

An Insight of GST in India



[Volume II]



THE INSTITUTE OF COST ACCOUNTANTS OF INDIA

(Statutory body under an Act of Parliament)

www.icmai.in



An Insight of Goods & Services Tax (GST) in India

October 2015

GST - media to achieve mission of

MAKE IN INDIA

- through ease of doing business

(Volume II - Reference)

Publications by the Institute on Goods & Services Tax (GST) in India:

- (1) Concept Paper on Goods & Services Tax - September 2009 (issued prior to the First Discussion Paper issued by the Government of India on November 2009)
- (2) Implementation of GST in India - a Technical Guide - April 2010
- (3) Insight of GST in India - 2nd Concept Paper by the Institute (as on date) - October,2015

Contents prepared by the:

Tax Research Department

The Institute of Cost Accountants of India

(Statutory Body under an Act of Parliament)

taxresearch@icmai.in

Prepared under the guidance of :

Taxation Committee

The Institute of Cost Accountants of India

(Statutory Body under an Act of Parliament)

Issued by:

The Institute of Cost Accountants of India

(Statutory Body under an Act of Parliament)

www.icmai.in



16th October, 2015

MESSAGE

It gives me immense pleasure to know that Institute of Cost Accountants of India is coming up with a publication titled "An Insight into GST in India".

I find from the title sketch that the book deals with how GST in India works as a tool to empower economic growth and functions as an engine for generation of employment in India. This publication captures the best practices of GST especially "Place of Supply Rules" and how such practices can be tailored to fit into the Indian context.

I hope the publication being published by the Institute would help in dissemination of information on the relevance and importance of GST in India – as an important factor to facilitate ease of doing business in India and benefit the consumers at large.

I wish all success for this publication.

(Arun Jaitley)

Mr. P. V. Bhattad,
President,
Institute of Cost Accountants of India,
CMA, Bhawan, 3,
Institutional Area, Lodi Road,
New Delhi – 110 003



Bashir Ahmed

IAS (Retd.)

(Former Commissioner of Commercial Tax (J&K))

Advisor

THE EMPOWERED COMMITTEE OF
STATE FINANCE MINISTERS
(CONSTITUTED BY GOVERNMENT OF INDIA)
C-406, DELHI SECRETARIAT,
I.P. ESTATE, NEW DELHI - 110 002
TEL : 2339 2433, FAX : 2339 2181
E-mail : vatcouncil@yahoo.com

The Institute of cost accountants of India is a statutory body and is responsible for regulation and management of Accountancy. It has been doing an outstanding job in its field of responsibility.

I am glad that institute is bringing out a publication "An Insight of Goods and Services Tax in India". GST will be the most comprehensive reform in the field of Indirect Taxes since our independence. I am sure that this publication will be able to spread awareness among the stakeholders regarding the various aspects of the GST, which is necessary for the successful implementation of this new tax regime.

I wish the institute and Shr. A.B. Nawal, Chairman taxation committee of the Institute all success in this endeavour.


Bashir Ahmed 15/10/15



Sumit Dutt Majumdar

Former Chairman – Central Board of Excise & Customs &
Author of Book “GST in India”

FOREWARD

The Institute of Cost Accountants of India is a well-known organization, that has been prescribing various Cost Accounting Standards, which help the Revenue Authorities for arriving at fair assessment under different Indirect Tax Laws. I am confident that, even under Goods and Services Tax (GST Regime), the Institute will continue to support the stake holders with much greater responsibility. I also envisaged the CMAs to be facilitators to the Stake Holders for being GST compliant.

The publication by the Institute titled, “An Insight of GST in India” attempts to sketch an outline of the various elements of GST including its structure, proposed model, taxes to be subsumed, tax mechanism, valuation of goods and services, interstate movements of goods and services etc. Although the GST laws, rules and procedures have not yet been put in the public domain, this publication has envisaged the probable business processes and dealt with the critical aspects of Registration, Returns, Place of Supply of Goods & Services Rules etc. It has also covered the expected impact of GST on various sectors and has made a comparative analysis of different situations in the Pre-GST & Post-GST Era.

In short, the Institute has done an excellent job in bringing out this publication. I congratulate the Institute in general and CMA A. B. Nawal - Chairman, Taxation Committee in particular for this work, which would be of great help to the Tax Payers Community in the GST Regime.

I wish the Institute and CMA A. B. Nawal All the Very Best.

-SD

Sumit Dutt Majumdar

Former Chairman – CBE&C



Message of President

I am pleased to note that the Tax Research Department of the Institute under the guidance of the Taxation Committee has brought out the document titled “Insight into Goods & Services Tax (GST) in India, GST – media to achieve mission of Make in India - through ease of doing business.” GST is expected to ensure seamless and uniform indirect tax regime besides lowering inflation and promoting growth in the long run. GST will subsume central indirect taxes like excise duty, countervailing duty and service tax, also state levies like value added tax, octroi and entry tax, luxury tax.

The Institute is ready to support the Government in its initiatives like ‘Make in India’, Ease of doing business, Smart cities, Infrastructure growth, Agricultural reforms and Swatch Bharat etc. I am fully aware that in order to accomplish this task we have to constantly enhance our competencies and skill sets beyond the conventional cost accounting.

CMA professionals, by virtue of academic knowledge and practical training, are well equipped to play a pivotal role as an advisor and facilitator for due compliances of law relating to goods and services tax to the general business community. CMAs are a preferred source for sharing knowledge to spread tax-literacy and GST-awareness, as the economy is getting geared to shift the tax-incidence from Origin-to-destination principle. CMAs pledge to extend professional expertise for seamless roll-out and effective implementation of GST in India. With the implementation of GST in India CMAs would be in a much more professionally advanced stage as compared to peers. This is only due to the valuation issues which are only possible based on cost information duly authenticated by CMAs.

The role of the Cost & Management Accountants is unique in this respect due to being intimately connected with business activities of entrepreneurs and having in-depth knowledge of primary records including cost records, proper application of all the provisions of the statute towards availing of all Input Tax Credit may be ensured. The Cost & Management Accountants may provide rational and convincing recommendations towards ensuring the Government revenue and protecting all possible slippage of revenue.

I am sure that this document will serve as a base for understanding the concept of GST and its implications on one and all. I complement the efforts of the TRD and Taxation Committee in bringing out this important publication. I request one and all to send constructive suggestions to further improve the text of the document.

(CMA P.V. Bhattad)

15th October 2015



CMA Ashok B Nawal
Chairman – Taxation Committee
The Institute of Cost Accountants of India

PREFACE

Dear Colleagues,

It is my great pleasure and privilege to place before you the title "An Insight in GST in India". This is the first publication on GST of our Institute, which covers all the aspects of GST and GST update till date.

Goods and Services Tax (GST) in India as we are all aware and envisage to be the greatest indirect tax reform in the country post-independence. GST with its embedded element of simplicity in levy and collection of taxes as opposed to multiple / multi-point levy and collection of indirect tax, would remove the tax distortions besides reducing the cost of goods and services in the hands of the final consumer.

Unlike many others, I firmly believe that implementation of GST in India shall boost economic growth and overall development of industries in India. This will be an engine for generation of employment in India as simplicity and transparency under the proposed GST law would definitely promote and motivate investors to Make in India, the prime mission set by our Honorable Prime Minister, Shri Narendra Modi. Let us all raise to the need of the economy and the Nation at large in smooth implementation of GST in India and to make India the 'destination-country for investment'.

The publication titled "An Insight of GST in India" prepared and published by the Institute articulates an outline of the proposed Goods and Services Tax statute, as envisaged from various discussions, government pronouncements, international best practices and response from trade and industry associations.

The title contents the need for Tax reforms that forms the genesis for introduction of Goods and Services Tax (GST) in India. The tax reform will bring about a transformation in the tax-structure as multi-incident levy would be replaced by single-incidence levy, mitigating tax distortions besides reducing the cost of goods and services in the hands of the final consumer.

The title sketch GST in India as a tool to empower economic growth and an engine for generation of employment in India. It is explained in lucid language with diagrammatic representation, flow chart, illustrations and examples by making a pre and post-GST scenario evaluation.

Institute of Cost Accountants of India considers this as a privilege to propose a draft "Place of Supply Rules" - based on international best practices and discussions in various forums, crafted to the need for Indian economy. Valuation of Taxable Supply without consideration have been much emphasized upon and would be demonstrated further in our future publications.

The Taxation Committee of the Institute express gratitude to all the well-wishers for their valuable suggestions in the process of making and development of this title. The Institute and its esteemed members pledge to raise to the need of the economy and the Nation at large in smooth implementation of GST in India and to make India the 'destination-country for investment'. Let us all join hands together to introduce the simplified and transparent tax structure through the proposed GST law which would definitely promote and motivate investors to Make in India, the prime mission set by our Honorable Prime Minister, Shri Narendra Modi.

CMAs would be a major facilitator to spread GST awareness amongst the mass besides transforming them to be GST compliant.

Our Institute had been prescribing various Cost Accounting Standards, which had helped the both the Revenue Authorities and Tax Payers for arriving at fair assessment under indirect tax laws. The Taxation Committee of the Institute is mandated to serve the needs of the society and CMAs would be a major facilitator to spread GST awareness amongst the mass besides transforming them to be GST compliant.

It is always preached by the Institute that 'cost information is the only relevant information available to both tax administrators and tax payers for making fair assessment under tax laws ". In India, with the mandatory prescription of maintenance of cost records and cost audits thereunder, as specified, will facilitate the both the tax administrators and tax payers to bring about certainty and fair tax assessment/adjudication.

This book will be certainly useful for the members and the Institute to be familiar with forthcoming GST law. Our members will act as a Facilitator between all the stake holders, Govt., Tax Payer and ultimate Consumer. We will ensure 100% statutory compliances, seamless flow of Input Tax Credit, smooth & efficient tax collection mechanism and also will ensure the benefit of GST will be passed on in the hands of consumer.

We will be continuously updating this publication no sooner draft GST Act is made in public domain and any further enactments whenever take place. Valuable suggestions and constructive feedback from users and readers would be highly appreciated, gratefully acknowledged and suitably incorporated.

I express my sincere thanks to CMA Chiranjib Das, Joint Director, Tax Research Dept(TRD), CMA Amit Dey, CA Satendra Gupta, CS and other colleagues of TRD. I also express my gratitude for kind messages sent by **Shri. Arun Jaitely, Minister of Finance, Corporate Affairs and Information & Broadcasting India**, Shri. Bashir Ahmed - Advisor Empowered Committee of State Finance Commissioner, Shri Sumit Dutt Majumdar - Former Chairman, CBEC., Shri. Upender Gupta, Commissioner, GST and Member of Taxation Committee of Institute of Cost Accountants of India and Shri. P V Bhattad, Hon. President of Institute of Cost Accountants of India.

I am thankful to my colleagues in the Council for reposing confidence on me to serve the profession as Chairman of the Taxation Committee.

I wish all success for CMAs and students of the Institute and look forward for many more technical publications post-implementation of GST in India.

Thank You.

Contents

Part-A	Topics	Pg.No.
1.	Indirect Taxation - Present Structure and Challenges	10
2.	Make in India - in a cost-effective way	13
3.	Ease of doing Business in India	16
4.	Tax REFORMS in India	22
5.	Goods and Services Tax (GST) in India	24
	5.1 Introduction	24
	5.2 Relevance of GST	25
	5.3 Principle of Equity	27
	5.4 Common Economic Market (CEM) - Post GST	28
	5.5 GST Model - Internationally	29
	5.6 Proposed GST Model for India	30
	5.6.1 Goods & Services Tax (GST) in India - Type of GST	31
	5.6.2 Goods & Services Tax (GST) in India - Why Consumption Type of GST ?	31
	5.6.3: Goods & Services Tax (GST) in India- Why Destination-based instead of Origin-based ?	32
	5.7 GST Coverage	33
	5.7.1 Coverage in General	33
	5.7.2 Amendments made to the Seventh Schedule to the Constitution	34
	5.8: Taxes to be subsumed post-GST	35
	5.8.1 : Principles for subsuming taxes under Goods & Services Tax (GST) in India	36
	5.8.2: Other Indirect Taxes to continue post-GST	36
	5.8.3: Additional Tax - Tax Cascade continues	36
	5.9 Tax Mechanism - Levy and Chargeability	37
	5.9.1 : Rate structure for Levy and Chargeability:	38
	5.9.2. Threshold Limit	38
	5.9.3. Composition Scheme / Compounded Levy Scheme	40
	5.10 Valuation of Goods and Services	42
	5.10.1 Valuation of goods and services for a consideration	42
	5.10.2 Valuation of goods and services without a consideration	43
	5.10.2.1 Captive Consumption - CAS 4 Certification	44
	5.10.2.2 Stock Transfer	48
	5.10.2.3.Valuation of Stock Transfer for GST levy (Suggested)	50

5.10.3 Works Contract	52
5.10.3.1 Elements of Cost of Works Contract	53
5.10.3.2. Determination of Cost of Works Contract	54
5.10.3.3. Explanations to the context of Works Contract	55
5.10.3.4 Determination of Cost of Sale portion and Service portion under Works Contract	57
5.10.4: Job work	60
5.10.5: Consignment Sale	66
5.11 IGST Model - Taxation of Inter-State Sales / Supplies	67
5.11.1 Present Taxation of Inter-State Sales	67
5.11.2 Proposed Taxation of Inter-State Sales	67
5.11.3 Requirements of IGST Model	68
5.11.4 Working of IGST Model	68
5.11.5 Pre-GST (i.e. Present Scenario)	70
5.11.6 Post- GST (Proposed Scenario)	71
5.11.7 Comparative Analysis : Inter-State Supply	71
5.11.8 Advantages of IGST Model - for Tax payers	72
5.11.9 Advantages of IGST Model - for Tax Administrators	72
5.11.10 : Import	72
5.11.10.1 A diagrammatic representation of GST treatment of imported goods (as envisaged)	74
5.11.10.2 A diagrammatic representation of "Imports and Supplies through Agents" (as envisaged)	75
5.12.Export	76
5.13 Capital Goods	76
5.14 Place of Supply Rules - Suggested	76
5.14.1 To determine where supply is to be taxed	77
5.14.2 Important Concepts in GST	78
5.14.3 Place of Supply Rules - Service	82
5.14.4 Place of Supply Rules - Goods	93
5.15 GST Network (GSTN)	93
5.16 GST Registration Process (Inserted - Report Of The Joint Committee On Business Processes For GST On GST Registration - Empowered Committee Of State Finance Ministers (New Delhi-July, 2015)	94
5.17 GST Payment Process (Inserted - Report Of The Joint Committee On Business Processes For GST On GST Payment Process - Empowered Committee Of State Finance Ministers (New Delhi-April,	95

	2015)	
	5.18 GST Return Mechanism (Inserted - Report Of The Joint Committee On Business Processes For GST On GST Return - Empowered Committee Of State Finance Ministers (New Delhi-October, 2015)	95
	5.18.1 Tax Payer and Periodicity of Returns	95
	5.18.2 Components of GST -1 Return (suggested)	95
	5.18.3 Process of Filing of GST -1 Return	96
	5.19 GST Refund Mechanism (Inserted - Report Of The Joint Committee On Business Processes For GST On GST Refund Process - Empowered Committee Of State Finance Ministers (New Delhi-August, 2015)	96
	5.20 Administration, Audit and Adjudication : in post - GST era	97
	5.21 Accounting Entries	98
	5.21.1 Accounting Entries - Financial Records	98
	5.21.2. Accounting Entries - Integrated Accounting	110
	5.22 Business Segments - Impact analysis	117
	5.23 Challenges before Government & Transitional Issues in GST	134
	5.24 Pre- GST and Post- GST - Comparative Analysis	142
	5.24.1. Goods manufactured, Raw material purchased within the state and Finished goods sold within the state	142
	5.24.2. Goods manufactured, Raw material purchased within the state and finished goods sold outside the state in India	144
	5.24.3. Goods manufactured, Raw material purchased from outside the state and Finished goods sold within the state	145
	5.24.4. Goods manufactured, Raw material purchased from outside the state and Finished goods sold outside the state	146
	5.24.5. Goods purchased within the state and also sold within the state	147
	5.24.6. Goods purchased within the state and sold outside the state	148
	5.24.7. Goods purchased outside the state and sold within the state	149
	5.24.8. Goods purchased and sold outside the state	150
	5.25 Genesis of GST in India	151

	5.25.1 Flow diagram since inception of GST thought process for implementation in India	151
	5.25.2 GST- Constitutional Development	152
	5.25.3 Constitution of India- Towards GST	152
	5.25.4 GST Rates & Revenue Neutral Rate(RNR)	154
	5.26 International Scenario	156
6.	Impact of GST on various Sectors	183
	6.1 Retail Sector	183
	6.2 IT SECTOR	186
	6.3 E-Commerce	188
	6.4 Food Service Businesses	189
	6.5 Real Estate	190
	6.6 Transport Sector	192
	6.7 Telecommunication	193
	6.8 Financial Services	194
	6.9 FMCG (Fast Moving Consumer Goods)	195
	6.10 Logistics	196
	6.11 Auto Industry	199
	6.12 Pharma Industry	200
	6.13 Petroleum Products	201
	6.14 Tobacco	204
	6.15 Alcohol	206
	6.16 Power	210
	6.17 Textile Sector	211
	6.18 Manufacturing Sector	212
	6.19 Agriculture	214
7.	Recommendations	217
8.	Role of CMA's in GST	219
	References	227
Part-B	Government pronouncements	
	Appendix 1 - Report Of The Joint Committee On Business Processes For GST On GST Refund Process - Empowered Committee Of State Finance Ministers (New Delhi-August, 2015)	
	Appendix 2 - Report Of The Joint Committee On Business Processes For GST On GST Registration - Empowered Committee Of State Finance Ministers (New Delhi-July, 2015)	
	Appendix 3 - Report Of The Joint Committee On Business Processes For GST On GST Payment Process - Empowered Committee Of State Finance Ministers (New Delhi-April, 2015)	
	Appendix 4 - Report Of The Joint Committee On Business Processes For GST On GST Return - Empowered Committee Of State Finance Ministers (New Delhi-October, 2015)	

An Insight of Goods & Services Tax (GST) in India

Appendix 5 - Select Committee Report on 122 nd Constitutional Amendment Bill	
Comparative Study of Select Committee Report & Original 122nd Constitutional Amendment Bill	
Appendix 6 - The Constitution (122 nd Amendment) Bill, 2014	
Salient features of 122nd Constitutional Amendment Bill (GST)	
Analysis of 122nd Constitutional Amendment Bill (GST)	
Appendix 7 - IT Strategy for GST	
Appendix 8 - Seventy Third Report of Parliamentary Standing Committee on Finance (2012-13) on Constitution 115 th Amendment) Bill, 2011	
Appendix 9 - Taxation on Service Based on a Negative List of Services Concept Paper for Public Debate	
Appendix 10 - Revised Concept Paper on Taxation of Services Based on Negative List	
Appendix 11 - The Constitution (115 th Amendment) Bill, 2011	
Appendix 12 - Relevant Extract of TAGUP Report	
Appendix 13 - Extract of Task Force Report of 13 th Finance Commission on GST	
Appendix 14 - Comments of the Department of Revenue (DOR) on First Discussion Paper on GST	
Appendix 15 - First Discussion Paper on Goods and Service Tax in India	
Appendix 16 - Working Paper [No. 1 /2009 - DEA] on GST - GST Reforms and Inter-Governmental Consideration In India	

REPORT

OF

THE JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST

ON

REFUND PROCESSES

Empowered Committee of State Finance Ministers

New Delhi

August, 2015

INDEX

Contents	Page No.
1.0 Introduction.....	1
2.0 Situations where refund would arise.....	2
(A) Excess Payment of Tax due to mistake or inadvertence.....	3
(B) Export (including deemed export).....	5
(C) Finalization of Provisional Assessment.....	13
(D) Refund of Pre-deposit for filing appeal including refund arising in pursuance of an appellate authority's order.....	15
(E) Payment of Duty/Tax during investigation, but no/less liability arises at the time of finalization of investigation/ adjudication.....	16
(F) Refund for Tax payment on Purchase by UN bodies, Supplies to CSD Canteens, Para-military forces canteens, etc.	18
(G) Refund from Manufacturing / Generation/ Production/ Creation of Tax- free supplies or Non-GST Supplies.....	20
(H) Refund of Carry Forward Input Tax Credit.....	22
(I) Refund on account of year-end or volume based incentives provided by the supplier through credit notes.....	23
(J) Tax Refund for International Tourists	24
3.0 Refund Forms.....	25
4.0 Time period for filing Refund and relevant date	25
5.0 Supporting Documents	26
6.0 Receipt of Refund Application and procedure for generating proof of Receipt of application for Refund.....	28
7.0 Number of copies of applications to be filed.....	29

8.0 Requirement for taxpayer to keep a copy of refund application for the prescribed period.....	29
9.0 Procedure and time within which preliminary scrutiny of submission of the relevant documents is carried out.....	29
10.0 Procedure for dealing with refund thereafter including examination of principle of “Unjust Enrichment.”.....	30
11.0 Minimum amount below which refund shall not be granted.....	31
12.0 Sanctioning of Refund.....	32
13.0 Verification and Control.....	32
14.0 Interest.....	34
15.0 Adjustment.....	35
16.0 Recovery of erroneous Refund.....	35
17.0 Constitution order of Joint Committee on Business Processes for GST (Annexure-I).....	36
18.0 Constitution of Sub-Committee on GST Refund Processes (Annexure-II).....	38
19.0 List of Participants of the meeting held on 22 nd July, 2015 and 23 rd July, 2015 (Annexure-III).....	40
20.0 Refund Claim Form (ANNEXURE – IV)	43
21.0 Refund Order (ANNEXURE-V).....	45
22.0 Reduction / Adjustment Summary (ANNEXURE-VI)	47
23.0 Refund Claim Form (ANNEXURE-VII).....	48

REPORT OF THE JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST
ON
REFUND PROCESSES IN GST REGIME

INTRODUCTION:

1.0 During the Empowered Committee meeting held on 10th March, 2014, it was decided that a Joint Committee under the co-convenership of the Additional Secretary (Revenue), Government of India and the Member Secretary, Empowered Committee should be constituted to look into the Report of the Sub-Group-I on Business Processes for GST and make suitable recommendations for Registration and Return to the Empowered Committee. It was also decided that the Joint Committee should also give its recommendations on Refund Processes in GST regime. Accordingly, a Joint Committee, in consultation with the Government of India, was constituted on 7th April, 2014 (Annexure-I).

1.1 In the second meeting of the Joint Committee on Business Processes for GST held on 12th November, 2014, it was decided to constitute a Sub-Committee on GST Refund Processes. Pursuant to that decision, a Sub-Committee under the Co-convenership of Shri Manoj Ahuja, Commissioner, Commercial Tax, Odisha and Shri Upender Gupta, Additional Commissioner, GST, CBEC, Government of India was constituted on 14th November, 2014 (Annexure-II). Shri Sanjeev Khirwar, Commissioner, Trade Taxes, Delhi was co-opted as a member of the Sub-Committee.

1.2 The Sub-Committee examined the present practices prevalent in the Central and the State VAT laws and also noted the proposed structure for verifications, etc. envisaged under the IGST Model. The Sub-Committee submitted its Report on 28th January, 2015. The Report of the Sub-Committee was considered by the Joint Committee on Business Processes for GST in its meeting held on 2nd February, 2015 and 3rd February, 2015. The list of the participants of the last meeting of the Joint Committee on Business Processes is

appended at Annexure-III. The Joint Committee broadly agreed with the recommendations of the Sub-Committee and the two Conveners of the Sub-Committee were requested to finalise the Report of the Sub-Committee keeping in view the observations made during the meeting of the Joint Committee on Business Processes on 2nd February, 2015 and 3rd February, 2015. Accordingly, a final Report was received on 11th February, 2015 from the Co-convenor of the Sub-Committee. The Report of the Joint Committee on Business Processes for GST was prepared accordingly. The Report was further discussed in the Joint Committee on Business Processes for GST meeting held on 22nd and 23rd July, 2015. Changes have been incorporated as per discussions.

SITUATIONS WHERE REFUNDS WOULD ARISE.

2.0 In the taxation administration, refund refers to any amount that is due to the tax payer from the tax administration. In the present taxation system it is considered as a strained area, both for the taxpayer and the tax administration. So in order to establish an effective and efficient tax administration system it is essential that issues on which refund arises ought to be kept at minimum and be clearly defined in the law. Since GST is going to subsume many of the existing taxation laws such as Central Excise, Service Tax, VAT, CST, etc., the situations under which refund arise under these laws are as follows:

- (A) Excess payment of tax due to mistake or inadvertence.
- (B) Export (including deemed export) of goods / services under claim of rebate or Refund of accumulated input credit of duty / tax when goods / services are exported.
- (C) Finalization of provisional assessment.

- (D) Refund of Pre – deposit for filing appeal including refund arising in pursuance of an appellate authority's order (when the appeal is decided in favor of the appellant).
- (E) Payment of duty / tax during investigation but no/ less liability arises at the time of finalization of investigation / adjudication.
- (F) Refund of tax payment on purchases made by Embassies or UN bodies.
- (G) Credit accumulation due to output being tax exempt or nil-rated.
- (H) Credit accumulation due to inverted duty structure i.e. due to tax rate differential between output and inputs.
- (I) Year-end or volume based incentives provided by the supplier through credit notes.
- (J) Tax Refund for International Tourists

Each of the situations mentioned above are being discussed hereunder individually for better appreciation of the issue and the proposed process to handle them under the proposed GST regime:

(A) EXCESS PAYMENT OF TAX DUE TO MISTAKE OR INADVERTENTCE.

- i) As the heading suggests, it refers to the situations where the tax payer has made excess payment of tax either by mistake or by inadvertence resulting in more payment of tax than due to the Government. Since the tax that has been paid is in excess, which was actually not required to be paid, the same should be refunded to the taxpayer.
- ii) Such excess payment may be on account of:-
 - a) wrong mention of nature of tax (CGST / SGST / IGST),
 - b) wrong mention of GSTIN, or
 - c) wrong mention of tax amount.
- iii) In first two situations i.e. in case of wrong mention of nature of tax (CGST / SGST / IGST) or in case of wrong mention of GSTIN, the tax

administration is required to verify the correctness of the taxpayer's claim and therefore the taxpayer may file a refund application which should be decided within a period to be prescribed by the GST Law.

- iv) A dealer is required to make tax payment on two accounts i.e. payment linked to a return or payment in response to a specific demand arising out of audit, etc. The IT system should be in a position to make a distinction between these two type of payment. Perhaps the payment challan may have a field to select the purpose of payment.
- v) The GST Law Drafting Committee / Payment Committee may decide as to whether the payment is to be made tax period wise or a system of Personal Ledger Account (PLA) is to be used. Maharashtra has suggested that Kerala model of return cum challan may also be examined by the GST Law Drafting Committee / Payment Committee.
- vi) In the third situation i.e. where the amount has been mentioned wrongly, the refund of excess amount of tax, at the option of the taxpayer, would either be automatically carried forward for adjustment against future tax liabilities or be refunded on submission of application (return itself can be treated as a refund application) by the taxpayer. The automatic carry forward would be allowed if the excess payment was made against a return and not against any other liability. The GST Law may provide for automatic set off if the excess payment of tax is not on account of interpretation of notifications, application of exemptions etc., i.e. the excess payment is not on account of difference of opinion between the tax administration and the taxpayer. The GST Law may also lay down the time limit within which the excess amount of tax, as reflected in the return filed by a taxpayer for that relevant period, can be re- credited *suomoto* and can be utilized by the taxpayer for payment of future tax liability.

- vii) The refund may be on account of CGST, SGST or IGST as the case may be.

(B) EXPORT (INCLUDING DEEMED EXPORT) OF GOODS / SERVICES UNDER CLAIM OF REBATE OR REFUND OF ACCUMULATED CREDIT OF TAX WHEN GOODS / SERVICES ARE EXPORTED: The treatment for export of goods and services and that of deemed export would be different under GST regime because of their inherent nature. Therefore these are being discussed separately as follows:

EXPORT OF GOODS:

- i) Presently under the Central Law, every exporter has three options available for neutralization of taxes paid on inputs used for export goods or taxes paid on finished goods exported by him which are delineated hereunder:
- a) Obtaining non duty paid inputs and exporting final product without payment of duty.
 - b) Obtaining duty paid inputs and claiming refund of the same at the time of export of the finished goods without payment of duty.
 - c) Obtaining duty paid inputs, availing the input tax credit thereon and exporting finished goods after payment of duty (after utilizing such input tax credit) and thereafter claiming the rebate of the duty paid on exported goods.
- ii) It was noted that in the proposed GST regime, exports are proposed to be Zero rated which means that the export goods would not suffer any actual tax liability although the inputs for them would be tax paid which would be subsequently neutralized. So there should be a mechanism whereby the GST paid on the inputs or on exported finished

goods, either through cash or by utilization of input tax credit, is refunded to the exporter. This would serve two objectives simultaneously. On the one hand, the ITC chain through the various dealers will not be broken and on the other hand, the exporter of the finished goods will get the refund of the GST paid on the inputs or on finished goods thereby making the exports actually free from the burden of taxes. The system should be simple and efficient so that exporters do not experience any hassles while claiming refund of taxes. For this it is essential to devise a system based verification mechanism so that human intervention is reduced to the minimum.

- iii) It is recommended that the first option mentioned above i.e. option to procure duty free inputs for exported goods should not be available in the GST regime. This would obviate the requirement of submission of statutory form and the supplier of goods to the actual exporter would be required to pay the GST and will not be required to comply with various formalities presently required for making tax free supplies.
- iv) It is further recommended that other two options may be made available to the exporter in the proposed GST regime. It is recommended that GST Law drafting Committee may provide for the provision of rebate and the legality of the same will be examined at the time of vetting of the GST law by the Law Ministry.
- v) Since the process for payment of refund of GST paid on inputs (including input services) or payment of rebate of GST paid on finished goods is similar to a large extent, the same is being discussed here together. The following process is proposed for making this system as simple as possible:

- a) The IEC details of taxpayer will be captured at the time of issuance of GSTIN and the same can be verified online with DGFT for verifying the correctness of the exporter's particulars.
- b) The refund of ITC / rebate of GST paid on exported goods may be granted on submission of application to this effect by the taxpayer.
- c) Since the trigger point for refund is export of goods, therefore the event of export needs to be verified (mostly online) so as to minimize cases of erroneous / fraudulent claims of refund / rebate.
- d) It is recommended that linkage between ICEGATE of Customs administration and the proposed GSTN of GST administration may be established so that online verification of the exports can be carried out. In any case such linkage has to be established to verify IGST paid at the time of import of goods / services.
- e) It is also noted that, as per IGST Model, there is a requirement for online filing of invoice wise sale / purchase details by the taxpayers' along with the monthly returns. These details can be linked with the Customs data (for export cases) available with ICEGATE.
- f) Normally for export verification the following documents are sought from the applicant :
 - i) Shipping Bill (Export Promotion copy);
 - ii) Mate's Receipt / Transporter's Challan (in case of export by road);
 - iii) Export invoice;
 - iv) Packing list;
 - v) Bill of Lading/ Airway Bill;
 - vi) Bank Realization Certificate (BRC).

- g) Since it is proposed to establish linkage between ICEGATE and GSTN, therefore shipping bill, which includes relevant details from the export invoice and packing list, can be verified online and there would not be any need for the exporter to submit the same. Further, Mate's Receipt and Bill of Lading are the crucial documents that determine the occurrence of event of export, the exporter would be required to upload the scanned copies of the same with online refund application. As regards the BRC, it was noted that as per the RBI guidelines, the exporter has a time period of one year from the date of export, within which the export proceeds are required to be remitted into India. Thus BRC will not be available till the time export proceeds are realized. Therefore it is recommended that submission of BRC may not be insisted upon at the time of filing of refund application and post facto verification can be carried out by the tax authorities. The refund in such cases should be subject to submission of BRC details within a period of maximum one year or such period as extended by RBI from the date of the export. If such details are not submitted at the portal at which the refund application was made, the portal should generate an alert/report for the concerned tax authorities to take up appropriate action. In case of any short receipt of export receipts, necessary action for recovery of proportionate refunded amount may be taken accordingly.
- h) BRC, however, may be verified at the time of exports itself if the payment has already been received in advance. It is also recommended that e-BRC module may be integrated in the Refund process under GST.

- i) The time limit for filing of refund application is normally linked with the date of export and it is proposed that this time limit should be fixed at one year from the date of export. This date is the date on which the proper officer under the Customs Act gives an order for export of goods commonly known as “*Let Export Order*” (LEO). This date can also be verified online in view of the proposed linkage between ICEGATE and GSTN.
- j) Once the export is established, verification of the duty paid on the final products at the time of export is required to be carried out. For this, normally, copy of challans/ invoices evidencing duty payment are sought from the exporter and the same are verified manually by the jurisdictional authority. In the proposed GSTN, the payment of GST on exported goods can be verified online (as the sales invoices are required to be filed along with the monthly return) and there is no need for separate submission of these documents. Once the GST paid character of exported goods is established, refund can be sanctioned.
- k) In respect of refund claimed for GST paid on inputs (including input services) used for exported goods, once the export is established, verification of the GST paid on the inputs (including input services) as well as their utilization for the exports is required to be carried out. For this normally copy of invoices evidencing GST payment are sought from the exporter and the same are verified manually by the jurisdictional authority. Besides a declaration is filed by the applicant with the proper officer declaring *inter alia* input-output ratio for inputs on which refund is sought. In the proposed GST regime, the GST paid character of inputs (including input services) can be established online (as the purchase invoices

are required to be filed along with the monthly return) and the refund of input tax credit on inputs (including input services) can be sanctioned once the input tax credit has been matched from the purchase and sale statements filed by the exporter and supplier respectively and there is no need for separate submission of these documents. As regards utilization of the inputs for exports, a simple formula can be adopted that will provide for proportionate credit based on export turnover divided by total turnover. Moreover, a declaration can be obtained from the exporter regarding utilization of inputs in the exported goods.

EXPORT OF SERVICES.

- i) It is noted that in case of export of services there are no custom documents that can substantiate the occurrence of event of export as no shipping bill is required to be filed. Thus invoice and Bank Realization Certificate (BRC) are the only documents that can substantiate the occurrence of event of exports. It is, therefore, recommended that in the case of export of services, BRC would be required before sanction of the refund of GST paid on inputs (input services) / rebate of GST paid on exported services.
- ii) It is further noted that the invoice and BRC are the crucial documents for filing of the refund application. Therefore the relevant date, in case of export of services, will be the date of invoice or the date of BRC, whichever is later. This will take care of the situation if the payment has already been received in advance. It is also recommended that e-BRC module may be integrated in the refund process under GST.

- iii) It is suggested that since exports of services cannot be verified online through ICEGATE, there should be a separate application for refund of service exported.

DEEMED EXPORT OF GOODS OR SERVICES.

- i) It was noted that there is a concept of deemed export for situations listed in Chapter 8 of the Foreign Trade Policy. Supplier of domestically produced duty paid goods when supplied to EOUs / SEZs / Projects under International Competitive Bidding (ICB) / Mega Power Plants / World Bank Funded Projects can seek refund of terminal excise duty as also drawback of the duty paid on the inputs used in manufacture of such goods. However such refund is not permissible for VAT paid on such domestically supplied goods.
- ii) It is recommended that the deemed export need to be treated on equal footing as export and the similar provision as detailed above for actual exports of goods or services would be applicable except the following:
 - a) The supplier of final goods, in the course of deemed export, will pay the IGST on his supplies and can claim refund, only if, the IGST amount has not collected from the recipient. It is also required to be verified that the recipient has not availed the input tax credit in respect of such supplies.
 - b) The supplier may file a simple refund application along with a Chartered Accountant's Certificate certifying the fact of non-passing of the GST burden by him, being claimed as refund. GST Law Drafting Committee may prescribe a threshold amount below which self-certification (instead of CA Certificate) would be sufficient.

- c) The recipient unit would be eligible for refund of IGST, if it has actually paid IGST at the time of obtaining goods / services from the domestic supplier. In no case, both the supplier and the recipient unit can obtain refund at the same time in respect of the same transaction. A suitable validation to block such double claim should be built in the GSTN /refund processing backend system.
 - d) Such recipients may not be registered under GST regime and therefore they would have to submit copies of all the invoices, etc. in case claim of refund is filed by them.
- iii) It is also recommended that this recommendation may be specifically brought to the notice of EC as this is deviation from the present practice being followed by the States.

GENERAL:

- i) It was suggested that as a thumb rule, up to 90% of the refund claimed by the taxpayer may be sanctioned automatically by the system. The balance amount of refund may be granted after completion of verification of documents / accounts to be done at the end of the financial year and to be completed within a period of three months. The issue was discussed and it is recommended that partial refund may not be allowed and entire refund claim may be sanctioned within the time limit laid down in the GST Law.
- ii) It was noted that there may be certain goods on which Customs Export Duty may be leviable. It is recommended that in such cases refund of ITC of GST paid on inputs (including input services) used for such exported goods may not be admissible.

- iii) Requirement of BRC for sanction of refund in respect of export of services and as a post facto verification in case of export of goods may be provided in the GST Law.
- iv) It was noted that the exports would be treated as inter-state supplies and therefore IGST would be required to be paid by the taxpayer in cases GST is paid at the time of export. Refund of such IGST would have to be paid by the Centre. In case of refund of GST paid on inputs (including input services) used for exported goods, the refund of CGST, SGST or IGST may arise and the same needs to be paid by the respective tax administration. A suitable validation to block use of same tax invoices for more than one refund claim should be built in the GSTN /refund processing backend system.
- v) It was further noted that the principle of unjust enrichment is not applicable in case of actual export of goods or services as the recipient is located outside the taxable territory. In case of deemed exports, however, the concept is applicable.
- vi) It is further recommended that the amount of input tax credit claimed as refund may be blocked at the time of time of submission of application for refund itself. And if the refund claim is rejected wholly or partially the rejected portion of the ITC claim amount will be restored in the ITC ledger of the applicant.

(C) FINALIZATION OF PROVISIONAL ASSESSMENT:

As discussed in Para No. (I) below, the issues relating to provisional assessment being presently followed by Central Tax Authorities would be handled by the system of issuance of debit and credit notes, therefore refund may not arise in such cases. The process has been delineated

here under, if the GST Law provides for continuance of the system of provisional assessment:

- i) In the proposed GST regime the returns of the taxpayer will be electronically filed. In the return itself there should be a field for indicating whether the tax being paid is provisional or final. In case the tax has been paid on provisional basis, there should be a drop box that would indicate the reasons for which the tax has been paid on provisional basis.
- ii) Once such a return comes up before the assessing officer and if he agrees with the reason mentioned by the taxpayer, the return / assessment may be kept provisional.
- iii) Thereafter the return may be taken up for finalization once the issue involved in provisional assessment is settled. GST law may prescribe time period for finalization i.e. 90 days and this time line should not be breached, as far as possible.
- iv) At the time of finalization of the return / assessment by the assessing officer, a speaking order may be issued which will also mention the amount that the taxpayer is required to pay or is eligible for refund.
- v) The refund would be granted only if the incidence of GST paid by him has not been passed on to the consumer (the concept of unjust enrichment). This issue would be examined by the assessing officer at the time of finalization of assessment.
- vi) The model GST Law may provide for appropriate provisions relating to the principle of unjust enrichment.
- vii) For satisfying the requirement of unjust enrichment, the taxpayer would be required to submit a Chartered Accountant's Certificate certifying the fact of non-passing of the GST burden by the taxpayer, being claimed as refund. GST Law Drafting Committee may prescribe a

threshold amount below which self certification (instead of CA Certificate) would be sufficient. This would also settle the issue of ITC that would have been claimed by the purchaser on the basis of the provisional tax paid by the taxpayer as ITC would have to be reversed by the recipient before sanction of refund to the supplier.

- viii) The differential amount claimed as refund will be reflected in the return for the month in which the finalization takes place.
- ix) The refund may be on account of CGST, SGST or IGST as the case may be.

(D) REFUND OF PRE – DEPOSIT FOR FILING APPEAL INCLUDING REFUND ARISING IN PURSUANCE OF AN APPELLATE AUTHORITY’S ORDER.

Refund arising in pursuance of appellate authority’s order is another area that has been subject of judicial scrutiny and strictures. The following process is recommended in order to make this process streamlined, efficient and in line with the judicial decisions on the matter:

- i) Looking at the policy objective of making the refund process hassle free, it is recommended that the taxpayer may file a simple refund application along with a Chartered Accountant’s Certificate certifying the fact of non-passing of the GST burden by the taxpayer, being claimed as refund. As mentioned earlier, the GST Law Drafting Committee may prescribe a threshold amount below which self certification (instead of CA Certificate) would be sufficient.
- ii) The refund may not be kept in abeyance if the appellate authority’s order (in pursuance of which refund arises) is appealed against at the next higher appellate forum unless the jurisdictional authority has obtained a stay from the higher appellate authority against the

operation of the appellate authority's order in pursuance of which refund has arisen. This position may be appropriately reflected in the GST Law itself so that any ambiguity on this issue can be avoided and the tax administrations are made more accountable for early action in case of such refunds.

- iii) GST Law may provide for certain predefined period during which refund may not be granted which can be regarded as the mandatory waiting period for the outcome of the appeal / application for stay.
- iv) GST Law Drafting Committee may also consider for providing powers to jurisdictional authority at sufficiently senior level for withholding the refund in exceptional cases on the condition that interest at appropriate rate has to be paid.
- v) The refund may be on account of CGST, SGST or IGST as the case may be.

(E) PAYMENT OF DUTY/TAX DURING INVESTIGATION BUT NO / LESS LIABILITY ARISES AT THE TIME OF FINALIZATION OF INVESTIGATION / ADJUDICATION :

Presently the Central Law (State Laws do not have similar provision) does not debar suo-motto payments during investigation / audit without issuance of a formal show cause notice / demand. If the GST Law does not debar such payments during investigation / audit process and ultimately no / less demand arises vis-à-vis amount already paid, then refund of such amount may be handled as per the procedure given below:

- i) A separate mechanism for the accounting of such payments has to be designed.

- ii) Refund in such cases requires utmost attention as such amount of tax paid during investigation, etc. become non leviable once the investigation is finalized and / or an adjudication order in favor of the taxpayer is issued. Therefore this process should be simple and hassle free.
- iii) As soon as the investigation, etc. is over which does not lead to issuance of a show cause notice or where after investigation, show cause notice is issued but the adjudication order is in favor of the taxpayer i.e. where the demand of duty is dropped in full or in part, the taxpayer should be immediately eligible to claim refund of the amount that is found to have been paid in excess during investigation, etc.
- iv) Looking at the policy objective of making the refund process hassle free, it is recommended that the taxpayer may file a simple refund application along with a Chartered Accountant's Certificate certifying the fact of non-passing of the GST burden by him, being claimed as refund. GST Law Drafting Committee may prescribe a threshold amount below which self certification (instead of CA Certificate) would be sufficient.
- v) However, as every adjudication order can potentially be appealed against, the model GST Law may provide for a time limit after which only the refund can be sanctioned either by cash or by adjustment order at the option of the tax payer by the jurisdictional officers. This time limit should be concurrent with the time limit available for filing of an appeal so that department has time to file an appeal along with stay application, if any against adjudication order.
- vi) Refund may be withheld only if the department has obtained a stay order on the operation of the adjudication order, failing which, refund has to be allowed.

- vii) The GST Law Drafting Committee may also consider for providing powers to jurisdictional authority at sufficiently senior level for withholding the refund in exceptional cases on the condition that interest at appropriate rate has to be paid.
- viii) The refund may be on account of CGST, SGST or IGST as the case may be.

(F) REFUND FOR TAX PAYMENT ON PURCHASE BY UN BODIES, SUPPLIES TO CSD CANTEENS, PARA MILITARY FORCES CANTEENS, ETC.:

- i) Presently the UN bodies are eligible for refund of taxes paid by them at the time of purchases made by them from the market. GST Law may provide for similar provision and in such a case, the following process for grant of refund is recommended.
 - a) Refund on purchases by UN Bodies may be granted from only one office each of both the tax administrations within one State.
 - b) UN Bodies may be assigned a unique identification number (ID) the structure of which would be uniform across the States in conformity with the GSTIN Structure. (Some other structure may have to be considered as such bodies do not have PAN)
 - c) The registration document, return document and invoice would contain a column for capturing this Unique ID.
 - d) There has to be a separate field for allotting ID to such bodies.
 - e) While making supplies to such bodies, the suppliers must indicate the Unique ID on the invoices.
 - f) The UN Bodies may file their purchase statements (without purchase invoices) along with their claim for refund.
 - g) The GST Law may provide that some purchases are ineligible for refund (e.g. invoice value less than the prescribed threshold,

goods / services specified as ineligible for refund, etc.). Such cases should be specifically marked in the purchase statement or may not be included in the purchase statement.

- h) The net claim will be related to GST paid on total purchases minus GST paid on ineligible purchases.
- i) The IT system will carry out the matching with the sales statements of the counter party suppliers.
- j) The matched and claimed to be eligible invoices will be seen by the jurisdictional authority to verify that none of the ineligible purchases have been included in the refund claim.
- k) The refund may be granted based on the matching and the limited manual verification.
- l) There might be situations when the supplier does not declare the supply in his monthly return. In such a case, unmatched invoices will get marked by the IT system and the supplier will be notified accordingly.
- m) The UN body may be granted refund along with its next claim if any of the unmatched supplies have been accepted and related GST has been paid by the supplier and return has been filed subsequently.
- n) The personal purchases by the staff may also be done seeking ID of the UN body on the invoice.
- o) Such invoices in the statement can be marked as “for personal consumption” for any additional verification in case of any restriction under the GST Law.
- p) GST Law Drafting Committee may provide for appropriate provisions whether refund has to be given for the personal purchases by the staff of UN bodies and Embassies. Such provisions may also relate to limits or restrictions, if any on such refunds.

- ii) It is recommended that the suppliers to CSD Canteens, Para Military Canteens would not be eligible for exemption. The procedure as detailed above would apply in respect of supplies to CSD Canteens, Para Military Forces canteens etc. and these bodies would claim refund.
- iii) Form of application for refund which may be used by such bodies is enclosed as Annexure-VII to this document.
- iv) The refund may be on account of CGST, SGST or IGST as the case may be.

(G) TAX CREDIT ON INPUTS USED FOR MANUFACTURING /GENERATION /PRODUCTION /CREATION OF TAX FREE SUPPLIES OR NON-GST SUPPLIES:

- i) There would be certain goods or services which may be either exempted or NIL rated in GST regime. Further there may be certain goods or services which may not be brought under GST regime. Persons supplying such exempted / nil rated / non-GST goods or services would be receiving goods or services as their input supplies after payment of GST.
- ii) The issue, whether such taxpayers are entitled to cash refund of the GST paid by them in respect of such input supplies (including input services or capital goods) which will be used for making supplies without payment of GST, was discussed at length.
- iii) It is felt that the ITC is allowed to remove cascading and under modern VAT laws, tax is charged on value addition only and not on tax paid at the earlier level of supply chain. It is for this reason that the ultimate consumer is liable to bear the tax. Most State VAT administrations as well as Centre do not allow refund of ITC on inputs used for tax exempt / nil rated goods.

- iv) Further the inputs (including input services or capital goods) received by such suppliers would become exempt if the refund is allowed to them, which is not intended by tax design.
- v) It is recommended that the model GST Law may provide that the suppliers of exempted / NIL rated / non GST goods or services would not be entitled to the ITC of GST paid on inputs (including input services or capital goods) received by them and consequently for refund of GST paid by them. In case of mixed supplies, ITC may be allowed proportionately.
- vi) The tax credit on the inputs used for supply of exempted / NIL rated / non GST goods or services should be treated as “ineligible input tax credit” and there should be an appropriate provision in the return to provide the related invoice details.
- vii) In addition to ineligible input tax credit arising from inputs used for supply of exempted / Nil rated / non-GST goods or services, there may be other types of ineligible input tax credits such as those related to specified capital goods / assets. It is recommended that the model GST law may provide for the full scope of such ineligible input tax credits.
- viii) It is also recommended that such ineligible tax credit should accrue to the importing States in accordance with the Place of Supply Rules. This imperative will also apply to the inter-state supplies procured by the economic entities / government departments / public bodies supplying tax exempt / nil-rated / non-GST goods and services only. The mechanism for flow of such funds to the importing state by way of a system based apportionment in a consistent manner may be decided as a part of the return process.

(H) REFUND OF CARRY FORWARD INPUT TAX CREDIT.

