3.1 ORIGIN
3.2 BACKGROUND
3.3 AN INTEGRATED REGIME – BIRTH OF AN IDEA
3.4 SIGNIFICANCE OF GST
3.5 IMPACT OF GST
3.6 GST – THE ROAD MAP AND THE CHALLENGES
3.7 CONSTITUTIONAL AMENDMENT ON TAXATION POWER
3.8 GST AND ITS OPERATIONS
3.9 GST MODELS
3.10 GST – ALTERNATIVE MODELS AND ISSUES
3.11 OVERVIEW OF THE DISCUSSION PAPER ON GST
3.12 CHRONOLOGY FOR IMPLEMENTATION OF GST
3.13 OPERATIONAL DEFINITION OF GST
3.14 PROPOSED FEATURES IN INDIAN CONTEXT
3.15 DESIRABLE FEATURES OF GSTN–AN IT INFRASTRUCTURE FOR GST
3.16 STAKEHOLDERS
3.17 WORKFLOWS
3.18 A COMMON GST PORTAL
3.19 GLOBAL EXPERIENCES IN GOODS AND SERVICES TAX
3.20 STRIKING BALANCE
3.21 MISSION MODE PROJECT ON COMMERCIAL TAXES
GST is a comprehensive value added tax on goods and services. It is collected on value added at each stage of sale and purchase in the supply chain without State boundaries. “The success of GST depends on proper administration. Much will depend on its simplicity and efficient implementation, which are even more difficult in a disparate federal setup”.¹

3.1 ORIGIN

Goods and Services Tax also known as the Value Added Tax (VAT) or Harmonized Sales Tax (HST) was first devised by a German economist during the 18th century. He envisioned a sales tax on goods that did not affect the cost of manufacture or distribution but was collected on the final price charged to the consumer. The numbers of transactions are immaterial and the tax is at a fixed percentage of the final price. The tax was finally adopted by France in 1954. Maurice Lauré, Joint Director of the French Tax Authority, the Direction générale des impôts, was the first to introduce VAT on April 10, 1954. Initially directed at large businesses, it was extended over time to include all business sectors.

3.2 BACKGROUND

The Indian indirect tax regime is characterized by multiple levies, such as excise duty, Customs duty, VAT, Central sales tax, service tax, and including local levies, such as octroi and entry tax. Historically, none of these taxes were creditable against one another, barring a part of the Customs duty and excise; over the last few years, service tax has also been brought into the creditable basket. The excise duties, Customs duties and service tax belong to one basket of creditable taxes, VAT, Central sales tax and octroi belong to another basket of entirely non-creditable taxes.

¹ Sukumar Mukhopadhyay -Former Member, Central Board of Excise & Customs,” Business Environment, Chartered Financial Analysts, April 2008, P.16
The Central Government to levy certain taxes, and the State Government to levy certain other taxes—this distribution of power was clear and unequivocal. As a result, over the last six decades, both the Central and the State Governments have steadfastly worked at refining and expanding their respective tax regimes, but as the saying goes, the twain never met. In fact, until the introduction of VAT recently, even a single regime such as sales tax often entailed multiple levies, since sales tax levied across different States was largely non-creditable.

3.3 AN INTEGRATED REGIME – BIRTH OF AN IDEA

By the turn of the century, it was largely recognized that the existing regime of multiple (and largely non-creditable taxes) needed to go. Hence, the Central and State Governments worked at arriving by evolving a new regime; while there were considerable hiccups in the process, States eventually agreed to a gradual overhaul of the indirect tax regime in two significant phases:

- The first being the replacement of the erstwhile sales tax regime with a relatively more uniform VAT regime across many States coupled with the gradual elimination of the Central Sales Tax, and
- The second being the eventual merger of all of these into an integrated system of Goods and Services Tax (GST) by 2012. The proposed goods and services tax (GST) is in fact the brainchild of Ex-Finance Minister Mr. P. Chidambaram. It is be a multi-stage consumption tax to be imposed on wide range of goods and services. The process of introduction of VAT started in 2003 but was completed recently. The rate of Central sales tax has been reduced from 4% to (proposed) 2%, and is expected to be fully removed by the time GST is introduced.

3.4 SIGNIFICANCE OF GST

- Introduction of GST would result in abolition of multiple types of taxes on goods and services.  
- Reduces effective rates of tax to one or two floor rates.
- Reduces compliance cost and increases voluntary compliance.
- Removes cascading effect of taxation and removes distortion in the economy.

---

• Enhances manufacturing and distribution efficiency, reduces cost of production of goods and services, increases demand and production of goods and services.

• As it is neutral to business processes, business models, organization structure, geographic location and product substitutes, it will promote economic efficiency and sustainable long-term economic growth.

• Will give competitive edge in international market for goods and services produced in India, leading to increased exports.

• Reduces litigation, harassment and corruption.

• Will result in widening tax base and increased revenue to the Centre and State.

• Reduces administrative cost for the Government.

3.5 IMPACT OF GST

The most significant impact of the introduction of GST will be the removal of the cascading effect of the various taxes, since in an ideal GST scenario; all indirect taxes will be creditable against one another. The overall impact of taxes on businesses is reduced. Besides, the artificial (tax) barriers to trade that currently exist should be fully removed. All of these, coupled with the relative clarity that a GST regime offers, should result in the reduction or rationalization of prices. Another equally significant offshoot of this regime is streamlining of the administration and collection of the indirect levies, since GST will attempt to tax the value added at each stage of the supply chain. The government revenue is not boosted but brings to book many of the defaulters, and hence results in the creation of a robust tax regime.

3.5.1 Impact on purchase of goods under GST

In the current scenario, purchase of goods ordinarily is subject to VAT/ CST and in case the goods are purchased from a manufacturer, the purchase is also subject to excise duty. In the GST regime, interstate purchases would be subject to IGST and local purchases would be subject to CGST and SGST. The Exhibit: 3.1 illustrate the impact of GST.
Exhibit: 3.1

Impact on purchase of goods under GST


Note: The corollary to the above would be the impact on sales.
3.5.2 Impact on procurement of services under GST

In the current scenario, procurement of taxable services would be subject to service tax. Considering that service tax is levied by the Central Government, the tax would be the same, whether procured locally or interstate. In the GST regime, services procured from outside the State would be subject to IGST and services procured from within the State, would be subject to CGST and SGST. The below Exhibit: 3.2 illustrate the impact.

Exhibit: 3.2

Impact on procurement of services under GST


Note: The corollary to the above would be the impact on rendering of services.
3.6 GST – THE ROAD MAP AND THE CHALLENGES

The concept of the desirable and aspiration form of GST for India has been, and remains, evolving. Initially, GST was intended as a fully-integrated system encompassing within itself all of the existing indirect taxes. Clearly, this is no mean task and apart from the political and economic will, it also requires some significant changes in the Constitutional distribution of power.

3.7 CONSTITUTIONAL AMENDMENT ON TAXATION POWER\(^3\).

The constitutional amendment on taxation powers are given below in the following Exhibit 3.3.

**Exhibit: 3.3**

**Constitutional Amendments in Taxation Powers**


An indicator of the magnitude of the task is the recent sound bytes that have been (reportedly) attributed to the specially constituted Joint Working Group and the larger Empowered Committee of State Finance Ministers, which is tasked with the
responsibility of looking into and ensuring the implementation of GST. The Working Group has submitted its findings to the Committee. While Group’s findings, the likely form of GST that India will adopt is that of dual GST: a Central tax and separate State level taxes.4

3.8 GST AND ITS OPERATIONS

In GST regime, goods and services are not differentiated as it moves through the supply chain. The fundamental feature of GST is the eligibility of the manufacturers and dealers to claim credit for ‘input tax’ paid at each stage without any limit or the barriers of State boundaries till it reaches the ultimate consumer. In GST structure, different stages of production and distribution are interpreted as a mere tax pass-through, and the incidence of tax is essentially borne by the final consumer within a taxing jurisdiction. A well-designed GST on all goods and services is the most efficient method of taxation to eliminate distortions. In the Indian context, if GST is implemented in real form, it would integrate all taxes currently levied in India by Central and State governments on goods and services like excise duty, service tax, State VAT/sales tax, entry tax or octroi, State excise, countervailing Custom duty, telecom license fee, luxury tax, tax on consumption/sale of electricity, entertainment tax etc.

