

GST- A Revolution in Indirect Tax Law

Good and Services Tax is the most logical steps towards the comprehensive indirect tax reform in India since independence. Goods and Services Tax is to be implemented shortly by the Government of India. GST is leviable on every transaction involving supply of goods and/or services as well combination thereof. ***However, there is still no clarity for transactions relating to works contracts, government services and immovable property.***

GST is a multipoint tax uses Value addition principle. GST is collected on the value added at each stage of supply or provision of service in the supply chain. ***GST paid on the procurement of goods and services can be set off against GST due on supply of goods and services.*** Tax credit mechanism of GST thus levies net tax at each stage of supply chain but the consumer bears entire GST charged by last person in supply chain. GST in true spirit, is a consumption based indirect tax.

Why Goods and service tax?

One of the main reasons of the introduction of GST is to avoid cascading effect of taxes in India. There are certain problems in the system that has not been solved till date. We shall talk about these problems now.

The credit of Input VAT is available against the output VAT. In the same manner, the credit of Input excise/service tax is available for set off against the output liability of excise/service tax. However, ***the credit of VAT is not available against excise and vice versa.*** We all know that VAT is

computed on a value which includes excise duty. In the same manner, CENVAT credit is allowed only for excise duty paid on inputs, and not on the VAT paid on the input raw material. This shows that there is tax on tax.

India needs GST because it has to fill the divide of Goods and Services. Services at times are so interwoven in goods that it is difficult to slice each of them out resulting in cascading tax effect. GST as a unified tax on goods and services, permits input tax credit on purchase of goods and/or procuring services against tax due on supply thereof. GST eliminates cascading effect of multiple taxes on goods and services levied through several indirect tax laws by the Central and State Governments and shall thus rationalize tax burden on entire chain of goods and/or services.

The present forms of CENVAT and State VAT have remained incomplete in removing fully the cascading burden of taxes already paid at earlier stages.

Besides, **there are several other taxes, which both the Central Government and the State Government levy on production, manufacture and distributive trade, where no set-off is available in the form of input tax credit.** These taxes add to the cost of goods and services through "tax on tax" which the final consumer has to bear.

Since, with the introduction of GST, all the cascading effects of CENVAT and service tax would be removed with a continuous chain of set-off from the producer's point to the retailer's point, other major Central and State taxes would be subsumed in GST and CST will also be phased out, the final net burden of tax on goods, under GST would, in general, fall.

Since there would be a transparent and complete chain of set-offs, this will help widening the coverage of tax base and improve tax compliance. This

may lead to higher generation of revenues which may in turn lead to the possibility of lowering of average tax burden.

Principle of taxation- “A tax treated under the destination principle becomes a consumption tax since goods are taxed where consumed, not where produced.”

Goods as well as services would be liable to GST on consumption basis as against the present origin basis. This will redefine the taxing jurisdiction.

Highlights of the GST as Per GST Bill 2014

1. Dual GST – [Central GST + State GST]
2. GST to be levied on all transactions whether comprising goods or services or both.
3. GST to be levied on value addition at each stage of supply of goods or services or both in entire supply chain.
4. Tax credit allowed to successive supplier on same pattern as in VAT and CENVAT.
4. Taxes recommended by GST Council levied by Union and states be subsumed under GST.
5. Stamp duty, toll tax, passenger tax, road tax – not decided
6. Comprehensive coverage of services with few exceptions
7. Exports continue to be zero rated.
8. Taxes to be subsumed:

(i) **Union taxes/levies:** Central Excise, Additional excise duties, Excise duties under the Medicinal and Toilet Preparations (Excise Duties) Act,1955, Service tax, Additional duties of Customs (CVD), Special additional duties of Customs, Central sales Tax, Central surcharges and Cesses so far as they relate to the supply of goods and services. Note: No mention of Basic Custom duty, hence it shall remain in force.