- i) As stated earlier, ITC is allowed to remove cascading and under modern VAT laws, tax is charged on value addition only and tax is not charged on tax. It is for this reason that the ultimate consumer is liable to bear the tax burden.
- ii) It is noted that the ITC may accumulate on account of the following reasons :
 - a) Inverted Duty Structure i.e. GST on output supplies is less than the GST on the input supplies;
 - b) Stock accumulation;
 - c) Capital goods; and
 - d) Partial Reverse charge mechanism for certain services.
- iii) As regards the accumulated ITC attributed to accumulation of stock or capital goods, it is recommended that GST Law may provide that refund of carried forward ITC may not be allowed and such amount would be carried forward to the next tax period (s). The GST Law may provide for appropriate provisions in this regard.
- iv) Under the proposed GST law, it is proposed to have fewer tax rates and fewer exemptions and therefore it is felt that chances of inverted duty structure would not be there or would be very minimal. But still there might be a possibility that ITC may accumulate on account of inverted duty structure.
- v) It is recommended that in such case, cash refund may be granted after due audit and should be sanctioned only after the input tax credit has been matched from the purchase and sales statements filed along with monthly returns. The refund would be granted on submission of application. It may be mentioned, however, that presently the Centre does not grant refund in such cases.
- vi) Two options i.e. blocking the utilization of input tax credit claimed as refund at the time of submission of application for refund itself or debiting the input tax credit account / cash ledger subject to the amount

available in either account at the time of issuance of sanction order of refund were discussed. It is recommended that the first option should be adopted. Suitable linkage between the refund application and blocking of the “carry forward input tax credit” in the return/cash ledger should be built in GSTN and refund backend processing system.

- vii) ITC may also accumulate on account of circumstances wherein liability to pay service tax is under Partial reverse Charge Mechanism. Presently the liability to pay service tax is either on the service provider or on service recipient or on both. The third category is popularly known as joint / partial reverse charge where both the service provider and the service recipient are liable to pay the service tax.
- viii) In case of partial reverse charge, service provider may be left with unutilized balance in the input credit account as he is not liable to discharge the tax liability in full. In such cases, refund may be granted if the GST law provides for a joint reverse charge mechanism.
- ix) The refund may be on account of CGST, SGST or IGST as the case may be.

(I) REFUND ON ACCOUNT OF YEAR END OR VOLUME BASED INCENTIVES PROVIDED BY THE SUPPLIER THROUGH CREDIT NOTES.

It is noted that suppliers are allowing year end or volume based discounts through credit notes. Such practice is being misused by the trade where the downstream dealers show negative value-additions. Some States have placed restrictions on such ITC. It is felt that the GST Law may provide for suitable provisions in this regard as provisions for such discounts is a trade practice and will have to be permitted in the GST regime. The following procedure is recommended:

- i) The refund would be granted on submission of a simple application along with a Chartered Accountant’s Certificate certifying the fact of non-passing of the GST burden by the taxpayer, being claimed as refund. The GST Law Drafting Committee may prescribe a threshold

amount below which self-certification (instead of CA Certificate) would be sufficient.

- ii) In such cases, the eligibility for ITC at the buyer's end and the output liability at the supplier's end will get simultaneously reduced / adjusted on the basis of credit notes issued by the supplier and the corresponding debit notes issued by the buyers.
- iii) This would also obviate the need for resorting to provisional assessment presently provided in Central Law and discussed in para (C) above.
- iv) The GST Law may contain suitable provision to this effect and the GSTN should have suitable validations to this effect. The validation should include matching of credit and debit notes and reversal of the reduction of the output tax liability in case of the mismatch.
- v) The refund may be on account of CGST, SGST or IGST as the case may be.

(J) TAX REFUND FOR INTERNATIONAL TOURISTS.

Tax Refund for International Tourist (TRT) scheme provides an opportunity to the foreign tourists to purchase goods during their stay in any country on payment of GST and obtain refund of the GST so paid, at the time of exit from the country. Nearly 52 countries have adopted such kind of refund mechanism. It was noted that such a scheme helps in attracting tourist and is in line with avowed objective of GST regime of zero rating of goods and Make in India initiative of Government of India. State governments are offering VAT refunds to foreign diplomats and officials of multilateral agencies. This scheme will be implemented through particular retailers who are registered for this scheme. Refund of GST will be available at designated airports and ports only and the refund of the GST paid on retail purchase by the foreign tourists during their stay in India is allowed. A part of the eligible amount of refund will

be deducted as handling fee for services rendered. GST law drafting Committee may provide for this provision as well delineate the details of the scheme.

REFUND FORMS.

3.0 The form should be simple to fill, easy to understand and more importantly, in the context of the technological world, it should be in electronic format. The forms for Refund Claim, Refund order and Reduction / Adjustment summary are enclosed as Annexure –IV to VII to this document.

TIME PERIOD FOR FILING OF REFUND AND RELEVANT DATE.

4.0. It is recommended that a period of one year from the relevant date may be allowed for filing of refund application. Relevant date for filing of each kind of refund needs to be defined separately. The following dates are recommended as relevant dates for different type of refund cases:

- i) Date of payment of GST when the refund arises on account of excess payment of GST due to mistake or inadvertence.
- ii) Date on which proper officer under the Custom Act gives an order for export known as “*LET EXPORT ORDER*” for the purpose of refund filed on account of export of goods under claim of rebate of GST paid on exported goods or refund of accumulated input credit of GST when goods are exported.
- iii) Date of BRC in case of refund on account of export of services under claim of rebate of GST paid on exported services or refund of accumulated input credit of GST when services are exported.

- iv) Date of the finalization order where refund arises on account of finalization of provisional assessment. (May not be required if the GST law does not provide for provisional assessment)
- v) Date of communication of the appellate authority's order where the refund arises in pursuance of an appellate authority's order in favor of the taxpayer.
- vi) Date of communication of adjudication order or order relating to completion of investigation when refund arises on account of payment of GST during investigation, etc. when no/less liability arose at the time of finalization of investigation proceedings or issuance of adjudication order.
- vii) Date of providing of service (normally the date of invoice) where refund arises on account of accumulated credit of GST in case of a liability to pay service tax in partial reverse charge cases.
- viii) Date of payment of GST for refund arising out of payment of GST on petroleum products, etc. to Embassies or UN bodies or to CSD canteens, etc. on the basis of applications filed by such persons.
- ix) Last day of the financial year in case of refund of accumulated ITC on account of inverted duty structure.

SUPPORTING DOCUMENTS.

5.0 Documents evidencing tax payments required to be enclosed with the refund application should be minimal but adequate so that both the taxpayer and tax authority find it easy to deal with the application. Normally following documents are required to establish the rightful claim of refund:

- i) Copy of TR-6 / GAR-7/ PLA / copy of return evidencing payment of duty. It is recommended that these forms may not be called for as in the

proposed GST scenario payment of duty will be in electronic mode and the same will be easily visible to the refund sanctioning authority on screen.

- ii) Copy of invoices (in original) (for the purpose of evidencing the supply of goods and the fact that duty is not reflected in the same). It is noted that the IGST Committee has recommended that the taxpayers would upload their invoice details on monthly basis. Once the same is done and the refund sanctioning authority is able to examine and view them on screen then submission of invoices can be dispensed with. It was noted that the field relating to “Quantity” is not captured in the invoice details proposed to be uploaded either before or alongwith the Return. It was further noted that this information would be required in case of refund in relation to exports. The applicant for refund in such cases would submit the copies of the invoices or a statement containing details of quantity along with the refund application. Documents evidencing export. In the proposed GST scenario it is recommended that the ICEGATE and GSTN would be inter linked, and therefore these documents can be verified on line and therefore can be dispensed with.
- iii) Documents evidencing that the tax burden has not been passed on to the buyer. Since GST is an Indirect tax, there will be a rebuttable presumption that the tax has been passed on to the ultimate consumer. Therefore there is a need for establishing that principle of “unjust enrichment” does not apply to the refund claim. It is recommended that a Chartered Accountant’s Certificate certifying the fact of non-passing of the GST burden by the taxpayer, being claimed as refund should be called for. The GST Law Drafting Committee may prescribe a threshold amount below which self-certification (instead of CA Certificate) would be sufficient.

- iv) Any other document as prescribed by the refund sanctioning authority. It is recommended that the state and central tax authorities together prescribe the documents that are required for demonstrating the legitimacy and correctness of refund claimed and checklists can be generated for refund sanctioning process.

RECEIPT OF REFUND APPLICATION AND PROCEDURE FOR GENERATING PROOF OF RECEIPT OF APPLICATION FOR REFUND.

6.0 It is recommended that the State Tax authorities shall deal with the SGST refund and Central Tax authorities shall deal with refund of CGST and IGST. The following procedure is proposed in this regard:

- i) Applicant may be given the option of filing refund application either through the GSTN portal or through the respective State / Central Tax portal. Filing through GSTN portal may be beneficial for those applicants whose refund relates to CGST / IGST as well as SGST or the refund arises in different State Tax jurisdictions. Instead of filing applications with different tax authorities, the same may be filed with the GSTN portal which will forward it to the respective tax authority.
- ii) On filing of the electronic application, a receipt/ acknowledgement number may be generated and communicated to the applicant via SMS and email for future reference. A provision may be made to display the application for refund in dealer's online dashboard when he logs into the system.
- iii) The “carry forward input tax credit” in the return and the cash ledger should get reduced automatically, if the application is filed at GSTN portal itself. In case the application is filed at the tax department portal, suitable integration of that portal with GSTN portal should be

established to reduce/block the amount before taking up the refund processing.

- iv) It should be clearly mentioned / highlighted that generation of this number does not in any way affirm the legality, correctness or completeness of the refund application.

NUMBER OF COPIES OF APPLICATIONS TO BE FILED:

7.0 As the filing of the electronic refund application is a preferred mode, filing of multiple copies of applications is not required.

REQUIREMENT FOR TAXPAYER TO KEEP A COPY OF REFUND APPLICATION FOR THE PRESCRIBED PERIOD:

8.0 Since the application for refund is expected to be filed electronically, the application form should have a print option along with the option for the applicant to download the same so that he can store the same for future reference and record. This would serve the purpose of record keeping for the applicant.

PROCEDURE AND TIME WITHIN WHICH PRELIMINARY SCRUTINY OF SUBMISSION OF THE RELEVANT DOCUMENTS IS CARRIED OUT:

9.0 After the receipt of the application in the jurisdictional officer's menu, the same should be examined for deficiency, if any. Since the recommendation is to reduce the number of documents that are to be filed along with the application and most of the documents related to refund application will be available online, it is recommended that the preliminary scrutiny may be carried out within 30 common working days and

deficiency, if any, should be communicated to the applicant directly from the respective tax portal. (In case refund relates to different jurisdictions or involves both central and state GST levy, then the said deficiency needs to be forwarded to GSTN also which will communicate the same to the corresponding tax authority relating to that refund).

9.1 It is recommended that tax authorities should make efforts to ensure that piecemeal queries are avoided. Applicant may file his reply through the respective tax authority portal / GSTN. Any further queries should be raised only with the approval of higher authorities so that unnecessary queries are avoided. Once the refund application is found to be complete in all respect, the same may be communicated to applicant via SMS and e mail and the date of communication shall be considered as the relevant date for the purpose of time limit prescribed for sanctioning of refund and initiation of interest clause.

PROCEDURE FOR DEALING WITH REFUND THEREAFTER INCLUDING EXAMINATION OF PRINCIPLE OF “UNJUST ENRICHMENT” :

10.0 Once the refund application is found to be complete and the fact of completeness has been intimated to the applicant, the jurisdictional tax authority should examine the same in the light of the provisions of the GST Law relating to refund. Important parameters include the timeliness of refund application, tax payment, date of export (if relating to export), reasons for refund etc.

10.1 It is recommended that for the sake of uniformity, the state and central laws should have similar provisions.

10.2 As GST is an indirect levy, there is always a rebuttable presumption that the tax has been passed on to the ultimate consumer by the applicant. So it is essential that every refund application should be examined in light of the principle of “unjust enrichment” and the appropriate provisions may be incorporated in the GST law. The burden of discharging the obligation under “unjust enrichment” should be on the applicant and documents manifesting the same should be submitted along with the application. As discussed above, a Chartered Accountant’s Certificate certifying the fact of non-passing of the GST burden by the taxpayer, being claimed as refund should be submitted. The GST Law Drafting Committee may prescribe a threshold amount below which self-certification (instead of CA Certificate) would be sufficient.

10.3 If the refund is not found to be legal or correct for any reason, then the jurisdictional authority should issue Show Cause Notice (SCN) to the applicant and thereafter the refund will be kept in abeyance in the system till the SCN is adjudicated. In case, the refund application is found to be in order but does not satisfy the test of unjust enrichment, the refund amount, after sanction, would be credited to the Consumer Welfare Fund. The GST Law Drafting Committee may examine whether such amount should be credited to Consumer Welfare Fund or to the consolidated fund of State / Union.

MINIMUM AMOUNT BELOW WHICH REFUND SHALL NOT BE GRANTED:

11. Filing of refund application and processing of the same involves investment of resources, in terms of time, money and manpower, by both

the applicant and tax administration. Therefore the amount should not be meager enough to create uneconomical burden on the applicant as well as tax administration. Looking at the rising inflation, it is recommended that an amount in the range of Rs. 500-1000/- may be fixed below which refund shall not be granted. This limit should be uniform for both CGST/IGST and SGST.

SANCTIONING OF REFUND.

12. To make the process of refund hassle free, it is important that even this last stage of refund processing should be simple and free from human intervention so that the applicant may have a pleasant experience while dealing with tax authorities. Therefore it becomes significant that once the tax authority decides about sanctioning of the refund, the same shall be granted to the applicant promptly. For this it would be essential that the details of the bank account are sought from the applicant at the time of filing of the refund application itself so that the amount of refund can be transferred to the applicant electronically through NEFT /RTGS/ECS.

VERIFICATION AND CONTROL.

13. Every refund that is sanctioned would need to go through a process of review by higher authorities in order to ensure the correctness of the decision of refund sanctioning authority. So once the refund is sanctioned, the same shall be transferred through the IT system to the menu of the higher authority along with the documents on the basis of which decision was taken by the refund sanctioning authority. Any documents that were sought besides those in the application should also be forwarded manually to the higher authority for taking a decision about review of the order. It is essential that there is simultaneous flow of the refund documents in paper

along with the electronic application to the audit section so that the process of post audit can be carried out concurrently.

13.1 It is recommended that looking at the higher level of compliance and self regulating mechanism in the form of system based ITC verification, uploading of sales and purchase invoices, reconciliation, compliance rating etc. post audit of refund application (and not of the accounts of the taxpayer) can be dispensed with if so decided by the respective Tax Jurisdiction for refunds upto Rs. One lakh for normal taxpayers and for refund upto Rs. 2 lakhs for certain prescribed categories of applicants (like public sector undertakings, applicants having the AEO Status, etc.) but the process of review of refund may be provided in the GST Law.

13.2 Besides this, for refund amounts exceeding a pre-determined amount a provision for pre-audit of refund application (and not of the accounts of the taxpayer) before the sanction of the refund may be provided for. Keeping in view the points mentioned above regarding increased compliance, self-regulation and system based verification, etc., it is recommended that the monetary limit for pre-audit of the refunds sanctioned may be kept at Rs. one crore or as may be decided by the respective Tax Jurisdiction. The procedure for pre-audit will be same as that for the post audit except that the application will have to move to and fro between the refund sanctioning authority and the audit authority before grant of refund. The GST Law may provide that the process of audit should be time bound with clearly defined timeline so that quality of audit does not suffer from insufficiency of time.

13.3 It is recommended that either the review procedure or system of pre-audit & post-audit may be kept in the GST Law. GST Law Drafting Committee may provide for the appropriate provision.

INTEREST:

14. It is recommended that the GST Law may provide for a prescribed time limit of 90 days from the date of the system generated acknowledgment of refund application within which refund has to be paid. It may also be provided in the GST law that, interest clause will start automatically once the prescribed time limit for sanctioning of refund has been breached.

14.1 The issue relating to dealing with the refund cases in which refund application has been filed but the same is found to be incomplete or deficient was discussed. It is recommended that the GST Law may clearly specify that the time limit for payment of interest will start from the date of the electronically generated acknowledgement of the refund application signifying that the application is complete in all respects. The GST Law may also provide for a time limit of 30 days from the date of receipt of refund application for raising queries/ deficiency memos by tax authorities regarding incompleteness of the refund documents. Piecemeal queries must be avoided. Once the applicant files a reply to the deficiency memo and the refund application is found complete as per the prescribed documents, the same should be acknowledged electronically by the refund sanctioning authority and the time limit for interest will start from the date of such electronic acknowledgement.

14.2 It is recommended that the rate of interest for delayed payment of refund and that in case of default in payment of GST should be different. The Committee recommends that the rate of interest in case of refund may be around 6% and that in case of default in payment of interest may be

around 18%. The GST Law may provide accordingly. The GST Law may also provide that the interest will accrue from the last date when refund should have been sanctioned even when the refund is ordered to be paid by the order of the appellate authority in the appeal filed by the applicant against order of rejection passed by the refund sanctioning authority. This would discourage refund sanctioning authority from rejecting refund claims on frivolous grounds.

ADJUSTMENT:

15 In some cases, the taxpayer may have outstanding demand under GST Act. The GST Law may provide for adjusting the refund claim against any amount of un-stayed confirmed demand lying beyond the appeal period. The refund order may clearly state the amount so adjusted and particulars of the adjusted demand may also be stated in the annexure to be attached with the order. Format of Application for refund and Refund order can be designed accordingly. Suggested format is enclosed as Annexure-IV to VI to this document.

RECOVERY OF ERRONEUS REFUND:

16 It is recommended that the GST law may provide for the provisions for recovery of erroneously granted refunds along with interest.

(Satish Chandra)
Member Secretary
Empowered Committee
of State Finance Ministers

(Rashmi Verma)
Additional Secretary
Department of Revenue
Government of India

ANNEXURE-I

CONSTITUTION ORDER OF JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST

EMPOWERED COMMITTEE OF STATE FINANCE MINISTERS

DELHI SECRETARIAT, IP ESTATE, NEW DELHI – 110002

Tel. No. 2339 2431, Fax: 2339 2432 e-mail: vatcouncil@yahoo.com

No.15/45/EC/GST/2014/32

Date: 7th April, 2014

JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST

During the last Empowered Committee meeting held on 10th March, 2014, it was decided that a Joint Committee under the co-convenership of the Additional Secretary (Revenue), Government of India and the Member Secretary, Empowered Committee should be constituted to look into the Report of the Sub-Group-I on Business Processes for GST and make suitable recommendations for Registration and Return to the Empowered Committee. It was also decided that the Joint Committee should also keep in view the Registration and Return requirements necessary for IGST Model. Accordingly, a Joint Committee, in consultation with the Government of India, is constituted with the following members:

Government of India

- (1) Smt. Rashmi Verma, Additional Secretary (Revenue) -- Co-convener
- (2) Shri P.K. Mohanty, Joint Secretary (TRU-I)
- (3) Shri M. Vinod Kumar, Joint Secretary (TRU-II)
- (4) Shri J.M. Kennedy, Director (TRU-II)
- (5) Director/Deputy Secretary holding the charge of
State Taxes Section

States Government

- (1) Dr. J.B. Ekka, Commissioner of Taxes, Assam
- (2) Shri Prashant Goyal, Commissioner, Trade & Taxes, Delhi
- (3) Shri H.V. Patel, Commissioner, Commercial Tax, Gujarat
- (4) Shri Sudhir Rajpal, Commissioner, Excise & Taxation, Haryana

- (5) Shri Kifayat Hussain Rizvi, Commissioner, Commercial Tax, J&K
- (6) Shri Ajay Seth, Commissioner, Commercial Tax, Karnataka
- (7) Shri Shyam Jagannathan, Commissioner, Commercial Tax, Kerala
- (8) Shri Amit Rathore, Commissioner, Commercial Tax, Madhya Pradesh
- (9) Dr. Nitin Kareer, Commissioner, Sales Tax, Maharashtra
- (10) Shri Abhishek Bhagotia, Commissioner, Commercial Tax, Meghalaya
- (11) Shri Manoj Ahuja, Commissioner, Commercial Tax, Odisha
- (12) Shri Sanjay Malhotra, Commissioner, Commercial Tax, Rajasthan
- (13) Shri K. Rajaraman, Commissioner, Commercial Tax, Tamil Nadu
- (14) Shri M.K. Narayan, Commissioner, Commercial Tax, Uttar Pradesh
- (15) Shri Dilip Jawalkar, Commissioner, Commercial Tax, Uttarakhand
- (16) Shri Binod Kumar, Commissioner, Commercial Tax, West Bengal

Empowered Committee of State Finance Ministers

- (1) Shri Satish Chandra, Member Secretary -- Co-convener

2. The Committee will submit its report to the Empowered Committee in two months time.

Sd/-
(Satish Chandra)
Member Secretary
Empowered Committee of
State Finance Ministers

Copy to: All the Members of the Joint Committee

Copy also to:

- (1) PS to Chairman, Empowered Committee of State Finance Ministers
- (2) Adviser to Chairman, Empowered Committee of State Finance Ministers
- (3) Sr.A.O./OSD/F.O./A.O., Empowered Committee of State Finance Ministers

ANNEXURE-II

CONSTITUTION OF SUB-COMMITTEE ON GST REFUND PROCESSES

EMPOWERED COMMITTEE OF STATE FINANCE MINISTERS

DELHI SECRETARIAT, IP ESTATE, NEW DELHI – 110002

Tel. No. 2339 2431, Fax: 2339 2432 e-mail: vatcouncil@yahoo.com, vatcouncil@gmail.com

No.15/45/EC/GST/2014/170

Date: 14th November, 2014

CONSTITUTION OF SUB-COMMITTEE ON GST REFUND PROCESSES

During the last meeting of the Joint Committee on Business Process for GST held on 12th November, 2014, it was decided to form a Sub-Committee to look into the GST refund processes. Accordingly, a Sub-Committee consisting of the following is constituted:

Government of India

- (1) Shri Upender Gupta, Additional Commissioner, GST Cell -- Co-convener
- (2) Shri Manish Sinha, Director (CX)
- (3) Shri Rajiv Yadav, Director (ST)

State Governments

- (1) Shri Manoj Ahuja, Commissioner, Commercial Tax -- Co-convener
Government of Odisha
- (2) Shri Amit Rathore, Commissioner, Commercial Tax,
Government of Madhya Pradesh
- (3) Dr. Nitin Kareer, Commissioner, Sales Tax, Government
of Maharashtra
- (4) Shri M. Girees Kumar, Commissioner, Commercial Tax,
Government of Kerala

Goods and Services Tax Network

- (1) Shri Prakash Kumar, Chief Executive Officer

Special Invitee

- (1) Shri Ajay Seth
2. The Sub-Committee should submit its report in one month's time.

Sd/-
(Satish Chandra)
Member Secretary
Empowered Committee of
State Finance Ministers

Copy to: All the Members of the Committee

LIST OF PARTICIPANTS OF THE MEETING HELD ON 22ND AND
23RD JULY, 2015

Government of India

1. Smt. Rashmi Verma, Additional Secretary (Revenue), Government of India
2. Shri Rajeev Yadav, Director (Service Tax), CBEC, Government of India
3. Shri B.B. Agrawal, Principal Commissioner, CBEC, Government of India
4. Shri Upender Gupta, Commissioner, GST, CBEC, Government of India
5. Shri M.K. Sinha, Commissioner (LTU), Audit, CBEC, Government of India
6. Shri G.D. Lohani, Commissioner, CBEC, Government of India
7. Shri Ravneet Singh Khurana, Deputy Commissioner, CBEC, Government of India
8. Shri Sachin Jain, Additional Commissioner, CBEC, Government of India
9. Shri P.K. Manderna, Superintendent (GST Cell), Government of India

States

1. Shri Gautam Das Gupta, Deputy Commissioner of Taxes, Assam
2. Shri T. Ramesh Babu, Additional Commissioner, Commercial Tax, Andhra Pradesh
3. Shri Arun Kumar Mishra, Joint Secretary, Finance, Bihar
4. Shri Santosh Kumar Sinha, Additional Commissioner, Commercial Tax, Bihar
5. Shri Deepak Kanan, Additional Commissioner, Commercial Tax (GST), Bihar
6. Shri R.K. Trivedi, Additional Commissioner, Commercial Tax, Chhattisgarh
7. Shri Kishor Bhalla, Deputy Commissioner (VAT), Daman & Diu and Dadra & Nagar Haveli
8. Shri Vijay Kumar, Commissioner (VAT), Trade and Taxes, Delhi
9. Shri Jagmal Singh, Deputy Director, Trade and Taxes, Delhi
10. Shri Dipak M. Bandekar, Additional Commissioner, Commercial Tax, Goa
11. Dr. P.D. Vaghela, Commissioner, Commercial Tax, Gujarat
12. Ms. Aarti Kanwar, Special Commissioner, Commercial Tax, Gujarat

13. Shri Shyamal Misra, Commissioner, Excise & Taxation, Haryana
14. Shri Hanuman Singh, Additional Commissioner, Excise & Taxation, Haryana
15. Shri J.C. Chauhan, Commissioner, Excise & Taxation, Himachal Pradesh
16. Shri P.K. Bhat, Additional Commissioner, Commercial Tax, Jammu & Kashmir
17. Smt. Nidhi Khare, Secretary-cum-Commissioner, Commercial Tax, Jharkhand
18. Dr. M.P.Ravi Prasad, Joint Commissioner, Commercial Tax, Karnataka
19. Dr. Rajan Khobragade, Commissioner, Commercial Tax, Kerala
20. Shri M.I. Mansur, Assistant Commissioner, Commercial Tax, Kerala
21. Shri Sudip Gupta, Deputy Commissioner, Commercial Tax, Madhya Pradesh
22. Shri P. Velrasu, Special Commissioner, Sales Tax, Maharashtra
23. Shri B.V. Borhade, Joint Commissioner, Sales Tax, Maharashtra
24. Shri P.M. Kulkarni, Deputy Commissioner, Sales Tax, Maharashtra
25. Shri K. Sanglawma, Commissioner of Taxes, Mizoram
26. Shri H. Rangthanmawia, Superintendent of Taxes (GST Cell), Mizoram
27. Shri Niten Chandra, Commissioner, Commercial Tax, Odisha
28. Shri Sahadev Sahoo, Joint Commissioner, Commercial Tax, Odisha
29. Shri K. Sridhar, Deputy Commissioner, Commercial Tax, Puducherry
30. Dr. Karthik, Additional Secretary, Punjab
31. Shri Pawag Garg, Additional Commissioner, Excise & Taxation, Punjab
32. Shri Vaibhav Galriya, Commissioner, Commercial Tax, Rajasthan
33. Shri Manoj Rai, Joint Commissioner, Commercial Tax, Sikkim
34. Shri D. Soundraraja Pandian, Joint Commissioner (Taxation), Commercial Taxes, Tamil Nadu
35. Shri K. Chandrasekhar Reddy, Additional Commissioner, Commercial Tax, Telangana
36. Shri Vikas Singh, Commissioner of Taxes and Excise, Mizoram
37. Shri Vivek Kumar, Additional Commissioner, Commercial Tax, Uttar Pradesh
38. Shri Abhijit Gupta, Commercial Tax Officer (IT), Uttar Pradesh
39. Shri N.C. Sharma, Additional Commissioner, Commercial Tax, Uttarakhand
40. Smt. Ujjaini Datta, Joint Secretary, Finance, West Bengal

Goods and Services Tax Network (GSTN)

1. Shri Navin Kumar, Chairman, Goods and Services Tax Network
2. Shri Prakash Kumar, Chief Executive Officer, Goods and Services Tax Network

Empowered Committee of State Finance Ministers

1. Shri Satish Chandra, Member Secretary, Empowered Committee
2. Shri Bashir Ahmed, Adviser, Empowered Committee

ANNEXURE-IV

Government of -----

Department of -----

Form GST –

Refund Claim Form under ----- Goods & Services Tax Act, -----

(To be used by Tax Payers only)

1. GSTIN															

2. Full Name of Taxpayer															

3. Taxpayer's address	Building Name/ Number														
	Area/ Road														
	Locality/ Market														
	Pin Code														

4. Amount of refund claimed (Rs.)	IGST	CGST	SGST

5. Ground for claiming refund (provide reasons in detail, attach additional sheets, if required) [Attach /upload supporting documents)	

6. Tax Period for which refund claimed	From								To							
		dd	mm	yy	dd	mm	yy									

7. Details of Bank Account															
i) Bank Account No.															
ii) Bank Account Type															
iii) Operated in the name of															
iv) Name & Address of Bank/Branch															
v) MICR No. / IFSC															

8. Verification

I/We _____ hereby solemnly affirm and declare that the information given hereinabove is true and correct to the best of my/our knowledge and belief and nothing has been concealed therefrom.

Signature of Authorised Signatory _____

Full Name (*first name, middle, surname*) _____

Designation / Status _____

Place																						

Date								
	Day		Month		Year			

ANNEXURE-V

Department of -----

Government of -----

Form GST –

[See Rule -]

Reference No.

Date -

Refund order under ----- Goods & Services Tax Act, ----

[illegible][illegible][illegible]

4. Receipt No. & date of refund application	Receipt No. -	Receipt date -

5. Act	Tick ☒ one	☐ IGST	☐ CGST	☐ SGST
6. Type of refund application	Tick ☒ one	☐ Return type	☐ Return type	☐ Application

Note - Return type can be regular & composition (say, GST-20,21) etc.

7. Tax Period for which refund claimed	From							To							
		dd	mm	yy		dd	mm		yy						

[illegible]

(vi) Net amount of refund payable	(iii + iv – v)																		
9. Details of Bank Account																			
i) Bank Account No.																			
ii) Bank Account Type																			
iii) Operated in the name of																			
iv) Name & Address of Bank/Branch																			
v) MICR No. / IFSC																			

(Signature)

Name

(Designation)

Ward/Circle/Unit/Other

(Place)

(Date)

Note - Please quote your GSTIN while communicating with the department ----- in this matter or in any other matter whatsoever.

ANNEXURE-VI

Reduction / Adjustment Summary

Sr No.	Description	Year & Tax Period	Amount (reduction / adjustment)	Order No.	Order date	Balance demand, if any remaining after adjustment
1	2	3	4	5	6	7
1.	Reduction of refund amount					
2.	Adjustment against outstanding demand					
	Total					

(Signature)

Name

(Designation)

Ward/Circle/Unit/Other

(Place)

(Date)

ANNEXURE-VII

Department of -----

Government of -----

Form GST - [See Rule --]

Refund Claim Form under ---- Goods & Services Tax Act, -----

[To be used only by Embassies, International and Public Organisations and their Officials]

1. Registration No.												

2. Tax Period for which refund claimed	From							To						
		dd	mm	yy	dd	mm	yy							

3. Full Name of Embassy / Organisation /													

4. Address of Embassy / Organisation	Building Name/ Number													
	Area/ Road													
	Locality/ Market													
	Pin Code													
	Email Id													
	Telephone Number													
	Fax Number													

5. Entry Number of ---- Schedule under which the applicant is eligible to claim refund		

6. Amount of refund claimed (Rs.) (As per invoice detail provided below)	IGST				CGST				SGST			

7. Details of purchases of tax paid goods in respect of which refund of tax is sought

Sr. No.	Invoice date	Invoice No.	Supplier's GSTIN	Supplier's Name	Value / Price (excluding tax)	Tax (Rs.)		
						IGST	CGST	SGST
1	2	3	4	5	6	7	8	9
Total								

8. Details of Bank Account in which refund should be remitted	Bank Account Number																		
	Bank Account Type																		
	Operated in the name of																		
	MICR / IFSC																		
	Name of Bank																		
	Address of Branch																		

9. Verification

I/We _____ hereby solemnly affirm and declare that the information given hereinabove is true and correct to the best of my/our knowledge and belief and nothing has been concealed therefrom.

Signature of Authorised Signatory _____

Full Name (*first name, middle, surname*) _____

Designation / Status _____

Place																				

Date																				
	Day		Month		Year															

REPORT

OF

THE JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST

ON

GST REGISTRATION

Empowered Committee of State Finance Ministers

New Delhi

July, 2015

Sl No.	Chapters	Page Number
1	Introduction	3
2	Assumptions	4
3	Structure of registration number	8
4	Procedure for obtaining Registration	10
5	Facilitation Centers and Tax Return Preparer Scheme	10
6	New Applicants	11
7	Migration of existing registrants	19
8	Registration of Compounding Dealers	22
9	Amendments in the Registration Form	22
10	Cancellation/surrender of registration	23
11	Explanation of the Entries in the Form (<i>should be attached to the Form</i>)	24-26
Annexures		
I	Constitution Order of Joint Committee on Business Process for GST	27-28
II	List of Participants of the meeting held on 2 nd and 3 rd February, 2015	29-30
III	GST Registration Application Form	31-39
IV	Application Form for Surrender / Cancellation of registration	40-42
V	Application Form to opt for Compounding Scheme	43-44
VI	Application Form to withdraw from Compounding Scheme	45-46
VII	Application for Amendment of registration subsequent to Registration	47
VIII	<u>Extract of the report of the Committee on the problem of dual control, threshold and exemptions in GST regime</u>	48
IX	Extract of the minutes of refinement to the process for States option for two-way API based integration	49-50
X	<u>Extract of the report of the Committee on IGST and Imports.</u>	51-52

Report of the Joint Committee on Business Processes for GST on Registration Processes in GST Regime

1.0 Introduction

During the Empowered Committee meeting held on 10th March, 2014, it was decided that a Joint Committee under the co-convenership of the Additional Secretary (Revenue), Government of India and the Member Secretary, Empowered Committee should be constituted to look into the Report of the Sub-Group-I on Business Processes for GST and make suitable recommendations for Registration and Return to the Empowered Committee. It was also decided that the Joint Committee should also keep in view the Registration and Return requirements necessary for IGST Model. Accordingly, a Joint Committee, in consultation with the Government of India, was constituted on 7th April, 2014 (Annexure-I).

1.1. The Committee held its deliberations on 28th October, 2014, 12th November, 2014, 25th November, 2014, 22nd December, 2014, 2nd and 3rd February, 2015, 19th and 20th February, 2015, 16th and 17th April, 2015 and 7th and 8th July, 2015. The Report of the Joint Committee on Business Processes on Registration was accordingly circulated to all the States. However, this Report was further discussed in the meeting of the Joint Committee on Business Processes held on 22nd and 23rd July, 2015. Some changes were made as per the discussions in the meeting of the Joint Committee on Business Processes held on 22nd and 23rd July, 2015. The report of the Joint Committee on Business Processes on Registration was accordingly finalized. The list of the participants of the meeting of the Joint Committee on Business Processes held on 22nd and 23rd July, 2015 is appended at Annexure-II.

1.2. Registration of a business with the tax authorities implies obtaining a unique identification code from the concerned tax authorities so that all the operations of and data relating to the business can be agglomerated and correlated. In any tax system this is the most fundamental requirement for identification of the business for tax purposes or for having any compliance verification program. Registration under Goods and Service Tax (GST) regime will confer following advantages to the business:

- Legally recognized as supplier of goods or services.
- Proper accounting of taxes paid on the input goods or services which can be utilized for payment of GST due on supply of goods or services or both by the business.
- Pass on the credit of the taxes paid on the goods or services supplied to purchasers or recipients.

2.0 Assumptions

2.1 The business process proposed in this document is based on the following assumptions:

(1) A legal person without GST registration can neither collect GST from his customers nor claim any input tax credit of GST paid by him.

(2) There will be a threshold of Gross Annual Turnover including exports and exempted supplies (to be calculated on all-India basis¹) below which any person engaged in supply of Goods or Services or both will not be required to take registration. Once a dealer crosses the required threshold or he starts a new business, registration application must be filed within 30 days from the date of the dealer's liability for obtaining such registration. Effective date of registration would be the date of application in all cases i.e. whether the application has been filed within prescribed time limit of 30 days or otherwise. The taxpayer would be eligible for ITC in respect of all his purchases from the date of application in case application for registration has been filed within 30 days. The taxpayer would, however, not be eligible for ITC in respect of his purchases prior to the date of registration in case the registration application is not filed within the prescribed time limit of 30 days, although Centre is of the view that such a provision may not stand the test of judicial scrutiny. On the other hand States, based on their experience under VAT, were of the view that having relevant provision in the GST law has helped them contest cases in courts. **GST Law Drafting Committee to make provision relating to eligibility for ITC accordingly as well as for levying penalty in case of a dealer failing to register within the stipulated time period.**

¹ Please refer Para 7 of the **Report of the Committee on the Problem of Dual Control, Threshold and Exemptions in GST Regime (Annexure-VIII)**

(3) However, such person with all-India gross annual turnover below the threshold turnover would be allowed to take registration, if he wants to. By taking such voluntary registration he can enter the credit chain even prior to crossing the threshold limit, provided he does not opt for the Compounding scheme (as defined below).

(4) There will be another relatively higher threshold of Gross Annual Turnover (to be calculated on all-India basis) to be called Compounding turnover up to which the registered person can opt to pay tax at a specified percentage of the turnover, without entering the credit chain. Such registered person will neither be allowed to collect tax from his customers nor claim any input tax credit. Compounding dealers shall remain under compounding scheme till their turnover crosses threshold or they opt out of the scheme. Such dealers don't have to apply every year to remain under the compounding scheme. However, if the compounding dealer opts out of compounding in a financial year, for any reason, but eligible and wish to avail compounding in the next financial year, such dealer will have to apply afresh for compounding in the beginning of the financial year in which he wishes to claim compounding scheme.

(5) All other taxable persons will be required to take GST registration. Such persons will be able to take the credit of taxes paid on inputs / input services / capital goods and pass on the credit of GST to his customers / recipients of goods or services or both.

(6) The registered person eligible for the Compounding scheme but opting against the Compounding can pay regular taxes and file tax returns on monthly basis, and thereby make his supplies eligible for input tax credit in the hands of the purchasers/recipients.

(7) Irrespective of turnover, if a taxable person carries out any inter-state supply and / or is liable to pay GST under reverse charge, he will be compulsorily required to take registration. Such person shall neither be eligible for exemption threshold nor for Compounding scheme. **However, an individual importing services for personal consumption will not be liable to pay GST under reverse charge or register under GST if the GST law so provides.**

(8) All UN bodies seeking to claim refund of taxes paid by them would be required to

obtain a unique identification number (ID) from the GST portal. The structure of the said ID would be uniform across the States in uniformity with GSTIN structure and the same will be common for the Centre and the States. The supplier supplying to these organizations is expected to mention the UID on the invoices and treat such supplies as B2B supplies and the invoices of the same will be uploaded by the supplier.

(9) A unique identification number (ID) would be given by the respective state tax authorities through GST portal to Government authorities / PSUs **not making outwards supplies of GST goods (and thus not liable to obtain GST registration)** but are making inter-state purchases. The structure of the said ID would be uniform across the States in uniformity with GSTIN structure. The supplier supplying to these organizations is expected to mention the UID on the invoices and treat such supplies as B2B supplies and the invoices of the same will be uploaded by the supplier.

(10) **The concept of Input Service Distributor (ISD) presently being followed in Centre's Law may continue if the GST Law so provides.** They would be required to obtain GSTIN for distributing the credit of GST paid on services proposed to be used at multiple locations which are separately registered. This would be an exception/ deviation in case of services only. **GST Law Drafting Committee to make appropriate provisions for the same.**[While, at this stage it has been decided to make exception only for services, it is worth mentioning here that the Cenvat Credit Rules provide for a mechanism to allow distribution of inputs, which is basically a mechanism to distribute credit on inputs. Such mechanism is necessary for service provider as the location of payment of GST may be distinct from the location where goods are received. Therefore, drafting Committee may look into this issue.]

(11) All existing registered persons, whether with the Centre or State under any of the tax statutes being subsumed in GST, would be allotted a GST registration number called Goods and Services Tax Identification Number (GSTIN) on voluntary basis. Dealers who are below the GST threshold will have option to remain in GST chain. **GST Law Drafting Committee to make appropriate provision.**

(12) Tax authorities, in case of enforcement cases, may grant suo-moto registration. If

such person does not have PAN, the registration would be initially temporary and later converted into a PAN based registration. [GSTN to develop temporary registration numbering system]

2.2 For each State the taxable person will have to take a separate registration, even though the taxable person may be supplying goods or services or both from more than one State as a single legal entity.

2.3 Multiple registrations within one State to business verticals [as defined in Accounting Standard (AS) 17 issued by ICAI] of a taxable person may also be permitted, subject to all the verticals being on the same scheme of tax treatment **if the GST Law so provides.**

2.4 A supplier who is not registered on regular basis, whether on mandatory or voluntary basis, in other State (s) and desires to conduct business in a particular State for a limited period, will have to obtain registration in that State for that limited period. Such suppliers are known as casual dealers and shall not be allowed to opt for composition scheme. However, the supplier would be eligible to claim ITC on purchases / inward supplies. The period of registration would be mentioned in the registration certificate also. The format of Registration Certificate for such taxpayers is different from the regular taxpayers. Even the application form for registration will have field for ascertaining estimated supplies. Return for such taxpayers would also be different. Such taxpayers would be required to self-assess their likely liability and deposit the same as an Advance Tax. Such amount would be deposited by way of two Demand Drafts (one for Centre and other for State) which would be returned to the taxpayer after he has discharged his final liability. **The GST Law Drafting Committee may provide for conditions for registration and tax payment.**

2.5 A Non-resident Supplier is a person who, in the course of business, makes an intra-state supply of goods or services or both, but is not a resident in the state in which he has applied for registration, but is already registered in any other state. Since the Non-Resident Supplier is already registered in another State, there would be an easy way of registering such entities in the State in which registration is applied as Non-Resident Supplier. The provisions applicable on casual dealers (as detailed in para

2.4 above) may apply to them except that no security deposit or advance tax collection may be made in their case.

3.0 Structure of registration number

3.1 Each taxpayer will be allotted a State wise PAN-based 15-digit Goods and Services Taxpayer Identification Number (GSTIN).

3.2 Various digits in GSTIN will denote the following:

State Code		PAN										Entity Code	BLANK	Check Digit
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15

3.3 In the GSTIN, the State Code as defined under the Indian Census 2011 would be adopted. In terms of the Indian Census 2011, each State has been allotted a unique two digit code e.g. '09' for the State of Uttar Pradesh and '27' for the State of Maharashtra.

3.4 13th digit would be alpha-numeric (1-9 and then A-Z) and would be assigned depending on the number of registrations a legal entity (having the same PAN) has within one State. For example, a legal entity with single registration within a State would have '1' as 13th digit of the GSTIN. If the same legal entity goes for a second registration for a second business vertical in the same State, the 13th digit of GSTIN assigned to this second entity would be '2'. This way 35 business verticals of the same legal entity can be registered within a State.

3.5 14th digit of GSTIN would be kept BLANK for future use.

3.6 In GST regime, multiple registrations within a State for business verticals of a taxable person would be allowed. This provision should be subject to following specific stipulations –

- (1) Input Tax Credit across the business verticals of such taxable persons shall not be allowed unless the goods or services are actually supplied across the verticals.
- (2) For the purpose of recovery of dues, all business verticals, though separately registered, will be considered as a single legal entity. **(Final view needs to be taken by the GST Law drafting committee)**

3.7 Switching over from Compounding scheme to Normal scheme and *vice-versa* would be dealt in the manner described below –

- (1) Any existing taxpayer not under Compounding scheme may opt for Compounding scheme, if eligible, only from the beginning of the next Financial Year. The application will have to be filed on or before 31st March of the previous year so that Returns can be filed accordingly.
- (2) Compounding dealer may be allowed to switch over to Normal scheme even during the year if they so want, with a condition that they cannot switch over to Compounding scheme again during the same financial year.
- (3) Any existing taxpayer under the Compounding scheme upon crossing the Compounding threshold will be switched over to the Normal scheme automatically from the day following the day of crossing the Compounding threshold. **GST Law drafting committee should provide for a suitable time-period of inputs and capital goods purchases on which ITC would be permitted at the time of switching over to Normal scheme.**
- (4) For the changes covered by (1) to (3) above, the validation in the return module should change automatically under intimation to the concerned taxpayer and both the tax authorities. A suitable validation / dependency of the return module should be established.

The above changes should also be published on the common portal in addition to being

intimated to other taxpayers who have identified such taxpayer as their counter-party taxpayer.

4.0 Procedure for obtaining Registration

4.1 For obtaining registration, all the taxable persons shall interact with tax authorities through a common portal called GST Common Portal² that would be set up by Goods and Services Tax Network (GSTN). The portal will have backend integration with the respective IT systems of the Centre and States.

4.2 The procedure prescribed in para 6.0 below is meant for new applicants. The procedure for migration of existing registrants either with the Centre or State or both is dealt in para 7.0 below.

4.3 A new applicant would be allowed to apply for registration without prior enrollment. Once a complete application is submitted online, a message asking for confirmation will be sent through e-mail and SMS to the authorized signatory of the applicant. On receipt of such confirmation from the authorized signatory, Acknowledgement Number would be generated and intimated to the applicant. Once the application is approved and GSTIN is generated, the same along with Log-in ID and temporary Password will be sent to the authorized signatory. This credential will be permanently used to access the GST Common Portal subsequently. Provision for capturing e-mail and Mobile Number of authorized representative of the taxpayer has also been incorporated in the proposed GST Registration Form. It would be the responsibility of the taxpayer to keep this information updated.

4.4 Online verification of PAN of the Business / Sole Proprietor/ Partner/Karta/**Managing Director and whole time directors**/Member of Managing Committee of Association, Managing trustee/authorized signatory etc. of the business would be mandatory and without such verification, registration application will **not be allowed to be submitted**.

5.0 Facilitation Center and Tax Return Preparer Scheme

5.1 In order to cater to the needs of taxpayers who are not IT savvy, following facilities shall be

² Refinement to the process for States opting for two-way API based integration and flexibility (decision dated 18.4.2012 of EC) will be formulated separately(**Annexure-IX**).

made available:-

5.2 Tax Return Preparer (TRP): A taxable person may prepare his registration application / returns himself or can approach the TRP for assistance. TRP will prepare the said registration document / return in prescribed format on the basis of the information furnished to him by the taxable person. The legal responsibility of the correctness of information contained in the forms prepared by the TRP will rest with the taxable person only and the TRP shall not be liable for any errors or incorrect information. **If so provided in the GST law, TRPs would be approved by the tax administration of the Centre and the States and will also be provided appropriate training by them, as per common curriculum to be devised by EC/ GST Council.**

5.3 Facilitation Centre (FC) shall be responsible for the digitization and / or uploading of the forms and documents including summary sheet duly signed by the Authorized Signatory and given to it by the taxable person. After uploading the data on common portal using the ID and Password of FC, a print-out of acknowledgement will be taken and signed by the FC and handed over to the taxable person for his records. The FC will scan and upload the summary sheet duly signed by the Authorized Signatory. This is the system in vogue for submitting TDS returns by more than 2 million tax deductors to the Income Tax Department.

5.4 Registration of TRP/FC is recommended. Final view may be taken by the GST Law drafting committee on the same.

6.0 New Applicants

6.1 The process highlighted in the paragraphs below is applicable for new applicants for registration, both mandatory and voluntary.

6.2 New applicant can apply for registration:

(1) at the GST Common Portal directly³; or

³ Refinement to the process for states opting for two-way API based integration and flexibility (decision dated 18.4.2012 of EC) will be formulated separately(**Annexure-IX**).

(2) at the GST Common Portal through the Facilitation Center (FC)

Multiple applications can be filed at one go where a taxable person seeks registration in more than one State or for more than one business vertical located in a single / multiple State(s).

6.3 Following scanned documents are required to be filed along with the application for Registration –

Relevant Box No. in the Registration Form	Document required to be uploaded	Reason for requirement
2. Constitution of Business	• Partnership Deed in case of Partnership Firm ; • Registration Certificate in case of other businesses like Society, Trust etc. which are not captured in PAN.	In case of Companies, GSTN would strive for online verification of Company Identification Number (CIN) from MCA21. Constitution of business / applicant as per PAN would be taken except for businesses such as Society, Trust etc. which are not captured in PAN. Partnership Deed would be required to be submitted in case of Partnership Firms.
11. Details of the Principal Place of business	• In case of Own premises – any document in support of the ownership of the premises like Latest Tax Paid Receipt or Municipal Khata copy or Electricity Bill copy • In case of Rented or Leased premises – a copy of the valid Rent / Lease Agreement with any	This is required as an evidence to show possession of business premises. If the documentary evidence in Rent Agreement or Consent letter shows that the Lessor is different from that shown in the document produced in support of the ownership of the property, then the case must be flagged as a “Risk

	document in support of the ownership of the premises of the Lessor like Latest Tax Paid Receipt or Municipal Khata copy or Electricity Bill copy • In case of premises obtained from others, other than by way of Lease or Rent – a copy of the Consent Letter with any document in support of the ownership of the premises of the Consenter like Municipal Khata copy or Electricity Bill copy • Customer ID or account ID of the owner of the property in the record of electricity providing company, wherever available should be sought for address verification.	Case”, warranting a post registration visit for verification. GST Law Drafting Committee may add penalty provision for providing wrong lease details.
12. Details of Bank Account (s)	Opening page of the Bank Passbook held in the name of the Proprietor / Business Concern – containing the Account No., Name of the Account Holder, MICR and IFS Codes and Branch details	This is required for all the bank accounts through which the taxpayer would be conducting business.
17. Details of Authorised Signatory	For each Authorised Signatory • Letter of Authorisation or copy of Resolution of the Managing Committee or Board of Directors to that effect	This is required to verify whether the person signing as Authorised Signatory is duly empowered to do so.
Photograph	• Proprietary Concern – Proprietor • Partnership Firm / LLP – Managing/ Authorized	

	Partners (personal details of all partners is to be submitted but photos of only ten partners including that of Managing Partner is to be submitted) • HUF – Karta • Company – Managing Director or the Authorised Person • Trust – Managing Trustee • Association of Person or Body of Individual –Members of Managing Committee (personal details of all members is to be submitted but photos of only ten members including that of Chairman is to be submitted) • Local Body – CEO or his equivalent • Statutory Body – CEO or his equivalent • Others – Person in Charge

6.3.1 For Field No 16 (i.e. Details of Proprietor / all partners / Karta / Managing Director and whole-time Director / Members of the Managing Committee of Association of Persons / Board of Trustees etc.) and Field No 17 (i.e. Details of the Authorized Signatory), verification of PAN with CBDT database and GSTN database will be carried out online before the submitted application is sent to the State/ Centre. In case of mismatch the applicant will be given an opportunity to correct the same.

