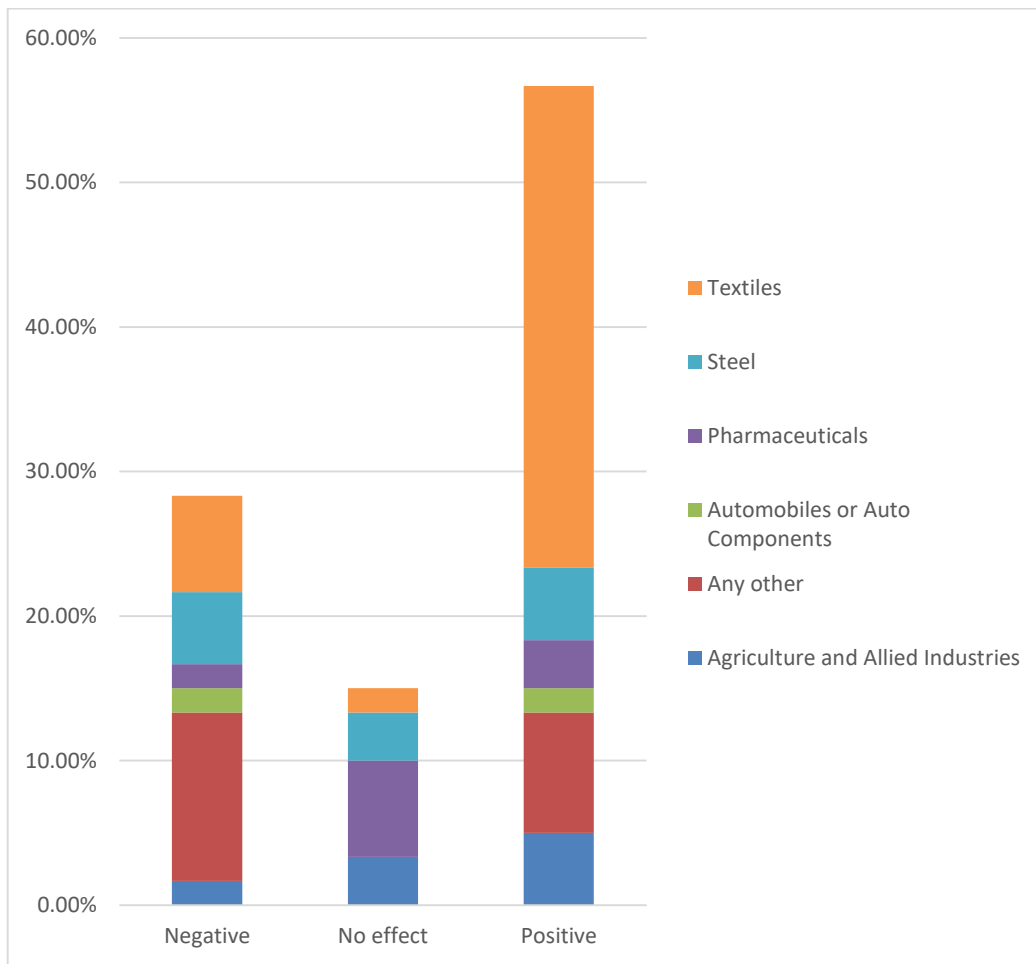
Major issue of GST:



The SME Manufacturing Industry Category Sample is divided into six. Agriculture & allied, automobile, pharmaceutical, steel, textiles, any other. And industries are facing major issues with respect to anomaly and other challenges in their business. Hence, there is a widespread anomaly with respect to the tax rates charged.