(ii) **State taxes/levies:** State level VAT, Entertainment Tax (other than the tax levied by the local bodies), Octroi and Entry tax , Purchase tax, Luxury Tax, Taxes on Lottery, betting and gambling and State surcharges and Cesses so far as they relate to the supply of goods and services.

9. Central Government to compensate loss to States due to GST implementation for a period upto 5 yrs.

10. Item kept out of GST Alcoholic liquor for human consumption

GST Bill 2014-Important Definitions

1. GST [Article 366 (12A) of Constitution]

“Any tax on supply of goods or services or both except taxes on supply of alcoholic liquor or human consumption”

2. Goods [Article 366(12)]

“Goods include all materials, commodities and articles.”

3. Services [Article 366(26A)]

“Services means anything other than goods.”

4. Supply - The term 'supply' has not defined nor any conditions have been pre-fixed which imply **that free supply will attract GST.**

Taxable Event

TAXABLE EVENT- Supply of goods and/or services

PERSON LIABLE TO TAX- Any person, providing or supplying goods or services

SITUS OF TAX/ PLACE OF TAXATION - GST is a consumption based levy as per place and time of supply provisions/rules.

Dual GST- means two GST taxes on all transactions both by the Central Government and the State across the value chain

An example to show how does it work??

The illustration shown below indicates, in terms of a hypothetical example with a manufacturer, one wholesaler and one retailer, how GST will work. Let us suppose that **GST rate is 10%**, with the manufacturer making value addition of Rs.30 on his purchases worth Rs.100 of input of goods and services used in the manufacturing process. The manufacturer will then pay net GST of Rs.3 after setting-off Rs.10 as GST paid on his inputs (i.e. Input Tax Credit) from gross GST of Rs.13.

The **manufacturer sells the goods to the wholesaler**. When the wholesaler sells the same goods after making value addition of (say), Rs.20, he pays net GST of only Rs.2, after setting-off of Input Tax Credit of Rs.13 from the gross GST of Rs.15 to the manufacturer.

Similarly, when a **retailer sells the same goods** after a value addition of (say) Rs.10, he pays net GST of only Re.1, after setting-off Rs.15 from his gross GST of Rs.16 paid to wholesaler. Thus, the manufacturer, wholesaler and retailer have to pay only Rs.6 (= Rs.3+Rs. 2+Re. 1) as GST on the value addition along the entire value chain from the producer to the retailer,

after setting-off GST paid at the earlier stages. The overall burden of GST on the goods is thus much less. This is shown in the table below. The same illustration will hold in the case of final service provider as well.

Stage of supply chain	Purchase value of Input	Value addition	Value at which supply of goods and services made to next stage	Rate of GST	GST on output	Input Tax credit	Net GST= GST on output - Input tax credit
Manufacturer	100	30	130	10%	13	10	13-10 = 3
Wholesaler	130	20	150	10%	15	13	15-13 = 2
Retailer	150	10	160	10%	16	15	16-15 = 1

THE DUAL GST MODEL

See these abbreviations before understand them-

SGST- State GST, collected by the state Govt.

Prepared By: Rohit Kapoor

Email: rohitkpr1992@gmail.com

Mobile: 9899218725

Facebook: www.facebook.com/ConnectwithRK

CGST- Central GST, collected by the Central Govt.

IGST –Integrated GST, collected by the Central Govt.

Now look at the chart given below

Transaction	New System	Old System	Comments
Sale within the state	SGCT CGST	VAT	Under the new system, a transaction of sale within the state shall have two taxes, SGST- which goes to the state; and CGST which goes to the centre.
Sale outside the state	IGST	CST	Under the new system, a transaction of interstate shall have only one type of tax, the IGST- which goes to the centre.

HOW GST OPERATES?

