Chapter No. - VI

Finding, Conclusions & Suggestions

This Research suggests that GST Model for the country that could be adopted in short term and identifies issues that arise in designing and implementation of comprehensive GST in India.

A) Design of a GST model involves three key components:

- Determination of the system – origin based, destination based, single point, multi point and so on

- Identification of activities and/or goods and services to be covered under each system

- Determination of level of government imposing and collecting GST.

There is a fair degree of consensus in India so far as system is concerned; we have adopted and are moving towards consolidation of goods and services tax under destination based multi point system of taxation. Also, there is fair degree of consensus so far as coverage of activities and goods and services are concerned; we will, like most other countries, continue to have customs duty which would not be rebatable and rest of the principal taxes i.e. CENVAT, State VAT and Service Taxes would form part of proposed GST.

B) Few other issues remain to be addressed like whether stamp duty should also become part of GST, which are other taxes being levied by each of the states and to determine whether they
should become part of GST or remain out of it. Stamp duty, being more in the nature of tax on property, rather than on transaction, ought to remain outside GST as is the position in other countries. However, to the extent, stamp duties are imposed on agreements involving sale of goods and/or provision of services (e.g. agreement for works contract in the State of Maharashtra), the same ought to be removed. Similar other issue relates to octroi duty which is currently levied by various municipalities and, in some cases, by states on entry of goods in the local area for use, consumption or sale therein. This also ought to be merged with GST and a mechanism to transfer resources to local authorities from out of the total revenues of the states needs to be worked out.

C) This Concept Paper thus addresses the third key component on which consensus building is in progress. This component of the design is relevant for a country having federal structure of governance (e.g. Canada, Brazil or, for that matter, even European Union).

There are three alternatives in this context:

(i) GST at Union Government Level only (Alternative I)
(ii) GST at State Government Level only (Alternative II)
(iii) GST at both, Union and State Government Levels (Alternative III)
A) Alternative I: GST at Union Level Only

This Model envisages principal indirect taxes on goods and services to be levied by Union Government only. No such taxes to be levied by State Governments leading to only one GST throughout the country.

- Ideal structure from business perspective – greater stability and facilitation of decision making – also, businesses will have to deal with only one tax authority and comply with only one tax- there will be significant reduction of compliance costs

- Excellent from consumer perspective as the consumer will know exactly how much is the indirect tax burden in the goods and service consumed by it

- Cascading effect can be removed to a large extent as there will not be taxes at two levels leading to improved competitiveness

- Feel good factor for any one doing business with the country Cons

- Near impossibility of achieving the structure – will require modification of Constitution
o States may not agree to give up power of taxation and depend on the Union for resources

o Entire infrastructure developed for taxation at both levels will have to undergo huge change

B) Alternative II : GST at State Level Only

This Model envisages levy of GST by State Governments only meaning only State specific GST across the country and no GST by Union Government.

o Reduction of cascading effect of taxes as there will not be tax at two levels.

o Amendment(s) will be required in Constitution which may be supported by industrial and large states and opposed by smaller states which do not have significant source of revenues

o Businesses will have to comply with tax laws of each State – not worse off than current situation but not better off as well except that they will not have to deal with Central Level taxation which is the current position. At the same time, decision making will be impacted and may affect business stability
Governments, both local and Union will not find it workable as it will require complete change in its finances and allocation of resources - entire distribution of taxes will need to undergo changes - Centre can retain entire direct tax collection and States may retain indirect taxation collection. But, that too will not be workable as revenue collection by each state will vary depending on the level of activities in each state and need for support to states – redistribution of taxes will become an issue.

There may be unhealthy competition among states using local tax structure as a tool to attract investments within the states, which may be at the cost of other states. This could lead to retaliatory measures by other states.

Entire infrastructure for taxation will have to undergo change as States will need additional resources whereas Union’s infrastructure will be freed up.

C) Alternative III: GST at both levels

This model envisages GST at two levels operating parallelly – one, at Union Level and another at State Level.

