

Goods and Services Tax*

Deciphering Some Conceptual Issues

117th Induction Training Programme for IAS officers
LBSNAA Mussoorie
3.8.2015
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Fiscal Autonomy Vs. Tax Autonomy of the States
(Its all about political economy)
Mature Markets. Emerging Markets
(Formal & informal markets)

*Magnitude: Indirect taxes of Centre and States are about Rs. 11 lakh crore in 2013-14, with Central tax buoyancy being 1.32 at the Centre and 1.17 in the States

Scheme of Presentation

1. What is Tax to GDP ratio, market and magnitude of present taxes ?
2. GST as a reform & Reactions to Reforms?
3. Constitutional provisions for taxes
4. Definition of GST
5. Issues in VAT and magnitude of Indirect taxes
6. Expected outcome of GST
7. Experience of other countries and expectations
8. Salient features our GST
9. Constitutional amendment bill & GST Council
10. Model of GST & IGST – value addition and flow of input credits
11. What is GSTN
12. Potential threats and benefits

Tax to GDP Ratio

Most recent years from OECD or World Bank

Denmark 48 France 45 Germany 36.7 Portugal
33.4 Greece 33 UK 32.9
Canada 30.6 Turkey 29.3 USA 25.4
Korea 24.3 Chile 20.2 Mexico 19.7
Russia 15.4 Brazil 14.4 Egypt 13.2
China 10.4 India 10.8 Afghanistan 7.5

GDP (in 2014 (at Constant 2005 US\$. In trillion)

Japan 4.7 USA 14.7 China 5.2 Germany 3.2 France 2.3 UK 2.6 India 1.6
Korea 1.2 Mexico 1.06 Brazil 1.2 Denmark 0.27

Comments ?

GST...

.... harmonizes common national market,
eliminates multiple tax systems and authorities
brings ease to the business, increases compliance
& eliminates tax on tax (cascading effect).

How?

Resistance to Reform can be explained by using Hirschman's Perversity Thesis, Futility Thesis and Jeopardy Thesis

Constitutional Provisions

Article 268.

Duties levied by the Union but collected and appropriated by the States.

Article 269.

Taxes levied and collected by the Union but assigned to the States.

Article 270. Taxes levied and collected by the Union and distributed between the Union and the States.

Article 271.

Surcharge on certain duties and taxes for purposes of the Union.

Article 272 Taxes which are levied and collected by the Union and may be distributed between the Union and the States.

Article 274 Prior recommendation of President required to Bills affecting taxation in which States are interested.

Article 276.

Taxes on professions, trades, callings and employments.

GST Defined...

...in Article 366 (12A) to mean "any tax on supply of goods or services or both except taxes on supply of the alcoholic liquor for human consumption".

Share of indirect taxes (Centre)

A snapshot (2014-15)

- Service sector constitutes 60% of GDP but service tax contribution is 1.36% of total taxes
- Manufacturing sector constitutes 26% of GDP but Central excise contribution is 1.49% of GDP