Prepared By: Rohit Kapoor

Email: rohitkpr1992@gmail.com

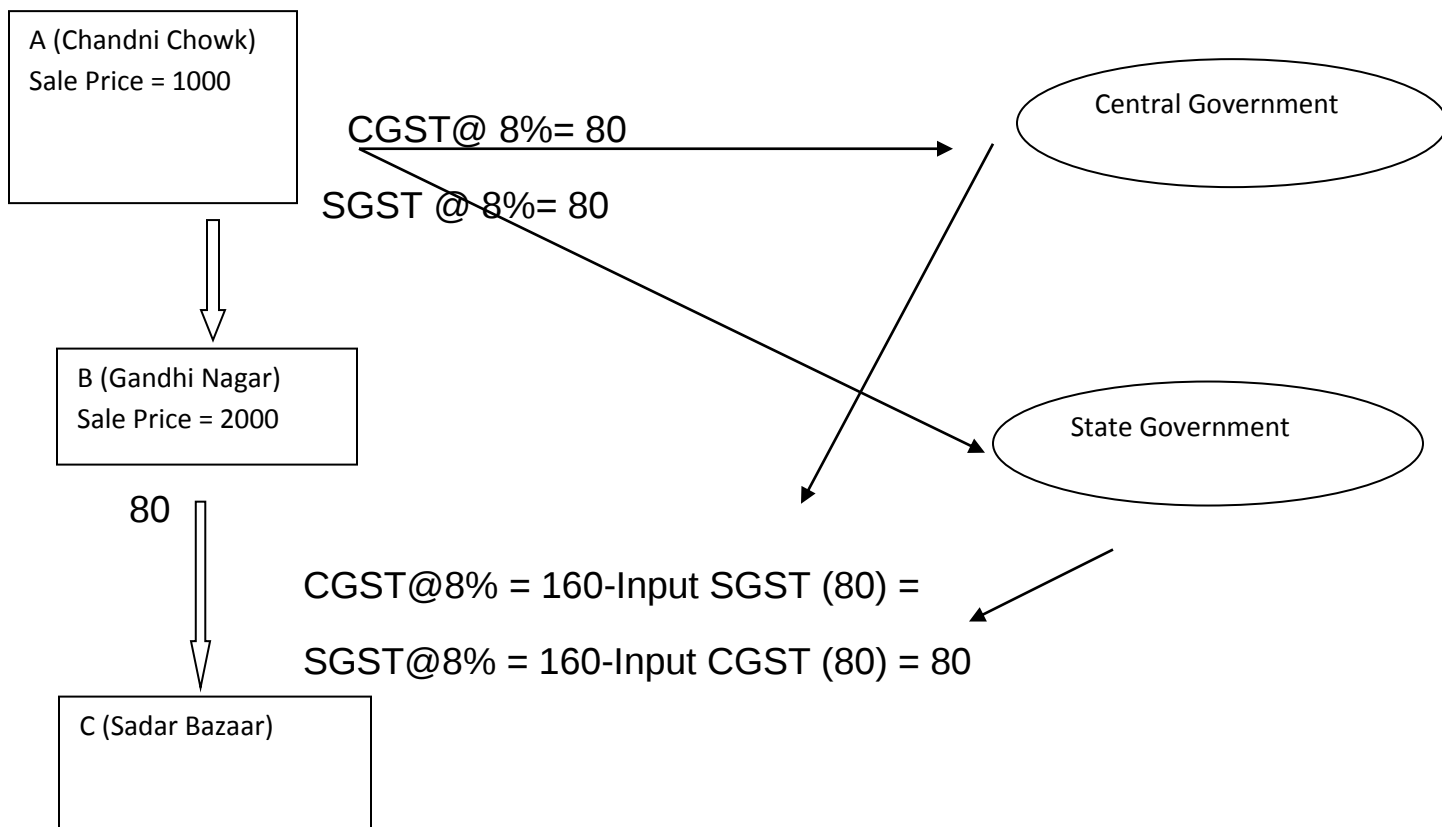
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Facebook: www.facebook.com/ConnectwithRK

CGST and SGST rates have been assumed to be 8%.

Case1: Sale in one state, resale in the same state.