3.8.1 Global scenario and GST

More than 150 countries have introduced GST/National VAT in some form. It has been a part of the tax system in Europe for the past 50 years and is the preferred form of the indirect tax in the Asia-Pacific region. There are different models of GST currently in force, each with its own peculiarities. While country such as Singapore virtually taxes everything at a single rate, some countries have more than one rate (a zero rate, certain exemptions and higher and lower rates). In some countries it is recoverable only on goods used in the production process and specified service. The standard GST rates in most of the countries ranges between 15-20% which is shown in the Table: 3.1. In Scandinavian countries (north Europe) where social security coverage is higher, it ranges between 22-25 percent.

4 Sukumar Mukhopadhyay - Former Member, Central Board of Excise & Customs,” Business Environment, Chartered Financial Analysts, April 2008, P.18
Table: 3.1

Global GST rates

<table>
<thead>
<tr>
<th>Country</th>
<th>Standard Rate</th>
<th>Country</th>
<th>Standard Rate</th>
<th>Country</th>
<th>Standard Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>20</td>
<td>Greece</td>
<td>18</td>
<td>Norway</td>
<td>25</td>
</tr>
<tr>
<td>Belgium</td>
<td>21</td>
<td>Argentina</td>
<td>21</td>
<td>Denmark</td>
<td>25</td>
</tr>
<tr>
<td>Portugal</td>
<td>19</td>
<td>Chile</td>
<td>19</td>
<td>Sweden</td>
<td>25</td>
</tr>
<tr>
<td>Ireland</td>
<td>21</td>
<td>Spain</td>
<td>16</td>
<td>Finland</td>
<td>22</td>
</tr>
<tr>
<td>Poland</td>
<td>22</td>
<td>Romania</td>
<td>19</td>
<td>Italy</td>
<td>20</td>
</tr>
<tr>
<td>France</td>
<td>19.6</td>
<td>Luxembourg</td>
<td>15</td>
<td>Switzerland</td>
<td>7.6</td>
</tr>
<tr>
<td>Germany</td>
<td>16</td>
<td>Netherlands</td>
<td>19</td>
<td>U.K</td>
<td>17.5</td>
</tr>
<tr>
<td>Australia</td>
<td>10</td>
<td>Columbia</td>
<td>16</td>
<td>Maldives</td>
<td>20</td>
</tr>
<tr>
<td>Barbados</td>
<td>15</td>
<td>Japan</td>
<td>5</td>
<td>Indonesia</td>
<td>10</td>
</tr>
<tr>
<td>Canada</td>
<td>7</td>
<td>Mexico</td>
<td>15</td>
<td>China</td>
<td>16</td>
</tr>
<tr>
<td>Botswana</td>
<td>10</td>
<td>Latvia</td>
<td>18</td>
<td>South Africa</td>
<td>14</td>
</tr>
<tr>
<td>Zambia</td>
<td>17.5</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: http://en.wikipedia.org/wiki/Tax_rates_around_the_world

In India, the standard rate of excise duty is 16% on manufacture’s sale price. In addition there is a State VAT at 4% and 12.5, at a lower end with 4% VAT it works out to 13.5%. It is feasible to fix tax neutral GST rate of 20% (less if existing duty exemptions are reduced) covering both Central and State’s revenue share.5 “They (European countries) have kept the standard rate at 15 per cent and there is a band which ranges between 15 per cent and 25 per cent. So, there is flexibility, which we were also demanding. Also, there is a reduced rate of five per cent. They also have exemption thresholds”.6

---

6 Business Standard Tuesday, Sep 27, 2011 Pg 6
Exhibit: 3.4

Global GST rates

Source: http://en.wikipedia.org/wiki/Tax_rates_around_the_world
3.9 GST MODELS

The proposed GST regime is a great milestone in the legislative history of indirect taxation and is a foundation of a new era in the indirect tax administration of the country. The States have not given its consent on the proposed structure. As the basic intricacies of the unified tax are still not finalized it is imperative to examine the various GST models. The indirect tax models can be derived on the basis of point of levy, number of levies, and the credit mechanism. In other words, the variety of models for taxation of goods and services can be derived from a combination of:

- Origin based single point levy- The present excise duty structure is an instance of origin based levy and the duty is levied at the time of manufacture.
- Destination based single point levy- Retail sales tax is a comparable instance.
- Destination based multi point levy with input tax credit mechanism- GST which is prevalent in various countries and is proposed to be implemented in India.

3.10 GST– ALTERNATIVE MODELS AND ISSUES

3.10.1 Design of a GST model involves three key components

- Determination of the system – origin based, destination based, and 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 tax as system is concerned. There is fair degree of consensus on coverage of activities and goods and services. India will 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.
- Few other issues remain to be addressed like a) whether stamp duty should also become part of GST? b) Which is other taxes being levied by each of the States and c) 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 agreements involving sale of goods and/or provision of services. The 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 should 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.

- The third key component is consensus building. 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:
  - GST at Union Government Level only (Alternative I)
  - GST at State Government Level only (Alternative II)
  - GST at both, Union and State Government Levels (Alternative III)
- Canada has GST at Union Level extending to all goods and services covering all stages of value addition. In addition, there is tax at province (State) level in different forms which include VAT, Retail Sales tax and so on. European Union (EU) nations (each one is independent nation but, part of a Union and have agreed to adopt common principles for taxation of goods and services) have adopted “classic” VAT.
- In Indian context, an additional dimension is added by the provisions of Constitution which specifically reserve power to impose tax on specific activities to specific level of government.

### 3.10.2 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.

- **The merits are** a) Ideal structure from business perspective – greater stability and facilitation of decision making; b) businesses will have to deal with only one tax authority and comply with only one tax – there will be significant reduction of compliance costs; c) Excellent from consumer prospective as the consumer will know exactly how much is indirect-tax burden in the goods and service consumed by it; d) Cascading effect can be removed to a large extent as there will not be taxes at two levels leading to improved competitiveness; e)
Feel good factor for any one doing business with the country.

- **The Constraints are** a) Near impossibility of achieving the structure– will require modification of Constitution; b) States may not agree to give up power of taxation and depend on the Union for resources; c) Entire infrastructure developed for taxation at both levels will have to undergo huge change.

### 3.10.3 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.

- **The positive factor is** Reduction of cascading effect of taxes as there will not be tax at two levels.

- **The limitations are** a) 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; b) Businesses will have to comply with tax laws of each State – not worse off that 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; c) Decision making will be impacted and may affect business stability; d) 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; e) Centre can retain entire direct tax collection and States may retain indirect taxation collection; f) 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; g) Entire infrastructure for taxation will have to undergo change as States will need additional resources whereas Union’s infrastructure will be freed up.
3.10.4 Alternative III – GST at both levels

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

- **The relative significance** a) This model is achievable in the short term; b) No significant change required in the current structure of indirect taxation although, some amendments may be required to the Constitution; c) It removes the cascading effect of taxes to some extent; d) No change required in infrastructure of tax departments at the Union and State levels

- **The shortcomings are** a) Not ideal model – tax would continue to be at two levels and compliance costs may not reduce significantly; b) 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.

**Proposed GST Model** The existing multiplicity of taxes under present regime will undergo total change with the introduction of Goods and Services Tax (GST) with effect from April 2012. Goods and Service Tax is a destination based tax or a consumption based tax which can be termed as a consumption tax collected on the value-addition made in the goods and services at each stage of the supply chain. The seller of such goods or provider of services can take input credit of the tax paid. Unlike the existing tax regime, cross utilization of credit is possible under GST which would help to lower the taxes on production. The cost to the ultimate consumer will also be lowered. GST is intended to lower the tax structure, boost the trade and industry, cost of compliance and lessen litigation. GST would subsume all the indirect taxes as above except Customs duty and Octroi. Though no official information is available on the details of the GST implementation, India is likely going to have a dual GST with rate pegged between 16% and 20%. There are quite a few challenges that will haunt the trade and industry during the GST implementation which are procedural – (1) Transition method (2) Unfulfilled obligations under FTP scheme (3) Pending litigations (4) Refunds (5) Import transactions (6) Dispute Resolution (7) Assessment and scrutiny (8) Preparedness of the authorities, etc. Under GST, exemptions will be minimal and there will be no Zero tax rate. Services being taxed at
10% will be costlier under GST. GST models relevant to the Indian context are listed below:

- Concurrent Dual GST
- Non-concurrent Dual GST
- National GST
- State GST.

