GOODS & SERVICES TAX
- An Overview

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Forum of Free Enterprise

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"Free Enterprise was born with man and shall survive as long as man survives".

- **A. D. Shroff**
Founder-President
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SHAILESH KAPADIA

(24-12-1949 – 19-10-1988)

Late Mr. Shailesh Kapadia, FCA, was a Chartered Accountant by profession and was a partner of M/s G.M. Kapadia & Co. and M/s Kapadia Associates, Chartered Accountants, Mumbai.

Shailesh qualified as a Chartered Accountant in 1974 after completing his Articles with M/s Dalal & Shah and M/s G.M. Kapadia & Co., Chartered Accountants, Mumbai. Shailesh had done his schooling at Scindia School, Gwalior and he graduated in Commerce from the Sydenham College of Commerce & Economics, Mumbai, in 1970.

Shailesh enjoyed the confidence of clients, colleagues and friends. He had a charming personality and was able to achieve almost every task allotted to him. In his short but dynamic professional career, spanning over fourteen years, Shailesh held important positions in various professional and public institutions.

Shailesh's leadership qualities came to the fore when he was the President of the Bombay Chartered Accountants' Society in the year 1982-83. During his tenure he successfully organized the Third Regional Conference at Mumbai.

Shailesh was member, Institute of Fiscal Studies, U.K.; member of the Law Committee and Vice-Chairman of the Direct Taxation Committee, Indian Merchants' Chamber. He was also a Director of several public companies in India and Trustee of various public Charitable Trusts.

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GST : A Business Perspective

Jamshyd Godrej *

The Goods & Services Tax (**'GST'**), is the biggest reform in the Indian indirect tax structure since the economy opened up, twenty six years ago. The 122nd Constitution Amendment Bill which was cleared in the Rajya Sabha last August laid the foundation for the change. It was further cemented by the formation of the GST Council & passage of the GST Act and Rules.

As per the current law, businesses are required to pay multiple taxes and adhere to multiple compliances and timelines. Once GST comes to play, all taxes will come under one umbrella, making it much simpler for the industry. The GST Law will also prove to be a boon for the industry that currently has to deal with different tax processes in all different States. The hassle of dealing with

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different State Governments with varied Rules will be done away with.

This tax aims to make India a single market, avoid the effect of cascading taxes and reduce tax burden on the consumer. The key features of this tax regime are elimination of tax on tax, lower rates, faster growth and system driven compliances for the industry as well as the consumers.

While GST will impact various stakeholders differently, the consumer shall be the most benefitted party. Consumer items continue to be exempt from a levy of GST or are to be subjected to GST at lower rate as more than 50% of the items within the consumer price index bracket are placed at a lower rate than they presently are.

Having said the above, I am mindful that this is a complete change for the Industry and its functioning. The way of dealing with transactions would completely undergo a change with the new concept of supply resulting in a paradigm shift from the age old scanner of manufacture, sale and service concepts. This would not only entail changes in business processes but would completely change the accounting processes and the ERP system of every business would require to adapt to this change quickly.

For Corporates, now the decision to set up manufacturing operations and supply chain would be influenced not by tax benefits, but based on business efficiencies. With destination based principle of taxation and export to be zero rated, the competitiveness of Indian firms would surely increase.

The law in the current form has been successful in attempting the above. Credit should be given to the Tax Authorities and the political willingness to achieve this by both the Houses of Parliament, State Governments and the Finance Ministry.

With the support of the industry and the receptive consumers, GST will be successfully implemented and accepted by India. My sincere hope for the future is an India in which trade is free, compliances are easier, growth is phenomenal and consumers are satisfied. This would have been best achieved through a single low rate structure, similar to what was originally proposed.

India Goods and Services Tax – a Macro Overview

Bhavna Doshi*

The Tax

India Goods and Services Tax (GST), a new consolidated indirect tax, introduced from 1 July 2017, is a common tax on supply of both, goods and services, to be commonly levied and collected by Centre, 28 States and 7 Union Territories, on a common base, at common rates, having common procedures to be administered fully electronically through a common digital platform.

GST replaces several current levies and cesses at both Central Government and State Government level. Key among these levies and cesses are the Central Excise Duty levied under Central Excise Act, 1944 on manufacture of goods in India, Service tax levied under Finance Act, 1994 on provision of services and State Value Added Tax levied under

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State specific VAT legislations on sale and purchase of goods within the State (intra-state transactions of sale or purchase of goods).

The Mega Reform –Journey to Reality

Consolidating several levies and cesses at different levels into GST was a mammoth task. To begin with, it required amendment to the Constitution of India as the Constitution authorizes specific level of government (Central/State/Local) to impose specified taxes on specified activities. The Constitution authorizes Union Government to impose tax on imports and on manufacture of goods in India (Central Excise Duty) and State

Governments to impose tax on activity of sale or purchase of goods within the State (intra-state transactions). Authority to levy service tax was with Central Government and it was derived from residuary powers of Central Government.