Achievable in the short term
- No significant change required in the current structure of indirect taxation although, some amendments may be required to the Constitution

- Partial removal of cascading effect of taxes

- No change required in infrastructure of tax departments at the Union and State levels Cons

- Not ideal model – tax would continue to be at two levels and compliance costs may not reduce significantly

- Constitutional amendments may be required – principal one being extension of CENVAT to the consumer level and granting authority to states to impose taxes on services

- Uncertainty of states changing laws, rates of taxation and like will continue affecting business sentiments

- Taxation of services at state level especially services provided nation wide (e.g. telecommunication service, transportation service) will pose challenge.
Suggested GST Model For INDIA

The Research Paper suggest that Alternative III - GST at two levels – Union and State operating parallely be adopted to begin with this reform process. Although, it is not ideal Model, we recommend the same to – kick start the move to GST as:

- It is the most workable model especially taking into consideration the changes required in the Constitution and achievability in the short term.

- This Model builds on the current structure of taxation of goods and services and does not envisage drastic changes in the broad mechanism for levy and collection of taxes.

- It results in allocation of taxes between Union and States and between states based on fair and transparent criteria of consumption within a state.

Implementation Imperatives:

This implementation of this suggested Model will require following steps:

- Constitutional Amendments : Consolidate separate entries in the Constitution empowering Union and State Governments to impose taxes on manufacture and sale of goods and services into one entry which empowers both Union and State
Governments to impose tax on sale and supply of goods and services. Alternatively, modify Constitution only to the extent required immediately specifically, to extend CENVAT to consumer level and to authorize states to collect and retain tax on services.

- Amend CST law to introduce VAT on import of goods and introduce import VAT—tax on imports is within the jurisdiction of Union Government and Union Government could appropriate it to the State Governments. This collection would need to be allocated to the states where the goods move on importation since that is the state where the sale will take place and which will give credit for import VAT against output VAT.

- Consolidate taxes on services imposed under different enactments by State Governments e.g., duty on entertainment, and electricity, luxury tax.

- Consolidate taxes on goods and services at each Union Level and State Level

This will require many steps, significant ones being: - bringing into effect provision empowering State Governments to collect and retain Service Tax; determination of services which could be taxed at both levels and those which could be taxed only by Union Government. Ideally, all services ought to be taxed at both levels as services are used by businesses for making sales or providing services which could be taxable at either or both levels and non availability of input tax credit could lead to cascading. At the same time, considering difficulties of developing
structure or taxation of services which are nationwide such that there is no double taxation or no
taxation is extremely tough task and, therefore, to begin with, some services like
telecommunication, transportation, banking and financial services could be retained at the Union
level - enacting comprehensive GST law (Standard draft could be used at both levels)
consolidating CENVAT and Service Tax at Union Level and State VAT and taxes on various
services at the state level - determination of tax system for sales and services involving inter-
state movements. A Concept Paper on these issues is under development at Fiscal Law
Committee. - Determination of GST rate at Union and State Levels – Current standard rate of 16
% adopted for CENVAT can be lowered and possibly brought down with extension of CENVAT
to consumer level due to additional revenue to be generated from subsequent value addition
which is currently not captured although, some part of it is already captured under Service Tax.
Similarly, the standard rate of State VAT of 12.5 % could be reduced as additional resources will
be generated from taxation of services. - Developing standard system of classification to be
adopted by both Union and States - the current system adopted for Customs and CENVAT may
be adopted by the States with separate list of items of local nature which may not find place in
Customs or CENVAT classification list.

Concluding Remarks:

The foregoing analysis shows that there has been a significant progress in tax reforms in recent
years and that has helped to enhance the tax-GDP ratio close to the levels that prevailed prior to
reducing customs. This, however, is only the beginning and considerable distance in reforming
the tax system is yet to be covered. The tax system reform including reform in administration is
a continuous exercise. The reforms will have to continue not only at the centre, but also at state
and local levels as well. One important objective of sub national reform is to ensure common market in the federation. It is also necessary that consumption taxes should be calibrated in a co-coordinated manner in the spirit of co-operative federalism. Domestic and external trade taxes should also be calibrated to ensure the desired degree of protection to industry and the desired burden of consumption taxes to the community. Broadening the base of both central and state taxes and keeping the tax structures simple are important international lessons to be adopted in calibrating further reforms.