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A Study Of Implications Of Goods And Service Tax In India

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ABSTRACT

India has witnessed major reforms in taxation since 1991. Introduction of VAT was a major breakthrough in the reforms of indirect taxes in India. But both CENVAT and VAT also have shortcomings. The Goods and Service Tax (GST) is one of the biggest taxation reforms in India, the decision on which is pending in Parliament since March 2011. The central idea behind this form of taxation is to replace existing levies like value-added tax, excise duty, service tax, and sales tax by levying a comprehensive tax on the manufacture, sale and consumption of goods and services in the country. GST is expected to unite the country economically as it will remove various forms of taxes that are currently levied at different points. The present paper attempts to highlight the major implications of the introduction of GST in India. The study, based on secondary data, highlights the impact of GST on micro and macro level of the economy. It is suggested that GST need to be implemented at the earliest to reap the benefit of it.

KEY WORDS: VAT, CENVAT, GST, Impact, Revenue.

INTRODUCTION

Any country should maintain optimization of equity and efficiency in the system of taxation for Socio-economic growth. Models of taxation should enhance the rate of growth of tax revenue by preventing adverse effects of taxes and by promoting natural compliance and making broad based taxation system. The models of taxation in India over the last 60 years were characterized by cascading and distortionary tax on production and distribution of goods and services that lead to misallocation of resources and hampered economic growth. Moreover, these models inhibit voluntary compliance. These models have a negative effect on the size of tax base and dampen the process of revenue mobilization. To address these problems, Central Value Added Tax (CENVAT) was introduced in 2000.

Introduction of VAT was a major breakthrough in the reforms of indirect taxes in India. But both CENVAT and VAT also have shortcomings. CENVAT does not cover the input value added in the supply chain before the production. Several central taxes such as additional excise duty, custom duties, surcharge etc have not been subsumed in the CENVAT. Therefore, the benefits of input tax and service tax set-off have not reached the producers and traders. Several state taxes such as entertainment tax, luxury tax etc. have not been subsumed in the VAT. Even after various initiatives by the various machineries at the centre the present taxation system is complicated and unfriendly. In this perspective, Dr Vijay Kelkar suggested a rational, scientific, simplified and modern unified tax system in tune with developed nations form the base behind the introduction of Goods and Service Tax (GST) in India.

THE CONCEPT OF GST

GST is a broad based, single, comprehensive tax levied on goods and services at each point of sale of goods or provision of service, in which, the seller or service provider may claim the input credit of tax which he has paid while purchasing the goods or availing the service; the final consumer will thus bear only the GST charged by the last dealer in the supply chain. With the introduction of GST at the State level, the additional burden of CENVAT and services tax would be comprehensively removed and all the indirect taxes of the centre and the states will get subsumed into GST. This will reduce the multiplicity of taxes. GST is a major improvement over the previous system of VAT. GST will help-widening the coverage of tax base and improve tax compliance. This may lead to higher revenue which further results in lowering of tax burden. Although there are many hurdles to be crossed before the implementation of GST like consensus over rates, constitutional amendment, compensation mechanism for States losing out on revenue, varying models, dispute resolution etc. the Central government has reiterated its commitment towards the adoption of a unique, transparent, flawless, GST for enhancing the international competitiveness of India consequent to globalization and liberalization. There are many impediments to the proposed transition. Therefore it is pertinent to study its possible implications. It is in this perspective; the present paper aims to understand the features of the proposed GST and its impact.

KEY FEATURES OF GST

- The GST would be applicable to all transactions of goods and services made for a consideration except the exempted goods and services, goods which are outside the purview of GST.
- GST will be paid to the accounts of the Centre (Central GST) and the States (State GST) separately, rates for which would be prescribed appropriately, reflecting revenue considerations and acceptability.
- Since the Central GST and State GST are to be treated individually, taxes paid against the Central GST shall be allowed to be taken as input tax credit (ITC) for the Central GST and could be utilized only against the payment of Central GST.
- The GST will be levied on import of goods and services into the country
- The rules for taking and utilization of credit for the Central GST and the State GST would be aligned.
- To the extent feasible, uniform procedure for collection of both Central GST and State GST would be prescribed in the respective legislation for Central GST and State GST.
- Each taxpayer would be allotted a PAN-linked taxpayer identification number with a total of 13/15 digits. This would bring the GST PAN-linked system in line with the prevailing PAN-based system for Income tax, facilitating data exchange and taxpayer compliance
- The taxpayer would need to submit common format for periodical returns, to both the concerned Central and State GST authorities.