Consolidating these taxes under one common levy on goods and services required that levy on manufacture is removed on goods covered under GST and authority is granted to both, Union as also the State Governments, to levy tax on supply of both, goods and services. So, enable Union Government to impose tax on the whole supply chain (as against only upto manufacturing level) and State Governments to also impose tax on services.

The agreement as to the amendments and the language of amended articles of the Constitution was achieved after detailed deliberations over, almost nine years, through the Empowered Committee of State Finance Ministers. The efforts also saw one failed attempt in that, the 115th Constitution Amendment Bill, 2011 could not be passed by the Parliament and it lapsed with end of term of Parliament. New elected government picked up the task from where it was left prior to election. The 2011 draft of the amendments was reworked, different concerns, especially of compensation to the State Governments, should they suffer loss on account of GST introduction and other aspects, were addressed and a new amendment bill, the 122nd Constitution Amendment Bill, 2014 was introduced in Lok Sabha. This Bill was passed after due deliberations and process by Parliament, it received assent of 50 % of the State Legislatures and was finally enacted as the Constitution (One Hundred and First) Amendment Act, 2016, with assent of President of India on 8 September, 2016.

This paved way for constitution of GST Council, as set out in Article 279A of the Constitution of India, which has representations of Central Government and all the State Governments.

The GST Council considered drafts of legislations relating to Central GST (C-GST) and State/Union Territory GST (S-GST/UT-GST) and Compensation Cess. This too took several rounds of discussions and detailed consideration of provisions at several levels including the GST Council. The C-GST Act, UT-GST Act and Compensation Cess Act received approval of Lower House of Parliament (Lok Sabha) on 29 March, 2017. These enactments received assent of the President on 12 April, 2017.

This was followed by enactment of State Level GST Legislations by States. Most States could hold Legislative Assembly Sessions and passed Bills whereas some States (Kerala and West Bengal, among the larger States) introduced the levies through Ordinances.

While all State Governments (except Jammu and Kashmir) and Central Government implemented GST from 1 July, 2017, the State of Jammu and Kashmir implemented it from 8 July, 2017 on account of special rules governing that State.

While the process of amendment to the Constitution and enactment of Acts was in progress, drafts of rules setting out processes were issued from time to time for public comments, suggestions were examined, public consultations were held and also discussed at length at GST Council and finally issued on the D-day.

Rate schedules were another area requiring detailed considerations. These too were broadly agreed and announced in May 2017, based on preliminary discussion at the GST Council. They were further deliberated and finalized after considering difficulties pointed out by trade bodies and others.

And, the GST saw the light of the day at midnight of 30 June 2017 and 1 July, 2017 and the new levy, GST came into effect !

Introduction of GST is a truly unparalleled accomplishment for a country having federal structure of governance, population of over a billion people and wide diversity in many ways.

The Model – Australia, EU and Canada and India

Our new indirect tax system retains the basic principles of value added tax system, adopts features of indirect taxation system of some developed, more advanced/ experienced nations, encompasses latest recommendations of Organisation of Economic Co-operation and Development (OECD) for consumption taxes and tops it with India's unique challenges, traditions, culture, level of development, and experience of our own taxation systems.

When we look around the world for comparables, we find Australia, Canada and EU has some comparable features in their tax reforms and consumption tax models.

Australia consolidated wholesale sales tax and state level duties and taxes into a federal level system of GST in 2000 and they adopted a standard rate of 10 % (comparatively lower rate). So, they now have only one Federal GST and states do not levy sales tax as also few other levies, duties which they were levying prior to introduction of federal level GST described as "New Tax System". It used pricing control and anti-profiteering provisions to monitor prices.[1]

European Union Council issued a direction[2] in 1977 to all member nations to harmonize their national VAT systems through which tax was levied on supply of goods and services; turnover taxes. The objective was to achieve a common base for taxation, apply common meanings to the terms "taxable person", "taxable transaction" and others, common provisions relating to place of supply of goods and services, common list of exemptions, deductions, assessment basis and the like so as to achieve non-discrimination as to origin of goods and services and permit fair competition among member nations. The system, in a way, is similar to our State Level VAT system (except that EU VAT is

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1 *GST final report - ACCC oversight of pricing responses to the introduction of the new tax system-January 2003 - https://www.accc.gov.au/system/files/GST%20Final%20 Report.rtf*

2 *Sixth Directive, 77/388/EEC -17 May 1977 – ref http:// eur-lex.europa.eu/legal-content/EN/TXT/?uri=URISERV% 3Al31006*

at independent country level and includes taxation of services and importation of goods); not strictly comparable with our New GST system.

Canada has a federal structure of governance and they have national as well provincial level (similar to States in our system) GST[3]. The rate of the national level GST is uniformly applied across the country but, States determine their own system of taxation including rate of tax on supply of goods and services and they have varied systems. One province (Ontario) has value added tax system described as Provincial Tax System;, some provinces impose tax only at retail level (British Columbia, Manitoba and Sasketchewan); some provinces (Nova Scotia, Newfoundland and Labrador) have merged their provincial taxes with national tax and adopted harmonized system of taxation (HST) administered by national administrator; the Canada Revenue Agency , one province (Alberta) does not impose provincial tax at all[4]. So, this is also not comparable with Indian system of GST[5].

