

A Primer on Proposed Tax System on Goods and Services

Part-I: Basic Concept and Framework

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Introduction:

With the release of the First Discussion Paper (FDP) by the Empowered Committee (EC) on the proposed Goods and Services Tax (GST), the country is moving into an era of major tax reform in the arena of indirect taxes. Looking to the title of the paper one would have expected a thread-bare analysis on various aspects of the proposed tax system. However, a major portion of the FDP deals with the historical part viz. individuals and the agencies involved in initiating the idea and the stages through which it has evolved into. An overall impression emerging on its complete reading is that it is more of a loud thinking rather than Discussion Paper as we generally understands. This is for the reason that there are number of issues remaining unanswered. Hence, perhaps for this reason only, it has been titled as “First”. It also implies that few more papers are in the pipe line and, therefore, one should expect few blanks to be filled in.

As can be seen from the FDP, it is a major step in the process of carrying out structural changes in the arena of indirect taxes, affecting allocation of resources amongst the States and the Central Government (CG), imparting discipline amongst the State Governments (SGs), extensive use of technology, extending the tax base by adding substantially large number of dealers within the tax-net, permitting extensive input tax-credit (ITC) etc. For the tax-payer such a change is bound to be confusing and leading to uncertainty. This is for the reason that GST will affect the top-line i.e. sales. Any tax which affects the selling rate is bound to affect the volume of business. Since, GST proposes to add few more taxes, knowledge of intricate part of GST, and devising strategy to cope with the uncertainty, assumes importance. Looking to the broad contour as emerging from FDP, it appears that there will be hardly any dealer who will not get affected by introduction of GST. An attempt has been made in this analysis to explain broad out-line of the proposed GST and its implications. The analysis will consist of three parts viz.

- a) Salient Features and Broad Framework (Part - I)
- b) Mechanism of Input tax Credit (Part – II)
- c) Controversial Issues remaining unanswered (Part – III)

For better understanding, all the parts will be in the form of question and answer. The first part deal with Salient features of GST and its broad framework as follow:

- 1 Basic features
- 2 Measure of Levy
- 3 Chargeability of Tax
- 4 Taxable Event
- 5 Taxable Person
- 6 Definition of Supply of Goods and Services
- 7 Classification of Goods and Services

8	Valuation of Goods and services
9	Rate of Tax
10	Exemptions
11	Computation of Tax Liability
12	Input Tax Credit Mechanism
13	Discharge of Tax Liability
14	Subsuming of existing taxes
15	Inter-State Transactions of GS
16	Export of GS
17	Special Economic Zone and GST
18	Import of Goods under GST
19	Accounting Aspect of GST
20	Preparation for GST
21	Benefits of GST
22	Administrative Work under GST
23	Information Technology Infrastructure
24	Relevance of Knowledge of GST

1.0 Basic Features of GST

1.1 What is GST? How does it work?

GST is a tax on goods and services with comprehensive and continuous chain of set-off benefits from the producer's / service provider's point up to the retailer's level i.e. up to the last level in the chain. It is essentially a tax only on value addition at each stage. The whole structure is devised in such a way that only the final consumer should bear the tax.

1.2 What is the necessity for having the GST?

Justification of Levying GST at Central Level

In the case of Excise (ED), duties paid on the raw material consumed are being permitted as input credit only. For the taxes / duties paid for post-manufacturing expenses, there is no mechanism for input credit under the Central Excise Duty Act. This is for the reason that ED is charged at the stage of manufacture and not subsequent thereto. Under the existing system, there is no tax on the value added in the distribution channel.

Secondly, over a period of time, the CG has started charging Additional ED, Additional Customs Duty, Surcharges etc. for which no input credit is permitted. Thus, these duties have led to charging of VAT on it i.e. tax on tax. In order to remove cascading of taxes it is necessary that there should be only one tax with appropriate mechanism for tax credit.

Thirdly, credit for Service Tax (ST) is being permitted to a manufacturer / service provider to a limited extent. Both ED and ST are levied through different statute. In order to permit credit of ST paid in respect of all the services consumed, it is necessary to have a comprehensive system under which both the goods and services are covered.

Fourthly, a major defect in the existing system is that value for the purpose of computing tax under VAT is cost of goods plus ED paid to the CG. Thus, VAT is charged on the duty paid to the CG. This leads to cascading of taxes i.e. levying tax on taxes. In order to make the GS competitive at the global level, it is necessary that the cascading of taxes be

removed. It can be done only when there is a comprehensive tax system wherein ITC is seamless i.e. a continuous chain of set-off from the original producer's / service provider's point up to the retailer's level.

Fifthly, as on today, ST is levied on restricted items only. There are large numbers of services remaining to be taxed. If the system has to be made comprehensive and ITC to be seamless, it is necessary that the SGs should be empowered to levy tax on services. At present, under the provisions of the Constitution only the CG is permitted to levy tax on services. In order to make the system seamless all the SGs will have to be permitted to levy taxes on services.

Justification for GST at State Level

A major defect under the existing structure of state VAT has been levying of tax on ED paid to the Central Government. This goes against the basic principles of not levying tax on tax. For example, if the cost of goods is Rs. 100 and rate of ED is 10.00%, VAT @ 4.00% will have to be paid of Rs. 4.40 i.e. 4.00% of Rs. 110. It can be seen that Rs. 4.00 is VAT on the value of the goods while Rs 0.40 is VAT on ED.

Secondly, VAT is also being charged in respect of Additional ED, Additional Custom Duty etc. All these have distorted the whole structure and lead to cascading of taxes.

