2018

UNPACKING GST

A Primer

CBGA

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LIST OF ABBREVIATIONS

CGST	Central Goods and Services Tax
CST	Central Sales Tax
CVD	Counter Vailing Duty
GST	Goods and Services Tax
GSTC	GST Council
GSTDSA	GST Dispute Settlement Authority
GSTN	GST Network
GSTRs	GST Returns
IGST	Integrated Goods and Services Tax
ITC	Input Tax Credit
MSMEs	Micro, Small and Medium Scale Enterprises
RCM	Reverse Charge Mechanism
SAD	Special Additional Duty
SEZs	Special Economic Zones
SGST	State Goods and Services Tax
UTGST	Union Territory Goods and Services Tax
VA	Value Added
VAT	Value Added Tax

INTRODUCTION

It is now little more than a year that the Goods and Services Tax (GST) was implemented in India on July 1, 2017. Many have hailed it as a game changer and a bold reform. GST is expected to overhaul the indirect tax system of the country. It replaces various central and state level taxes and establishes a uniform tax throughout the country. The idea is that similar goods and services shall be taxed at the same rate across the country.

By doing so GST was projected to:

1. Simplify the indirect tax system
2. Reduce 'cascading' of taxes
3. Make the indirect tax system more transparent
4. Increase compliance

In the process, GST is also expected to bring about several benefits for the economy and its various stakeholders.

But so far, a number of concerns have been raised both with regard to the implementation and the design of GST. Following which both GST rates and rules have gone through various amendments. There have been more than 400 notifications, over 100 circulars and FAQs issued so far. Already new rate categories have been carved out, products and services have been moved from one tax bracket to another, the list under 28 per cent tax bracket has been drastically cut. The refund filing mechanism, the due dates and the forms have been changed several times. There are already talks of many more changes in the future, many of which are against the architecture of GST.

In addition, some features of GST have been deferred for the time being and are even likely to be scrapped from the GST law.

In short, the design as well as rules and regulations of GST are still evolving. More changes are likely to be brought in the near future. It is likely that even as this Primer is being published, some more changes are announced.

This Primer provides the relevant changes brought in up to the 30th GST Council meeting held on September 28, 2018.

In this Primer we explore different aspects of GST and attempt to present those in simplified language. There are total three sections with various subsections.

In Section I–Understanding GST, we look at the prominent features of GST, followed by what is meant by a Value Added Tax (VAT) and how it can reduce the problem of double taxation. We also discuss how GST is different from the earlier indirect tax system. The next sub-section explores why some commodities and suppliers have been exempted and excluded from GST. One of the important features of GST, the rules regarding small

enterprises, is discussed next. In the final subsection we look at the formula worked out for compensating States in case they face any loss in revenue following the implementation of GST.

Section II – Implementing GST, delves into the need to amend the Constitution to bring in GST. The key organisations responsible for implementing GST are discussed thereafter. The rules for tax returns filing are taken up in the next sub-section. In the final two sub-sections the Anti-profiteering provision (meant to ensure that businesses pass on the benefits of GST to consumers) and the e-way bill, a measure introduced to reduce tax evasion, are discussed.

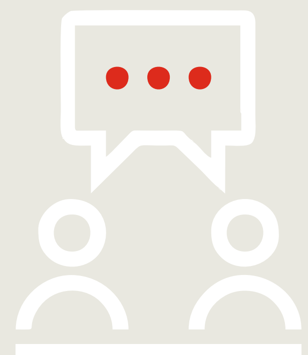
In Section III – Analysing GST, the final section, we look at the key differences of the current GST Act from the Bills introduced in 2011 and in 2014. The last two sub-sections examine some of the important issues related to the design of GST and the possible impact of GST on various stakeholders.

In the Appendix, we look in detail at some of the important Central and State level taxes, many of which have been brought under GST for most goods and services.

Section - I

Understanding

GST



SOME PROMINENT FEATURES OF GST

Briefly

GST has replaced a host of indirect taxes that existed earlier.

GST is one tax that is applicable on both goods and services.

Under GST the tax rates are uniform across the country and do not vary from State to State.

One Indirect Tax on Supply of Goods and Services

You, I and everyone pay taxes when we purchase goods and services. Some of us also pay income taxes when we earn above a certain threshold. The latter is known as direct taxes since we cannot shift the burden of the tax to another person or entity. The former is known as indirect taxes since the burden of taxes can be shifted, say, from businesses to the final consumer.

Until now we had a number of indirect taxes that were levied on various goods and services, beginning from the stage of production to final sale. So for example, there were taxes for manufacturing of goods (Central Excise Duty), on sale of goods (Sales Tax), on services provided by service providers (Service Tax), and so on.

The Goods and Services Tax (GST) subsumes almost all such indirect taxes (except for some taxes levied by municipalities and gram panchayats) and replaces them by one indirect tax: the ***GST***.

Taxes subsumed under GST

Central Taxes	State Taxes
1. Central Excise Duty 2. Additional Excise Duties 3. Excise Duty levied under the Medicinal and Toiletries Preparation Act 4. Service Tax 5. Central Sales Tax (CST) 6. Additional Customs Duty, commonly known as Countervailing Duty (CVD) 7. Special Additional Duty of Customs (SAD) 8. Surcharges and cesses (In India, cess is applied on a specific commodity or service and is imposedas an addition to an existing tax. The revenue that is raised from it is also meant to meet certain specified objectives, such as Swachh Bharat cess. Surcharge is an additional charge levied on any tax, but revenue from surcharge can be spent for any purposes).	1. State VAT/ Sales tax 2. Entertainment tax (other than those levied by local bodies, such as municipalities) 3. Purchase Tax 4. Luxury Tax 5. Taxes on lottery, betting and gambling 6. Taxes on Advertisements 7. Entry Tax (All forms) 8. State Cess and Surcharges

GST is applicable on the supply of both goods and services. As it is levied on the supply of goods and services it is different from the earlier concept of indirect tax which was levied on the manufacture or sale of goods or provision of services or movement of goods and so on. Like all indirect taxes, GST too is a tax on consumption.

A Value Added Tax

GST is a Value Added Tax (VAT), meaning that the tax is to be levied on the value added (explained below) at different stages of the production/supply chain until it reaches its final destination – the consumer. The final tax is to be paid by the end consumer and the revenue collected is to be kept by the Centre and the State where the final consumption takes place. This makes GST a destination-based tax.

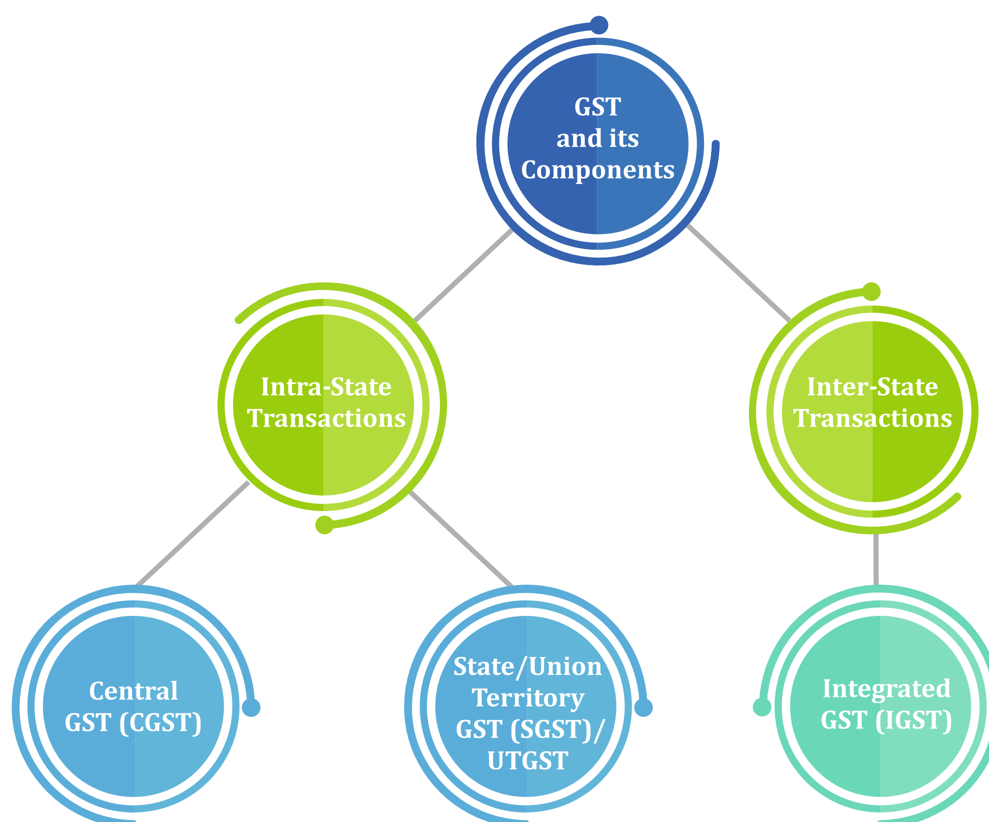
Components of GST

Although GST is a single tax, it has two components when transactions occur within a State or Union Territory, with the Centre and States simultaneously levying tax on transaction of supply of goods and services.

The GST to be levied by the Centre on within-State supply of goods or services is called Central GST (CGST) and that to be levied by the States and Union Territories without legislature, is called State GST (SGST) and Union Territory GST (UTGST) respectively.

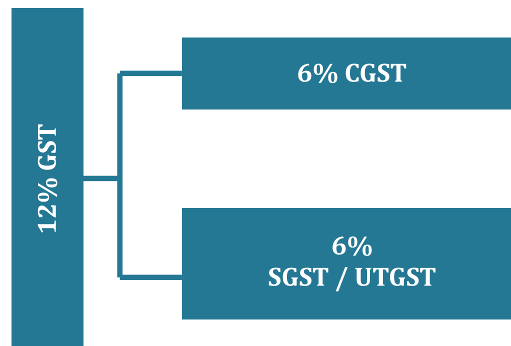
Integrated GST (IGST) is GST charged when transactions of supply of goods and services take place from one state to another. It is to be levied by the Centre and the tax collected is to be shared with the State where the final consumption takes place.

Figure 1: GST and its Components



This means that of, say, a 12 per cent GST, 6 per cent goes to the Centre and the other 6 per cent goes to the State (or the Union Territory).

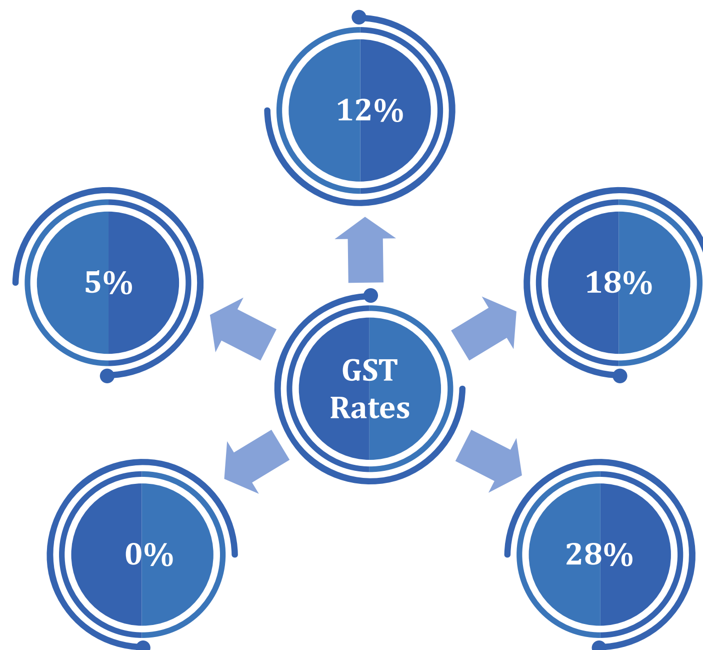
Figure 2: Division of GST between CGST and SGST/UTGST



Rates of GST

While GST is one tax, it does not mean that there is only one tax rate that is to be levied on supply of goods and services. There are five broad GST rates that are applicable for different categories of goods and services.