The above mentioned models and the key aspects of each of them are summarized in the Table: 3.2 below:

**Table: 3.2**

**GST Models**

<table>
<thead>
<tr>
<th>Key Aspect</th>
<th>Concurrent Dual GST</th>
<th>Non-concurrent Dual GST</th>
<th>National GST</th>
<th>State GST</th>
</tr>
</thead>
<tbody>
<tr>
<td>Requirement for Constitutional amendment in Indian context</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Revenue Sharing</td>
<td>No</td>
<td>The Centre may partly or fully transfer the revenues collected from the taxation of services</td>
<td>Yes</td>
<td>Reduction in fiscal transfers from Centre to State</td>
</tr>
<tr>
<td>Example</td>
<td>Canada and Brazil</td>
<td>Similar to present Indian indirect tax structure in many ways but of course not identical</td>
<td>Australia</td>
<td>USA</td>
</tr>
</tbody>
</table>

*Source: Institute of Cost Accountants of India, Concept Paper, GST Model for India-Suggestions, 2009*
3.10.5 Concurrent Dual GST

This model in common parlance is generally referred to as a dual GST model’. Under this model, there is a Central GST (CGST) and a State GST (SGST) and each of the tax is levied on a comprehensive base comprising both goods and services. In other words, supply of goods and services attracts both CGST and SGST. It is pertinent to mention that both CGST and SGST can be merged into a single national GST (Model 3) with an appropriate sharing of revenues between the Centre and the States. The federal structure of the Indian Constitution, is concerned dual GST is a political necessity. Under the Dual GST model, the tax is levied concurrently by both the Centre and the States. Not only the Central Government but also the Empowered Committee has shown positive signals in favour of the Dual GST model.7

3.11 OVERVIEW OF THE DISCUSSION PAPER ON GST

The key features of the proposed GST as laid down in the discussion paper provide a very interesting and useful first reference for any discussion of GST in India. As a beginning, the design proposed in the paper provides considerable detail and structure to the new regime. The key features are summarized as follows:

- **Dual GST:** A Central and a State GST to be applied on the same base. Each tax would operate on the principles of input tax credit, where tax credit for each tax would be self-contained. No cross-credit would be allowed except in the case of interstate transactions. For interstate transactions, the discussion paper proposes a regime called IGST, wherein the exporter charges IGST in place of the GST in such transactions; claims input tax credit for any taxes paid, and remits the balance to the Central government. The exporting State remits any local taxes that are claimed as credit by the exporter to the Central government/Central administrator. In the importing State, the importing dealer is allowed to claim tax credit for the IGST paid from the Central government. The claims across States will be cleared by a Central clearing house kind of mechanism. It is proposed to cover both B-B and B-C transactions.

---

• **Uniform State GST threshold is desirable – proposed at Rs. 10 lakh:** Threshold for Central GST for goods could be kept at Rs. 1.5 Crore and for Central GST on services may also be appropriately high. For composition scheme - upper limit of Rs. 50 lakh and a floor rate of 0.5% across the States, with option for GST registration if desired.

• **Rate Structure:** Apart from exemptions for all commodities presently exempt in the State VAT system, it is proposed to have two rates – a lower rate for “necessary items and goods of basic importance” and a standard rate. It is suggested that a similar approach be adopted by the centre for taxation of goods. For services, however, a single rate is proposed. It is also proposed that all exports out of the country will be zero-rated and all imports into the country would be subject to GST, with credit being made available in subsequent transactions.

- Central and State taxes to be subsumed in GST include Central excise, additional excise duties, service tax, additional Customs duty, special additional duty of Customs, surcharges and cesses, for the centre and State VAT, entertainment tax, luxury tax, betting taxes, State cesses and surcharges on supply of goods and entry tax not in lieu of octroi.
  - On purchase tax there is no clear view.
  - On tobacco, alcohol and petroleum products, it is proposed that status quo remains. In other words, alcoholic products and tobacco would be subject to GST, with traditional excises imposed by States on the former and centre on the latter in the case of petroleum products, it is proposed that crude, motor spirits, diesel and ATF would be kept outside GST.

• **Multiple Statutes:** One for the centre and one each for the States. The discussion paper proposes that the “basic features of law such as chargeability, definition of taxable event and taxable person, measure of levy including valuation provisions, basis of classification, etc, would be uniform across these statutes as far as practicable”.\(^8\) Rules for taking and utilization of credit for the Central GST and the State GST would be aligned. To the extent

---

\(^8\) R Kavitha Rao, Pinaki Chakraborty, Goods and service tax in India: An assessment of the base”, January 2,2010 VOL XLV NO1 Economic and political weekly, p.no 50.
feasible, uniform procedure for collection of both Central GST and State GST would be prescribed in the respective legislation: while separate returns are mandates for the two taxes, it is proposed to aim for a common format.

- **Tax administration by respective tax departments**: Timely refund, when credit accumulation takes place – by designing interconnectivity between different tax departments. For sharing of information between the different tax departments, administrations including income tax a PAN-linked tax payer identification number are to be allotted.

The following are the points of distinction between the Empowered Committee of the State Finance Ministers and the Report of the Thirteenth Finance Commission Task Force on GST. However to introduce the GST successfully in India, the Centre and State Governments must reach a consensus on the structure of GST

- **RATE OF TAX**: According to the Empowered Committee, there should be multiple SGST rates for goods. Standard rate i.e. 7% - 8% and lower rate i.e. 4%-5%. Single rate for services (both for CGST and SGST. On the other hand, single rate of GST for all goods and services i.e. 5% for CGST and 7% for SGST is put forward by Thirteenth Finance Commission.

- **THRESHOLD LEVEL**: According to the Empowered Committee, multiple thresholds for SGST to be Rs 1 million and proposed threshold for CGST to be Rs 15 million. On the other hand, uniform threshold i.e. Rs 1 million for both CGST and SGST is put forward by Thirteenth Finance Commission.

- **TAXES TO BE SUBSUMED**: According to the Empowered Committee, subsume most of the transaction based levies but may exclude octroi, purchase tax on food grains, electricity cess, stamp duties. On the other hand, subsume purchase tax, stamp duty, electricity duty is put forward by Thirteenth Finance Commission.

- **ECONOMY COVERAGE**: According to the Empowered Committee, Alcoholic products and Petroleum Products to be kept out of GST. Tobacco products to be subject to GST with input tax credit. On the other hand, Alcohol, emission fuels and tobacco to be subject to dual levy of GST and excise without any credit of the excise component. Also comprehensive
taxation adopted for real estate and financial services is put forward by Thirteenth Finance Commission.

3.11.1 Implementation imperatives

The implementation of this suggested Model requires 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 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.

3.12 CHRONOLOGY FOR IMPLEMENTATION OF GST

The initial seeds of GST were sowed way back in 1994 in a report of the National Institute of Public Finance and Policy, led by late Dr. Amaresh Bagchi. While recommending a State VAT, the Bagchi committee report\(^9\) recognized that it was not a perfect solution but was feasible option within the framework of the Constitution and would lay the foundation for an even more rational regime in future, which is now envisaged as the GST. A snapshot on the run up to GST in April 2012 has shown in Exhibit 3.1.

\(^9\) Dr. Amaresh Bagchi, et al (1994)
3.12.1 Concurrent List

Systems of GST

Apart from the GST models, it is important to understand the systems of GST as well. The various prevalent systems of GST primarily revolve around issues pertaining to availment of credits and payment of taxes. The three systems\(^\text{10}\) prevalent internationally are depicted in the Exhibit 3.2 below:

---

\(^{10}\) V.S. Datey, “Service Tax & VAT”, Taxmann’s Publications, New Delhi, 2009, pg. 36-38
**Exhibit: 3.6**

**Systems of GST**

<table>
<thead>
<tr>
<th>Systems of GST</th>
</tr>
</thead>
<tbody>
<tr>
<td>Invoice System</td>
</tr>
<tr>
<td>Payment System</td>
</tr>
<tr>
<td>Hybrid System</td>
</tr>
</tbody>
</table>

**Invoice System**

The input credit can be availed on the basis of invoice when such an invoice is received. Similarly, the output tax needs to be discharged after the invoice is raised. The facts with respect to payments made for procurements and payments received on supplies are immaterial. This is similar to the existing provisions of VAT in India.