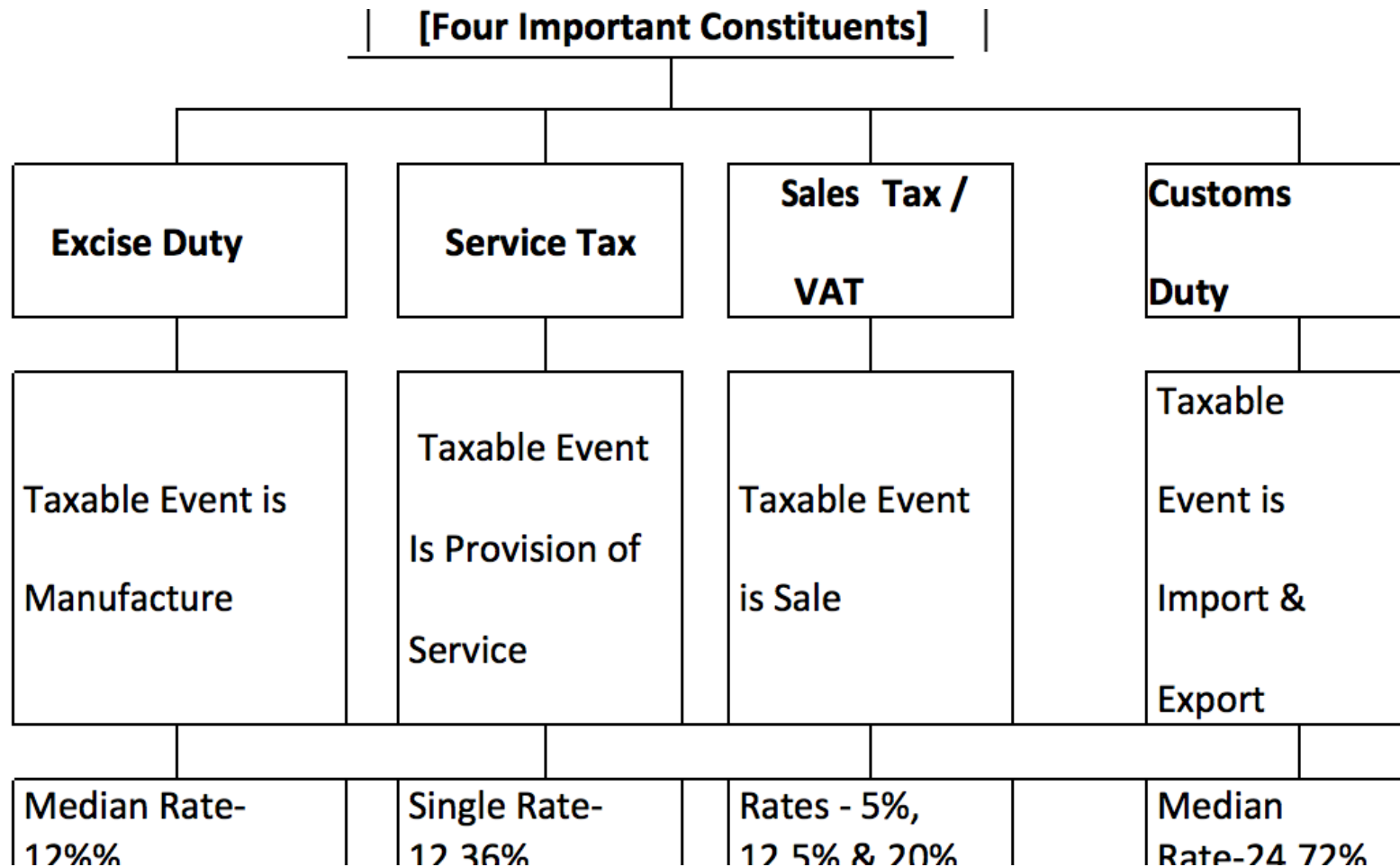
What is the message ?

Central Excise Duty/CENVAT (1986) is origin based single point tax levied at manufacturing level
Service Tax (1994) started on selective services. Now on it is on all Service other than on
Negative List.
States started VAT from April 2005. It is only on goods. It was to reduce cascading effect

Key issue with VAT in States

- Basic value for charging state VAT on a manufactured product includes Cenvat (central excise) Basic Excise Duty
- This is tax on tax, as CST & Basic Excise duty paid is not allowed to be taken as input tax credit
- Resulting increased cost of the product and tax on tax,
- Just because CST cannot be taken as credit for interstate sales, manufacturing companies are forced to open warehouses in different states, which results in increased cost of transportation and infrastructure
- Separate taxation of goods and services require splitting up of transaction value into value of goods and services for taxation which leads to greater complexities in tax administration and increased litigation cost.

Present Taxes (Centre & States)