Effect of the change in rates (if any) on your business operations and profitability:





Anova: Single Factor

SUMMARY

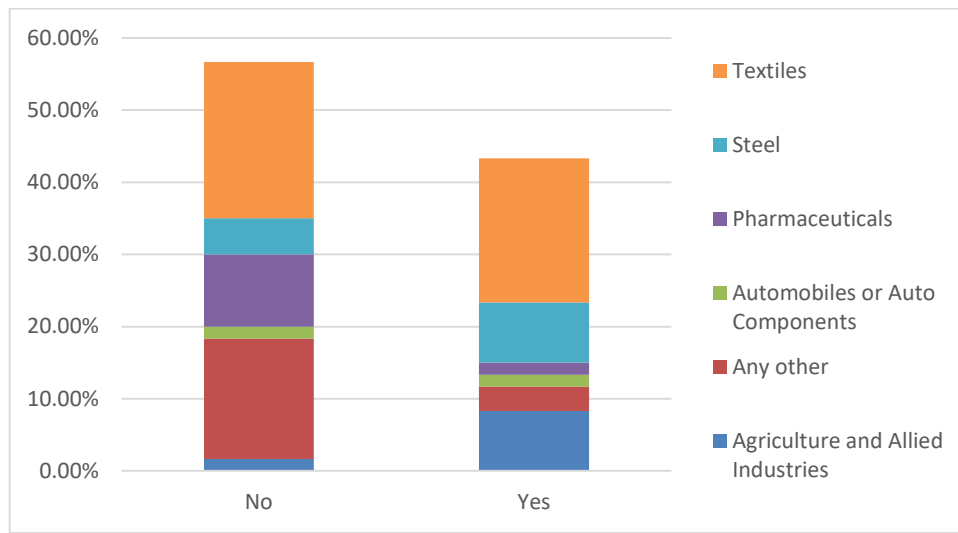
Groups	Count	Sum	Average	Variance
Column 1	3	0.100	0.033	0.000
Column 2	3	0.200	0.067	0.004
Column 3	3	0.033	0.011	0.000
Column 4	3	0.117	0.039	0.001
Column 5	3	0.133	0.044	0.000
Column 6	3	0.417	0.139	0.029

ANOVA

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	0.03	5	0.01	1.06	0.43	3.11
Within Groups	0.07	12	0.01			
Total	0.10	17				

As per ANOVA Single factor tool the F value i.e., 1.06 is less than F critical value i.e., 3.11. And the P-value is 0.43 which is more than the 0.05. Null hypothesis is accepted. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

Face technical difficulties on the Goods and Service Tax Network (GSTN):



Anova: Single Factor

SUMMARY

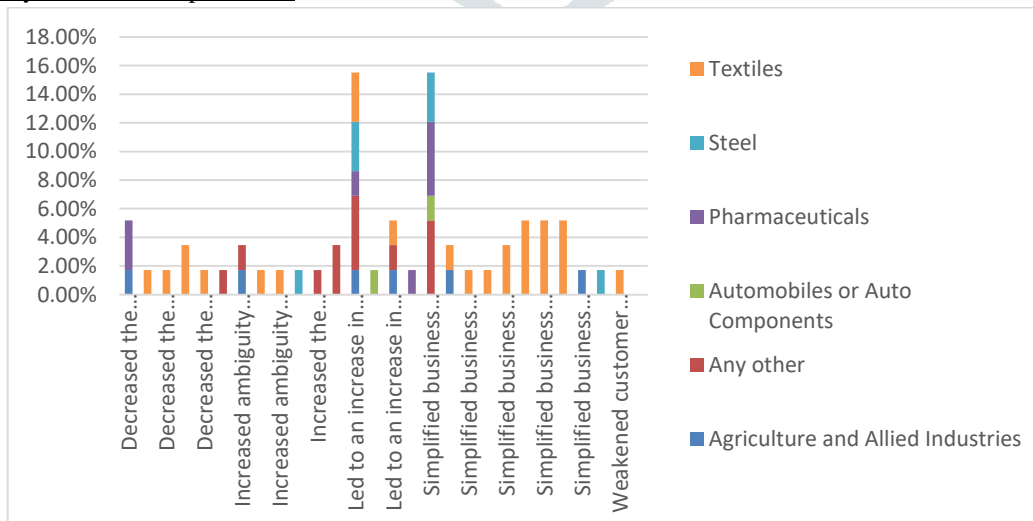
Groups	Count	Sum	Average	Variance
Column 1	2	6	3	8
Column 2	2	12	6	32
Column 3	2	2	1	0
Column 4	2	7	3.5	12.5
Column 5	2	8	4	2
Column 6	2	25	12.5	0.5