We, in India, have adopted dual model for taxation of goods and services whereby Central Government and State Governments (including Union Territories) will levy and administer the new tax, GST on supply of

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3 *Introduced from 1.1.1991*

4 *https://en.wikipedia.org/wiki/Goods_and_services_tax_(Canada)*

5 *https://en.wikipedia.org/wiki/Goods_and_services_tax_(Canada)*

goods and services. Uniformity, non-discrimination, no non-double taxation or no non-taxation are sought to be achieved through overarching GST Council, a body established through the Constitution having powers to make recommendations on all key aspects of GST like rate, tax base, goods, services , taxes to be subsumed in GST and so on. This body is somewhat on the lines of European Commission. The voting powers within GST Council are so fixed that neither Centre alone nor States (even if they all join hands) can change the decisions of the Council, a path breaking move to achieve uniformity and stability, as is described, 'one tax across the nation'.

GST Features

We have adopted, as charging event, the concept of "supply", the term used internationally, replacing manufacture, sale and provision of services as major taxes, Central Excise Duty (on manufacture levied by Central Government), State Value Added Tax (on sale of goods levied by State Governments), Service tax (on provision of service levied by Central Government), Octroi and Entry tax (on entry of goods in local area for consumption levied by Local Authorities and State Governments), Luxury tax (on specified services levied by State Governments) and specified cesses levied by Central and State Governments merged into one tax, GST, levied at the same rate by Central and State Governments on common base.

All taxable goods and services, across the country, when they move from one state to another, will have paid tax, the Integrated GST (I-GST) which is sum of Central GST (C-GST) and State GST (S-GST) or Union Territory GST (UT-GST). This will be so, even in cases where goods/services move to own branches, depots, distributors, stockists, otherwise than on sale/transfer of property in goods. The I-GST so paid, to the extent of B2B (and, in most cases, when the goods move to own branches, depots and like will be B2B transactions) will be fully creditable unlike the earlier system where, Central Sales Tax (CST) was not levied on transfer of stocks to own depot, branch (against F form). CST was levied at concessional rate for B2B transactions (against C form) and was not creditable; it was retained by the originating State.

The objective of this design feature of our GST system is to ensure that goods and services moving across States do not have to be supported by C/F/I and like forms, prevalent under the current system for no or concessional rate of tax (forms to be obtained from tax department) as also verified at check-posts set up by State Governments at their borders to capture movement of goods without taxes, can be done away with (to achieve one tax across the nation without, sort of, border restrictions) and, at the same time, provide reasonable assurance to the State Governments of non-leakage of revenue. Of course, unscrupulous will attempt to find ways around it; vigilance and way bill mechanism in the new system seek to track such leakages.

So far as movement of goods and services pursuant to supply within a State is concerned, goods and services would have paid due tax, C-GST plus either S-GST or UT-GST.

I would not be surprised, if, after few years, some of the Union Territories merge their UT-GST and some smaller States merge their S-GST with C-GST and hand over tax administration to Central Government – like Harmonized GST of Canada. This could result in fair degree of saving of tax compliance cost for businesses and administration cost for governments at State/UT level.

Gains and Pains

The charge on supplies within one legal entity [identified based on Permanent Account No (PAN) allotted by Income tax Department], when goods move to another State to self has a logic in that it enables transfer of input tax credit from one State to another where sale will take place and the input tax credit can be utilized. This feature is enabled through I-GST mechanism which is a sort of settlement mechanism. I- GST can be used for payment of I-GST itself, C-GST, S-GST and UT-GST and, in same manner, all those taxes, C-GST, S-GST and UT-GST, can be used for paying I-GST. Same is not true so far as C-GST and S-GST/UT –GST are concerned. They will move parallel and not meet meaning, C-GST input tax credit cannot be utilized for payment of S-GST/UT GST and vice versa.

This requirement of payment of tax on inter-state transfer of stocks will add cost in terms of cash flow management. But, bigger worry of businesses is valuation – whether administrations will be flexible on this aspect since the transaction is tax neutral. Current provision, to the effect that value declared by tax payer for such supplies will be accepted if the taxable person is eligible for “full” input tax credit or that, the value could be 90 % of the sale price at the time of supply to third parties, is met with skepticism.

The inclusion of such provision for services is though puzzling. Valuation of services for transfers within an organisation will be a challenge and, it appears that the department’s perspective is that even employee cost must be included to arrive at open market value of services. This means, taxing employee services which are specifically excluded from charge of GST. There is provision for input service distribution and that could have been used for transfer of input tax credits in case of services. Some rethink is required on this aspect. Hopefully, sooner than later!