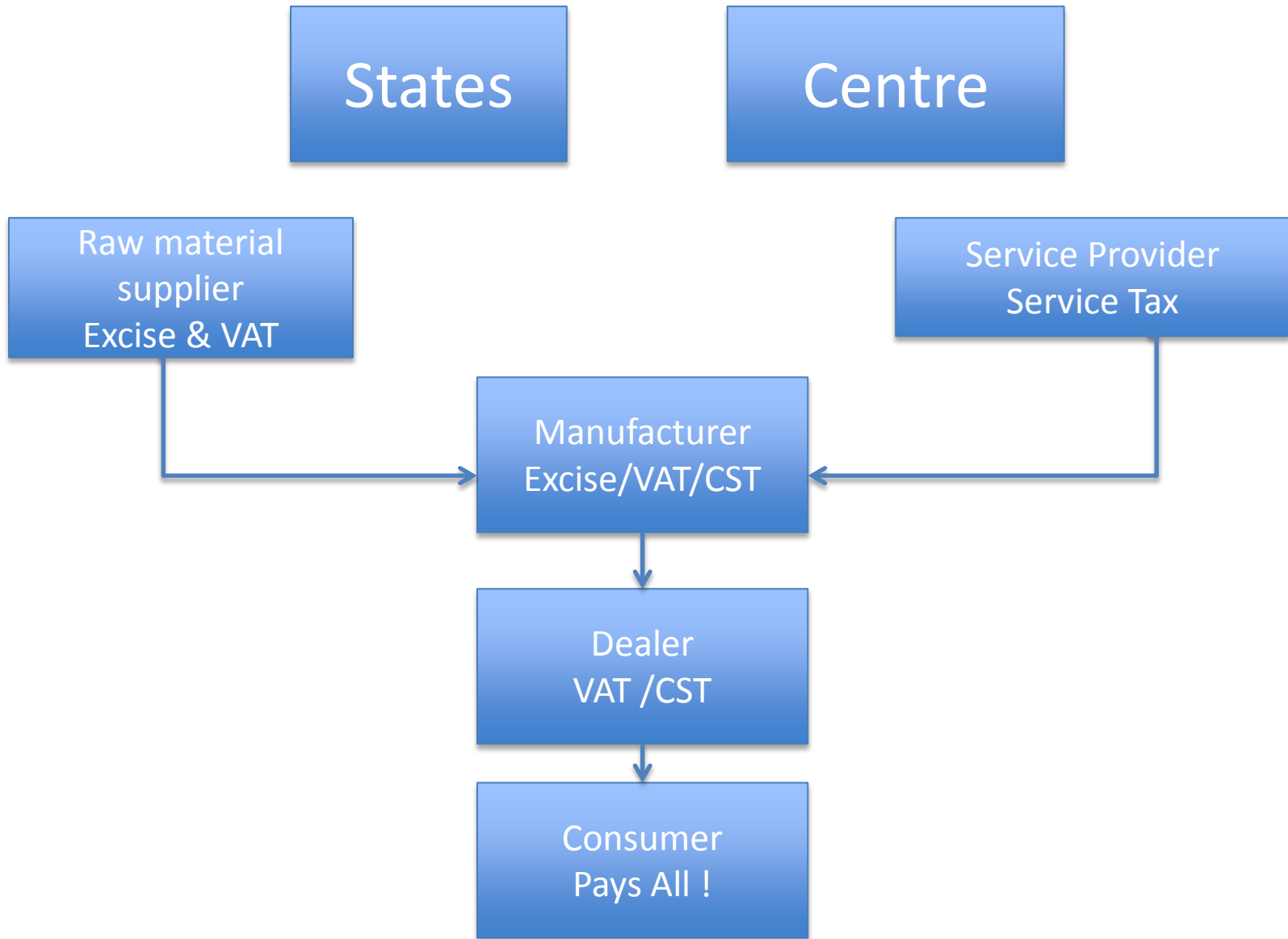


Issue in the Present System

- Tax Cascading
- CENVAT: definitional issues as to what constitutes manufacturing, and valuation issues for determining the value on which the tax is to be levied
- Complexity in determining the nature of transaction – Sale vs. Service, due to composite bundles offered for sale to consumers under a variety of supply-chain arrangements
- Inability of States to levy Service Tax
- Inability of the Centre to tax beyond manufacturing
- Lack of Uniformity in Provisions and Rates
- Narrow Base & variety of exemptions
- Complexity in Administration

Tax Pass-Thru

(A formal and efficient market ensures incidence is on the consumer.
Transactions through informal markets do not tax credits)



Why GST ?

- Incidence of tax should fall only on domestic consumption
- No export of taxes across taxing jurisdictions
- Integrate Indian market should be integrated into a single common market
- Enhance the cause of cooperative federalism
- Enhancing the neutrality between present consumption and future consumption
- Enhance neutrality of tax system to the form of organisation
- Enhance neutrality of tax system to the source of finance
- Establish efficient and effective tax compliance system
- Revenue focus be on buoyancy rather than immediate target objective.