Figure 3: GST Rate Slabs



- Further, cesses are to be levied over and above the peak rate on certain goods such as tobacco and related products, aerated beverages, luxury cars, etc.
- In addition to these there are two more tax rates of: 0.25 per cent on unworked diamonds, precious and semi-precious stones; and 3 per cent on gold, silver, coin, etc. These GST rates are uniform across all States.

Table 1: GST Rates For Goods and Services For Reference

Rate	Goods	Services
0% (Exempted Items)	Food Grains, Fresh Milk and Pasteurised Milk, Eggs (in shell), Curd, Natural Honey (not put in containers), Vegetables (other than those put up in unit container), Prasad, Common Salt, Sanitary Napkins, Fish Seeds, Betel Leaves, Contraceptive, Newspaper, Rice (not put in containers)	Health care services by a clinical establishment, an authorised medical practitioner or para-medics, Services provided by way of transportation of a patient in an ambulance, Services provided by an educational institution to its students, faculty and staff support services to agriculture, forestry, fishing, animal husbandry, Transport of passengers by non-airconditioned contract carriage other than radio taxi
5%	Atta, Vegetable Oil, Broomsticks, Natural Rubber, E-Waste, Sugar, Tea (other than unprocessed green leaves of tea), Coffee, Edible Oil, Ultra High Temperature Milk, Milk Food For Babies, Packed Paneer, PDS Kerosene, LPG, Beet Sugar, Agarbatti	Transport of passengers, Transport of passengers by air, Transport of goods by rail, Supply of tour operators services, Tailoring services
12%	Yarn of manmade staple fibre, Butter, Ghee, Mobiles, Fruit Juice, Sugar boiled confectionery, Anaesthetics, Medical grade oxygen, Surgical rubber gloves or medical examination rubber gloves, Exercise book, graph book, etc., Synthetic or artificial filament yarns	Transport of passengers by air in other than economy class, Transport of goods in containers by rail by any person other than Indian Railways, Service of exploration, mining or drilling of petroleum crude or natural gas or both
18%	Mineral Water, Tableware, kitchenware, etc. made of plastics, Chocolates, Rear Tyres/ Tubes For Tractors; Hydraulic Pumps, Bumpers, Break Assembly, Gear Boxes, Articles of leather or of composition leather, Footwear with outer soles of rubber, plastics, leather, etc., Wood, Particle board, Plywood, Refrigerator	Education services, Human health and social care services, Postal and courier services, Electricity, gas, water and other distribution services, Financial and related services; real estate services; and rental and leasing services, Research and development services, Legal and accounting services
28%	Pan masala, Marble, Granite, Cars, Cement, Tobacco in various forms, Air-conditioning machines Motorcycles, Road tractors, New pneumatic tyres	Gambling, Other services (washing, cleaning and dyeing services; beauty and physical well-being services, etc.)

Notes: 1)Rates of Goods and Services as on September 20, 2018;
2)The above is not a complete or exhaustive list of items. Some of the items also attract Cess in addition to GST at the applicable rates.
Source: Central Board of Indirect Taxes and Customs (CBEC) website[1]

[1] Available at: https://cbec-gst.gov.in/gst-goods-services-rates.html

Salient features of the GST model adopted in India

GST is largely technology-driven. It will reduce the human interface to a large extent and is expected to bring more transparency in indirect tax system

The Goods and Services Tax Council (GSTC), of which the Union finance minister and the finance ministers of all States are members, decides the rules, the rates, threshold limit, etc.

GST is to be levied on all goods and services, except for alcoholic liquor for human consumption, real estate, electricity and transactions which are below the prescribed threshold limit

Petroleum and petroleum products are outside the purview of GST for the time being but shall be subject to the levy of GST at a later date notified on the recommendation of the Goods and Services Tax Council

Manufacturers, traders whose aggregate annual turnover is more than Rs. 20 lakhs (Rs. 10 lakhs in the case of some States) need to register for GST

Manufacturers, dealers/traders who carry out inter-state transactions will have to register for GST *even if their aggregate annual turnover is less than Rs. 20 lakhs*

Manufacturers, traders or restaurants whose aggregate turnover in the preceding financial year did not cross Rs. 1.5 crores (Rs. 75 Lakhs in some States) can opt for the Composition Scheme. Under this scheme eligible entities need not pay tax at normal rate but can pay at a prescribed percentage of her/his turnover every quarter.

Imports of goods and services will attract IGST, as they are to be treated at par with inter-state movement. Imports of goods will continue to attract Basic Customs Duty, but not Counter Vailing Duty (CVD) and Special Additional Duty (SAD) as these have been subsumed in GST.

Exports, supplies to SEZs and SEZ units are zero rated, which means no tax will be levied on them

The administration of the Central GST and Integrated GST would be with the Centre and that for State GST with the States

The Central GST and State GST are to be deposited into the accounts of the Centre and the States separately

Those depositing the tax would need to submit periodical returns to the concerned GST authorities

Compensation will be provided to the States for a period of first five years if there is any loss of revenue compared to the pre-GST period, arising on account of implementation of the Goods and Services Tax

A VAT WITH COMPREHENSIVE PROVISION OF INPUT TAX CREDIT

Briefly

GST is a Value Added Tax (VAT), i.e. it is levied on the value added portion instead of the whole value of output.

Taxing only the value added portion (and not the whole value of output) helps to eliminate the problem of double taxation.

This is because in VAT system of taxes it is possible to get credit for taxes already embedded in the inputs purchased, i.e. it is possible to get Input Tax Credit (ITC).

As mentioned earlier, indirect taxes are levied on goods and services- whether final goods/services or those in the intermediate stages of production/supply.

Generally, the production and distribution of goods/services involve a large number of processes performed by different entities.

For example, a shirt goes through various stages of production and different kinds of processes and then stages of supply before it reaches the end consumer. Different stages of the value chain usually consist of several entities, with each specialising in one or two aspects of production and/or supply of shirt. And at every stage several inputs are used to produce the output.

Let us assume that Firm 1 buys fibre and then it is spun into yarn using some inputs. In the next stage, Firm 2 weaves yarn into fabric. Following that, fabric is dyed, printed and finished by Firm 3 before it goes to the shirt manufacturer. At this stage a number of inputs such as colour, different chemicals, etc. are used for making the final output. The manufacturer also buys buttons from Firm 4 and needles from Firm 5. Using all these

inputs the shirt manufacturer, Firm 6, makes the shirt. It is sold to the wholesaler, Firm 7. The wholesaler then sells it to the retailer, Firm 8, who then sells it to the final consumer. And each entity involved in the production and supply/or supply chain adds some value.

Indirect taxes are levied on different stages of the production and supply chain. And these taxes can be levied:

- Either, on the whole value of output produced at each stage;
- Or, only on the value added (VA) at each stage of the chain. The latter kind of tax is called a Value Added Tax (VAT).

Value of Output = Value Added + Cost of Material

This distinction is important as taxes impact the cost of producing goods and services.

For instance, value of output when taken as a whole includes the cost of inputs, i.e. the raw materials used as well as the taxes applied on them.

Hence when tax is applied on the total value of output, it results into two things:

1) The raw materials (that have already been taxed) get taxed again.
2) The tax component of the raw material also gets taxed again.

Therefore, tax on the value of output leads to the same input being taxed repeatedly at the intermediate and final stages. That is, it leads to the problem of double taxation or *cascading of taxes.* As a result of this cascading of taxes, the tax burden increases manifold and results in higher cost of goods and services.

Value Added Tax and Input Tax Credit

Applying a Value Added Tax (VAT), on the other hand, eliminates the problem of double taxation.

The simple idea behind VAT is that instead of the whole value of output only the 'value added' portion is taxed. Value added shows the contribution made by a firm in the production/supply chain. Therefore, when VAT is applied at any stage of the production/supply chain, only the contribution made at that particular stage is taxed. This means inputs used at any stage of the supply chain, on which taxes have been paid already, will not be taxed again. As the tax is applied only on value added, this eliminates the problem of cascading effects of taxes (explained in detail in the next section).

For this to work, it is crucial that a mechanism exists such that when depositing tax on the output at any stage, one can get credit for or set-off the taxes already embedded in the inputs purchased. This mechanism is known as Input Tax Credit (ITC).

THE DIFFERENCE BETWEEN GST AND THE PREVIOUS INDIRECT TAX SYSTEM

Briefly

The earlier indirect tax system was complicated, had multiple taxes and with tax rates that varied across States.

The earlier system also had the provision of ITC, but it was limited.

India's indirect tax system has undergone several reforms over the last few decades. As part of such reforms, VAT was introduced, at different points in time, in both central taxes and state level taxes. VAT at the Central level (CENVAT) and State level (State VAT) was introduced to reduce the problem of 'cascading of taxes' for manufacturing and distribution respectively.

However, the problem of cascading effect of taxes remained and the tax system continued to be complicated.

So, it can be asked, if the problem of double taxation remained despite introducing VAT at various levels in the earlier indirect tax system, then how GST can solve the problem. In order to understand this, it is important to know what the problems were in the indirect tax system that existed to prior to the implementation of GST.

Indirect Tax System Prior to GST

Separate Jurisdiction of Taxes: In the indirect tax system prior to GST, the Constitution of India clearly demarcated the taxation powers of the government at different levels – the Centre, States and Local Bodies.

Thus, the Centre had the power to levy taxes on manufacture of goods (except alcoholic liquor for human consumption, opium, narcotics etc.), imports and services, but not on sale of goods. It also had the power to tax inter-state movement of goods, although the revenue earned was retained by the State where the sale originated.

States on the other hand had the right to levy taxes on sale of goods, or on movement of goods within states, but not on services or imports.

Taxation powers of different activities distributed between Centre & States

Activities under Central taxation	Activities under State level taxation
• Manufacture(except alcohol for human consumption) –Central Excise duty • Services – Service tax • Inter-State sales - CST (tax collected by the Centre but the revenue is retained by originating States)	• Sales carried out within a State • Sale of goods across the border of a State- Entry tax /Octroi/ Luxury tax, etc.

Multiple indirect taxes with multiple rates: Prior to the implementation of GST, we had a number of indirect taxes that were levied on various goods and services, beginning from the stage of production to final sale. So for example, there were taxes for:

- Central excise duty on manufacturing of goods,
- State VAT/Sales tax on sale of goods within states,
- Service tax on services provided by service providers,
- Central Sales Tax (CST) on inter-state movement of goods.
- In addition to these there were a number of other taxes that were levied.

The multiple taxes were accompanied by multiple rates for most kinds of taxes and in case of taxes levied by the States, the tax rates also varied from State to State.

- **A mix of VAT and non-VAT levies:**

Of these various taxes some taxes were in the nature of *VAT with the provision of ITC, similar to GST.* In addition to these, there were several other taxes that were levied on the whole value of goods and therefore did not provide the benefit of ITC (for details see appendix).

Table 2: VAT and non-VAT levies

VAT	Non-VAT
Central VAT (CENVAT) for central excise duties	Central Sales Tax
Service tax	Entry tax /Octroi
State VAT	Luxury Tax

In all, multiple kinds of taxes with multiple rates, which differed from State to State, gave rise to a complicated indirect tax structure.