Thirdly, despite having introduced VAT, many of the States have continued with levy of various types of indirect taxes like luxury tax, entertainment tax etc.

Fourthly, despite having introduced VAT, tax is being levied on inter-state transfer of goods. Since no input credit is permitted in respect of CST paid, it has led to additional burden for the dealers. It has hindered the growth of inter-state transactions and led to lots of administrative problems like issue / collection of C / F Form etc.

The solution for the entire problem lies in having a continuous chain of set-off from the original producer's point and service provider's point up to the retailer's level which would eliminate the burden of all cascading effects, including the burden of CENVAT and service tax. With the removal of various indirect taxes levied by the SGs there will be reduction in the multiplicity of taxes bringing down the compliance cost.

With GST, the burden of CST will also be phased out. Under the proposed system, the buyer in importing will be able to claim taxes paid to the dealer in exporting state as input credit.

1.3 How is GST being implemented in various other countries?

There are broadly four models of GST which is being implemented in various countries. They are (i) National GST (ii) State GST (iii) Dual GST (Non-concurrent) and (iv) Dual GST (Concurrent).

In the case of National GST, the tax is levied and collected by the CG. Revenue generated is shared with the SGs as per pre-determined formula. It involves transferring of funds from the CG to the SGs.

In the case of State GST, tax is levied and collected by the SG. It does not involve any transfer of funds from one government to another.

Under the third model tax is levied by both the CG and SGs. However, the CG levies tax on services and the SGs levies the tax on the goods.

Under the fourth model, tax is levied by both the CG and the SGs on the goods and services.

1.4 Which model of GST is being proposed for India?

The proposed GST is as per the fourth model.

1.5 What are the salient features of the proposed GST model?

1) The GST shall have two components: one levied by the Centre i.e. CGST and the other levied by the States i.e. SGST. Rates for CGST and SGST would be prescribed appropriately, reflecting revenue considerations and acceptability.

2) The CGST and the SGST would be applicable to all transactions of GS made for a consideration except the exempted goods and services, goods which are outside the purview of GST and the transactions which are below the prescribed threshold limits.

3) The CGST and SGST will be required to be paid to the accounts of the Centre and the States separately.

4) As the CGST and SGST are to be treated separately, taxes paid against the CGST shall be allowed to be taken as input tax credit (ITC) for the CGST and could be utilized only against the payment of CGST. The same principle will be applicable for the SGST. A taxpayer or exporter would have to maintain separate details in books of account for utilization or refund of credit. Further, the rules for taking and utilization of credit for the CGST and the SGST would be aligned.

5) Cross utilization of ITC between the CGST and the SGST would not be allowed except in the case of inter-State supply of goods and services under the IGST model.

6) Uniform procedure for collection of both CGST and SGST would be prescribed in the respective legislation for CGST and SGST.

7) The administration of the CGST and SGST will rest with the CG and respective SGs. It means that both the CG and SGs would have concurrent jurisdiction for the same transaction.

8) A uniform State GST threshold across States gross annual turnover of Rs.10 lakh both for goods and services for all the States and Union Territories may be adopted. Keeping in view the interest of small traders and small scale industries and to avoid dual control, the threshold for CGST for goods may be kept at Rs.1.5 crore and the threshold for CGST for services may also be appropriately high.

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

10) The taxpayer will be required to submit periodical returns, in common format as far as possible, to both the CGST authority and to the concerned SGST authorities.

11) Each taxpayer will be allotted a PAN-linked taxpayer identification number with a total of 13/15 digits. This would bring the GST PAN-linked system in line with the prevailing PAN-based system for Income tax, facilitating data exchange and taxpayer compliance.

12) Functions such as assessment, enforcement, scrutiny and audit would be undertaken by the authority which is collecting the tax, with information sharing between the Centre and the States.

1.6 How will it be implemented?

It will be implemented through multiple statutes i.e. one for CGST and SGST statute for every State. However, the basic features of law such as chargeability, definition of taxable event and taxable person, measure of levy including valuation provisions, basis of classification etc. would be uniform across these statutes as far as practicable.

1.7 Can India not have single GST?

India is a federal country where both the Centre and the States have been assigned the powers to levy and collect taxes through appropriate legislation. Both the levels of Government have distinct responsibilities to perform according to the division of powers prescribed in the Constitution for which they need to raise resources. A dual GST will, therefore, be in keeping with the Constitutional requirement of fiscal federalism.

1.8 How would a particular transaction of GS be taxed simultaneously under CGST and SGST?

Under the proposed system, GST would be levied simultaneously on every transaction of supply of GS except (i) the exempted goods and services, (ii) goods which are outside the purview of GST and (iii) the transactions which are below the prescribed threshold limits.

2.0 Measure of Levy

2.1 Who will be levying the tax?

Tax will be levied by both the CG and the SGs.

2.2 Will it be concurrent?

Yes. It will be concurrent. It means that the same transaction will be taxed by both the CG and SGs.

3.0 Chargeability of Tax

3.1 Under which statute GST will be levied?

As per the FDP, broadly there will be two statutes under which GST will be levied. Firstly, the CG will be levying GST which will be known as CGST. It will be in replacement of the existing ED and other taxes. Secondly, SGs will be levying GST under respective GST Act. Thus, there will be two parallel statutes governing the tax liability of the same transaction.

3.2 Which items of goods and services will be covered under GST?

All the items of goods and services are proposed to be covered. Exemptions will be granted to few selected items.

3.3 Does it mean that the same transaction of GS will be taxable by both the Central and the SGs?

Yes. The same transaction will be taxed by both the CG and CG. For example, at present, in the case of goods manufactured, a dealer is paying ED and VAT on sale of goods. In the same manner, after introduction of GST, all the traders will be paying both the types of taxes i.e. CGST and SGST.