6.4A registration form has been designed and is annexed as Annexure-III. This form should be developed by GSTN as per the standard practices / protocols on IT notified by the Govt. of India e.g. for digitally capturing a postal address, name etc. *In case there is no standard practice for any of the field, the same should be developed by the GSTN and form designed accordingly.* Fields marked by asterisk in the form are mandatory fields and must be filled by the applicant.

Separate application forms are to be designed for:

- (1) Multiple registration for business verticals of same legal entity (it must be registered already) within a State;
- (2) Application for registration in more than one State (that can be filed at one go);
- (3) Amendments to existing Registration(s);
- (4) Cancellation of Registration(s);

- (5) Option to avail / withdraw from the Compounding scheme;
- (6) Enrolment of Tax Practitioner or Facilitation Centre if provided for in the GST Law;
- (7) Assignment of Role (by a dealer) to TP/FC, as agent of the dealer if so provided for in the GST Law;
- (8) Application for new registration on account of Succession / Amalgamation / De-merger etc. of existing GST registrants;
- (9) Application by UN bodies for getting a Unique Identification Number (ID).

6.5 In some North-eastern States, individuals (Proprietorship firms) are exempt from Income Tax. However, to obtain GSTIN they will have to obtain a PAN before they can apply for registration under GST. Further Government departments will also be required to obtain PAN if they are required to obtain registration under GST. Under *GST regime, registration will not be allowed without a valid PAN.*

6.6 If applicant files application through the Facilitation Center, then the above procedure shall be followed by him through the FC by making available the requisite documents to the FC. The User ID and Password of taxable person will however be forwarded by portal to the e-mail furnished by the taxable person (that of primary authorized signatory) and by SMS to the mobile number furnished by taxable person or by post, if the taxable person so desires. It will not be sent to FC.

6.7 The GST common portal shall carry out preliminary verification / validation, including real-time PAN validation with CBDT portal, Adhaar No validation with UIDAI, CIN (Company Identification) with MCA and other numbers issued by other Departments through inter-portal connectivity before submission of the application form. Taxpayers would have the option to sign the submitted application using valid digital signatures (if the applicant is required to obtain DSC under any other prevalent law then he will have to submit his registration application using the same). In the absence of digital signature, taxpayers would have to send a signed copy of the summary extract of the submitted application form printed from the portal to a central processing center to be operated by GSTN. The location details of this central processing center would be intimated to the applicant along with the application acknowledgement number. The application will be processed even without waiting for receipt of the signed copy of the summary extract. If the signed copy is not received within

30 days, a reminder will be sent through e-mail and SMS to the authorized signatory through the portal. If the copy is not received within 30 days after such reminder being sent, the system will prompt the concerned tax authority to initiate the action for cancellation of the registration. Such cancellation will have prospective effect i.e. from the date of cancellation. GST portal would acknowledge the receipt of application for registration and issue an Acknowledgement Number which could be used by the applicant for tracking his application. Such Acknowledgement Number would not contain the details of jurisdictional officers.

6.8 The application form will be passed on by GST portal to the IT system of the concerned State/ Central tax authorities for onward submission to appropriate jurisdictional officer (based on the location of the principal place of business) along with the following information –

- (1) Uploaded scanned documents;
- (2) State specific data and documents;
- (3) Details if the business entity is already having registration in other States. This should also include GST compliance rating⁴;
- (4) Details of the PAN(s) of individuals mentioned in the application which are part of the other GST registrations;
- (5) Acknowledgment number stated in para 6.7 above;
- (6) Details of any record of black-listing or earlier rejection of application for common PAN(s).
- (7) Last day for response as per the 3 common working day limit for both tax authorities as set out through Holiday Master.

On receipt of application in their respective system, the Centre / State authorities would forward the application to jurisdictional officers who shall examine whether the uploaded documents (as detailed in para 6.3 above) are in order and respond back to the common portal within 3 common working days, excluding the day of submission of the application on the portal, using

⁴ Please refer para 23 IX. of the report of the Committee on IGST and GST on imports (**Annexure-X**).

the Digital Signature Certificates.

An indicative process for processing of the application by the concerned tax authorities will be drafted and shared separately. Submission of latitude and longitude data in respect of principal place of business will be of help in automatic identification of jurisdictional officer in case of geographically distributed officials mapped on a digital map. However, submission of latitude and longitude would be optional.

6.9 After verification, the following situations are possible:

- (1) If the information and the uploaded documents are found in order, the State and the Central authorities shall approve the application and communicate the approval to the common portal within 3 common working days. The portal will then automatically generate the Registration Certificate.
- (2) If during the process of verification, one of the authorities raises some query or notices some error, the same shall be communicated to the applicant either by the Tax Authority directly or through the GST Common Portal and also simultaneously to the other authority and to the GST Common Portal within 3 common working days. The applicant will reply to the query / rectify the error / answer the query within a period informed by the concerned tax authorities (Normally this period would be seven days). A separate sub-process and interactive form for this purpose will have to be designed. On receipt of additional document or clarification, the relevant tax authority will respond within 7 common working days. **(time-period that would be allowed to the applicant for rectification of any error will be decided by the GST Law drafting committee)**
- (3) Thereafter the processing of registration application will commence resulting in either grant of registration or refusal to grant registration. If either of the two authorities (Centre or State) refuses to grant registration, the registration will not be granted.
- (4) In case registration is refused, the applicant will be informed about the reasons for such refusal through a speaking order. The applicant shall have the right to appeal

against the decision of the Authority. **A deeming provision to the effect that rejection of the registration application by one authority amounts to rejection by both Centre and State will need to be incorporated in the GST law.**

- (5) The tax authorities in the Centre and State would have a period of 3 common working days to respond to the application, either conveying approval or raising a query. In case any of the authority neither reject the application nor raise a query within 3 common working days, then the registration would be deemed to have been approved by both the authorities and the GST Common Portal will automatically generate the registration certificate. In case either authority raises a query within 3 common working days, applicant will have to respond to the same within next 7 common working days failing which the application will be rejected. After the applicant has responded to the query raised by any authority, a period of another 7 common working days will be given to the authorities to respond to the application. In case any of the authority neither rejects the application nor raises a query during this period, then the registration would be deemed to have been approved by both the authorities and the GST Common Portal will automatically generate the registration certificate. (**GST law to have provision for the same**)

6.10 The applicant shall be informed of the fact of grant or rejection of his registration application through an e-mail and SMS by the GST common portal. Jurisdictional details would be intimated to the applicant at this stage.

6.11 In case registration is granted, applicant can download the Registration Certificate from the GST common portal. **GST law may provide that GST Registration certificate shall be displayed at the principal place of business of the taxpayer.**

6.12 The GST common portal will provide a risk profile to the tax authorities based on the risk parameters made available by the tax authorities. The Central/State tax authorities will also have their own risk profile based on their own risk parameters. It was noted that submission of Adhaar No. cannot be made compulsory. Non –submission of Adhaar No. could be one of the risk parameters for deciding about the post registration physical verification. **On the basis of both risk profiles, the**

jurisdictional officer of tax authorities will take a decision about post registration verification of the application if so provided in the GST Law.

6.13 GST Law Drafting Committee may provide for appropriate provision for imposition of substantial penalty in cases of fraudulent registrations.

7.0 Migration of existing registrants

7.1 Existing registrants are those who are either registered with States or with the Centre or with both.

7.2 In case of such registrants, the system shall be designed to migrate cleaned and verified data from the existing database to the GST Common Portal and a GSTIN shall be generated. With regard to the migration of data of the existing registrants, following steps are necessary:

- (1) The process of migration of data must be started sufficiently in advance so that the business of existing registrants does not suffer and transition from the present system to GST is smooth.
- (2) At present, tax payers are separately registered with State and/ or with Central tax administrations or with both based on their business activity. In the GST regime, a taxpayer will have to obtain State wise registration. Even within a State, the taxpayer may either opt for a single registration or multiple registrations for different business verticals.
- (3) Analysis of registration data available with States and Centre conducted by NSDL and GSTN reveals the following:
 - a) The number of fields in the registration database of various State VAT and CBEC system are different than that finalized for GST. The number of fields varies from 50 to 107 in case of States/Centre whereas GST Registration Form has 120 fields. Thus there is a gap of 13 to 70 fields, meaning that data will have to be collected from the taxpayers.
 - b) As per report of NSDL, which conducted as is study of State Systems as well as that of CBEC, in majority of cases, the available data does not comply with Metadata and Data Standards (MDDS) of Government of India. This is also confirmed by the feedback

received from States in May 2015. Importing such data, which is not MDDS compliant, will lead to wrong or incomplete results on query.

- c) The data from States also shows that they do not have scanned copies of supporting documents for mandatory fields like principle place of business, photos of MD or Karta etc. in their database. This again will have to be collected from them.

Since, lots of reports will be using registration database, purity of registration data will be of paramount importance. Migrating half-complete and incorrect data from existing registration databases to GST database will adversely impact the reports and intelligence derived out of it. Thus data will have to be collected afresh from the existing taxpayers. GSTIN can be issued based on State and validated PAN. In case of taxpayers under Excise and VAT, source of data for issuing GSTIN should be VAT data as in most cases Excise assessee will also be registered under VAT. For taxpayers under Service Tax the source of data for issuing GSTIN should be Service Tax.

Out of six mandatory data fields in the GST Registration field, three can be filled up from validated PAN data, namely PAN, name of business, constitution of business. The name of State is known in case of VAT data. The remaining two mandatory data fields namely 'Principal Place of Business' and 'details of promoters' will have to be collected from taxpayers along with non-mandatory items. In case of Service Tax, State will have to be collected before generating GSTIN. With this the following process has been suggested:

(4) For Taxpayers Registered under State VAT/Excise

- i. GSTIN will be generated by NSDL in case of all VAT TINs where PAN has been validated. Along with a password the GSTIN will be sent to respective State Tax Authorities.
- ii. State tax authorities will communicate the GSTIN/password to taxpayers, with instruction to log on the GST portal and fill up the remaining data. State specific data over and above what is contained in the GST Registration Form can be collected after GST registration becomes operational.

- iii. The data so collected by GSTN/NSDL will be provided to States so that they can undertake the verification exercise as per their convenience after 1/4/2016 in a staggered manner spread over a period of one to two quarters so that it does not affect the working of the tax authorities. This is being suggested as the dealer is already registered with VAT department.
 - iv. In case, PAN has been validated but the email or mobile numbers of dealers are not available, such dealers may be advised through newspaper advertisement to visit the GST portal and use the following data for user authentication:
 - 1. VAT-TIN
 - 2. PAN
 - 3. Date of Birth/Date of Incorporation in DDMMYYYY format. (This data is available with PAN Database)
 - i. Date of birth of proprietor in case of Proprietorship firm.
 - ii. Date of incorporation in case of all other types of dealers.
 - v. In those cases where PAN has not been validated, State VAT department will have to collect the taxpayers.
- (5) In case of Service Tax, the taxpayers are not registered under a State, a different approach will have to be adopted.
- I. Since all Service Taxpayers have user ID and password and Service Tax has their email IDs, they may advise the taxpayers to intimate State(s) where they would like to get themselves registered in.
 - II. Service Tax portal will check from GST portal whether GSTIN has been generated for combination of State and PAN of the taxpayer. If not generated, request GST portal to generate the same.
 - III. GST portal will generate the GSTIN and communicate to Service Tax, which will be communicated to the taxpayer asking him/her to provide remaining data at GST Portal.
- (6) Any verification / updation of the information as outlined above would have to be

done by the taxable person within a specified period.

(7) If the verification/update is not done within the stipulated period, the GSTIN will be suspended till the taxable person does the needful.

(8) Any verification by State / Central authorities can be done after GSTIN is issued.

8.0 Registration of Compounding Dealers

8.1 Dealers below the Compounding ceiling will be provided with an option of availing the Compounding scheme i.e. they can pay the tax at Compounding rate (to be specified) without entering the credit chain.

8.2 Although the Compounding scheme is only a temporary phase before the taxable person starts functioning as a normal taxable person, separate format annexed as Annexure-V has been prescribed for enabling such taxable persons to opt for Compounding scheme. When the taxable person opts for Compounding scheme he should indicate so in the registration form and GST Common Portal would internally flag him as a Compounding dealer. Later on when he goes out of the Compounding scheme due to his turnover crossing the Compounding ceiling (change will be triggered by the tax return values) or he opts out of the scheme (through an amendment application annexed as Annexure-VI), the said flag will be removed and he would continue operating with the same registration number, without undertaking any fresh registration.

9.0 Amendments in the Registration Form

9.1 Capturing registration information is not a one-time activity and any change in critical information should be entered at the common portal within a stipulated time period. Except the fields mentioned in Para 7.2 (7) above, changes to other registration data can be done on self-service basis. The changes to fields mentioned in Para 7.2 (7) above and a change to Compounding scheme will require submission of reasons and prescribed relevant documents, and will be subject to approval by the concerned tax authorities. All amendments in the details in registration application form will be

retained in the database of the GSTN and will be made visible to the tax authorities.

10.0 Cancellation/Surrender of registration

10.1 In the following cases, the registration can be either surrendered by the registrant or cancelled by the tax authorities:

- (1) Closure of business of tax payer;
- (2) Gross Annual Turnover including exports and exempted supplies (to be calculated on all-India basis) falling below threshold for registration;
- (3) Transfer of business for any reason including due to death of the proprietor of a proprietorship firm;
- (4) Amalgamation of taxable person with other legal entities or de-merger;
- (5) Non commencement of business by the tax payer within the stipulated time period prescribed under the GST laws **(Suitable provision to be made in the GST law).**

10.2 In case of surrender, the system will send an acknowledgment by SMS and e-Mail to the applicant regarding his surrender of registration and he will be deemed to be unregistered from the date of such acknowledgement. There will be a provision in the system to prompt such surrendered registrants to update their address and mobile number at a prescribed periodicity till all dues are cleared/refunds made. Application form for Surrender / Cancellation of registration is annexed as Annexure-IV.

10.3 GST Law drafting committee would make appropriate provision for recovery of arrears, other dues and compliance verification pertaining to past periods.

10.4 The cancellation of registration may be done by tax authorities in the following situations:

- (1) In case signed copy of the summary extract of submitted application form is not received even after a reminder;
- (2) In case a tax payer contravenes specified provision of the GST law;
- (3) In case a taxpayer has not filed any return at all during a predetermined period (say six months). In case a taxpayer has filed a nil return continuously for this period, then the provisions of cancellation will not be applicable. **(GST Law drafting committee should provide for the time period for which if there is a continuous failure by a taxpayer to file returns, the registration shall be cancelled)**

- (4) The cancellation of registration may be preceded by system generated notice giving 7 days' time for furnishing reply by the taxpayer. Principle of natural justice to be followed before cancellation, i.e., giving an opportunity to taxpayer to be heard and passing of order.

10.5 If the taxpayer approaches the tax authority for revocation of surrendered or cancelled registration, the surrendered / cancelled registration can be revoked. The action for revocation would be initiated by that Authority which has cancelled the registration or had earlier accepted the surrender of registration.

10.6 The GST Law would contain appropriate provisions relating to revocation / surrender / cancellation of registration.

10.7 The action for revocation / cancellation of registration would have to be initiated by both Centre and State tax authorities. Once the registration is cancelled by one authority it would be deemed to be cancelled by other authority also.

10.8 The cancellation or surrender of registration would always have prospective effect.

11.0 Explanation of the Entries in the Form (should be attached to the Form)

11.1 The critical information / documents required from the applicant while making the application has been outlined in para 6.3 above. Here the manner of organization of the said information in the registration form (Annexure-III) has been explained.

11.2 The form has fields from 1- 21 requiring various details from the applicant. These fields have been organized so that applicant can introduce himself and the nature of his business to the tax authorities in simple interactive manner. To maintain uniformity in the manner of submission of the form, the fields are provided in the standard conventional manner. These can be adopted from the forms notified by the Information Technology department of the Central and State Governments. For example, the legal name can be either a single field or it could be split into first name, middle name and last name. *In case there is no standard practice for any of the fields,*

the same should be developed by the GST common portal. The form is self-explanatory and has online validation facility before the submission of the form. Wherever possible, drop down menu will be provided so that the form is user friendly and there is no dispute about the information submitted.

11.3 The fields marked with asterisk are the critical fields and need to be filled before the form can be submitted to the portal. In case of non-availability of the information such as PAN Number with the applicant, the common portal will direct the applicant to the website of the income tax department where he can submit the application for obtaining the PAN and after obtaining PAN, can apply for registration under GST.

11.4 Fields 1-5 are the basic introductory fields and need no explanation.

11.5 Field 6 is relevant for taxable persons opting for Compounding scheme.

11.6 Field 7 asks for date of commencement of business in the State in which the taxable person is applying for registration. As has been discussed earlier, the taxable person in the GST regime will be required to take State specific single registration for CGST, IGST and SGST purposes (multiple registrations in a state for business verticals are permitted) .

11.7 Field 8 asks for the date on which liability to pay tax has arisen. Field 9 asks for the details of time period for which registration is required by the casual dealers. Field ‘From’ – ‘To’ - will be mandatory for casual /non-resident dealers in the registration application. For others field ‘From’ only would be mandatory. Field 10 captures the reason for such liability. This field would not be enabled in case of registration application by casual/non-resident dealer.

11.8 Field 11 is for the existing registrants. They have to indicate the details of their existing registrations, so that information already available in the respective data bases can be culled out and made use by the tax authorities for granting new registration to the applicant under GST.

11.9 Field 12 asks for the details of the principal place of business of the applicant. Principal place of Business in the State is the place declared by the taxable person, where-

- (1) He will make available all the records to the tax authorities when called for.
- (2) The tax authorities will serve all the communications, notices, orders etc. and service of the communications, notices and orders at this place will be treated as legal service of such communications, etc.

11.10 Field 13 seeks the details of the Bank Accounts of the applicant. The taxable person is required to disclose the details of all the bank accounts maintained by him for conducting his business.

11.11 Field 14 and 15 ask for the details of top 5 goods or services **(in terms of turnover or any other parameter to be specified by the GST Law drafting Committee)** which taxable person is supplying or likely to supply.

11.12 Field 16 captures details of the additional places of business. In this field the applicant has to give the details of all the places from where he conducts the business.

11.13 Field 17 asks for the details of Proprietor, partners, Karta, Directors, Member of Managing Committee of Association, Managing trustee etc. of the business depending on the constitution of the business.

11.14 Field 18 asks for the details of the authorized signatory.

11.15 Field 19 asks for the details of authorized representative (TRP / CA/ Advocate, etc.) of the taxpayer.

11.16 Field 20 is kept to capture any State specific information, **if so provided in the GST law.**

11.17 Field 21 is required to capture the scanned documents (as mentioned in para 6.3. above) required to be uploaded along with the application

11.18 Field 22 is the field for verification and declaration made by the applicant about correctness of the information submitted by him in the registration application.

(Satish Chandra)
Member Secretary
Empowered Committee
of State Finance Ministers

(Rashmi Verma)
Additional Secretary
Department of Revenue
Government of India

ANNEXURE-I

**CONSTITUTION ORDER OF JOINT COMMITTEE ON BUSINESS
PROCESSES FOR GST**

EMPOWERED COMMITTEE OF STATE FINANCE MINISTERS

DELHI SECRETARIAT, IP ESTATE, NEW DELHI – 110002

Tel. No. 2339 2431, Fax: 2339 2432 e-mail: vatcouncil@yahoo.com

No.15/45/EC/GST/2014/32

Date: 7th April, 2014

JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST

During the last Empowered Committee meeting held on 10th March, 2014, it was decided that a Joint Committee under the co-convenership of the Additional Secretary (Revenue), Government of India and the Member Secretary, Empowered Committee should be constituted to look into the Report of the Sub-Group-I on Business Processes for GST and make suitable recommendations for Registration and Return to the Empowered Committee. It was also decided that the Joint Committee should also keep in view the Registration and Return requirements necessary for IGST Model. Accordingly, a Joint Committee, in consultation with the Government of India, is constituted with the following members:

Government of India

- (1) Smt. Rashmi Verma, Additional Secretary (Revenue) -- Co-convener
- (2) Shri P.K. Mohanty, Joint Secretary (TRU-I)
- (3) Shri M. Vinod Kumar, Joint Secretary (TRU-II)
- (4) Shri J.M. Kennedy, Director (TRU-II)
- (5) Director/Deputy Secretary holding the charge of
State Taxes Section

States Government

- (1) Dr. J.B. Ekka, Commissioner of Taxes, Assam
- (2) Shri Prashant Goyal, Commissioner, Trade & Taxes, Delhi
- (3) Shri H.V. Patel, Commissioner, Commercial Tax, Gujarat
- (4) ShriSudhirRajpal, Commissioner, Excise & Taxation, Haryana
- (5) ShriKifayatHussainRizvi, Commissioner, Commercial Tax, J&K
- (6) Shri Ajay Seth, Commissioner, Commercial Tax, Karnataka
- (7) ShriShyamJagannathan, Commissioner, Commercial Tax, Kerala
- (8) ShriAmitRathore, Commissioner, Commercial Tax, Madhya Pradesh
- (9) Dr. Nitin Kareer, Commissioner, Sales Tax, Maharashtra

- (10) ShriAbhishekBhagotia, Commissioner, Commercial Tax, Meghalaya
- (11) Shri Manoj Ahuja, Commissioner, Commercial Tax, Odisha
- (12) Shri Sanjay Malhotra, Commissioner, Commercial Tax, Rajasthan
- (13) Shri K. Rajaraman, Commissioner, Commercial Tax, Tamil Nadu
- (14) Shri M.K. Narayan, Commissioner, Commercial Tax, Uttar Pradesh
- (15) ShriDilipJawalkar, Commissioner, Commercial Tax, Uttarakhand
- (16) ShriBinod Kumar, Commissioner, Commercial Tax, West Bengal

Empowered Committee of State Finance Ministers

(1) Shri Satish Chandra, Member Secretary -- Co-convener

2. The Committee will submit its report to the Empowered Committee in two months time.

Sd/-

(Satish Chandra)
Member Secretary
Empowered Committee of
State Finance Ministers

Copy to: All the Members of the Joint Committee

Copy also to:

- (1) PS to Chairman, Empowered Committee of State Finance Ministers
- (2) Adviser to Chairman, Empowered Committee of State Finance Ministers
- (3) Sr.A.O./OSD/F.O./A.O., Empowered Committee of State Finance Ministers

ANNEXURE-II

LIST OF PARTICIPANTS OF THE MEETING HELD ON 22ND AND 23RD JULY, 2015

Government of India

1. Smt. Rashmi Verma, Additional Secretary (Revenue), Government of India
2. Shri Rajeev Yadav, Director (Service Tax), CBEC, Government of India
3. Shri B.B. Agrawal, Principal Commissioner, CBEC, Government of India
4. Shri Upender Gupta, Commissioner, GST, CBEC, Government of India
5. Shri M.K. Sinha, Commissioner (LTU), Audit, CBEC, Government of India
6. Shri G.D. Lohani, Commissioner, CBEC, Government of India
7. Shri Ravneet Singh Khurana, Deputy Commissioner, CBEC, Government of India
8. Shri Sachin Jain, Additional Commissioner, CBEC, Government of India
9. Shri P.K. Manderna, Superintendent (GST Cell), Government of India

States

1. Shri Gautam Das Gupta, Deputy Commissioner of Taxes, Assam
2. Shri T. Ramesh Babu, Additional Commissioner, Commercial Tax, Andhra Pradesh
3. Shri Arun Kumar Mishra, Joint Secretary, Finance, Bihar
4. Shri Santosh Kumar Sinha, Additional Commissioner, Commercial Tax, Bihar
5. Shri Deepak Kanan, Additional Commissioner, Commercial Tax (GST), Bihar
6. Shri R.K. Trivedi, Additional Commissioner, Commercial Tax, Chhattisgarh
7. Shri Kishor Bhalla, Deputy Commissioner (VAT), Daman & Diu and Dadra & Nagar Haveli
8. Shri Vijay Kumar, Commissioner (VAT), Trade and Taxes, Delhi
9. Shri Jagmal Singh, Deputy Director, Trade and Taxes, Delhi
10. Shri Dipak M. Bandekar, Additional Commissioner, Commercial Tax, Goa
11. Dr. P.D. Vaghela, Commissioner, Commercial Tax, Gujarat
12. Ms. Aarti Kanwar, Special Commissioner, Commercial Tax, Gujarat
13. Shri Shyamal Misra, Commissioner, Excise & Taxation, Haryana
14. Shri Hanuman Singh, Additional Commissioner, Excise & Taxation, Haryana
15. Shri J.C. Chauhan, Commissioner, Excise & Taxation, Himachal Pradesh
16. Shri P.K. Bhat, Additional Commissioner, Commercial Tax, Jammu & Kashmir
17. Smt. Nidhi Khare, Secretary-cum-Commissioner, Commercial Tax, Jharkhand
18. Dr. M.P. Ravi Prasad, Joint Commissioner, Commercial Tax, Karnataka
19. Dr. Rajan Khobragade, Commissioner, Commercial Tax, Kerala
20. Shri M.I. Mansur, Assistant Commissioner, Commercial Tax, Kerala
21. Shri Sudip Gupta, Deputy Commissioner, Commercial Tax, Madhya Pradesh
22. Shri P. Velrasu, Special Commissioner, Sales Tax, Maharashtra
23. Shri B.V. Borhade, Joint Commissioner, Sales Tax, Maharashtra
24. Shri P.M. Kulkarni, Deputy Commissioner, Sales Tax, Maharashtra
25. Shri K. Sanglawma, Commissioner of Taxes, Mizoram
26. Shri H. Rangthanmawia, Superintendent of Taxes (GST Cell), Mizoram
27. Shri Niten Chandra, Commissioner, Commercial Tax, Odisha
28. Shri Sahadev Sahoo, Joint Commissioner, Commercial Tax, Odisha
29. Shri K. Sridhar, Deputy Commissioner, Commercial Tax, Puducherry
30. Dr. Karthik, Additional Secretary, Punjab
31. Shri Pawag Garg, Additional Commissioner, Excise & Taxation, Punjab

32. Shri Vaibhav Galriya, Commissioner, Commercial Tax, Rajasthan
33. Shri Manoj Rai, Joint Commissioner, Commercial Tax, Sikkim
34. Shri D. Soundraraja Pandian, Joint Commissioner (Taxation), Commercial Taxes, Tamil Nadu
35. Shri K. Chandrasekhar Reddy, Additional Commissioner, Commercial Tax, Telangana
36. Shri Vikas Singh, Commissioner of Taxes and Excise, Mizoram
37. Shri Vivek Kumar, Additional Commissioner, Commercial Tax, Uttar Pradesh
38. Shri Abhijit Gupta, Commercial Tax Officer (IT), Uttar Pradesh
39. Shri N.C. Sharma, Additional Commissioner, Commercial Tax, Uttarakhand
40. Smt. Ujjaini Datta, Joint Secretary, Finance, West Bengal

Goods and Services Tax Network (GSTN)

1. Shri Navin Kumar, Chairman, Goods and Services Tax Network
2. Shri Prakash Kumar, Chief Executive Officer, Goods and Services Tax Network

Empowered Committee of State Finance Ministers

1. Shri Satish Chandra, Member Secretary, Empowered Committee
2. Shri Bashir Ahmed, Adviser, Empowered Committee

ANNEXURE-III
Form GST –

[See Rule ____]

Application for Registration under Goods and Services Tax Act, Year

1	Legal Name of Business*	
1A	Trade Name (optional)	

2	Constitution of Business (Please Select the Appropriate)*

Proprietorship	☐	Partnership	☐
Hindu Undivided Family	☐	Private Limited Company	☐
Public Limited Company	☐	Society/Club/Trust/Association of Persons	☐
Government Department	☐	Public Sector Undertaking	☐
Unlimited Company	☐	LLP's	☐
Local Authority	☐	Statutory Body	☐
Others (Please Specify)	☐		

In case of Proprietorship*

3	Name of Proprietor										
4	PAN of the proprietor										

In case of other Businesses*

4A	PAN of the Business										

5	Name of the State and its Code*	Drop down for Name of State & Codes	▲

6	Option For Composition	Yes ☐	No ☐

7	Date of commencement of business								
		D	D	M	M	Y	Y	Y	Y
8	Date on which liability to pay tax arises	D	D	M	M	Y	Y	Y	Y
9	Estimated supplies (in case of casual dealers)								
	Period for which registration is required – From								
	To								
10	Reason of liability to obtain registration (from the dropdown)	▲							

(1) Due to crossing the Threshold

- (2) Due to inter-State supply
- (3) Due to liability to pay as recipient of services
- (4) Due to being Input Service Distributor (ISD)
- (5) UN bodies for allotment of Unique Identification Number (ID)
- (6) Due to transfer of Business which includes change in the ownership of business (if transferee is not a registered entity)
- (7) Due to death of the Proprietor (if the successor is not a registered entity)
- (8) Due to de-merger
- (9) Due to change in constitution of business
- (10) Due to Merger /Amalgamation of two or more registered taxpayers
- (11) Being casual Dealer
- (12) Being Non resident Dealer
- (13) None of the above – on voluntary basis

11 Indicate Existing Registrations

	Yes/No	Registration Details
Central Excise		
Service Tax		
State VAT Registration (TIN)		
CST Registration No		
IEC No.(Importer Exporter Code Number)		
Corporate Identity Number (CIN)		
GSTIN		

12 Details of Principal Place of Business*

ADDRESS											
Building No/Flat No/Door No				Floor No							
Name of the Premises/Building				Road/Street/Lane							
Locality/Area/Village				District/Town/City							
Latitude (optional)				Longitude (optional)							
PIN Code											
CONTACT DETAILS											
Telephone number				Fax Number							
Mobile Number											
Email Address											
Nature of possession of premises											
Owned	☐	Leased	☐	Rented	☐	Consent	☐	Shared	☐		

Please Tick the Nature of Business Activity being carried out at above mentioned Premises					
Factory / Manufacturing	☐	Wholesale Business	☐	Retail Business	☐
Warehouse/Deport	☐	Bonded Warehouse	☐	Service Provision	☐
Office/Sale Office	☐	Leasing Business	☐	Service Recipient	☐
EOU/ STP/ EHTP	☐	SEZ	☐	Input Service Distributor (ISD)	☐

Works Contract	☐				

13. Details of Bank Accounts (s)

Total number of Bank Accounts maintained by the applicant for conducting business	

Details of Bank Account 1

Account Number														
Type of Account							IFSC							
Name of the Bank														
Branch and Address of the Bank & Branch	To be auto-populated (Edit mode)													
PIN Code							State							

Details of Bank Account 2

Account Number														
Type of Account														
Name of the Bank														
Branch and Address of the Bank & Branch	To be auto-populated (Edit mode)													
PIN Code								State						

Details 3...n (Multiple fields will be available to capture the details of all the additional Bank A/c)

14 Details of the **Goods/Commodities** supplied by the Business

Please specify top 5 Commodities		
S.N o.	Description of Goods	HSN Code (4 digit code)
1		
2		
...		
5		

15 Details of **Services** supplied by the Business.

Please specify top 5 Services		
S. No.	Description of Services	Service Accounting Code
1		

2		

5		

16 Details of Additional Place of Business

Number of additional places	

Premises 1

Details of Additional Place of Business

ADDRESS												
Building No/Flat No/Door No								Floor No				
Name of the Premises/Building								Road/Street/Lane				
Locality/Area/Village								District/Town/City				
PIN Code												
CONTACT DETAILS												
Telephone number									Fax Number			
Mobile Number												
Email Address												
Nature of possession of premises												
Owned	☐	Leased	☐	Rented	☐	Consent	☐	Shared	☐			

Please Tick the Nature of Business Activity being carried out at above mentioned Premises					
Factory / Manufacturing	☐	Wholesale Business	☐	Retail Business	☐
Warehouse/Depot	☐	Bonded Warehouse	☐	Service Provision	☐
Office/Sale Office	☐	Leasing Business	☐	Service Recipient	☐
EOU/ STP/ EHTP	☐	SEZ	☐	Input Service Distributor (ISD)	☐
Works Contract	☐				

Premises 2.....n (Multiple fields will be available to capture the details of all the additional places of business within the state)

17 Details of Proprietor/all Partners/Karta/Managing Directors and whole time Director/Members of Managing Committee of Associations/Board of Trustees etc. *

Total Number of Persons

Please provide details in the table below. In case you need more tables, click on add table

- In case of **Proprietorship**: Details of Owner/Proprietor
- In case of **Partnership**: Details of **all Managing/ Authorized Partners** (personal details of all partners but photos of only ten partners including that of Managing Partner is to be submitted)
- In case of **Companies** registered under Companies Act: **Managing Director and whole time directors**
- In case of **HUF**: Details of **Karta of HUF**

- In case of **Trust**: Details of **Managing Trustee**
- In case of **Association of Persons**: Details of Members of Managing Committee (personal details of all members but photos of only ten members including that of Chairman is to be submitted)
- In case of Local Authority: Details of CEO or equivalent
- In case of Statutory Body: Details of CEO or equivalent
- In case of others: Details of person responsible for day to day affairs of the business

[illegible]

Mobile Number													
E-mail address									Gender	M	☒	F	☒
Telephone No									FAX No				

[illegible]

Details 2...n (Multiple fields will be available to capture the details of other persons)

18 Details of Authorized Signatory

Number of Authorized Signatory

11

Details of Signatory No. 1

Details of Signatory No. 1															
	First Name				Middle Name				Surname						
Name of Person															
Name of Father / Husband															
Designation					Date of Birth										
									DD		MM		YYYY		
PAN															

UID No													
DIN No. (if any)													
Mobile Number													
E-mail address									Gender	M	☐	F	☐
Telephone No								FAX No					
Residential Address													
Building No/Flat No/Door No								Floor No					
Name of the Premises/Building								Road/Street/Lane					
Locality/Area/Village								District/Town/City					
PIN Code								State					

Details 2....n (Multiple field will be available to capture the details of other authorized persons)

19 Details of Authorized Representative (TRP / CA / Advocate etc.)

	First Name	Middle Name	Surname									
Name of Person												
Status	TRP / CA / Advocate etc.											
Mobile Number												
E-mail address												
Telephone No								FAX No				

20 State Specific Information

- Field 1
- Field 2
-
-
- Field n

21 Document Upload

A customized list of documents required to be uploaded (as detailed in para 6.3 of the process document) as per the field values in the form should be auto-populated with provision to upload relevant document against each entry in the list.

22 Verification

I hereby solemnly affirm and declare that the information given herein above is true and correct to the best of my knowledge and belief and nothing has been concealed therefrom

Place
Date

Name of Authorized Signatory
Designation

Instructions to Taxable Person

1. **Field 4:** In case of Proprietary concerns, only PAN of the Proprietor will be required while in case of other business entities, only PAN of the business will be required.
2. **Field 4A:** PAN should be in same name as the Legal Name in Field 1.
3. **Field 6:** If “Yes” option is selected, the applicant will be asked to confirm that the likely all-India annual turnover including exports and exempted supplies during next 12 months **(depending on the exact legal formulation to be made by the GST Drafting Law Committee)** is below Rs. Lakh.
4. **Field 17:** In case of multiple authorized signatories provided by the Dealer, any one of them can sign this form as Authorized Signatory
5. **Field marked with * are mandatory fields.** Any changes in these fields require approval from proper officer.

All communication will be made to the Mobile Number and e-mail mentioned in Principal Place of Business.

XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX

Suggestions for System Development

1. Pin Code should be the field requiring primary data, and the other two field should get auto-populated (based on master values) with option to enter locality/area/village if that is not in the portal master. Alternatively, a validation between PIN Code and Locality/Area/Village and District/Town/City should be inbuilt.
2. For Field No 17 (i.e. Details of Proprietor / all partners / Karta / Managing Director and whole-time Director / Members of the Managing Committee of Association of Persons / Board of Trustees etc.) and Field No 18 (Details of the Authorised Signatory) providing PAN would be mandatory for Indian nationals. For foreign national passports details would be required.
3. In Field 10, there should be an option to enter details of multiple entities which are merged

and the application is on behalf of the merged entity

4. In Field No. 9 (Period for which registration is required – From/ To) validity period of registration is captured. The “From Date” is mandatory for all dealers but the “To Date” should be mandatory only for Casual/non-resident Dealers. Following validation needs to be built in
 - Inserting of a radio buttons – Whether regular dealer or Casual/non-resident dealer
 - In case of Casual/non-resident dealer – both from date and to date are enabled, and both are mandatory fields. Further, the “from date” could be retrospective date (in view of para 2.1 (2)).
 - In case of Regular dealer – only from date is enabled and is mandatory and this could be retrospective date (in view of para 2.1 (2)).
 - Further, the system must be able to display all the previous registrations obtained as Casual/non-resident Dealer with from date and to date and the LVO in which he was registered and arrears of amounts if any standing in his name.
5. Field No. 10 (Reason of liability to obtain registration) should not be enabled for casual dealers. Voluntary registration is to be enabled.
6. Field No. 11 (Indicate existing registrations) – Following state specific fields need to be captured:
 - Professions Tax E.C. No.
 - Professions Tax R.C. No.
 - State Excise License No. and the name of the person in whose name Excise Licence is held.
7. For Field No. 12 (Details of Principal Place of Business) and Field No. 16 (Details of Additional Place of Business), it is required to display the earlier places of business – i.e. Address, From date and To date from the History Table, for the efficiency of tax administration. Though this may not be useful in new registrations, it is required in case of amendments, when the addresses are changed, additional places are added or deleted. This would not need modification in the registration format and business process, but the software/database should take care of the displaying these details when an amendment form is being filled or when the departmental officer views it. In case of casual dealers, principal place of business will be the place where he will run his business.

8. For Field No. 14 (Details of Goods/ Commodities supplied by the Business) history of existing/ deleted/ added commodities and services with from date and to date needs to be captured by the software. This would give a detailed picture of the nature of the commodities dealt by the dealer. Further, it is also better if the dealer identifies one of the commodities/ service as the main commodity/ service, he is dealing in. This is required to match the GST return information with the details obtained from macro-economic parameters and matching with NIC Activity classification, based on which the macro-economic performance is presented.
9. For Field No. 17 (Details of Proprietor/all Partners/Karta/Managing Directors and whole time Director/Members of Managing Committee of Associations/Board of Trustees etc.) –All changes in Partners or Directors, or Managing Persons, must be kept in the database to enable the jurisdictional officer to see the history of the persons entered earlier, and from date and to date. Photos of maximum of 10 partners including that of Managing Partner is required to be uploaded.

XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX

ANNEXURE-IV

Form GST -

[See Rule ____]

Application for Surrender of Registration under Goods and Services Tax Act, Year

Please file **your tax return** for the tax period in which the effective date of cancellation of your registration falls before applying for cancellation. **Filed no. 2 to 5 would get auto populated on the basis of information mentioned in filed no. 1.**

1. GSTIN														

2. Full Name of Registrant														
3. Trade Name, if any														
4. Address of Principal Place of Business														
5. Address for correspondence (e-mail, mobile, landline etc.)														

6. Reason for Surrender <u>Tick ☒ one</u>	☐ Discontinuance of business ☐ Death of sole proprietor ☐ Has ceased to be liable to pay tax ☐ Amalgamation etc.	☐ Closure of incorporated body ☐ Dissolution of firm ☐ Merger ☐ Others (specify the reason)

(Note: In case of death of Sole Proprietor application will have to be made by the legal heir / successor manually before the concerned tax authorities)

7. In case of amalgamation or merger, provide particulars of registration in which merged, amalgamated etc.			
(i) GSTIN			
(ii) Name			
(iii) Principal Place of Business			

(The new entity in which the applicant proposes to amalgamate itself must be registered with the tax

authority before the filing of the surrender application. This application can only be made after that.)

8. Date from which registration under -----Act, 20-- is to be surrendered			/			/			
	<u>Day</u>			<u>Month</u>			<u>Year</u>		

9. Amount of GST payable in respect of goods / capital goods held on the date of surrender of registration (Rs.)	Turnover	Tax	
		CGST	SGST

10. Details of amount of GST paid as calculated at 9 above. (This needs to be amended in view of maintenance of ITC / Cash Ledger)	i) Date of deposit			-			-				
		Day		Month		Year					
	ii) Challan No.										
	(iii) Name of Bank & Branch										

11. Verification	
(i) I/We _____ hereby solemnly affirm and declare that the information given hereinabove is true and correct to the best of my/our knowledge and belief and nothing has been concealed therefrom.	
(ii) I/We undertake to discharge any tax liability which is found to be payable subsequent to the surrender of registration and the tax authorities shall be free to take any action as prescribed in the law.	
Signature of Authorised Signatory	
Full Name	
Designation/Status	

Place																						

Date							
	Day		Month		Year		

ANNEXURE-V

Form GST -

[See Rule]

Application to Opt for Composition Scheme

(For existing taxpayer)

Filed no. 2 & 3 would get auto populated on the basis of information mentioned in filed no. 1.

1. GSTIN															

2. Full Name of Applicant Dealer															

3. Please Tick the Nature of Business Activity being carried out at above mentioned Premises					
Factory / Manufacturing	☐	Wholesale Business	☐	Retail Business	☐
Warehouse/Deport	☐	Bonded Warehouse	☐	Service Provision	☐
Office/Sale Office	☐	Leasing Business	☐	Service Recipient	☐
EOU/ STP/ EHTP	☐	SEZ	☐	Input Service Distributor (ISD)	☐

4. Year for which composition scheme is sought					-				

5. Turnover in the preceding year	(Rs.)								

6. Estimated Turnover in the current year	(Rs.)								

7. Tax Payable on Opening Stock lying at the beginning of the current	Description	Turnover (Rs.)	Tax Payable											
			CGST				SGST				IGST			
	(i) Trading Stock													
(Iii) Raw material														

year(provision for capital goods may have to be made if the GST law provides for proportionate credit in case of mixed use)	(iii) Packaging Material																			
	(iv) Finished Goods																			
	Total																			

8. Details of Tax paid calculated as per (7) above(This needs to be amended in view of maintenance of ITC / Cash Ledger)	Description										
	(i) Amount of tax paid (Rs.)										
	(iii) Date of Deposit			/			/				
		dd		mm				yyyy			
	(iii) Challan No.										

9. Verification

I/We _____ hereby solemnly affirm and declare that the information given hereinabove is true and correct to the best of my/our knowledge and belief and nothing has been concealed therefrom.

Signature of Authorised Signatory _____

Full Name (*first name, middle, surname*) _____

Designation/Status _____

Place																				

Date								
	Day		Month		Year			

ANNEXURE-VI

Form GST -

[See Rule]

Application for withdrawal from Composition Scheme

(For existing taxpayer)

Filed no. 2 & 3 would get auto populated on the basis of information mentioned in filed no. 1.

1. GSTIN															

2. Full Name of Applicant Dealer															

3. Please Tick the Nature of Business Activity being carried out at above mentioned Premises					
Factory / Manufacturing	☐	Wholesale Business	☐	Retail Business	☐
Warehouse/Deport	☐	Bonded Warehouse	☐	Service Provision	☐
Office/Sale Office	☐	Leasing Business	☐	Service Recipient	☐
EOU/ STP/ EHTP	☐	SEZ	☐	Input Service Distributor (ISD)	☐
Works Contract	☐				

4. Date from which withdrawal from composition scheme is sought (dd/mm/yyyy)						-					

5. Turnover in the preceding year / period										

6. Reasons for withdrawal from composition scheme	

7. Input Tax Credit	Description	Turnover (Rs.)	Input Tax Credit (Rs.)

available on goods purchased and lying in stock on the day of withdrawal from the scheme (provision for capital goods may have to be made if the GST law provides for proportionate credit in case of mixed use)			CGST				SGST				IGST			
	(i) Trading Stock													
	(ii) Raw material													
	(iii) Packaging Material													
	(iv) Finished Goods													
	Total													

8. Verification

I/We _____ hereby solemnly affirm and declare that the information given hereinabove is true and correct to the best of my/our knowledge and belief and nothing has been concealed therefrom.

Signature of Authorised Signatory _____

Full Name (*first name, middle, surname*) _____

Designation/Status _____

Place																				

Date								
	Day		Month		Year			

ANNEXURE-VII

Form GST -

[See Rule]

Application for Amendment(s) in Particulars subsequent to Registration under Goods & Services Act Year

(This form would be used to amend fields mentioned in para 7.2(7) of the Process document as all other fields can be amended on self-service basis)

I GSTIN																			

II Full Name of Dealer																	

III Amendment summary

(Please put field reference in which amendments are sought, date of amendment and reason for amendment(s). attach additional sheets if required)

Field Ref.	Field Name	Date (mm/dd/yy)	Reason(s)

(Please edit /fill in only those following fields that are to be amended)

Complete Registration form should be copied here.

Facilities for uploading scanned documents including photographs (only in .jpg format) etc. needs to be provided.

ANNEXURE-VIII

EXTRACT OF THE REPORT OF THE COMMITTEE ON THE PROBLEM OF DUAL CONTROL, THRESHOLD AND EXEMPTIONS IN GST REGIME

Para 7. The matter was deliberated upon by the Committee. It was felt that the threshold, both for SGST and CGST should be common except for North-eastern States where the threshold could be prescribed at lower level. It was also felt by the Committee that the threshold both for services and goods should be same. However, for inter-state dealers, the threshold should be zero. The threshold should be worked out taking into account both the supply of goods and services on gross turnover basis. Such turnover would include the turnover of exempted goods and services (including non-taxable) and exports. It was also agreed that the turnover so calculated would be applicable for the purposes of Threshold, Compounding Scheme and Dual Control. While the State representatives felt that turnover should be State-wise of a legal entity, the representatives of Government of India strongly felt that it should be All India turnover of a legal entity, otherwise it may lead to tax evasion. It was pointed out by the Centre's representatives that if the turnover of an entity is considered State-wise, the threshold for CGST would increase steeply when calculating the turnover of the entity on an All India basis. This would adversely affect the revenue of the Centre. What would happen is that an entity will open office in States and Union Territories (which are 37 in number) for availing of State-wise threshold for SGST purposes. In such a scenario, the threshold for CGST purposes would work out to Rs. 9.25 Crores (Rs. 25 Lacs * 37). Similar impact would be there for the compounding scheme as well as for the issue relating to dual control. The suggestion of the Central Board of Excise and Customs (CBEC) that legal entity on all India basis should be taken was considered by the Committee and after due deliberations the suggestion was agreed to avoid tax evasion by the manufacturers/traders/dealers.

ANNEXURE-IX

EXTRACT OF THE MINUTES ON REFINEMENT TO THE PROCESS FOR STATES OPTION FOR TWO-WAY API BASED INTEGRATION AND FLEXIBILITY (DECISION DATED 18.04.2012 OF EC) WILL BE FORMULATED SEPARATELY

14. The Chairman, Empowered Committee asked the Member Secretary to indicate the recommendations of the Committee regarding strategic control of the Government on GST Network. The Member Secretary mentioned that a Committee of Principal Secretaries/Secretaries (Finance/Taxation) and Commissioners of Commercial Taxes met on 10th April, 2012 to discuss the various concerns raised by the States regarding GSTN-SPV. Dr. Nandan Nilekani, Chairman, Unique Identification Authority of India and Chairman, Empowered Group on IT Infrastructure for GST kindly agreed to join the discussion of the Committee. He, during the Committee meeting, clarified the position why the Government of India, Empowered Committee and the Empowered Group on IT Infrastructure for GST have recommended for setting up of a Non-profit Section 25 Private Company. During the meeting, concerns were raised regarding flexibility to be provided to the States and the strategic control of the Government on GSTN. After due deliberations, following recommendations were made by the Committee for the consideration of the Empowered Committee:

- (i) Following three options may be made available to the States for usage of services to be provided by GSTN:
 - a. 'Full service model' where the GSTN will offer the full range of GST services as a utility which the States can utilize.
 - b. 'Limited service model' where a State will use the GSTN for common registration, return and payments and has its own software for remaining GST functions.
 - c. 'Application Programming Interface (API) model' where the States will have their own software for flexibility but will, adhere to the common registration, return and payment formats defined by the GSTN (though they may collect additional data) and ensure that the rights of both States and Centre are protected in terms of getting instantaneous information and ensuring timely settlements of their respective share of taxes.
- (ii) The Committee noted that the ownership of the private equity holders will be widely dispersed and hence, the basic control would stay with the Government. The distinction between ownership and control was also noted.
- (iii) The Committee noted that the Empowered Committee had deliberated on the non-Government status of the SPV in detail in its earlier meetings and taken a considered view to approve it. However, Committee requested that the list of potential private equity partners should be decided in consultation with the Empowered Committee.
- (iv) The Committee noted that the mechanisms recommended by Empowered Group for ensuring strategic control would be adequate. However, the draft Memorandum of Association and Articles of Association incorporating necessary provisions should be placed before the Empowered Committee for consultation before finalisation.
- (v) To provide higher representations to the States, there should be an Advisory Committee of the GSTN-SPV in which all the States should be represented.