So, taking the example of a shirt, first Central Excise Duty was levied on the manufacture of shirt at the factory gate, then State VAT levied when the shirt moved from manufacturers to wholesalers, then again State VAT and some other taxes when it reached the retail shop. Thus, at every stage of the supply chain, some tax or the other was levied.

Limited availability of ITC:

A major problem with earlier system of VAT was that the *provision of setting-off taxes was not available across the entire supply chain.* This was because of the clear demarcation of jurisdiction of taxes, so Centre level VAT could not be set-off against State level VAT and vice versa.

Thus, for example, a retailer could claim ITC only against State VAT deposited by the wholesaler, but not against Central Excise Duty or Service Tax already embedded in the product. This meant that Central VAT (CENVAT) and or Service Tax on certain commodities remained included in the value of goods taxed under State VAT. Because the same set of goods were taxed repeatedly – once by the Centre and then by the State - *it did not fully remove the cascading burden of taxes.*

The problem of cascading of taxes was further compounded because several taxes, such as CST, Entry tax, did not have the provision of ITC.

To summarise, three problematic aspects of the previous indirect tax system were that:

1) There existed multiple taxes which complicated the tax system;
2) Only some of these taxes were in the nature of a VAT with the provision of ITC; and
3) The problem of cascading of taxes continued.

What is different about GST?

GST, on the other hand, is a single tax applicable at all stages of the supply chain. By bringing almost all Centre and State level taxes and levies on various goods and services under one umbrella, into a single tax, GST has the potential to make the taxation system simpler. So, instead of different kinds of taxes at different rates levied depending on whether a good is at the stage of manufacture or distribution, now only GST will be levied at all stages of a supply chain.

Potential to reduce the problem of cascading of taxes:

- Under GST there is no separation between different kinds of economic activity as far as taxation goes. Similarly, for taxes subsumed under GST, there is no separate jurisdiction of Centre and State level taxes based on the kinds of activity that can be taxed.

- Therefore, GST allows for seamless flow of ITC across the entire value chain, beginning from the stage of supply of production to final retail sales of both goods and services. So, unlike earlier whereby ITC for Central VAT was not allowed against State VAT or vice versa, GST removes such restrictions. GST, therefore, with its system of comprehensive and continuous mechanism of tax credits can reduce the problem of 'cascading' of taxes.

The example given below explains how the problem of cascading of taxes GST can be reduced in the GST era compared to the pre-GST era.

Cascading of Taxes in the Pre-GST Tax System: Suppose there are three entities involved in the production and distribution of a shirt, before it reaches the final consumer– the manufacturer A, the wholesaler B, and the retailer C.

Let us assume that value added at each stage is Rs. 100 and tax rate is 10 per cent at each stage. For the sake of simplicity we also assume that there is no provision of getting tax refund (ITC) at any stage of the supply chain. Finally we also assume A does not have any input cost.

A manufactures the shirt and in the process adds value of Rs. 100. Central Excise duty (at the rate of 10 per cent) is chargeable at the factory gate. When selling to B this tax of Rs. 10 is added to arrive at the final price of the shirt.

The wholesaler B buys the shirt at Rs. 110 and adds value of Rs. 100 by packaging the shirt for the final consumer. The total value of B's output is then Rs. 210 (VAT of Rs. 100+input cost of Rs. 110).

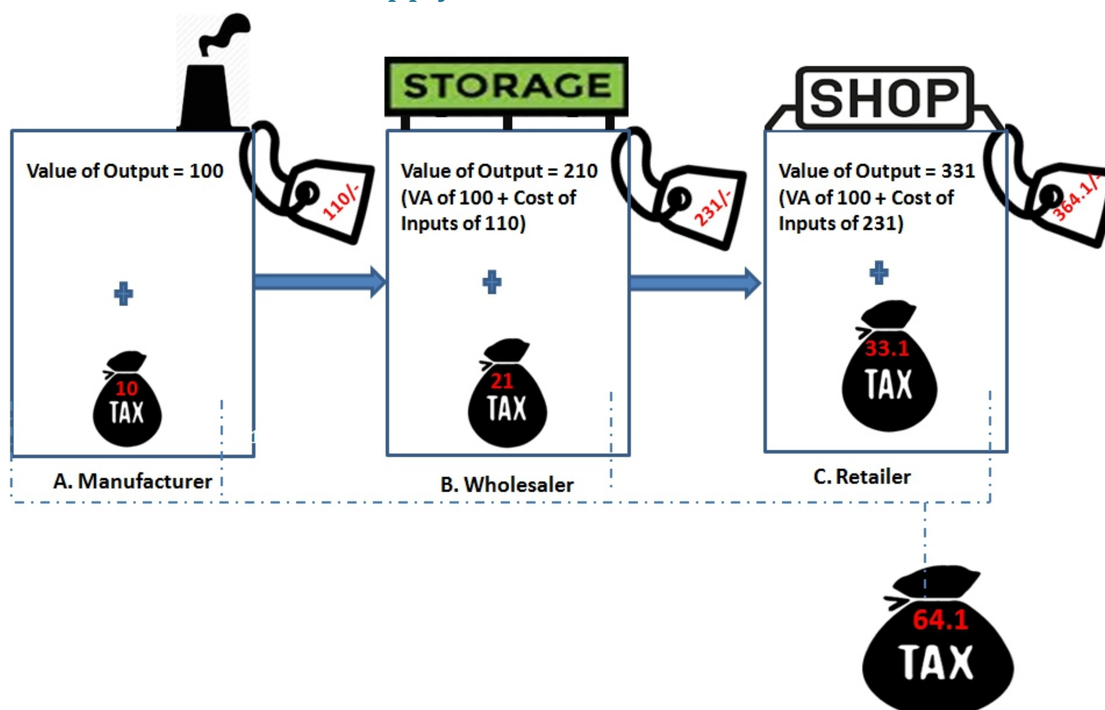
Since there is no system of ITC, B is required to deposit State VAT on the entire value of the shirt, i.e. on Rs. 210, which includes the Central Excise Duty to the tune of Rs. 10.

Note, since value added by B is Rs. 100, the tax amount at this stage should have been Rs. 10. Instead the tax amount is Rs. 21, i.e. on the whole value of the product. This is cascading of taxes or tax on tax, as now State VAT is not only chargeable on the entire value of the shirt i.e. Rs. 100, but also on tax i.e. Rs. 10, already paid by A in the earlier stage.

The total tax amount up to this point is Rs. 31, of which Rs. 10 is deposited by A and Rs. 21 by B. The whole tax amount is passed on to C in form of higher prices and hence increases cost of inputs for C.

Now C adds value by providing a convenient window of sale for the final consumer. As value addition by C is of Rs. 100, the total value of C's output is Rs. 331 (VA of 100 +raw material cost of Rs. 231). Since no ITC is available, the tax levied at this stage too is on the whole value of the output, which amounts to Rs. 33.1. Adding up tax liabilities at various stages, it turns out that the total tax burden, which is largely passed on to the end consumer, is Rs. 10+21+33.1 or Rs. 64.1.

Figure 4a: Cascading of Taxes and Tax Burden in the Pre-GST Regime-The Case of Intra-State Supply



Possibility of Reduced Cascading in the GST Regime: In the GST regime, tax liability can reduce significantly as it provides the benefit of availing ITC at *every stage of the production and supply chain.* Taking the previous example, we assume that the GST rate is 10 per cent at different stages of the chain and all the three entities do value addition of Rs. 100.

Once A manufactures the shirt and adds value of Rs. 100, GST (at the rate of 10 per cent) is levied when supplying to B. As A does not use any taxable inputs, there is no ITC available, hence the tax of Rs. 10 is added to arrive at the final price of the shirt, which is Rs. 110. When selling to B, A deposits the GST amount of Rs. 10 with the government. A also has to submit the details/GST Number of the buyer (B in this case). Through this B will get a tax credit of Rs. 10.

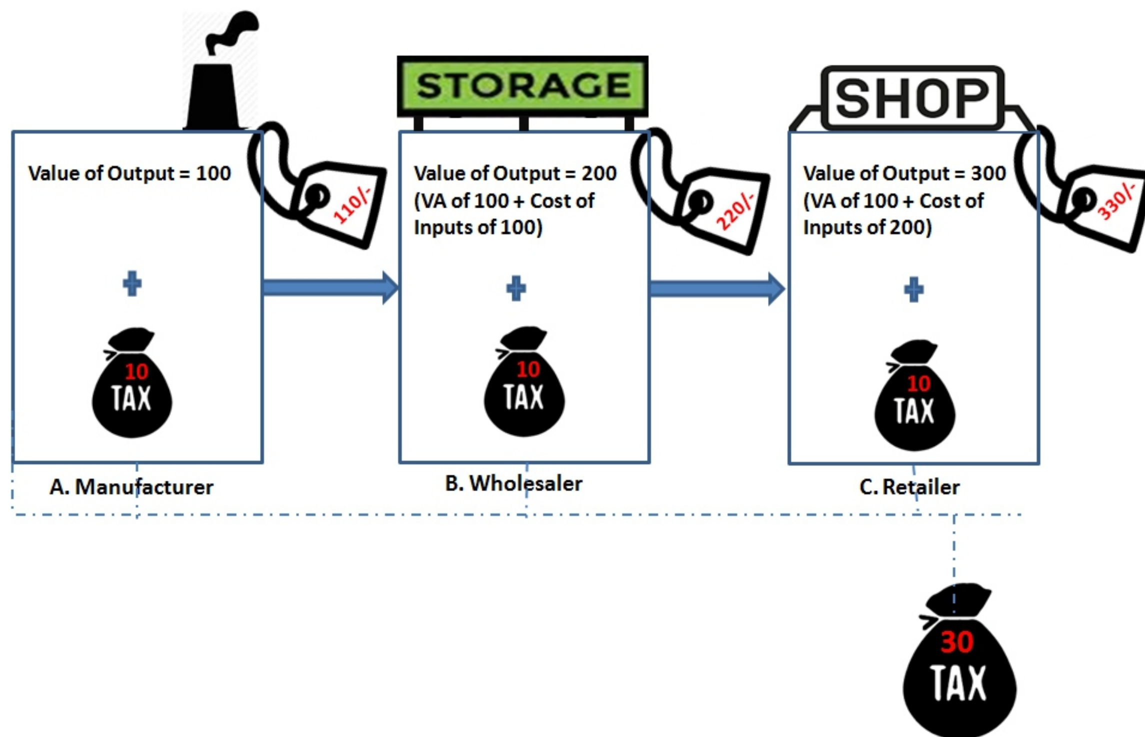
Since B can set off this tax, it will not be included as cost and hence the total value of B's output is Rs. 200 (VA of Rs. 100+input cost of Rs. 100). Although the tax payable on total value of B's output is Rs. 20 (10 per cent of Rs. 200), as B will get tax credit of Rs. 10 for inputs bought from A, the *net tax* that B has to deposit is Rs. 10. Note that this is exactly equal to the tax amount had it been levied only the value added of Rs. 100 by B.

As the figure below shows, for B the *tax liability net of ITC in the GST* regime is Rs. 10, much lower than the tax liability of Rs. 21 in the previous regime.

Similarly, C also gets the benefit of ITC so that the total value of C's output is Rs. 300 (VA of Rs. 100+input cost of Rs. 200). The tax chargeable is Rs. 30. But since it can avail the tax credit of Rs. 20 that was deposited in the earlier stages of the value chain, the net tax it has to deposit is Rs. 10. As the input costs and the taxes on inputs are not to be included, this eliminates the problem of cascading of taxes.