Our GST adopts same basic principles of value addition – which we had adopted for Central Excise Duty, State VAT and Service tax. The chain for taxation starts from origin and ends when it reaches the ultimate consumer. Taxes paid at each of the earlier stages are rebated through mechanism of input tax credit. Ideally, therefore, no tax cost should stick to businesses, they being mere pass through entities. Practically, that does not happen due to non-allowance of input tax credit on several grounds like exempt supplies with taxable supplies, supplies used for personal purposes or those, where input tax credit is specifically restricted like motor vehicles.

A provision not to allow input tax credit when no tax is payable on output is a reasonable one as the chain of input tax credit stops there. The difficulty arises when the list of disallowable input tax credit becomes large. The items on which input tax credit is not allowable under our GST include expenses like outdoor catering, rent-a-cab, free samples, health insurance of employees and others. These have been subject matter of significant litigation in the past and attempt appears to be to clarify intent and avoid litigation; provide certainty. However, it is desirable that tax paid on all inputs, goods and services, used for purpose of business ought to be eligible for input tax credit to minimize tax cost and cascading.

Exports will be zero rated and imports will be charged to IGST, collected, at the time of clearance of import consignments, with the Customs duties. There is a feature in export of services that appears to be different from current regime of service taxation. A supply of service where supplier is in India and place of supply is outside India is an interstate transaction. Where the recipient is also outside India, consideration is received in convertible foreign exchange and the supplier and recipient are not establishments of distinct persons (different establishment of the same legal entity), the transaction is "export of service"[6] and will be zero rated. The difference is, if these three conditions are not fulfilled, supply will be subjected to IGST though the place of supply is outside India.

The rates and exemptions under GST are more or less maintained at the current level to ensure that the current overall tax burden does not increase in GST. There are four rate bands, 5% and 12% (merit rate), 18 % (standard rate) and 28 % (demerit rate). Special rate of 0.25 % is prescribed for rough diamonds and 3 % for gold, gold jewellery, silver and processed diamonds.[7] There is also Compensation Cess which varies significantly and is fairly steep for luxury/sin goods like tobacco and tobacco products. It ranges from 1 % to 15 % for motor vehicles depending on specifications. The exercise of rate fitment is an ongoing exercise.

The varied rate structure is different from other countries and a question often asked, in the

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6 S2(6) of IGST Act,2017

7 Statement of Revenue Secretary post GST Council Meeting of 3 June 2017- Business Standard Article of 5 June,2017- business-standard.com backdrop of one of the objectives of GST of simplification of current complex indirect tax structure, is: is this simplification? While there could be no two arguments that ideally, one ought to have only two rates, merit and standard, given the diversity and need for consideration of all strata of society, variable rate was a must for our country. Over a period of time, this too will be modified and we too will move to two or three rate structure.

Several areas where there was litigation and department has accepted the position or there are decisions of higher courts, have been incorporated in the law and will hopefully, reduce litigation. For example, a specific provision is made as regards amalgamation or merger of companies[8]. Not all issues are addressed though and, hopefully, will be addressed as we go along.

There are few pain points too like paying tax on reverse charge basis on purchases from unregistered persons, generating self invoice and like. Relief, in the form of exemption for intra-state purchases, in aggregate, of Rs 5000 (Rupees Five Thousand) in a day from unregistered supplier(s)[9] will reduce the rigour of this provision to some extent, especially for small and medium sized businesses. This specific provision will, no doubt, increase cost

8 S 87 0f CGST Act,2017

9 Notification No. 8/2017-Central Tax (Rate) dated 28 June,2017 of compliance and will lead to the threshold losing its relevance.

Reverse charge is also continued for few services like that of legal services provided by individual advocate or firm of advocates to business entity. This too is not compatible with GST concept and ought to have been avoided.

Need for pan India service providers to register in each state and work out tax liability state wise as also requirement for providing information about each branch together with name and address of the person in charge, besides proof of address, is a time consuming exercise. May be, going forward, IT system will soften this burden.

There is significant unease among pan India suppliers of goods and services about possibility of differing views/approaches that could be adopted by different authorities and likely multiple demands on identical transactions. A centralized audit system for such suppliers by a group comprising officers representing Central Government and State Governments (these could be rotated from State to State depending on the volume of activities in a State and can be done electronically without human intervention) is a solution, referred to in the passing, and may be adopted as the tax authorities across different States gain experience.

Requirement of quoting detailed HSN Code or Service Accounting Code at the time of registration on GSTN portal itself is causing huge anxiety especially for non-manufacturing sector. Asking this information, at this early stage of GST implementation, could be done away with. Broad industry classification could meet the objective; facilitating government in collating industry-wise data and simplifying process for tax payers from compliance perspective.

There are very detailed and exhaustive transition provisions which have envisaged various situations and dealt with them. Yet, there are areas that need to be addressed. Leasing industry is an example where transition provision is missing.

A provision that is causing significant apprehension during transition is that of “anti-profiteering”; up to what level should one go and how to determine it? There are mixed reports from Australia and more recently, Malaysia, as to effectiveness of such provisions in controlling prices post GST implementation. Some sectors like consumer goods or fast moving capital goods, where there is intense competition, will self-adjust prices and the likelihood of price increase is less. Monopolies and monopolistic sectors are the ones where Government will have to focus. This will certainly be an area of intense interest for all, especially, the consumer groups.