See: [Task Force on GST 13th FC](#)

Take-Away:

Income is taxed irrespective of source and use; therefore, consumption should also be taxed on the same principle.

Taxes to be Subsumed

Taxes under Centre GST

- Central excise duty & additional excise duties
- Additional customs duty and Special additional customs duty
- Service tax
- Cesses and surcharge

Taxes under State GST

- VAT/Sales tax
- Local tax- ET, LT etc
- CST to be replaced by IGST
- entry tax not in lieu of octroi
- Lotteries & Betting

An idea of GST Composition

GST Pool

No	Type of Tax	(Rs In Crores)		Percentage of Total
		2012-13 (Accounts)	After deducting 32% devolution for items 1 and 2	
1	Union Excise (excluding Cesses and surcharges)	176,535	120,044	16.69%
	Total Cesses and Surc	28,910	28,910	4.02%
2	Service Tax	132,601	90,169	12.53%
	Educational Cess and & Higher Educational Cess	3,425	3,425	0.48%
3	Sales Tax/VAT	410,507	410,507	57.07%
4	Other State/Local Tax	56,965	66,294	9.22%
	Total	808,944	719,349	100.00%

Central Excise Duty/CENVAT (1986) is origin based single point tax levied at manufacturing level
 Service Tax 1994 on selective services, now on all service other than on Negative List.
 States started VAT from April 2005. It is only on goods. To reduce cascading effect

GST Performance in Other Countries

No	Country	Tax	Year Implemented	Party	Election	Implementation (%)	Year (%)	Change (D)
1	New Zealand	GST	1986	Labour	Labour	18.20	9.60	D
2	Australia	GST	2000	Liberal/National coalition	Liberal/National coalition	3.10	6.10	I
3	Brazil	ICMS	1989	Brazilian Democratic Movement Party	Brazilian Democratic Movement Party	1969.88	1621.18	D
4	Canada	GST	1991	Progressive Conservative	Liberal Party of Canada	5.64	2.17	D
		HST	1997	Liberal Party of Canada	Liberal Party of Canada	0.78	1.00	D
5	Singapore	GST	1994	People's Action Party,	People's Action Party,	3.10	1.70	D
6	United Kingdom	VAT	1973	Conservative	Labour	9.20	16.00	I
7	South Africa	VAT	1991	National Party	Government of National Unity (African National Congress+ National Party+ Inkatha Freedom Party)	16.70	11.50	D
8	Spain	VAT	1986	Spanish Socialist Workers' Party (PSOE)	Spanish Socialist Workers' Party (PSOE)	8.25	4.60	D
9	Sweden	VAT	1969	Swedish Social Democratic Party	Swedish Social Democratic Party	3.86	8.12	I
10	Denmark	VAT	1967	Social Democratic Party	Social Democratic Party	5.81	2.56	D
11	Ghana	VAT	1995	National Democratic Congress	National Democratic Congress	59.46	44.36	D
12	Malta	VAT	1995	Nationalist Party	Malta Labour Party	3.97	1.96	D
13	Canada	VAT	1996	Nationalist Party	National Democratic	3.70	1.47	I

ASSOCHAM Estimates:

GST will reduce prices by 10%

GDP will grow by 1.5%

Tax/GDP ratio to go up by 1.5 %

(But 14th FC assumed no change)

Salient features

1. Dual model GST with CGST & SGST.
2. Rates for CGST and SGST would be prescribed appropriately, reflecting revenue considerations and acceptability. This dual model would be implemented through multiple statutes
3. CGST & SGST are to be paid to the accounts of the Centre and the States separately.
4. Taxes paid against the Central GST shall be allowed to be taken as input tax credit (ITC) for the Central GST and could be utilised only against the payment of Central GST. The same principle will be applicable for the State GST

Salient Features-2

5. Centre and States to have concurrent jurisdiction for the entire value chain and for all taxpayers on the basis of thresholds (Rs. 10 lakhs & Rs. 1.5 Crore) for goods and services prescribed for the States and the Centre.
6. Common format for tax returns, to both the CGST authority and to the concerned SGST authorities.
7. PAN-linked taxpayer identification number with a total of 13/15 digits for data exchange and better compliance
8. A GST Compensation Fund should be created under the administrative control of the **Council of Finance Ministers**. States to follow the agreed road map