- (vi) There should be an exit/sunset clause for dissolving the GSTN-SPV, if both the Centre and the States decide to do so.
- (vii) Any new developments during the process leading to the formation of GSTN SPV should be brought to the notice of the Empowered Committee.

15. The Chairman, Empowered Committee broadly indicated that the strategic control over the SPV will be available by virtue of thinly dispersed private shareholding, the composition of Board of Directors, special resolutions, share holders agreement, induction of deputationists from the Government and agreements between GSTN-SPV and Government, Advisory Committee of GSTN-SPV etc. After due deliberations, the recommendations of the Committee mentioned in para 14 was approved by the Empowered Committee.

16. It was also mentioned by the Member Secretary that during the meeting of the Hon'ble Union Finance Minister on 17th April, 2012, the issue regarding finalizing the other details of the formation of the GSTN-SPV came up for discussion. It was felt that the Empowered Group on IT Infrastructure for GST, chaired by Dr. Nandan Nilekani, may also look into this aspect as well. The Empowered Committee accordingly decided to endorse the same.

ANNEXURE-X

EXTRACT OF THE REPORT OF THE COMMITTEE ON IGST AND GST ON IMPORTS

I. Norms for blacklisting of dealers for blocking tax credits

A system of “GST Compliance Rating” can be introduced. Any fall in the rating below a prescribed level will have impact of blacklisting a dealer. The rating is only a measure to facilitate informed choices by the purchasers and not a punishment measure. There should be clear declaration in the law that blacklisting does not mean that ITC claim on other non-blacklisted dealers is assured by the Government as any eligibility for ITC primarily depends on the selling dealer owning up the tax invoice and paying the due tax. However, if the rating falls below the prescribed level resulting in that dealer becoming blacklisted, purchases from him will no longer be eligible for ITC, on self-assessment basis, (they however will be eligible for availing the ITC only after the tax has been paid by such selling dealers) by the buyers, till improvement of the rating to normal level.

IX.A. Trigger for Blacklisting

- i. Continuous default for 3 months in paying ITC that has been reversed.
- ii. Continuous default of 3 months or any 3 month-period over duration of 12 months in uploading sales details leading to reversal of ITC for others. Defaulters of even a single event should also be flagged and put in public domain as being a potential black listed dealer so as to alert the buyers.
- iii. Continuous short reporting of sales beyond a prescribed limit of 5% (of total sales) for a period of 6 months.

IX.B. Default

Not doing the activity within the prescribed cut off dates. A system of rating the dealers based on their compliance should also be done and put in public domain to inform prospective buyers.

IX.C. Rating and Compliance Profile

There should also be a continuous rating system, provided under model law, for dealers based on parameters such as promptness in e-return filing, discrepancies detected where the dealer has had to make corrections, making prompt payment in lieu of reversed ITC, etc. The profiles for all dealers would be posted in public domain so that the dealer community is kept aware of the compliance profile of all registered dealers with whom they may have to deal with during the course of their business. While the system of blacklisting may only highlight deviant behaviour after it crosses a certain threshold, a system-updated dealer profile will serve as a continuing

rating mechanism for the entire community and leaders within a certain industry can set a benchmark for others to emulate.

IX.D. Blacklisting

- i. Only for regulating ITC by others.
- ii. Will be based on dealer rating. A dealer will be blacklisted if dealer rating falls below the prescribed limit.
- iii. To be put in public domain.
- iv. To be notified (auto-SMS) to all dealers who have pre-registered this dealer (black listed now) as their supplier.
- v. To be prospective only (from month next to blacklisting)
- vi. Blacklisted GSTINs cannot be uploaded in purchase details. Corresponding denial of ITC to be supported by suitable provision in the law.
- vii. ITC reversal in hands of the buyer should take place for disowning of any tax invoice with date prior to effect of blacklisting of the seller.
- viii. Once blacklisting is lifted, buyers can avail unclaimed ITC subject to this dealer uploading sales details along with tax and interest.

REPORT

OF

THE JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST

ON

GST PAYMENT PROCESS

Empowered Committee of State Finance Ministers

New Delhi

April, 2015

INDEX

Contents	Page No.
1. Introduction.....	1
2. Payment by taxpayers through internet banking including Credit Card/Debit card.....	5
A. Process involved in e-payment of GST	6
B. Role to be played by each stakeholder.....	13
(i) GSTN.....	13
(ii) e- FPBs of authorised banks.....	15
(iii) e-Kuber (Core Banking System) of RBI.....	17
(iv) CAS.....	19
(v) e-PAOs of Centre and e-Treasuries of State Governments.....	19
(vi) Pr. CCA, CBEC & Accountant General of States.....	21
2. Over the Counter payments through Authorised banks.....	21
A. Process involved in OTC payments	22
B. Role to be played by each stakeholder.....	29
(i) Branch of authorised bank.....	29
4. Payment through NEFT / RTGS from any bank (including other than Authorised bank).....	30
A. Process involved in OTC payments	32
B. Role to be played by each stakeholder.....	39
(i) Branch of remitter bank.....	39
(ii) RBI performing functions akin to authorized banks.....	39
5. Payment across departmental counters.....	40

6. Penalty mechanism for erring banks.....	41
7. Banking arrangements under GST.....	42
8. Accounting System under GST.....	46
9. Proposed Accounting System under GST.....	47
10. Reconciliation of Receipts.....	50
11. Reconciliation by GSTN.....	52
12. Reconciliation by Accounting Authorities.....	53
13. Resolution of Reconciliation Outcomes (discrepancies noted during the reconciliation process).....	54
First leg of communication of data.....	54
Second leg of communication of data.....	55
Third leg of communication of data.....	56
Fourth leg of communication of data.....	65
14. Recording by Tax Authorities.....	66
15. Challan Correction Mechanism.....	67
16. Challan Format.....	69
17. Constitution of Joint Committee on Business Processes (Annexure-I).....	71
18. Constitution of Sub-Committee on Payment Processes under GST (Annexure-II).....	73
19. List of Participants of the meeting held on 16 th April, 2015 and 17 th April, 2015 (Annexure-III).....	75
20. GST Challan Form (Annexure-IV).....	77
21. Issue of charge back in CC /DC payment (Annexure-V).....	80
22. List of banks presently authorised in Centre & States (Annexure-VI).....	83

Report of the Joint Committee on Business Processes for GST– Payment

INTRODUCTION

During the Empowered Committee meeting held on 10th March, 2014, it was decided that a Joint Committee under the co-convenership of the Additional Secretary (Revenue), Government of India and the Member Secretary, Empowered Committee should be constituted to look into the Report of the Sub-Group-I on Business Processes for GST and make suitable recommendations for Payment and Return to the Empowered Committee. Accordingly, a Joint Committee, in consultation with the Government of India, was constituted on 7th April, 2014 (Annexure-I). The Committee held its deliberations on 28th October, 2014, 12th November, 2014, 25th November, 2014, 22nd December, 2014, 2nd and 3rd February, 2015, 19th and 20th February, 2015 and 16th and 17th April, 2015.

2. The Joint Committee on Business Processes for GST held on 2nd February, 2015, it was decided to constitute a sub-committee on GST Payment Process. Pursuant to that decision, the Member Secretary, Empowered Committee constituted the Sub-Committee vide his memorandum letter dated 3rd February, 2015 (Annexure-II). Shri V Rajendaran, DG (Government Accounts), CAG, Mrs. Krishna Tyagi, CCA, CBEC, Government of India, Shri Madan Mohan, Jt. CGA, Government of India and Shri G Sreekumar, CGM, RBI were co-opted as members of the Sub-Committee. Shri Ravneet S. Khurana, Deputy Commissioner GST Cell, CBEC also participated in the deliberations of the Sub-Committee. The Sub-Committee met in Bengaluru on 14th and 15th February, 2015 and on 06th and 7th April, 2015. The Sub-Committee also exchanged

drafts on emails during the interregnum period. The Sub-Committee submitted its final report on 10th April, 2015.

3. The report of the Sub-Committee was discussed in the meeting of the Joint Committee of Business Processes held in Delhi on 16th and 17th April 2015 and was accepted with certain modifications. The meeting of the Joint Committee was attended by the officers as listed in **Annexure III**.

4. In modern day taxation regime, every transaction of the tax payer with the tax administration should be transparent, responsive and simple. It has been experience of tax administrations that more the system and procedures are made electronic more is the efficiency of tax administration and greater is the satisfaction of taxpayer. In this context, payment system of GST should also be based on Information Technology which can handle both the receipt and payment processes.

5. The objectives of this report are as under:

- a) Highlight key issues in tax collection, collation, remittance and reporting of tax collection into Government account;
- b) Need for a uniform system of banking arrangements for collection, remittance and reporting of GST to both Central and State Governments;
- c) Proper accounting and bank reconciliation of taxes derived from basic data of payments made by taxpayers to banks, with the required classification of heads of accounts indicated on the Challan;
- d) Designing the format of a new Challan for use by the taxpayers paying GST;
- e) Developing a detailed accounting procedure common to both Central and State Governments for GST, covering all relevant aspects of payments, accounting and

related banking arrangements.

6. It is noted that under GST regime, some taxes and duties may remain outside the purview of GST and will continue to be collected in the manner prescribed under existing accounting procedures/rules/manuals, etc. This means that two types of challans (one for GST and other for non-GST) will be used and accounted for by the respective Pay and Accounts Offices (PAOs)/State AGs.

7. The payment processes under proposed GST regime should have the following features:

- a) **Electronically generated** challan from GSTN Common Portal in all modes of payment and no use of manually prepared challan;
- b) **Facilitation** for the taxpayer by providing hassle free, anytime, anywhere mode of payment of tax;
- c) **Convenience** of making payment online;
- d) **Logical** tax collection data in electronic format;
- e) **Faster** remittance of tax revenue to the Government Account;
- f) **Paperless** transactions;
- g) **Speedy** Accounting and reporting;
- h) **Electronic** reconciliation of all receipts;
- i) **Simplified** procedure for banks;
- j) **Warehousing** of Digital Challan.

8. With the above features in mind the following **three modes of payment** are proposed.

- a) Payment by taxpayers through Internet Banking through authorized banks and through credit card/debit card;

(Section 45 of RBI Act, 1934 permit banks other than RBI to be appointed as agency banks for carrying out government business. Agency banks are permitted to both receive and make payments on behalf of the Government and therefore act as Banker to respective governments. However, authorized banks are only permitted to receive payment of GST on behalf of the Government, and keeping this distinction in view, the expression ‘authorized bank’ is used throughout this Document.)

- b) Over the Counter payment (OTC) through authorized banks;
- c) Payment through NEFT/RTGS from any bank (including other than authorized banks).

9. **Mode of payment described at b) above will be available for payments up to Rs. 10,000/- per challan only. Model GST law may have suitable provisions in relation to this.** However, there should not be any IT system constraints for this i.e. the systems should be able to receive payments through all three modes irrespective of the amount. Other means of payment, such as payment by book adjustment as is presently being allowed by Government of India to some departments / State governments or payment by debit to export scrips, while paying tax would not be allowed. It is also noted that all taxpayers under Centre are paying taxes electronically and possibly the same situation exists in some State Tax administrations. It is **desirable that under the GST regime, all taxpayers should gradually move to internet payment over an indicative time frame.**

10. The Committee recommends that RBI should play the role of an aggregator through its e-Kuber system. Such role will facilitate participation of larger number of banks in GST receipts enhancing convenience for the tax payers and provide single source of information for credit of the receipts to Government accounts and thereby simplifying accounting and reconciliation tasks. In case of any discrepancy found during the reconciliation by the Accounting Authorities, they would directly interact with RBI. Joint CGA suggested that as per the provisions of Section 20 of the RBI Act, 1934 in the proposed scenario, RBI would be the sole banker to the Governments. RBI, on the other hand, has indicated that Section 20 and Section 45 of the RBI Act, 1934 are not mutually exclusive and therefore there would not be any conflict in the role envisaged for the RBI in the proposed model.

11. Each of the above modes is discussed separately along with the role of stakeholders involved, process of reporting, accounting and reconciliation of data. As already mentioned above, it is envisaged that for each mode of payment, the challan will be generated electronically at the GSTN and no manual challan will be used under any mode of payment.

**I. PAYMENT BY TAXPAYERS THROUGH INTERNET BANKING THROUGH
AUTHORIZED BANKS AND THROUGH CREDIT CARD/ DEBIT CARD.**

12. With increasing spread of internet and electronic communication, this mode has emerged as one of the preferred modes of tax payment for both the taxpayers and administrators. As the name suggests, this mode of payment involves payments by the taxpayers that utilize the electronic network, right from the generation of the challan by the taxpayer to the ultimate reconciliation of the data by the Accounting authorities.

Before understanding the process involved in e-payments, it is important to list the stakeholders involved in this mode of payment. The following stakeholders will play a key role in establishing an effective e-payment network in the proposed GST scenario:

- a) GSTN (Goods and Service Tax Network);
- b) e- FPBs (Electronic Focal Point Branches) of authorized banks;
- c) e-Kuber of RBI;
- d) Central Accounts Section (CAS) of RBI, Nagpur;
- e) e-PAOs (Electronic Pay and account Offices) / e-Treasuries of State Governments;
- f) Pr. CCA, CBEC (Principal Chief Controller of Accounts) / Accountant General of the States;
- g) Tax authorities of Centre and States.

Process involved in e-payment of GST:

13. Every tax payer who wants to avail the facility of e-payment will access GSTN for generation of the Challan through which payment is to be made. The following methods for creation of draft challan for GST payments are recommended:

- a) By Registered tax payer or his authorized person by logging on to GSTN Common Portal where basic details (such as name, address, email, mobile no. and GSTIN) of the tax payer will be auto populated in the challan;
- b) By authorized representatives of tax payers by logging on to the GSTN Common Portal whereafter the list of registered taxpayers represented by him will be displayed. He can select any tax payer on whose behalf he proposes to pay GST and challan details for such tax payer will be auto populated;

- c) By grant of temporary Registration number by any one Tax authority on GSTN Common Portal which can be used by both the tax authorities for facilitating tax payments on behalf of an unregistered person. Such a situation can arise during enforcement action by a tax authority and this temporary registration can be later converted into a regular registration number (GSTIN) if the tax payer has a regular GST liability to discharge after the enforcement action (detailed procedure described in Para 78 below);
- d) By creation of a challan without requirement of USER ID and Password, for enabling payment of GST by a registered or an unregistered person on behalf of a taxpayer as per the directions of the tax authority using the GSTIN (like the present provision under Service tax). In this method, GSTN would provide for a validation check (like CAPTCHA) so that challan can be created by a person and not by machine.

14. The issue whether challans should have provision for entering jurisdictional location (e.g. Commissionerate, division and range) was discussed in detail and it was decided that the same will not be mentioned in the challan. Instead, the Tax authorities would send the Taxpayers updated master data to GSTN as well as to Accounting Authorities. The incremental changes in the said master would also be sent on real time basis by the Tax authorities to GSTN and Accounting authorities. As challan would not have a jurisdictional location code, the Accounting Authorities would use the TAXPAYER Master received from Tax authorities for mapping the challans with the Jurisdictional PAOs / tax authorities' offices by having a suitable mapping mechanism.

15. Upon creation of the draft challan, the taxpayer will fill in the details of the taxes that are to be paid. The challan page will have sets of mandatory fields, which the user has to provide. The tax payer will have the option to pay CGST, IGST, Additional Tax and SGST concurrently. The tax payers can partially fill in the challan form and temporarily “save” the challan for completion at a later stage. A saved challan can be “edited” before finalization. After the tax payer has finalized the challan, he will generate the challan, for use of payment of taxes. The remitter will have option of printing the challan for his record. The challan so generated will have a 14-digit (yyymm followed by 10-digit) Unique Common Portal Identification Number (CPIN), assigned only when the challan is finally generated, this will help the portal and other authorities in identifying the challan. The CPIN would be a running serial number to be initialized every calendar month. After the challan is generated, it will be frozen and will not be allowed to be modified. The CPIN/challan so generated would be valid for a period of seven days. In case of payment through Mode III, CPINs would remain live with RBI for a period of 30 days. GSTN would purge all unused CPINs on the day immediately after the date on which the validity period is over (i.e. 7 days if Mode I or II is selected and 30 days if Mode III is selected for payment). At the end of each day (EOD), GSTN would send all the CPINs generated on that day to the Accounting authority of the Centre and to those accounting authorities of the states that so desire. The suggested format of the challan is appended at **Annexure – IV** which is a common format for all three modes of payment. Since the challan would be prepared electronically, chances of errors will be minimal. However to deal with challan correction in exceptional circumstances, a challan correction mechanism, prepared in consultation with the office of Pr. CCA, CBEC is detailed in paras 123 and 124 below.

16. Since there are three modes of payment, the tax payer has to choose the e-payment mode. This mode will also cover payment by Credit/Debit Card which can be used only after log in on the GSTN.

17. Once e-payment mode is selected, options will be shown to taxpayer to choose between Internet Banking and Credit / Debit Cards for making payment. In case Internet Banking mode is selected, a field with drop down box detailing names of various authorized banks, registered with GSTN for Internet Banking, would be displayed. The taxpayer will have option of choosing his preferred bank for Internet Banking. Credit and Debit Cards of all banks shall be accepted. However, the payment gateway services should be obtained by GSTN from the authorised banks or their payment gateway SPVs only. To encourage competition, preferably more than one such gateway should be provided on the GSTN portal, with display of their respective charge rate and service performance level. The taxpayer can choose any of the gateways available on the portal for making the payment. The exact charge should be calculated separately by the gateway service provider. The gateway provider should collect this amount separately over and above the challan amount. The challan amount should be fully credited to respective Government accounts maintained with the authorised bank (acquiring bank for CC/DC payments), while the gateway charges should be retained back by the gateway provider. The Government/GSTN should procure the payment gateway services from the authorised banks (or their SPVs) through an appropriate competitive process to keep the charge rates low. The Committee also deliberated the issue of charge back claims in case of credit card based payment, and felt that the possibility of such claims on payments to the government is minimal and manageable.

especially in view of implementation of two-step authentication norm by the banks. In addition, the taxpayer would be required to pre-register his credit card, from which the tax payment is intended, with the GSTN system. GSTN may also attempt to put in a system with banks in getting the credit card verified by taking a confirmation from the credit card service provider. The payments using credit cards can therefore be allowed without any monetary limit to facilitate ease of doing business. In the event of such claims, recommended standard operating procedure, prepared in consultation with RBI, is enclosed as **Annexure-V**.

18. In case of Payment Gateway, the first choice for a taxpayer would be to select the card type to be used for making the payment. Upon choosing the card type, the taxpayer would be displayed available gateway service providers servicing the card type. Once a taxpayer chooses a gateway, the interface of the gateway would be invoked. Alongside, GSTN will forward the same electronic string as was passed for Internet Banking (details in **para 19** below). The service provider will capture and verify the card details and debit the challan amount and additional gateway charges from the card holder. The Payment Gateway service providers are expected to build their interface with GSTN common portal to capture challan amount breakup in terms of CGST, IGST, Additional Tax and SGST. Along with the interface, associated accounts for CGST, IGST, Additional Tax and state-wise accounts for SGST should be created by the Authorized banks associated with the gateway service providers. The breakup received from GSTN common portal will be used to credit the amounts received under respective accounts created for the purpose. The Committee noted that in respect of credit card payments, presently the acquiring bank is permitted to transfer the amount to the merchant on

T+3 basis. Thus there may arise some situations where the taxpayers account has been debited on T+0 basis whereas Government's account in authorised bank would be credited on T+3 basis. It was informed by RBI that this time could be reduced to T+1 basis by suitable negotiations with the payment gateways. It is recommended that suitable negotiations may be carried out by the Accounting authorities and RBI with payment gateways to credit the amount on T+1 basis.

19. In case of payment through Internet Banking, once the taxpayer chooses a particular bank for payment of taxes, GSTN will direct him to the website of the selected bank. Alongside, GSTN will forward an electronic string to the selected bank carrying the following details for each challan on real time basis:

- a) GSTIN;
- b) CPIN;
- c) Challan Amount;
- d) Break Up of the Amount into CGST, IGST, Additional Tax and SGST ;
- e) State/UT Government to which SGST remittance pertains.

GSTN in consultation with banks would decide about the requirement of merchant code as a GSTN identifier.

20. Taxpayer will make the payment using the **USER ID** and **Password** provided by the bank to enter into the secured e- banking area of his bank. He will select an account for debiting the total tax amount and authorize the payment. While making the payment, the bank will display the breakup of total amount payable into CGST, IGST, Additional Tax and SGST and seek confirmation from the user. No change in the break up as well as the total amount would be allowed on the Bank's portal. In case the user

wants to change the break up or the total amount, he should abort the transaction and go back to GSTN portal from the bank's portal and reinitiate the process.

21. After the successful completion of a transaction, e-FPB of the concerned bank will create a unique Challan Identification Number (CIN) against the CPIN. This will be a unique 17-digit number containing 14-digit CPIN generated by GSTN for a particular challan and unique 3-digit Bank code (MICR based which will be communicated by RBI to GSTN). The incorporation of the date of payment in the CIN may be examined from the IT's perspective. This CIN, as a combination of CPIN and Bank Code, will be reported by the banks along with its own Unique Bank reference number (BRN). Such CIN is an indicator of successful transaction and will be used as a key field for accounting, reconciliation etc. by taxpayers, accounting authorities and tax authorities. After every successful e-payment transaction, there will be an instantaneous reverse flow of information through an electronic data string from the collecting bank to the GSTN containing the following details:

- a) CIN;
- b) GSTIN;
- c) Bank Reference number (BRN);

[Since there could be maximum of four credits against one debit, banking practice may be ascertained by GSTN. If such transactions (i.e. four credits against one debit require multiple BRNs i.e. one for each credit entry), all BRNs should be reported.]

- d) Challan amount;
- e) Date of Payment;

f) Time of Payment

22. If the transaction cycle is not completed because of failure of credential verification, there would be no response from the bank to portal informing about the same. If a response (positive or negative) is not received by GSTN within the stipulated period (few minutes), there would be a feature in GSTN to re-ping the bank system and seek a response against CPIN. There may be a scenario in which the internet banking transaction is successful, but the connection drops before the control comes back to GSTN portal, and the re-ping facility will help in finding the status of such transactions.

23. Upon receipt of confirmation from the bank regarding successful completion of the transaction, GSTN will inform the relevant tax authorities about payment of taxes. A copy of the paid challan (downloadable/printable) with auto-populated CIN, date and time of payment and a statement confirming receipt of the amount by the bank will be provided to the taxpayer by GSTN.

24. Thereafter the tax paid challan (CIN) will be credited to the tax ledger account of the taxpayer. It was discussed and agreed by the Committee that there would be 20 ledger accounts (one for each Major heads i.e. CGST, IGST, Additional Tax & SGST and 4 Minor heads for each Major Head i.e. Interest, Penalty, Fees & Others).

Role to be played by each Stakeholder.

GSTN.

25. In the framework of GST administration, GSTN is envisaged to be a “pass through portal” that works as a common interface between taxpayers, tax authorities,

authorized banks, RBI and accounting authorities. So GSTN will play the following role in this mode of payment:

- a) Generation of challan along with CPIN;
- b) Facilitating e-payments by providing a linkage to Internet Banking interfaces of authorized banks and payment gateways of authorised banks for CC/DC based payments;
- c) Receipt of real time data from IT system (e-FPBs) of each authorized bank regarding successful completion of payment transaction by the taxpayer (CIN);
- d) Generating receipt containing BRN No. of collecting bank for taxpayer acknowledging receipt of payment by the bank. A further facility of generating receipt containing RBI's scroll number for taxpayer would also be provided;
- e) Information to the respective Tax Authorities on real time basis for each successful transaction reported by banks. The communication at this stage may contain a minimal set consisting of GSTIN, CIN (i.e. CPIN + Bank Code), BRN(s), Challan amount, break-up of the amount into CGST, IGST, Additional Tax and SGST and date of payment;
- f) At EOD, GSTN will also send the details of CPIN generated for the particular day to the Accounting Authority of the Centre (to facilitate estimation of revenue and fund management) and to such State accounting authorities that may so desire;
- g) On T+1 morning, GSTN will generate a consolidated file containing a summary as well as entire details of the challans for which successful transactions were reported by the banks on real time basis for the date value of T=0 (for this purpose, daily transactions would include transactions from 20:01 hrs on previous day to 20:00 hrs in the current day). The file will be sent to the

respective accounting authorities. At this stage, the challan data will also include CIN (i.e. CPIN + Bank Code) and BRN reported by the banks. GSTN would generate this file on all working days including the days on which no transaction took place;

- h) GSTN will receive 39 consolidated e-scrolls from RBI (one each for CGST, IGST and Additional Tax and one each for SGST for each State/UT Govt, see para 26(a) below) on T+1 basis. The contents of the scrolls are mentioned in **para 28** below;
- i) On receipt of consolidated transaction level e-scrolls from RBI during latter part of the day, GSTN will carry out preliminary system based reconciliation with reference to the successful transactions already reported real time by the banks and consolidated by GSTN as per step (g) above. GSTN will append the RBI scroll Number on each challan and thereafter forward its reconciliation results to the respective accounting authorities;
- j) Once the amount reflected in the CIN, received by GSTN from Bank on real time basis, is credited in the cash ledger of the taxpayer, GSTN will lock that CIN to prevent its further usage;
- k) Purge all unused CPINs after the expiry of seven days in case of Mode I & II / 30 days in case of Mode III;
- l) Receive TAXPAYER master as well as updates thereto from the respective Tax Authorities on real time basis.

e- FPBs (ELECTRONIC FOCAL POINT BRANCHES) OF AUTHORIZED BANKS.

26. There would be a single e-FPB for each Authorized bank for the entire country. It will perform the following role.

- a) Each e-FPB will open a major head wise (CGST, IGST, Additional Tax and SGST) account of each government (total 39 accounts) to which the remittances received by it would be credited. Currently, the Constitutional Amendment Bill states that the Additional Tax will be collected by Centre and assigned to States. If this arrangement is continued, the e-FPB will maintain one account for Additional Tax for Centre. A Committee has been constituted by the EC to examine the operational issue of Additional Tax and if it is decided that this tax will be collected by the respective State Government and retained by them, separate accounts for every State will have to be maintained for Additional Tax also, on the lines of SGST;
- b) Sending real time data regarding successful completion of payment transaction by the taxpayer (CIN);
- c) At the end of each day (T+1), each e-FPB will be responsible for preparing daily luggage files Major Head wise (CGST, IGST, Additional Tax and SGST) for each government detailing receipts from all modes of payments on a particular day (including nil payment days) and forwarding it to RBI in the morning. Each luggage file will have a Unique Serial Number which will be a running serial number extending through a financial year which will facilitate identification of missing files. This luggage file number will become part of the electronic file. For operational purposes such as size of the file, it may be broken up into different parts with each part being numbered uniquely and also mentioning the total number of parts of that file;
- d) In the morning of each day (T+1), each e-FPB will also forward the daily luggage file mentioned above to accounting authorities of the Centre and the respective

State, in case their accounting authorities so desire, so that they can independently monitor delayed remittances, if any, from the banks to the Government account in RBI;

e) On the first day of every month, e-FPB will provide Datewise Monthly Statements (DMS) for each tax and government separately to RBI for the preceding month with following details:

- i) Name of Tax;
- ii) Government Name;
- iii) Datewise number of successful transactions and total credit reported to RBI; and
- iv) List of discrepancies remaining unresolved at the end of the report month (MOE UIN, CIN, BRN, Amount, Nature of discrepancy).

These statements will be simultaneously communicated to the respective Accounting Authorities, if they desire so.

27. Each authorised bank should have one or more service branch in each State to serve as GST help desk and to receive queries / e mails to resolve the issues from Taxpayers, Tax Authorities and Accounting Authorities.

e-Kuber (Core Banking System) of RBI.

28. The following functions will be performed by RBI (e-Kuber):

- a) RBI will consolidate luggage files received from all authorized banks, debit their accounts and correspondingly credit the CGST, IGST and Additional Tax accounts of Government of India and SGST accounts of each State/UT Government maintained in RBI(39 accounts);

- b) RBI would send consolidated, digitally signed e-scrolls, along with all the challan details, for each type of Tax (one each for CGST, IGST and Additional Tax for Government of India, and separate e-scrolls of SGST for each State/UT Governments) per day (including NIL payment day) after including the amount collected by it in Mode – III to Accounting Authority of Centre (e-PAO) / each State (e-Treasury) and GSTN simultaneously. Daily Major head account-wise scroll from RBI will consist of following information:-
- (i) Merchant Code given to GSTN;
 - (ii) Scroll Number and Date;
 - (iii) Name of Government to which the scroll pertains;
 - (iv) CIN;
 - (v) GSTIN;
 - (vi) BRN;
 - (vii) RBI Transaction Number;
 - (viii) Mode of payment;
 - (ix) Tax amount;
 - (x) Control parameters like total transaction, Total Amount in the scroll, etc.
- c) If any discrepancy is reported by Accounting Authority or GSTN, it would carry out the correction mechanism with the authorized bank and thereafter report the corrected data to respective Accounting Authority and GSTN.
- d) RBI will consolidate Datewise Monthly Statements (DMS) received from the banks for each tax and government, validate the consolidated statements (39) with reference to its own data of e-scrolls reported during the report month, have a systemic review of unresolved discrepancies and communicate the

statements to the respective accounting authorities within 3 days from end of the report month.

Central Accounts Section (CAS) of Reserve Bank of India, Nagpur.

29. CAS, Nagpur reports daily consolidated credits and debits to each Government and Accounting Authorities. Such daily statements cover all receipts and payments for the respective governments including inter-government transactions. GST credits will be one of the items reported by CAS, Nagpur in its daily statements. The scroll number mentioned in para 28 (b) (ii) above should be the credit identifier in the daily statements.

e-PAOs (Electronic Pay and Account Offices) of Centre and e-Treasuries of State Governments.

30. In the case of Central government, the existing e-PAO (Central Excise) and e-PAO (Service Tax) can work as e-PAO (IGST), e-PAO (CGST) in the GST regime. Another e-PAO (Additional Tax) can be operated till the time that the Additional Tax remains in force. All these e-PAOs can be located at Delhi itself. The State governments will need to establish their e-PAOs / e-Treasuries (proposed Central Accounting Unit in the RBI Report of 2014). The following functions will be performed by e-PAOs/e-Treasuries:

- a) At EOD, the Central Accounting Authority and those State accounting authorities that so desire will receive details of CPIN generated by GSTN for the particular day. (Centre's accounting authorities require this to facilitate estimation of revenue and fund management);
- b) Each morning (T+1), e-PAOs / e-Treasuries will receive from GSTN a consolidated file of entire details of the challans (including CIN) for which

successful transactions were reported by the banks to GSTN on real time basis for the previous day;

- c) Each morning (T+1), e-PAOs for CGST, IGST & Additional Tax and e-Treasuries of the State Government will get consolidated transaction level digitally signed daily e-scrolls from RBI (along with all the challan details) pertaining to the successful transactions of the previous day (date value T=0);
- d) E-FPB of authorized banks would also send such scrolls on T+1 basis to central accounting authorities and to those e-Treasuries that may so desire;
- e) They will also receive from GSTN, later in the day, results of reconciliation by GSTN with the bank's and its own data;
- f) The e-PAO and e-Treasuries of the States would reconcile the challan details [received in step b) above] with the e-Scroll information [received from RBI in step c) and from GSTN in step e) above], and do the detailed revenue accounting based on the information provided in the e-scroll provided by RBI to the accounting authorities;
- g) They will receive TAXPAYER master from the respective Tax Authorities (backend module) and the same would be required to be kept updated on real time basis by the respective Tax Authorities. The said TAXPAYER master would be used by the Accounting Authorities for mapping the challan details with the Jurisdictional PAOs by having a suitable mapping mechanism. This is a requirement of the Government of India for determining revenue from each formation. States may also follow a similar procedure, if they so desire;
- h) They will also provide CIN wise payment / challan details to the respective Tax Authorities daily or periodically as per requirements / norms of their

governments for departmental reconciliation and for updating Tax Authorities database that the tax amount has been accounted in the government's books. Accounting Authorities should provide their accounting reference number (in Government of India, CIN is used for this purpose; some State Governments seem to be generating their own accounting reference number) for each challan accounted by them along with the tax amount as per the credit accounted by them to the jurisdictional Tax Authorities for reconciling their records.

- i) They will provide verified Datewise Monthly Statement (DMS) to Pr. CCA, CBEC (Principal Chief Controller of Accounts) and Accountant General of the states.

Pr. CCA, CBEC (PRINCIPAL CHIEF CONTROLLER OF ACCOUNTS) AND ACCOUNTANT GENERAL OF THE STATES.

31. The following functions will be performed by them.

- a) They will receive daily and monthly Put Through Statements from CAS, RBI;
- b) They will also receive verified Datewise Monthly Statement (DMS) from e-PAOs and e-Treasuries of the States respectively;
- c) The reconciliation of both the data will be carried out by them;
- d) Office of Pr. CCA CBEC will also consolidate the total collection and forward the same to the Office of CGA for further consolidation.

II. OVER THE COUNTER PAYMENT THROUGH AUTHORIZED BANKS.

32. Another mode of payment that will be employed in the proposed GST regime will be Over the Counter (OTC) payments which will enable the taxpayers to make payment of the taxes at the Authorized Bank's counter. This will be beneficial for smaller taxpayers that do not have access to internet banking facilities. CCA raised an

issue that the authorized banks might be asked as to whether they would be able to scroll these OTC payments through e-FPBs. This was discussed and RBI's representative assured that the scrolling by e-FPBs of OTC payments in one scroll would be ensured. The authorized banks will be required to establish / upgrade their IT software for accepting GST receipts.

33. The following stakeholders will play a key role in establishing an effective OTC payment system in the proposed GST scenario:

- a) GSTN;
- b) Branches of Authorized Banks;
- c) e-FPBs of Authorized banks;
- d) e-Kuber of RBI;
- e) e- PAOs of Centre / e-Treasuries of State Governments;
- f) Pr. CCA, CBEC / Accountant General of the States;
- g) Tax authorities of Centre and States.

Process involved in Over the Counter payment of GST through authorized banks:

34. Every tax payer who wants to avail the facility of OTC payment (only for paying tax upto Rs. 10,000/- per challan), will access GSTN for generation of a challan through which payment is to be made.

35. Upon creation of the draft challan, the taxpayer will fill in the details of the taxes that are to be paid. From the available payment options, the taxpayer would select option of cheque, DD or cash based payment. The name of the authorized bank and its

location (city/town/village) where the instrument/cash is to be presented is required to be filled in necessarily. No outstation cheques are to be accepted except those which are payable at par at all branches of bank having presence at that location. In case cheque or DD is selected as the mode of payment, entry of Instrument details is recommended, but not mandatory, as the taxpayer may not have the instrument ready at the time of challan generation. The tax payers can partially fill in the challan form and temporarily “save” the challan for completion at a later stage. A saved challan can be “edited” before finalization. After the tax payer has finalized the challan, he will generate the challan, for use of payment of taxes. The challan so generated will have a Unique Common Portal Identification Number (CPIN), assigned only when the challan is finally generated, that will help the portal and other authorities in identifying the challan. After the challan is generated, it will be frozen and will not be allowed to be modified. The CPIN / challan so generated would be valid for a period of seven days within which payment is to be tendered. GSTN will inform the challan details including validity period to the CBS (Core Banking System) of the selected bank on a real time basis.

36. Upon successful saving of the challan details, the challan will be available on the dashboard of the taxpayer in downloadable/printable form. So the taxpayer can either download the challan form and print it offline or can print the challan directly from GSTN. If the payment is made by cheque or DD, the challan itself would have a disclaimer that the payment is subject to realization of cheque or DD.

37. Thereafter taxpayer will approach the branch of the authorized bank for payment of taxes along with the instrument or cash. Since the tax payer is required to pay four types of taxes and the amount is required to be credited in the accounts

maintained by bank for each type of tax, one option for the tax payer is to submit four instruments for crediting to the respective accounts. Four instruments may not be required if pooled account for realization of instrument is maintained. The matter was discussed in detail and it was recommended, that in the interest of facilitating the payment, each e-FPB should maintain a GST pool account so that the tax payer can issue only one instrument which will be written in the name of the GST pool account of the concerned bank. The bank's IT system upon realization of the instrument, will immediately first credit that amount to the GST pool account and then immediately transfer that amount to the respective tax accounts [CGST, IGST, Additional Tax or SGST(39 accounts) as per details in challan (CPIN Data)]. However RBI representatives observed that since there would be real-time sharing of data between GSTN and Agency Banks, the details would be available to the bank official before submission of the challan by the customer. In such a situation, GSTN would have already shared the break-up of the total amount to the bank and the bank needs to credit the same in the appropriate head. The internal Accounting mechanism of bank may be left to the bank to design, as the requirement here is the proper booking and reporting of the transaction which banks would have to ensure. It was decided that those banks need not operate a GST pool account which can credit the amount in the respective tax accounts 'on the fly'.

38. There should be a linkage between the GSTN and the Core Banking System (CBS) of the authorized banks whereby the details of challan are shared with the Authorized bank selected by the tax payer on real time basis so that they can be stored in the database of banks and also to facilitate the cashier / Teller to verify the details of the

challan submitted by the remitter. This will eliminate the need for manual feeding of the challan details by the cashier / Teller in the banking system and thereby reduce the errors in data processing.

39. The taxpayer should preferably carry two copies of the challan, one for the bank's record and another for himself to get acknowledgement. In the alternative, he can use a normal pay-in-slip and mention CPIN and challan amount in it. On approaching the bank, he should provide the challan itself or at least CPIN number on normal pay-in-slip to enable the cashier / teller to fetch the challan details in his system. There should be a customized IT application (software) in the bank's system to accept GST receipts on OTC basis. While each branch can accept GST receipts, the credits should always be to the GST accounts maintained and operated by e-FPB . The banks not having such system should not be allowed to accept OTC payments. The minimum requirements to be met by the banks for being authorized to accept GST receipts for all modes including OTC mode are detailed in **para 85** below.

40. The cashier / teller will verify the details of challan, payment instrument and amount provided by the taxpayer with those displayed in his system and should accept the receipt only when no discrepancy is found. If the challan has crossed its validity period of seven days, the bank's system itself should bar acceptance of the payment. In any case, the challan would also not be available in the GSTN and consequently in the bank's system because it would have been purged from the System by GSTN upon the expiry of the 7 day validity period.

41. The tax payer may make payment by cash or instruments drawn on the same bank or on some other bank in the same city. In case of cash payments or same bank

instruments, the payment would be realized immediately and a transaction number (BTR/BRN) and CIN will be generated immediately at the authorized bank's system which will be unique for each and every transaction. Such successful transactions shall be intimated to GSTN on real-time basis with details similar to those mentioned in **para 21** above. This message will convey to the common portal that the payment has been successfully received at the bank's counter.

42. After generation of BRN, the bank cashier may give a printed receipt from his system including the Bank's transaction number (BTR/BRN) and CIN. However, if it not found feasible to print a separate receipt, the cashier should record the BRN and CIN generated from the system, on the tax payer's copy of the challan or pay-in-slip as acknowledgment.

43. In case an instrument drawn on another bank in the same city is presented, the payment would not be realized immediately. In such case, CIN will not be generated immediately, and cashier should write only the system generated acknowledgment number on the challan / pay-in-slip and a stamp to the effect that the acknowledgment by the bank is subject to realization of the cheque / DD. The tax-payer need not visit the bank again to get CIN as the same will be communicated to him from GSTN as per the process detailed in **para 47 & 48** below. However, if he does not receive any communication from GSTN within 3 days, he should visit the bank to ascertain the status of his payment.

44. Where the instrument is drawn on another bank, there should be a validation in the bank's system to prevent out station cheques (except those payable at par across

cities), and to also prevent deduction of commission charges for instruments drawn on another bank in the same city.

45. The Authorized Bank would send the instrument for collection and the transaction would be treated as complete and successful only after the actual receipt of the amount by the said bank.

46. The bank will inform GSTN on real time basis in two stages. First when an instrument is given OTC. At this stage the Authorized bank will forward an electronic string to GSTN which will contain the following details:

- a) CPIN;
- b) GSTIN;
- c) Challan Amount;
- d) Bank's acknowledgement number.

On receipt of the above first message, GSTN should send a SMS to the tax payer, in addition to showing the status of the payment on its portal as subject to realization.

47. The bank's system would send a second message to GSTN once the cheque is realized, the total amount is credited first to GST pool account and thereafter the funds are credited to the respective tax accounts as per CPIN data (as stated in para 34 above, GST pool accounts are not required to be maintained by those banks who can credit the amount in the respective tax accounts 'on the fly'). On the day of realization, it will become a successful transaction to be reported to RBI on T+1 (T = 0 being day of realization). After the successful completion of transaction, the second

acknowledgement will have the same details as mentioned in para 46 above with three additional details:

- a) CIN;
- b) Date of Realization of Cheque;
- c) Time of realization of cheque;
- d) Bank Transaction Number (BRN/BTN).

On receipt of the second message, GSTN would send a SMS to the tax payer, in addition to updating the status of the payment on its portal.

48. This 2 stage intimation by authorized banks is recommended for the following reasons:

- a) Keep a watch on delays on the part of authorized banks in realization;
- b) Maintaining a system based control as all branches of authorized banks will be allowed for OTC.

49. On receipt of the real time information for a successful transaction as per **para 41** above (cash, cheque on same bank or DD) or receipt of the second message from Bank as per **para 47** above (cheque drawn on another bank), the tax paid challan will be credited to the tax ledger account of the taxpayer. If the OTC payment was subject to realization (**para 46**), the initial status on the dashboard will state so. If the cheque is dishonoured, the presenting bank should inform GSTN about the fact of dishonour and same will be informed by GSTN to taxpayer and reflected on his dashboard.

Role to be played by each stakeholder.

50. The role played by each stakeholder in this mode of payment will be the same as mentioned in Mode I. There is an additional stakeholder in this mode, namely Branch of Authorized bank that receives the remittances and its role is discussed below.

Branch of Authorized bank.

51. Being the first point of contact for the remittance by the taxpayer, the branch of the Authorized bank receiving the payment will play a key role in the accounting and reconciliation of data with GSTN. It will perform the following functions:

- a) Accept the payment only through the customized GST software/screen in its system.
- b) Provide an acknowledgement to the tax payer;
- c) Send the instrument (if pertaining to another bank) to the clearing house for realization and record the result in the IT system as and when the response is received. Such recording should be system based rather than manual and include realization or dishonouring of the cheque, as the case may be, so that the IT software can take up further action including intimation to GSTN on real time basis;
- d) Credit the realized amount into either GST pool account, if so, maintained by the authorized bank (in its e-FPB) and thereafter transfer the said amount into the individual tax head accounts as indicated in the challan (all Authorized banks must develop a suitable GST software for this purpose) or to credit the amount directly to the respective government's account (39 accounts).
- e) In case the instrument is dishonoured, the presenting bank should inform GSTN.

52. It is to be noted that banks will have to develop a mechanism/IT application where all these amounts tendered at individual branches of an authorized bank are only handled through the e-FPB of that authorized bank. This is because the tax accounts will be maintained only by the e-FPB. Individual branches have not been authorized by RBI to operate Government account. **It is also important to provide for a mechanism in GST Law to debar those tax payers whose cheques have once bounced from using this mode of payment. The most effective mechanism will be through GSTN which should debar such defaulters from using this mode.**

III. PAYMENT THROUGH NEFT/RTGS FROM ANY BANK (INCLUDING OTHER THAN AUTHORIZED BANKS):

53. The third mode of payment envisaged under the GST regime is OTC payment through all banks including other than authorized banks, i.e., a bank where a tax payer may have account but that bank may not be authorized by the Government to accept GST receipts. The payment through this mode will strictly be a matter of normal banking service of NEFT / RTGS provided by that bank to its customer. The chances of error in this mode are similar to that of any remittance done through NEFT / RTGS. However, care needs to be taken to ensure that CPIN number is correctly mentioned in NEFT / RTGS message. The Committee recommends that this mode being a new mode of remittance should be scaled up gradually starting with a pilot run by RBI. It was informed by RBI that a detailed process flow could be worked out with specific provisions for validations. RBI further informed that this concept was being tested in Karnataka and this experience would be further used for developing this mode of payment. NEFT / RTGS mandate would have the same validity period of seven days as

the CPIN and the date upto which it would remain valid would be printed on it. The Committee observed that in this mode of payment, it would not be possible to automatically ensure that a CPIN was not used beyond its validity period of 7 days. It was decided that CPIN once generated and intimated by GSTN to RBI in this mode though will have a validity period of 7 days but would remain live with RBI for a period of 30 days. In case the payment is received after the expiry of the said 30 days, RBI would return the amount to the remitter bank. **Beside this, it was also decided that there should be a provision in the GST law whereby any taxpayer using this mode beyond the validity period (seven days) of the CPIN more than two times would be barred by GSTN from availing this mode of payment.**

54. Although the process under this mode will be more or less similar to the OTC payment discussed earlier in **paras 32–52** above, but due to involvement of a new stakeholder i.e. a non-authorized bank, certain modifications are required for this process. This process will be beneficial for those taxpayers who do not have a bank account in any of the authorized banks or find such bank to be far away for OTC payment or want to make the payment directly from their account in their own bank only. In this mode, only payment through National Electronic Funds Transfer (NEFT) / Real Time Gross Settlement (RTGS) is to be allowed as other payment instruments would require the Central and the State Governments to create accounts with non-authorized banks also which will not be desirable.

Process involved in payment through NEFT / RTGS from any Bank (including other than authorised banks):

55. Every tax payer who wants to avail the facility of payment through NEFT/RTGS mode will access GSTN for generation of a challan through which payment is to be made.

56. Upon creation of the draft challan, the taxpayer will fill in the details of the taxes that are to be paid. As agreed by the RBI representative, RBI would itself be the recipient of the amount transferred through NEFT / RTGS, thus eliminating the need for a link-up first with an authorized branch to receive the payment and thereafter its transfer to the RBI. RBI would thus perform the role of Authorized bank and that of e-FPB in this mode of payment. In this view, the name of the authorized bank will be auto populated as RBI. As a part of the challan preparation, a tax payer will have to choose the mode of payment as NEFT / RTGS from any bank. The challan so generated will have a Unique Common Portal Identification Number (CPIN), assigned only when the challan is finally generated. The generated Challan will have a NEFT / RTGS mandate associated with it. This mandate will contain NEFT / RTGS pooling bank account details (i.e. of RBI) along with IFSC for receiving money. After the challan is generated, it will be frozen and will not be allowed to be modified. The CPIN so generated would be valid for a period of seven days within which payment is to be tendered but would remain live with RBI for a period of 30 days. NEFT/RTGS mandate would have the validity period of CPIN printed on it. As mentioned above, there shall be a provision in the GST Law whereby any taxpayer using challan under this mode beyond the validity period of

seven days of the CPIN more than two times would be barred from availing this facility by GSTN.

57. Upon successful saving of the challan details, the challan will be available on the dashboard of the taxpayer in downloadable / printable form. So the taxpayer can either download the challan form or print it offline or can print the challan directly from GSTN.

58. Besides the generation of challan, GSTN will also generate NEFT / RTGS mandate form in prescribed format. The CPIN generated at the portal shall be incorporated in NEFT/RTGS mandate form in "Account Name" field. RBI would provide for suitable validations for this field. The "Sender to Receiver" field shall carry the entry "GST Payment". In case of NEFT / RTGS payments, there shall also be a disclaimer on the challan copy and the mandate form that the payment through NEFT / RTGS is a transaction between the tax payer and his bank and the payment will be deemed to be received by the government only when the amount is credited to the designated account in RBI. **The payments in this mode would be permitted only against cheques and no cash payments would be permitted to initiate NEFT / RTGS transaction for the reasons mentioned in Para 67 below.**

59. The following details will be available in the NEFT / RTGS mandate form.

- a) Beneficiary IFSC : IFSC of RBI hosting the NEFT / RTGS account for GST;
- b) Beneficiary Account Number : Account Number of RBI's pooled account for GST;
- c) Account Name : CPIN of relevant challan (suitable validation to be provided by RBI);

- d) Total Amount;
- e) Sender to Receiver Remarks: GST Payment.

The form will have a provision to write the NEFT/RTGS charges manually and then record the total amount to be collected by the bank (sum of challan amount and charges). The entire NEFT/RTGS form will be auto-populated except the part relating to the charges.

60. Thereafter taxpayer can print a copy of NEFT / RTGS mandate form and approach his bank branch (any bank) for payment of taxes (within a period of seven days of the generation of CPIN, so that when the amount is received by RBI, the CPIN is still valid.) The payments in this mode would be permitted only against cheques and no cash payments would be permitted to initiate NEFT / RTGS transaction. NEFT/RTGS mandate would have validity period of CPIN printed on it. As already mentioned above, there should be a provision in GST law whereby any taxpayer using this mode beyond the validity period (seven days) of the CPIN more than twice would be barred from availing this facility by GSTN.