In the example illustrated below, goods are moving from **Chandni Chowk** to **Gandhi Nagar**. Since it is sale within the state, CGST and SGST would be levied. The collection goes to the Central and the State Govt. as below. Then the goods are resold from **Gandhi Nagar** to **Sadar Bazaar**. This is again within the state, so SGST and CGST would be levied. Sale price is increased so tax liability will also increase. *In case of resale, the credit of input CGST and SGST is claimed as shown; and the remaining taxes goes to the respective govt.*

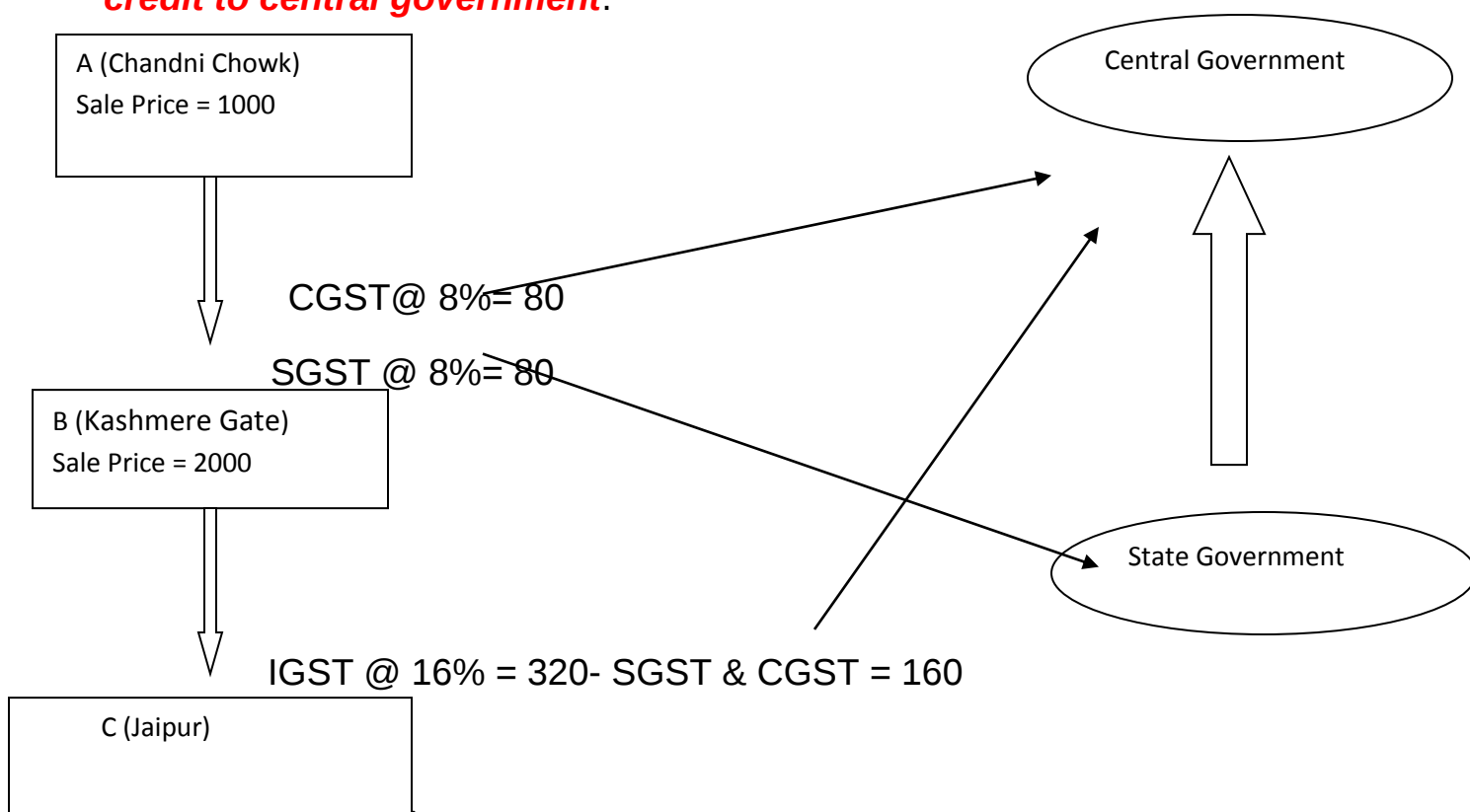


Rate of IGST has been assumed to be 16 %.