Salient features

9. assessment, enforcement, scrutiny and audit would be undertaken by the authority which is collecting the tax, with information sharing between the Centre and the States.
10. Petroleum and Petroleum products shall not be subject to the levy of till notified at a future date on the recommendations of GST Council.
11. taxes on tobacco and tobacco products imposed by the centre shall continue to be levied over and above GST
12. GST rate will be uniform across the country. However, to give fiscal autonomy to the states and centre, there will be a provision of a tax band over and above the rate of the floor rates of CGST, SGST and IGST

122nd Constitutional Amendment Bill

- Introduced in Parliament on 19th Dec. 2014
- After the bill is passed by both the Houses of Parliament by 2/3rd majority, it will be sent to state legislatures for ratification
- The ratifications by at least 50% of state legislatures is required to bring the bill in effect.

GST Bill - Salient features

1. Enables the Centre and States to introduce law for levying GST on supply of goods or services or both
2. All supply of goods or services or both will attract CGST (levied by Centre) and SGST (levied by State) *unless kept out of purview* of GST
3. Specifically provides that 'services' means anything other than goods. This broad definition of the term 'service' will altogether remove the disputes for defining any thing as 'goods or services'
4. GST shall *subsume various* indirect taxes being levied by the Union and the State governments
5. Special provisions for levy of additional tax (@1%) on supply of goods accruing to the origin State.

Salient features

6. The GST Council is to be entrusted with the responsibility of making recommendations on all key aspects related to the levy
 - The Council , to be constituted within 60 days of the Bill becoming an Act, shall comprise of Union Finance Minister as Chairman Union Minister of State in -charge of Revenue or Finance as member and Minister in charge of Finance or Taxation or any other Minister nominated by each State Government as its members
7. Compensation to States in cases of loss of revenue post GST introduction
8. While discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services