3.4 At present, VAT is levied on the value which is inclusive of ED. Whether SGST will be levied on CGST as well?

Answer: No. Both the GST would be levied on the same price or value. For sale **within the state**, its structure will look like as follow:

Name of Seller						
Address of Seller						
TIN No.			IGST No.....			
TAX INVOICE (Original / Duplicate / Triplicate)						
Bill Book No:		Bill No:		Date:		
Purchaser's Name:						
Purchaser's Address:						
Purchaser's TIN No.						
Sr. No.	Description of Goods Sold	HSN Code	Qty.	Unit	Rate Rs.	Total Rs.
	ABXCD	xxxxxx	100	Nos.	10	1,000
					Total	1,000
Add: Central GST @ 4.00%			On Rs.		1,000	40

	Add: State GST @ 4.00%	On Rs.	1,000	40
			Total	1080
(Rupees One thousand eighty only)		Signature of Authorised Person		

For sale outside the state, its structure will look like as follow:

Name of Seller						
Address of Seller						
TIN No.			IGST No.....			
TAX INVOICE (Original / Duplicate / Triplicate)						
Bill Book No:		Bill No:		Date:		
Purchaser's Name:						
Purchaser's Address:						
Purchaser's TIN No.						
Sr. No.	Description of Goods Sold	HSN Code	Qty.	Unit	Rate Rs.	Total Rs.
	ABXCD	xxxxxx	100	Nos.	10	1,000
					Total	1,000
Add: IGST @ 8.00%			On Rs.	1,000		80
				Total		1080
(Rupees One thousand eighty only)			Signature of Authorised Person			

In respect of goods **exported**, it will look like as follow:

Name of Seller						
Address of Seller						
TIN No.			IGST No.....			
TAX INVOICE (Original / Duplicate / Triplicate)						
Bill Book No:		Bill No:		Date:		
Purchaser's Name:						
Purchaser's Address:						
Sr. No.	Description of Goods Sold	HSN Code	Qty.	Unit	Rate Rs.	Total Rs.
	ABXCD	xxxxxx	100	Nos.	10	1,000
					Total	1,000
Add: IGST @ 0.00%			On Rs.	1,000		0

				Total	1,000
(Rupees One thousand only)					
			Signature of Authorised Person		

4.0 Taxable Event (TE)

4.1 *At what point of time the tax will be levied?*

At present, ED is levied at the point of manufacture and VAT is paid at the time of transfer of property in goods to the buyer. Since, the CG proposes to levy tax on the value added in the entire distribution channel, the TE will have to be beyond the stage of manufacturing. Secondly, under the existing system, since VAT is levied on transfer of property, no tax is required to be paid on transfer of goods to the branch. This results into lots of administrative hassles and disputes. Therefore, the best solution appears to be levy of tax on supply of goods rather than on transfer of property in the goods. Since, each branch / depot will be taxable entity, and with the proposed seamless process of ITC, it will be easier to levy tax on supply of goods rather than transfer of property. However, the FDP is silent on this aspect and we will have to wait till the bill is released for discussion.

4.2 *Will TE cover both i.e. supply of goods and rendering of services?*

Yes. The definition of TE will cover both the type transactions under a single statute.

4.3 *What will be the nature of TE?*

One can say that it will be combination of the definition of sales as defined under local VAT Act and the term "Service". Since the Finance Act does not define the word "service", the TE may cover services in negative terms. It is comparatively easy to define tangible goods. Therefore, services can be defined negatively i.e. one which does not involve supply of goods.

4.4 *Will it not involve new language and terminology?*

Yes. In order to make the statute comprehensive, it will be necessary to employ new terminology. Language of the statute will also get changed totally.

4.5 *What impact the change in TE can have?*

Definition of new TE will expand the tax net substantially, taking in its sweep almost all the commercial transactions taking place in the economy.

4.6 *GST is proposed to be levied by both the CG and SGs. How will it be defined under CGST and SGST?*

The tax proposed is concurrent. Therefore, the definition of TE under CGST and SGST will have to be identical.

5.0 Taxable Person (TP)

5.1 *Who will be liable to pay the tax?*

Since it is proposed to make the whole system comprehensive, it will cover all types of person carrying on business activities, more specifically manufacturer, job-worker, trader, importer, exporter, all types of service providers etc.

5.2 Whether it will cover branches / depots as well?

If the TE is going to be supply of goods, the TP will cover all the branches and depots etc. It means that if a company is having four branches in four different states, all the four branches will be considered as TP under each jurisdiction of SGs. For CGST and IGST also it will be considered as different TP.

5.3 Whether all these types of business entities will be subject to CGST, SGST, IGST and CVD?

Yes. All the dealers / business entities will have to pay both the types of tax on all the transactions. However, in the case of a dealer having turnover below the threshold exemption limit, can opt for exemption and can remain outside the jurisdiction of CGST. Thus, a dealer dealing within the state only and opting for exemption under threshold limit will be TP under SGST.

In the case of a dealer entering into sell / buy goods inter-state, will be taxable person under IGST as well. Thus, he will be TP under three statutes i.e. CGT, SGST and IGST.

In the case of importer, apart from CGST and SGST, the importer will have to pay tax on import of goods as well. So he will be a TP in respect of three statutes viz. CGST, SGST, and CVD.

In the case of an importer importing goods and selling inter-state, will be TP under four statutes viz. CGST, SGST, IGST and for CVD.