Case2: Sale in one state, resale in another state.

In the example illustrated below, goods are moving from **Chandni Chowk** to **Kashmere Gate**. Since it is sale within the state, CGST and SGST would be levied. The collection goes to the Central and the State Govt. as shown in diagram below. Later the goods are resold from **Kashmere Gate** to **Jaipur** (Outside the state). Therefore IGST would be levied and the whole IGST goes to the central govt.

Against IGST, both input taxes are taken as credit though SGST being a state levy is not collected by the central government. **This is the crux of GST. Since this amounts to loss to the central government, the state government compensates the central government by transferring the credit to central government.**



Prepared By: Rohit Kapoor

Email: rohitkpr1992@gmail.com

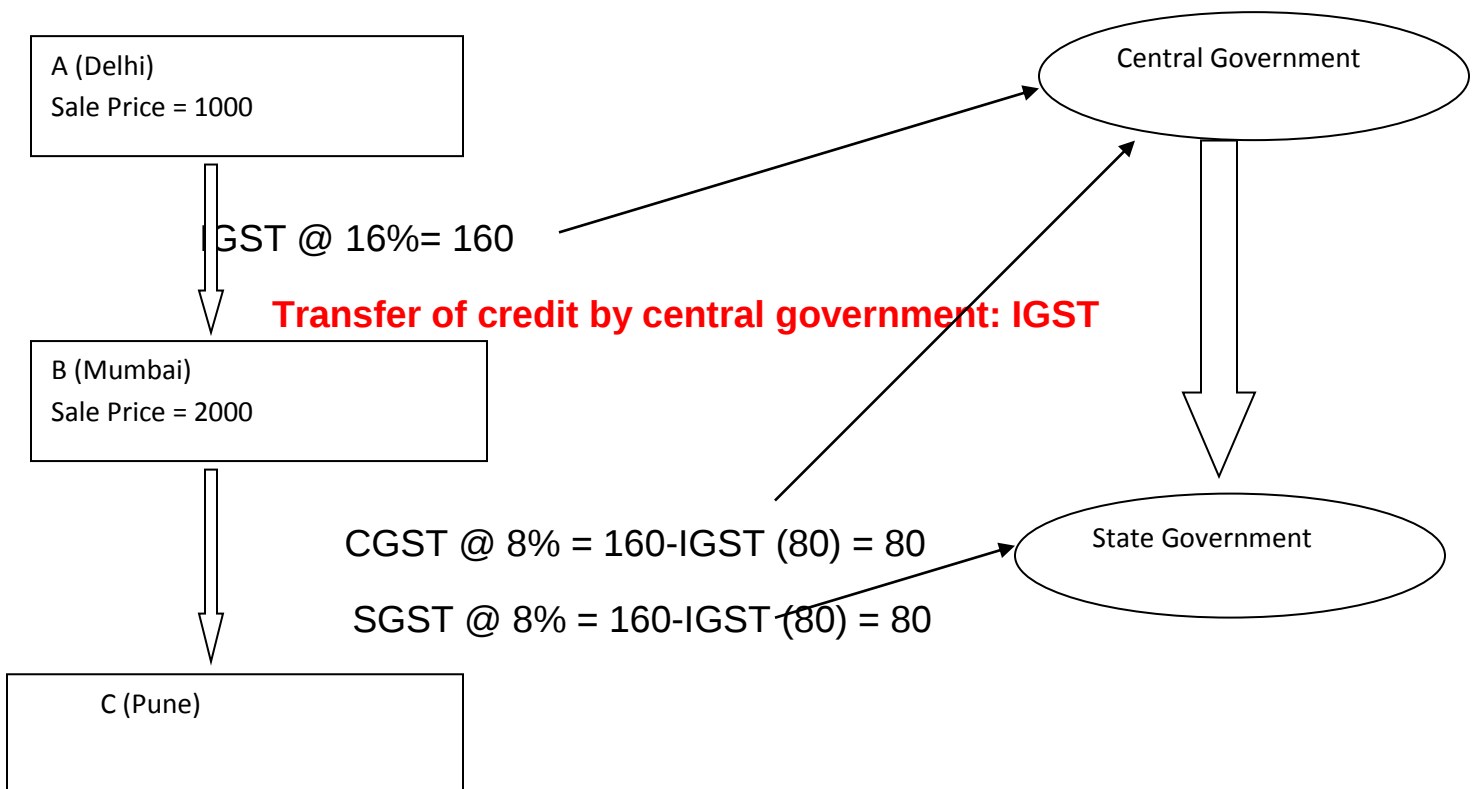
Mobile: 9899218725

Facebook: www.facebook.com/ConnectwithRK

Transfer of credit: SGST

Case3: Sale outside the state, resale in that state.

In this case, goods are moving from **Delhi** to **Mumbai**. Since it is an interstate sale, IGST would be levied. The collection goes to the central govt. Later the goods are resold from **Mumbai** to **Pune** (within the same state). Therefore CGST and SGST would be levied. 50% of the IGST can be set off against CGST and remaining 50 % of the IGST can be set off against SGST which is taken as credit. It is important to note that though IGST is not collected by the state govt., still its credit is claimed against SGST. *Since this amounts to loss to the State government, the central government compensates the state government by transferring the credit to state government.*



ADVANTAGE OF GST

How will GST benefit the small entrepreneurs and small traders?

Uniform State GST threshold of INR 25 Lakhs for both goods and services.

How will GST benefit the common consumers?

With the introduction of GST, all the cascading effects of CENVAT and service tax will be more comprehensively removed with a continuous chain of set-off from the producer's point to the retailer's point than what was possible under the prevailing CENVAT and VAT regime.