**Payment System**

Under the payment system of the GST, the input credit on supplies procured can be availed on the basis of payment. Even the output tax needs to be discharged after the payment is received for the supplies made to the customers. The facts with respect to invoices received for procurements and invoices raised for supplies made to customers have no significance. This system is similar to the existing provisions of Service Tax as per the provisions of the Finance Act, 1994.

**Hybrid System**

This system is the blend of invoice system and payment system. The input credit can be availed on the basis of invoice when such an invoice is received. However, the output tax needs to be discharged after the payment is received for the supplies made to the customers. This system is the most beneficial one from the aspect of the assessee as the credit can be taken immediately on receipt of an invoice but the tax needs to be discharged only after the payment for the supplies received.

GST is divided into three types. They are:

- **Central Goods, Service Tax(CGST):** All the taxes(Additional Excise, Counter Veiling Duty, cesses, Central Excise, Customs) that come under Central Government are included in this kind.
• **State Goods, Service Tax(SGST):** All the taxes which come under State government(VAT, Entertainment Tax, luxury tax, betting-gambling tax, octroi, entry tax, purchase tax, State tax, and lottery tax) are included in this type.

• **Special organization in Central level (IGST):** It was conducted by Central government & The taxes that are paid had IGST redemption. It distributes those taxes among the countries. The only thing is that the demands and plans of this IGST are in motion but not yet decided.

### 3.12.2 GST tax rates:

There will be five types of rates that will collect under this kind. They are as follows:

• **Standard tax rates:** Most of the taxes come under this category.

• **Limited tax rates:** Tax is been collected for the medical & other major basic goods in this category.

• **Special tax rates:** Special tax is been collected on the goods & items like tobacco, Liquor, jewellery etc; under this category.

• **Redemption rates:** This kind of tax is applicable to the backward areas & there is redemption of taxes for goods under this system & where GST & credit facility is not applicable. All these kinds of procedures will be banned if GST exists.

• **Zero rate:** Though tax is not applicable to the goods that are imported there is the facility of refund under this system.

### 3.12.3 Working of GST

**Table: 3.3**

<table>
<thead>
<tr>
<th>Systems of GST</th>
</tr>
</thead>
<tbody>
<tr>
<td>TAX PAYABLE</td>
</tr>
<tr>
<td>----------------</td>
</tr>
<tr>
<td>Intra-State sale</td>
</tr>
<tr>
<td>Interstate sale</td>
</tr>
</tbody>
</table>
## COMPUTATION OF TAX LIABILITY: PRESENT SCENARIO Vs. GST REGIME

### INTRA-STATE

<table>
<thead>
<tr>
<th></th>
<th>Present</th>
<th>GST</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Excise Duty(@ 8.24%)</td>
<td>8.24</td>
<td>Subsumed</td>
</tr>
<tr>
<td>VAT @ 12.5%</td>
<td>13.53</td>
<td>Subsumed</td>
</tr>
<tr>
<td>CGST @ 8%</td>
<td>8</td>
<td></td>
</tr>
<tr>
<td>SGST @ 8%</td>
<td>8</td>
<td></td>
</tr>
<tr>
<td><strong>Total Taxes</strong></td>
<td>21.77</td>
<td>16</td>
</tr>
</tbody>
</table>

### INTER – STATE

<table>
<thead>
<tr>
<th></th>
<th>Present</th>
<th>GST</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Excise Duty(@ 8.24%)</td>
<td>8.24</td>
<td>Subsumed</td>
</tr>
<tr>
<td>CST @ 2%</td>
<td>2.16</td>
<td>Subsumed</td>
</tr>
<tr>
<td>IGST @ 16%</td>
<td></td>
<td>16</td>
</tr>
<tr>
<td>CGST @ 8%</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>SGST @ 8%</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td><strong>Total Taxes</strong></td>
<td>10.4*</td>
<td>16</td>
</tr>
</tbody>
</table>

### VALUE OF GOODS

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>* CGST@8%</td>
<td>8</td>
</tr>
<tr>
<td>* SGST@8%</td>
<td>8</td>
</tr>
</tbody>
</table>


*However there may be other local taxes such as Entry tax & Octroi

*CSGT = Central GST/SGT = State GST/IGST = Integrated GST

### 3.13 OPERATIONAL DEFINITION OF GST

**GST council.** GST Council will make recommendations on all key matters pertaining to GST like taxation rates under both CGST and SGST, exemptions from GST etc. Union Finance Minister will chair the council with Finance Ministers from States as members. The Council members may also elect a Vice-Chairperson of the Council from the members. The Dispute Settlement Authority will be responsible for any
disputes amidst Union/States/members with respect to GST. The Authority would have one Chairperson and two members. The chairperson should be judge from Supreme Court or Chief Justice from a high court and appointed by President of India on the recommendation of Chief Justice of India. Two other members should be experts from field of law/economics/public affairs on the recommendation of GST Council. This has been done to balance the interests of the parties.

**Service tax.** Service tax is levied on specified services, referred to as taxable services, when rendered by a service provider. Service tax is presently taxed at 10%. Ordinarily, service tax is payable by the service provider, except in specified cases. As service provider, credit is allowed on excise duty and countervailing duty paid on inputs and capital goods and the service tax paid on input service. The credit is allowed as a set-off against the service tax payable on taxable services.

**Empowered Committee of State Finance Ministers** The first preliminary discussion on State-level VAT took place in a meeting of Chief Ministers convened by Dr. Manmohan Singh, the then Union Finance Minister in 1995. In this meeting, the basic issues on VAT were discussed in general terms and this was followed up by periodic interactions of State Finance Ministers. Thereafter, in a significant meeting of all the Chief Ministers, convened on November 16, 1999 by Shri Yashwant Sinha, the then Union Finance Minister, two important decisions, among others, were taken. First, before the introduction of State-level VAT, the unhealthy sales tax “rate war” among the States would have to end, and sales tax rates would need to be harmonised by implementing uniform floor rates of sales tax for different categories of commodities with effect from January 1, 2000. Secondly, on the basis of achievement of the first objective, steps would be taken by the States for introduction of State-level VAT after adequate preparation. For implementing these decisions, a Standing Committee of State Finance Ministers was formed which was then made an Empowered Committee of State Finance Ministers.

**Input tax credit** The proposed dual Goods and Service tax (GST) system would be designed in such a manner that the Central GST chain and the State GST chain would be independent of each other. This would imply that a dealer would not be able to use the input tax credit available under the Central GST chain in the State level GST chain. The Central GST chain is likely to integrate the existing excise duty and service taxes levied at the Central level. The State level GST chain is likely to
integrate the current State-level VAT, other local levies and services tax on certain specific services on which States may get the powers to levy service tax. There will be full input tax credit in the Central GST chain and also in the State level chain but there would be no usability of Central GST into the State-level GST chain. Input tax credit would be allowed only at one chain and no carry forward of the credit from one chain to the other would be allowed. The structure would only address the cascading effect only in the respective chain and not in the parallel one. Cross utilization of credit of CGST between goods and services would be allowed. Similarly, the facility of cross utilization of credit will be available in case of SGST.

**Threshold limit** A threshold of gross annual turnover of Rs.10 lakh both for goods and services for all the States and Union Territories will be adopted with adequate compensation for the States (particularly, the States in North-Eastern Region and Special Category States) where lower threshold had prevailed in the VAT regime. After taking into consideration the interest of small traders and small scale industries and to avoid dual control, it has been decided that the threshold for Central GST for goods will be Rs.1.5 Crore and the threshold for services should also be appropriately high.

**Selective Concessions/Exemptions** While a linear tax structure with few exemptions would be ideal, the GST structure is likely to continue with sector specific concessions and exemptions. It was observed by Dr. Shome (erstwhile advisor to the finance minister), ‘that shades of policy interventions is a fact of life and we have to weave such positive suggestions in the framework and that by 2010, we will have a structure that will overhaul all taxes into one, of course with some exemptions.’ No tax will be payable on goods and services which shall be declared as exempted supplies and for such supplies, the assessee will not be able to claim any input tax credit. However certain supplies may be classified as zero rated goods and services thereby making it eligible to input tax credit.