BENEFITS OF GST

For business and industry

- Easy compliance
- Removal of cascading
- Improved competitiveness

For Central and State Governments

- Simple and easy to administer
- Better controls on leakage
- Consolidation of tax base
- Higher revenue efficiency

For the consumer

- Single and Transparent tax proportionate to the value of goods and services
- Reduction of prices

SHORTCOMING OF GST

- States are not having any right to make any changes in rate, it reduce the fiscal autonomy of states therefore autonomy should be given to states to change rate so that they can meet out their revenue crisis.
- States should be allowed to adjust their rates according to the social & economic objectives of states so that they can use the tax system as a tool for achieving their social & economic objectives

REVIEW OF LITERATURE

Value added tax was first introduced by a French economist Maurice Laure, in 1954. The tax was designed such that the burden is borne by the final consumer. Since VAT can be applied on goods as well as services it has also been termed as goods and services tax (GST). During the last four decades VAT has become an important instrument of indirect taxation of 130 countries resulting in one-fifth of the world's tax revenue. Tax reform in many of the developing countries has focused on moving to VAT. Most of these countries have gained thus indicating that other countries would gain from its adoption (**Keen and Lockwood, 2007**).

Hamilton et al (1991) use a general equilibrium model to analyze the impact of GST on economic growth in Canada. The federal sales tax (FST) in Canada, as in 1989, created several distortions. One of the important distortions refers to tax applied on capital goods used in production process. It was about 4 per cent on capital goods. The removal of taxes from capital goods would, over time, lower the cost of capital to domestic producers. This would lead to increases in investments, productivity and domestic real output. The GST reforms would have substantial impacts on real output, particularly for sectors which rely heavily on taxed inputs and those which compete in the international markets – either exports or import competing domestic products. The GST reform would increase the real output of the Canadian economy by approximately 1.4 per cent, i.e. about \$9 billion over 1989.

Devarajan et al (1991) analyze the impact of introducing 10 per cent VAT in Thailand using a general equilibrium model to identify gainers and losers and the effect on output, prices and incomes. Though the paper provides an overall view of the changes in aggregate exports and imports it does not bring out sectoral changes therein. It does not provide reference to the type of the model used.

Meagher and Parmenter (1993) analyze short-run implications of Australia's tax reforms of 1992 proposed as *Fightback (Liberal and national Parties, 1992)*. *Fightback* was a radical economic reform package and incorporated move to 15 per cent GST. They use a general equilibrium model for their analysis. The conclusion states that: "The GST does not discriminate between imports and domestic commodities and affects exports only in a minor indirect way. Hence, its impact on cost-sensitive industries exposed to international competition is smaller than the impacts of other taxes. Hence the implications of the GST for output and

employment are relatively small". However, the paper does not lay out changes in the composition of Australia's foreign trade.

Dixon and Rimmer (1999) use a general equilibrium model to analyse the impact of Australia's tax reforms contained in Treasury Paper (ANTS) of 1998. ANTS programme proposed tax reforms including move to 10 per cent GST. The paper concludes that the long run resource allocation gains flowing from the proposed tax changes will be negligible. Terms-of-trade effect would be negative. Composition of exports would change away from services and in favour of goods. For example, the package would harm tourism and benefit traditional exporters like iron ore.

Wittwer and Kym (2002) use a computable general equilibrium model (CGE) to analyse the impact of the GST and wine tax reform on Australia's wine industry introduced in 2000. It is concluded that export-oriented premium segment would gain at the expense of non-premium segment of wine industry. The implicit message is that such gains would originate from increased prospects of exports of the premium wine segment.

McLure (2003) outlines characteristics of a well designed indirect tax regime in the context of Canada. While consumers should be taxed at single rate sales of inputs to business should not carry any tax liability. With regard to exports the tax should be levied under the destination principle, i.e. exports should be tax-free and imports should be taxed at the same rate as domestic products.

Dr. R. Vasanthagopal, (2011) in his study "GST in India: A Big Leap in the Indirect Taxation System", found that the positive impacts are dependent on a neutral and rational design of the GST, balancing the conflicting interests of various stakeholders, full political commitment for a fundamental tax reform with a constitutional amendment, the switchover to a flawless GST would be a big leap in the indirect taxation system and also give a new impetus to India's economic change. It is also noted that, buoyed by the success of GST, more than 140 countries have introduced GST in some form to other and is fast becoming the preferred form of indirect tax in the Asia Pacific region.