The elimination of cascading also results in lower tax liability across the value chain. Adding up tax liabilities at various stages, it turns out that the total tax, which is passed on to the end consumer, is Rs. 10+10+10 or Rs. 30.

Figure 4b: Reduced Cascading of Taxes and Tax Burden under GST- The Case of Intra-State Supply



The above example is of an ideal situation. However, there are several operational and implementation challenges that beset GST on the ground.

In sum, GST, by subsuming most of the Central and State level taxes into a single tax and by allowing a set-off of prior-stage taxes across the entire value chain, *has the potential to:*

1) Simplify the indirect tax system; and

2) Mitigate the problem of cascading of taxes.

COMMODITIES AND SUPPLIERS EXEMPT AND EXCLUDED FROM GST

Briefly

Commodities of mass consumption are taxed at zero rate.

Petrol and petroleum products, alcohol for human consumption, electricity, etc. are outside the ambit of GST as they are important sources of revenue for States.

Small enterprises are also exempted from registering for GST to avoid the unnecessary burden of compliance and taxes that they can ill afford.

Commodities exempt (i.e. zero rated) from GST:

1. A number of basic consumption goods such as unbranded food products (food grains, pulses, fruits, vegetable, etc.) along with education and health care and some other services. These are strictly not out of GST but taxed at zero rate.

Commodities excluded from GST:

2. Alcoholic liquor for human consumption, real estate, electricity; and
3. Petroleum and petroleum products – these are outside the purview of GST temporarily, but shall be subject to the levy of GST at a later date decided by the Goods and Services Tax Council (GSTC).

Reasons for exempting some commodities from GST:

- The main reason for keeping basic consumption goods and certain services at zero rate is that GST is an indirect tax and indirect taxes adversely affect the poor most. Therefore, it is important that tax rates are nil or very low on consumption goods and services that form a large proportion of consumption basket of the poor.

Reasons for excluding some commodities from GST

- Tax collected from petrol and petroleum products, alcohol for human consumption, electricity, real estate, etc. forms anywhere between 40 per cent - 50 per cent of the total tax revenue earned by various states.
- As it is not clear how GST will impact the tax revenue earned by different States, these have been left out of the ambit of GST so that States and the Centre have the leeway to raise additional resources through these. As long as these items remain out of GST, these will continue to be covered by taxes such as Central Excise Duty

Suppliers who need not register for GST:

1. Suppliers of goods which only carry out intra-state transactions and have annual aggregate turnover of less than Rs. 20 lakhs (Rs. 10 lakhs in the case of some States), are not required to register under GST.[2]
2. Service providers whose annual aggregate turnover is less than Rs. 20 lakhs (Rs. 10 lakhs in the case of some States), are not required to register under GST even if they carry out inter-state transaction, or provide services through e-commerce platforms.[3]

[2] If an enterprise's turnover consists of supply of only goods/services which are exempt under GST, this clause does not apply.
[3] As per 23rd GST Council meeting held on November 11, 2017, https://cleartax.in/s/taxable-person-gst

- **Reasons for keeping small enterprises out of the tax net:**
- It is difficult to administer small enterprises and the cost of administering by tax authorities such enterprises is very high compared to the tax paid by them. Thus, keeping small enterprises out of the tax net helps to reduce the cost of monitoring them.
- Small enterprises don't have to face daunting compliance costs such as that of paying salary of accountants, fees of tax lawyers, etc., if they are kept out of the tax net.
- If kept out of the tax net, small enterprises can get price advantage in the market because of lower tax incidence.

THRESHOLD LIMIT AND OTHER RULES CONCERNING SMALL BUSINESSES

Briefly

The threshold level for registering for GST has been lowered significantly (compared to excise duty) in order to bring more enterprises into the tax net.

The composition scheme, meant for smaller enterprises, has both advantages and disadvantages.

Change in Threshold Limit for Depositing Taxes: Under GST the threshold limit for levying taxes is different from that in the previous indirect tax system. This is particularly so for small businesses of various kinds. Earlier, manufacturers/producers with annual turnover less than Rs. 1.5 crores were generally exempted from paying Central excise duty. Similarly, dealers and retailers, earning below a certain threshold were also exempted from State VAT. The threshold for State VAT varied from State to State and ranged between Rs. 5 to 20 lakhs.

Under GST, the threshold limit is uniform across all States and all kinds of supplies. This means there is no longer any differentiation between manufactures, or dealers or retailers, when it comes to threshold level for taxation. That, in turn, means that the threshold limit has been lowered significantly for those who are manufacturers. At the same time, the threshold level for traders, dealers, etc. has been raised compared to what it was earlier in several States. In all, suppliers of goods and services with all India aggregate annual turnover of more than Rs. 20 lakhs (Rs. 10 lakhs in the case of some States) need to register for GST and adhere to all the rules of GST.[4]

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[4]Enterprises with annual turnover between Rs. 20 lakhs and Rs. 1.5 crore can opt for the composition scheme and pay lower rates of taxes.

Threshold Limits for Levy of Tax

- **Pre-GST**
  Central Excise- Rs. 1.5 crores
  Service Tax- Rs. 10 lakhs
  VAT- Varied from Rs. 5 to Rs. 20 lakhs from State to State

- **Under GST**
  CGST/SGST - Rs. 20 lakhs (Rs. 10 lakhs for some States)[5], provided manufacturers and/or traders only carry out *intra-State transactions;*

If, on the other hand, manufacturers and/or traders have inter-state transactions, they will have to register for GST even if their aggregate annual turnover is below Rs. 20 lakhs.

Service providers need not register for GST even if they carry out inter-state transactions as long as their aggregate annual turnover is less than Rs. 20 lakhs.[6]

However, this threshold level does not apply to those who were already registered under any of the previous indirect tax regimes (VAT, Excise Duty, Service Tax Laws), even if their aggregate annual turnover is less than Rs. 20 lakhs (Rs. 10 lakhs in some States).

This change in the threshold level has significant implications for lakhs of micro, small and medium scale enterprises (MSMEs) that engage in manufacturing. Earlier, excise duty was not levied on such manufacturing enterprises, which form the bulk of India's manufacturing sector, as long as their annual turnover was less than Rs.1.5 crores. Now under GST, many such enterprises will have to register for GST and deposit GST, if applicable.

Tax Implications for those dealing with small unregistered enterprises: Tax implications, however, do not end even if an enterprise does not register under GST because their annual turnover falls below Rs. 20 lakhs. The only thing that happens is that the responsibility of depositing tax shifts from the unregistered dealer to the registered one. This is because of a mechanism called the Reverse Charge Mechanism(RCM) for goods[7] that has been introduced under GST. This is applicable for transactions between registered and unregistered entities (a large proportion of which are in the informal sector) and for certain specified goods and services. The aim of reverse charge under GST is to bring under the tax net all large enough transactions, even when the transactions are with the informal sector.

[5] In the 28 GST Council meeting held in July 2018, the threshold limit for GST exemption has been increased from Rs. 10 Lakh to Rs. 20 Lakh for 6 States, namely, Sikkim, Arunachal Pradesh, Himachal Pradesh, Uttarakhand, Assam & Meghalaya.
[6] https://cleartax.in/s/aggregate-turnover-under-gst-for-registration
[7] Reverse Charge Mechanism in service tax for some services was there in the previous tax system. Under GST it has been extended to goods as well.

Reverse Charge Mechanism(RCM): Reverse charge, as the terms suggests, simply means that the chargeability of tax gets reversed. So unlike the normal practice whereby GST is to be deposited by a supplier of goods and/or services, under Reverse Charge Mechanism, liability to deposit tax is on the registered recipient of such goods or services and not on the supplier of goods and/or services.

This is applicable only if the total value of goods/services purchased by registered enterprises from unregistered entities exceeds Rs. 5,000 in a day. Tax deposited on reverse charge basis will be available for ITC as long as such goods and/or services are used, or will be used, for business. In this case, the recipient (i.e., who deposits the tax) can avail ITC. Reverse Charge Mechanism has been put on hold until September 2019 as per the decision taken in the 28th GST Council (GSTC) meeting held on 21 July, 2018.

GST Composition Scheme: There is yet another option available for small enterprises. This scheme can be opted for by enterprises whose turnover is more than Rs. 20 lakhs but less than Rs. 1.5 crores. This is known as the GST Composition Scheme, and is an extension of the VAT Composition Scheme that existed earlier.

Under GST, enterprises that opt for this scheme will only have to pay tax at a flat rate (see Table below). These enterprises do not need to issue invoices. The scheme was initially only open to manufacturers, traders and restaurants but not to other service providers. But following the 28th GSTC meeting held on July 21, 2018, service providers with annual turnover up to Rs. 5 lakhs too are eligible for GST Composition Scheme.

Table 3: GST Rates under Composition Scheme

Types of Suppliers/Businesses	GST	CGST	SGST
Manufacturer/Traders of Goods and Services	1%	0.5%	0.5%
Restaurants not serving alcohol	5%	2.5%	2.5%

While there are a number of advantages of this scheme, it also has several disadvantages.

Advantages of registering under the Composition Scheme:

- Much lower tax liability compared to normal rates of GST;
- Lesser compliance as returns need to be filed quarterly and not monthly like others registered under GST;
- No need to issue invoices, hence lesser problem of maintaining books of record, etc.

Disadvantages of registering under the Composition Scheme:

- Cannot supply goods and services which are taxed at zero rate;
- Cannot carry out inter-state transactions and hence the territory of business is limited;
- No Input Tax Credit available to composition dealers;
- Have to bear the tax burden as invoices cannot be raised and tax cannot be passed on to anyone else.

COMPENSATION TO STATES

Briefly

States will get compensation if, after the implementation of GST, their tax revenue grows at less than 14 per cent compared to the revenue earned in the year 2015-16.

Compensation will be available for the first five years.

GST is a destination-based tax which means that tax revenue earned on inter-State transactions is collected by the Centre and shared with the State where the final consumption takes place. In contrast, under the earlier system, CST was levied on inter-state transactions and the revenue so earned was kept by the State from where the goods originated.

So, many *producing* States such as Maharashtra, Tamil Nadu, Gujarat, Karnataka, had the apprehension that they would lose out on tax revenue under GST when goods and services produced in their State are consumed in another State.

In order to resolve such issues, and to provide compensation to States in case of revenue shortfall, the Goods and Services Tax (Compensation to States) Bill, 2017, was brought in. As per this Bill compensation will be provided only for the first five years after the implementation of GST.

Calculation of Compensation: States are to be provided compensation only if a State's tax revenue in any financial year grows at less than 14 per cent compared to the revenue earned in the year 2015-16 (the year that has been decided as the base year for calculating

the rate of growth of revenue). The taxes for which revenue will be compensated are the State level taxes that have been subsumed under GST, namely,

(i) State Value Added Tax (VAT)

(ii) Entry tax, Octroi

(iii) Central Sales Tax (since the revenue accrued to the State even though the tax was levied by the Centre);

(iv) Taxes on luxuries,

(v) Taxes on advertisements, etc.

Hence, revenue generated by States from taxes on supply of a) alcohol for human consumption, b) certain petroleum products, c) electricity, etc., will not be accounted for as part of the revenue generated in 2015-16 in the calculation of compensation.

Financing Compensation to States: As mentioned above, under GST, cesses will be levied over and above the peak rate on certain goods such as tobacco and related products, coal, aerated beverages, luxury cars, etc. The revenue generated from the cesses will be used to finance compensation to States. The receipts from the cess are to be deposited to a GST Compensation Fund, and can't be used by Centre for any purpose other than compensating the revenue loss of States.