Certain major Central and State taxes will also be subsumed in GST and CST will be phased out. Other things remaining the same, the burden of tax on goods would, in general, fall under GST and that would benefit the consumers.

How will GST benefit the exporters?

The subsuming of major Central and State taxes in GST, complete and comprehensive setoff of input goods and services and phasing out of Central Sales Tax (CST) would reduce the cost of locally manufactured goods and services. This will increase the competitiveness of Indian goods and services in the international market and give boost to Indian exports.

Composition Scheme

Both the Centre and States are of the same view that there should be a Compounding Scheme for the purpose of GST with an upper ceiling on gross annual turnover and a floor rate with respect to gross annual turnover.

50 lakh of gross annual turnover floor rate of 0.5% across the states.

Tax Payer Identification Number

Each taxpayer could 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.

The exact design would be worked out in consultation with the Income-Tax Department.

CONCLUSION -GST is expected to play a key role in bringing about more transparency into the tax system. Instead of fiscal concessions, concessions to select industries on grounds such as environmental protection etc. could be provided in a transparent manner through cash refunds or otherwise.

While unified rate may be there, states may be allowed to charge rates most suitable to them such as on alcohol, petroleum products, etc. A very strong infrastructure network would be required to administer GST which would include facility for online payment of tax and e-filing of returns. The GST as a new levy could be a very effective tool and break through in indirect tax reforms, provided it is made simple and assessee-friendly – not like the present tax system.

The passage of the GST Bill has been indefinitely delayed after opposition parties declined to support the tax reform measures. The government has now changed the rollout deadline from April 1, 2016 to June 1.

GST model law will be ready by January next

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Written By: Rohit Kapoor

Email: rohitkpr1992@gmail.com

Mobile: 9899218725

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