Entirely digital administration is a super feature of our GST system facilitating several processes like enabling businesses to comply with laws of all the States from one location; complete one to one matching of invoices to avoid disputes and demands at a later date. But, this feature has its own challenges relating to connectivity issues, comparability and so on. Here again, as we gain experience, systems and processes will be streamlined. Technology platform will significantly ease verification of input tax credits and overall compliances as is the experience with TDS under Income tax.

Mindset change

In midst of all this, the most encouraging factor is the constructive approach of Governments, with full support and attention from the highest level, from Prime Minister, Union Finance Minister, State Chief Ministers, all Finance Ministers and other functionaries. They are addressing concerns and suggestions in most rational and consensual manner. We do hope this positivity continues and percolates down to the administrative officers; we do hope to see complete “mind set change” all around and Governments to adopt the maxim that the objective of tax gatherers is to collect due tax in a fair manner and not penalties; they should not be unjustly enriched!

Reflections on Economic Impact of GST

Sunil S. Bhandare*

The transition to the GST regime with effect from July 1, 2017 is found to be virtually smooth, albeit, as is to be expected from such momentous, game-changing reform, there are still some instances of confusion and disruptions. There have been quite a few detractors of GST, and also reports that in a few places traders having gone on strike in protest against GST – illustratively, Surat and Ahmedbad textiles and garment traders. What is, however, encouraging is the fact that since the launching of GST, a progressively positive outlook is discernible in many sectors of the economy. Further, the spokespersons of Ministry of Finance [MOF] and Govt. of India continue to assuage genuine apprehensions of concerned stakeholders about substantive and specific features of GST, especially about the

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rate structure, registration, filing of returns and other compliance requirements from business, industry and professionals. Thus, a fuller, smoother and more effective change over to GST would hopefully be accomplished within a reasonable time-span.

As is to be expected, the MOF is closely monitoring the impact of GST, especially on supply and pricing of products and services in the market place. The official spokespersons have been reassuring that no major disruption has been witnessed so far. They are also promising that appropriate corrective measures would be taken based on feedback and ongoing experiences from markets and concerned firms, organizations and other entities. Moreover, there is going to be strict vigilance on cases of 'profiteering', wherever the benefit of reduced tax incidence is not passed on to the ultimate consumer. The monitoring body for this purpose is likely to be set up by the GST Council. However, it must be stressed candidly that any sudden modification in the already effective rate structure – and that too adverse in terms of tax incidence, as has been done by the GST Council recently in case of cigarettes through increased cess – does [and would] create unnerving sentiments in the markets. Going forward, such changes causing adverse incremental incidence of GST rates on goods and services, need to be eschewed with a view to creating a credible, stable and sustainable GST environment in the economy.

GST Rates Structure

Before turning to the core of this article, a word about the GST rate structure: After the passage of various separate legislations by the Parliament and States Assemblies, namely, Central GST (CGST; Integrated GST (IGST); Union Territory GST (UTGST); the Bill for Compensation to States; and SGST (States GST), the most important task accomplished by the GST Council was the fitment of well over 1200 commodities as well as some 600 services under the approved rate structure. This was one of the toughest challenges faced by the GST Council, given the complexities of the then prevailing India’s domestic indirect tax system. But the GST Council achieved this remarkable feat by reaching out an agreement on classification of goods and services and fixing them under the appropriate rate structure.

Accordingly, there are four primary GST rates slabs for various items – low rate of 5%; standard rates of 12% and 18%; and the high rate of 28%. Gold and jewelry attracts concessional GST rate of 3%, while rough diamonds at 0.25%. Besides, essential goods are either exempt or subject to zero tax rating. Apart from this, an additional cess [at varying rates] is applicable on sin and luxury goods. Evidently, 81% of all goods and services fall below or in 18% tax bracket. While 7% of the items come under the exempted category, 14% fall in the lower slab of 5% tax; 14% of the items in 12%; and 43% of items under the 18% slab. The highest slab of 28% along with cesses in some cases is attracted by the remaining 19% of goods and services. [Please see the Annexure: Table 1 and Table 2 for the rate structure with illustrative list of goods and services, respectively]

It is also important to recognize the fact that the GST framework has now been completely rationalized by subsuming nine central taxes under CGST [Central GST], namely, Central Excise Duty, Additional Excise Duty, Service Tax, Countervailing Duty, Special Additional Duty of Customs, Central Sales Tax, Central Cesses, et al. Like-wise, the SGST [State GST] subsumes seven or eight different states taxes such as VAT/ Sales Tax, Luxury Tax, Entertainment Tax, Entry Tax, Octroi, et al. Such transformation in the indirect tax system would certainly go a long way in removing most of the inefficiencies associated with the erstwhile complex web of India's indirect tax structure.