**Service Tax under GST** Service Tax is levied at 10.3% (inclusive of Education Cess) percent tax on more than 100 services. States do not levy or collect service taxes at present, but get a share from the Centre's collections. It is proposed that States will keep the entire collection from certain services from this year. States would also tax another set of proposed new services, collect and appropriate as part of compensation for Central sales tax phase-out in 2010. Since there would be issues on taxing cross
border services it is expected that the State GST would only include services that are essentially of "Local Nature". It has also been reported that Service tax rate under Central GST and State GST is likely to be uniform. Though State Service Tax proposed to be levied on new local services would add to the cost, an redeeming feature is that Input Tax Credit would be eligible on the State Service Tax and a host of other levies like Entry Tax, Electricity Tax, and Luxury Tax etc that would be integrated under State GST. Of course, the service should qualify as an eligible Input Service.

**Tax Base for Dual GST Levy** Though nothing has been explicitly said on the tax base for the State GST, it has been reported that the dual GST Structure would ensure that there is no double taxation and it would help trim the present cascading effect of tax to benefit industry and consumers. So there is a likelihood that the levy of Central GST and State GST would be on the same tax base as only this can help trim the present cascading effect of tax.

**Implications of GST on imports and exports** Imports would be subject to GST. Both CGST and SGST will be levied on import of goods and services into the country. The incidence of tax will follow the destination principle and the tax revenue in case of SGST will accrue to the State where the imported goods and services are consumed. Full and complete set-off will be available on the GST paid on import on goods and services. Exports, however, will be zero-rated, meaning exporters of goods and services need not pay GST on their exports. GST paid by them on the procurement of goods and services will be refunded subject to certain conditions, limitations and procedures.

**System of Zero rating** The system of zero rating ensures that the benefit of zero rating is availed only after satisfaction of the condition that the tax is paid in the importing State. The dealer in the importing State will capture the interstate procurements in the periodic return and pay the relevant tax on such procurements. In case the liability to pay tax is not discharged within the stipulated time, zero rating will be reversed and then the seller in the exporting State will be required to pay the tax. For the successful implementation of the system of zero rating with pre-payment, a reliable mechanism should be put in place to identify interstate transactions and thereby ensure that there is no evasion of taxes. Exports would be zero-rated. Similar benefits may be given to Special Economic Zones (SEZs). However, such benefits
will only be allowed to the processing zones of the SEZs. No benefit to the sales from an SEZ to Domestic Tariff Area (DTA) will be allowed.

**Taxation of certain goods:** Certain goods like alcoholic beverages, tobacco and petroleum are subject to higher rate of taxes as it attracts multiple taxes like excise duties, license fees, cess, interstate import and export fees etc. This is mainly done to discourage the consumption of such products. Alcoholic beverages would be kept out of the purview of GST. Sales Tax/VAT can be continued to be levied on alcoholic beverages as per the existing practice. In case it has been made Vatable by some States, there will be no objection to that. Excise Duty, which is presently being levied by the States will also not be affected.

Tobacco products will be subjected to GST with Input Tax Credit (ITC). Centre may also be allowed to levy excise duty on tobacco products over and above GST without ITC. Petroleum products, i.e. crude, motor spirit (including ATF) and HSD would be kept outside GST as is the prevailing practice in India. Sales Tax could continue to be levied by the States on these products with prevailing floor rate. Similarly, Centre could also continue its levies. Whether natural gas will be within the purview of GST or not has not yet been decided.

### 3.14 PROPOSED FEATURES IN INDIAN CONTEXT

#### 3.14.1 Taxes to be subsumed

The Dual GST which would be implemented in India will subsume many consumption taxes. The objective of this tax reform is to reduce complexity and remove the effect of tax cascading. By subsuming a large number of taxes and levies, there would be a larger pool of tax credits allowing a free flow of credit utilization at intra and inter State levels. Further, the objective is to subsume all of those taxes which are currently applicable on sale of goods or rendering of services levied by either federal or State Government. At the federal level, the CGST will primarily subsume the following taxes:

- Central excise duty
- Service tax

---

• Additional duties of Customs in lieu of excise (or popularly known as CVD)
• Special Additional Duty of Customs in lieu of Sales Tax/VAT -4%(SAD)

Further, at the State level, it is proposed that SGST will subsume the following:

• State Value Added Tax
• Entertainment tax
• Luxury tax
• Entry tax not in lieu of Octroi
• Lottery taxes
• Taxes on betting and gambling
• Electricity duty (as it is proposed to cover even electricity under GST)
• State surcharges relation to supply of goods and services.

3.14.2 Steps for Implementation of GST

In order to effect the proposed model of GST, the Government would be required to amend the Constitution to empower the State to levy tax on services and to empower the Centre to levy tax on goods. States are required to be empowered to levy tax on import. Besides Constitutional amendments, GST implementation would also require installation of requisite IT infrastructure both at the Central and State level.
Exhibit: 3.7

Indirect Taxes Past-Future

Central Excise Duty  State VAT/Sales tax

Additional Excise Duty  Entertainment Tax

Excise duty on Medicinal and Toiletries Preparations Act  Tax on lottery, betting and gambling

Countervailing Duty  CGST
Entry Tax not in lieu of Octroi  SGST

Special Additional Duty  Luxury Tax

Service Tax  State cesses and surcharges relating to supply of goods and services

Other Surcharges & Cess  Purchases tax

3.15 DESIRABLE FEATURES OF GSTN–AN IT INFRASTRUCTURE FOR GST

**Simplicity for taxpayers:** The process of filing of tax returns and payment of tax should be simple and uniform and should be independent of taxpayer’s location and size of business. In addition, the compliance process should not place any undue burden on the taxpayer and should be an integral part of his business process.

**Respect autonomy of States:** The design of the IT system should respect the constitutional autonomy of the States. Several business processes will be re-engineered as a new IT system for GST is put into place. There should be no dilution of the autonomy of States as a result of the IT system, or the re-engineering. On the contrary, it should strengthen the autonomy of States. This is a key factor in the design of the IT system presented in the rest of this document.

**Uniformity of policy administration:** The business processes surrounding GST need to be standardized. Uniformity of policy administration across States and centre will lead to a better taxpayer experience, and cut down costs of compliance as well as tax administration.

**Enable digitization and automation of the whole chain:** All the business processes surrounding GST should be automated to the extent possible, and all documents processed electronically. This will lead to faster processing and reconciliation of tax information and enable risk based scrutiny by tax authorities. For small taxpayers, facilitation centres can be set up to ease the migration.

**Reduce leakages:** A fully electronic GST can dramatically increase tax collections by reducing leakages. Tools such as matching the input tax credit, data mining and pattern detection will detect tax evasion and thus increase collections.

**Leverage existing investments:** Existing IT investments of States should be leveraged. The Mission Mode Project on Commercial Tax should be aligned with the GST implementation going forward. Exhibit 3.5 depicts the features of GSTN.
3.16 STAKEHOLDERS

The stakeholders of GSTN are shown in the Exhibit 3.6 below:

**Small taxpayers:** The economic activity in India is concentrated among small taxpayers. They may not have the skill or the resources to effectively migrate to GST. Thus, adequate preparations must be done to ensure smooth migration for small taxpayers to GST. This includes extensive consultations, setting up of facilitation centers, education and training.

**Corporate taxpayers:** Corporate taxpayers may operate across various States and typically have sophisticated IT systems for accounting, e-filing returns, payments etc. Common file formats and message specifications should be released early to allow IT vendors that provide software to corporate taxpayers to modify and release updated versions with GST support.

**State tax authorities:** The State tax authorities would be responsible for collecting SGST. Common file formats, interfaces, and policy administration will enable accurate and timely assessments, and risk-based investigations resulting in enhanced productivity and revenues.
Exhibit: 3.9

Stakeholders

Source: Ministry of Finance, The IT Strategy for GST, July 2010

CBEC: CBEC would be responsible for collecting CGST and IGST. Common file formats, interfaces, and policy administration will increase the productivity of CBEC. It will allow for accurate and timely assessment, risk-based investigations and facilitate IGST settlement by Centre at agreed time intervals.

RBI: The Reserve Bank of India can facilitate the interface with various banks to facilitate movement of States’ and center’s funds. The processes of funds settlements and documentary compliance are independent.