5.4 Why should a dealer get himself registered under CGST?

If he does not get registered, he will not be entitled to claim ITC of CGST paid on goods purchased. So, its burden will fall on him. In the case of B2B transaction, a buyer would not like to buy goods from such a dealer as he will not be entitled to claim ITC for such purchases.

5.5 What will happen for an importer of goods? Whether he will have to get himself registered under CGST?

It is proposed to levy tax on import of goods. ITC for the same will be permitted while computing tax liability. Therefore, in the case of B2B transactions, it is necessary for the importer to get registered under CGST and SGST as well.

5.6 What will happen in the case of inter-state transactions? Whether all the dealers will have to get registered under the proposed IGST system?

No. If the dealer is not making any sale / purchase of goods in inter-state, it will not be necessary. However, if he proposes to buy the goods and avail the ITC of the taxes paid, it will be necessary to get registered under IGST. In the same manner, if he proposes to sell the goods inter-state it will be necessary to have registration under IGST. This is for the reason that if the seller is not registered under IGST, the buyer of the goods in the other state will not get ITC for the tax paid under IGST.

6.0 Definition of Supply of Goods and Services

6.1 Which types of goods and services will be covered?

All the goods covered under existing ED and VAT will be covered. In respect of services, its scope may be extended. However, FDP is silent about it.

6.2 When can the goods said to have been supplied or the services rendered?

FDP does not throw any light on this aspect. One will have to wait till the draft bill is released.

7.0 Classification of Goods and Services

7.1 How the goods and services will be classified?

At present, due to large number of rates of taxes, disputes relating to classification have arisen. In order to avoid the same, it is proposed that, broadly, there will be only two types of rates of taxes. As far as services are concerned there will be only one rate. This rate will be applicable to both CGST and SGST. The rate of tax on services will also be aligned with the rate of tax on goods so that the dispute regarding goods and service no longer remains. Apart from that since the ITC will be seamless, there will be no need for abatement in value for certain types of transactions. Therefore, in the case of services classification will also lose significance.

7.2 Whether the classification will remain the same throughout the chain of supply?

Yes. If we look at the sources of goods there are two main sources viz. goods manufactured within the country and the goods imported.

In the case of goods manufactured within the country, source of classification will be invoice issued by the manufacturer. Since the ITC will be permitted on the basis of invoice, classification of goods as declared by the manufacturer in the invoice will continue till the goods are consumed.

As far as goods imported are concerned, under the proposed system, all the goods imported will be bearing duty like Counter Veiling Duty (CVD). In the case of custom duty, Harmonised System is being followed. Classification of goods at the time of import of goods will be followed throughout. This will impart lots of consistency.

8.0 Valuation of Goods and services

8.1 On which value the tax will be levied?

Tax will be levied on the value as declared in the invoice.

8.2 Will the same value be considered for CGST and SGST?

Yes. The same invoice will be containing two different types of taxes viz. CGST and SGST. Value for tax will be the same as shown in the invoice.

8.3 At present, VAT is being computed on value of goods and ED thereon. How the problem of paying tax on tax will be removed?

For the purpose of computing SGST, value of the goods only will be considered. Tax to be paid to CG as CGST will not be included.

8.4 *Whether the existing system of abatement under the Central Excise will continue?*

No. Since, it is proposed to extend the CGST to distribution channel i.e. beyond the point of manufacturing, it will not be necessary to do so. As per the proposal, the process of ITC will be seamless. Hence, the dealer will be able to claim ITC on all the types of expenses incurred for the business rather than keeping it restricted to certain activities as at present.

8.5 *Whether the existing system of abatement in value in certain types of services will continue?*

No. Since the process of ITC will be seamless and being permitted in respect of all the taxes paid, it will not be necessary to do so.

8.6 *Whether the existing system of composition scheme for Works Contract will continue?*

No. Since ITC for tax paid on goods purchased will be permitted, there will not be any need for the same.

9.0 Rate of Tax

9.1 *How many types of the rates will be?*

There will be a two-rate structure – lower rate for necessary items and goods of basic importance and a standard rate for goods in general. There will also be a special rate for precious metals and a list of exempted items.

9.2 *Whether it will be the same under CGST and SGST?*

For CGST relating to goods, the CG will have a two-rate structure, with conformity in the levels of rate under the SGST. For taxation of services, there may be a single rate for both CGST and SGST. The exact value of the SGST and CGST rates, including the rate for services, will be made known duly in course of appropriate legislative actions.

9.3 *What will be the rate structure for IGST?*

It will be total of the rate as applicable under CGST and SGST.

9.4 *What will be the rate structure for CVD?*

It will be total of the rate as applicable under CGST and SGST.

9.5 *What will be the rate of tax for various commodities and services?*

A: The exact rate of tax under SGST and CGST has yet not been finalized. The process of arriving at the revenue neutral rate is still going on. It will take some time.

10.0 Exemption of Goods and Services

10.1 *What is the concept of providing threshold exemption for GST?*

The present threshold limits prescribed in different State VAT Acts below which VAT is not applicable varies from State to State. It is felt that a uniform State GST threshold across States is desirable and, therefore, it is proposed that a threshold of gross annual turnover of Rs. 10 lacs both for goods and services for all the States and Union Territories might be adopted. The EC is considering the threshold for Central GST for

goods at Rs.1.5 Cr. Threshold for services is proposed to be fixed at appropriately high level. The following table will give clear picture:

	Threshold exemption limit under	
	CGST	SGST
Goods / Commodities	Rs. 1.50 cr.	Rs. 10.00 lacs
Services	Not declared so far	Rs. 10.00 lacs

10.2 What is the scope of composition and compounding scheme under GST?

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

10.3 Which items of GS will be exempt?

Keeping the interest of SGs in mind, the exempted list under VAT regime including Goods of Local Importance may be retained in the exempted list under State GST in the initial years.