If there is any unutilised money in the Compensation Fund, it will be distributed in the following manner:

(I) Fifty per cent of the fund to be shared between the States in accordance with the compensation required by different States; and

(ii) The remaining 50 per cent will be part of the Centre's divisible pool of taxes.

These cesses, however, will be removed after five years, and the idea is that if any State incurs losses even after five years from implementation of GST, they would have to find alternative sources of revenue.

Section - II

Implementing
GST

CONSTITUTIONAL AMENDMENT

Briefly

For implementing GST, the Constitution had to be amended so that the Centre and States have taxation power over the same goods and services concurrently.

As mentioned earlier, before the introduction of GST, the Constitution of India provided for division of powers of taxation between the Centre and States. Because of this division, the States did not have the power to levy tax on supply of services or on imports. On the other hand, the Centre did not have any power to levy tax on the sale of goods. What this meant is that neither the Centre nor States had the power to tax supply of both goods and services.

Since GST is a tax levied on supply of goods and/or services, it was essential to amend the Constitution to empower the Centre to levy tax on sale of goods and States to levy tax on services.

For this purpose, the Constitution of India was amended by the Constitution Act, 2016 (One Hundred and First Amendment). The 122nd Constitutional Amendment Bill was passed by the parliament in August 2016. Following the President's approval on it in September 2016, it became the 101st Constitutional Amendment Act. This act paved the way for introduction of the Goods and Services Tax (GST).

The 101st Constitutional Amendment Act (2016)

- **Amends the Constitutional provisions in**
  - **Articles** 248, 249, 250, 268, 269, 270, 271, 286 of the Constitution – Alters the current tax structure and the specific powers of the State and Central governments and the distribution of revenue between the two.
  - Article 366 of the Constitution – Defines 'goods and services tax'.
  - Article 368 of the Constitution – Provides that an amendment to the functioning of GST Council will require a constitutional amendment.
- **New Articles Introduced**
  - **Article 246. A:** This article provides that both Parliament and State legislatures shall have concurrent powers to make laws with respect to goods and services tax (GST). The Parliament will retain exclusive power to legislate on inter-state trade or commerce.
  - **Article 269. A:** This article provides that GST on interstate transactions shall be levied and collected by the Centre. Tax collected will be shared between the Centre and States as per the recommendations of the GST Council.
  - **Article 279. A:** This article provides for constitution of the GST Council by president within sixty days from this act coming into force.
  - **Omits** Article 268. A of the Constitution. – Deletion of provision for service taxes.

KEY ORGANISATIONS RESPONSIBLE FOR IMPLEMENTING GST

Briefly

The GST Council and the GST Network are crucial for implementation of GST.

GST Council is responsible for all rules and regulations related to GST.

GST Network is the Information Technology backbone for all processes related to GST.

The two key organisations that form the mainstay for implementing GST are - The GST Council (GSTC) and the GST Network (GSTN). The former frames all the rules and regulations associated with GST and the latter is the Information Technology backbone necessary for the implementation of GST.

GST COUNCIL

1. Organisation Structure

The Goods and Services Tax Council (GSTC) is a constitutional body, which represents the State and the Central executive. The members of the GSTC include the Union Finance Minister (chairperson), Union Minister of State in charge of revenue and the State Finance/Taxation Ministers in respective states.

As per the 101st Constitutional Amendment Act, approval of any decision of the Council requires a majority of not less than 75 per cent (3/4th) of the weighted votes of the Members present and voting. The voting strength in the GSTC is divided as given below:

Voting strength in the GSTC

1. Central government has a weightage of ⅓ of the total votes cast.
2. All States taken together have a weightage of ⅔ of the total votes cast, with each State having equal voting strength.
3. For the proceedings of a meeting to be a valid, at least 50 per cent of the total number of the members of the GSTC should be present.

2. Functions

The function of GSTC is to make recommendations on:

1. The goods and services to be taxed under GST and those that are to be exempted;
2. The threshold limit of annual turnover below which entities need not register for GST;
3. The rates including floor rates with bands of GST;
4. The date on which the GST shall be levied on petroleum and petroleum products such as crude oil, high speed diesel, natural gas and aviation turbine fuel;
5. Principles of levy, apportionment of IGST and the principles that govern the place of supply;
6. Any special rate or rates for a specified period to raise additional resources during any natural calamity or disaster;
7. Special provision with respect to the Northeast States, Himachal Pradesh and Uttarakhand; and
8. Any other matter relating to the GST, as the Council may decide.[8]

3. Principle for deciding GST Rates by GSTC

The idea behind GST is that there should be a uniform tax rate applicable across goods and services that are similar in nature. Accordingly, even the list of exempted goods and services are harmonised for the Centre and States as well as across States. According to the rate fitment committee of GST, which comprises tax officials of the Central and State governments, GST rates have been fixed for various goods and services such that the GST rate for an item will be, to the extent possible, the one that is nearest to the earlier rate. That is, GST rates on most goods are approximately equal to the earlier tax incidence due to VAT and excise duty.

[8] See 'Frequently Asked Questions (FAQs) on Goods and Services Tax (GST)', (2017), Central Board of Excise & Customs, 2nd Edition, March 31, 2017; available at http://www.cbec.gov.in/resources/htdocs-cbec/deptt_offcr/faq-on-gst-second-edition.pdf.

GST NETWORK

1. Organisation Structure

The structure of ownership of GSTN is set to change in the future as per the decision taken in the 27th GST Council Meeting held in May 2018. As of now, the GST Network (GSTN) is a private, not-for-profit company registered under the Companies Act 2013. Private financial institutions own 51 per cent of the GSTN, with the rest (49 per cent) being owned by the government – the Centre, all States and the Empowered Committee of State Finance Ministers (EC).

Table 4: Shareholding Pattern of GSTN

Shareholder	Share (in %)
Central government	24.5
State governments & EC	24.5
HDFC	10
HDFC Bank	10
ICICI Bank	10
LIC Housing Finance Ltd.	11
NSE Strategic Investment Co.	10

Source:GST Network Website

However, in the 27th GST Council meeting held in May 2018, it has been decided that the 51 per cent share held by private entities are to be taken over by the government and eventually the Central government and the State governments collectively will hold equal proportions (i.e. 50 per cent Centre and 50 per cent all States together).

2. Role and Functions of GSTN

The role of technology is crucial in implementing GST. All processes related to GST, such as registration for GST, depositing taxes, uploading invoices and receipts for receiving ITC, return filing, etc. are to be done online. Therefore it is important to have an Information and Technology (IT) platform which can perform the necessary functions for smooth implementation and functioning of GST. The GST Network (GSTN) is expected to facilitate taxpayers in various processes related to GST.

As the GSTN website notes, the GSTN has been set up with the aim to provide"IT infrastructure and services to the Central and State Governments, tax payers and other stakeholders for implementation of the Goods and Services Tax (GST)".[9]

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[9] For more details, see GST Network Website: http://www.gstn.org/

Functions of the GSTN

The major functions of the GSTN include, among other things, facilitating:

- **Filing of registration application:**
  - GSTN provides the common platform for filing of application for registration under GST for all taxpayers across the country.
- **Filing of tax returns:**
  - Under GST one common return is to be filed for CGST, SGST and IGST and there is no longer any need to file separate tax returns with Central and State Authorities. The returns are to be filed on the GSTN.
  - When filing returns, invoices also need to be uploaded for claiming ITC. GSTN will do the job of matching the invoices uploaded on the basis of invoice level data filed by taxpayers.
- **Creation of challan for tax payment:**
  - GSTN also creates the tax challan, which is a form used to fill in the details of the taxes to be deposited with the government. The Challan created can then be used by tax payers to make the tax payment into any of the authorised banks. The function of GSTN is to make a summary of all payment confirmations received by it from Banks at the end of the day and share that with the Reserve Bank of India (RBI) and accounting authorities for reconciliation.

In short, GSTN will handle:

- Registrations
- Invoice uploads
- Various returns filing
- Payments & Refunds.[10]

[10] ibid

TAX RETURNS FILING AND PENALTY FOR NOT FILING RETURNS ON TIME

Briefly

The tax returns filing system is designed to curb tax evasion and provide Input Tax Credit across the value chain of different goods and services.

The returns filing system is complicated and multiple returns need to be filed every month.

Because of this and snags in the GST Network, the GST Council is expected to bring in easier norms for filing returns from April, 2019.

Under the GST regime, filing return is critical for getting input tax credit.

Not filing returns and even not filing them on time can result in a host of penalties, delay in refunds and can even adversely affect an enterprise's compliance rating. Some of these aspects related to returns fling under GST are given below.

- **A large number of returns to be filed:** As per the norms decided in the first few months of introducing GST, enterprises that register for GST (other than those opting for the composition scheme) were to file three GST Returns (GSTRs) per month.

In addition, an annual return needs to be filed at the end of each financial year. Thus, an enterprise (barring those opting for the composition scheme) needs to file a total of 37 returns in a year, *if they operate in a single State.* The number of returns to be filed increases manifold, if an enterprise has operations in more than one State. So an enterprise providing goods and/or services and having presence in multiple States, will need to obtain GST registration and file returns in all the States they operate in. In short, the number of returns to be filed increases depending on the number of States an enterprise operates in, the number of branches they have, etc.

To file GST returns, GST compliant sales and purchase invoices are required.

The table below shows the details pertaining to some of the main forms:

Table 5: Main GSTR forms and their details

Return form	Particulars to be filed
GSTR-1	Details of sales/outward supplies of goods and/or services
GSTR-2	Details of purchases/inward supplies of taxable goods and services made for claiming ITC
GSTR-3	Summary and final details of outward supplies and inward supplies, along with the payment of amount of tax
GSTR-3B	Provisional Return to be filed by all registered businesses even if there are no transactions during the return period
GSTR-9	Annual Return

Source: GST Return, https://cleartax.in/s/gst-returns

This was what was initially planned. As per this design, registered enterprises were only required to file one return (GSTR- 1) and the rest two were to get auto-filled on the GSTN portal. Thus, information provided by the seller were to be matched with that of the buyer and these two were to be automatically matched to arrive at the summary return, GSTR-3 to calculate the ITC claims. These forms were also meant to ensure that ITC could only be claimed by the purchaser if the supplier has deposited the required amount of tax at its end.

However, because of the complexity of the system and snags in the GSTN, forms GSTR-2 and GSTR-3 have been suspended till further notice.

Instead of GSTR-3, businesses can continue to file GSTR-3B**.** GSTR-3B was initially introduced to ease the changeover for businesses from the previous tax system to the GST system, but its use has now been extended to September 2018. GSTR-3B is simpler compared to GSTR-3, as it does not require a comparison of invoices between supplier and purchaser.

This means that the system of invoice matching, critical for curbing tax evasion, is not yet in place.

The number of returns to be filed is much lesser for those opting for the composition scheme. Such enterprises need to file two returns – one quarterly and an annual return.

Changes to be brought in for return filing:

In the 28th GSTC meeting held in July 2018, decision has been taken to reduce the burden of complicated return filing that exists so far.

The new system will take six months to one year to be fully functional. As per the announcement by the government on December 4, 2018, the new and simplified GST return forms will roll-out from April 1, 2019.[11]

- The changes being envisaged are: Enterprises with annual turnover up to Rs. 5 crores can opt to file GST return on a quarterly basis.
- Enterprises with annual turnover over Rs. 5 crores, have to file monthly returns.
- Only suppliers need to upload invoices on GSTN. The buyer shall be eligible to avail credit on the basis of such uploaded invoices.

- **Penalty for not filing returns on time**

Not filing returns as well as not filing them on time come with a large penalty.

If returns are not filed within time, the registered enterprises will have to pay:

- A late fees, and
- Interest of 18 per cent on the outstanding amount of tax.