Banks: Banks can accept duty from the taxpayers and process challans. All tax collections (whether physical or electronic) will happen at bank branches, or through the banks’ IT systems. Banks will route the tax collected to the concerned authorities through the RBI channel. Other Stakeholders include CAG, GSTN, TRPs and facilitation agencies.
3.17 WORKFLOWS

The Exhibit 3.7 shows the workflow of GSTN. The following three processes constitute the most important workflows of the GST administration and would be covered in the first phase:

Registration: A unique ID is necessary to identify each taxpayer. The PAN based ID should be common to both the States and the centre. A common PAN-based taxpayer registration has several benefits including a unified view of taxpayers for all tax authorities. A PAN based registration system has already been implemented in CBEC and several States are also capturing PAN data.

Returns: Both, the States and centre require taxpayers to file periodic returns to assess whether the taxpayers have computed, collected, and deposited their taxes correctly. ITC credit can also be verified on the basis of the returns filed and revenues reconciled against challan data from banks.

Exhibit: 3.10

Workflows of GSTN

Source: Ministry of Finance, The IT Strategy for GST, July 2010
**Challans:** Challans are the payment instruments used by taxpayers to actually pay their taxes. Challans are deposited at collecting banks and are forwarded by them to the tax administrations.

**IGST:** Under GST, interstate trade will be leviable to IGST. Under IGST, the tax paid by the selling dealer in the exporting State will be available as ITC to the purchasing dealer in the importing State. This requires verification of ITC claims and transfer of funds from one State to another. Further, in an interstate business to consumer transaction, tax collected in one State has to be transferred to another State as finalized by the business processes. Thus, periodic interstate settlement is required.

In addition, there are several other workflows such as processing refunds, taxpayer audits, and appeals. It is reiterated that the core services envisaged through common portal are limited to registration, payments and returns in the first phase. Other value added services will be added subsequently based on the needs of the Stakeholders. The IT infrastructure should be designed taking into account all stakeholders, and all related workflows.

### 3.18 A COMMON GST PORTAL

The solution architecture should be designed to meet the design goals for GSTN, described in the previous section. For the purpose of simplicity for taxpayers, uniformity of tax administration, digitization of all documents, and automation of related processes, it is necessary to have:

- Common PAN-based registration
- Common standardized return for all taxes (with different account heads for CGST, SGST, and IGST)
- Common standardized challan for all taxes (with different account heads for CGST, SGST, and IGST)

This solution architecture, explains the role of the common GST portal, and its connections with other systems.

Reforming the consumption tax system in an inter-governmental context is an extremely difficult issue. In a globalizing environment, it is necessary than the tax system generates sufficient revenues to provide efficient infrastructure. However,
these revenues would be raised by minimizing the three costs – the cost of collection, the cost of compliance and the economic costs arising from distortions. In an inter-governmental context, all these have to be achieved while ensuring fiscal autonomy to sub-national jurisdictions. A completely harmonized tax system which is very much desired by the businesses can be achieved only at the cost of fiscal autonomy of the States. Complete harmonization is equivalent to uniformity and this takes away the powers of the States to vary their public services and taxes.12

For the purpose of smooth transition to IGST, Tax information Exchange System (TINXSYS) has been developed as a Centralized exchange of all interstate dealers spread across the various State and Union Territories of India. TINXSYS is designed to help the Commercial Tax Departments of various States and Union Territories to effectively monitor the interstate trade. TINXSYS can be used by any dealer to verify the details of the counter party dealer of any other State. Department can also use TINXSYS for verification of Central Statutory Forms issued by other State Commercial Tax Departments and submitted to them by the dealers in support of claim for concessions.

3.18.1 Opposition for implementation

Opposition from States: At present, the States are opposing the proposed GST. Arriving at an acceptable GST rate has been bogged down by differences among the States and also between States and other entities like the TFC task force on GST architecture. Thumb rule is that larger the number of taxes subsumed in GST, lower will be the revenue neutral rate. The States have been reluctant to subsume all taxes into GST as it would mean loss of power to unilaterally change some taxes. 1) Two drafts of the proposed new tax regime failed to find acceptability by States and the third has been referred to empowered committee of State finance ministers. 2) Improper Structure: There is much debate on the likely aggregate rate of the GST. It is also possible that several other design elements of the GST can undergo changes. 3) GST requires constitutional amendments currently the Centre cannot impose tax beyond manufacturing and States cannot levy service tax. Unlike Direct Tax Code (DTC), GST is a transaction-based tax and hence can be introduced any time.

In India, VAT is a tax on sales, which the Constitution reserves for the States. Excise duties and service tax are levied by the Centre. GST would unify the three, so that there would be a single document. (i) There would also be a single registration with the tax authority. The simplification would be a relief to business. (ii) One hopes that as the taxable event will be simply defined as 'supply' of goods or services, all the current litigation on whether a particular transaction is a 'sale' or whether it is a 'service' and whether the item is 'manufactured' would be rendered redundant. (iii) Additionally, there ought to be increase in revenue for the governments, due to change in threshold for entering taxable level, and also due to closing of loopholes that plague the present system. While suggesting a model for the base and rate structure of GST, the following should be kept in mind by the joint Working Group which was formed under the aegis of the empowered committee of state finance ministers to prepare a road map for the introduction of GST by 2012.  

3.18.2 Obstacles or Barriers in Implementation of GST\textsuperscript{14}:

The introduction of GST has already been delayed by a year and a half mainly due to differences amongst the Centre and States. The introduction of GST will need constitutional amendment, which is required to be passed with two-third majority in both the houses of parliament and ratification by a simple majority by at least half of state assemblies. Accordingly, the support of all chief ministers is extremely crucial for such radical reform of indirect taxes. Thus, the support of the main opposition party BJP is obviously required to pass the bill in Parliament.

3.18.3 Initiatives towards Implementation

The optimistic Union Finance Minister believes to double the size of India’s economy within a short span of time. By the implementation of GST, India will be able to promote exports, raise employment, boost growth and thereby it will be able to gain

\textsuperscript{13} The Financial Express, Tuesday, June 12, 2007.

\textsuperscript{14} The Journal of Chartered Accountant, vol. 60, No. 4, October 2011.
yearly $15 billion as estimated by the experts. The revenue from GST shall be shared equally between the centre and states; implying that out of 20% tax proposed for goods, 10% would go to the State concerned. Similarly revenue from services and essential items shall also be shared equally. The peak effective rate will be about 15%, which is quite acceptable to the trade and industry.

- GST should be so designed that it should be revenue fair with sufficient growth of revenue to the centre and every State. Interests of the Special Category, North-Eastern States and Union Territories Have to be especially kept in mind.
- The Group will examine different models and see the manner in which the power of levy, collection and appropriation of revenue should be vested in the Centre and the States by looking at the pros and cons of various models.
- The various models suggested by the Working Group should ensure that double taxation is avoided.
- The Working Group would ensure that the suggested models take into account the problems faced during Interstate transactions and any revenue loss.
- The Working Group should consider how exempted goods and services and Non-VAT items such as petroleum goods and alcohol might be treated under the new regime.
- The models developed should reflect the interests of the Trade, Industry, Agriculture and Consumers, with due concern to the Centre-State relations.

The Government is encouraging the use of the system both by dealers and States. Similar IT structures would be required to be put in place by all State Governments and in near future every taxpayer would be required to comply with GST online to ensure its proper implementation.

3.19 GLOBAL EXPERIENCES IN GOODS AND SERVICES TAX

The Goods and Services Tax (GST) also known as the National VAT (Value Added Tax) has been introduced in more than 150 countries. Most of the countries have a unified GST system. Brazil and Canada follow a dual system where GST is levied by both the Union and the State governments. France was the first country to introduce GST system in 1954. The standard GST rate in most countries ranges between 15-
20%. Most of the sectors are taxed except for few exemptions. The United States of America does not have a national level VAT.

**AUSTRALIA**

The GST (Goods and Services Tax) is a value added tax on the supply of goods and services in Australia, including items that are imported. In most cases, GST does not apply to exports of goods or services, or other items consumed outside Australia.