10.4 Whether the list of items exempt GS under CGST and SGST will be the same?

It may be difficult to do so. However, the CG may follow the same.

10.5 What will happen if a particular type of goods is exempt under one state and is taxable under the other state?

Let us examine this issue from three different perspectives:

CGST: Tax will be levied as per the rate prescribed under CGST.

SGST: Tax will be levied as per the rate prescribed under SGST.

IGST and CVD: It is not clear as to how the rate for IGST and CVD will be determined in such cases as the rate for it is proposed to be total of CGST and SGST.

11.0 Computation of Tax Liability

11.1 How the tax liability will be computed?

Tax liability will be computed with reference to the value as declared in the invoice with the provision for ITC for the taxes paid.

11.2 Whether different types of tax liability will have to be computed separately?

Yes. Tax liability for CGST, SGST and IGST will have to be computed on periodical basis. In the case of CVD, it will have to be paid at the time of import of goods i.e. at the time of making payment of custom duty. Its computation will be for each transaction separately.

12.0 Input Tax Credit Mechanism

12.1 Will the dealer have the option of claiming tax paid under CGST, SGST, IGST or CVD?

Yes. According to FDP, the system will be seamless making it possible for the taxpayer to claim credit for all the taxes paid for purchases made and the expenses incurred for the business.

12.2 Which items will be covered under mechanism of ITC?

FDP states that taxes paid in respect of all the goods purchased and expenses incurred for the business will be considered for ITC.

12.3 Will cross utilization of credits between goods and services be allowed under GST regime?

Cross utilization of credit of CGST between goods and services would be allowed. Similarly, the facility of cross utilization of credit will be available in case of SGST. However, the cross utilization of CGST and SGST would generally not be allowed except in the case of inter-State supply of goods and services under the IGST model.

12.4 All these sound confusing. There are four different types of taxes viz. CGST, SGST, IGST and CVD. There are goods and services on which all these taxes are proposed to be levied. How will the system operate without cross-utilisation?

Let us put the whole issue in tabular format so that complexity of the problem can be realised.

ITC available under		Tax liability arising under							
		CGST liability for		SGST liability for		IGST liability for		CVD liability for	
		G	S	G	S	G	S	G	S
CGST	G	Y	Y	N	N	Y	Y	Liability arising under CVD being such that it will have to be paid at the time of import of GS. However, FDP is silent about it.	
	S	Y	Y	N	N	Y	Y		
SGST	G	N	N	Y	Y	Y	Y		
	S	N	N	Y	Y	Y	Y		
IGST	G	See Note 1 below				Y	Y		
	S					Y	Y		
CVD	G	See Note 2 below				See Note 3 below			
	S					See Note 3 below			

The above Table has been prepared on the basis of the issues emerging from details available from FDP. The idea is to highlight the range and complexities involved herein. The indicators shown above are not final and need to be amended depending on actual provisions under the respective statute for CGST, SGST, IGST and CVD.

Note 1: FDP makes a passing reference of adjustment of ITC under SGST against tax liability arising under IGST. However, it is not clear whether ITC arising under IGST can be adjusted against tax liability arising under CGST. FDP speaks about the rate of tax under IGST being total of the rate of tax under CGST and SGST. It is also not clear how the revenue raised will be shared with the SGs. It is not clear whether identity of tax liability under CGST will be kept separate i.e. not permitting any set-off against tax paid under SGST and IGST.

Note 2: As per FDP tax paid as CVD on import of goods will be permitted as ITC. However, it is not clear in what manner and to what extent. FDP states that the rate of CVD will be combine of the applicable rate of tax under CGST and GST. If that is the case, a part of CVD will have to be shared by CG with the respective SGs. In the alternative payment of CVD has to be split into two parts viz. CVD payable to CG and SG. Under that scenario it will be possible to keep track of ITC in respect of CVD and claiming respective amount against CGST and SGST. However, all these may complicate the whole structure.

Note 3: Whether ITC of CDV paid can be claimed against the tax liability arising under SGST? Ideally speaking there should not be any problem. If the SGs are going to collect / share revenue from CDV there should not be any problem for the same. If ITC arising under purchases made locally can be claimed as ITC against IGST, portion as applicable to SGs under CVD should be permitted as set-off.

12.5 At present, taxes paid on petroleum products are not considered for ITC. What will happen under GST?

No ITC will be permitted for the taxes paid on petroleum products.

12.6 What will happen to tax paid on capital goods?

It appears that ITC will be permitted of the taxes paid on capital goods. However, it may be permitted in a phased manner.

12.7 All the states are following different systems for granting ITC under VAT. In most of the cases, taxes paid on large number of goods purchased and expenses incurred are denied tax credit on one pretext or the other. What will be the scope of ITC under SGST?

Yes, it is true. Many SGs have laid down number of restrictions on availment of ITC of the taxes paid on goods purchased and expenses incurred for the business. Definition of the term tax eligible for input credit, as provided under local VAT law, are restrictive. Even under the Service Tax, tax paid on large number of services is being not considered. This defeats the basic idea of avoiding cascading of taxes.

Unfortunately, the draftsman turns the blind eye to the spirit of the proposed structure as announced by the policy makers. Statutes are drafted in such a way that tax credit is always permitted lower than what has been announced by the policy makers. The administering authority, in order to achieve the revenue collection target and for various other reasons, interpret these statutes in such way that only a small part of the tax paid is permitted as ITC. So for the tax payers availing tax credit to the full extent remains a pipe-dream.