61. GSTN will inform RBI on real time basis the following details:

- a) CPIN;
- b) GSTIN;
- c) Challan Amount;
- d) Break Up of the Amount into CGST, IGST, Additional Tax and SGST;
- e) State/UT Government to which SGST remittance pertains.

62. The accepting bank should add its charges for doing NEFT / RTGS remittance and collect gross amount from the customer. The amount indicated as GST amount for remittance should be transferred by the remitter bank to the designated account of the government in RBI. For the proper identification of the transaction, there should be a Unique Transaction Reference (UTR) that should be conveyed along with file details to RBI. The remitter bank must also mention the CPIN in the NEFT/RTGS mandate as part of the Account Name. The Remarks field shall mention 'GST Payment'.

63. Upon successful completion of the transfer at the end of the remitter bank, the remitter will get a receipt detailing Unique Transaction Reference (UTR). Taxpayer should thereafter login back to GSTN portal and update the challan details with Unique Transaction Reference (UTR) provided by the remitter bank for NEFT / RTGS transaction. An alternate SMS based facility for such updating by the tax payer (instead of internet based) may be established by GSTN to facilitate those taxpayers who do not have an internet access. On receipt of the transaction number, GSTN will communicate this Unique Transaction Reference (UTR) (for the corresponding CPIN) also to RBI on real time basis.

64. Once the RBI receives the payment in its account with NEFT/RTGS message, it will link up the payment with the CPIN earlier received from GSTN and report the transaction to GSTN on real time basis through an electronic string which will contain the following details:

- a) CIN (CPIN and Bank Code of RBI);
- b) GSTIN;
- c) Challan Amount;

- d) BRN of RBI;
- e) Unique Transaction Reference (UTR);
- f) Time of Payment;
- g) Date of Payment.

65. Upon receipt of the electronic string regarding successful completion of the transaction by GSTN, the tax paid challan will be credited to the cash ledger of the taxpayer. The GSTN will thereafter lock the CIN so that it cannot be used again.

66. As recommended in para 58 above, the Mode III may be implemented with arrangement of CPIN being mentioned as the “Account Name” in NEFT/RTGS message. RBI will provide for a suitable validation for this field. In such arrangement, the chances of error will be only marginal as the remitter banks take care to mention the account name correctly in any NEFT/RTGS message. In case of error, NEFT/RTGS unique transaction number (UTR) intimated by the tax payer can be used as a secondary identifier. The primary matching by RBI should be with reference to CPIN only, i.e., CPIN as contained in NEFT/RTGS message and CPIN data provided by GSTN. On successful matching, the GST pooled account should be debited and the respective 39 tax accounts (CGST, IGST, Additional Tax and SGST) should be credited simultaneously as per the challan details with generation of CIN and BRNs. At this stage, the transaction should be treated as successful and CIN and BRNs should be communicated to GSTN by RBI.

67. As stated in para 15 above, though the CPIN is valid for a period of 7 days, the same would remain live with RBI for a period of 30 days. Thus RBI can accept the payment during the said period of 30 days. In case payment is received after the expiry

of 30 days, RBI would refund the said amount to the remitter bank. Keeping in view this requirement, it has been recommended, as mentioned above, that payments in cash would not be accepted for initiating NEFT / RTGS transaction.

68. The Committee deliberated the need for a pooled GST account. Based on inputs provided by RBI, a receiving account is necessary for NEFT/RTGS process. Therefore, a pooled GST account as an operational necessity will have to be opened in RBI. This account may be opened in the name of the Accounting Authority of the Government of India solely for the operational reasons as a transit account. There should be a validation in RBI system that no funds pertaining to the transactions with date value $T=0$ are left in this account when the scroll is prepared on $T+1$.

69. If the matching based on CPIN does not succeed, the role of UTR as secondary matching identifier becomes important. However, it is possible that RBI may receive NEFT/RTGS message even before the tax payer updates his challan with UTR number and GSTN informs RBI on real time basis. In case of failure of CPIN based matching and UTR not being available, the funds will remain in the pooled account till the UTR is received or scroll is prepared, whichever is earlier. Such credit in the pooled account should be with a “CPIN mis-match” flag that a secondary level matching needs to be carried out before scroll is generated on $T+1$ basis. Once UTR is provided by GSTN, the secondary matching of all such transactions remaining in the pooled account should be carried out. If a transaction can now be linked to the correct challan, the respective Tax accounts should be credited with generation of CIN and BRNs. There should be a validation in RBI system that all the transactions with “CPIN mis-match” and date value $T=0$ in the pooled account are subjected to secondary level matching before generation of scroll for all taxes.

70. If the matching based on CPIN and UTR NEFT / RTGS transaction number UTR both fails, the entire receipt should be credited to CGST account with a “CPIN mis-match” flag so that the Accounting Authorities of Government of India can account such amount under a separate suspense sub-head (possibly receipts awaiting transfer i.e. RAT).

71. In all such cases of CGST credits with “CPIN mis-match”, the tax payer will not get a confirmation SMS from GSTN and his ledger will not reflect the payment. He can be expected to provide UTR at this stage. Once the UTR becomes available, GSTN should carry out the matching with CPIN, and communicate following details to the Accounting Authorities of Government of India and concerned State Government.

- a) RBI scroll number and date which carried the credit (CGST scroll);
- b) BRN;
- c) CIN (of credit to CGST account with “CPIN mis-match” flag);
- d) Challan amount;
- e) Breakup of total amount in CGST, IGST, Additional Tax and SGST;
- f) Name of State Government to whom SGST pertains.

72. Based on the communication from GSTN, CGST Accounting Authorities shall take steps for clearing the suspense sub-head by transferring the credit to CGST, IGST and Additional Tax accounting heads, and for carrying out inter-government transfer to the concerned State Government.

73. The reconciliation between e-Scroll sent by RBI on T+1 and the transaction details available with GSTN (provided earlier by RBI) will be performed using CIN and Unique Transaction Reference (UTR).

Role to be played by each stakeholder.

74. As for the role played by each stakeholder in this mode of payment, it will be same as for their role in OTC payments through authorized banks. The role of Branch of remitter bank that transfers the funds to RBI and the additional role of RBI performing the functions akin to authorized banks is discussed below.

Branch of remitter bank.

75. The branch of the remitter bank would perform the following functions:

- a) Remitter bank is required to ensure that the correct CPIN is entered in the NEFT / RTGS message and also inform UTR to the taxpayer;
- b) Transfer the amount indicated in the NEFT / RTGS message [which includes Unique Transaction Reference (UTR)] to RBI.

RBI performing functions akin to authorized banks.

76. RBI's role for the Mode III will be akin to that of authorised banks for other modes, i.e, RBI will be the bank which will receive the funds directly from a taxpayer's account in a pooled account. It should be possible to have a suitable IT system which will carry out CPIN or UTR based matching (as detailed in para 66 above) for each NEFT/RTGS receipt and credit the remittance to a specially created pooled GST account and thereafter transfer it to the respective tax accounts of each government.

77. Once the remittances are received by RBI, it will perform the following functions:

- a) RBI will receive and validate the NEFT/RTGS transaction against the Challan details received by it;

- b) RBI would communicate the receipt of payment (CIN) to GSTN on real time basis;
- c) On first day of every month, RBI as e-FPB will provide Datewise Monthly Statements (DMS) for each tax and government separately to the concerned wing of RBI for the preceding month with following details:
 - i) Name of Tax;
 - ii) Government Name;
 - iii) Date wise number of successful transactions and total credit reported to RBI; and
 - iv) List of discrepancies remaining unresolved at the end of the report month (MOE UIN, CIN, BRN, Amount, Nature of discrepancy).

These statements will be simultaneously communicated to accounting authorities of the Centre and the respective States in case their accounting authorities so desire.

- d) RBI will also be responsible for incorporating these payment details in their daily master scroll generated by them as an aggregator for amounts received through Mode I and II.

PAYMENT ACROSS DEPARTMENTAL COUNTER.

78. The issue was discussed in the Joint Committee on Business Process and it was decided that since the emphasis in GST regime is towards automation and least human interface between the tax administration and the taxpayer, therefore there is no need to provide for this mode i.e. payment across departmental counters. It was also stated that

taxpayers have been provided various other modes to facilitate anytime, anywhere payment and this mode would be retrograde especially when e-payment is being declared as the preferred mode of payment. However, the departmental officers will accept the deposit of taxes during the course of enforcement and anti-evasion investigations including by flying squads, etc. While doing so, if the concerned person is not already registered, the departmental officer will create a temporary GSTIN on the GSTN common portal. For this purpose, GSTN will provide a separate module and a GSTIN series for giving temporary GSTIN. The officer will collect the amount in respect of all types of taxes payable by him in cash/cheque/DD from the said person, issue a temporary receipt to him, generate the challan from GSTN, fill up the challan (at a later stage, if not possible at that time) and remit the amount using Mode2. GSTN will provide a facility for linking of the temporary GSTIN to the permanent GSTIN, if taken at a later stage.

PENALTY MECHANISM FOR ERRING BANKS.

79. At present, banks are subjected to penalty for delayed fund remittances only. Current system of remuneration to banks for collection of Central Excise, Service Tax and Customs duties is determined on the basis of challans. New parameters of bank performance could be developed, based on timely remittance and reporting of error-free data to all stakeholders. A system of incentives / penalties to be administered by the respective Accounting Authority (i.e. if defaults arise in remission of CGST/IGST/Additional Tax, by Accounting Authority of Centre and if defaults arise in remission of SGST, by Accounting Authority of the concerned state) can be built-in, based on a transparent evaluation mechanism of the quality of data of collection

reported by banks for accounting and reconciliation purposes. The CGA has suggested that penalties for inaccurate reporting and delayed settlement of taxes is already in place in the case of Direct Taxes and the same may be put in place in GST regime. It is further recommended that a framework of desired features and validations at Banks for collection of taxes under GST regime should be devised by RBI in consultation with the Accounting Authorities. Any bank found not having built capabilities to adhere to the framework, should not be allowed to collect GST receipts. Due care should be taken so that discontinuities arising from manual interventions in the banks' internal processes are removed. The Committee also recommends that, over a long term, Accounting Authority should develop a service quality rating for the participating banks based on identified transparent and quantifiable parameters.

BANKING ARRANGEMENTS UNDER GST:

80. At present Central Government and each State Finance Department prescribes banking arrangements for collection of government taxes. At present, Central and State governments utilize the services of Public Sector Banks/ Other Public Sector Banks (IDBI)/ Private Sector Banks (ICICI Bank, Axis Bank, HDFC Bank) for tax collection. The committee was informed that Non-Scheduled and Cooperative banks operating in State(s) are not permitted to collect taxes.

81. The list of all authorized banks participating in the GSTN should be common across all states. This can be a super set consisting of existing authorized banks of the Central Government and all State Governments and Union Territories. A list of banks that have been presently authorized either by the Centre or State Tax Authorities has been provided by RBI and the same is enclosed as **Annexure-VI**. It is recommended that

all these banks may be considered for authorization in the GST regime in consultation with the Department of Financial Services.

82. Only those banks should be accredited who refine their IT systems to handle GST remittances in a seamless manner obviating need for manual intervention for data entry, funds flow and exchange of data.

83. It is also noted that a participating bank in the current context has limited mandate for tax receipts as compared to that of an authorized bank. The mandate of participating banks, though essentially agents of RBI, is limited to acceptance of tax receipts through internet banking mode only. Whereas, authorized banks have a broader mandate of accepting government receipts through both internet banking mode and physical mode (OTC) of Cash, DD and Cheques, in addition to mandate of making government payments. In order to give a broader choice to the tax payers, and hence to enhance ease of doing business, it is recommended that the participating banks can also be allowed to accept GST receipts through OTC mode envisaged in this report.

84. Out of the superset of existing authorized banks and participating banks only those banks should be authorized to accept GST receipts who meet the minimum requirements suggested below. The objective of these minimum requirements is to ensure that a bank has the capability to handle GST receipts in a seamless manner in a consistent and error free manner underpinned by a robust IT system with no process flow discontinuities.

85. Minimum requirements to be met by a bank for being authorized for GST remittances are recommended to be as follows:

- a) A centralized application for handling GST receipts for both modes (internet banking and OTC) in an end-to-end manner should be established.
- b) There should not be any process flow discontinuities for any mode of the receipt.
- c) The system should not require any post-event data entry at any stage.
- d) The data entry at any stage of the process should be limited to the operations performed at the bank's end.
- e) The data received from GSTN portal should not require any fresh data entry and should not be open for modification.
- f) There should be functional integration with GSTN portal and banks for both modes.
- g) The IT system should have the ability to receive challan data and to communicate successful remittances on real time basis to GSTN portal for both modes.
- h) The collation of data and reporting to GSTN portal and to RBI should be system based and not require manual operations.
- i) The standards of communication prescribed by RBI (**ISO 20022**) should be followed.
- j) There should be an upfront (before being authorized) as well as periodic audit of the IT system and the centralized application for handling GST receipts. The system audit should cover operational, technical and security aspects as per terms of reference and periodicity set by GSTN in consultation with Accounting Authorities.
- k) One branch of the concerned authorized bank in the entire country should be established / designated as the e-FPB (Electronic Focal Point Branches) to handle

all backend operations of GST receipts including operation of 39 tax accounts, data collation, reporting and reconciliation with RBI / GSTN / Accounting Authorities.

- l) In addition, one or more branch of the concerned authorized bank in each State Capital should serve as GST helpdesk (Refer Para 27 above).
- m) Three separate tax accounts for Government of India (one each for CGST, IGST and Additional Tax) and one tax account for each State/UT Government (36 in total) (for SGST) should be set up and operated by e-FPB alone.
- n) The credit to respective tax accounts should be simultaneous with debit to the tax-payer's account in case of internet banking mode, realization of a cheque or submission of DD/cash in case of OTC mode and receipt of NEFT / RTGS remittances from remitter banks into RBI's pool account and then its transfer to tax accounts.
- o) The above mentioned credit to the respective tax accounts should be by the IT system itself as per the mandate contained in the Challan data received from GSTN and not require manual intervention.
- p) In addition to tax specific 39 accounts (for CGST, IGST, Additional Tax and SGST account for each State / UT Government), a common pooled account for cheque/Draft and CC/DC payments should be set up and operated by e-FPB (but not required by those banks who can credit the amount 'on the fly').
- q) As a part of the daily consolidated but transaction level report of successful receipts in each government account to RBI, there should be an assurance that all transactions credited to respective CGST, IGST, Additional Tax and SGST Accounts are being reported to RBI and no balances are left in these accounts

meant for cheque realization. RBI will need to build a similar assurance for NEFT/RTGS remittances.

- r) Suitable validations prescribed by GST Law should be inbuilt in the IT system / GST application. Some of such validations will pertain to non-acceptance of outstation cheques and non-deduction of cheque collection charges for OTC receipts, and mark up and collection of CC/DC charges (to be agreed) from tax payers.

86. It was agreed that the minimum standards to be met by the participating banks, as encapsulated above, should be communicated to the banks well in advance in consultation with RBI.

ACCOUNTING SYSTEMS UNDER GST:

87. State governments/UTs accounting system also follows, to a large extent, the general principles and procedures of Central government accounting, with minor variations in respect of classification of tax heads of accounts. While the List of Major and Minor Heads of accounts are common to both Central and State/UT Governments accounts, classification below Minor Heads may vary at the State level.

88. Under the proposed GST regime, it is recommended that a uniform system of banking arrangement for both the Central and State/UTs governments to facilitate fund flow, reporting and accounting may be framed.

PROPOSED ACCOUNTING SYSTEM UNDER GST:

89. Four different Major Heads of accounts would be required to be opened for classifying CGST, IGST, Additional Tax and SGST along with underlying minor heads and sub-heads, wherever required, to account for various taxes.

90. There is a need to standardize these accounting codes for all items covered under GST regime among all the States and UTs, since settlement of IGST would be based on centralized reporting. SGST will be accounted for by the States and credited to individual State Treasuries, through the existing system followed in each State. SGST will not be reflected in accounts of the Central Government.

91. There may be cases of mis-classification and erroneous scrolling under Major Heads of accounts which may lead to less or excess revenue settlements between the Centre and State(s). To deal with such transactions, detailed accounting procedures should be designed. It is recognized that it is IT system issue, and not an accounting issue. The debit from tax-payers account should result in auto-credit to respective accounts of Government of India and the concerned State Government. Except in case of remittance through any authorized bank including a non-agency bank (where the funds have to necessarily come to a designated account in RBI), there should not be any mix-up of the funds belonging to two governments.

92. The CGA has suggested the following in this regard.

- a) Codal provisions of the DDO & PAO should be complied with for discharge of PAO's role. The automation as proposed should conform to this basic requirement.

- b) PAO is the sole authority for receipt, payment and reconciliation of accounts book with Bank Reconciliation statement (BRS).
- c) Any compromise on this fundamental work flow may lead to legal complications in preparation of Finance Accounts / Appropriation Accounts which is constitutional mandate.
- d) Each challan detail must be linked with one DDO and PAO and bank account.
- e) As part of standard operating process, accounts classification should be done by the PAO in his books and no one else. Bank is not involved in classification of accounts.

93. The challan will reflect only the net tax paid amount along with related bifurcations of nature of tax liability, such as, Interest, Penalty, Fees, other charges, etc. Presently, the Tax Payment Challan information forms the basis of accounting and reconciliation between the banks, RBI, Tax authorities and Accounting authorities of the Centre/States/UTs. A list of sample tax accounting codes under GST is proposed in the table below:-

S. No.	Type of Tax Liability	Sample Accounting Code
1	CGST - Tax	00010001
2	CGST – Interest	00010002
3	CGST – Penalty	00010003
4	CGST – Fees	00010004

5	CGST – Other	00010005
6	IGST – Tax	00020001
7	IGST – Interest	00020002
8	IGST – Penalty	00020003
9	IGST – Fees	00020004
10	IGST – Other	00020005
11	SGST- Tax	00030001
12	SGST – Interest	00030002
13	SGST – Penalty	00030003
14	SGST – Fees	00030004
15	SGST – Other	00030005
16	Additional Tax – Tax	00040001
17	Additional Tax – Interest	00040002
18	Additional Tax – Penalty	00040003
19	Additional Tax – Fees	00040004
20	Additional Tax – Others	00040005

The actual accounting codes have to be finalized by CGA in consultation with CAG on the basis of proposals from Tax Authorities.

94. CGST, IGST and Additional Tax components will be accounted for under Consolidated Fund of India (CFI). Transfers of due IGST amount and Additional Tax to the States can thereafter be made there from as per the existing procedure.

95. The interest, penalty, fees or other charges, if any, under GST will need to be accounted for separately. Hence, they would be reflected under separate heads in the Tax Payment Challan.

96. The IT audit of the process flows and settlement of funds by the FPBs / Link cells with RBI will be conducted periodically by a CERT-IN empanelled agency selected by the office of Pr. CCA, CBEC, or by a designated authority of States/UTs so as to ensure correctness of revenue collections.

RECONCILIATION OF RECEIPTS:

97. Well-developed and stabilized IT systems without manual process discontinuities in banks, RBI and common portal should eliminate/reduce possibilities of errors. However, there may still be reconciliation challenges arising due to errors encountered during the stabilization phase of the IT systems of the stakeholders and their mutual functional integration. Even in the post stabilization phase, some errors may be seen due to problems external to the IT systems, e.g., in the public network used for sharing the data. A process and standard operating procedure for handling the

errors, if they arise, will have to be established, as multiple agencies would be handling funds and related information pertaining to different governments.

98. The proposed GST payment process envisages a paradigm shift from the processes and validations currently being used for payment of taxes to the Government. This shift is aimed at establishing a convenient, consistent and efficient payment process for the tax payers as well as for the 37 governments simultaneously. This shift is possible in view of current IT capabilities in the eco-system and the experience gained in various systems for payments to the governments.

99. Following are the fundamental changes from the existing systems:

- a) Tax payer will generate the electronic challan, and therefore that challan data can be trusted for its correctness for its contents, as filled in by the taxpayer.
- b) The challan thus generated on GSTN portal will provide a unique Id (CPIN) which would be used uptill the time payment has been received by the bank and CIN (CPIN plus Bank Code) has been generated. The said CIN would be used thereafter for accounting, reconciliation, etc.
- c) All modes of payment will use the system generated electronic challan and there would not be re-digitization of the challan data, as recorded by the taxpayer, by any agency in their part of the workflow.
- d) Any agency handling the payment process will merely add its unique Id and parameter to the basic data received by it from another agency earlier in the workflow chain, and thereafter pass on the data to the agency next in the chain.

e) RBI will play the role of the aggregator for flow of funds as well as information from the banks.

f) GSTN will have the primary anchor position in the payment process with responsibility for information flow to various agencies whereas RBI will have the primary anchor's role in relation to funds flow, information flow about receipts and correction of discrepancies noticed during reconciliation process.

g) e-Scroll from RBI will be the basis for accounting, reconciliation and other incidental activities to be carried out by the accounting authorities of both Centre and States.

100. In view of these fundamental changes, the key Id for information exchange with banks and RBI should use the unique Id generated by GSTN, i.e., CPIN. Once the payment has been made by the taxpayer and CIN is generated and reported by the recipient bank along with its transaction number (BRN), CIN which has CPIN embedded there in, would be used as key Id in subsequent stages. CIN is recommended to be used as a key Id as it is the sole indicator of the receipt of actual payment. Similarly, the transaction reported by RBI for the funds flow (credit) to government accounts through the e-scrolls should form the basis for accounting as it reflects the actual credit in the Government Accounts.

Reconciliation by GSTN:

101. GSTN through its IT system should carry out reconciliation in following two stages:

a) When the banks report each successful transaction on real time basis, the IT system should validate the bank's message with reference to CPIN and total amount of the challan, and communicate the discrepancy, if any, immediately. This validation and real time response by GSTN is particularly relevant for Mode II and III for which the entire payment is not in a single workflow.

b) When consolidated e-scrolls are received from RBI on T+1 basis, GSTN should carry out the reconciliation between those scrolls and the consolidated challan files communicated to the Accounting Authorities earlier in the day. The discrepancies should be communicated by GSTN to the Accounting Authorities and RBI simultaneously on the same day. The purpose of this reconciliation is to assist those Accounting Authorities who may not have IT systems to carry out transaction level reconciliation in an automated manner, and to identify systemic and service level issues for taking up with the authorized banks and RBI.

102. The role of GSTN in the reconciliation process should be limited to the above set of activities. GSTN should not be expected to take up MOE process for any error type as that is fairly resource intensive, requires manual appreciation of facts and is time consuming. The transaction level resolution of discrepancies through the Memorandum of Error (MOE) process with RBI and banks should be the responsibility of the respective Accounting Authorities.

Reconciliation by Accounting Authorities.

103. The Accounting Authorities through their IT systems are expected to carry out the reconciliation at their level *de novo* based on communication by GSTN of challan data for successful transaction received on T+1 basis (State AG authorities to be assisted

for setting up accounting interface with GSTN) or through Tax Authorities system (based on the integration capabilities at Central / State level) and e-scrolls received from RBI for each day on T+1 basis. The reconciliation results communicated by GSTN would act as additional validation in the reconciliation process. The reconciliation would be performed on the basis of CIN, which will be the unique identifier across all databases.

Resolution of Reconciliation Outcomes (discrepancies noted during the reconciliation process).

104. There would be to and fro data transmission between GSTN, e-FPB of Authorized Banks, banks other than authorized Banks, RBI, Accounting Authorities and Tax Authorities. There is a scope of error occurring at each leg of communication. The process for reconciliation of such errors in each leg of communication is discussed in succeeding paras.

First leg of communication of data (CPIN linked to a GSTIN) starts from GSTN to Authorized banks.

105. If the data forwarded by GSTN (CPIN linked to a GSTIN) itself has an error then this error will be reflected in all the later transactions. So significance of accuracy of this data cannot be overemphasized. It would be important for GSTN to maintain a robust system for maintaining data integrity and keeping the data error free by having suitable validations at the time of creation of CPIN. Key elements here are CPIN and GSTIN.

Second leg of communication of data (CIN with embedded CPIN) starts from Authorized banks / RBI to GSTN (T-0):

106. This communication is not meant to be the basis for accounting, but act as an enabler to reduce errors in the overall process and to facilitate fleet-footed monitoring by the Tax Authorities. The IT system of the authorized banks should have the following validations to reduce possibility of discrepancies in this leg:-

- a) In any reporting of successful transactions by the banks to GSTN, CPIN field is never a blank;
- b) The response sent back to GSTN is always against a CPIN received from GSTN;
- c) Sum total of all credits to Tax accounts for a particular CPIN adds up to the challan amount.
- d) CIN reported by the authorized banks/RBI should always have a CPIN embedded in it.

107. In spite of the above mentioned validations, if a discrepancy is found in a bank's response, the discrepancy will get noticed in the real time validation of the response by the GSTN. The response sent by e-FPB of authorized bank (in Mode I & II) / RBI (in Mode III) should be validated with the data sent earlier by GSTN to Authorized bank / RBI. Key elements are CPIN, GSTIN, CIN & Challan amount in case of authorized banks and CPIN, GSTIN, CIN, NEFT/RTGS UTR and Challan amount in case of RBI. This validation between CPIN available with GSTN and CIN received from e-FPB of authorized banks / RBI should be done on real time basis and the discrepancies, if found should be communicated to the concerned banks immediately by GSTN's IT system so as to enable

time to the banks for correction, if possible, before communicating the receipts to RBI on T+1 basis.

108. The validation by GSTN may throw up following discrepancies in the transaction being reported (with CIN added by the bank) by e-FPB of authorized bank / RBI:

- a) without CPIN;
- b) with incorrect CPIN;
- c) with challan amount mismatch.

109. In all these cases, the resolution at e-FPB may require manual intervention. The bank may resend the data to GSTN after correction. If the bank is unable to resolve by T+1 reporting time to RBI, the bank should include the transaction in the luggage file with whatever CPIN data it may have for that transaction. It will be type (c) error in the third leg.

Third leg of communication of data (luggage file) starts from Authorized banks to RBI (T+1).

110. In this leg, the data is being collated and transferred by authorized banks to RBI in daily luggage files for each type of tax of Government of India (CGST, IGST & Additional Tax) and SGST (state wise; for 29 states and 7 UTs) separately [there will be total thirty nine luggage files (3+29+7)]. The key element here is CIN. So the accurate reporting of the same by the authorized bank to RBI has to be underlined. As RBI would prepare e-scrolls based on this data, correctness and cleanliness of this data is crucial. RBI collates daily luggage files (thirty nine) received from all the authorized banks, includes payments received directly by it in Mode III, adds RBI Transaction Id for all

modes, prepares and sends daily e-scroll (one for each major head for Centre and each State) to GSTN and Accounting Authorities. Reconciliation by GSTN and Accounting Authorities (of the Centre and the States) will be initiated after they receive their respective files (Government of India authorities will receive three files while State Authorities will receive a file each). Errors in this leg of communication would be detected at this stage. Various situations that can be envisaged in this leg are as follows:

a) Transaction reported to GSTN by authorized banks but not to RBI (CIN reported to GSTN but not included in luggage file):

111. To prevent/minimize this type of error, the bank's IT system should have a validation that all credits to the Tax accounts for the date value being the previous day should get reported to RBI in the luggage file. This discrepancy will be detected at the stage when GSTN and Accounting Authorities compare the challan data (CIN) of the day received from authorized banks with the e-scroll of the corresponding date received from RBI on T+1 basis. If GSTN detects such a discrepancy, it will communicate the same to the relevant Accounting Authority and RBI. On the basis of this information or on the result of their own reconciliation with reference to CINs reported earlier by GSTN, the Accounting Authority will generate a Memorandum of Error (MOE) with a Unique Identification Number (UIN) and communicate the same to the RBI and copy the same to the concerned authorized bank and GSTN. GSTN being only a pass through portal, should not be entrusted the work of MOE and its resolution. Moreover, MOE process requires manual appreciation of facts, accounting expertise and decision making on behalf of each Government, which will be beyond GSTN's mandate/capacity. The steps involved in the correction mechanism in the aforesaid situation are as follows:

- i) GSTN to report the error to the relevant Accounting Authority (and Tax Authority, if GOI or concerned State so wants) and RBI, if the discrepancy is detected by GSTN;
- ii) The relevant Accounting Authority to generate a MOE with a UIN and communicate the same to RBI with a copy to concerned authorized bank for resolution (Accounting Authorities of the Centre and States will have to initiate MOE in respect of their respective taxes) (This may be on the basis of discrepancy detected and communicated by GSTN or by the Accounting Authorities themselves);
- iii) RBI to ascertain from e-FPB of the concerned authorized bank / RBI and get the discrepancy corrected. E-FPB of the concerned Authorized bank / RBI must rectify this discrepancy within a period of two days from the date of receipt of MOE from the Accounting Authority;
- iv) Rectification by the concerned e- FPB / RBI will be by way of identifying the missing transaction, putting it in a separate luggage file containing the UIN of the relevant MOE and then transmitting the same to RBI;
- v) RBI will send a separate e-scroll relating to MOE to the concerned Accounting Authority containing the missing transaction;

Points at iv) and v) are design issues, which can be decided by GSTN in consultation with RBI. The reporting by e-FPB and thereafter by RBI can be through separate files as mentioned above, or the normal luggage file from banks and scroll from RBI can contain the now resolved transaction with a MOE resolution flag and UIN as additional field for the relevant record.

vi) Accounting Authority to note the correction of MOE and report the same to GSTN and the concerned Tax authority thereby completing the transaction cycle;

vii) RBI to take steps to penalize the e-FPB of the concerned Authorized bank.

b) **Transaction reported by Bank to RBI but not to GSTN (CIN included in luggage file but CIN not reported to GSTN):**

112. In case of payment through internet banking (Mode I), this seems to be an unlikely scenario, as all payments will be processed at the Core Banking Solution (CBS) of the concerned e-FPB of authorized bank and therefore the compiled data that it reports to RBI on T+1 basis will be nothing but the compilation of data (CIN) already reported by e-FPB of authorized bank on real time basis to GSTN. This discrepancy may however arise due to communication failure even after the prescribed rounds of pinging.

113. This discrepancy can arise in other modes of payment (Mode II and III), because the payment cycle is not a single workflow, is spread over a longer period of minimum two days and requires participation of various banking officials even though the entire cycle is supposed to be done on the IT system customized for GST payments.

Such a discrepancy will be detected by GSTN when it undertakes a reconciliation of the challan details (CIN) of a day available with it with the e-scroll of the same day received from RBI on T+1 basis. In such cases, the correction mechanism will involve the following steps:

i) If CPIN and associated data reported in the scrolls received from RBI matches with GSTN's CPIN data, GSTN can forward the entire challan details of that CPIN to

the concerned Accounting Authorities with a copy to Tax Authorities. **There will not be any need for MOE in such case.** The Accounting Authorities will carry out the accounting based on scroll data received from RBI and tally it with the challan data (CIN) now received from GSTN. GSTN would also update the taxpayer's cash ledger after confirming the payment from the authorized bank / RBI;

ii) If e-FPB of an authorized bank has reported a transaction to RBI in GST luggage file, without it being a GST transaction or without realization of the amount, it should take up such cases for refund outside the MOE process as a more comprehensive verification will be needed before allowing the refund. For minimizing this kind of error, the bank's IT system should have validations/controls mentioned in **para 85** above;

iii) Only if the CPIN and associated data in the scroll does not match with GSTN's data there will be a need for MOE. That will be type c) error, discussed in the paragraph below. In those cases, the Accounting Authority should create MOE with a UIN and communicate it to RBI with a copy to e-FPB of the concerned authorized bank. (The Accounting Authorities will identify the concerned bank on the basis of bank code contained in the CIN reported against the successful CPIN in the e-scroll received from RBI).

c) **Transaction reported to RBI but with incorrect details of CIN (CIN level mismatch).**

114. This kind of error can be minimized through suitable validations in the bank's IT system. If the error still occurs, it will be noted when the scroll data is processed by GSTN / Accounting Authorities. Even if the error gets noticed earlier as mentioned in

para 109 above but remains unresolved till the time of reporting to RBI on T+1 basis, the bank should report the transaction to RBI with whatever CIN data it has received from the e-FPB of authorized bank. The bank should not hold back any balance in the tax accounts beyond the reporting time to RBI in respect of transactions of the previous day. When such unresolved transaction is reported to RBI, it should carry a flag indicating type of discrepancy. RBI should credit the amount to the account of the respective government as mentioned in the luggage file. As the scroll from RBI will have an unresolved CPIN discrepancy, the Accounting Authorities may credit the amount to a separate sub-head under the relevant major head and simultaneously take up MOE process. If the discrepancy pertains to the total challan amount, its impact on individual taxes will get known during reconciliation of the scroll data with the challan data, and the Accounting Authorities of the affected government should take up MOE process.

d) Money transferred to wrong government accounts though CIN matches with data in e-scroll received from RBI (major head level):

115. It may so happen that while sending the luggage file to RBI, the e-FPB of the authorized bank / RBI reflects the amount received in a tax head different from the one specified in the challan (major head level) (CPIN).

116. In such a situation, Accounting Authorities will play a crucial role as they are statutorily responsible not only for proper accounting of money but also for its credit into the correct government account. This discrepancy will be ascertained by the Accounting Authorities while carrying out reconciliation between the challan data obtained from GSTN on T+1 basis (detailing major heads) and e-scroll (for each major

head separately) received from RBI. Steps involved in the correction mechanism are as follows:

- i) The relevant Accounting authority would generate MOE with UIN and communicate the same to RBI. Accounting Authorities of the Centre and States will have to initiate MOE in respect of their respective taxes;
- ii) RBI to ascertain from e-FPB of the concerned Authorized bank / RBI (in case of Mode III) and get the discrepancy corrected within a time period of 2 days from the receipt of MOE from the Accounting Authorities;
- iii) E- FPB of the concerned Authorized bank / RBI would verify the details in the CIN transmitted to GSTN with the details transmitted to RBI in the daily luggage file. Thereafter correction entry would be transmitted to RBI in a separate luggage file with UIN of MOE;
- iv) On the basis of information transmitted by e-FPB of the concerned Authorized bank, RBI would carry out the corrective Debit/Credit entries in the accounts of the concerned governments;
- v) Thereafter RBI would send a separate e-scroll relating to MOE to the relevant Accounting authority about the corrective entry carried out resulting in reconciliation and correction;
- vi) Relevant Accounting Authority to account for the corrective entry in its records and report correction of MOE to GSTN and relevant Tax authority thereby completing the transaction cycle;
- vii) RBI to take steps to penalize e-FPB.

e) **CIN neither transmitted to GSTN nor conveyed in luggage file from authorized bank to RBI and therefore not included in e-scroll received from RBI.**

117. This scenario will reflect the failure of the system at two ends. In this scenario the taxpayer has properly paid taxes into the government account through authorized / non-authorized banks but the same has neither been reported to GSTN nor to RBI thereby in effect eliminating the transaction from the system itself. So it is crucial that suitable protocol should be developed for dealing with this kind of errors. It has to be kept in mind here that CPIN generated at GSTN has a validity period of only 7 days within which the payment is to be tendered. **This error cannot be ascertained on the basis of any reconciliation as there will not be any flow of information from authorized banks / RBI.** The error will be noticed only when the taxpayer on not receiving a credit confirmation SMS from GSTN or not finding the credit in his ledger inform GSTN. Steps involved in correction are:

i) In case of OTC payment through authorized banks in cash or by instruments drawn on the same bank, taxpayer will be provided with an instantaneous acknowledgement by the bank containing CIN. As CIN is available with the taxpayer, he should inform GSTN about the transaction (CIN, bank branch where OTC payment was made and date of payment). On the basis of this information, GSTN should ascertain from e-FPB of the concerned authorized bank regarding receipt of payment. Once the confirmation is received through an electronic string, GSTN will validate the same against CPIN and thereafter the tax paid challan (CIN) will be credited to the taxpayer's ledger. e-FPB of the Authorized bank is now

expected to include this receipt in the luggage file for the day for transmission to RBI.

ii) In case of OTC payment through authorized banks by instruments drawn on another bank in the same city, the process of giving acknowledgement would be in two steps. In case CIN is not reported to GSTN by the e-FPB of the authorized bank, the taxpayer may follow the procedure detailed in sub-para i) above. E-FPB of the authorized bank is now expected to include this receipt in the luggage file for the day for transmission to RBI.

iii) In case of OTC payment through banks via NEFT/RTGS, upon successful completion of the transfer at the end of the bank, the taxpayer will get a receipt detailing Unique Transaction Reference (UTR). Taxpayer can thereafter login into GSTN and update the details of UTR provided by the bank for NEFT/RTGS transaction in the challan. GSTN is expected to communicate the UTR to RBI. In case the CIN is not communicated by RBI, GSTN will now take up the matter with RBI (instead of with authorized bank) in the manner detailed in sub para i) above. RBI is now expected to include this receipt in the e-scroll for the day, if NEFT/RTGS remittance was received. If the remittance was not received, RBI will inform GSTN accordingly. In turn, the tax payer will be intimated by GSTN for taking up the matter with his bank (through which NEFT / RTGS was effected by him) for deficiency of service.

f) **Sum total of amount for a CIN reported in e-scroll by RBI is lesser / greater than that reported by e-FPB of authorized bank / RBI to GSTN.**

118. This error relating to the shortfall can occur if a bank has deducted collection charges in Mode II and a bank has collected remittance charges for NEFT / RTGS transaction from the challan amount Mode III . Such errors in Mode II can be minimized through suitable validations in the bank's IT system. In such case, one of the tax amounts will be less than the amount indicated in the challan. The relevant Accounting Authority (for whom the amount received is less than the amount mentioned in challan) will have to take up MOE process with RBI with a copy to the concerned bank as detailed in **para 116** above for getting the shortfall amount.

119. In case the amount in the scroll is more than the challan amount for any tax, the bank will have to raise the MOE with the concerned Accounting Authority for the refund. Without approval of the Accounting Authority, the banks should not be allowed to adjust the excess amount against future receipts.

Fourth leg of communication of data is between RBI and GSTN & Accounting Authorities:

120. RBI is collating luggage files from e-FPBs of various authorized banks, including amount received by it in Mode III and thereafter generating and transmitting e-scrolls Major head wise to Government of India and SGST (state wise). During collation of the data, an error can creep into e-scroll resulting in missing / additional transaction. Since there is simultaneous flow of information to two different agencies i.e. GSTN and Accounting Authorities, following situations may arise:

- a) Transaction reported to GSTN by e-FPB of authorized banks but not by RBI in its e-scroll (CIN level);

- b) Transaction reported by RBI in its e-scroll but not by e-FPB of authorized bank / RBI to GSTN (CIN level);
- c) Transaction reported by RBI but with incorrect details of CIN (CIN level);
- d) Sum total of the amount for CIN reported to RBI is lesser/greater than that received by GSTN/Accounting Authority.
- e) There is mismatch between tax wise amounts while the total challan amount matches.

121. In all the situations mentioned above, the reconciliation and error correction mechanism would be similar to that in the third leg of communication (para 110 to 119 above) as the source of discrepancy cannot be identified. It can be at the bank level or at RBI level. Therefore, the concerned Accounting Authorities should take up MOE with RBI with a copy to concerned authorized bank. RBI should first verify the data at its own end for corrective measure, if the error had arisen from its actions, if the source of error is found by RBI to be the one of the authorized bank, it should facilitate/ensure corrective measure by the identified bank in a time bound manner.

Recording by Tax Authorities:

122. After reconciliation and successful accounting of each payment, the transaction level data with unique accounting number, if required by a State Government (some governments have that practice) should be communicated by the Accounting Authorities to the Tax Department's system for updating the records, which would finally contain following unique Ids for each receipt:

- a) CIN;

- b) GSTIN;
- c) Bank Transaction Number (BRN);
- d) RBI Transaction Number;
- e) Accounting Entry ID Number/confirmation flag.

The presence of all the above mentioned five fields would constitute the assurance for credit to the government account with RBI, and the reconciliation and accounting in the government books.

Challan Correction Mechanism.

123. In view of the presumptions listed above, the requirement of providing for a challan correction mechanism would be minimal though not completely ruled out. The Committee recommends for providing the correction mechanism in following situations:–

- a) **ERROR IN GSTIN:** This may happen in situations where the payment of tax is being made by either authorized representative such as CA or any other person on behalf of the taxpayer. Such kind of error will have no impact on the transfer of the funds to the account of the concerned governments as the money will be correctly transferred on the basis of the CIN. Further once the payment confirmation is received by GSTN from the concerned bank then the amount will be credited to the ledger of the taxpayer whose GSTIN is mentioned in the electronic string that is relayed by the bank to GSTN (earlier the same GSTIN was communicated by GSTN to bank). Therefore taking into account both the above factors as well as the fact that Challan has been generated either by the taxpayer himself or through his authorized representative and the mistake being committed has no impact on the

funds with tax administration, there is no need for providing an error correction mechanism for the same. The authorized representative, acting as an agent for the taxpayer should be responsible to the principal for any error committed while performing authorized acts and tax administration should have no role to play in this matter.

b) **ERROR IN MAJOR HEAD:** In such a scenario, the bank though has collected the correct amount but has credited the wrong head of tax account. This would impact the transfer of funds to the account of the respective governments as bank has transferred the funds on the basis of the data not detailed in CPIN. Thus bank would be required to withdraw funds from one account and credit the other account(s). It is proposed to permit banks to rectify such error before the end of the day during which the amount has been received by the bank as at the end of the day, the amount would have been credited in respective government accounts and thereafter the same would also have been accounted by Accounting Authorities of the Centre and State. No correction in the challan data is required even in this case. If the error is noted after reporting of the credit on T+1 basis, the normal MOE process should be used.

c) **ERROR IN TOTAL AMOUNT:** If the amount paid is in excess then there is provision for either claim of refund by the taxpayer or the amount can be carried forward to the next period and therefore there is no need to provide for correction mechanism.

124. In view of recommended maintenance of cash ledger, the fields relating to ‘Tax period’ and ‘purpose’ will not be captured in the challan as being done presently and therefore correction mechanism for correcting these two fields has not been provided for.

CHALLAN FORMAT:

125. e-Challan will remain the source document for the purpose of accounting and reconciliation by the accounting authorities of the Centre/States/UTs. The Office of C & AG has stressed upon the need for ensuring the availability of e-Challan for accounting and reconciliation purposes. A proper Challan format (**Annexure –IV**) that covers all the details required for accounting and reconciliation is essential to be prescribed, that will be treated as proof of payment to the government.

126. In the GST regime, the existing practice of entry of challan data at the bank branch level will be dispensed with as the challan would be shared on real time basis from the GSTN portal to the CBS of the authorized bank / RBI indicated in the challan.

127. Central Government Accounts (Receipt and Payment) Rules, 1983 provides for submission of Challan in form GAR 7 along with the payments to facilitate the Pay and Accounts Officer to classify the receipts accurately in his accounts. The form will need to be suitably modified for use in the electronic systems envisaged for GST payments. Almost all the information currently required in GAR 7 has been provided in proposed GST challan form. However, as discussed in **para 14 above**, the jurisdictional location

code will not be available in the challan and the same would need to be mapped with the help of the backend system of each tax administration.

(Satish Chandra)

Member Secretary

Empowered Committee

of State Finance Ministers

(Rashmi Verma)

Additional Secretary

Department of Revenue

Government of India

Annexure-I

EMPOWERED COMMITTEE OF STATE FINANCE MINISTERS

DELHI SECRETARIAT, IP ESTATE, NEW DELHI – 110002

Tel. No. 2339 2431, Fax: 2339 2432 e-mail: vatcouncil@yahoo.com

No.15/45/EC/GST/2014/32

Date: 7th April, 2014

JOINT COMMITTEE ON BUSINESS PROCESSES FOR GST

During the last Empowered Committee meeting held on 10th March, 2014, it was decided that a Joint Committee under the co-convenership of the Additional Secretary (Revenue), Government of India and the Member Secretary, Empowered Committee should be constituted to look into the Report of the Sub-Group-I on Business Processes for GST and make suitable recommendations for Registration and Return to the Empowered Committee. It was also decided that the Joint Committee should also keep in view the Registration and Return requirements necessary for IGST Model. Accordingly, a Joint Committee, in consultation with the Government of India, is constituted with the following members.

Government of India

- (1) Smt. Rashmi Verma, Additional Secretary (Revenue) -- Co-convenor
- (2) Shri P.K. Mohanty, Joint Secretary (TRU-I)
- (3) Shri M. Vinod Kumar, Joint Secretary (TRU-II)
- (4) Shri J.M. Kennedy, Director (TRU-II)
- (5) Director/Deputy Secretary holding the charge of
State Taxes Section

States Government

- (1) Dr. J.B. Ekka, Commissioner of Taxes, Assam
- (2) Shri Prashant Goyal, Commissioner, Trade & Taxes, Delhi
- (3) Shri H.V. Patel, Commissioner, Commercial Tax, Gujarat
- (4) Shri Sudhir Rajpal, Commissioner, Excise & Taxation, Haryana
- (5) Shri Kifayat Hussain Rizvi, Commissioner, Commercial Tax, J&K
- (6) Shri Ajay Seth, Commissioner, Commercial Tax, Karnataka
- (7) Shri Shyam Jagannathan, Commissioner, Commercial Tax, Kerala
- (8) Shri Amit Rathore, Commissioner, Commercial Tax, Madhya Pradesh
- (9) Dr. Nitin Kareer, Commissioner, Sales Tax, Maharashtra
- (10) Shri Abhishek Bhagotia, Commissioner, Commercial Tax, Meghalaya

- (11) Shri Manoj Ahuja, Commissioner, Commercial Tax, Odisha
- (12) Shri Sanjay Malhotra, Commissioner, Commercial Tax, Rajasthan
- (13) Shri K. Rajaraman, Commissioner, Commercial Tax, Tamil Nadu
- (14) Shri M.K. Narayan, Commissioner, Commercial Tax, Uttar Pradesh
- (15) Shri Dilip Jawalkar, Commissioner, Commercial Tax, Uttarakhand
- (16) Shri Binod Kumar, Commissioner, Commercial Tax, West Bengal

Empowered Committee of State Finance Ministers

- (1) Shri Satish Chandra, Member Secretary -- Co-convener

2. The Committee will submit its report to the Empowered Committee in two months time.

Sd/-
(Satish Chandra)
Member Secretary
Empowered Committee of
State Finance Ministers

Copy to: All the Members of the Joint Committee

Copy also to:

- (1) PS to Chairman, Empowered Committee of State Finance Ministers
- (2) Adviser to Chairman, Empowered Committee of State Finance Ministers
- (3) Sr.A.O./OSD/F.O./A.O., Empowered Committee of State Finance Ministers

Annexure-II

EMPOWERED COMMITTEE OF STATE FINANCE MINISTERS

DELHI SECRETARIAT, IP ESTATE, NEW DELHI – 110002

Tel. No. 2339 2431, Fax: 2339 2432 e-mail: vatcouncil@yahoo.com, vatcouncil@gmail.com

No.15/45/EC/GST/2015/20

Date: 3rd February, 2015

SUB-COMMITTEE ON PAYMENT PROCESSES UNDER GST

During the meeting of the Joint Committee on Business Processes for GST held on 2nd February, 2015, it was decided that a Sub-Committee should be constituted to consider the Report of the Committee for Finalizing Payment Processes under GST and to give its recommendations for the consideration of the Joint Committee on Business Process for GST. Accordingly, a Sub-Committee consisting of the following officers was constituted:

Government of India

1. Shri Shashank Priya, Commissioner, GST Cell, CBEC, Government of India	Co-convener
2. Shri Upender Gupta, Additional Commissioner, CBEC Government of India	Member
3. Shri Manish Saxena, Additional Director, Directorate General of Systems, Government of India	Member

States

1. Shri Ritvik Ranjanam Pandey, Commissioner, Commercial Tax, Karnataka	Co-convener
2. Shri K. Rajaraman, Principal Secretary/Commissioner, Commercial Taxes, Tamil Nadu	Member
3. Shri Manoj Ahuja, Commissioner, Commercial Tax Odisha	Member
4. Dr. P.D. Vaghela, Commissioner, Commercial Tax, Gujarat	Member

Goods and Services Tax Network

1. Shri Prakash Kumar, Chief Executive Officer, GSTN Member

Special Invitee

1. Shri Ajay Seth, former Commissioner, Commercial Tax, Karnataka Member

2. It was also decided to request RBI, Principal Chief Controller of Accounts, CBEC and Controller General of Accounts to nominate senior officers to attend the meetings of the Sub-Committee/Committee.

3. It was further decided that the first meeting of the Sub-Committee will be held at 10.00 am on 14th February, 2015 at Hotel Le Meridien, Bangalore. All the members of the Sub-Committee are requested to kindly make it convenient to attend the meeting of the Sub-Committee. They are also requested to intimate their travel programme to Shri Ritvik Ranjanam Pandey, Commissioner Commercial Tax, Karnataka (Tel: 080-22264495, Fax: 080-22263595 and e-mail: ritvik@gov.in) so that necessary arrangements for their boarding, lodging and transport could be made under intimation to the Empowered Committee.