ANOVA

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	161	5	32.2	3.51	0.08	4.39
Within Groups	55	6	9.17			
Total	216	11				

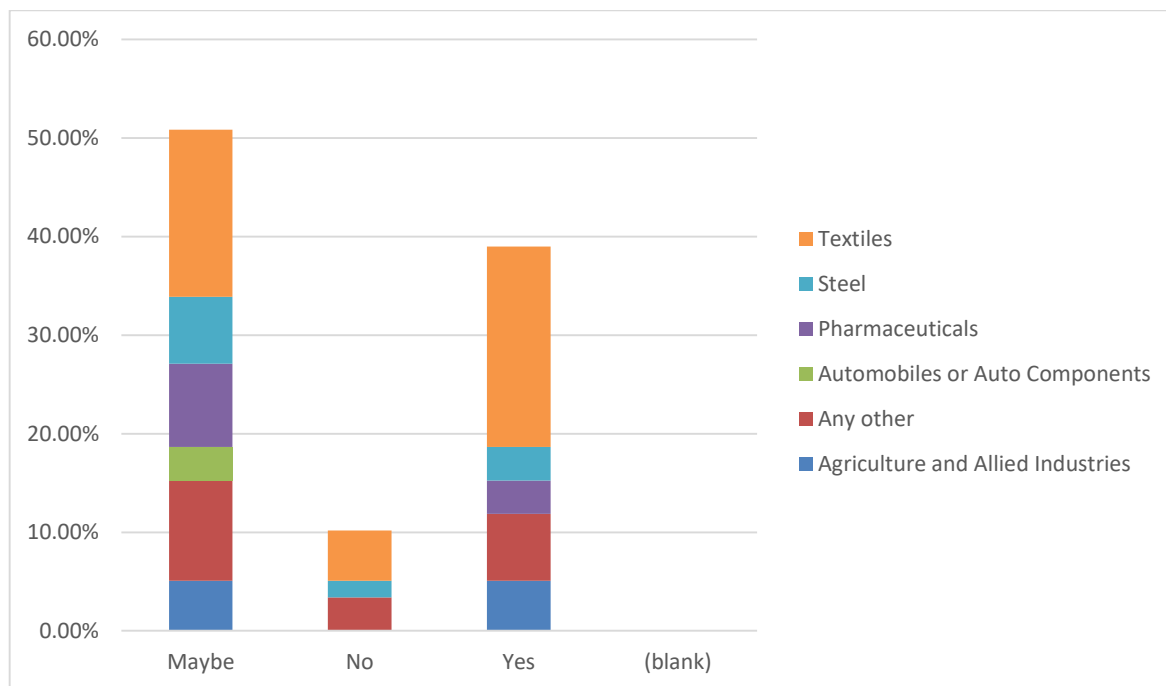
As per ANOVA Single factor tool the F value i.e., 3.51 is less than F critical value i.e., 4.39. And the P-value is 0.08 which is more than the 0.05. Null hypothesis is accepted. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

Effect of GST on your business operations:



The SME Manufacturing Industry Category Sample is divided into six. Agriculture & allied, automobile, pharmaceutical, steel, textiles, any other. And industries demand for their business has got improved at the same time there business become simple and easy. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

Expect to see a further growth in demand for our goods on implementation of GST:



Anova: Single Factor

**SUMMARY**

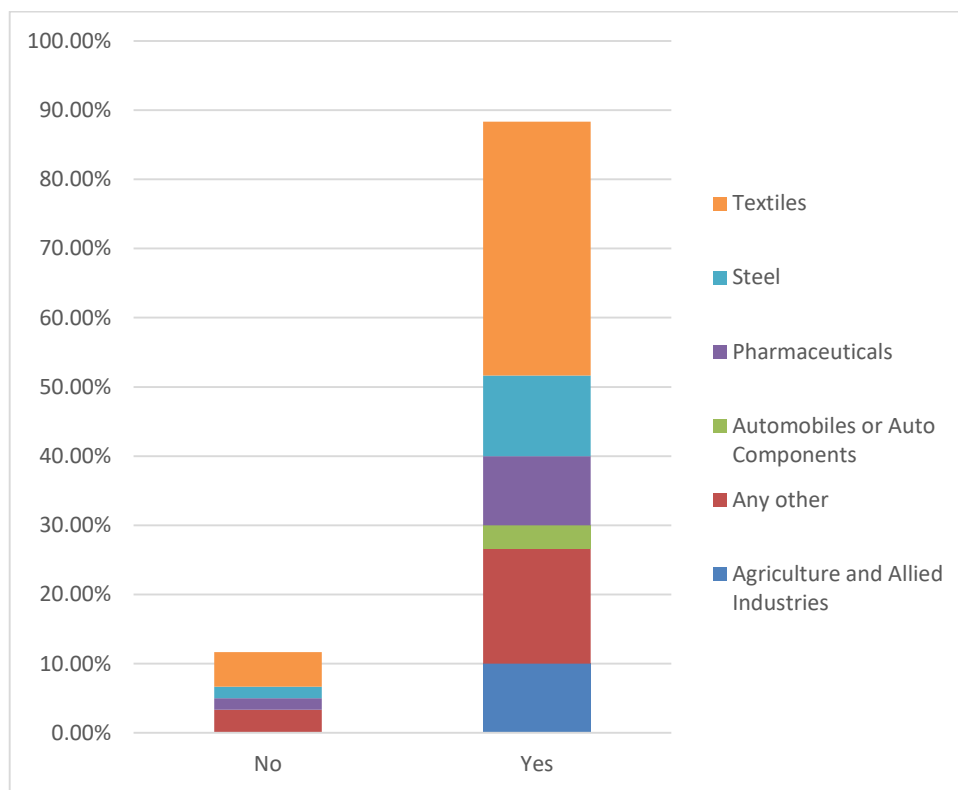
Groups	Count	Sum	Average	Variance
Column 1	2	6	3	0
Column 2	3	12	4	4
Column 3	1	2	2	
Column 4	2	7	3.5	4.5
Column 5	3	7	2.33	2.33
Column 6	3	25	8.33	22.33

**ANOVA**

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	70.52	5	14.10	1.82	0.21	3.69
Within Groups	61.83	8	7.73			
Total	132.36	13				

As per ANOVA Single factor tool the F value i.e., 1.82 is less than F critical value i.e., 3.69. And the P-value is 0.21 which is more than the 0.05. Null hypothesis is accepted. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

The current tax regime is better than the previous tax regime:



Anova: Single Factor

SUMMARY

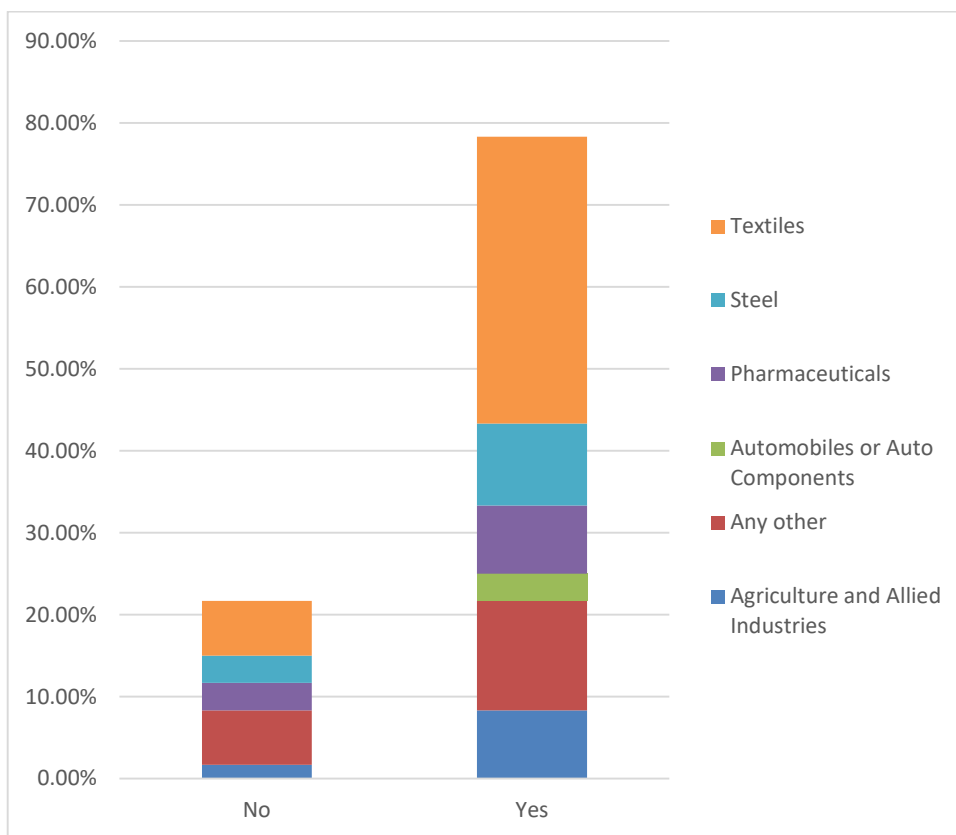
Groups	Count	Sum	Average	Variance
Column 1	1	6	6	
Column 2	2	12	6	32
Column 3	1	2	2	
Column 4	2	7	3.5	12.5
Column 5	2	8	4	18
Column 6	2	25	12.5	180.5

ANOVA

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	121	5	24.2	0.40	0.83	6.26
Within Groups	243	4	60.75			
Total	364	9				

As per ANOVA Single factor tool the F value i.e., 0.40 is less than F critical value i.e., 6.26. And the P-value is 0.83 which is more than the 0.05. Null hypothesis is accepted. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

Concept of 'One Nation One Tax - GST' opened doors for new business opportunities for your business outside your home market:



Anova: Single Factor

**SUMMARY**

Groups	Count	Sum	Average	Variance
Column 1	2	6	3	8
Column 2	2	12	6	8
Column 3	1	2	2	
Column 4	2	7	3.5	4.5
Column 5	2	8	4	8
Column 6	2	25	12.5	144.5

**ANOVA**

Source of Variation	SS	df	MS	F	P-value	F crit
Between Groups	135.73	5	27.15	0.78	0.60	5.05
Within Groups	173	5	34.6			
Total	308.73	10				

As per ANOVA Single factor tool the F value i.e., 0.78 is less than F critical value i.e., 5.05. And the P-value is 0.60 which is more than the 0.05. Null hypothesis is accepted. Hence, there is no insignificant impact of GST on SMEs in manufacturing industry.

**CONCLUSION**

The Goods and Services Tax has brought a tremendous amount of revolution in the Indian market and many of the manufacturing industries are in favour of GST implementation and but few of the industries are having widespread anomaly with respect to tax rates charged. With over a period we are sure that this anomaly will surely going to be fade away and the SMEs will find a smooth functioning GST in their respective business.

A majority of textile manufacturers were unhappy due to roll out of the new tax regime as there was a lot of anomaly around the tax structures and most importantly that their sector was largely operated through informal channels by circulating cash affording tiny profit margins.

The impact on Goods and Service tax on the Manufacturing industry in Mumbai city was positive and was yet to open more avenues for the manufacturers as they had not yet recorded their financials covering. GST and the impact though being roughly positive, it had increased costs pertaining to compliance procedures of the tax regime.

The SME Manufacturing Industry Category Sample is divided into Agriculture & allied, automobile, pharmaceutical, steel, textiles, any other. And these industries demand for their business has got improved at the same time their business become simple and easy. Concept of 'One Nation One Tax - GST' opened doors for new business opportunities for SMEs business outside home market. Hence, there is a significant impact of GST on SMEs in manufacturing industry.

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