Girish Garg, (2014) in his study "Basic Concepts and Features of Goods and Service Tax in India", found that GST is the most logical steps towards the comprehensive indirect tax reform in our country since independence. GST creates a single, unified Indian market to make the economy stronger. Experts say that GST is likely to improve tax collections and Boost India's economic development by breaking tax barriers between States and integrating India through a uniform tax rate. Under GST, the taxation burden will be divided equitably between manufacturing and services, through a lower tax rate by increasing the tax base and minimizing exemptions.

OBJECTIVES OF THE STUDY

The following are the objectives of the present study.

- 1) To understand the concept of Goods and Service Tax
- 2) To know the benefit of Goods and Service Tax
- 3) To understand the possible impact of GST

METHODOLOGY

The present paper is exploratory and based on secondary sources of available data from journals, magazines, articles and reports. The objectives of the study require descriptive research design. Keeping in view of the set objectives, this research design was adopted to have greater accuracy and in depth analysis of the research study. The analysis of the impact of GST on various areas has been made by reviewing the reports and available literature. An hypothetical example of comparative impact of GST on consumer price has also been exhibited.

ANALYSIS OF IMPACT

Impact of GST on Agriculture

Through a comprehensive and wider coverage of input and service taxes set-off, subsuming of several Central and State taxes in the GST and phasing out of CST, the GST could increase the prices of agricultural produce between 0.61 and 1.18 per cent. This price increase would be a boon to millions of farmers in India (Thirteenth Finance Commission, 2009).

Impact of GST on manufacturing industry

Unlike the present multistage taxation, a flawless GST can help manufacturing sector to reduce their cost to the extent of almost 50 per cent. This will help them to compete with their counterparts in the west. In the words of Vijay L Kelkar, Even a two per cent reduction in production cost will increase profits by over 20 per cent, giving headroom for reducing prices and benefitting end-users (Kelkar, Vijay, 2009). It is estimated that the implementation of GST would reduce the overall prices of all manufacturing sectors between 1.22 and 2.53 per cent (Thirteenth Finance Commission, 2009).

Impact of GST on MSMEs

The existing threshold of goods under State VAT is Rs. 5 lakh for a majority of bigger States and a lower threshold for North Eastern States and Special Category States. The present GST proposal is that the enterprises above the turnover threshold Rs. 10 lakh both for goods and services will have to be registered. Again, keeping in view the interest of micro, small and medium enterprises and to avoid dual control, the

States consider that the threshold for Central GST for goods may be kept at Rs.1.5 Crore and the threshold for services should also be appropriately high (Empowered Committee of Finance Ministers, 2009). Therefore the Increase in threshold will adequately protect the interests of small traders and industries.

Impact of GST on Housing Sector

At present, stamp duty on land and other indirect taxes on inputs are included in the value of a constructed property. On registration of the property, stamp duty is payable on the entire cost including the embedded taxes. There is no mechanism for complete set-off of these taxes which results in an increase in the overall cost of the property. The GST provides for including within its scope the transactions in real estate. Therefore, for a registered real estate builder, all taxes on inputs (including that of land) will be off-set against the tax payable on the constructed property. This will reduce cost of housing to the extent of embedded taxes and hence will benefit the poor.

Role of GST in Poverty alleviation

At present, primary food articles like rice and wheat are liable to tax by many States either at the time of purchase or at the time of sale at a lower rate. But under the GST, all food items covered under the public distribution system including rice and wheat are proposed to be exempted. As a result primary food items like rice and wheat would be exempted from GST. Since expenditure on food constitutes a large proportion of the total consumption expenditure of the poor, the GST acts as a poverty reduction tool. Moreover, basic health and education services are also intended to be fully exempted. In any case, these services will continue to be exempted from tax and therefore no additional burden will arise on account of implementation of GST (Thirteenth Finance Commission (2009)).

Role of GST on employment generation

GST contributes to increased growth of income and output in various sectors of the economy. On account of this increase in higher growth, there will be large scale employment opportunities.

Role of GST in price reduction

GST is a regressive tax system as it minimizes the number of tax rates to a single (dual) rate. However, there is allegation that the subsuming of major Central and State taxes in GST, continuous chain of set-off of input goods and services and phasing out of CST the commitment of taxes on goods would come down under GST. It is anticipated that, other things remaining the same, this would encourage manufacturers and distributors to reduce the prices of their produce and ultimately benefit the consumers. Hence, it is argued that GST would be pro-poor and not regressive.