Assessing the Economic Impact

Surely, these are early times to make any meaningful and substantive micro as well as macro level impact analysis, albeit the immediate reports do suggest that prices of many consumer products, intermediate goods and capital goods have either remained steady or experienced marginal up or down variances. But all such cost and price variances either beneficial or adverse to the manufacturers, traders and consumers, vis-à-vis the scenario prevailing prior to the change-over to GST, have so far been found to be within a moderate band-width. Admittedly, there have been many instances of traders destocking inventory, and the consequent slowing down or contraction of output in large segments of the manufacturing sector. But much of this response has been attributable to the initial lack of clarity on GST rates and traders' typical mindset/ hesitation to come within the ambit of GST registration procedures and related compliance requirements.

Surely, all such resistance and distractions are on the mend as the Governments across our federal system have moved forward decisively with the GST implementation. There is so much of awareness and educational efforts from the Government for the benefit of all stakeholders through well-articulated official media campaign explaining the essential features of GST, and dispel any doubts and misrepresentation of facts. More significantly, the new 'one nation, one tax' regime has already led to removal of a host of check posts at inter-state borders, including Octroi nakas prevalent in some States – the classic case of latter being that of Mumbai and some key locations in Maharashtra. For decades, such barriers used to clog the movement of traffic for hours [if not days] and delay transportation and shipments of goods both for domestic consumption and exports. As a consequence, Indian economy suffered hugely in ensuring efficient distribution network, logistics management and achieving competitive expansion of domestic and export markets. It is widely reported that there is now a virtual dismantling of inter-state barriers to trade and mitigation of harassment from the 'rent-seeking' corrupt inspector raj associated with the earlier tax regime. But there still may be a long way to go!

Incidentally, the stock markets, which are often perceived to be discounting the future prospects of the economy in general and of the corporate sector in particular, seem to have expressed their 'vote of confidence' over the GST launch. Illustratively, the SENSEX has been scaling new peaks practically every week – since the launching of GST; it has risen to an all-time high of 32,673 on July 27, 2017 before retreating somewhat on the next day. In the current financial year so far, it has risen by as much as 9.2% from level of 29,620 as on March 31. Undoubtedly, this phenomenon cannot entirely be attributed to the GST reform, but we believe this is one of the dominant factors in fortifying the investment outlook in the secondary markets of our economy. It may perhaps take some more time for such buoyancy to transmit into the real capital formation activity in the corporate and other sectors of the economy, as there are many other dominant issues such as excess capacities, impaired twin balance sheet problems of banks and major borrowers, etc. holding back the 'animal spirit' of business and industry.

Be that as it may, there obviously would be **multiple dimensions while evaluating the economic impact of GST.** The points of impact are principally through the GST rates structure and the built-in mechanism of set-off through an input tax credit, i.e, through the tax paid on the purchase of goods and services available for set-off against the tax payable on supply or sale of goods and services – and collected from the consumers at the point of consumption destination. This system, thus, eliminates the distortions in the cost and pricing mechanism through cascading of taxes under the previous indirect tax regime.

The economic impact of GST would obviously be visible and realizable both at the micro and macro levels through five key parameters: ***First,*** the changes in cost and prices of goods and services at specific product/service categories due to the incidence of GST along with the benefit of input tax credit. It has been proclaimed by the GST Council and official spokespersons of the Ministry of Finance (MOF) that in deciding the GST rates all the efforts have been made to make them closer to the then prevailing effective tax burden so that the transition to the new indirect tax system is revenue neutral. In the process, it would also virtually avoid any adverse distortions in the existing costing and pricing of products and services.

At the micro level, there are reports that prices of most products have remained virtually unchanged, but decreased in some, while increasing in others. ***At the macro level***, it is reasonable to expect only marginal deviations [with slightly upward bias in the short-run due to supply disruptions] in CPI and WPI inflation rates from the trends observed in the recent months due to the GST. Over the medium to longer-term perspective, the GST reform is going to be beneficial due to elimination of cascading of taxes; better working capital management; efficiency and productivity gains; et al.

Incidentally, the Revenue Secretary, Government of India, stated sometime in June 2017 that “the internal estimate is that inflation should be down by 2%. But this is subject to all producers passing the benefit of downward revision”. Various members of the Council, who represent the interest of their respective States, have also been very positive about the outcome of their efforts so far and the Kerala’s FM believes that the GST roll out would confer *“windfall gains”* on consumers. He also pointed out that “in the current structure, 70% of commodities face 28% plus tax rate. Now, only 20% of those goods will be taxed at the 28% slab”.

Second, the impact on production and investment: at the micro as well at the macro level, there is bound to be some moderate short-term setback to growth of economic activities, especially in manufacturing and construction – a large part of this would be felt by the MSME and the unorganized sectors of the economy, wherein GST literacy is currently found to be wanting and considerable degree of confusion and misinformation prevails. Hopefully, all that would be resolved over the period of next three to four months and normalcy would set in gradually. The challenges of investment revival have been of a long-term nature, as briefly mentioned before, and the GST *per se* is certainly not going to resolve them in the immediate future. However, over the medium to long-term scenario, GST offers several positive features for strengthening the investment profile of the economy – not just in terms of efficiency and productivity in the use of capital through reduction in incidence of effective tax on capital equipment and gains through increased turnover of capital, but also in ease of doing business.