12.8 How will it be claimed?

No detailed procedures are available at present. However, the dealer will have to deduct amount of tax paid on purchases made or expenses incurred at the time of determining periodical tax liability.

12.9 Whether cross-utilisation of ITC will be permitted?

This is a complex issue. Although, FDP explicitly makes it clear that cross utilisation between CGST and SGST will not be permitted. However, in the case of IGST, cross utilisation of CGST and SGST is proposed to be permitted. Apart from that CVD paid will also be permitted to be claimed as tax credit. Its manner of claiming against CGST and SGST is not clear. In fact, there are lots of grey areas herein.

12.10 What will happen to excess ITC accumulated over a period of time? Whether refund of tax will be permitted?

FDP states that in the case of export of goods and services, efforts will be made to ensure that refund of ITC accumulated is granted at an early date. However, there is no clarity about granting of refund in the cases wherein, for certain reasons, ITC gets accumulated over a long period of time or where there are no chances of it being getting adjusted against the tax liability.

13.0 Discharge of Tax Liability

13.1 Different types of taxes viz. CGST, SGST, IGST, CVD are proposed to be levied. What will be the mechanism for discharging of the tax liability?

Since each tax will be levied under different statute, and there being the question of allocation of resources amongst the CG and SGs, it appears that each tax will be required to be paid separately. Apart from that, cross-utilisation of ITC not being made available will also make it necessary to discharge the tax liability separately.

14.0 Subsuming of Existing Taxes

14.1 What will happen to the existing statutes like Central Excise, VAT etc. levying various types of taxes? Will they continue? How will they be dealt with?

There are various Central, State and Local levies which are of the nature of indirect taxes. It is proposed to subsume the same in GST. Following principles have been laid down while configuring the scheme of taxation.

(i) Taxes or levies to be subsumed should be primarily in the nature of indirect taxes, either on the supply of goods or on the supply of services.

(ii) Taxes or levies to be subsumed should be part of the transaction chain which commences with import/ manufacture/ production of goods or provision of services at one end and the consumption of goods and services at the other.

(iii) The subsumation should result in free flow of tax credit in intra and inter-State levels.

(iv) The taxes, levies and fees that are not specifically related to supply of goods & services should not be subsumed under GST.

(v) Revenue fairness for both the Union and the States individually would need to be attempted.

Considering the above, EC is of the view that the following Taxes should be subsumed under the proposed scheme of GST:

	Taxes / Duties to be subsumed under CGST	Taxes / Duties to be subsumed under SGST
1	Central Excise Duty	VAT / Sales tax
2	Additional Excise Duties	Entertainment tax (unless it is levied by the local bodies).
3	The Excise Duty levied under the Medicinal and Toiletries Preparation Act	Luxury tax
4	Service Tax	Taxes on lottery, betting and gambling.
5	Additional Customs Duty, commonly known as Countervailing Duty (CVD)	State Cesses and Surcharges in so far as they relate to supply of goods and services.
6	Special Additional Duty of Customs - 4% (SAD)	Entry tax not in lieu of Octroi.
7	Surcharges, and	
8	Cesses	

15.0 Inter-State Transactions (IST) of GS

15.1 How IST of GS will be treated?

The existing Central Sales Tax Act (CST) will be discontinued. Instead, a new statute known as IGST will come into place. It will empower the CG to levy and collect the tax on the inter-state transfer of the GS.

15.2 What will be mechanism for the same?

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

15.3 What are the advantages of such a system?

According to FDP, following are the major advantages of IGST Mode:

- a) Maintenance of uninterrupted ITC chain on inter-State transactions.
- b) No upfront payment of tax or substantial blockage of funds for the inter-State seller or buyer.
- c) No refund claim in exporting State, as ITC is used up while paying the tax.

d)Self monitoring model.

e)Level of computerization is limited to inter-State dealers and Central and State Governments should be able to computerize their processes expeditiously.

f) As all inter-State dealers will be e-registered and correspondence with them will be by e-mail, the compliance level will improve substantially.

g)Model can take 'Business to Business' as well as 'Business to Consumer' transactions into account

15.4 Who will collect the tax?

As per the FDP, it will be levied and collected by the CG.

15.5 Whether the SGs will get any share in the revenue so collected by the CG?

FDP states that the rate of tax in IGST will be the rate under CGST and SGST. Since, the whole mechanism is proposed on the basis of levying the tax on destination, the SGs exporting the GS will stand to lose substantial revenue. FDP is silent on this aspect.

15.6 Whether the buyer will be able to claim ITC of the taxes paid?

Yes. Buyer of the GS registered under the IGST will be eligible to claim tax paid under IGST.

16.0 Export of GS under GST

16.1 How the export of GS will be treated under GST?

Exports would be zero-rated. In view of this, the question of disallowance of ITC will not arise. ITC accumulated on account of the same can be made use of in respect of the tax liability arising for the local sales. In respect of 100% EoU, accumulated ITC will be permitted as refund.

16.2 How will GST benefit the exporters?

It is expected that the subsuming of major Central and State taxes in GST, complete and comprehensive setoff of input GS and phasing out of Central Sales Tax (CST) would reduce the cost of locally manufactured GS. This will increase the competitiveness of Indian goods and services in the international market and give boost to Indian exports. The uniformity in tax rates and procedures across the country will also go a long way in reducing the compliance cost.