Impact of GST on International Trade

It is sought that the export of taxes to other countries to be eliminated through duty drawback on the basis of estimated incidence of embedded taxes. By considering the weaknesses of the present system, the GST requires that exports from the taxing jurisdiction would be tax free and imports into the jurisdiction would be

taxed at the same rate as products produced and consumed within the jurisdiction. Consequently, both export-oriented industries and import-substituting industries would become internationally more competitive. As a result, while exports can be expected to register an increase, imports are likely to decrease. The gains in exports are expected to vary between 3.2 and 6.3 per cent and imports are expected to gain somewhere between 2.4 and 4.7 per cent (Thirteenth Finance Commission, 2009).

Impact of GST on GDP

The implementation of GST on goods and services is expected to induce India's Gross Domestic Product somewhere within a range of 0.9 to 1.7 per cent. Again, these additional gains in GDP would be earned during ever year over and above the growth in GDP which would have been achieved otherwise.

Impact GST on Government Revenue

Since all goods and services come under GST, the number of exemptions would reduce very much. Again, the tendency of tax evasion by producers and distributors will be low as to the single and low rate of tax proposed under GST. Further, increased GDP, indirect positive impact on direct tax collections, gain for the government on account of reduction in the price level of a large number of goods and services consumed by the government. As a result, GST contributes to the increase in government revenue.

Table 1: ANALYSIS OF PRICE UNDER PRESENT TAX SYSTEM & UNDER GST

A	MANUFACTURER TO WHOLESALER	UNDER PRESENT TAXES (Rs)	UNDER GST (Rs)
	Cost of Production	100000	100000
	Margin of profit @20%	20000	20000
	Price	120000	120000
	central excise @ 14%	16800	NIL
	VAT @ 12.5%	17100	NIL
	Central GST at Assumed rate of 12%	NIL	14400
	State GST At Assumed Rate of 8%	NIL	9600
	Total Price of Manufacturer	153900	144000
B	WHOLESALER TO RETAILER		
	Cost of goods to Wholesaler (after input tax)	136800	120000
	Margin of profit @ 5%	6840	6000
	Price	143640	126000
	VAT @ 12.5%	855	NIL
	Central GST at Assumed rate of 12%	NIL	720
	State GST At Assumed Rate of 8%	NIL	480
	Total Price of Wholesaler	144495	127200
C	RETAILER TO FINAL CONSUMER		
	Cost of goods to Retailer	144495	127200
	Margin of Profit @ 10%	14449.5	12720
	Total	158944.5	139920
	VAT @ 12.5%	1806.1875	NIL
	Central GST at Assumed rate of 12%	NIL	1526.4
	State GST At Assumed Rate of 8%	NIL	1017.6
	TOTAL PRICE TO FINAL CONSUMER	160750.6875	142464
	TAX COMPONENT IN THE PRICE TO THE FINAL	36561.20	27744

TOTAL PRICE EXCLUDING TAXES	124189.5	114720
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(Source: Authors own computation)

The GST must be applied on all sectors both tradable and non-tradable. Thus all services must fall under the preview GST and that the export should be fully tax rebated. The countries now introducing GST without weaknesses of the past would get benefits of expansion of their international trade with special affect on exports.

Along with prudent accounting policies, transparency and the support of electronic controls, introduction of GST brings down the peak rates of taxation and enhance revenue growth. The table 1 exhibits the comparison of the present rate of tax and the proposed GST

SUGGESTIONS AND CONCLUSION

GST is a single national uniform tax levied across India on all goods and services. In GST, all Indirect taxes such as excise duty, octroi, central sales tax (CST) and value-added tax (VAT) etc. will be subsumed under a single regime. Introduction of The Goods and Services Tax (GST) will be a significant step towards a comprehensive indirect tax reform in the country. It is expected that GST brings about efficiency and transparency in the indirect tax system in India. GST will also encourage an unbiased tax structure that is neutral to business processes and geographical locations. Recognizing its positive implication on various sectors in India, it requires a consensus among all political parties and state governments. Due to lack of consensus among the States and Centre on various aspects relating to limiting fiscal autonomy of the States, the implementation of GST has been delayed several times. In India, Implementation of GST would greatly help in removing economic distortions caused by present complex tax structure and also will help in development of a common national market. Therefore, the governments shall make consensus effort to implement GST and reap the benefit of it.

The switch over to a flawless GST would strengthen the indirect tax system gives a new impetus to India's economic change. The positive impact of GST depends on its neutral and rational design balancing the conflicting interests of various stakeholders. It depends on complete political will for a fundamental tax reform with necessary constitutional amendment. On the success of GST more than 130 countries including Asia pacific region have introduced in some form or the other. There are several issues and challenges in the introduction of GST. While some of these are short-term issues, some others are long term issues and thus have a lasting impact on the business. An understanding of potential issues is imperative for timely implementation of measures to overcome these issues and avoid potential impediments.

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