Sd/-

(Satish Chandra)

Member Secretary

Empowered Committee of

State Finance Ministers

Copy to:

Additional Secretary (Revenue), Government of India with the request to kindly request RBI, Principal Chief Controller of Accounts, CBEC and Controller General of Accounts to nominate suitable officers to attend the meeting in Bangalore and subsequent meeting of the Joint Committee on Business Process for GST, when the Business Process for payment is considered by the Committee.

Copy to: All the members of the Sub-Committee

Copy also to:

Adviser/OSD/Sr.A.O./A.O., Empowered Committee of State Finance Ministers.

Annexure–III

LIST OF PARTICIPANTS OF THE MEETING HELD ON 16TH AND 17TH APRIL, 2015

Government of India

1. Smt. Rashmi Verma, Additional Secretary (Revenue), Government of India
2. Shri Manish Saxena, Additional Director, Director General of Systems, CBEC, Government of India
3. Shri M.K. Sinha, Director (Central Excise), Government of India
4. Shri Rajeev Yadav, Director (Service Tax), CBEC, Government of India
5. Shri Shashank Priya, Commissioner, GST, CBEC, Government of India
6. Shri Ravneet Singh Khurana, Deputy Commissioner, CBEC, Government of India
7. Shri Upender Gupta, Additional Commissioner, GST, CBEC, Government of India

States

1. Dr. Ravi Kota, Commissioner of Taxes, Assam
2. Shri Sanjeev Khirwar, Commissioner (VAT), Trade and Taxes, Delhi
3. Shri Jagmal Singh, Deputy Director, Trade and Taxes, Delhi
4. Shri Umesh Kumar Tyagi, Special Commissioner, Trade and Taxes, Delhi
5. Dr. P.D. Vaghela, Commissioner, Commercial Tax, Gujarat
6. Shri Riddhesh P. Raval, Assistant Commissioner, Commercial Tax, Gujarat
7. Shri Shyamal Misra, Commissioner, Excise & Taxation, Haryana
8. Shri Hanuman Singh, Additional Commissioner, Excise & Taxation, Haryana
9. Shri Zaffar Ahmad Bhat, Commissioner, Commercial Tax, Jammu & Kashmir
10. Dr. Shamim Ahmad, Additional Commissioner, Commercial Taxes, Jammu & Kashmir
11. Shri Ritvik Ranjanam Pandey, Commissioner, Commercial Tax, Karnataka
12. Dr. M.P.Ravi Prasad, Joint Commissioner, Commercial Tax, Karnataka
13. Shri M. Girees Kumar, Commissioner, Commercial Tax, Kerala
14. Shri M.I. Mansur, Assistant Commissioner, Commercial Tax, Kerala
15. Shri Sudip Gupta, Deputy Commissioner, Commercial Tax, Madhya Pradesh
16. Shri Rajiv Jalota, Commissioner, Sales Tax, Maharashtra
17. Shri P. Velrasu, Special Commissioner, Sales Tax, Maharashtra
18. Shri Manoj Ahuja, Commissioner, Commercial Tax, Odisha
19. Shri Sahadev Sahoo, Joint Commissioner, Commercial Tax, Odisha
20. Shri Vaibhav Galriya, Commissioner, Commercial Tax, Rajasthan
21. Shri K. Rajaraman, Principal Secretary/Commissioner, Commercial Taxes, Tamil Nadu

22. Shri K.Gnanasekaran, Additional Commissioner, Commercial Taxes, Tamil Nadu
23. Shri Mritunjay Kumar Narayan, Commissioner, Commercial Tax, Uttar Pradesh
24. Shri Rakesh Verma, Joint Commissioner, Commercial Tax, Uttar Pradesh
25. Shri Puneet Tripathi, Assistant Commissioner, Commercial Tax, Uttar Pradesh
26. Shri N.C. Sharma, Additional Commissioner, Commercial Tax, Uttarakhand
27. Shri Vipin Chandra, Joint Commissioner, Commercial Tax, Uttarakhand
28. Shri Khalid Aizaz Anwar, Joint Commissioner, Commercial Tax, West Bengal

Goods and Services Tax Network (GSTN)

1. Shri Navin Kumar, Chairman, Goods and Services Tax Network
2. Shri Prakash Kumar, Chief Executive Officer, Goods and Services Tax Network

Special Invitee

1. Smt. Nidhi Khare, Commissioner, Commercial Tax, Jharkhand

CCA

1. Mrs. Krishna Tyagi, Chief Controller of Accounts, CBEC
2. Alok Kumar Verma, Controller of Accounts, CBEC

CGA

1. Shri Chandan Mishra Dwivedi, Deputy Comptroller and General of Accounts

RBI

1. Shri G. Sreekumar, CGM, RBI
2. Shri Manish Parashar, Deputy GM, RBI

Empowered Committee of State Finance Ministers

1. Shri Satish Chandra, Member Secretary, Empowered Committee
2. Shri Bashir Ahmed, Adviser, Empowered Committee

PWC

1. Shri Kalyan K. Pal, PWC

Annexure-IV

GST CHALLAN FORM

CPIN	<<Auto Generated after submission of information>>

GSTIN	<<Filled in/Auto populated>>
Name	<<Auto Populated>>
Address	<<Auto Populated>>

Date	
Email address	<<Auto Populated>>
Mobile No.	<<Auto Populated>>

Tax Liability					
	Tax	Interest	Penalty	Others	Total
Government of India					
CGST					
IGST					
Additional Tax					
Government of <State>					
SGST					
				Total Challan Amount	

Note :

1. Different colors to reduce possibility of data entry errors to be provided.
2. Accounting Codes are to be provided for at the backend

Mode of Payment (relevant Portion to become active when selected)

☐ e-Payment	
Net Banking	☐
Credit Card	☐

☐ Authorised Bank OTC	
Name of Receiving Bank (where	

Debit Card ☐	
Name of Bank	
Name of Payment Gateway (in case of payment through CC /DC)	

instrument is proposed to be deposited)		
Name of Branch (Optional)		
Name of City/Town/Village where payment is proposed to be made		
Details of instrument(optional)		
Cash ☐	Ch/DD No.	
	IFSC Code	
Cheque ☐	Bank	
DD ☐	Branch	

Note : Only local cheques (not outstation cheques to be accepted)

☐ NEFT/RTGS Remitting Bank	
Name of Bank	
Name of Branch	
IFSC Code	
Name and Code of Beneficiary Bank (RBI and its code)	
Name of the beneficiary account (Description 'GST payment' to be auto Populated)	

Beneficiary Account Number (CPIN Auto Populated)	

Note:

1. Payments through RTGS / NEFT
2. Beneficiary to be defined as the RBI
and its account. This would be auto
populated by GSTN
3. Charges to be over and above Tax
amount

Paid Challan Information

Bank Reference No.	
CIN	
Date of Clearing	
NEFT/RTGS Unique Ref No.	

Challan Received at

Annexure V

Issue of charge back in CC/DC Payment

1. Under the charge back claim, a taxpayer after making payment through credit card may seek refund of the money till 60 days of the transaction. Usually such refunds can be sought under three scenarios:
 - (i) Payment was made fraudulently by someone using the card of others;
 - (ii) Extra payment was made because of some technical error during payment;
 - (iii) Some service was not delivered for the payment made.
2. During the past few years, there have been significant changes in the security systems surrounding a transaction done through credit cards. The nature of such transactions has undergone changes because of introduction of two factor authentication and OTP (one time password) as per RBI's regulations. Under such circumstances it has become more improbable to have fraudulent transactions. Banks also have stopped entertaining claims caused by fraudulent transactions. As such scenario (i), i.e., payment through fraudulent use can be practically ruled out.
3. In scenario (ii) arising from technical errors, the errors can be detected even before any transaction is reported to RBI on T+1 basis. The acquiring banks should have a validation in their IT system that no double payment is reported for a tax against the same CPIN. If a credit card has been charged twice for the same challan total amount, the additional collection may be refunded by the acquiring bank.

4. In case the technical error of charging the card twice is noticed after the transaction has been reported to GSTN on real time basis but before the reporting to RBI on T+1 basis, the acquiring bank can refund the amount under real time intimation to GSTN. Thereafter, such double payment should not be reported to RBI.
5. In case the technical error is detected after reporting to RBI on T+1, the acquiring bank should send the claim to GSTN with full details. GSTN should verify its database, and confirm to the bank regarding double payment received against the same CPIN.
6. There should be a validation in GSTN's system that such double payments (para 4 and 5 above) are either not reflected in the tax payer's ledger or the second payment against the same CPIN is barred from utilization. Based on the confirmation from GSTN, the acquiring bank can refund the extra payment.
7. For scenario (iii) arising from claim of non-delivery of service, the acquiring bank should send the claims to GSTN with full details. GSTN can rebut the claim by providing a copy of the Challan (pdf file generated from its system) used for making the payment and details of the tax-payer's ledger account in which credit was made to show that the service was provided. The bank can use the above details /document as a sufficient basis to repudiate any charge back claim for non-delivery of service. Such evidences have to be provided to banks within 48 hours of the claim.
8. Even if the charge back request for scenario (iii) is received by the acquiring bank before reporting of the transaction to RBI on T+1, the bank should send the claim to GSTN for a response. GSTN should verify its record, and rebut the claim as mentioned in para 7 above. GSTN will have 48 hrs to send its response. In the meantime at T+1 event,

the acquiring bank should report the transaction to RBI in normal course. The bank should not hold back the funds. Subsequently when the response is received from GSTN, the bank may either decide to reject the claim (most likely as it is fairly easy to establish that the tax was actually paid to the Government and there was no denial of service) or accept the claim. If the claim is accepted, the process suggested in para 9 below may be followed.

9. In case the charge back is accepted after reporting to RBI (either in case of scenario (ii) or in case of scenario (iii) when GSTN's rebuttal is not accepted) and refund is made by the acquiring bank to the issuing bank, such refund should be reported as a new transaction to RBI. The report to RBI as well as the entry in RBI's scroll should be as a debit entry identified using the original CPIN. On receipt of such information, GSTN should debit the taxpayer's ledger and inform the Tax Authorities who should recover the amount from the said taxpayer.

Annexure VI

List of Banks presently authorised in Centre and States

S. NO.	Name of Bank
1.	ALLAHABAD BANK
2.	ANDHRA BANK
3.	BANK OF INDIA
4.	BANK OF BARODA
5.	BANK OF MAHARASHTRA
6.	CANARA BANK
7.	CENTRAL BANK OF INDIA
8.	CORPORATION BANK
9.	DENA BANK
10.	INDIAN BANK
11.	INDIAN OVERSEAS BANK
12.	ORIENTAL BANK OF COMMERCE
13.	PUNJAB NATIONAL BANK
14.	PUNJAB & SIND BANK
15.	SYNDICATE BANK
16.	UNION BANK OF INDIA
17.	UNITED BANK OF INDIA
18.	UCO BANK
19.	VIJAYA BANK
20.	STATE BANK OF INDIA

21.	STATE BANK OF BIKANER & JAIPUR
22.	STATE BANK OF HYDERABAD
23.	STATE BANK OF MYSORE
24.	STATE BANK OF PATIALA
25.	STATE BANK OF TRAVANCORE
26.	IDBI Bank Ltd

REPORT

OF

THE JOINT COMMITTEE ON BUSINESS PROCESS FOR GST

ON

GST RETURN

Empowered Committee of State Finance Ministers

New Delhi

October, 2015

Table of Contents

1.	Introduction	4
2.	Periodicity of Return Filing	6
3.	Monthly Return	9
3.1.	Components of valid GST Return for Outward Supplies made by the Taxpayer (GSTR-1)	9
3.2.	Components of valid GST Return for Inward Supplies received by the Taxpayer (GSTR-2)	13
3.3	Components of valid GST Return (GSTR-3)	15
3.4	Quarterly Return for compounding Taxpayer (GSTR-4)	19
3.5	Non-resident foreign taxpayers (GSTR-5)	19
3.6	Components of a valid ISD Return (GSTR-6)	20
3.7	Components of a valid TDS Return (GSTR-7)	21
3.8	Steps for Return Filing	21
3.9	Acknowledgement	23
3.10	Contents of Invoice level information	24
3.11	Where will the taxpayer file Return?	30
3.12	Revision of Return	33
3.13	Non-filing, late-filing and short filing of return	34
4.	Return of Casual/Non-Resident Taxpayers	35
5.	Annual Return (GSTR-8)	36
6.	Processing of Return	37
7.	Annexures	
	I: List of participants in the meeting held on 09 th October, 2015	39
	II: Form GSTR-1	41
	III: Form GSTR-2	45

IV: Form GSTR-3	49
V: Form GSTR-4	58
VI: Form GSTR-5	61
VII: Form GSTR-6	63
VIII: Form GSTR-7	65
IX: Form GSTR-8	66

1. Introduction

1.1 During the Empowered Committee meeting held on 10th March, 2014, it was decided that a Joint Committee under the co-convenership of the Additional Secretary (Revenue), Government of India and the Member Secretary, Empowered Committee should be constituted to look into the Report of the Sub-Group-I on Business Processes for GST and make suitable recommendations for Registration and Return to the Empowered Committee. It was also decided that the Joint Committee should also keep in view the Registration and Return requirements necessary for IGST Model. Accordingly, a Joint Committee, in consultation with the Government of India, was constituted on 7th April, 2014.

1.2 The Committee held its deliberations on 28th October, 2014, 12th November, 2014, 25th November, 2014, 22nd December, 2014, 2nd and 3rd February, 2015, 19th and 20th February, 2015, 16th and 17th April 2015, 7th and 8th July, 2015, 22nd and 23rd July, 2015 and 9th October, 2015. The list of the participants of the last meeting of the Committee held on 9th October, 2015 is appended. (Annexure-I)

1.3 A return is a statement of specified particulars relating to business activity undertaken by the taxable person during a prescribed period. A taxable person has a legal obligation:

- (i) To declare his tax liability for a given period in the return;
- (ii) Furnish details about the taxes paid in accordance with that return; and
- (iii) File correct and complete return within stipulated time frame.

1.4 GST is a self-assessed destination based taxation system. The submission and processing of return is an important link between the taxpayer and tax administration as it is an important tool for:

- (i) Compliance verification program of tax administration;
- (ii) Providing necessary inputs for taking policy decision;
- (iii) Management of audit and anti-evasion programs of tax administration;
- (iv) Finalization of the tax liabilities of the taxpayer within stipulated period of limitation.

1.5 This document lists out the salient aspects of the process related to filing of GST returns.

1.6 There will be common e-return for CGST, SGST, IGST and Additional Tax.

Who needs to file Return in GST regime?

1.7 Every registered person is required to file a return for the prescribed tax period. A return needs to be filed even if there is no business activity (i.e. Nil Return) during the said tax period of return.

1.8 UN agencies etc. will have unique GST ID and will file return for the month (in simpler form) during which they make purchases. They would not be required to file regular return. They would submit their purchase statements (without purchase invoices) as per the periodicity prescribed for claim of refund.

1.9 Government entities / PSUs , etc. not dealing in GST supplies or persons exclusively dealing in exempted / Nil rated / non –GST goods or services would neither be required to obtain registration nor required to file returns under the GST law. However, State tax authorities may assign Departmental ID to such government departments/ PSUs / other persons. They will ask the suppliers to quote the Department ID in the supply invoices for all inter-State purchases being made to them. Such supplies will be at par with B2C supplies and will be governed by relevant provisions relating to B2C supplies.

2. Periodicity of Return Filing

2.1 Common periodicity of returns for a class of taxpayers would be enforced. There will be different frequency for filing of returns for different class of taxpayers, after payment of due tax, either prior to or at the time of filing return. The return can be filed without payment of self-assessed tax as per the return but such return would be treated as an invalid return and would not be taken into consideration for matching of invoices and for inter-governmental fund settlement among States and the Centre. The periodicity of return for different categories of taxpayers is as follows:

S. No.	Return / Ledger	For	To be filed by
1	GSTR 1	Outward supplies made by taxpayer (other than compounding taxpayer and ISD)	10 th of the next month
2	GSTR 2	Inward supplies received by a taxpayer (other than a compounding taxpayer and	15 th of the next month

		ISD)	
3	GSTR 3	Monthly return (other than compounding taxpayer and ISD)	20 th of the next month
4	GSTR 4	Quarterly return for compounding Taxpayer	18 th of the month next to quarter
5	GSTR 5	Periodic return by Non-Resident Foreign Taxpayer	Last day of registration
6	GSTR 6	Return for Input Service Distributor (ISD)	15 th of the next month
7	GSTR 7	Return for Tax Deducted at Source	10 th of the next month
8	GSTR 8	Annual Return	By 31 st December of next FY
9	ITC Ledger of taxpayer		Continuous
10	Cash Ledger of taxpayer		Continuous
11	Tax ledger of taxpayer		Continuous

2.2 Other important points relating to periodicity of return filing are as under:-

- (i) Normal / Regular taxpayers (including casual taxpayers) would have to file GSTR-1 (details of outward supplies) (Annexure-II), GSTR-2 (details of inward supplies) (Annexure-III) and GSTR-3 (monthly Return) (Annexure-IV) for each registration.
- (ii) Normal / Regular taxpayers with multiple registrations (for business verticals) within a State would have to file GSTR-1, GSTR-2 and GSTR-3 for each of the registrations separately.
- (iii) Compounding taxpayers would have to file a quarterly return called GSTR-4 (Annexure-V).
- (iv) Taxpayers otherwise eligible for the compounding scheme can opt against the compounding and file monthly returns and thereby make their supplies eligible for ITC in hands of the purchasers.
- (v) Casual/ Non - Resident Taxpayers (other than foreigners) would have to file GSTR-1, GSTR-2 and GSTR-3 returns for the period for which they have obtained registration. The registration of Casual/Non -Resident taxpayers will be done in the same manner as that of Normal / Regular taxpayers.

- (vi) Non- Resident Taxpayers (foreigners) would be required to file GSTR-5 return for the period for which they have obtained registration within a period of seven days after the date of expiry of registration. In case registration period is for more than one month, monthly return(s) would be filed and thereafter return for remaining period would be filed within a period of seven days as stated earlier. For these taxpayers the registration format to be used will be the same as that for UN Bodies/Embassies (Annexure-VI).
- (vii) Annual return (GSTR-8) (Annexure-IX) will be filed by all normal / regular taxpayers. It will be based on financial records.
- (viii) Compounding taxpayer will also file a simple annual return.
- (ix) Cut-off date for filing of details of outward supplies (GSTR-1), inward supplies (GSTR-2) and Monthly return (GSTR-3) would be 10th, 15th and 20th day respectively of the succeeding month for all Monthly filers.
- (x) Cut-off date for filing of Quarterly return (GSTR-4) by compounding taxpayer would be 18th day of the first month of the succeeding quarter.
- (xi) Cut-off date for filing of Input Service Distributor return (GSTR-6) (Annexure-VII) would be 15th day of the succeeding month.
- (xii) Cut-off date for filing of TDS (Tax Deducted at Source) return (GSTR-7) (Annexure-VIII) by Tax Deductor would be 10th day of the succeeding month.
- (xiii) For Annual return, the cut-off date would be 31st December following the end of the financial year for which it is filed.
- (xiv) The filing of return would be only through online mode although the facility of offline generation and preparation of returns would be provided. The returns prepared in offline mode would have to be uploaded.

3. Monthly Return: There would be separate returns for the outward supplies, inward supplies and a consolidated return based on these two returns. Besides that, there would be separate returns for the Input Service Distributors, non-resident taxpayers (foreigners) and Tax Deductors. The components of each of these return is being discussed hereunder:

3.1. Components of valid GST Return for Outward Supplies made by the Taxpayer (GSTR-1):

3.1.1 This return form would capture the following information:

1. Basic details of the Taxpayer i.e. Name along with GSTIN
2. Period to which the Return pertains
3. Gross Turnover of the Taxpayer in the previous Financial Year. This information would be submitted by the taxpayers only in the first year and will be auto-populated in subsequent years.
4. Final invoice-level supply information pertaining to the tax period separately for goods and services:
 - (i) For all B2B supplies (whether inter-state or intra-state), invoice level specified details will be uploaded.
 - (ii) For all inter-state B2C supplies (including to non-registered Government entities, Consumer / person dealing in exempted / NIL rated / non GST goods or services), the suppliers will upload invoice level details in respect of every invoice whose value is more than Rs. 2,50,000/-. For invoices below this value, State-wise summary of supply statement will be filed covering those invoices where there is

address on record. The address of the buyer has to be mandatorily reflected in every invoice having a value of Rs. 50,000/- or more. **(Model GST Law may provide for such a provision)**. Invoices for a value less than Rs. 50,000/- that do not have address on record will be treated as intra-state supply. In other words, State-wise summary of inter-State supply would be filed covering (a) those invoices value of which is less than Rs. 50000/- and where address is on record and (b) those invoices whose value is between Rs. 50000/- to Rs. 250000/-.

(iii) The recommendation of the Committee on IGST and GST on Imports with respect to the details about HSN code for goods and Accounting code for services to be captured in an invoice have been accepted with certain modifications. The details proposed by this Committee are as follows:-

- a) HSN code (4-digit) for Goods and Accounting Codes for Services will be mandatory initially for all taxpayers with turnover in the preceding financial year above **Rs. 5 Crore** (For the first year of operations of GST, self-declaration of turnover of previous financial year will be taken as the basis as all India turnover data will not be available in the first year. From the 2nd year onwards, turnover of previous financial year under GST will be used for satisfying this condition).
- b) For taxpayers with turnover between Rs 1.5 Crores and Rs 5 Crores in the preceding financial year, HSN codes may be specified only at

2-digit chapter level as an optional exercise to start with. From second year of GST operations, mentioning 2-digit chapter level HSN Code will be mandatory for all taxpayers with turnover in previous financial year between Rs. 1.5 Crores and Rs. 5.0 Crores.

- c) Any taxpayer, irrespective of his turnover, may use HSN code at 6-digit or 8-digit level if he so desires.
 - d) To start with, compounding dealers may not be required to specify HSN at 2-digit level also.
 - e) Prescribed Accounting code will be mandatory for those services for which Place of Supply Rules are dependent on nature of services to apply the destination principle, irrespective of turnover.
 - f) HSN Codes at 8-digit level and Accounting Codes for services will be mandatory in case of exports and imports.
- (iv) The above parameters with respect to HSN code for goods and Accounting Code for services will apply for submitting the information in return relating to relevant invoice level information for B2B supplies (both intra-state and inter-state) and inter-state B2C supplies (where taxable value per invoice is more than Rs. 2.5 lakhs). It is proposed that in the return form the description of goods and services may not be required to be submitted by the taxpayer as the same will be identified through the submission of HSN code for goods and Accounting Code for services. In order to differentiate between the HSN code and the Service Accounting Code (SAC), the latter will be prefixed with “s”. The taxpayers who have turnover below the limit of Rs. 1.5 Crore will have

to mention the description of goods/service, as the case may be, wherever applicable.

- (v) For all Intra-State B2C supplies (including to non-registered Government entities, consumer / person dealing in exempted / NIL rated / non GST goods or services), consolidated sales (supply) details will be uploaded. However a dealer may at his option furnish invoice wise information in respect of exempted and nil rated supplies also.
 - (vi) The supply information will also have details relating to the Place of Supply in order to identify the destination state as per the Place of Supply Rules where it is different from the location of the recipient.
 - (vii) Details relating to supplies attracting Reverse charge will also be submitted
5. Details relating to advance received against a supply to be made in future will be submitted in accordance with the Point of Taxation Rules as framed in the GST law.
 6. Details relating to taxes already paid on advance receipts for which invoices are issued in the current tax period will be submitted.
 7. Details relating to supplies exported (including deemed exports) both on payment of IGST as well as without payment of IGST would be submitted.
 8. There will be a separate table for submitting the details of revisions in relation to the outward supply invoices pertaining to previous tax periods. This will include the details of Credit/Debit Note issued by the suppliers and the differential value impact and the concomitant tax payable or refund/tax credit sought.

9. There will be a separate table for effecting modifications/correcting errors in the returns submitted earlier. The time period for correcting these errors will be provided in the GST Law.

10. There will be a separate table for submitting details in relation to NIL rated, Exempted and Non GST outward supplies to (both inter-state and intra-state) to registered taxpayers and consumers.

3.1.2 The return (GSTR-1) would be filed by the 10th of the succeeding month. Late filing would be permitted on payment of late fees only.

3.2. Components of valid GST Return for Inward Supplies received by the Taxpayer (GSTR-2):

3.2.1 This return form would capture the following information:

1. Basic details of the Taxpayer i.e. Name along with GSTIN
2. Period to which the Return pertains
3. Final invoice-level inward supply information pertaining to the tax period for goods and services separately
4. The information submitted in GSTR-1 by the Counterparty Supplier of the taxpayer will be auto populated in the concerned tables of GSTR-2. The same may be modified i.e. added or deleted by the Taxpayer while filing the GSTR-2. The recipient would be permitted to add invoices (not uploaded by the counterparty supplier) if he is in possession of invoices and have received the goods or services.

5. There will be separate tables for submitting details relating to import of Goods/Capital Goods from outside India and for the services received from outside India.
6. The details of inward supplies would be auto-populated in the ITC ledger of the taxpayer on submission of his return. The taxpayer will select the invoice details regarding the in-eligibility and eligibility of ITC in relation to these inward supplies and the quantum available in a particular tax period.
7. There will be a separate table for submitting details in relation to ITC received on an invoice on which partial credit has been availed earlier.
8. In respect of capital goods, there will be a field to capture appropriate information regarding availment of ITC over a period **(to be prescribed in GST Law in terms of duration and number of installments)** from the date of accountal of capital goods in the taxpayer's books of accounts. **[GST Law may provide that Input credit pertaining to Capital Goods will be allowed to be availed over a period of 2 years in two equal installments]**
9. In respect of inputs, there can be two situations. If inputs are received in one lot, the ITC will be given in the return period in which the purchase is recorded in the books of accounts. In case inputs covered under one invoice are received in more than one instance/lot, the ITC will be given in the return period in which the last purchase is recorded in the books of accounts. **(GST Law to contain appropriate provision in this regard)**. A note in this regard has been incorporated in the Return form for the guidance of the taxpayer.

10. There will be a separate table for submitting the details of revisions in relation to inward supply invoices pertaining to previous tax periods (including post purchase discounts received). This will include the details of Credit/Debit Note issued by the suppliers and the differential value impact and concomitant tax payable or refund/tax credit sought.
11. There will be a separate table for effecting modifications/correcting errors in the returns submitted earlier. The time period for correcting these errors will be provided in the GST Law.
12. There will be a separate table for submitting details in relation to NIL rated, Exempted and Non GST inward Supplies (Both Inter-State and Intra-State) including those received from compounding taxpayers and unregistered dealers.
13. There will be a separate table for the ISD credit received by the taxpayer.
14. There would be a separate table for TDS Credit received by the taxpayer.

3.2.2 Auto Population in this return from GSTR-1 will be done on or after 11th of the succeeding month. Addition or Deletion of the invoice by the taxpayer will be permitted between 12th and 15th of the succeeding month. Adjustments would be permitted on 16th and 17th of the succeeding month.

3.2.3 The return (GSTR-2) would be filed by 17th of the succeeding month. Late filing would be permitted on payment of late fees only.

3.3. Components of valid GST Return (GSTR-3).

3.3.1 The GST Monthly Return form would capture the following information.

1. Basic details of the Taxpayer i.e. Name and Address along with GSTIN
2. Period to which the Return pertains
3. Turnover Details including Gross Turnover, Export Turnover, Exempted Domestic Turnover, Nil Rated Domestic Turnover, Non GST Turnover and Net Taxable Turnover
4. Final aggregate level outward and inward supply information. These details will be auto populated from GSTR-1 and GSTR-2.
5. There will be separate tables for calculating tax amounts on outward and inward supplies based on the information contained in various tables in the GSTR-3 return.
6. There will be a separate table for capturing the TDS credit received and which has been credited to his cash ledger (the deductee).
7. Tax liability under CGST, SGST, IGST and Additional Tax.
8. Details regarding revision of invoices relating to outward and inward supplies (as per details in para 3.1.1 and 3.2.2 above)
9. Details of other liabilities (i.e. Interest, Penalty, Fee, others etc.).
10. Information about ITC ledger, Cash ledger and Liability ledger (these are running electronic ledgers maintained on the dashboard of taxpayer by GSTN). These would be updated in real time on an activity in connection with these ledgers by the taxpayer. Both the ITC ledger and the cash ledger will be utilized by the taxpayer for discharging the tax liabilities of the returns and

others. Details in these ledgers will get auto populated from previous tax period return (irrespective of mode of filing return i.e. online / offline utility)

11.Details of ITC utilized against tax liability of CGST, SGST and IGST on supplies of goods and services.

12.Net tax payable under CGST, SGST, IGST and Additional Tax.

13.Details of the payment of tax under various tax heads of CGST, SGST, IGST and Additional Tax separately would be populated from the debit entry in Credit/Cash ledger. **GST Law may have provision for maintaining four head wise account for CGST, SGST, IGST and Additional tax and at associated minor heads for interest, penalty, fee and others.** Excess payment, if any, will be carried forward to the next return period. The taxpayer will have the option of claiming refund of excess payment through the return for which appropriate field will be provided in the return form. The return form would display all bank account numbers mentioned in the registration, out of which one will be selected by the taxpayer to which the refund will be credited.

14.Details of other payments – Interest/Penalties/Fee/Others, etc. This will be auto populated from the Debit entry in Cash ledger irrespective of mode of filing i.e. online / offline utility.

15.Details of ITC balance (CGST, SGST and IGST) **at the end of the tax period will be auto-populated in the ITC ledger irrespective of mode of filing return. In case of net exporter or taxpayers dealing with inverted duty structure or similar other cases, where input tax credit is greater than output tax due on supply, the taxpayer would be eligible for refund. The return would have a**

field to enable the tax payer to claim the refund or to carry forward the ITC balance (CGST, SGST and IGST). The return form should display all bank account numbers mentioned in the registration, out of which one will be selected by the taxpayer to which the refund will be credited. **To begin with GST law may provide that the refund will be processed quarterly.**

16.Details of cash balance (CGST, SGST, IGST and Additional tax) in personal ledger at the end of the tax period (this will be auto populated irrespective of mode of filing return).

17.Information regarding quantity of goods (as per Unique Quantity Code) supplied will not be contained in the monthly return. However, the same would be submitted by the taxpayer in the annual return. **(GST Law may contain appropriate provision in this regard)**. The format of the annual return would have a suitable field for this purpose.

3.3.2 The return (GSTR-3) would be entirely auto- populated through GSTR-1 (of counterparty suppliers), own GSTR-2, ISD return (GSTR-6) (of Input Service Distributor), TDS return (GSTR-7) (of counterparty deductor), own ITC Ledger, own cash ledger, own Tax Liability ledger. However, the taxpayer may fill the missing details to begin with.

3.3.3 The return would be permitted to be filed both on online and offline mode. In case of offline mode, payment by debit to cash / ITC ledger can be done at an earlier date also and such debit entry number would be verified at the time of uploading of the return. In online mode, both debiting and filing can be done simultaneously.

3.3.4 The return would be filed by 20th of the succeeding month. Late filing would be permitted on payment of late fees only.

3.4 Quarterly Return for compounding Taxpayers (GSTR-4):

3.4.1 After crossing the threshold exemption limit, the taxpayers may opt for compounding scheme wherein they would be required to pay taxes at fixed rate without any ITC facilities. Such taxpayers would be required to file a simplified quarterly return (GSTR-4) as per the format prescribed. In this return the taxpayer is only required to indicate the total value of supply made during the period of return and the tax paid at the compounding rate along with the details of payment of tax in the return. The compounding taxpayer will also need to declare invoice-level purchase information (auto-drafted from supply invoice information uploaded by counter-party taxpayers) for the purchases from normal taxpayers. The Compounding taxpayer will also be required to submit details of the goods and services imported from outside India. The Compounding taxpayers would be allowed to export supplies outside India. **GST Law may provide for suitable provisions with respect to the eligibility of such taxpayers to purchase only tax paid supplies and that they can make purchases from unregistered suppliers on payment of GST on reverse charge basis.**

3.5 Non-Resident Foreign Taxpayers (GSTR-5):

3.5.1 Non-Resident foreign taxpayers would be required to file GSTR-5 for the period for which they have obtained registration within a period of seven days after the date of expiry of registration. In case registration period is for more than one month, monthly return(s) would be filed and thereafter return for remaining period would be filed within a period of seven days as stated earlier.

3.6 Components of a valid ISD Return (GSTR-6):

3.6.1 This return form would capture the following information:

1. Basic details of the Taxpayer i.e. Name along with GSTIN
2. Period to which the Return pertains
3. Final invoice-level inward supply information pertaining to the tax period separately for goods and services on which the ITC is being claimed. This will be auto populated on the basis of GSTR-1 filed by the Counterparty Supplier of the taxpayer. The same may be modified i.e. added or deleted by the Taxpayer while filing the ISD return. The recipient would be permitted to add invoices (not uploaded by the counterparty supplier) if he is in possession of invoices and have received the services.
4. Details of the Invoices along with the GSTIN of the receiver of the credit i.e. to whom the ISD is distributing credit.
5. There will be separate ISD Ledger in the return that will detail the Opening Balance of ITC (to be auto- populated on the basis of previous return), credit for ITC services received, debit for ITC reversal and ITC distributed and Closing Balance.

3.6.2 This return would be filed by 15th of the succeeding month. Late filing would be permitted on payment of late fees only.

3.7 Components of a valid TDS Return (GSTR-7):

3.7.1 This return would capture the following information:

1. Basic details of the Taxpayer i.e. Name along with GSTIN

2. Period to which the Return pertains
3. Details of GSTIN of the Supplier along with the invoices against which the Tax has been deducted. This will also contain the details of tax deducted against each major head i.e. CGST, SGST and IGST.
4. Details of other payments - Interest/Penalties/Fee/Others, etc. (This will be auto populated from the Debit entry in Cash ledger)

3.7.2 This return would be filed by 10th of the succeeding month. Late filing would be permitted on payment of late fees only.

3.8 Steps for Return Filing.

Step 1. The taxpayer will upload the final GSTR-1 return form either directly through data entry at the GST Common Portal or by uploading the file containing the said GSTR-1 return form through Apps by 10th day of month succeeding the month during which supplies has been made. The increase / decrease (in supply invoices) would be allowed, only on the basis of the details uploaded by the counter-party purchaser in GSTR-2, upto 17th day of the month. (i.e. within a period of 7 days). In other words, the supplier would not be allowed to include any missing invoices on his own after 10th day of the month.

GSTN will facilitate periodic (may be daily, weekly etc.) upload of such information to minimize last minute load on the system. GSTN will facilitate offline preparation of GSTR-1.

Step2: GST Common Portal (GSTN) will auto-draft the provisional GSTR-2 of taxpayer based on the supply invoice details reported by the counter-party taxpayer (supplier) on a near real-time basis.

Step3: Purchasing taxpayer will accept / reject/ modify such auto-drafted provisional GSTR-2. (A taxpayer will have the option to download his provisional purchase statement from the Portal or through Apps using Application Programming Interface (APIs) and update / modify it off-line).

Step4: Purchasing taxpayer will also be able to add additional purchase invoice details in his GSTR-2 which have not been uploaded by counter-party taxpayer (supplier) as described in *Step 1 and 2* above, provided he is in possession of valid invoice issued by counter-party taxpayer and he has actually received such supplies.

Step5: Taxpayers will have the option to do reconciliation of inward supplies with counter-party taxpayers (suppliers) during the next 7 days by following up with their counter-party taxpayers for any missing supply invoices in the GSTR-1 of the counter-party taxpayers, and prompt them to accept the same as uploaded by the purchasing taxpayer. All the invoices would be auto-populated in the ITC ledger of taxpayer. The taxpayer would, however, indicate the eligibility / partial eligibility for ITC in those cases where either he is not entitled or he is entitled for partial ITC.

Step 6: Taxpayers will finalize their GSTR-1 and GSTR-2 by using online facility at Common Portal or using GSTN compliant off-line facility in their accounting applications, determine the liability on their supplies, determine the amount of eligible ITC on their purchases and then generate the net tax liability from the system for each type of tax. Cash details as per personal ledger/ carried forward from previous tax period, ITC carried forward from previous tax period, ITC reversal and associated

Interest/Penalty, taxes paid during the current tax period etc. would get auto-populated in the GSTR-3.

Step 7: Taxpayers will pay the amount as shown in the draft GSTR-3 return generated automatically at the Portal post finalization of activities mentioned in Step 6 above.

Step8: Taxpayer will debit the ITC ledger and cash ledger and mention the debit entry No. in the GSTR-3 return and would submit the same.

3.9 Acknowledgement.

3.9.1 On submission of return, an Acknowledgement Number will be generated. In case of submission of a return which has been prepared by using offline tools, acknowledgement of submission will take some time as GSTN System will need to first verify details like the carry forward cash as per personal ledger, ITC, tax payment details etc. In such cases, initially a Transaction ID confirming receipt of data will be conveyed to the taxpayer, (as also envisaged in case of filing of short paid / non –paid return). Final acknowledgement of receipt of return will be generated after validation of data is completed, which will also lock-in the Transaction ID.

3.9.2 The acknowledgement of e-return would contain the following details:

- (i) Return acknowledgement number (unique number generated by the GSTN), Date and Time
- (ii) Transaction ID No., Date and Time
- (iii) GSTIN of taxpayer
- (iv) Relevant tax period details

- (v) Gross Supplies, Taxable Supplies and Tax paid / refund claimed (CGST, SGST, IGST and Additional tax separately) during the Return period

3.10 Contents of Invoice level information.

3.10.1. The following invoice level information would be captured in the return.

1. Invoices pertaining to B2B transactions (Intra-State, Inter-State and supplies to UN organizations/embassies) [both for supply and purchase transactions].

- (i) Goods and Services Tax Identification Number (GSTIN)/Unique ID issued to UN organizations/Embassies
- (ii) Invoice Number, Date and value
- (iii) HSN code for each item line (for Goods)/ Accounting code for each item line (for services)
- (iv) Taxable Value
- (v) Tax Rate (CGST & SGST or IGST and/ or Additional Tax)
- (vi) Tax Amounts (CGST & SGST or IGST and / or Additional Tax)
- (vii) Place of Supply (State)
- (viii) For Capital Goods, there will be separate column in the Table of the return for ease of tracking of credit due and availed over the period as prescribed by GST law
- (ix) An Invoice may have two items having different tax rates or different HSN codes in case of B2B supplies. If the invoice contains more than one tax rate/one HSN Code, the taxpayer would have to submit line-wise information separately for each HSN Code / each tax rate

2. Invoices pertaining to B2C transactions (Inter-State B2C supplies for consumer on record)[only supply transactions].

A. In respect of invoices whose taxable value is more than Rs. 2.5 lakhs (to enable transfer of funds to respective states):

- (i) Invoice Number, Date and value
- (ii) HSN Code for goods / Accounting code for services
- (iii) Taxable Value
- (iv) Tax Rate (IGST and Additional Tax)
- (v) Tax Amount (IGST and Additional Tax)
- (vi) Buyer's address (State Code)
- (vii) Departmental ID allotted by State Government to Government entities / PSUs , etc. not dealing in GST supplies or to persons dealing in exempted / Nil rated / non –GST goods or services
- (viii) Place of Supply (**State**) if different than S. No. (vi) above

B. For invoices whose taxable value is upto Rs 2.5 lakhs, only aggregated taxable value of all such invoices will be submitted, state-wise and tax rate-wise.

(GST Law may provide for mandatory mention of address of the buyer in every invoice whose taxable value is more than Rs. 50000/-)

3. *Invoices pertaining to B2C transactions (Intra-State B2C supplies)* [only supply transactions]:

For intra-state B2C supplies, aggregated taxable value of all such invoices will be submitted tax rate-wise.

4. *Invoice pertaining to Export and deemed export supply* [only supply transactions]:

- (i) Invoice Number, Date and value

- (ii) 8-digit HSN Code for goods/ Accounting Code of Services for each line item (as HSN Code / Accounting code is mandatory in case of exports)
- (iii) Taxable Value
- (iv) Tax Rate
- (v) Tax Amounts (IGST, CGST & SGST) (in case exports on payment of GST).
- (vi) Shipping Bill/ Bill of Export Number

5. Invoices pertaining to exempted including Nil rated supply [both for supply and purchase transaction]:

Aggregate value of all exempted (including Nil rated) supplies made by the taxpayer during the return period would be submitted. The aggregate value of exempted (including Nil rated) purchases would also be declared by the taxpayer in the return.

6. Bills of Entry relating to Import [only purchase transactions]:

- (i) Bill of Entry Number, Date and value
- (ii) Assessable Value for IGST
- (iii) 8-digit HSN Code for goods
- (iv) IGST rate
- (v) IGST Amount
- (vi) Importer's address (for transfer of IGST) [Will get auto populated in case of registered taxpayer. In case of others, it will have to be provided by them]

These details would be verified from Bill of Entry data available at ICES / ICEGATE.

7. Credit Note / Debit Note [for Sales-Purchase return, Post-sale discount]:

For sale–purchase return, on account of differential value/quantity/tax rates:

- (i) Debit / Credit Note Number
- (ii) Original Invoice Number and Date
- (iii) Taxable Value, Tax Rate and Tax Amount (CGST & SGST or IGST and Additional Tax) (that is being modified)

The credit/debit note will be reflected in the monthly return in which such notes have been issued.

GST Law may provide the time period within which sales return can be made and the date (invoice date or date of receipt by the buyer) from which such time period is to be calculated.

8. *Post sales discount.*

GST Law may provide what constitutes a sale price especially with respect to post sales discount. The Law may also contain suitable provisions about admissibility or otherwise of post supply discounts. The adjustments for post sales discount will be completed before filing of annual return. The credit/debit note will be reflected in the monthly return in which the said adjustment is made.

9. *Advances received against a supply to be made in future.*

GST law may provide for Point of Taxation Rules which will determine the point at which the taxes would be paid by the taxable person. So, accordingly,

if the tax is to be paid on the basis of advance payment received against a future supply of goods and/or services, then the following details would be required to be provided:

- (i) GSTIN/UID/GDI/Name of customer
- (ii) State Code
- (iii) HSN Code for goods / Accounting code for services
- (iv) Amount of advance received
- (v) Tax Rate (CGST and SGST or IGST and Additional Tax)
- (vi) Tax Amount (CGST and SGST or IGST and Additional Tax)

10. TDS

GST law may provide for provision of TDS (Tax Deducted at source) for certain supplies of goods and/or services made to specified categories of purchasers who will be obligated to deduct tax at a certain percentage from the payment due to the suppliers. They will be required to file a TDS return and submit the following details:

- (i) GSTIN/GDI of deductor
- (ii) GSTIN of deductee/supplier
- (iii) Invoice no. with date (iv) TDS Certificate no. with date and value
- (v) Taxable value

(v) Rate of TDS for IGST, CGST and SGST as applicable

(vi) Amount of IGST, CGST and SGST as applicable, deducted as TDS

11. ISD:

GST law may retain the concept of Input Service Distributor (ISD). Accordingly, ISDs would be required to file a monthly return and submit the following details:

(i) Details of ISD i.e. GSTIN, name and address

(ii) Details of recipient i.e. GSTIN, name and address

(iii) Details of the inward supply invoices on the basis of which Input Tax Credit is claimed.

(iv) Invoice / Document no. with date

(v) Amount of IGST, CGST, SGST Credit, as applicable, being distributed.

3.10.2 GST Law may provide the suitable provisions for the mandatory fields and data structure which must be contained in a GST invoice.

3.11 Where will the taxpayer file Return?

3.11.1 A registered Tax Payer shall file GST Return at GST Common Portal either:

- (i) by himself logging on to the GST Common Portal using his own user ID and password;

- (ii) Through his authorized representative using the user Id and password (allotted to the authorized representative by the tax authorities), as chosen at the time of registration, logging on to the GST Common Portal.

The filing may be done either directly or by using Applications developed by accounting companies / IT companies which will interact with GST System using APIs or through Facilitation Center (FC).

3.11.2 At the time of registration, every taxpayer has to enroll with GST Common Portal (GSTN). A unique User-ID and Password will be generated and intimated to the taxpayer. This User-ID and Password shall be used by him for filing the tax return on the Common Portal as well. However, a taxable person may prepare and submit his returns himself or can use services of a TRP. The process for filing return through TRP is given below:

- (i) A TRP will have to be chosen by the taxpayer out of TRPs registered with respective State tax authorities/CBEC. (taxpayer will have the option to change TRP any time);
- (ii) The TRPs registered with tax authorities will be provided separate user ID and password;
- (iii) Using his own user Id and password, the TRP will prepare the return in prescribed format on the basis of the information furnished to him by the taxable person. (The legal responsibility of the correctness of information contained in the return prepared by the TRP will rest with

the taxable person only and the TRP shall not be liable for any errors or incorrect information.);

- (iv) The TRP will be able to upload all types of return, based on the information provided by the taxpayer who has authorized him to do so at the portal;
- (v) The system will generate an email and SMS having basic data of return and send the same to the taxpayer;
- (vi) The taxpayer can accept the correctness of the return and submit the same by just clicking on the link provided in the e-mail. In case he does not respond to the e-mail, return will be considered as not submitted;
- (vii) In case taxpayer wants to respond to the SMS, he may do so by replying YES and mention the OTP sent alongwith the SMS. In case he does not respond to the SMS, return will be considered as not submitted;
- (viii) **This mechanism may be provided in the GST law and the TRPs would have to be approved by the tax administration and allotted a Unique ID and will also be provided appropriate training by them.**

3.11.3 The return can also be submitted by the taxpayer through any Facilitation Center (FC) approved by the Tax authorities and selected by the taxpayer at GST System. The taxpayer shall make available the requisite documents to the facilitation center. Facilitation Centre (FC) shall be responsible for the uploading of all types of return given to it by the taxable person. After uploading the data on the common

portal using the ID and Password of FC, the GSTN system will generate an email/SMS for the taxpayer. The process explained in Para 3.11.2 above will be followed. With e-sign being worked out by Department of Electronics and Information Technology (DEITY), individual signing of return by one-time Digital Signature Certificate (DSC) can also be completed. This will do away with the requirement of print-out of acknowledgement of return proposed earlier based on the current system of ITR filing.

3.11.4 Registration of TRP/FC will be done by CBEC / respective State tax authorities and the registration data will be shared with GSTN to enable applicants/taxpayers to choose one from the available list of registered TRPs/FCs. The GST Law may also contain suitable provisions about it.

3.11.5 The common portal will display the electronic form to be used for filing the return. The form can be downloaded, filled and then uploaded using approved e-tools.

3.11.6 The portal will provide a form generation utility which can be downloaded by the taxpayer for preparation of the return offline and for conducting the preliminary arithmetic checks before return is uploaded on the portal using APIs.

3.11.7 Along with the return, taxpayer is not required to submit any other document. The documents as required for scrutiny or audit shall be made available by the taxpayer to the audit party deputed by the CBEC /State tax authorities/CAG.

3.11.8 The Common Portal will maintain and display the ledger of the Tax Payer providing information about the tax deposited, input tax credit availed/taken, input

tax credit utilized, tax liability created, balance ITC carried forward, tax payments made by debiting the ledgers under respective major tax heads, refund granted and balance in respective cash ledger and credit ledger carried forward [Separate ledger will be maintained for ITC and Cash for each Taxpayer]. The information of Interest on delayed payments, Penalty for legal defaults, Tax Demand as per adjudication/appellate orders, etc. would also be provided. The ledger will also give the status of the tax dues or excess payment on any given date. Thus such ledger would have eight pages and cash ledger would have 20 pages.

3.11.9 A return related liability should mean the tax liability for the transactions (including credit/debit notes) of the return period and the additional liability arising out of any ITC reversal or late inclusion of the supply in the return period. Arrears pertaining to audit/reassessment/enforcement outcomes would be handled separately, and not mixed with the return related liabilities and payments. The payments made on this account, however, would be reflected in the return.

3.12 Revision of Return

3.12.1 There would be no revision of returns.

3.12.2 All unreported invoices of previous tax period would be reflected in the return for the month in which they are proposed to be included. The interest, if applicable will be auto populated.

3.12.3 All under-reported invoice and ITC revision will have to be corrected using credit/debit note and such credit / debit note would be reflected in the return for the month in which such adjustment is carried out. The credit/debit note will have

provision to record original invoice, date etc. to enable the system to link the same with the original invoice as also to calculate the interest, if applicable. **Its format will be like the invoice.**

3.12.4 There would be separate tables in the returns for reflecting those adjustments for which credit / debit notes are not required to be issued / issued. The interest, if applicable will be auto populated.

3.13 Non-filing, late-filing and short-filing of return

A. Non-Filers & Late-Filers

In case of failure by the taxpayer to submit periodic returns, a defaulter list will be generated by the IT system by comparing the return filers with the registrant database. Such defaulter list will be provided to the respective GST Authorities for necessary enforcement and follow up action.