17.0 Special Economic Zone (SEZ) and GST

17.1 How the sale and purchase of GS to and from SEZ will be treated?

As in the case of exports, benefits may be given to Special Economic Zones (SEZs) also. However, such benefits will only be allowed to the processing zones of the SEZs. It means that sales made by units in SEZ to Domestic Tariff Area will be taxable.

18.0 Import of Goods

18.1 *As the taxes are proposed to be levied on the entire distribution channel, how import of GS will be treated?*

It is proposed to levy GST on value of goods imported. Both CGST and SGST will be levied on import of GS into the country. The incidence of tax will follow the destination principle and the tax revenue in case of SGST will accrue to the State where the imported goods and services are consumed. Full and complete set-off will be available on the GST paid on import on GS.

18.2 *Whether this duty will be over and above Custom Duty levied at present?*

Yes. Custom Duty will continue to be levied as at present. GST will be required to be paid additionally on the value of imported GS.

19.0 Accounting Aspects of GST

19.1 *Whether the dealer will have to make any changes in his accounting system?*

Yes. The dealer will have to make various changes in the existing accounting system. For example, since cross-utilisation of ITC is not permitted, track of ITC in respect of each type of tax will have to be kept. In the same manner, periodical tax liability will have to be computed under each types of statute. Since liability is required to be monitored separately, payment of tax will also be required to be made separately under each statute.

20.0 Preparation for GST

20.1 *What preparations are required at the level of CG and SG for implementing GST?*

Both the CG and SGs will have to put-in lot of efforts on various fronts for implementing GST. Some of them are as follow:

- a) Amendments in Existing Statutes
- b) Incorporating new statutes
- c) Tax Collection
- d) Assessment of Tax Liability
- e) Sharing of Revenue between CG and SGs
- f) Exchange of information about Inter-state transactions

20.2 *Looking to the above it appears to be a gigantic task. Whether the Government machinery is in place for such a mammoth changes?*

No. It will require considerable input in terms of man-hours and financial resources to put the whole mechanism into operation.

20.3 *Whether the tax-payers are ready for such a change?*

Barring few enlightened persons in the industry in the large cities, hardly anyone is aware about financial and tax implications involved herein. Hardly, any trader is aware that a new statute on the line of central excise is proposed to be made applicable. Even assuming that the threshold exemption limit is kept at Rs. 1.50 cr., it may not be possible for them to keep out of the tax net for various reasons. Nor it is possible to say anything at this stage as the rate of tax as applicable and administrative work involved is made known. In fact, most of the tax-payers are in the dark about the proposed tax system.

21.0 Benefits of GST

21.1 GST is bound to affect each and every one whether he is a manufacturer, trader, importer, exporter or consumer. It will also affect the revenue of the CG and SGs. What impact it can have on the revenue of the government?

Impact of GST will be manifold. Firstly, since the CGST will be extended to the entire distribution channel, the CG will derive substantial additional revenue.

Secondly, levy of CVD on the GS imported will also boost the revenue.

Thirdly, various GS not covered at present under the existing Service Tax will get taxed under the proposed system.

Fourthly, with the levy of CVD on goods imported, tax will be levied on the value added in the imported traded goods. Since there is no system of tracking of GS imported, substantial amount of value added remains untaxed or get leaked. With the registration of each and every GS, it will be possible to have track of each and GS imported till the last point of distribution channel.

Fifthly, since all the transactions of inter-state transfer are proposed to be monitored electronically, it will be possible to have close monitoring of the same. This may lead to trap the transactions, which remains out of the system.

Sixthly, at present no tax is being paid on transfer of the goods to the branch and the goods sent on consignment basis. With the coverage of both of these types of the transactions, additional revenue should also flow.

Looking to all these aspects, there is no doubt that the tax collections of the CG and SGs will get substantial boost on introduction of GST.

21.2 How can the burden of tax, in general, fall under GST?

Theoretically, on the introduction of GST, the burden of tax on GS should fall. However, this is subject to condition that the rate of tax remains as under the existing system. Since the revenue neutral rate may be higher as compared to the existing rate, total tax burden may not fall.

Secondly, with the extension of the tax to various GS, overall burden of tax will also arise.

It should be remembered that for most of the goods, commodities and services the market is imperfect one. Therefore, any reduction in the tax in the form of ITC will get adjusted by corresponding increase in the price of the GS. This will make it appear that the prices have remained as they were but benefiting the manufacturer, trader etc. in the distribution channel.

21.3 In what respect it will affect the manufacturers and traders?

All those involved in the business right from stage one i.e. manufacture and import of GS till it reaches to the ultimate consumer will get affected. As far as traders are concerned,

there will be manifold impact viz. financially, administratively, business strategy etc. Let us examine each of this one in detail.

Financial Impact:

Depending upon the rate of tax, financial impact will be known. If the rate of tax is higher than the existing rate, financial outflow will be more. Although, ITC will be available for additional amount of tax paid, impact will be felt for the GS remaining in the pipeline.

Secondly, substantial impact will be felt in the case of GS imported as the dealer will have to pay CVD. Of course, CVD will be permitted. However, as we know, there is always a time gap from import of goods, value creation process and ultimate sale of goods. Depending upon the timeframe involved, additional working capital will be required to finance the same.

Thirdly, since cross-utilisation of ITC will not be permitted, there may be accumulation of ITC either under CGST or SGST. It will involve additional working capital.

Fourthly, with the removal of CST and ITC being permitted of IGST paid, there will major impact on existing supply chain. All the manufacturers and traders will have to work out new strategy and reduce additional tax liability arising, if any. There may be new opportunities in terms of ITC being made available for various goods and commodities. Thus, each and every manufacturer, importer, trader will have to sit down and have a look at the strategy for purchase and sale of the goods.