Late fee for different types of returns including GSTR-1 and GSTR-3B are:

- Rs. 50 per day of delay
- Rs. 20 per day of delay for nil returns.

[11] Financial Express (Online) (2018): "GST returns update: Date announced for roll-out of new, simplified form; here's all you need to know", December 4, available at https://www.financialexpress.com/economy/gst-returns-update-date-announced-for-roll-out-of-new-simplified-form-heres-all-you-need-to know/1402984/lite/#referrer=https%3A%2F%2F www.google.com&_tf=From%20%251%24s

ANTI-PROFITEERING PROVISION

Briefly

The provision of tax credit/refund across the entire value chain is expected to reduce costs and hence prices.

To ensure that businesses actually pass on the benefits to the consumers, Anti-profiteering provision has been introduced in GST.

But this too has its own challenges.

It is expected that eventually GST, along with the provision of input tax credit, will reduce costs and consequently bring down prices. However, experiences in other countries show that for a short time after the introduction of GST, inflationary pressures have increased. This has happened despite GST providing the benefit of input tax credit. In order to avoid this situation, GST in India has brought in an important provision – the Anti-profiteering provision- so as to prevent businesses and traders from making excessive profits due to GST. Under the Anti-profiteering provision of GST, an authority is to be set up to examine whether input tax credits have been passed on to consumers in the form of commensurate reduction in price.

Meaning of 'profiteering'

In the context of GST, profiteering is said to occur when businesses and traders do not pass on the benefits of either higher input tax credit or reduced tax rate to the consumers. Not passing on the benefits help them to increase their profit unduly and at the cost of consumers.

Anti-profiteering bodies and its processes

To ensure that the benefits accruing due to introduction of GST are duly shared with consumers in the form of reduced prices, an anti-profiteering body has been set up under GST. The National Anti-Profiteering Authority (NAA) is the apex body mandated to ensure that the benefits of GST rate reduction are passed on to consumers. NAA was constituted in November 2017 for a two-year period.

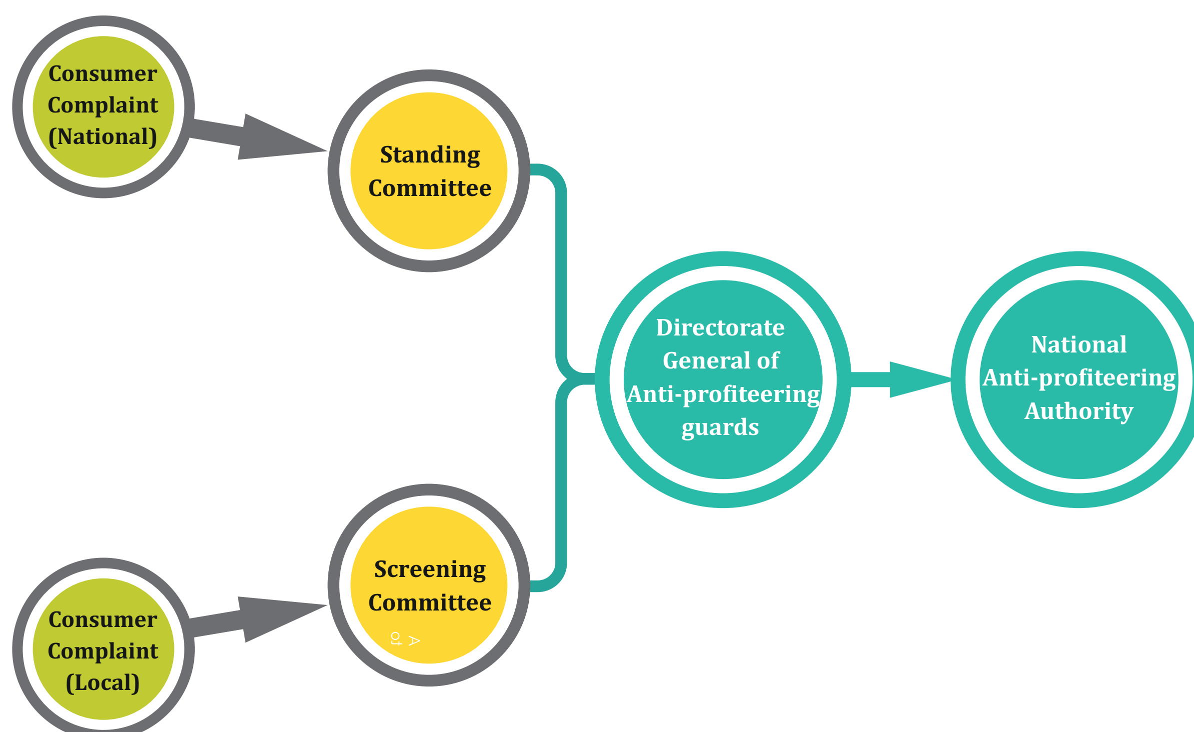
The NAA can act on complaints from consumers if companies/tradersdo not reduce prices for products on which GST rate has been reduced.

Consumers can file complaints if they find that, say, a super-market is selling products at a higher price stating that it is due to GST. Consumers can also file complaints if they have proof that tax rate on a certain product has reduced but it is being sold at the old price.

The mechanism of identifying profiteers involves a three-stage process:

- Complaints of local nature are to be first sent to the State-level 'Screening Committee', while those of national level will be marked for the 'Standing Committee.'
- In case the complaints have merit, the respective committees would refer the cases for further investigation to the Directorate General of Anti-profiteering. The Directorate General of Anti-profiteering then would conduct the investigation within a stipulated period of three months and send its report to the National Anti-profiteering Authority (NAA).

Figure 5: Anti-profiteering bodies



- If the NAA finds that a company has not passed on GST benefits, it can take a number of steps, such as:
  - Direct the business to pass on the benefits to consumers;
  - Ask the company to transfer the amount to the 'consumer welfare fund' within a specified timeline in case the beneficiary cannot be identified;
  - Direct the company to return the undue profit earned (from not passing on the reduction in incidence of tax to consumers) along with an 18 per cent interest, and also impose penalty;
  - Cancel registration of any entity or business if it fails to pass on to consumers the benefit of lower taxes under the GST regime.

Possible Challenges

The main challenges in implementing the anti-profiteering tool will be correctly measuring and identifying profiteers. Another challenge will be to ensure that profiteers are penalised within a short time frame, so that consumers do not have to bear the brunt of inflation.

When it comes to rules, there are no clear cut guidelines as to what is meant by commensurate reduction in price.[12]

Also, as there are several factors that can influence the price and taxes are only one of such factors, it might be challenging to isolate the impact of GST on prices. For instance, a rise in the cost of raw material can lead to rise in prices, even if GST rates remain unchanged or are reduced.

[12] Ghosh, Sujit, Sudipta Bhattacharjee and Abhishek Garg (2017), "Challenges in Implementation of GST", Aarthika Charche, FPI Journal of Economics & Governance, Vol. 2 No.1, January to June, pp. 61-64.

THE E-WAY BILL

Briefly

The E-way bill is an electronic permit required for inter-state and intra-state transport of goods in motorised vehicles.

E-way bill is mandatory for all inter-state and within-states transport of goods valued above a certain amount.

What is e-way bill and how does it work?

E-way bill is an electronic permit required under GST for inter-state and intra-state transport of goods in motorised vehicles. It can be generated from the GSTN by any of the registered parties to a transaction - the supplier, the recipient or the transporter- before the movement of goods begins. Alternatively, e-way bill can also be generated through SMS, Android Application, etc.

Tax invoice/delivery challan/bill of supply related to the supply of goods need to be provided, along with details of the transporter and the mode of transportation for generating e-way bill.

After an e-way bill is generated a unique e-way bill number (EBN) is allocated and is made available to the supplier, recipient, and the transporter.

The validity of the e-way bill varies depending on the distance that the goods have to travel. Typically, the bill's validity is one day for every 100 kilometers of movement of goods.

When is it needed?

- E-way bill is mandatory for all inter-state transport of goods valued above Rs. 50,000, beginning from April 1, 2018. The limit of Rs 50,000 is applicable to individual consignments in a conveyance, and not to the total value of consignment in a conveyance. This means when multiple consignments are being transported together in a conveyance, e-way bill is necessary only if the value of any individual consignment exceeds Rs. 50,000. Value of exempted goods will not be included in the calculation of the Rs. 50,000 limit.
- E-way bill has been made mandatory for intra-state movement of goods as well beginning from April 15, 2018. This has been done in a phased manner with almost all States and Union Territories having implemented it by the end of June 2018. The limit beyond which an e-way bill is necessary is different from Rs 50,000 for some Sates, such as West Bengal, Tamil Nadu.
- In certain specified cases the e-way bill is mandatory even if the individual value of the goods being transported is less than Rs. 50,000. These include:
    - Inter-state movement of goods between the Principal and the Job-worker (i.e. the person who undertakes any process or treatment on goods belonging to the Principal - the registered taxable entity)
    - Inter-state movement of handicraft goods by a dealer exempted from GST registration

When it is not needed?

- For transportation of perishable items such as meat, milk and milk products and fruits and vegetables, e-way bill is not required. Similarly, it is also not required for transportation of gold and silver jewellery, cooking gas cylinders, raw silk, wool and handlooms.
- If the mode of transport is not motorised vehicle.

How can it help in reducing tax-evasion?

The e-way bill is being seen as a key anti-tax evasion measure. Tax authorities believe its implementation will dissuade tax evaders from under reporting transactions.

The way it will work is that every e-way bill generated by a sender or buyer of goods will be automatically updated in the outward sales return of the supplier. This way there will be very little scope for tax evasions as it will help check instances where the entire transaction is not recorded due to connivance/collusion between the seller and buyer. In the earlier tax regime, tax officials had to manually cross-check the way bill with the tax returns filed, to verify if all the consignments came within the tax net.

Section - III

Analysing

GST

KEY DIFFERENCES OF THE CURRENT GST ACT FROM THE BILLS INTRODUCED IN 2011 AND IN 2014

Briefly

GST in India has a long history with different governments making attempts to introduce GST.

The Constitutional Amendment Bills were introduced in 2011, 2014 and finally passed to become as Constitution Amendment Act in 2016, with several changes made over the years.

GST in India has a long history with different governments making attempts to introduce GST.

The NDA government in 2000 first propounded the idea of GST

But it wasn't until 2006, when serious attempts were made in this direction. In 2006, the Finance minister of the UPA government in his budget speech called for the implementation of GST and proposed that GST be introduced in 2010.

Subsequently, in 2011, the GST Bill (115th Constitutional Amendment Bill) was tabled in the Lok Sabha. However, due to the lack of consensus over various aspects of the proposed Bill, it was not passed. As a result the result the legislation lapsed with the dissolution of the 15thLok Sabha in 2013.[13]

In December 2014, the NDA government introduced the Constitutional (122nd Amendment) Bill in the parliament.