Third, the impact on tax buoyancy: the GST framework ensures widening of the tax base, especially through “a quantum leap in transactions trails and logistical efficiencies”. In effect, it is expected that the elasticity of indirect tax revenues in relation to economic growth would improve significantly thanks to [a] larger canvass of the economy [*a la* unorganized/ informal sector] likely to be progressively brought within its fold; [b] plugging of the loopholes and leakages; [c] improvement in tax administration; and [c] incremental economic growth, especially in manufacturing, construction and services sectors. India's aggregate tax [Center and States combined] to GDP ratio is hovering in the range of 16 to 17% for the past many years, of which the ratio of all indirect taxes of GDP is in the range of 10.5 to 11.5%. Ideally, the economy of our size and structural spread need to have at least 4 to 5 percentage points higher aggregate tax/GDP ratio. Hopefully, the new GST regime could contribute at least half of that incremental ratio in the next three to five years. Incidentally, in OECD countries [advanced economies] the average tax/GDP ratio is about 33%, but several emerging market economies, the ratio is 20% or more.

Fourth, the improved tax buoyancy would obviously have several beneficial spin offs. It would strengthen the government's efforts of fiscal consolidation; generate fiscal space for investment in physical and social infrastructure; encourage government to push direct tax reforms – rationalization and reduction in corporate and personal income tax rates; facilitate better management of public debt, et al. Such improvement in fiscal health would augur well from the perspective of the monetary policy as well – it would facilitate the Monetary Policy Committee and the RBI to ease interest rates, if at the same time, the CPI inflation rate is anchored within the comfort zone. But all such beneficial spin offs would require effective implementation of GST and going forward moving towards more simple GST rate structure

– preferably not more than three rates schedule [including the exempt or zero rating]. These are medium to long-term expectations from the GST system.

Fifth, the positive impact on export competitiveness: India's external sector is expected to receive impetus under the GST framework. In particular, since exports will be zero rated, exporters would be entitled to claim the entire trail of input tax credits. Besides, the gains in overall competitiveness of manufacturing activities under the GST structure would also incentivize incremental export efforts from both the existing exporters and a new class of manufacturers over the medium to long-term period. Also, it is pointed out that the GST regime would eliminate the erstwhile distortions caused by an inverted duty structure under which domestic producers hitherto used to pay high costs on taxed intermediate inputs made elsewhere in the country, making them less competitive relative to imports which land at lower cost. This would also improve competitiveness of industry and encourage increased export efforts. Equally importantly, the GST regime would enhance India's status in the ease of doing business, and consequently, encourage better FDI flows– some of which could serve exclusively the global markets. There are some reports about the lack of clarity and confusion prevailing with respect to Export Oriented Units [EOUs] and Special Economic Zones [SEZs] about certain provisions of the GST, and hopefully, all those will be sorted out promptly by the GST Council and the MOF.

Concluding Observations

In summing up, several inadequacies and anomalies have been found in the GST reform; and some of its features are found not in conformity with advice and expectations of the eminent economists and fiscal policy experts in the country. Many of them wanted only a single or at best two or three rates structure, based primarily on considerations of simplicity and effectiveness administration that is free from leakages and corruption. However, the actual operational GST framework has come to embed multiple rates including some special categories and levy of cesses. Experts wanted electricity and all petroleum products [crude petroleum, high-speed diesel, petrol, natural gas and aviation turbine fuel] to attract GST, but the GST Council/MOF decided otherwise.

Experts have argued that were GST to be endowed with above features, the gains to the economy would have been far superior. But in the interest of reaching out consensus among the States and across the major political parties holding divergent views, compromising approach became imperative. Be that as it may, we consider that the GST reform has been the most formidable achievement of the NDA government and it also establishes, as very rightly commented upon by the Chief Economic Advisor, GOI, Dr. Arvind Subramanian “a really daring experiment in governance of cooperative federalism”.

There is now a legitimate growing curiosity about the likely beneficial impact of this widely perceived ‘game changing’ GST policy reform. As amply emphasized before, these are early times to put across any conclusive assessment of the economic impact of GST. However, it may be relevant to unveil briefly what the NACAER study had observed ***way back in December 2009.*** By using various macro-economic parameters like international trade, prices, capital, employment, etc., it came to the conclusion that the GST would ***“provide gains to India’s GDP somewhere within a range of 0.9 to 1.7 per cent”.*** Surely, much water has flown since then, and growth profile and structure of the Indian economy as well as the domestic indirect tax system have witnessed significant changes over the last about eight years. There is apparently no new quantitative assessment undertaken since then on the likely impact of GST on macro and sectoral growth or any other major economic parameters.