It was introduced by the Howard Government on 1st July 2000, replacing the previous Federal wholesale sales tax system and designed to phase out a number of various State and Territory Government taxes, duties and levies such as banking taxes and stamp duty. The basic premise of the new tax was to broaden the tax base, which was heavily biased toward the provision of services. Prior to the GST, Australia operated a Wholesale Sales Tax (WST) which imposed a tax on wholesales of goods. The WST was implemented in the 30's when Australia had an economy dominated by goods. Over the years however, Australia's economy evolved to be more services based, and the GST served to strip the unfair tax advantage that service providing businesses had over suppliers of goods.

The GST is levied at a flat rate of 10% on most goods and services, apart from GST exempt items, and input taxed goods and services. GST is administered by the Tax Office on behalf of the Australian Government, and is appropriated to the States and territories.

**CANADA**


**Harmonised Sales Tax:** In Canada, the Harmonized Sales Tax combines the Goods and Services Tax (GST) and Provincial Sales Tax (PST) into a single sales tax. In 1997, the provinces of Nova Scotia, New Brunswick and Newfoundland and Labrador and the Government of Canada merged their respective sales taxes into the Harmonized Sales Tax (HST). In those provinces, the current HST rate is 13%. HST
is administered by the federal government, with revenues divided among participating
governments according to a formula. All other provinces continue to impose a
separate sales tax at the retail level only, with the exception of Alberta, which does
not have a provincial sales tax. Ontario proposed in its 2009 Budget to harmonize its
8% retail sales tax with the GST effective July 1, 2010. In July, 2009, the province of
British Columbia announced plans to also merge the PST and GST effective July 1,
2010. In PEI and Quebec, the provincial taxes include the GST in their base. The
three territories of Canada (Yukon, Northwest Territories and Nunavut) do not have
territorial sales taxes. The government of Quebec administers both the federal GST
and the provincial Quebec Sales Tax (QST). It is the only province to administer the
federal tax. The HST is composed of the GST and the 8% provincial tax and applies
to the same base of goods and services that are taxable under GST. HST follows the
same general rules as GST. GST/HST registrants continue to collect GST on taxable
supplies (other than zero-rated

BRAZIL

The Tax on Circulation of Goods and Services (TCMS) is the main State tax, and is
due on operations involving circulation of goods (including manufacturing,
marketing, and imports) and on interstate and inter-municipal transport and
communications services. ICMS is non-cumulative, and thus tax due may be offset by
credits arising from the purchase of raw materials, intermediary products, and
packaging materials which allows the taxpayer to record input tax credits from the
ICMS paid on the purchase of raw materials, intermediary products, packaging
materials. Tax credits for goods destined to become fixed assets may be accepted,
subject to certain restrictions. Rates applied to interState commerce are 7% or 12%,
depending on the destination. Export goods are exempted from ICMS.

NEW ZEALAND

Goods and Services Tax (GST) is a Value Added Tax introduced in New Zealand on
October 1, 1986 at 10%, and later increased to 12.5% on June 30, 1989. End users pay
this tax on all liable goods and services directly, in that it is included in the purchase
price of goods and services. GST registered organisations only pay GST on the
difference between GST-liable sales and GST-liable supplies (i.e. pay GST on the
difference between what they sell and what they buy: income less expenditure). This
is accomplished by reconciling GST received (through sales) and GST paid (through purchases) at regular periods (typically every 2 months, with some qualifying companies opting for 1 month or 6 month periods), then either paying the difference to Inland Revenue Department (IRD) if the GST collected on sales is higher, or receiving are funded from IRD if the GST paid on purchases is higher.

Unlike most similar taxation regimes, there are few exemptions - all types of food are taxed at the same rate, for example. Exceptions that are present include rents collected on residential rental properties, donations and financial services. The headline price must always be GST-inclusive in advertising and stores. The only exceptions are for businesses which claim a mainly wholesale client-base. Otherwise, displaying a prominent GST-exclusive price (i.e. larger and more obvious than the GST-inclusive price), is illegal.

**SINGAPORE**

Goods and Services Tax was introduced in Singapore on April 1, 1994, at 3%, but later increased to 4% on 1 January 2003, and 5% on 1 January 2004. It was raised again to 7% on 1 July 2007. Singapore’s GST is a broad-based consumption tax levied on import of goods, as well as nearly all supplies of goods and services. The only exemptions are for the sales and leases of residential properties and most financial services. Export of goods and international services are zero-rated. With an ageing population, Singapore’s income tax base is expected to decline. With a broad-based GST, the taxation burden will be more evenly spread among the population. Thus, the GST was introduced as part of a larger exercise to put in place a tax structure to see the country into the future. In Singapore, the tax is broad based which include all essential goods like water, electricity, rice, etc. Hence, a low income worker who would not pay income taxes would have to pay GST on his daily living expenses. This can be a burden especially during times of high inflation when the 7% tax is paid on the increasing price of daily essentials. GST is a self-assessed tax. Businesses are required to continually assess the need to be registered for GST.

**EUROPEAN UNION**

The European Union Value Added Tax ("EU VAT") is a value added tax encompassing member States in the European Union Value Added Tax Area. Joining in this is compulsory for member States of the European Union. As a consumption
The EU VAT taxes the consumption of goods and services in the EU VAT area. The EU VAT's key issue asks where the supply and consumption occurs thereby determining which member State will collect the VAT and what VAT rate will be charged. Each Member State's national VAT legislation must comply with the provisions of EU VAT law as set out in Directive 2006/112/EC. This Directive sets out the basic framework for EU VAT, but does allows Member States some degree of flexibility in implementation of VAT legislation. For example different rates of VAT are allowed in different EU member States. However Directive 2006/112 requires Member States to have a minimum standard rate of VAT of 15% and one or two reduced rates not to be below 5%. Some Member States have a 0% VAT rate on certain supplies- these Member States would have agreed this as part of their EU Accession Treaty, (for example, newspapers and certain magazines in Belgium). The current maximum rate in operation in the EU is 25%, though member States are free to set higher rates.

DENMARK

In Denmark, VAT is generally applied at one rate, and with few exceptions is not split into two or more rates as in other countries (e.g. Germany), where reduced rates apply to essential goods such as e.g., foodstuffs. The current standard rate of VAT in Denmark is 25%. That makes Denmark one of the countries with the highest value added tax, alongside Norway and Sweden. A number of services are not taxable, for instance public transportation of private persons, health care services, publishing newspapers, rent of premises (the lessor can, though, voluntarily register as VAT payer, except for residential premises) and travel agency operations.

FINLAND

In Finland, the standard rate of VAT is 22%. In addition, two reduced rates are in use: 17%, which is applied on food and animal feed, and 8%, which is applied on passenger transportation services, cinema performances, physical exercise services, books, and pharmaceuticals, entrance fees to commercial cultural and entertainment events and facilities. Supplies of some goods and services are exempt under the conditions defined in the Finnish VAT Act: hospital and medical care; social welfare services; educational, financial and insurance services; lotteries and money games; transactions concerning bank notes and coins used as legal tender; real property
including building land; certain transactions carried out by blind persons and interpretation services for deaf persons. The seller of these tax-exempt services or goods is not subject to VAT and does not pay tax on sales. Such sellers therefore may not deduct VAT included in the purchase prices of his inputs.

**NORWAY**

In Norway, VAT is split into three levels: 25% is the general VAT, 14% for foods and restaurant take-out (food eaten in a restaurant has 25%), 8% for person transport, movie tickets, and hotel stays. Books and newspapers are free of VAT, while magazines and periodicals with a less than 80% subscription rate are taxed.

**ICELAND**

In Iceland, VAT is split into two levels: 24.5% for most goods and services but 7% for certain goods and services. The 7% level is applied for hotel and guesthouse stays, license fees for radio stations, newspapers and magazines, books; hot water, electricity and oil for heating houses, food for human consumption (but not alcoholic beverages), access to toll roads and music.

**SWEDEN**

In Sweden, VAT is split into three levels: 25% for most goods and services including restaurants bills, 12% for foods (incl. bring home from restaurants) and hotel stays (but breakfast at 25%) and 6% for printed matter, cultural services, and transport of private persons. Some services are not taxable for example education of children and adults if public utility, and health and dental care, but education is taxable at 25% in case of courses for adults at a private school. Dance events (for the guests) have 25%, concerts and stage shows have 6%, and some types of cultural events have 0%.