[13] "GST Bill: How the tax reform advanced through the years" (2015), The Indian Express, August 11, available at http://indianexpress.com/article/business/economy/gst-bill-how-the-tax-reform-advanced-through-the-years

In August **2016,** the bill was passed with some changes in the 2014 Bill. Consequently, the President gave his assent to the Bill in September 2016, enacting the 101st Constitutional Amendment Act (2016).[14]

The 2016 Act has three key differences to the 2011 and 2014 Bills. They relate to:

- Additional tax up to 1 per cent on interstate trade: The proposal to impose 1 per cent additional GST on inter-state movement of goods, which was not there in the 2011 Bill, was introduced in the 2014 Bill. This was brought in mainly to replace the previous CST so that producing States do not lose revenue after implementation of GST. But as this would have resulted in substantial cascading of taxes, it was dropped in the 2016 Act.
- Compensation to States: The difference between the 2014 Bill and the 2016 Act with regard to compensation to States was that the former did not make it mandatory for the Parliament to compensate States but only stated that it may do so. The 2016 Bill however made it mandatory for the Union government to provide compensation to States for any loss of revenues. The period for which such compensation is to be provided is up to five years from the date of implementation of GST.
- Dispute resolution: The 2011 Bill provided for an independent GST Dispute Settlement Authority (GSTDSA) to be headed by a retired judge. The jurisdiction of this independent constitutional institution was limited to adjucating any dispute or complaint by the Central or State government only if there were deviations from any of the recommendations' of the GST Council which 'results in a loss of revenue' for the Central or State government or 'affects the harmonised structure'. This structure, in which executive and judicial bodies (such as the GSTDSA) were to determine tax rates, was seen as something that could impinge on the rights of legislatures. The proposal for an independent body such as the GSTDSA was dropped in the 2014 Bill and the only thing that remained was that the GST Council may decide on the modalities to resolve disputes. The 2016 Act makes the dispute resolution more definitive by providing for a standing mechanism to resolve disputes between: (a) the Centre vs. one or more States; (b) the Centre and States vs. one or more States; (c) State vs. State.

[14] Times of India (2016): "President Pranab Mukherjee gives assent to Constitution Amendment Bill on GST" (2016, The Times of India), available at https://timesofindia.indiatimes.com/india/President-Pranab-Mukherjee-gives-assent-to-Constitution-Amendment-Bill-on-GST/articleshow/54193004

Other aspects which have undergone some changes over the years are given in the table below.

Table 6: Other Changes in the 2011, 2014 Bills and 2016 Act

115th Constitutional Amendment Bill (2011)	122nd Constitutional Amendment Bill (2014)	Constitutional Amendment Act (2016)
Exempt goods include: Five petroleum and its products (crude, high speed diesel, natural gas, aero turbine fuels) and alcohol	Exempt goods only include alcohol. However, the 5 petroleum products (mentioned in the older bill) have been exempted for the time being.	Clause (12) of the Act says "The Goods and Services Tax Council shall recommend the date on which the goods and services tax be levied on petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel”
GSTC required the 'consensus' of all members present at the meeting	GSTC requires approval of 75% present at the meeting	Same as 2014 bill
Quorum of the GSTC set at 1/3rd of the members	Quorum of the GSTC set at 1/2 of the members	Same as 2014 bill

ISSUES RELATED TO DESIGN OF GST

Briefly

Having multiple rates does make GST complex.

At the same time multi-rate structure is needed to keep a check on prices of goods and services, especially those consumed by the poor.

The goods that remain outside the ambit of GST are major sources of revenue. But keeping them outside GST can have several negative ramifications.

1. Multi-rate structure of GST

One of the main aims of GST is to simplify the indirect tax system and hence the idea of subsuming multiple taxes (and tax rates) and cesses that existed in the previous indirect tax system. According to some experts, an 'ideal' GST should have only one or two rates, apart from a zero rate, and very few exemptions. A number of developed countries have a single or a small number of GST rates. India, however, has adopted a GST model with multiple tax rates for different categories of goods and services.

As we saw earlier, there are as many as seven GST slabs/rates that are to be levied on different categories of goods and services. In addition to these, cesses are to be levied over and above the peak rate on certain goods such as tobacco and related products, aerated beverages, luxury cars etc.

Having multiple tax brackets can have several disadvantages:

- The tax system becomes more complicated, diluting the objective of GST to simplify taxation, at least to some extent. For instance, textiles and fabrics are taxed at 5 per cent under GST but yarn is taxed at 18 per cent. As a result, textile manufacturers do not have clarity on how to price their products. [15]
- Increases cost of compliance and tax administration: Having so many tax rates also increases compliance burden for those who have to deposit taxes as well as administrative cost.
- It opens up the possibility of classification disputes as well as leave scope for tax evasion. For certain goods, the tax rate to be applied is decided based on the end-use of the good. For example, fertilizer is taxed at 5 per cent if used for agriculture and 18 per cent if used for anything else. As tax experts note, this can give rise to tax evasion as it is not possible to check the end use even when written declaration are taken from buyers regarding the end use.[16] In most such cases, there can be a tendency to classify the product such that it comes in the lower tax bracket in order to avoid paying high taxes.

This is also the reason why several countries that have adopted GST have a single rate structure of GST.

But multi-rate GST structure seems to have been adopted in order to:

- Protect existing government (both Central and State) revenue; and
- Keep a check on prices of goods and services.

For instance, adopting a low single rate or few low rates might have led to a significant decline in revenues compared to earlier. The alternative – of levying one or two high tax rates on all goods - might have helped garner revenue. But one or two high tax rates on all goods would have increased tax on a large number of mass consumption goods, pushing up prices.

For example, a steep increase in the GST rate for food items, which attracted a lower rate of tax earlier, would have had adverse effect on most household budgets. Given that GST is an indirect tax this would have adversely affected the poor most. Therefore, considerations of protecting government revenue as well as protecting the interest of consumers, especially the poor, seem to have led to a multi-rate structure of GST.

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[15] Anand, Nupur (2017), "The Modi government's "good and simple tax" has become a confusing mess", QuartzIndia, October 24, available at https://qz.com/1109003/gst-the-modi-governments-good-and-simple-tax-has-become-a-confusing-mess

[16] Dave, Sachin (2017), "Ambiguity remains for several products under GST", Economic Times, December 25, available at : //economictimes.indiatimes.com/articleshow/62235848.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

The revenue considerations explain why nearly 60 per cent of all goods under GST fall in the either 12 per cent or 18 per cent rate brackets. Keeping inflation at bay, on the other hand explains why both the 0 per cent and 5 per cent bracket exist and why 30 per cent of the CPI basket and essential services are exempt.

2. Crucial goods that remain outside the ambit of GST

As mentioned earlier, a number of crucial goods such as petrol, diesel, crude oil, natural gas, aviation fuel, electricity, potable alcohol and real estate, are currently outside GST. All these will continue to be covered by Central Excise Duty and State VAT as long as they remain outside the ambit of GST.

This means that the tax rates can be changed more easily, as, unlike GST, consent is not needed from a large number of State finance ministers.

But keeping these outside GST can dilute several purported benefits of GST. Some of the possible negative repercussions that can arise are:

- For instance, petroleum products are what is known as "universal intermediaries", as they affect costs of all goods and services either because these need to be transported or because petroleum products come in as direct inputs. Therefore, if taxes, such as excise duty or State VAT, on these are increased in order to raise revenue (as has been happening), it can lead to an increase in prices of all other goods and services.
- As the benefit of ITC will not be available for goods kept outside the ambit of GST, taxes paid on them will remain embedded in goods and services whenever these are used as inputs. That in turn means that the cascading effect of taxes will continue.
- Real estate is a known generator of black money. So keeping it out of the purview of GST means that the possibility of reducing suspicious transactions will be that much less.

POSSIBLE IMPACTS OF GST

Briefly

The impact of GST is likely to be different for various stakeholders and cannot be predicted accurately.

GST is likely to significantly reduce the power of the States in deciding their taxes and respective fiscal policy.

Economic Growth

It is speculated that GST will help in improving the ease of doing business in India as it harmonises taxes, reduces cascading effect of taxation and increases tax compliance (based on the a robust IT system that GSTN offers). All of this is expected to attract further investments (domestic as well as foreign) and consequently catalyse economic growth.

Several empirical analyses (based on data of countries that have implemented GST) show that GST does not have a high positive correlation with economic growth in developing countries.[17]

It may however be difficult to accurately predict the effect of GST on the Indian economy as experiences with GST have varied across economies. Each country's experience is a function of its economic reality and the GST model implemented. Canada, for instance, did not see economic growth with five different standard rates and cascading of tax still continuing in two States (Quebec and Prince Edward Island).[18]

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[17] Hakim, Karia, Bujang (2016), "Does goods and services tax stimulate economic growth? International evidence" Journal of Business and Retail Management Research (JBRMR), Vol. 10, Issue 3, pp. 137-146, July

[18] Baheti, Manoj, Siddhartha Sanyal, Sandeep Gupta (2009) "GST: The Next Big reform" Edelweiss Securities Limited, August 21, available at http://www.edelresearch.com/showreportpdf-13567/GST-AUG-09-EDEL

In short, the other view is that tax reforms by itself cannot act as a magic bullet and increase economic growth. GST should be supplemented by efforts to increase consumption. In the case of India, given that the move of demonetisation has drastically reduced consumption, there is a view that GST may not be able to bring a huge impact to economic growth unless the effects of demonetisation on consumption are reversed.

2. Prices of goods and services

The implementation of GST shall increase the prices of some goods while decrease that of others. In effect, GST shall affect different goods and services differently.

The impact of GST on consumers will depend significantly on:

- **How tax rates differ from the present rates**

  For consumers, GST may be a mixed bag in terms of the impact it has on prices of goods. A number of basic consumption goods such as unbranded food products, like food grains, pulses, fruits, vegetable, etc. along with education and health care services, have been kept in the zero tax bracket with other items being placed at tax rates of 5 per cent, 12 per cent and 18 per cent and 28 per cent. Thus, taxes may be lower for some goods and for some others it might go up.

  When it comes to services, which form a large chunk of GDP, since tax on several services is set to rise their prices may also go up.

- **Whether tax revenue remains the same or changes**

  As mentioned above, prices of individual goods can change either way; that of some may increase, while that of others may decline.

  However, what happens to the overall price level depends on whether tax revenue collected from GST (as a percentage of GDP), changes compared to what was collected earlier. If tax collected from GST remains the same (compared to what was collected from the taxes that have been subsumed under GST), then the average price level is unlikely to change. In fact, the moves to bring more goods and/or services under the tax net, and increase compliance, are to ensure that tax revenue does not decline drastically because of introduction of GST. What this means is that even if cascading effect is reduced, prices are unlikely to come down, as long as tax collected from GST remains unchanged compared to what was collected earlier. In fact, as several economists have pointed out, the average price level may even increase under the GST regime.[19]

- **Whether costs/prices of products left out of the ambit of GST increase**

  Another aspect to be taken into account is the price implication of keeping several

[19] See, Das, S. (2017), "Some Concerns Regarding the Goods and Services Tax", Economic and Political Weekly, Vol.52, Issue No. 9, March 4 and Kumar, Arun (2015), "Macroeconomic Aspects of Goods and Services Tax", Economic and Political Weekly, Vol.50, Issue No. 29, July 18

petroleum products (which act as universal intermediates), electricity, out of the purview of GST. For example, in the case of the final output of petroleum products which are out of the GST, the amount of GST that petroleum companies will pay on their inputs (such as hiring of rigs and purchase of equipment and services for crude oil production and refining) cannot be offset against the tax levied on the final products. Any increase in cost of these industries will be passed on to the consumers and hence can pose an inflationary threat.

3. Impact on businesses

It is expected that GST will increase compliance and a number of businesses, which were earlier outside the tax net, will now come under the tax net.

In terms of the impact of GST, there are some challenges that are common to businesses of all types. Major challenges include:

- The process of filing returns or correcting them on the GSTN portal being beset with technical problems,
- Working capital getting blocked because of refunds of ITC getting delayed;
- Problems in keeping track of frequent rate changes by the government and incorporating these in their internal systems in a timely manner. [20]

Other than these, the impact of GST may be very different for big business houses on the one hand and small and marginal enterprises on the other.