But the study recently [March 2017] prepared by ***two economists working for the US Fed Reserve System*** makes an interesting reading. After taking a comprehensive look at the current tax system [i.e. all domestic indirect taxation] and relating it to the proposed new GST system and formulating an analytical model, the authors have come to the conclusion that "*the GST is expected to raise overall Indian welfare and is projected to be an inclusive policy in that it would be welfare improving for all Indian states. Furthermore, the model suggests that* ***the GST would lead to real GDP gains of 4.2 percent under the baseline assumptions, driven by a surge in manufacturing output".*** As is to be expected the study also refers to a few caveats in its analysis such as the fact that theirs is a static model and hence, the impact of GST should be interpreted as a long-run effect. Also, is the fact that the model is unable to address services trade; the impact on tax revenues is also not evaluated; and so on.

Hence, both these studies need to be looked as indicative of shape of things to come. In our analysis, we have highlighted five key parameters through which the economic impact of GST would be visible. We must also stress that segregating the GST economic impact from other simultaneous economic policy measures [for example, demonetization, increased digitalization of the economy, ongoing rigorous efforts of the RBI/ MOF to resolve the festering twin balance sheet problems – of banks and corporate borrowers, etc.] is surely going to be a daunting task.

We, therefore, expect that the MOF would now initiate a full-fledged assessment on the economic impact of GST – both at the micro and macro level – through various economic and policy research institutions and think tanks like the NITI Aayog, NCAER, and several others. Such independent, dispassionate and comprehensive analysis and assessments from divergent institutions is vital to guide more rational recalibration of the current GST framework, going forward…

Appendix

Table 1: The GST Rate Structure – Goods Classification

GST Rate (%)	% of Items Covered	***Illustrative Selected Specific Goods***
0 – Exempt	7	Essential consumer goods like foodgrains, milk, eggs, curd, buter milk, fresh vegetables, coconuts, atta, bread, vegetable oil, common salt, fish, live poultry, meat animals, firewood and fuel wood, postal items, printed books, newspapers, etc. Intermediate goods like raw silk, silk wastes, wool, khadi yarn, handloom, manually operated or animal driven agri equipments, etc. Unbranded chena, panner, natural honey, pooja samugri, etc.
5	14	Mostly consumer goods like sugar, tea, coffee, edible oils, milk powder, milk food, PDS kerosene, LPG, fish products, cashew nuts, dried rapes & resins, spices, etc. and branded products like cereals, chena, paneer, honey, etc. Industrial intermediates like oil cakes, tobacco leaves, sulphur, natural graphite, newsprint, etc.

12	17	A large segment of consumer goods like butter, ghee, cheese, cashew, almonds, fruit juices, jams and jellies, sausages, meat and meat products, dry fruits, etc. Industrial goods like marbles and granite blocks; wood and wood products; paper and paper boards ; certain pharmaceutical products; textile yarn ; etc.
18	43	Capital goods like machinery, instruments and appratus; Consumer goods like hair oil, soap, toothpaste, pasta, corn flakes, jams, soups, ice-cream, footware, etc.; Intermediate goods like chemicals, steel, optical fibres, synthetic yarns and man-mde fibres, etc.
28 Luxury Goods	19	Consumer durables like refrigerators and airconditioners; lamps & lighting fittings; watches and clocks; cement; custard powder; shampoo; perfume; aerated drinks; cigarrete lighters, smoking pipes; motor cycles, etc. Luxury Cars 28% + 15% cess Small Petrol Cars 28% + 1% cess Small Diesel Cars 28% + 3% cess

Table 2: The GST Rate Structure – Services Classification		
Illustrative List	**Existing Rate (%)**	**GST Rate (%)**
Government services [by Central, States and Local Authrities, with certain exceptions like those provided by postal dept, those in relation to aircraft or vessel at airports and ports, transport of goods and passengers, etc]; services provided by the RBI and core service provided by the banks, life insurance businesses, Employees' State Insurance Corporation, etc; health care; education; travelling in metro, local train, religious travel; services for conduct of any religious ceremony; transport services provided for transport of agricultural produce, milk, organic manure, defence equipments, etc.	0 – Exempt	0 – Exempt
Transport of passengers in rail in first class or airconditioned coach, by air in economy class, etc. Transport of goods by rail or in vessel, services of goods transport agency; supply of tour operator services, etc. Services by way of job work for [a] printing of newpapers, [b] printing of books; [c] textile yarns; [d] cut and polished diamonds, etc. Selling space for advertisement in newspapers, etc.	Some of these were exempt earlier or levied at 6%	5

Non-AC restaurants; transport of passengers by air other than economy class; transport of goods by containers in rail by any person other than by Indian Railways; construction of complex, building, civil structure, etc;	Some of these may have attracted 15% or lower	12
Supply of food/ drinks in restaurants having license to serve liquor or AC resturants; services by way of admission to circus, theatrical performance, drama, etc; composite supply of works contract; telecom; financial, etc.	15	18
Five star hotels & restaurants; admission to entertainment events including cinematogrpah films, amusement parks, theme park, etc.; services provided by the race club; gambling, etc.	15 + luxury tax varying in various states	28

“People must come to accept private enterprise not as a necessary evil, but as an affirmative good”.

- Eugene Black
Former President,
World Bank

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