21.4 How will GST benefit the small entrepreneurs and small traders?

If the manufacturer passes on the benefit of ITC on CGST to the distribution channel, there may be some benefit to the small traders. As far as small manufacturers are concerned, the benefit will be in the form of no tax being levied on excise duty charged. But it all depends upon the rate of tax. If it is going to be more than the existing rate, there may not be any benefit at all. In any case, there will be additional administrative burden in the form of filing of periodical forms under CGST, SGST, IGST and CVD.

21.5 In what respect it will affect the ultimate consumers?

In the absence of rate of tax being known, it is difficult to say. However, wherever the rate of tax is being raised as compared to the existing rates, prices are bound to go up. In view of the market being not perfectly competitive, it is doubtful whether the benefit of ITC will reach to the consumers. Hence, the question of reduction in prices for the ultimate consumers is remote. We have seen so far in the past that reduction in excise duty or sales tax rate has hardly ever brought down the prices benefiting the consumer. It is the fundamental principle of economics that the prices can come down only if there is excess of supply as compared to demand. As long as demand exceeds supply, the prices are bound to increase or, at the most, it may remain static. Today, we are observing drastic reduction in rate of services in telecommunication industry. It is the result of large number of service providers / suppliers. It should always be remembered that a businessman is carrying on activities for earning profit and not for charity. Therefore,

there is no reason for him to pass on the ITC in the form of reduced selling prices as long as the consumer is ready to pay the existing prices. In nutshell, GST is bound to have beneficial effect for the Government Revenue and the businessman.

21.6 *What impact it can have on the revenue collection of the Central and State Government?*

As we have seen in the recent past, in the case of VAT, implementation of GST is having positive impact on the Revenue collection of SGs. It should be remembered that the so called “Revenue Neutral Rate” (RNR) can never be neutral in strict sense. It will always be in favour of the CG and SGs. Secondly, with the extension of excise duty like tax by the CG on the entire distribution channel, it will take into its sweep large number of traders. This is bound to increase the tax collection of CG. Thirdly, with imposition of CVD on all the imports of GS, a new source of revenue will emerge. It is true that ITC will be permitted of such duty paid. However, there is always time gap between payment of duty and claiming of credit of the same by the entity adding the value in the next step.

We all know that with the opening of the Indian economy and permitting to import the goods freely have open flood-gates for foreign goods and commodities. At present, there is no system of keeping track of VAT paid on goods imported and sold in the country. With imposition of CVD on such imported goods and commodities, unaccounted sale of imported goods will get trapped. This also is bound to increase revenue of both the CG and SG substantially.

With the introduction of GST, an interesting development will be in the area of tracking the transaction. With the introduction of unique number being allotted to each manufacturer / trader / importer and periodical reporting of all the transactions electronically, should make it possible for the Government Agencies to trace the leakages. However, it all depends on quality and effectiveness of the hardware and software being deployed. So far, the experience in this respect in the area of VAT, Excise Duty and Service Tax has been extremely disappointing.

22.0 Administrative Work under GST

22.1 *Which type of administrative work will be involved in complying with the GST requirements?*

As we all know each statute levying tax involves registration, filing of various periodical returns, keeping track of ITC, computation of tax liability, payment of taxes, assessment etc. For each taxing statutes, all these process will have to be followed. Since there will be four new types of taxes viz. CGST, SGST, IGST and CVD, the work process as mentioned will have to be carried out with respect to all of these statutes. Naturally, paper work is bound to increase.

22.2 *Will not all these increase the administrative work for the dealer?*

Yes, it will.

23.0 Information Technology Infrastructure

23.1 Looking to the whole scheme it appears that GST will require mammoth IT Infrastructure. Do we have such kind of structure?

We are passing through horrifying experience of filing e-returns and various forms under VAT, Excise Duty, Service Tax etc. Despite tall claims made by both the CG and SGs, the system everywhere is in a mess. None of the tax payers are happy about it. Not only that the hardware deployed is extremely slow in responding to tax payers requirements, software is equally not to talk about anything. Software applications are full of bugs. Human resources required under e-systems are substantially more than what it used to be under the earlier system. Electronic system is supposed to bring down use of paper. However, in reality, after introduction of e-filing it has gone up drastically.

Apart from that the Government Department has also hardly been using the database generated. We have seen the quality of notices, orders and other communication generated by the system employed in the Government Department.

What is more worrying is that the entire system created so far will become obsolete and will have to be thrown away. New software applications will have to be developed and installed within a short span of time and all of us will have to go through the pain of identifying the bugs / errors and rectification thereof. It will take another four to five years for settling down.

24.0 Relevance of Knowledge of GST:

24.1 If it is going to take some time to implement the proposed system, is it necessary to devote any time and energy for learning the same?

It is difficult to guess the date from which GST will become effective. However, it is certain that the policy makers are determined to implement it. Each and every businessman and service provider, one or the other way, will get affected. Since GST affects the top-line of the business, any adverse impact on it may upset the whole business plan and profitability of the business.

In the process of conducting business, at times, a businessman is required to make commitment for two or three years wherein apart from technical terms and conditions, detailed commercial terms are laid down. Any changes in the tax structure in future are bound to affect the profitability substantially. It is true that it may not be possible to provide for such changes in the contract but one can certainly take cognizance of its impact on the cost.

Therefore, basic knowledge of GST is necessary. It is not necessary to prepare a detailed new business plan / strategy or revise the existing supply chain arrangement. Since the whole process will be time and energy consuming, it will be advisable to make preparation as early as possible.