For *big businesses,* the move to a uniform tax rate can help:

- Make the supply chain more efficient;
- Reduce transportation time and hence costs for inter-state movement of goods and services; and

For other *small businesses (many of which are in the informal sector),* the GST provides the benefit of not having to pay taxes under GST if their annual turnover is less than Rs. 20 lakhs (Rs. 10 lakhs in case of some States). This is to help small businesses avoid the challenges of having to file regular returns, maintain invoices and others documents.

However, there is still a possibility of small businesses facing other challenges:

- A number of small manufacturing units, which were earlier exempt from paying Excise duty will now have to register for GST and pay taxes if their annual turnover exceeds the threshold set under GST. *This implies an increase in the taxation of small enterprises, including those in the informal sector, which in turn can take away their competitive edge over bigger enterprise and even make them unviable.*

[20] Jain, Mayank (2017), "Interview: Capital block, slow refunds, ambiguities in law among major GST hiccups, says tax expert", October, 3, scroll.in, available at https://scroll.in/article/852207/interview-capital-block-slow-refunds-ambiguities-in-law-among-major-gst-hiccups-says-tax-expert

- Small firms (those below the threshold) may be pushed to register under GST by their clients. This is because clients of small firms will not be able to get ITC for supplies made by firms which do not register themselves on the GST Network.
- The likelihood of this happening increases because of the new clause – the Reverse Charge Mechanism (RCM). On the face of it, RCM seems to shift the burden of taxation from small enterprises with limited resources to large companies with enough resources. But in reality, larger firms might not be ready to bear the tax burden and hence this can act as an additional factor for pushing small firms to register or lose business completely.
- Confirming to the compliance requirements under GST – depositing the required taxes, hiring people to file returns periodically, the need to use information technology, etc. – can increase their costs and even make many of them unviable.
- In fact, the cost of compliance of GST, such as the number of returns to be filed, the fees for tax accountants, do not change proportionately as the size of a firm / enterprise increases. Since these costs are more in the nature of being fixed costs, "the burden of such costs is greater on the small producer".[21]

4. Government Revenue

There is no uniform view regarding the likely impact of GST on government revenue. One view is that many State governments are likely to face a reduction in tax revenue post implementation of GST. The other view suggests that GST may actually increase total tax revenue, including that of the States.

The latter view is based on the expectation that compliance is likely to improve under GST as each transaction will have to be uploaded online to avail the benefit of ITC. The chain of tax credits, in turn, would make it difficult to conceal all transactions. Also, it is believed that businesses/dealers/retailers will have fewer incentives to evade taxes as they know that they can offset the tax paid at one stage in the next stage. This should then help bring more number of people/enterprises in the tax net, including those that were not paying taxes earlier. The combination of improved compliance and a larger number of people/enterprises coming in the tax net is expected to improve revenues.

For the Central government, doing away with specific cesses such as the *Swachh Bharat cess, Krishi Kalyan cess* (a major chunk of which is imposed and collected from services), could result in a significant loss of revenue from these sources. At the same time, it will now get access to a part of the indirect tax revenue generated by States.

For State governments there were some genuine concerns about losing revenue under GST, especially for States like Gujarat, Maharashtra which earned a lot of revenue from

[21] Patnaik, Prabhat (2017), "GST Regime Targets 'Informal Sector' to Centralize Political Authority and Control", October, 9, TheCitizen, available at http://www.thecitizen.in/index.php/en/NewsDetail/index/4/11943/GST-Regime-Targets-Informal-Sector-to-Centralize-Political-Authority-And-Capital

Central Sales Tax – which was an origin based tax. But since GST is a destination-based tax, the revenue earned on inter-state movement of goods and services goes to the State where the final sale happens. As a result, there are apprehensions that producing States from where goods and services originate could lose revenue. So, unlike earlier, whereby Maharashtra would earn the tax revenue for goods produced in Maharashtra, under the GST regime Bihar will earn the tax revenue if the final consumption takes place in Bihar.

It is, however, not clear, how much the States such as Bihar, Uttar Pradesh, that are net consumers (that is they import goods and services from other States more than they export) stand to gain. This is because producing States are also more prosperous because of more economic activity and generally have higher levels of consumption as well. By the same logic, poorer States with lower purchasing power are likely to have lower levels of consumption; hence the gain in tax revenue may not be much.

At the same time, the producing States will now also get to tax services, which they could not earlier. Since consumption of services increases with purchasing power, the better-off States may gain more than poorer States.

5. Impact on the federal structure of India

Federalism is an essential element of Indian polity. GST could significantly reduce the power of the States in deciding on their respective fiscal policy.

The GST can in fact impact fiscal federal relations in the country in different ways. One view is that the GST brings about a fundamental reordering of fiscal federal relations of India to one of cooperative federalism. On one hand both the Centre and the States have had to give up their exclusive domain of taxation. On the other hand, both have gained access to some taxes that they did not have earlier. Also, the structure of the GST Council is such that States, which have a two-thirds vote share in the Council, are critical partners in decision making. While the Centre has the veto power with one-third vote share, it would still need the support of a number of States to reach a three-fourths majority needed for passing through a decision. So, constitutionally, the Centre and the States are evenly matched as one cannot take any decision without the support of the other.

The other view is that GST, in particular the feature of having a uniform tax rate across the whole country, reduces the autonomy of the States to tax as they like in order to meet the specific revenue needs of their States, without prior approval of the GST Council. The current structure of the GST Council (as proposed in the 101st Constitutional amendment act) is such that the Centre has 33.33 per cent of votes, while all the States together have 66.67 per cent of votes and a decision requires the approval of 75 per cent of the members present.

The share of votes between the States and the Centre is such that even if all the States come together on any particular issue, the Centre would have the power to veto its decision. The Centre, on the other hand, requires the approval of only 19 States alongside its own to pass its decision (considering that all the members of the GST council are present).[22]

Although the States shall have a significant say in the GST council, as eminent economist, Prabhat Patnaik argues "the very fact of an elected State government having to petition the GST council ... for pursuing a fiscal strategy of its choice, is itself a constriction of democracy."[23]

6. More focus on regressive taxation

India has a tax-GDP ratio of around 17 per cent which is way below the averages of emerging market economies (21 per cent) and the Organisation for Economic Co-operation and Development (OECD) countries (34 per cent). GST is part of an attempt to increase this ratio by increasing indirect taxes.

A concern regarding greater focus on indirect taxes is its regressive nature. Taxes that impose a proportionately greater burden (in relation to their consumption or income) on the lower income groups than on the upper income groups are described as being regressive taxes. Indirect taxes, therefore, are generally considered to be regressive since the rich and the poor are subject to the same tax rate for similar goods they consume.

That indirect taxes like GST generally have better tax compliance and are easier to administer (because producers/ sellers do not mind paying the tax which will eventually be passed on to the consumer) only heightens the concern.

These concerns are reiterated by Allam, A Sarvar (2016) "taxation should not be a hindrance to business, but the objective of tax reform cannot be confined to the demands of business alone. Tax reform is an important aspect of public finance management, as taxation is used as an instrument of attaining certain social objectives, namely, redistribution of wealth and thereby reduction of inequalities."[24]

Thus, there is a strong cause for reforming direct tax system, in tandem with indirect tax reform like GST, so as to increase the proportion of direct tax revenue.

[22] $(19 \times 2.298) + 33.33 = 75.05$
[23] Patnaik, Prabhat (2016), "The Debate on GST", People's Democracy, August 16 edition
[24] Allam, A Sarvar (2016), "GST and the States: Sharing Tax Administration", Economic and Political Weekly, Vol.51, Issue No. 31, July 30.

APPENDIX

For a long time, India's indirect tax system had been considered to be very complex. This was largely because multiple taxes were levied on products at different stages of the production and supply chain. For instance, taxes were levied beginning from the stage of manufacturing, then on distribution and sale of goods, on services, and then on movement of goods from one State to another and so on. Some of these taxes were levied by the Central government and others by States and local bodies. The system of indirect tax regime that existed was not only complex, it also led to the problem of cascading of taxes - whereby an item was taxed repeatedly from the production to the final retail sales stage. As a result, the tax burden increased manifold and also impacted cost of goods and services.

Several reforms were brought in to reduce the problem of cascading of taxes. As part of such reforms, the Value Added Tax (VAT) was introduced, at different points in time, at the level of both the Centre and States. As mentioned above, the idea behind introducing VAT was that taxes would be levied only on the "value added" at each stage of the supply chain instead of the whole value of the output. This was expected to reduce the problem of cascading of taxes.

In 1978, the Government of India (GOI) suggested that India should go for manufacturing VAT (MANVAT) which would be applicable only to the manufacturing sector. But even this was not feasible since the manufacturing sector also had a large unorganised sector. Later on, in 1986 modified VAT(MODVAT) was implemented. It was initiated for those sectors of manufacturing which purchased largely from within the large-scale sector. This net was expanded over the years to include more and more goods. Services also were brought under tax net.

For States, the sales tax was replaced by the State VAT in 2005.

- **CENVAT, State VAT and Service Tax**

The taxes which were in the nature of VAT prior to GST were mainly, Central VAT (CENVAT) for central excise duties and Service Tax levied by the Centre and State VAT levied by respective State governments on sale of goods within the boundaries of the State.

CENVAT: Modified Value Added Tax (MOD VAT), introduced in 1986 by the Centre, was renamed as CENVAT in 2002. The scheme, applicable on a number of industries, made it possible for manufacturers to avail credit for tax paid on the inputs and utilise such credit for payment of tax on the final products manufactured by them. Central Excise Duty was applicable on manufactures with annual turnover more than Rs. 1.5 crores.

Service Tax: Service Tax was introduced in 1994 and the provision of ITC was brought in 2002. The scheme was initially limited only to credit on input service used in providing

taxable output services. Later on, Cenvat Credit Rules were further amended so that credit of input duties and tax could be extended across goods and services (but this was only up to the stage of production).[25]

State VAT: In 2005, VAT model of tax was introduced in States as well in order to address the problem of overlapping of taxes in sales tax levied by State governments.

But the problems of cascading effect did not go away completely. Also, as mentioned earlier in the Primer, the earlier indirect system also had several other taxes that did not provide the benefit of availing credit for taxes embedded in inputs. Some of these are discussed below.

- **Central Sales Tax (CST) and Entry Tax**

Central Sales Tax (CST): CST was levied when goods were sold across the border of a State. Although it was levied by the Centre, the revenue was collected and kept by the State from where the goods were supplied. CST was therefore an origin based tax. Since no input tax credit was available for CST, it was not possible to 'set off' input tax liability. This resulted in another tax being levied on a product when it was sold across the border of a State.[26]

Entry Tax: Many States also levied entry tax on specified goods when these entered a local area. Again, no ITC was available in case of entry tax.

As a result, cascading of taxes continued. This not only increased the tax component in prices of goods/services, but also resulted in a complex taxation model which was difficult to comply with for firms and administer for the tax department.

Complexity increased further because different States had different taxes (for example some States had Octroi/entry tax which other States did not) and different tax rates (sales tax rates on the same product could vary widely across States). All these increased the cost of production and in supply chain, provided opportunities for tax evasion and generally hampered tax collection.

[25] Service tax (2015), Department of Revenue, Ministry of Finance, GOI, available at: http://dor.gov.in/sites/default/files/service_tax1.pdf, Service Tax at a Glance, http://www.cbic.gov.in/resources//htdocs-servicetax/ovw/ovw1-1_st-ataglance-19may16.pdf (earlier available at: http://www.cbec.gov.in/resources//htdocs-servicetax/ovw/ovw1-1_st-ataglance-19may16.pdf)

[26] http://dor.gov.in/tax/introduction-central-sales-taxes

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