GST Common Portal can auto generate and send the notice to all non-filers (being done by many State VAT authorities) in the form of email and SMS. Jurisdictional tax authorities can get the same printed and dispatch such notices. The details of non-filers shall be made available on the dash board of jurisdictional officers. **GST Law may also provide for imposition of automatic late fees for non-filers and late filers which can also be in-built in the notices.**

B. Short-Filers

As per the requirement of the IGST model, Return should be allowed to be filed only on payment of due tax as self-assessed and declared in the return. It has,

however, been decided that e-Return should be allowed to be uploaded even in case of short payment for the limited purpose of having the information about self-assessed tax liability even though not paid. The invoice matching and inter-governmental fund settlement would, however, take place only after the full tax has been paid. Return without full payment of tax will be allowed to be uploaded but it will be treated as an invalid return and this return will not be used for matching of invoices and settlement of funds.

Any invalid return (including the one not supported by full payment) will merely be recorded with unique transaction ID, but not accepted in the system, and that aspect will be made known to the taxpayer at the time of communicating the ID itself.

[GST Law may provide adequate penal provisions for short-filing and non-filing of return]

4 Return for Casual/Non-Resident Taxpayers:

Casual/Non-Resident Taxpayers should file GSTR-1, GSTR-2 and GSTR-3 for the period for which they have obtained registration within a period of seven days after the date of expiry of registration. In case registration period is for more than one month, monthly return(s) would be filed and thereafter return for remaining period would be filed within a period of seven days as stated earlier.

5 Annual Return (GSTR-8):

5.1 All the Normal taxpayers would be required to submit Annual Return. This return to be filed annually is intended to provide 360 degree view about the activities of the taxpayer. This statement would provide a reconciliation of the returns with the audited financial statements of the taxpayer.

5.2 This return is a detailed return and captures the details of all the income and expenditure of the taxpayer and regroups them in accordance with the monthly returns filed by the taxpayer. This return also provides for the reconciliation of the monthly tax payments and will provide the opportunity to make good for any short reporting of activities undertaken supply wise. The said return would also capture the details of pending arrears against the taxpayer and the current status of the orders leading to such arrears. The details of all the refund claims pending with the tax authorities would also be captured. Since this return captures the minutest details of income and expenditure of the taxpayer, the gross profit/loss arrived on the basis of the details submitted in this statement should tally with the gross profit/loss indicated in the Profit and Loss Account of the dealer. Accordingly, this return is to be submitted along with the audited copies of the Annual Accounts of the dealer and would be filed by 31st December following the end of the financial year for which it is filed.

5.3 A separate reconciliation statement, duly certified by a Chartered Accountant, will have to be filed by those taxpayers who are required to get

their accounts audited under section 44AB of Income Tax Act 1961. Currently this limit is Rs 1 Crore.

5.4 Consolidated statement of purchases and supplies based on monthly returns filed by the taxpayer can be made available to taxpayers by GSTN common portal as a facilitation measure for enabling him to prepare annual return.

5.5 The format of Reconciliation statement would be finalized after finalization of GST Model law.

6 Processing of Return.

After the GST Return has been uploaded onto the GST Common Portal, the Portal will undertake the following activities:

- (i) Acknowledge the receipt of the return filed by the taxpayer after conducting required validations.
- (ii) Acknowledgement number would be issued as per procedure detailed in Para 3. 9 above.
- (iii) Once a return is acknowledged, forward that GST Return to tax authorities of Central and appropriate State Govt. through the established IT interface.
- (iv) The ITC claim will be confirmed to purchasing taxpayer in case of matched invoices after 20th of the month succeeding the month of the tax period

month provided counterparty supplying taxpayer has submitted the valid return (and paid self-assessed tax as per return).

- (v) Communicate to the taxpayers through SMS/e-Mail, about the macro-results of the matching. The details will be in the taxpayers' dashboard/ledger which can be viewed after log-in at the Portal.
- (vi) Auto-populate the ITC reversals due to mismatching of invoices in the taxpayer's account in the return for the 2nd month after filing of return for a particular month.
- (vii) Aggregation of cross-credit utilization of IGST and SGST for each State and generation of settlement instructions based on IGST model and as finalized by the Payments Committee. This has to be with dealer-wise details as the concerned tax administration's follow on activities will be dependent on that detailing.

(Satish Chandra)
Member Secretary
Empowered Committee
of State Finance Ministers

(Rashmi Verma)
Special Secretary
Department of Revenue
Government of India

LIST OF PARTICIPANTS OF THE MEETING HELD ON 9TH OCTOBER, 2015

Government of India

1. Smt. Rashmi Verma, Special Secretary (Revenue), Government of India
2. Shri Udai Singh Kumawat, Joint Secretary (Revenue), Government of India
3. Shri Manish Saxena, Additional Director, Directorate General of Systems, Government of India
4. Shri Shashank Priya, ADG, DG (GST), CBEC, Government of India
5. Shri Upender Gupta, Commissioner, GST, CBEC, Government of India
6. Shri G.D. Lohani, Commissioner, CBEC, Government of India
7. Shri Rajeev Yadav, Director (Service Tax), CBEC, Government of India
8. Shri Ravneet Singh Khurana, Deputy Commissioner, CBEC, Government of India
9. Shri Vishal Pratap Singh, Deputy Commissioner (GST), CBEC, Government of India
10. Smt. Aarti Saxena, Deputy Secretary (State Taxes), Government of India
11. Shri Tshering Y. Bhutia, Assistant Secretary, Department of Revenue, Government of India

States

1. Shri Gautam Das Gupta, Deputy Commissioner of Taxes, Assam
2. Shri T. Ramesh Babu, Additional Commissioner, Commercial Tax, Andhra Pradesh
3. Shri Ajay Kumar Chourasia, Joint Commissioner, Commercial Tax, Bihar
4. Shri Vijay Kumar, Commissioner (VAT), Trade and Taxes, Delhi
5. Shri Jagmal Singh, Deputy Director, Trade and Taxes, Delhi
6. Shri Dipak M. Bandekar, Commissioner, Commercial Tax, Goa
7. Dr. P.D. Vaghela, Commissioner, Commercial Tax, Gujarat
8. Shri Riddhesh Raval, Assistant Commissioner, Commercial Tax, Gujarat
9. Shri Hanuman Singh, Additional Commissioner, Excise & Taxation, Haryana
10. Shri Prediman Bhat, Additional Commissioner, Commercial Tax, Jammu & Kashmir
11. Shri S.K. Prasad, Deputy Commissioner, Commercial Tax, Jharkhand
12. Shri Ritvik Pandey, Commissioner, Commercial Tax, Karnataka
13. Dr. M.P.Ravi Prasad, Joint Commissioner, Commercial Tax, Karnataka
14. Dr. Rajan Khobragade, Commissioner, Commercial Tax, Kerala
15. Shri Sudip Gupta, Deputy Commissioner, Commercial Tax, Madhya Pradesh
16. Shri Niten Chandra, Commissioner, Commercial Tax, Odisha

17. Shri Dipankar Sahu, Deputy Commissioner(IT&P), Commercial Tax, Odisha
18. Shri K. Sridhar, Deputy Commissioner, Commercial Tax, Puducherry
19. Shri Pawag Garg, Additional Commissioner, Excise & Taxation, Punjab
20. Shri Dinesh Chandra Rakhecha, Assistant Commissioner, Commercial Tax, Rajasthan
21. Shri K. Rajaraman, Principal Secretary/Commissioner, Commercial Taxes, Tamil Nadu
22. Shri D. Soundraraja Pandian, Joint Commissioner (Taxation), Commercial Taxes, Tamil Nadu
23. Shri K. Chandrasekhar Reddy, Additional Commissioner, Commercial Tax, Telangana
24. Shri Rakesh Verma, Joint Commissioner, Commercial Tax, Uttar Pradesh
25. Shri Vivek Kumar, Additional Commissioner, Commercial Tax, Uttar Pradesh
26. Shri N.C. Sharma, Additional Commissioner, Commercial Tax, Uttarakhand
27. Shri Khalid Aizaz Anwar, Joint Commissioner, Commercial Tax, West Bengal

Goods and Services Tax Network (GSTN)

1. Shri Navin Kumar, Chairman, Goods and Services Tax Network
2. Shri Prakash Kumar, Chief Executive Officer, Goods and Services Tax Network
3. Shri S.B. Singh, SVP (Services), Goods and Services Tax Network
4. Shri K.P. Verma, VP (Services), Goods and Services Tax Network
5. Ms. Kalyaneshwari B. Patil, AVP (Services), Goods and Services Tax Network
6. Shri J. Rasal Dass Soloman, AVP (Services), Goods and Services Tax Network

Empowered Committee of State Finance Ministers

1. Shri Satish Chandra, Member Secretary, Empowered Committee
2. Shri Bashir Ahmed, Adviser, Empowered Committee
3. Shri V.P. Gupta, Senior Administrative Officer, Empowered Committee

ANNEXURE-II**GSTR-1****OUTWARD SUPPLIES MADE BY THE TAXPAYER**[To be furnished by the 10th of the month]

[Not to be furnished by compounding taxpayer/ISD]

1. **GSTIN:**
2. **Name of the taxpayer:**
(S. No. 1 and 2 will be auto-populated on logging)
3. **Gross Turnover of the taxpayer in the previous FY.....**
(To be submitted only in first year. To be auto populated in subsequent year)
4. **Period:** **Month.....** **Year**

5. Taxable outward supplies to a registered person

(figures in Rs)

GSTIN/ UIN	Invoice					IGST		CGST		SGST		Addl Tax [#]		POS (only if different from the location of recipient)	Indicate if supply attracts reverse charge \$
	No.	Date	Value	HSN/ SAC*	Taxable value	Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt		
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)

* As per Para 3.1 (4) (iii) of the return report

Not applicable to services and intra-state & specified inter-state supplies of goods

\$ To be filled only if a supply attracts reverse charge

Notes:

1. SAC to be different from HSN (may be prefix 'S')
2. Taxpayer has the option to furnish the details of nil rate and exempted supplies in this Table
3. In case of inter-state supplies, only IGST & Additional Tax (if applicable) would be filled
4. In case of intra-state supplies, CGST & SGST would be filled.

6. Taxable outward supplies to a consumer where place of supply is other than the State where supplier is located (Inter-state supplies) and Invoice value is more than Rs 2.5 lakh (optional in respect of other supplies)

(figures in Rs)

Recipient's State code	Name of the recipient/ GDI	Invoice					IGST		Addl Tax [#]		POS (only if different from the location of recipient)
		No.	Date	Value	HSN/ SAC*	Taxable value	Rate	Amt	Rate	Amt	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)

* As per Para 3.1 (4) (iii) of the return report

Not applicable to services and intra-state & specified inter-state supplies of goods

Notes:

1. SAC to be different from HSN (may be prefix 'S')
2. Taxpayer has the option to furnish the details of nil rate and exempted supplies in this Table

7. Taxable outward supplies to consumer (Other than 6 above)

(figures in Rs)

HSN/ SAC*	State code (Place of supply)	Aggregate Taxable Value	IGST		CGST		SGST		Addl Tax [#]	
			Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)

* As per Para 3.1 (4) (iii) of the return report

Not applicable to services and intra-state & specified inter-state supplies of goods

Notes:

1. SAC to be different from HSN (may be prefix 'S')
2. Taxpayer has the option to furnish the details of nil rate and exempted supplies in this Table

8. Details of Credit/Debit Notes

(figures in Rs)

Debit Note/credit note		Original Invoice		Differential 1 Value (Plus or Minus)	Differential Tax								
No.	Date	No.	Date			IGST		CGST		SGST		Addl Tax#	
						Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	

Debit Note

Credit Note

Not applicable to services and intra-state & specified inter-state supplies of goods

Note: Information about Credit Note / Debit Note to be submitted only if issued as a supplier.

9. Amendments to details of Outward Supplies of earlier tax periods (including post supply discounts)

(figures in Rs)

Original Invoice		GSTIN/ UIN	Revised Invoice				IGST		CGST		SGST		Addl Tax#		POS (only if different from the location of recipient)
No.	Date		No.	Date	HSN/ SAC	Taxable Value	Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt	
(1)	(2)	(3)	(4)	(5)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)

Not applicable to services and intra-state & specified inter-state supplies of goods

10. Nil rated, Exempted and Non GST outward supplies*

(figures in Rs)

	Nil Rated (Amount)	Exempted (Amount)	Non GST supplies (Amount)
(1)	(2)	(3)	(4)
Interstate supplies to registered person			
Intrastate supplies to registered person			
Interstate supplies to consumer			
Intrastate supplies to consumer			

- If the details of “nil” rated and “exempt” supplies have been provided in Table 5,6 and 7, then info in column (3) may only be furnished.

11. Supplies Exported (including deemed exports)

(figures in Rs)

	Invoice					Shipping bill/ bill of export		IGST		CGST		SGST	
	No.	Date	Value	HSN/ SAC*	Taxable value	No	Date	Rate	Amt	Rate	Amt	Rate	Amt
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
Without payment of GST													
With payment of GST													

* As per Para 3.1 (4) (iii) of the return report

12. Tax liability of amount received in advance against a supply to be made in future

(figures in Rs)

GSTIN/UI D/GDI/ Name of customer	State Code	HSN/SAC* of supply to be made	Amount of advance received without raising a bill	TAX							
				IGST		CGST		SGST		Addl Tax#	
				Rate	Tax	Rate	Tax	Rate	Tax	Rate	Tax
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)

* As per Para 3.1 (4) (iii) of the return report

Not applicable to services and intra-state & specified inter-state supplies of goods

Note: A transaction id would be generated by system for each transaction on which tax is paid in advance

13. Tax already paid (on advance receipt) on invoices issued in the current period

(figures in Rs)

Invoice No.	Transaction id (A number assigned by the system when tax was paid)	TAX Paid on receipt of advance							
		IGST		CGST		SGST		Addl Tax#	
		Rate	Tax	Rate	Tax	Rate	Tax	Rate	Tax
(1)	(2)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)

Not applicable to services and intra-state & specified inter-state supplies of goods

Note: Tax liability in respect of invoices issued in this period shall be net of tax already paid on advance receipt.

Usual Declaration

(Signatures of Authorized Person)

INSTRUCTIONS for furnishing the information

1. Terms used:

GSTIN: Goods and Services Taxpayer Identification Number

UID: Unique Identity Number for embassies

HSN: Harmonized System of Nomenclature for goods

SAC: Service Accounting Code

GDI: Government department unique ID where department does not have GSTIN

POS: Place of supply of goods or services – State Code to be mentioned

GSTR-2[To be furnished by the 15th of the month]

[Not to be furnished by compounding taxpayer /ISD]

Note:

1. Auto-population would be done, on the basis of GSTR1 of counter-party supplier, on or after 11th of succeeding month.
2. Addition of invoices / debit note / credit note, not submitted by counter-party supplier, would be permitted between 12th to 15th of succeeding month.
3. Adjustments would be permitted on 16th and 17th of succeeding month.
4. Further the other details that are not auto-populated, i.e. import of services, eligibility of ITC and quantum thereof and purchases from unregistered taxpayer shall be furnished.

INWARD SUPPLIES/PURCHASES RECEIVED

1. GSTIN.....

2. Name of taxpayer.....

(S. No. 1 and 2 will be auto-populated on logging)

3. Period : Month..... Year

4. From Registered taxpayers

GSTIN of supplier	Invoice					IGST		CGST		SGST		Addl. Tax#		Eligibility of ITC (select from drop down)	Total Tax available as ITC	ITC available this month
	No.	Date	Value	HSN/SAC*	Taxable value	Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt			
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
Other than supplies attracting reverse charge																
Auto populated	Shall be auto populated from counterparty GSTR1													Input		
														Capital goods		
														None		
Not auto populated (Claimed)														Same as above		
Supplies attracting reverse charge																
Auto populated														Same as above		
Others																

* As per Para 3.1 (4) (iii) of the return report

Not applicable to services and intra-state & specified inter-state supplies of goods

Note. If the supply is received in more than one lot, the invoice information should be reported in the return period in which the last lot is received and recorded in the books of accounts.

5. Goods /Capital goods received from Overseas (Import of goods)

(figures in Rs)

Bill of entry					IGST		Eligibility for ITC (select from drop down)	Total IGST available as ITC	ITC available this month
No.	Date	Value	HSN/SAC*	Taxable value	Rate	Amt			
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
							Input		
							Capital Goods		
							None		

* As per Para 3.1 (4) (iii) of the return report

6. Services received from a supplier located outside India (Import of services)

(figures in Rs)

Invoice					IGST		ITC Admissibility	
No	Date	Value	SAC	Taxable value	Rate	Amt	Total ITC admissible	ITC admissible this month
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)

7. Details of Credit/Debit Notes

(figures in Rs)

Debit Note/ credit note		Original Invoice		Differenti al Value (Plus or Minus)	Differential Tax								Eligibili ty for ITC (select from drop down as in Table 5 above)	Total IGST availab le as ITC	ITC availab le this month
No.	Date	No.	Date		IGST		CGST		SGST		Addl Tax#				
					Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt			
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)

Debit Note Received

Credit Note Received

		Column No.	1	to	13	shall be auto populated from							

Not applicable to services and intra-state & specified inter-state supplies of goods

8. Amendments to details of inward supplies received in earlier tax periods (including post purchase discounts received)

(figures in Rs)																	
Original Invoice		GSTIN/ UIN	Revised Invoice				IGST		CGST		SGST		Addl Tax #		Eligibility for ITC (select from drop down as in Table 5 above)	Total IGST available as ITC	ITC available this month
No.	Date		No.	Date	HSN/ SAC	Taxable Value	Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt			
(1)	(2)		(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)			
				Shall be auto populated from counterparty GSTR1													

Not applicable to services and intra-state & specified inter-state supplies of goods

9. Supplies received from compounding /unregistered dealer & other exempt/nil/non GST supplies

(figures in Rs)						
	HSN Code/ SAC code	Value of supplies received from				
		Compounding Dealer	Unregistered dealer	Any exempt supply not included in Table 4 above	Any nil rated supply not included in Table 4 above	Non GST Supply
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Interstate supplies						
Intrastate supplies						

10. ISD credit received

(figures in Rs)					
GSTIN_ISD	Invoice/Document details		ISD Credit		
	No	Date	IGST	CGST	SGST
(1)	(2)	(3)	(4)	(5)	(6)
	Shall be auto populated from counterparty ID5 return				

11. TDS Credit received

(figures in Rs)

GSTIN/ GDI/of TDS deductor	TDS Certificate		TDS					
			IGST		CGST		SGST	
	No	Date	Rate	Tax	Rate	Tax	Rate	Tax
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(3)
	Shall be auto populated from counterparty TDS return							

12. ITC Received on an invoice on which partial credit availed earlier

(figures in Rs)

Original invoice/ doc.		ITC availed					
		IGST		CGST		SGST	
No	Date	Earlier	This month	Earlier	This month	Earlier	This month
(2)	(3)	(4)	(5)	(6)	(7)	(8)	(3)
	ITC taken earlier shall be auto populated upon choosing the invoice number						

Usual declaration

Signature of Authorized Person

GSTR-3

GST RETURN

[To be furnished by the 20th of the month]

[Other than compounding taxpayer / ISD]

TAXPAYER DETAILS

1. GSTIN
2. Name of Taxpayer.....

- ### 3. Address

[illegible]

[S. Nos. 1, 2 and 3 shall be auto populated on logging]

4. Period Month..... Year.....

5. TURNOVER DETAILS

(figures in Rs)

A.	Gross Turnover	
B.	Export Turnover	
C.	Exempted Domestic Turnover	
D.	Nil rated Domestic Turnover	
E.	Non GST Turnover	
F.	Net Taxable Turnover	

6.Outward Supplies

6.1 Inter-state supplies to Registered taxpayers

(Auto populated from GSTR-1)

(figures in Rs)

State Code	Rate of Tax (Rate wise-Including Nil, exempt and Non GST)	Value	IGST	Additional Tax
(1)	(2)	(3)	(4)	(5)
Goods				
Services				

Note: To be auto-populated from Table 5 plus Table 8 plus Table 10 of GSTR-1

6.2 Intra-State Supplies to Registered taxpayers

(Auto populated from GSTR-1)

(figures in Rs)

Rate of Tax (Rate wise-Including Nil, exempt and Non GST)	Value	CGST	SGST
(1)	(2)	(3)	(4)
Goods			
Services			

Note: To be auto-populated from Table 5 plus Table 8 plus Table 10 of GSTR-1

6.3 Inter-State Supplies to Consumers

(Auto populated from GSTR-1)

(including unregistered Government Departments / persons dealing in exempted / NIL rated/ non GST goods or services)

(figures in Rs)

State Code	Rate of Tax (Rate wise-Including Nil, exempt and Non GST)	Value	IGST	Additional Tax
(1)	(2)	(3)	(4)	(5)
Goods				
Services				

Note: To be auto-populated from Table 6 plus Table 7 plus Table 8 plus Table 10 of GSTR-1

6.4 Intra-State Supplies to Consumers

(Auto populated from GSTR-1)

(figures in Rs)

Rate of Tax (Rate wise-Including Nil, exempt and Non GST)	Value	CGST	SGST
(1)	(2)	(3)	(4)
Goods			
Services			

Note: To be auto-populated from Table 7 plus Table 8 plus Table 10 of GSTR-1

6.5 Exports (including deemed exports)

(Auto populated from GSTR-1)

(figures in Rs)

Description	Taxable Value	IGST	CGST	SGST
(1)	(2)	(3)	(4)	(5)
Goods				
Without payment of GST				

With Payment of GST				
Services				
Without payment of GST				
With Payment of GST				

Note: To be auto-populated from Table 11 of GSTR-1

6.6 Revision of supply invoices pertaining to previous tax period (including post sales discounts or any clerical/other errors)

[Auto populated from GSTR1]

(figures in Rs)

Invoice No	Invoice Date	Differential Value (Plus or Minus)	IGST	CGST	SGST	Additional Tax
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Goods						
Services						

Note: To be auto-populated from Table 9 of GSTR-1

6.7 Total tax liability on outward supplies

(Auto Populated from the Tables above)

(figures in Rs)

Value	IGST	CGST	SGST	Additional Tax
(1)	(2)	(3)	(4)	(5)
Goods				
Services				

Note: To be auto-populated from Tables 6.1 to 6.6 above of this Return

7. Inward supplies

7.1 Inter-State supplies received

(Auto-populated from GSTR2)

(figures in Rs)

State Code	Rate of Tax (Rate wise-Including Nil, exempt and non-GST)	Value	IGST	ITC of IGST available in the current month	Addl Tax
(1)	(2)	(3)	(4)	(5)	(6)

Goods_Inputs					
Capital goods					
Services					

Note: To be auto-populated from Table 4 plus Table 7 plus Table 9 of GSTR-2

7.2 Intra-State supplies received

(Auto populated from GSTR -2)

(figures in Rs)

Rate of Tax (Rate wise-Including Nil, exempt, compounding dealer and non-GST)	Value	CGST	SGST	ITC-CGST available in current month	ITC-SGST available in current month
(1)	(2)	(3)	(4)	(5)	(6)
Goods_Inputs					
Capital Goods					
Services					

Note: To be auto-populated from Table 4 plus Table 7 plus Table 9 of GSTR-2

7.3 Imports

(Auto populated from GSTR -2)

(figures in Rs)

	Assessable Value	IGST	ITC- IGST available in current month
(1)	(2)	(3)	(4)
Goods_inputs			
Capital goods			
Services			

Note: To be auto-populated from Table 5 plus Table 6 of GSTR-2

7.4 Revision of purchase invoices pertaining to previous tax period (including post sales discounts received or any clerical / other errors)

(Auto populated from GSTR-2)

(figures in Rs)

Differential Value (+/-)	CGST	SGST	IGST	Additional Tax
(1)	(2)	(3)	(4)	(5)
Goods_Inputs				

Capital goods				
Services				

Note: To be auto-populated from Table 8 of GSTR-2

7.5 Total Tax liability on inward supplies on reverse charge

(figures in Rs)

Value	CGST	SGST	IGST	Additional Tax
(1)	(2)	(3)	(4)	(5)
Goods				
Services				

Note: To be auto-populated from Table 6 of GSTR-2

8 Total Tax liability for the month (Table 6.7 plus Table 7.5 of this Return)

(figures in Rs)

Value	CGST	SGST	IGST	Additional Tax
(1)	(2)	(3)	(4)	(5)
Goods				
Services				

9. TDS credit received during the month (Auto-populated from GSTR-2)

(figures in Rs)

GSTIN/ GDI/of TDS deductor	TDS Certificate		IGST		CGST		SGST	
	No	Date	Rate	Tax	Rate	Tax	Rate	Tax
(1)	(3)		(4)	(5)	(6)	(7)	(8)	(9)

Note: To be auto-populated from Table 11 of GSTR-2

10. ITC received during the month (auto populated from ITC Ledger)

(figures in Rs)

IGST		CGST		SGST	
Rate	Tax	Rate	Tax	Rate	Tax
(2)	(3)	(4)	(5)	(6)	(7)

11. Tax, fine and penalty paid (auto-populated from cash and ITC ledger)

(figures in Rs)

S. No.	Description	IGST	CGST	SGST	Addl Tax
(1)	(2)	(3)	(4)	(5)	(6)
1.	ITC Reversal paid (On account of adjustment)				
2.	ITC Reversal paid (On account of mismatch)				
3.	Interest				
4.	Tax for previous Tax periods				
5.	Tax for Current Tax period				
6.	Late fee				
7.	Penalty				
	Debit Nos. in Ledger				
1.	In Cash Ledger				
2.	In ITC ledger				

12. Refunds claim of excess ITC in specified cases and excess tax paid earlier

(1)	CGST	SGST	IGST
(2)	(3)	(4)	
Refund of ITC accumulation claimed in specified cases			
Refund of excess amount of tax paid earlier			
Refund from cash ledger			
Bank Account Number*			

*This should be one of the bank accounts mentioned in the GSTIN

Usual declaration

Signatures of Authorized Person

TAX Liability Ledger (Auto populated in real time)

(figures in Rs)

	CGST	SGST	IGST	Addl Tax	Total
(1)	(2)	(3)	(4)	(5)	(6)
Opening Tax Liability					
Tax liability arising out of return					
Tax liability on account of mismatch of					
Other tax liability					
TDS Liability					
Penalty					
Fees					
Interest					
Less : Tax paid (cash plus ITC)					
Closing balance					

The heads for tax, TDS and other liability shall be shown as drop down items for facilitation

CASH LEDGER (updated on real time)

(figures in Rs)

	CGST	SGST	IGST	Addl Tax	Total
(1)	(2)	(3)	(4)	(5)	(6)
Opening Balance					
Amount deposited [Auto populated from CIN]					
CIN					
CIN					
Amount of TDS Credit [Auto populated from TDS Return of counterparty deductor]					
Amount utilized for payment of tax					
Outstanding liability from earlier period					
For this tax period					
Any other liability paid (indicate reference from Tax liability register)					
Amount utilised for payment of interest/penalty and other amount paid					
Interest paid on delay in payment of tax					
Fees paid for late filing of return					
Others penalties paid					
Other amount paid (selection)					
Refund from cash ledger					
Closing balance					

ITC LEDGER (updated on real time)

(figures in Rs)

	CGST	SGST	IGST	Total
(1)	(2)	(3)	(4)	(5)
Opening Balance				
ITC availed (including revision in invoices) [first 4 will be auto-populated]				
Inputs				
Capital goods				
Services-received directly				
Services credit received from ISD				
Mismatched credit claimed				
Disputed credit claimed				
Credit claimed by a taxpayer on becoming regular taxpayer				
Any other ITC claimed (Please specify)				
Credit utilized				
ITC Reversal (On account of adjustment)				
ITC Reversal (On account of mismatch)				
ITC Revision for any reason				
ITC Disallowed				
Interest Liability related to Returns of previous Tax period				
Tax Liability of earlier Tax periods				
Tax payment for the month [selection]				
ITC_ refund under process/refund allowed				
Other tax liability paid				
Closing Balance				

GSTR-4**Quarterly Return for Compounding Dealer**(To be furnished by 18th of the month succeeding the quarter)

1. GSTIN

2. Name of the Taxpayer.....

3. Address

(S. No. 1, 2 and 3 shall be auto-populated on logging)

4. Period of Return From..... To.....

5. Inward supplies including supplies received from unregistered traders

(figures in Rs)

GSTIN of supplier	Invoice					IGST		CGST		SGST		Addl Tax	
	No	Date	Value	HSN/ SAC*	Taxable Value	Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)
Other than supplies attracting reverse charge													
Auto populated													
	Shall be auto populated from counterparty GSTR1												
Not auto populated (claimed)													
Supplies attracting reverse charge (including supplies received from unregistered dealer)													
Auto populated													
	Shall be auto populated from own GSTR1												
Others													

* As per Para 3.1 (4) (iii) of the return report

6. Goods /Capital goods received from Overseas (Import of goods)

(figures in Rs)

Bill of entry					IGST	
No.	Date	Value	HSN/ SAC*	Taxable value	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)

*at 8-digit level

7. Services received from a supplier located outside India (Import of services)

(figures in Rs)

Invoice					IGST	
No	Date	Value	SAC*	Assessable Value	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)

* As per Para 3.1 (4) (iii) of the return report

8. Outward Supplies made

(figures in Rs)

S.No.	Nature of supplies	Amount
(1)	(2)	(3)
1	Intra-state supplies	
2	Non GST Supplies	
3	Exports	

9. Tax Payable

(figures in Rs)

	IGST#	CGST#	SGST#	Compounding Tax
(1)	(2)	(3)	(4)	(5)
Tax payable as per return				
Interest payable for delayed payment of Tax				
Fees for late filing of return				
Others				
Total				

Tax paid in respect of supplies attracting reverse charge and those received from unregistered traders

10. Details of Tax Payment

(figures in Rs)

Cash Ledger Debit Entry No.	Date	IGST	CGST	SGST	Compounding Tax
(1)	(2)	(3)	(4)	(5)	(6)

11. Are you likely to cross composition limit before the date of next return. Y/N

Declaration.

(Signatures of Authorized Person)

GSTR-5

RETURN FOR NON RESIDENT TAXPAYERS (FOREIGNERS)

(To be furnished on monthly basis by 20th of the month & within 7 days after expiry of registration)

1. GSTIN
2. Name of the Taxpayer.....
3. Address

[illegible]

(S. No. 1, 2 and 3 shall be auto-populated on logging)

4. Period of Return From..... To.....

5. **Goods imported:**

(figures in Rs.)

[illegible]

* at 8-digit level

6. Outward supplies made:

(figures in Rs.)

S. No.	GSTIN, if any	Invoice					IGST		CGST		SGST	
		No.	Date	Value	HSN •	Taxable value	Rate	Amt	Rate	Amt	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)

* As per Para 3.1 (4) (iii) of the return report

7. ITC availed on inputs and input services

(figures in Rs.)

S. No.	GSTIN of supplier	Invoice					IGST		CGST		SGST	
		No.	Date	Value	HSN/SAC*	Taxable value	Rate	Amt	Rate	Amt	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)

* As per Para 3.1 (4) (iii) of the return report

8. Tax paid

(figures in Rs.)

Description	Tax payable (Table 6)	ITC utilized	Tax paid in cash (after adjusting ITC)
(1)	(2)	(3)	(4)
IGST			
CGST			
SGST			
Total			

9. Closing stock of Goods

S. No.	Description of goods	HSN*	UQC	Quantity	Value (Rs.)
(1)	(2)	(3)	(4)	(5)	(6)

* As per Para 3.1 (4) (iii) of the return report

Usual Declaration

Signature

ANNEXURE-VII

GSTR-6

RETURN FOR INPUT SERVICE DISTRIBUTOR

(To be furnished by 15th of the month)

(To be furnished by Input Service Distributor)

1. GSTIN:

2. Name of the Registered person:

(S.No. 1 and 2 will be auto-populated on logging)

3. Period: Month Year.....

4. From Registered taxpayers (to be auto-populated from counter party GSTR-1)
(figures in Rs)

GSTIN of supplier	Invoice					IGST		CGST		SGST		Total Tax available as ITC for distribution	ITC available this month for distribution
	No	Date	Value	SAC	Taxable Value	Rate	Amt	Rate	Amt	Rate	Amt		
(1)	(2)	(3)	(4)			(7)	(8)	(11)	(12)	(13)	(14)	(16)	(17)
Other than supplies attracting reverse charge													
Auto populated													
Claimed													
Supplies attracting reverse charge													

5. Input Service Distribution

(figures in Rs)

GSTIN of receiver of credit	Invoice/Document No.				
	No.	Date	ISD Credit distributed		
			CGST	SGST	IGST
(1)	(2)	(3)	(4)	(5)	(6)

6. ISD Ledger

(figures in Rs)

	CGST	SGST	IGST	Total
(1)	(2)	(3)	(4)	(5)
Opening Balance				
ITCs received*				
ITC Reversal				
ITC Distributed				
Closing balance				

* To be auto-populated from table No. 4 above

Usual Declaration.

(Signatures of Authorized Person)

ANNEXURE-VIII

GSTR-7

TDS Return

(To be furnished by 10th of the month)

(To be furnished by person liable to deduct TDS)

1. **GSTIN/GST TDS IN:**

2. **Name of dedutor :**

(S.No. 1 and 2 will be auto-populated on logging)

3. **Return period:** Month..... Year.....

4. TDS details

(figures in Rs.)

GSTIN of supplier	Invoice			CIN No. vide which TDS paid	TDS_IGST		TDS_CGST		TDS_SGST		TDS_All Taxes	
	No	Date	Value		Rate	Amt	Rate	Amt	Rate	Amt	Rate	Amt
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)

5 Other amount paid

(figures in Rs)

	CGST A/c	SGST A/c	IGST A/c	CIN No
(1)	(2)	(3)	(4)	
Interest on delayed payment of TDS				
Fees for late filing of return				
Others (pl specify)				
Total				

Declaration:

(Signatures of Authorized Person)

GSTR-8**ANNUAL RETURN**[To be furnished by the 31st December of the next Financial Year]

1. **GSTIN**
2. **Name of the Taxpayer**
- (S. No. 1 and 2 will be auto-populated on logging)
3. **Date of statutory Audit**
4. **Auditors**
5. **Details of expenditure:**

- (a) Total value of purchases on which ITC availed (inter-State)

Goods

Sl. No.	Description	HSN Code	UQC	Quantity	Tax Rate	Taxable Value	IGST Credit	Additional Tax paid

Services

Sl. No.	Description	Accounting Code	Tax Rate	Taxable Value	IGST Credit

- b) Total value of purchases on which ITC availed (intra-State)

Goods

Sl.No	Description	HSN Code	UQC	Quantity	Taxable Value	Tax Rate		Tax Credit	
						CGST	SGST	CGST	SGST

Services

Sl.No	Description	SAC	Taxable Value	Tax Rate		Tax Credit	
				CGST	SGST	CGST	SGST

C) Total value of purchases on which ITC availed (Imports)

Goods

Sl.No.	Description	HSN Code	UQC	Quantity	Tax Rate	CIF Value	IGST	Custom Duty paid

Services

Sl.No.	Description	SAC	Tax Rate	Taxable Value	IGST

(d) Other Purchases on which no ITC availed

Sl.No.	Goods/Services	Purchase Value

(e) Sales Returns

Sl.No	Goods	HSN Code	Taxable Value	CGST	SGST	IGST	Additional Tax

(f) Other Expenditure (Expenditure other than purchases)

Sl. No.	Specify Head	Amount

6. Details of Income.

(a) Total value of supplies on which GST paid (inter-State Supplies)

Goods

Sl. No.	Description	HSN Code	Tax Rate	Taxable Value	IGST	Additional Tax

Services

Sl. No.	Description	Accounting Code	Tax Rate	Taxable Value	IGST

(b) Total value of supplies on which GST Paid (intra-State Supplies)

Goods

Sl.No	Description	HSN Code	Taxable Value	Tax Rate		Tax	
				CGST	SGST	CGST	SGST

Services

Sl.No	Description	SAC	Taxable Value	Tax Rate		Tax	
				CGST	SGST	CGST	SGST

(c) Total value of supplies on which GST Paid (Exports)

Goods

Sl.No	Goods	HSN Code	Tax Rate	FOB Value	IGST	Custom Duty

Services

Sl.No	Services	SAC	Tax Rate	FOB Value	IGST

(d) Total value of supplies on which no GST Paid (Exports)

Goods

Sl.No	Goods	HSN Code	Tax Rate	FOB Value

Services

Sl.No	Services	SA	Tax Rate	FOB Value

(e) Value of Other Supplies on which no GST paid

Sl. No.	Goods/Services	Value

(f) Purchase Returns

Goods

Sl. No	Goods	HSN Code	Taxable Value	CGST	SGST	IGST	Additional Tax

Services

Sl. No	Services	SAC	Taxable Value	CGST	SGST	IGST

(g) Other Income (Income other than from supplies)

Sl. No.	Specify Head	Amount

7 Return reconciliation Statement

A CGST

Sl. No	Month	Tax Paid	Tax Payable (As per audited a/c)**	Difference	Interest	Penalty
	Total					

B SGST

Sl. No	Month	Tax Paid	Tax Payable (As per audited a/c)**	Difference	Interest	Penalty
	Total					

C IGST

Sl. No.	Month	Tax Paid	Tax Payable (As per audited a/c)**	Difference	Interest	Penalty
	Total					

D Additional Tax

Sl. No.	Month	Tax Paid	Tax Payable (As per audited a/c)**	Difference	Interest	Penalty
	Total					

**

1. Presently the statutory auditor is not required to calculate the tax payable on account of CE and ST.
2. Further there is bound to be difference in supply value when compared with the Taxable value determined in accordance with the Valuation Rules (this may be on account of certain permissible deductions from the supply value or on account of certain additions which may be required to be made to arrive at the taxable value).
3. A reconciliation format (reconciling the supply value with the taxable value), therefore, is required to be prescribed. Such a format can be prepared only after the GST law particularly the valuation Rules are finalized.

8. Other Amounts@@

A Arrears (Audit/Assessment etc.)

Sl. No.	Details of Order	Tax Payable	Interest	Penalty	Current Status of the Order
	Total				

B Refunds

Sl. No.	Details of Claim	Date of Filing	Amount of Refund	Current Status of the claim

This may be divided into parts:-

- i) amount already paid / refund already received during the year,
- ii) amount payable / refund pending.

9. Profit as Per the Profit and Loss Statement

Gross Profit

Profit after Tax

Net Profit



**PARLIAMENT OF INDIA
RAJYA SABHA**

REPORT OF THE SELECT COMMITTEE

ON

**THE CONSTITUTION
(ONE HUNDRED & TWENTY-SECOND AMENDMENT) BILL, 2014**

PRESENTED TO THE RAJYA SABHA ON 22nd July, 2015



**Rajya Sabha Secretariat, New Delhi
22nd July, 2015/Ashadha, 1937 (Saka)**



**PARLIAMENT OF INDIA
RAJYA SABHA**

REPORT OF THE SELECT COMMITTEE

ON

**THE CONSTITUTION
(ONE HUNDRED & TWENTY-SECOND AMENDMENT) BILL, 2014**

PRESENTED TO THE RAJYA SABHA ON 22nd July, 2015



**Rajya Sabha Secretariat, New Delhi
22nd July, 2015/Ashadha, 1937 (Saka)**

C O N T E N T S

		PAGES
1.	COMPOSITION OF THE COMMITTEE	(i)
2.	PREFACE	(ii)-(iv)
3.	ACRONYMS	(v)
4.	REPORT OF THE SELECT COMMITTEE	
	Chapter-I Introduction	1-10
	Chapter-II Clause by Clause Consideration	11-54
	Chapter-III Other Related Issues in Context of the Bill	55-79
5.	BILL AS REPORTED BY THE SELECT COMMITTEE	80-90
6.	NOTES OF DISSENT	91-110
7.	RECOMMENDATIONS/OBSERVATIONS AT A GLANCE	111-123
8.	ANNEXURE- I	124-125
	ANNEXURE- II	126
9.	* MINUTES OF THE MEETINGS OF THE COMMITTEE	-

*TO BE APPENDED AT THE PRINTING STAGE

COMPOSITION OF THE COMMITTEE
(Constituted on 12/05/2015)

1. Shri Bhupender Yadav – Chairman
2. Dr. Chandan Mitra
3. Shri Ajay Sancheti
4. Shri Madhusudan Mistry
5. Shri Mani Shankar Aiyar
6. Dr. Bhalchandra Mungekar
7. Shri Naresh Agrawal
8. Shri K. C. Tyagi
9. Shri Derek O'Brien
10. Shri A. Navaneethakrishanan
11. Shri Satish Chandra Misra
12. Shri K. N. Balagopal
13. Shri Dilip Kumar Tirkey
14. Shri C. M. Ramesh
15. Shri Praful Patel
16. Shrimati Kanimozhi
17. Shri Anil Desai
18. Shri Naresh Gujral
19. Mir Mohammad Fayaz
20. Shri D. Raja
21. Shri Rajeev Chandrasekhar

SECRETARIAT

1. Shri A. K. Singh, *Joint Secretary*
2. Shri Vimal Kumar, *Director*
3. Shri Sameer Suryapani, *Joint Director*
4. Shri Deepak Kalra, *Assistant Director*

(i)

PREFACE

I, the Chairman of the Select Committee of the Rajya Sabha on The Constitution (One Hundred and Twenty-second Amendment) Bill, 2014, to whom the aforesaid Bill, as passed by Lok Sabha on 6th May, 2015, was referred, having been authorised by the Select Committee to present the report on its behalf, present this Report of the Select Committee along with the Bill, annexed thereto.

2. The Committee heard the Secretaries, Ministry of Finance (Department of Revenue), Ministry of Law & Justice (Legislative Department), Ministry of Urban Development and Ministry of Panchayati Raj on the Bill. Apart from that, the Committee heard the views of Experts/Financial Institutions/ State Governments and other Stakeholders through this Bill.

3. While considering the Bill, the Committee took note of the following documents/papers placed before it:-

- (a) The Constitution (One Hundred & Twenty-Second Amendment), Bill, 2014 as passed by the Lok Sabha on 6th May, 2015;
- (b) Background Note on the Bill furnished by the Ministry of Finance (Department of Revenue);
- (c) Information/Papers on the Bill furnished by the Ministry of Law and Justice (Legislative Department);
- (d) Background note on the Bill furnished by the Ministry of Urban Development;
- (e) Background Note on the Bill furnished by the Ministry of Panchayati Raj;
- (f) Memoranda furnished by the State Governments;
- (g) Memoranda furnished by the Experts/other Stakeholders; and
- (h) Replies to Memoranda no. 1-58 furnished by Ministry of Finance (Department of Revenue)

4. The Committee heard the views of the Ministries of Finance (Department of Revenue) and Law & Justice (Legislative Department) at its sitting held on 22nd May, 2015. The Committee then held its second meeting on 29th May, 2015 and heard the view of the representatives of the Ministries of Urban Development, Panchayati Raj, Finance (Department of Revenue) and Law & Justice (Legislative Department). On 16th June, 2015, the Committee heard the view of Shri K. M. Mani, Finance Minister, Government of Kerala and Chairman, Empowered Committee of State Finance Ministers; Shri Sumit Dutt Majumdar, Consulting Editor, TIOL & Former Chairman, CBEC; Dr. Rathin Roy, Director, National Institute of Public Finance and Policy; Prof. Pinaki Chakraborty, National Institute of Public Finance and Policy; Prof. Abhijit Sen, Former Member, Planning Commission; Shri Sagar Shah, International Liaison Partner, BDO, India LLP; Shri Satya Poddar, Ernst & young LLP; Prof. Arun Kumar, Centre for Economic Studies and Planning, School of Social Sciences, JNU, Delhi and representative of Voluntary Health Association of India (VHAI); National Association of Software and Services Companies (NASSCOM); Manufactures' Association of Information and Technology (MAIT); American Chamber of Commerce in India (ACCI); Cellular Operators Association of India (COAI). In this meeting, the Ministries of Finance (Department of Revenue) and Law and Justice (Legislative Department), also clarified points/issues raised by the Hon'ble Members on the Bill. The Committee held clause by clause consideration of the Bill at its sitting held on 3rd, 10th and 17th July, 2015. Representatives of Ministries of Finance (Department of Revenue) and Law & Justice (Legislative Department) were also present in the meeting.

5. Apart from appropriate modifications in Enacting Formula and Clause I of the Bill, the Committee has also given some recommendations which are of critical importance but were not covered by the Bill. It is important that these recommendations are duly incorporated.

6. The Committee also conducted its study visit to Chennai, Kolkata and Mumbai from 21st to 25th June, 2015, wherein the Committee heard the views of State Government of Tamil Nadu, Puducherry, Kerala, West Bengal, Maharashtra, Gujarat and Goa. The Committee also heard the views of the experts namely Dr. V. Bhaskar, Former Special Chief Secretary, Finance Department, Govt. of Andhra Pradesh; Dr. Partho Shome, Former Chairman, Tax Administration Reforms Commission and Dr. Asim Das Gupta, Former Finance Minister, Government of West Bengal. Apart from this the Committee also heard various stakeholders (list enclosed at **Annexure-I**)

7. The Committee considered and adopted the report in its meeting held on the 20th July, 2015.

8. The Committee wishes to express its thanks to the officials of the Ministries of Finance (Department of Revenue) and Law & Justice (Legislative Department) concerned with the Bill for their cooperation and all the State Governments, Associations, Experts and other stakeholders for their valuable suggestions on the Amendment Bill.

9. The recommendations/observations of the Committee are set out at appropriate places in the report.

New Delhi

22nd July, 2015

..... Ashadha, 1937 (Saka)

BHUPENDER YADAV

Chairman,

Select Committee on The Constitution

(One Hundred & Twenty-Second Amendment) Bill, 2014,

Rajya Sabha

Acronyms

1.	ASSOCHAM	The Associated Chambers of Commerce and Industry of India
2.	CII	The Confederation of Indian Industry (CII)
3.	CST	Central Sales Tax
4.	CGST	Central Goods and Services Tax
5.	CVD	Countervailing Duty
6.	EC	Empowered Committee
7.	FICCI	Federation of Indian Chambers of Commerce and Industry
8.	GST	Goods and Services Tax
9.	GSTN	Goods and Services Tax Network
10.	VAT	Value Added Tax
11.	IGST	Integrated Goods and Services Tax
12.	MCGM	Municipal Corporation of Greater Mumbai (MCGM)
13.	NIPFP	National Institute of Public Finance and Policy
14.	NCAER	National Council of Applied Economic Research
15.	NSDL	National Securities Depository Limited
16.	RNR	Revenue Neutral Rates
17.	SGST	State Goods and Services Tax
18.	SFC	State Finance Commission

REPORT

CHAPTER- I

INTRODUCTION

1.1 The Constitution (One Hundred and Twenty Second Amendment) Bill, 2014 was passed by Lok Sabha on 6th May, 2015. The said Bill on a motion (**Annexure-I**) moved by the Minister of Finance, Corporate Affairs and Information and Broadcasting, was referred to the Select Committee for examination and the Committee was asked to submit its Report by the last day of the first week of the next Session(Monsoon Session).

1.2 The Bill contains 21 clauses on which the Committee has been asked to submit a report and these clauses proposes to, inter alia, amend Constitution of India by inserting new Articles-246 A, 269A and 279 A with respect to special provision to Goods and Services Tax, levy and collection of Goods and Services Tax in course of inter-state trade or commerce and Goods and Services Tax council, respectively. Apart from that, the bill also purports to amend Articles 248, 249, 250, 268, 269, 270, 271, 286, 366 and 368 of Constitution of India and amendment of the Sixth and the Seventh schedule of the Constitution as well. The Bill also seeks to repeal Article 268A of the Constitution.

1.3 By bringing this bill into effect, the Govt. of India intends to usher in fundamental systemic reforms in the indirect taxes dispensation currently being implemented in the country by integrating and harmonizing the tax structure across the country in the form of Goods and Services Tax (GST). The proposed amendments would subsume a number of indirect taxes presently being levied by Central and State Governments into GST thereby doing away the cascading of taxes and providing a common national market for Goods and Services. The aim to bring about these amendments in the Constitution is to confer simultaneous power on Parliament and State legislatures to make laws for levying GST simultaneously on every transaction of supply and Goods and Services.

1.4 This bill is a next step forward towards a comprehensive indirect tax reform in the country after the introduction of Value Added Tax (VAT). Though the indirect tax system in the country has been going through a series of reforms over the last two decades and one of them is the introduction of Value Added Tax called, CENVAT at the Central level providing credit of tax paid on inputs and capital goods upto the manufacturing stage and Subsequently, in 1994, a tax on services (commonly known as Service Tax) was introduced by the Centre. The Service Tax with the passage of time expanded its domain to cover more services and now applies to about 115 service categories which contributed growth in revenue from this tax. In 2004, the input tax credit scheme for CENVAT and Service Tax was merged to permit cross flow of credit across these taxes. As for the States, they have switched over from a multiple point Sales tax to a Value Added Tax (VAT) covering all transactions of sale of goods within the State up to the retail stage in a phased manner starting from 2005-06.

1.5 In spite of the fact that many of the aforesaid measures have been taken, goods and services continue to be bogged down with multiple indirect taxes at different stages of the value chain with significant tax cascading under the present indirect tax regime and therefore a need to introduce GST was strongly felt.