### 3.19.1 Interstate transactions of Goods and Services

Integrated GST (IGST) model for taxation of interstate transaction of goods and services is briefly explained. According to this model, Centre would levy IGST which would be CGST plus SGST on all interstate transactions of taxable goods and services with appropriate provision for consignment or stock transfer of goods and services. The interstate seller will pay IGST on value addition after adjusting available credit of IGST, CGST, and SGST on his purchases. The Exporting State will transfer to the
Centre the credit of SGST used in payment of IGST. The Importing dealer will claim credit of IGST while discharging his output tax liability in his own State. The Centre will transfer to the importing State the credit of IGST used in payment of SGST. The relevant information will also be submitted to the Central Agency which will act as a clearing house mechanism, verify the claims and inform the respective governments to transfer the funds.

3.19.2 The major advantages of this model are:

Maintenance of uninterrupted input tax credit claim on inter State transactions. No upfront payment of tax or substantial blockage of funds for the interstate seller or buyer. No refund claim in exporting State, as ITC is used up while paying the tax.

- **Self monitoring model**: Level of computerization is limited to interstate dealers and Central and State Governments should be able to computerize their processes expeditiously. As all interstate dealers will be e-registered and correspondence with them will be by e-mail, the compliance level will improve substantially. Model can take 'Business to Business' as well as 'Business to Consumer' transactions into account.

- **Composition/Compounding Scheme**: Composition/Compounding Scheme for the purpose of GST will have an upper ceiling on gross annual turnover and a floor tax rate with respect to gross annual turnover. In particular, there would be a compounding cut-off at Rs. 50 lakh of gross annual turnover and a floor rate of 0.5% across the States. The scheme would also allow option for GST registration for dealers with turnover below the compounding cut-off.

- **Taxpayer Identification number**: Each taxpayer will be allotted a PAN inked taxpayer identification number with a total of 13 to 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.

- **Documentation and compliance**: Due to the dual structure of the GST, the assesses will be required to maintain separate accounts for Central GST and State GST. There will be one periodical return for both CGST and SGST with one copy each to be submitted to the respective GST authority.
3.19.4 Challenges in implementation

The discussion paper traverses some distance in providing clarification on the new tax regime, and this is particularly true of the treatment of interstate transactions, there are many other areas which are still unclear. Furthermore, much more work needs to be done before a clear picture of the new tax system emerges. Some of the challenges to be faced in implementing the GST regime are summarized below:

- The first major hurdle to be crossed in implementing the GST is enacting the Constitutional amendment to enable the centre to expand the tax base to include wholesale and retail transactions and to empower the States to levy the tax on services. Since, both the centre and the States are agreed that the switchover is desirable, this may not be a major hurdle, but the procedure itself will take time.

- It is clear from the discussion paper that the most important requirement for introducing the GST is the setting up of the Centralized agency to settle the IGST claims and work as a clearing house. The systems to track inter- State transaction in goods and services is critical to ensure the success of SGST.

- The attempt to develop it through the Tax Information Exchange System (TINXSYS) was not successful as only some States opted for it. The problem is not merely one of setting up the IT system. It is necessary to evolve a system to achieve a total solution to deal with interstate trade in goods and services. This is a major challenge and the entire success of GST will hinge on this. An agency like the National Security Depository (NSDL) which has done commendable work in the case of setting up the tax information network (TIN) in income tax, which led to a sharp increase in revenues should be contracted early so that they can work out a competent system of tracking interstate transactions and ensure smooth working of the clearing house mechanism.

- So far the taxation of services levied by the centre has been a selective tax. This has made the estimation of a revenue neutral tax rate difficult as some services with significant revenue potential continue to be excluded from the tax system, the most prominent being a tax on railway fares and freights.
Besides the challenge of extending the tax to all services, there are also issues of defining “service”.

- It is necessary to estimate the revenue neutral rate of the tax at the centre and in each of the States. This is necessary not only to arrive at convergence on the tax rates to be levied but also to negotiate and finalize the compliance, it would be useful to keep the rates low, but that would require the centre taking a lead in assuring the comfort of insurance against fall in revenue at least for the next three years by promising to compensate the States for the revenue less. It may be recalled that when Thailand introduced VAT in January 1992, the estimated revenue neutral rate was 10%, but they decided to levy the tax at 7%. Not only did they realize the full revenue at this lower rate, but their income tax revenue too went up by 25%! During the Asian financial crisis they had to increase the rate to 10% under International Monetary Fund pressure, but once they came out of the crisis, they reverted back to 7%! Eventually, the success of GST will depend on improved compliance, higher productivity growth and buoyant revenues.

- Estimation of the revenue-neutral general rate would require the estimation of the tax base in each of the States and financial intermediation, which is a genuine development activity, from financial services. In some cases, it is possible to identify the service charges and in others it is inextricably mixed up with profits.

- The rate administrations, both at the Central and State levels have to prepare to deal with transitional issues. Assessments and refunds arising from the prevailing tax systems will continue even as the transition is made to GST and settlement of these would require simultaneous administration of both the new and the old systems.

- A major challenge in the introduction of GST in the country is building the capacity of the administration to implement the new tax. The tax administration at both Central and State levels will have to be augmented to deal with the new tax regime. Although GST is a natural transition from the VAT system, both CENVAT and State VAT prevailing at present are in substantial variance with the standard VAT system seen internationally, both
in their design as well as in its implementation. Bargaining and dispute resolution mechanism is important to ensure compliance of the agreements by all the parties concerned.

3.20 STRIKING BALANCE

A GST model that strikes a balance between harmonization and fiscal autonomy would be far better than the present complex system. Any simplification and harmonization in procedures that lead to a broader base, less exemptions, smaller number of rates (hence less classification problems and scope for corruption), will automatically result in greater compliance, less disputes, lower collection cost and higher tax collection. A more comprehensive input credit system would avoid ‘cascading’ or (or tax-on-tax effect) - thereby reducing prices and improving the international cost competitiveness of Indian goods and services. We should keep in mind that if we start with a narrow base now, it will be difficult to change it later. Changing tax rates also becomes troublesome in future as vested interest develop. Hence, it is better to go slow, build a consensus and put a good (though not necessarily ideal) system in place rather than push through a haphazard compromise hastily. 15

The empowered panel has also approved a Special Purpose Vehicle for creating IT infrastructure for GST as a not-for Profit Company under section 25 of the Companies Act. Private sector will hold 51% stake in the SPV and rest will be held jointly by States and Centre. The proposal will now go to union cabinet for its approval. The empowered panel had given in-principle clearance for creation of IT infrastructure that will allow traders all over the country to use their permanent account number as the tax identification number for all direct and indirect taxes in the country. Having a common identification number has benefits not just for the taxpayers but also for the tax authorities as it helps them keep tab on transactions by establishing links with other tax payments. The IT infrastructure is crucial for the success of the proposed GST, which will replace plethora of indirect taxes including excise duty, service tax, value added tax, octroi. 16

15 The Hindu, Business line, Wednesday, September 21, 2011 pg.6
16 The Economic Times, Saturday, 15th October 18, 2011, pg 5
3.21 MISSION MODE PROJECT ON COMMERCIAL TAXES

Under the National e-Governance Plan (NEGP) launched by the Department of Information Technology, the Department of Revenue is coordinating a Mission Mode Project on ‘Commercial Taxes’ (MMP-CT), which is an important e-Governance initiative in the field of State taxes. The Union Cabinet in February 2010 has approved Mission Mode Project for computerization of Commercial Taxes Administrations of State Governments under NeGP. This project, with an overall cost of 1133 crore, will help States to develop and upgrade the IT systems in their commercial taxes administrations. The focus of the project, on the one hand, is to provide improved set of services to the dealers and on the other, to improve the efficiency of the Commercial Taxes administrations of the State Governments. Under this project, Central Government and State Governments are required to share fund roughly in the ratio of 70:30. However, keeping the Special Category Status of North Eastern States, this ratio has been fixed at 90:10 (Central share: State Governments’ share) whereas UTs without Legislature will be funded 100% by Central Government. A Project Empowered Committee (PEC) under chairmanship of Revenue Secretary has been constituted for sanctioning of States’ proposals of computerization of Commercial Taxes Departments. The meetings of PEC cleared project proposals of 31 States/UTs, having overall cost of 936.50 crore. An amount of 275.64 crore has been released to 31 States/UTs as part of Central share still, 2011. Claims amounting to 717.62 crore were pending as on 31 December, 2010.