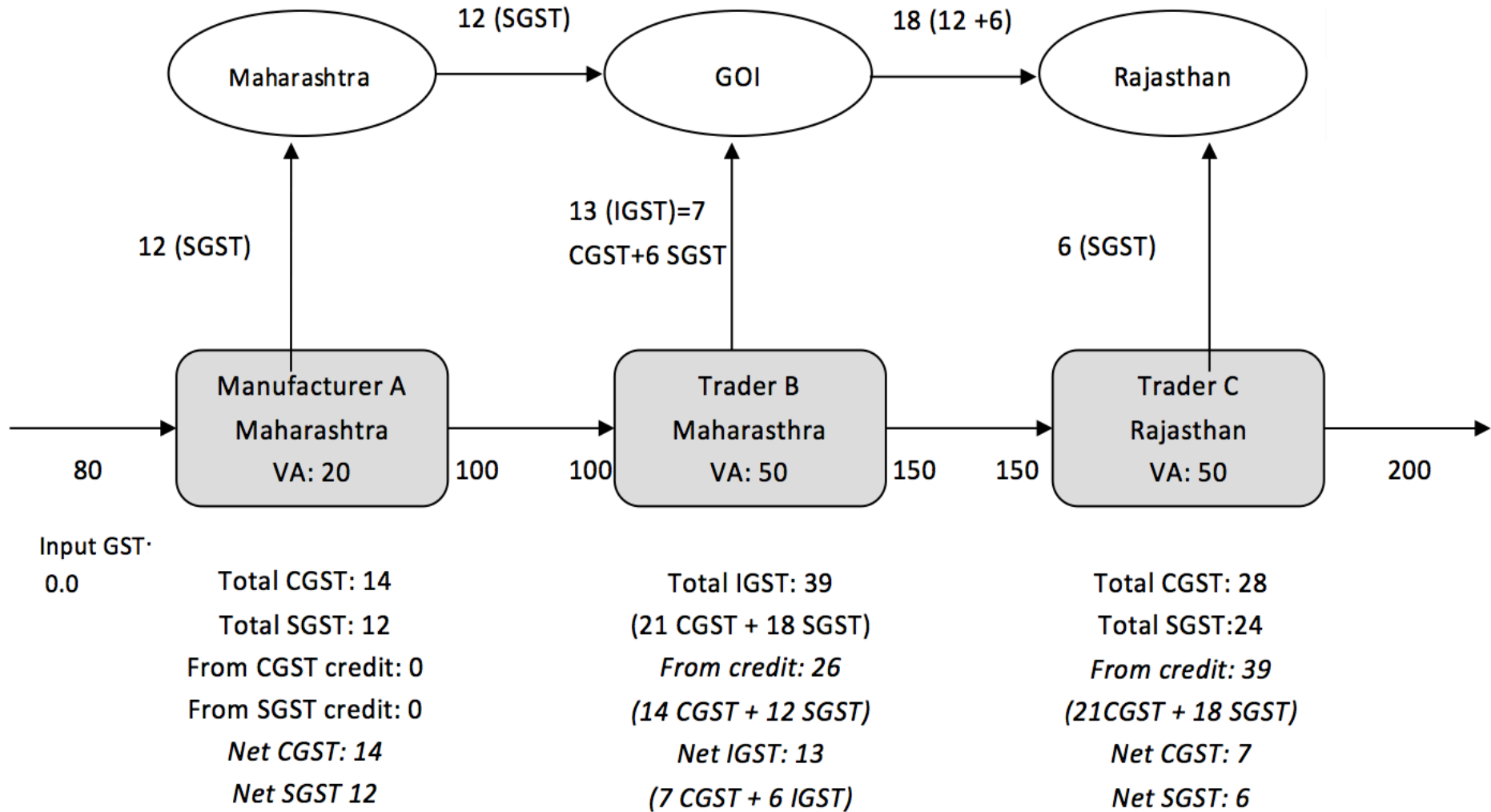
Model of GST

Assumption CGST @10% & SGST @ 5%

Stage of supply chain	Purchase value of input	Value addition	Output value for next Stage	Rate of CGST	Rate of SGST	CGST on Output	SGST on Output	Input tax credit on CGST	Input tax credit on SGST	Net CGST=CGST on output-input tax credit	Net SGST=SGST on output-input tax credit	Grand total of CGST and SGST including input CGST/SGST
Raw material								10	0	10	0	10
Manufacturer	100	30	130	10%	5%	13	6.5	10	0	$13-10 = 3$	$6.5-0 = 6.5$	9.5
Trader 1	130	20	150	10%	5%	15	7.5	13	6.5	$15-13 = 2$	$7.5-6.5=1$	3.0
Trader 2	150	10	160	10%	5%	16	8.0	15	7.5	$16-15 = 1$	$8-7.5=0.5$	1.5
Total										16	8	24

Model of IGST

Assume CGST @14% & SGST@12%



Pre-requisites for successful implementation of GST

- Extensive Computerisation and strong IT infrastructure
- E-filing of periodical returns
- E-payment of tax
- National portal for access of information; and
- Trained and well equipped staff

GSTN

(Stake holders: Small Tax Payers, Corporate Tax Payer, RBI, Banks, CBEC and State Tax Authorities)

- Incorporated on 28 March 2013
- Not for Profit Pvt. Limited Company
- Authorized capital - Rs. 10 Cr
- Strategic control of work will remain with Government
- Self sustaining revenue modal to levy user charge for availing services form tax payer and tax Authorities.
- Equity holder – Centre - 24.5%
- All States – 24.5%
- Financial Institutions – 51%

Issue: Who owns the data? And how the States & the Centre will be answerable to CAG when they don't own the data.

Potential Threats

- If the credit chain breaks difficult to give ITC, so cascading effect continues
- Consumers, households, companies, FIs will have to undergo behavioral changes relating to savings, investment, location of firms, form of firms linking to tax planning
- Uncertainty on Date of launching ?
- HR Capacity across the States?
- Audit trail of proposed Online system online!
- Uninterrupted Access to data for CAG, if not available
- Dual control by both Central Excise Dept. and State CTDs

Some benefits

- Tax neutrality between manufacture and services likely to create more blue collar jobs
- GST on real estate sector is likely to encourage tax compliance
- Reduces cost of capital by giving quick tax credits thus increasing productivity of capital
- CAG audit teams can cross check Returns submitted to SGST and CGST
- Concept of LTU may go, as each branch have to be a registered entity
- Litigation on relating to services like construction and contracts will go down

Going forward there Time will Answer many questions

Comments. Suggestions

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Thank you