1.6 In international arena GST is known for its end user consumption tax. The broad objectives of introducing the Goods and Services Tax (GST) would widen the tax base through the coverage of multifarious economic activities into its ambit and by cutting down exemptions; mitigate cascading and double taxation and enabling better compliance through the lowering of overall tax burden on goods and services. By doing away with latent or embedded taxes, it would provide leeway for the competitiveness of domestic industry vis-à-vis imports and in international markets. Unifying the tax structure across States, the new scheme of tax regime would pave way for a common national market for goods and services.

1.7 The proposal for the introduction of GST was first mooted in the Budget Speech for the financial year 2006-07. Since then, detailed deliberations and negotiations were held with the Empowered Committee of State Finance Ministers (EC) on the topic. The 115th Constitutional (Amendment) Bill, 2011, for the introduction of GST was first introduced in the Lok Sabha in March 2011. The Bill was referred to a Parliamentary Standing Committee (PSC) which submitted its report in August 2013. The Bill however lapsed with the dissolution of the 15th Lok Sabha.

Rationale behind moving towards GST:

1.8 Presently, the Constitution empowers the Central Government to levy excise duty on manufacturing and service tax on the supply of services. Further, it empowers the State Governments to levy sales tax or value added tax (VAT) on the sale of goods. This exclusive division of fiscal powers has led to a multiplicity of indirect taxes in the country. In addition, central sales tax (CST) is levied on intra-State sale of goods by the Central Government, but collected and retained by the exporting States. Further, many States levy an entry tax on the entry of goods in local areas.

1.9 This multiplicity of taxes at the State and Central levels has resulted in a complex indirect tax structure in the country that is ridden with hidden costs for the trade and industry. Firstly, there is no uniformity of tax rates and structure across States. Secondly, there is cascading of taxes due to 'tax on tax'. No credit of excise duty and service tax paid at the stage of manufacture is available to the traders while paying the State level sales tax or VAT, and vice-versa. Further, no credit of State taxes paid in one State can be availed in other States. Hence, the prices of goods and services get artificially inflated to the extent of this 'tax on tax'.

1.10 The introduction of GST would mark a clear departure from the scheme of distribution of fiscal powers envisaged in the Constitution. The proposed dual GST envisages taxation of the same taxable event, i.e., supply of goods and services, simultaneously by both the Centre and the States.

1.11 GST will simplify and harmonise the indirect tax regime in the country. It is expected to reduce cost of production and inflation in the economy, thereby making the Indian trade and industry more competitive, domestically as well as internationally. It is also expected that introduction of GST will foster a common or seamless Indian market and contribute significantly to the growth of the economy.

1.12 Further, GST will broaden the tax base, and result in better tax compliance due to a robust IT infrastructure. Due to the seamless transfer of input tax credit from one stage to another in the chain of value addition, there is an in-built mechanism in the design of GST that would incentivize tax compliance by traders.

Roadmap for the implementation of GST:

1.13 Amendment of the Constitution: Government introduced on 19.12.2014 the Constitution (122nd) Amendment Bill, 2014 in the Lok Sabha for amending the Constitution of India to facilitate introduction of Goods and Services Tax (GST) in the country. The Bill has been passed by the Lok Sabha on 06.05.2015 and is pending in Rajya Sabha. After the Bill is passed in both the Houses of the Parliament by two-thirds majority, the Constitutional Amendment Bill will be sent to State Legislatures for ratification. The ratification by at least 50% of the State Legislature will be required before the proposed amendments are brought in effect.

1.14 Enactment of enabling legislation in the Centre and States: For the levy of CGST, SGST and IGST, a set of three laws would need to be enacted. CGST and IGST laws would need to be enacted by the Parliament, and the SGST law would have to be enacted by each of the State Legislatures.

Status on design and mechanics of GST:

1.15 The contours of GST are still evolving. Key aspects of GST like the tax rate, tax base, exemption limits, place of supply rules for services, appropriate IGST model etc. will be finalized on passage of the Bill. In this regard, the Empowered Committee of State Finance Ministers(EC) and the Department of

Revenue, GOI, have constituted several working groups and committees for drafting the GST Rules and processes as follows:-

- i. Committee on Dual Control, Threshold and Exemptions in GST Regime;
- ii. Committee on IGST and GST on imports;
- iii. Committee on Revenue Neutral rates for State GST & Central GST and Place of Supply Rules;
- iv. Committee to draft model GST Law;
- v. Committee to examine the Report of the sub-Group-I on Business Processes.

Salient features of the Constitution (122nd) Amendment Bill, 2014:

1.16 The salient features of the GST Bill as introduced in the Lok Sabha are as follows:-

(a) subsuming of various Central indirect taxes and levies such as Central Excise Duty, Additional Excise Duties, Excise Duty levied under the Medicinal and Toilet Preparations (Excise Duties) Act, 1955, Service Tax, Additional Customs Duty commonly known as Countervailing Duty, Special Additional Duty of Customs, and Central Surcharges and Cesses so far as they relate to the supply of goods and services;

(b) subsuming of State Value Added Tax/Sales Tax, Entertainment Tax (other than the tax levied by the local bodies), Central Sales Tax (levied by the Centre and collected by the States), Octroi and Entry tax, Purchase Tax, Luxury tax, Taxes on lottery, betting and gambling; and State cesses and surcharges in so far as they relate to supply of goods and services;

(c) dispensing with the concept of 'declared goods of special importance' under the Constitution;

(d) levy of Integrated Goods and Services Tax on inter-State transactions of goods and services;

(e) levy of an additional tax on supply of goods, not exceeding one per cent. in the course of inter-State trade or commerce to be collected by the

Government of India for a period of two years, and assigned to the States from where the supply originates;

(f) conferring concurrent power upon Parliament and the State Legislatures to make laws governing goods and services tax;

(g) coverage of all goods and services, except alcoholic liquor for human consumption, for the levy of goods and services tax. In case of petroleum and petroleum products, it has been provided that these goods shall not be subject to the levy of Goods and Services Tax till a date notified on the recommendation of the Goods and Services Tax Council.

(h) compensation to the States for loss of revenue arising on account of implementation of the Goods and Services Tax for a period which may extend to five years;

(i) creation of Goods and Services Tax Council to examine issues relating to goods and services tax and make recommendations to the Union and the States on parameters like rates, exemption list and threshold limits. The Council shall function under the Chairmanship of the Union Finance Minister and will have the Union Minister of State in charge of Revenue or Finance as member, along with the Minister in-charge of Finance or Taxation or any other Minister nominated by each State Government. It is further provided that every decision of the Council shall be taken by a majority of not less than three-fourths of the weighted votes of the members present and voting in accordance with the following principles:—

(A) the vote of the Central Government shall have a weightage of one-third of the total votes cast, and

(B) the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast in that meeting.

Deliberations

1.17. The Committee held its first meeting on 22nd May, 2015. At its introductory meeting the Committee decided to chalk out its future course of action. As the State Governments were the main stakeholders, it was unanimously decided by the Committee to seek their written views on the Bill by 5th June, 2015. The Members were also requested to suggest the names of the Experts/stakeholders to be heard by the Committee.

1.18 In response thereto, the Committee received written memorandum from the State Governments of Madhya Pradesh, Bihar, Odisha, Himachal Pradesh, Uttar Pradesh, Punjab, Sikkim, UT of Puducherry, Maharashtra, Chhattisgarh, Goa, Gujarat, Kerala, West Bengal, Tamil Nadu, Karnataka and Assam.

The Committee heard the views of the Secretaries of Ministries of Finance (Department of Revenue) and Law & Justice (Legislative Department) on the Bill.

1.19 Secretary, Department of Revenue made a presentation before the Committee informing the Committee about a brief history and background of the Bill and the reason and purpose to bring about the constitutional Amendments proposed in the Bill.

1.20 The Committee held its second meeting on 29th May, 2015. As the Bill was going to have a wider implication on the Municipal Bodies and Gram Panchayat, the Committee invited Ministries of Urban Development and Panchayati Raj in the meeting. In addition to this, the Secretaries, Ministries of Finance (Department of Revenue) and Law and Justice (Legislative Department) had also been invited to be present in the meeting to clarify points/issues, if any, being raised by the Members on the Bill.

1.21 In his deposition before the Committee, Secretary, Ministry of Urban Development highlighted the importance of the Municipalities in the wake of urbanization and also thereby deteriorating the quality of life in the cities. He also emphasized that due to urbanization and their meager financial resources to cope with the demands of their present needs, these municipalities were facing unprecedented cash flow problems so the basic infrastructure in the cities has deteriorated to a great extent though on a comparable scale the life in cities has been more rewarding and comfortable than that of countryside. So, by way of the proposed constitutional amendment, the Ministry expected some positive changes in the present scenario whereby financial independence of the local bodies including gram panchayat could be realized in the new scheme of things and these bodies could match up and cope up with the demands and pressure being exerted on their resources and may not remain financially dependent on the sweet will of their respective states. In his deposition, before the Committee, Secretary, Panchayati Raj endorsed the views expressed by Secretary, Urban Development.

1.22. As the Bill was of very vast nature and has been described as a reform measure of unparalleled importance in the sphere of Indian Taxation regime in independent India, the Committee felt that State Governments being major stakeholders, their views would be crucial in preparation of Report on the Bill. Therefore, the Committee decided to undertake a study visit to Chennai, Kolkata and Mumbai from 21st to 25th June, 2015 to interact with the representatives of the various State Governments, Public and Private authorities/organisations/ financial institutions, etc on the Bill.

1.23 During its visit to Chennai, Kolkata and Mumbai, the Committee heard the views of the State Governments/ UTs of Tamil Nadu, Puducherry, Kerala, West Bengal, Maharashtra, Gujarat and Goa. Apart from this the Committee also heard the views of the experts namely Dr. V. Bhaskar, Former Special Chief Secretary, Finance Department, Govt. of Andhra Pradesh, Dr. Partho Shome, Former Chairman, Tax Administration Reforms Commission, Dr. Asim Das Gupta, Former Finance Minister, Govt. of West Bengal including the Industrial Houses i.e. CII, ASSOCHAM and FICCI on the Bill.

1.24 In addition to this, the Committee also heard the views of financial institutions/Associations/Organisations during the visit of the Committee. A list of the same is enclosed at **Annexure-II**

1.25 The Committee received 58 Memoranda from State Governments/Experts/other Stakeholders. These Memoranda were transmitted to the Ministry of Finance (Department of Revenue) for their comments and suggestions. While framing the specific and general recommendations on the Bill, the Committee has duly taken into consideration the suggestion made by the State Government/experts/other Stakeholders and the Department of Revenue on these memoranda.

CHAPTER-II

CLAUSE BY CLAUSE CONSIDERATION

Clause 1

2.1 This clause provides for short title and commencement of the Constitution (Amendment) Bill.

Recommendation

2.2 This clause has been adopted with no change.

Clause 2

2.3 This clause makes enabling provisions for the Union and States with respect to GST.

2.4 Sub-clause (1) of this clause seeks to provide that notwithstanding anything contained in articles 246 and 254, Parliament, and, subject to clause (2), the

Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by such State.

2.5 Sub-clause (2) of the said clause seeks to provide that Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce with an explanation that that provision of this article in respect of goods and services tax referred to in clause (5) of article 279A, that is, on petroleum crude, high speed diesel, petrol, natural gas and aviation turbine fuel shall take effect from the date recommended by the Goods and Services Tax Council.

2.6 In respect of this clause, apprehensions were expressed by some Members that the clause may affect the powers of the State Governments mentioned under the concurrent list. In this regard, the Committee felt that their apprehensions were unwarranted as the clause will not affect any powers of the State Government under concurrent list.

2.7 As regards the amendments proposed in article 246A (1) to insert the words, “not exceeding 18 per cent” between “goods and services tax” and imposed by the Union or by such State” is concerned, "the Members moving the amendment stressed the need to keep GST rates moderate and reasonable so that consumers are not excessively burdened, and to this end proposed that the GST Council be bound by the Constitution to not exceed 18% as the rate for an adequately revenue-generating GST."

Views of the Government

2.8 In response thereto, the Ministry of Finance, Department of Revenue has stated that rates of GST cannot be fixed in the Constitution as this is a dynamic variable. The rates of GST would have to be recommended by the GST Council depending on various factors such as economic conditions, revenue buoyancy, etc. At the same time, every effort would be made by the GST Council to ensure that the rate of GST is reasonable. Further, there may be certain demerit goods such as

tobacco, or luxury goods, that may, if the GST Council so decides, attract a higher rate of GST. RNR was calculated by NIPFP before introduction of GST Constitution amendment Bill. NIPFP and the Committee headed by CEA are working out rates under GST as per provisions of Bill.

2.9 The Department of Revenue stated that Petroleum products have been included under definition of “goods and services tax” provided in proposed clause (12A) of article 366. An Explanation has been added in proposed article 246A to clarify that GST will not be levied on petroleum and petroleum products till a future date to be recommended by the GST Council. This has been done after FM’s meeting with State Finance Ministers on 15.12.2014 and is also as per the recommendations of the Empowered Committee to protect the revenue streams of the States.

2.10 With regard to providing for a maximum rate of GST in the Bill, the Department of Revenue mentioned that rates of GST cannot be fixed in the Constitution, as this is a dynamic variable. The rates of GST would have to be recommended by the GST Council depending on various factors such as economic conditions, revenue buoyancy, etc. To allay fears of revenue loss a provision of compensation to States has been provided in the Bill. At the same time, every effort would be taken to ensure that the rate of GST is reasonable. Further, there may be certain demerit goods such as tobacco, or luxury goods, that may attract a higher rate of GST.

Views of the Stakeholders

2.11 Most of the State Governments in their written replies have objected to bringing petroleum products under the ambit of GST. Another suggestion was to include Aviation Gasoline in that list.

2.12 However, the Experts/stakeholders were of the considered opinion that it needs to be emphasised that since a large part of the petroleum and petroleum products are important intermediate inputs, it is absolutely necessary to bring them

under the GST ambit sooner than later to eliminate cascading effect and its associated inefficient economic cost. Even in a GST regime, these could be taxed at higher rate if revenues have to be protected. It is well known that petroleum and petroleum products and alcohol together contribute around 40 to 45 per cent of VAT/Sales tax revenues of States. The share of excise duty collection from petroleum and petroleum products is substantial for Central Government as well. It appears that revenue consideration alone is holding back inclusion of these items in GST. It is necessary for the Bill to specify a specific date for inclusion of these items under GST especially when the economic efficiency benefit from inclusion is much more than the direct short run revenue impact to the Central and the State Governments.

Recommendation

2.13 The clause has been adopted with no change.

Clause 3

2.14 This clause seeks to make consequential amendments in article 248 of the Constitution in view of the proposed amendment in clause 2 of the Bill. Since Union has residuary power to make laws on subjects not mentioned in any of the Lists, it is proposed to make it clear that if anything is not covered specifically then, as per Constitutional Scheme, it would fall under article 248.

Recommendation

2.15 This clause has been adopted with no change.

Clause 4

2.16 This clause seeks to make consequential amendments in article 249 of the Constitution in view of the proposed amendment in clause 2 of the Bill. This amendment enables Parliament to make laws in national interest, if so required as per the procedure laid therein.

Recommendation

2.17 **This clause has been adopted with no change.**

Clause 5

2.18 This clause seeks to make consequential amendments in article 250 of the Constitution in view of the proposed amendment in clause 2 of the Bill. The amendment makes it clear that Union may legislate as in other cases if a proclamation of emergency is in operation.

Recommendation

2.19 **This clause has been adopted with no change.**

Clause 6

2.20 This clause seeks to amend article 268 of the Constitution to omit the duties of excise on medicinal and toilet preparations from the purview of the power of the Government of India in view of the proposed imposition of goods and services tax on goods and services.

Recommendation

2.21 **This clause has been adopted with no change.**

Clause 7

2.22 This clause seeks to omit article 268A of the Constitution as inserted by section 2 of the Constitution (Eighty-eighth Amendment) Act, 2003. The said article empowers the Government of India to levy taxes on services. As it is proposed to bring tax on services under GST, such a provision would no longer be required for the reason that the provision though enacted, it is yet to be notified so far.

Recommendation

2.23 This clause has been adopted with no change.

Clause 8

2.24 This clause seeks to amend clause (1) of article 269 of the Constitution to insert after the words “consignment of goods” the words, figures and letter “except as provided in article 269A” in view of the new article 269A which provides for levy of goods and services tax on supplies in the course of inter-State trade or commerce and apportionment of such tax between the Union and the States in the manner provided by Parliament by law on the recommendations of the Goods and Services Tax Council.

Recommendation

2.25 This clause has been adopted with no change.

Clause 9

2.26 This clause seeks to insert a new article 269A which provides for goods and services tax on supplies in the course of inter-State trade or commerce which shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council. It also provides that Parliament may, by law, formulate the principles for determining the place of supply, and when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

2.27 As regards this clause, Members sought clarifications about the distinction between “supplies, sales and purchase; and consignment”.

2.28 Some Members suggested that that after 269A (1), the following proviso may be added:-

2.29 “Provided that the expression “supplies” shall not apply to goods and services supplied by one unit of a firm to another unit of the same firm under the same ownership in another location or State.

Provided further that if two or more firms are together engaged in the supply of the same end product, the expression “supplies” shall not apply to such transactions.”

Views of the Government

2.30 In this regard, the Ministry of Finance, Department of Revenue stated that while “sale” is for consideration, “consignments” are in the nature of branch transfers. “Supplies” would constitute both “sale” as well as “consignment” transactions. Further, since GST charged on supply of goods and services would be VATable, this would not have any cascading impact. Since input tax credit would be available for GST paid on both sales as well as consignments in the course of inter-State trade, there would be no cascading impact of levying GST on supplies of goods and services in the course of inter-State trade.

2.31 The words ‘on the recommendations of the GST Council’ have been added to proposed article 269A (1) vide this clause. This would ensure that the law made by Parliament for apportioning the proceeds of IGST between the Union and the States will be made on the recommendation of the GST Council. This has been done as per the recommendations of the Empowered Committee after their meeting in Shillong in November 2013.

Views of the Stakeholders

2.32 The stakeholders were of the view that proceeds of IGST shall be used for settlement of accounts among the States for flow of input tax credit in inter-State transactions, and in theory, there should be zero balance in the proceeds of IGST in a fiscal year. But, in practice, there may be a distinct possibility of a positive

balance in the proceeds of IGST at the end of a fiscal year. In that event, there should be a constitutionally appropriate mechanism for distribution of these remaining proceeds in a year, to be provided in terms of suitable provision in article 269A in clause 9.

Recommendation

2.33 The Committee feels that since imposition of GST on the supplies of goods and services in the course of inter-State trade would not lead to cascading of taxes, hence the Clause has been adopted with no change.

Clause 10

2.34 This clause seeks to amend clause (1) of article 270 of the Constitution to substitute the words, figures and letter “article 268, 268A and 269”, the words, figures and letter “article 268, 269 and article 269A” in view of the proposed amendments referred to above; to insert a new clause (1A) after the existing clause (1) of article 270 to provide that the goods and services tax levied and collected by the Government of India, except the tax apportioned with the States under clause (1) of article 269A, shall also be distributed between the Union and the States in the manner provided in clause (2).

Views of the Stakeholders

2.35 It was proposed by one of the State Government that the words “not apportioned” should be replaced with “not appropriated” in order to be in sync with the term used in the proposed Article 269A(1). Likewise, the word “distributed” should be replaced with the expression appropriated”.

Recommendation

2.36 This clause has been adopted with no change.

Clause 11

2.37 Clause 11 of the Bill seeks to amend article 271 of the Constitution to insert after the words “in those articles”, the words “except the goods and services tax under article 246A”, with a view to put restrictions on the powers of Parliament to levy surcharge for the purposes of the Union on the GST. In other words, it provides that goods and services on which GST is levied shall not be subject to any surcharge under article 271.

Recommendation

2.38 This clause has been adopted with no change.

Clause 12

2.39 Sub-clause (1) of this clause seeks to provide for insertion of a new article 279A which empowers the President to constitute, by order, a Council to be called the Goods and Services Tax Council consisting of the Members referred to in sub-clause (2) of this clause.

2.40 Sub-clause (2) of the said clause seeks to provide that the Goods and Services Tax Council shall consist of the Union Finance Minister as Chairperson; the Union Minister of State in charge of Revenue or Finance as Member; the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government as Members.

2.41 Sub-clause (3) of the said clause seeks to provide that the Members of the Goods and Services Tax Council referred to in sub-clause (c) of clause (2) shall, as soon as may be, choose one amongst themselves to be the Vice-Chairperson of the Council for such period as they may decide.

2.42 Sub-clause (4) of the said clause seeks to provide that the Goods and Services Tax Council shall make recommendations to the Union and the States on the taxes, cesses and surcharges levied by the Union, the States and the local bodies which may be subsumed in the goods and services tax; the goods and services that may be subjected to, or exempted from the goods and services tax;

model Goods and Services Tax Laws, principles of levy, apportionment of Integrated Goods and Services Tax and the principles that govern the place of supply; the threshold limit of turnover below which goods and services may be exempted from goods and services tax; the rates including floor rates with bands of goods and services tax; any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster; special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand; and any other matter relating to the goods and services tax, as the Council may decide.

2.43 Some Members proposed that under clause 4 (c), among the "principles" to be considered by the GST Council while preparing GST laws the principle of "share of local bodies in revenue buoyancy and compensation for losses sustained through taxes subsumed" should be included as articles 243H and 243X provide for State Legislatures to, by law, ensure the "sound finances" of the local bodies. This would also enable State Finance Commissions set up under articles 243 I and 243 Y to provide for augmenting the share of local bodies in revenue buoyancy generated by the adoption of GST.

2.44 With reference to sub-clause (4) (g) which provides for "special consideration" to certain States, some Members proposed, in keeping with article 243 B (2), that "special consideration" may also be extended to States like Goa and Union territories like Puducherry by adding at the end of 4(g) " and any State or Union territory having a population not exceeding twenty lakhs".

2.45 Sub-clause (5) of the said clause seeks to provide that 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. These items have been kept out of GST to protect the revenue interest of the States.

2.46 Some members sought the inclusion in clause 12(5) of highly revenue-generating products like tobacco and tobacco products, alcohol for human consumption and electricity supply and consumption within a period not later than five years so that India, within a few years, fulfills the fundamental GST objective of making the entire nation a single common market for all products.

2.47 Sub-clause (6) of the said clause seeks to provide that while discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

2.48 Sub-clause (7) of the said clause seeks to provide that one half of the total number of Members of the Goods and Services Tax Council shall constitute the quorum at its meetings so that the States have say in the matters of their interest.

2.49 Sub-clause (8) of the said clause seeks to provide that the Goods and Services Tax Council shall determine the procedure in the performance of its functions.

2.50 Sub-clause (9) of the said clause seeks to provide that every decision of the Goods and Services Tax Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the members present and voting, in accordance with the vote of the Central Government shall have a weightage of one-third of the total votes cast, and the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast, in that meeting. Sub-clause (10) of the said clause provides that No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of— any vacancy in, or any defect in, the constitution of the Council; or any defect in the appointment of a person as a member of the Council; or any procedural irregularity of the Council not affecting the merits of the case. Sub-Clause (11) of the said Clause provides that the Goods and Services Tax Council may decide about the modalities to resolve disputes arising out of its recommendation.

2.51 In respect of this clause some Members proposed amendment that while discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the destination based taxation principle and need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

2.52 Every decision of the Goods and Services Tax Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the members present and voting, in accordance with the following principles, namely:-

(a) The vote of the Central Government shall have a weightage of one-fourth of the total votes cast, and

(b) The votes of all the State Governments taken together shall have a weightage of three-fourth of the total votes cast, in that meeting. And the vote of each state shall have a weightage proportionate to the population of that State.

After 279A, add the following new article 279B:

2.53 (1) Parliament may, by law, provide for the establishment of a Goods and Services Tax Dispute Settlement Authority to adjudicate any dispute or complaint referred to it by a State Government or Governments of the Government of India arising out of a deviation from any of the recommendations of the Goods and Services Tax Council constituted under article 279A that results in a loss of revenue to a State Government or Governments or the Government of India or affects the harmonized structure of the Goods and Services Tax.

2.54 (2) The Goods and Services Tax Dispute Settlement Authority shall consist of a Chairperson and two other Members.

2.55 (3) The Chairperson of the Goods and Services Tax Dispute Settlement Authority shall be a person who has been Judge of the Supreme Court or Chief

Justice of a High Court to be appointed by the President on the recommendation of the Chief Justice of India.

2.56 (4) The two other members of the Goods and Services Tax Dispute settlement Authority shall be persons of proven capacity and expertise in the field of law, economics or public affairs to be appointed by the President on the recommendation of the Goods and Services Tax Council.

2.57 (5) The Goods and Services Tax Dispute Settlement Authority shall pass suitable orders including interim orders.

2.58 (6) A law made under clause (1) may specify the powers which may be exercised by the Goods and Services Tax Dispute Settlement Authority and provide for the procedure to be followed by it.

2.59 (7) Notwithstanding anything in this Constitution, Parliament may, by law, provide that no Court other than the Supreme Court shall exercise jurisdiction in respect of any such adjudication or dispute or complaint as is referred to in clause (1).

2.60 Explanation- For the purposes of this article, “State” includes a Union territory with Legislature.

Views of the Government

Proposed article 279A (4)(c):

2.61 The GST Council would now make recommendations on the model GST laws, principles of IGST apportionment, and place of supply rules. This has been done as per the recommendations of the Empowered Committee after their meeting in Shillong in November 2013. It may not be appropriate for the GST Council or any other body to stipulate the share of local bodies in the revenues collected by the respective States. 73rd Amendment of the Constitution provides for setting up of State Finance Commissions which have been given the responsibility to make recommendations on principles which govern distribution

of finances between the States and local bodies i.e., Panchayats and Municipalities. Deficiencies, if any, in functioning of State Finance Commissions in individual States may have to be dealt with separately.

2.62 The Department further clarified that taxing powers of local bodies -- Panchayats and Municipalities -- are derived from Acts and laws passed by the State Legislatures. The State Legislatures, under Article 243H and 243X of the Constitution, are authorized to make laws, which are the taxes that the local bodies will levy. This power has not been interfered with and the current structure in the Constitution remains intact.

2.63 So far as other arrangements which are currently provided under the Constitution with regard to formation of the State Finance Commissions and with regard to devolution which the State Governments should make are concerned, they also remain intact in the Constitution. These have not been interfered with.

Proposed article 279A (4)(e)

2.64 To give flexibility to the States, the provision of ‘bands’ over the GST floor rates, to be recommended by the GST Council, has been introduced. Depending on the local situations and requirements, the States have the option to levy slightly higher tax within this band. This shall also enable the States to cushion the impact of any potential loss of revenue arising out of implementation of GST. The word “band” does not need to be defined in the Constitution but would need to be defined in the model State tax law or the SGST law and the CGST law which shall be recommended by the GST Council. This provision has been made as per the recommendations of the Empowered Committee after their meeting in Bhubaneswar in January 2013, and also the recommendations of the Parliamentary Standing Committee.

Proposed article 279A (4) (f), (g)

2.65 Special category status has been granted to 11 States by the National Development Council comprising the Prime Minister, Union Ministers, Chief Ministers and members of the erstwhile Planning Commission (Now NITI Aayog). Provision of special category States is not based on population but on specific issues such as hilly and difficult terrain, strategic location along borders with neighbouring countries, economic and infrastructural backwardness, and non-viable nature of state finances. The proposed amendment shall mean inclusion of the State of Goa and UT of Puducherry in the list of States with special provisions. Goa has the highest per capita income in the country while Puducherry has fifth highest per capita income in the country. Neither of them have any of the specific problems listed in the criteria above.

Proposed article 279A (5)

2.66 Initially, as recommended by the Parliamentary Standing Committee on Finance and the Empowered Committee in its Bhubaneswar meeting in January 2013, 'petroleum products' had been proposed to be subsumed in GST. However, since taxes on petroleum products constitute a major portion of State revenues, many States expressed apprehension over possible revenue loss in case petroleum products are subsumed under GST. Hence, these products have been constitutionally brought under GST and it has been provided that they would not be subject to GST till notified at a future date on the recommendation of the GST Council. It may be mentioned that petroleum products constitute a major input in most manufacturing industries and their non inclusion would mean these industries would not be able to claim input tax credit for such inputs resulting in cascading of taxes and increased cost of production. It is expected that once GST regime is stabilised, the States may want to include petroleum under GST after two or three years itself. As per the proposed amendment, the GST Council shall not be able to make any recommendation before five years to include petroleum products under GST. Hence, it is better to keep the option open for Council to decide rather than binding the GST Council for five years.

2.67 Further, the Bill leaves it to the GST Council to recommend the date on which GST shall be applicable on petroleum products. Since the States would have 2/3rd vote share in the Council, if the States do not want GST to be imposed on petroleum products, in any case it would not be possible for GST to be imposed on petroleum products as long as the States do not agree. Further, losses, if any suffered by the States, will be compensated by the Centre.

Proposed article 279A (9)

2.68 The structure of GST Council represents the federal nature of governance in this country. This has been done as per the recommendations of the Empowered Committee after their meeting in Bhubaneswar in January 2013, and also the recommendations of the Parliamentary Standing Committee. This provision has been consciously adopted to ensure the federal balance in the functioning of the GST Council, and also to enhance co-operative federalism. The existing pattern of vote-share in the GST Council ensures that no decision can be taken by the Council either by the Centre or the States acting on their own. Hence, neither the States nor the Centre alone can take a decision in the Council. Providing 3/4th weightage to the States would upset the federal balance between the Centre and the States. Presently, in the concurrent list, in case of any difference between Central and State legislation, the Central legislation prevails. The present weightage of votes in the GST Council would ensure that neither the Centre nor the States are able to take a decision without the support of the other. In other words both would enjoy a veto.

2.69 Further, with Centre holding only 1/3rd of the votes, the Centre would require support of 20 States/Union Territories to get a resolution passed. This shows that Centre would need co-operation of States to get any decision taken at the GST Council.

Proposed article 279A (11)

2.70 The hitherto proposed article 279B for the creation of a GST Dispute Settlement Authority has been omitted, and a provision has been made in Article

279A itself empowering the GST Council to decide about the modalities to resolve the disputes arising out of its recommendations. The States were apprehensive that the proposed GST Dispute Settlement Authority under proposed article 279B would affect the fiscal powers of the States and the Union. Hence, this provision has been done away with. This has been done as per the recommendations of the Empowered Committee after their meeting in Bhubaneswar in January 2013, and also the recommendation of the Parliamentary Standing Committee.

2.71 It may further be mentioned that Article 279A (11) only provides that GST Council may decide the ‘modalities’ to resolve disputes arising out of its recommendations. The ‘modalities’ could include any dispute resolution mechanism which could be *inter-alia* negotiation, mediation, arbitration or even a judicial authority as deemed appropriate by the GST Council depending on the nature of dispute before it. Thus, as per the proposed Bill, the GST Council shall, by itself, not be resolving the disputes but decide on the modalities for resolving the disputes.

Views of the Stakeholders

2.72 The Stakeholders were of the view that vote of the Central Government and State Government shall have the weightage of 1/4th and 3/4th respectively otherwise it would be difficult to get the proposals approved, in the constitution of GST Council instead of the words ‘Union Minister of State in charge of Revenue or Finance’ it should be ‘Ministers’ in charge for these functions, as these positions are not explicitly mandated in the Constitution, No dispute resolution mechanism can be meaningful and effective without an explicit linkage between the empowerment clause for the levy of GST (Articles 246A and 366(12A)) and the GST Council recommendations, Goods and Services Tax Council shall be guided by the destination based taxation principle and need for a harmonized structure of goods and services tax and for the development of a harmonized national market for goods and services, Requisite provisions may be incorporated to make the decisions of the GST Council binding on the States and

the Union, Include the State/UT of Goa and Puducherry in Article 279A (4) (G), The Threshold limit for applicability of GST may be fixed at Rs. 50 Lacs, GST Rate may be kept in the range of 16-18%, Tax rate on Goods and Services is to be same to avoid disputes, Tax on interstate supply of goods from one state to other of the same company may be exempted from the purview of GST, The Input taxes paid by the exporters are to be refunded automatically, etc.

Recommendation

2.73 After having deliberated on the issue of finances of local bodies, the Committee strongly feels that the revenues of local bodies need to be sustained and protected for ensuring that standards of local governance are maintained. The Committee, thus, strongly recommends that the State Governments take adequate measures to ensure that adequate revenues flow to the local bodies, and their resources are not adversely affected. The Committee noted that Article 243H and 243X contain provisions for State Legislatures to authorize Panchayats and Municipalities to collect and appropriate taxes in the State list. The Committee further noted that Article 243I and 243Y provide for setting up of State Finance Commissions to make recommendations regarding devolution of funds to local bodies. The Committee noted that the above provisions notwithstanding, local bodies find managing their resource requirements quite challenging.

2.74 In light of above, with respect to Article 279A 4(e), the Committee strongly recommends that the word ‘band’ used in the proposed Article may be defined in GST laws. The Committee recommends the following definition of ‘band’:

“Band” : Range of GST rates over the floor rate within which Central Goods and Service Tax (CGST) or State Goods and Services Tax (SGST) may be levied on any specified goods or services or any specified class of

goods or services by the Central or a particular State Government as the case may be.

2.75 With respect to Article 279A(5), taking note of the provision that inclusion of petroleum products into GST can take place only on recommendation of GST Council which could happen only with the consent of both the Centre and the States, the Committee recommended that the clause be adopted with no change.

2.76 The Committee is aware that while discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

2.77 In view of the clarifications submitted by the Department of Revenue and Legislative Department, the Committee finds no merit in disturbing the voting pattern proposed in the Bill, as the same has been worked out on a formula where no one is at an disadvantageous or dominating position be it Centre or States. Moreover, under clause 2 Parliament and the Legislature of every State shall have power to make laws with respect to GST simultaneously.

2.78 In the GST Council, all the decisions have to be taken collectively by the Centre and States and in order to take decision on any issue 75% votes are necessary. So, in order to strike a fine balance Centre vote share has been kept at $1/3^{\text{rd}}$ and that of the States at $2/3^{\text{rd}}$. In that backdrop, the Committee recommends that these amendments may not be necessary since our Constitution is a federal Constitution and so, it is necessary to make the provisions providing for a manner that disallow the dominance of one over the other. Keeping this in view, the voting formula has been worked out. Hence, the clause has been adopted with no change.

2.79 The Committee, having noted the point mentioned by the Department of Revenue that the GST Council shall decide only the ‘modalities’ to resolve disputes, did not agree to recommend inclusion of Article 279B as was proposed in Constitution(115th Amendment) Bill, 2011.

Clause 13

2.80 This clause seeks to amend clauses (1) and (2) of article 286 of the Constitution which is a consequential amendment in view of the proposed amendments in clause 2 of the Bill.

2.81 One Member proposed insertion of a new clause (1A) in article 286 of the Constitution to provide as under-

“No law of a State shall impose, or authorize the imposition of, any restriction on reimbursement of a tax levied under the law of a State in respect of any supply of goods or of services of both inside the State, when such goods or services or both are supplied in the course of inter-State trade or commerce or export outside the territory of India.

Explanation.— For the purpose of this clause, consumption or use of goods or services or both whether partly or wholly, in supply of any other goods or services or both in the course of inter-State trade or commerce or export outside the territory of India, shall be deemed to be supply of goods or services or both in the course of inter-State trade or commerce or export outside the territory of India to the extent of such consumption or use. ”

Views of the Government

2.82 Article 286 put restriction on the imposition of tax on the sale or purchase of goods if such sale or purchase takes place outside the States or in the course of import of goods into or export of goods outside the territory of India. By making amendments so as to substitute the words “sale or purchase of goods” the words

“supply of goods or services or both”, the restrictions would continue to apply any IGST or CGST and therefore it may not be necessary to go for the above amendment.

2.83 Some Members sought the definition in the Constitution amendment Bill itself of the term "supply" in proposed clause I (A) of article 286.

Recommendation

2.84 **The term 'supply' would be defined in the various GST laws relating to CGST and SGST. Hence, the Committee feels that it would not be appropriate to insert the definition of supply in this clause. This clause has been adopted with no change.**

Clause 14

2.85 Clause 14 of the Bill seeks to insert a new definition clause (12A) in article 366 of the Constitution to define the words “goods and services tax”. It also seeks to insert two clauses (26A) and (26B) to define the words “Services” and “State”, respectively.

2.86 Some Members proposed amendments in clause (12A) to delete the word “any” and the words “except taxes on the supply of alcoholic liquor for human consumption so as to progressively ensure a true common market for all goods”.

2.87 In (26A) delete “anything other than goods” and substitute with “commercial transactions in intangibles so as to avoid the circular definition of 'services' meaning 'anything other than goods.'”

Views of the Government

2.88 In this regard the Ministry of Finance, Department of Revenue has stated that term ‘services’ has been so defined in order to give it wide amplitude so that all supplies that are not goods can potentially be covered within the ambit of services and no activity remains outside the taxable net. This would also minimize disputes.

2.89 On the issue of inclusion of Petroleum and petroleum products under GST constitutionally, Department of Revenue in their written submission stated that:

2.90 Petroleum and petroleum products have been included under GST constitutionally by keeping only “alcoholic liquor for human consumption” outside of definition of “goods and services tax” given in newly introduced clause (12A) of article 366. However, GST would be leviable on these products only w.e.f. the date recommended by the GST Council. This has been done taking into consideration the concern expressed by Empowered Committee in their various meetings about the likely loss of Revenue, if the Petroleum products are included in GST. Parliamentary Standing Committee had recommended that there should be no exclusions from GST provided under the Constitution Amendment Bill.

2.91 The Department of Revenue mentioned that petroleum products constitute a major input in most manufacturing industries and their non inclusion would mean these industries would not be able to claim input tax credit for such inputs resulting in cascading of taxes and increased cost of production. It is possible that once GST regime is stabilised, the States may want to include petroleum under GST after two or three years itself. In such a situation, since petroleum products have been included Constitutionally, including petroleum products under GST would not require a Constitution amendment.

Views of the Stakeholders

2.92 The Experts/Stakeholders were of the considered views that:

Definition of Services

2.93 “Supply of Services’ means any business activity which is not supply of goods.”

2.94 In view of Article 246A empowering both Centre and States to levy tax on supply of goods and services, it is the view that the Clause (29A) of Article 366 may be considered for deletion as this would become redundant.

Petroleum

2.95 The international practice is to include petroleum in the GST base, and then apply a supplementary excise on selected petroleum products (e.g., petrol and diesel). A credit is allowed for the GST portion of the tax to commercial or industrial use of the fuels, but not for the supplementary excise. It would be advisable for India also to adopt this structure.

2.96 Thus, it is recommended that the provisions limiting the scope of GST (to exclude petroleum products) be deleted. Specifically, Explanation to Article 246A is redundant. The GST Council has the powers in any case to exclude any products from the GST base, if it so decides.

Goods and Services Tax

2.97 It is advisable to change the definition of ‘goods and services tax’ in Article 366 (12A) as follows. Further, goods in Article 366(12) need to be redefined to include real property.

2.98 “goods and services tax” means a multi-stage destination-based value added tax on supply of goods, or services, or both, and levied as per the framework recommended by the GST Council.

2.99 “goods” includes, for purposes of the goods and services tax, all materials, commodities, articles, and immovable property

Recommendation

2.100 **Endorsing the view of the Department, the Committee feels that ‘services’ has been so defined in order to give it wide amplitude so that all supplies that are not goods can potentially be covered within the ambit of services and no activity remains outside the taxable net. This would also minimize disputes. Further, having noted the points mentioned by the Department of Revenue regarding inclusion of petroleum products under GST, the clause has been adopted with no change.**

Clause 15

2.101 This clause seeks to amend article 368 of the Constitution in view of the proposed amendments referred to in clause 12 of the said Bill so as to apply the special procedure provided in the proviso to clause (2) thereof which requires the ratification of the Bill by the Legislatures of not less than one half of the States in addition to the method of voting provided for amendment of the Constitution.

Recommendation

2.102 This clause has been adopted with no change.

Clause 16

2.103 This clause seeks to amend the sub-paragraph (3) of paragraph 8 of the Sixth Schedule to the Constitution with a view to empower the District Council for an autonomous district to have the power to levy and collect taxes on entertainment and amusements within such district.

Recommendation

2.104 This clause has been adopted with no change.

Clause 17

2.105 This clause seeks to amend the Seventh Schedule of the Constitution to substitute the items under entry 84 of the List I and to omit entries 92 and 92C; to omit entries 52 and 55 of List II and substitute the entries 54 and 62 of List II of the Seventh Schedule to the Constitution. These amendments are consequential to the insertion of new article 246A.

2.106 With a view to progressively promoting a common market in all goods and services, some Members proposed amendment to Entry 84 of Union List as follows:

- (g) sale and consumption of electricity'
- (h) alcohol for human consumption.

2.107 Some Members also sought clarifications as it does not figure in the Constitution (a) (ii): What is entry 92C?

Recommendation

2.108 Regarding the aforesaid Entry, the Committee is of the view that Entry 92C was inserted by the Constitution (Eighty-Eighth Amendment) Act, 2003 to empower the Union to impose service tax on certain services read with article 268A of the Constitution.

2.109 Notwithstanding, the service tax levied under the Finance Act, 1994 were continuing as such. The amendment was carried out in the Constitution but the provision was never brought into force. Since Parliament has enacted the said constitutional provision and as such the provision stands as the part of Constitution; and therefore, unless it is omitted by a Constitution Amendment Act by Parliament, it will continue to sit in the Constitution. On the need for formal repeal, the Law Commission, in its One Hundred and Forty-eighth Report on "Repeal of Certain Pre-1947 Central Acts", has observed that "the statutes, unlike human beings, do not die a natural death, with the possible exception of statute whose life is pre-determined by the Legislature at the time of their enactment. A statute, unless it is expressly enacted for a temporary period, survives until it is killed by repeal. To this extent, statutes enjoy immortality." Therefore, it is necessary to omit the said provision to ward of any future doubts about GST.

(iii) After Clause 17(b)(i), **add:**

Entry 53 shall be omitted

(iv) Further amend entry 54 to add between “alcoholic liquor for human consumption,” and “but not including sale” the words: and tobacco and tobacco products and sale and consumption of electricity,

(v) Further amend Clause 17(b)(iv) to read as follow:

2.110 “Entry 62. Taxes on entertainment and amusements and any other taxes, duties, tolls, levies, or royalties devolved by State legislatures to institutions of local self-government under articles 243 H and 243 X to the extent levied, collected and appropriated by a Panchayat or a Municipality or a Regional Council or a District Council”.

Views of the Government

2.111 Inclusion of electricity under GST has not been envisaged ever since the First Discussion Paper was published in 2009 on GST. Neither the Empowered Committee, nor the Parliamentary Standing Committee ever recommended inclusion of electricity under GST. Taxes on electricity and water have been treated separately from taxes on other goods and services in the Constitution. Entry 53 of List II (State List) deals with taxes on sale or consumption of electricity, and this entry is not being touched by the Constitution (122nd Amendment) Bill, 2014.

2.112 Further, in the case of alcohol, the States have been consistently opposing the inclusion of alcohol under GST. Even in the First Discussion Paper, it had been recommended that alcohol be excluded from GST. This is also as per the recommendations of the Empowered Committee.

2.113 Under the proposed Constitution scheme, the Centre has the power to tax one demerit good (tobacco), while the States have the power to tax the other demerit good (alcohol). Tobacco, unlike alcohol has been subsumed in GST, and

the States will have the right to levy SGST on it. This arrangement was specifically recommended in this light where alcohol, being the other demerit good, has not been subsumed into GST, and States retain the powers to levy excise duty as well as sales tax on alcohol. Centre has no powers *vis-à-vis* alcohol.

Views of the Government

2.114 As regards petroleum and petroleum products, the views of the Department have been recorded while dealing with the proposed Article 279A (5).

2.115 In their written replies, the Department of Revenue stated that all forms of Entry Tax have been subsumed under GST by omitting Entry 52 of List II (State list) of Seventh Schedule. The Parliamentary Standing Committee had recommended Entry tax to be subsumed under GST. At the same time, a Constitutional commitment has also been given to the States that their losses caused due to introduction of GST would be compensated for five years. The Department has also mentioned that provision of Entry tax is an impediment to creation of common market, which is a goal of GST, as it acts like a tariff barrier on movement of goods into a local area and discriminates between goods produced within and outside the area. It impedes free movement of goods and also increases compliance cost for business.

Views of the Stakeholders

Clause 17 (b) (ii) in List II-State List

2.116 For Entry 54, the following entry shall be substituted, namely:-

“54. Taxes on the sale of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel, tobacco and tobacco products and alcoholic liquor for human consumption, but not including

sale in the course of inter-State trade or commerce or sale in the course of international trade or commerce of such goods.";

2.117 State Governments may be allowed to levy higher taxes on tobacco and tobacco products; betting and Gambling activity may be kept out of the purview of GST; retain Entry 52 and Omit Entry 55; Insert a new Entry 54A "other polluting goods and services to be notified by GST Council.

2.118 Clause 17 (b) (iii) in List II-State List

2.119 "55. Taxes on advertisement other than advertisements published in the newspapers and advertisements broadcast by radio or television,"

Electricity

2.120 Electricity must form an integral part of the GST base, as is any other normal good. It is therefore suggested that electricity duty also be subsumed within the GST framework. This approach can reduce the cost of electricity by 20%, significantly enhancing the competitiveness of our domestic manufacturing sector.

2.121 The GST need not be a full replacement of the electricity duty. Only a part of the duty can be replaced by GST, which should be fully creditable to industrial/commercial users of electricity.

2.122 Given that Article 246A empowers the Union and States impose GST, notwithstanding anything contained in articles 246 and 254, GST can be extended to electricity even if Entry 53 in List II – State List (Taxes on the consumption or sale of electricity) is not omitted. Continuing this entry would allow States the flexibility to levy a supplementary tax to electricity in addition to GST, if they consider it necessary or desirable.

Real Estate

2.123 Real Estate merits inclusion in GST from another significant perspective, i.e., to bring transparency to the sector. Real estate is known to be the breeding ground of corruption. Bringing this sector into GST will significantly reduce tax evasion through more efficient transactions tracking and improved enforcement and compliance.

2.124 For inclusion of real Estate in the GST base, the definition of ‘goods and services tax’ under Clause 14 of the Bill should be broadened to include property, movable or immovable as suggested below.

2.125 Given the practice in other jurisdictions to levy supplementary taxes in the form of land transfer taxes, levy stamp duties, and registration fees on real property transactions, the existing entries in the Union and State Lists relating to these taxes on land and buildings can be left unchanged. The tax rates and base for these levies can be adjusted (including reducing them to zero) as per the recommendations of the GST.

Alcohol

2.126 Any explicit restrictions on the application of GST to alcohol in the Constitution itself are thus not appropriate. Accordingly, a change in the definition of GST in Article 366(12A) is recommended.

2.127 Alcohol should be given the same treatment as is being given to Petroleum and its products. In that case, the clause ‘except taxes on the supply of the alcoholic liquor for human consumption’ would have to be deleted from the definition of GST at Clause 12A of the Bill. Further, as has been done in the case of Petroleum and its products, the levy of GST on Alcohol may be postponed to a later date to be decided by the GST council. Till that time, the States will continue to levy State Excise duty and State VAT on Alcohol. The advantage would be that no further amendment of the Constitution would be needed, when the States agree to bring in Alcohol within GST at a later date.

Entertainment Tax

2.128 The Bill proposes that local levies such as octroi and entry taxes should be fully subsumed under the GST. This is necessary to ensure free flow of goods and services within the common market of India. This is equally true of the entertainment tax. The funding needs of the local bodies can be better addressed through vertical devolution of State GST revenues to local bodies, as opposed to such nuisance taxes which are difficult to administer and comply with, and do not yield much revenue. The quantum of revenues earned by local bodies from entertainment tax levied and collected by them is insignificant and constitutes a miniscule fraction of their budgets. For smaller towns and cities, the revenues from the tax might not cover even the cost of administration and enforcement.

2.129 It is recommended that Entry 62 in List II – State List be omitted.

Entry 84

2.130 List I Union List, the powers of the Union to levy supplementary taxes on petroleum and tobacco are limited to excise on the manufacture or production of these goods. By contrast, the powers of States for levy of supplementary taxes extend to purchase or sale of the specified products. It is desirable that the Union powers also be likewise extended to sale or purchase of the specified goods.

2.131 Purchase Tax/Entry Tax/Octroi are to be allowed as input Tax credit.

Recommendation

2.132 The Committee is of the view that the entry in the list II- State List empowers the State Government to make laws in respect of the subjects mentioned therein. The Committee is also of the considered view that taxes on electricity and water have been treated separately from taxes on other goods and services in the Constitution. Entry 53 of the List II (State List) deals with taxes on sale or consumption of electricity, and this entry is not being touched by the Constitution (122nd Amendment) Bill, 2014. The

Committee also noted the rationale for the provisions relating to alcohol for human consumption and tobacco as provided by the Department of Revenue. Hence, the clause has been adopted with no change.

Clause 18

2.133 Sub-clause (1) of this clause seeks to provide that an additional tax on supply of goods, not exceeding one per cent in the course of inter-State trade or commerce shall, notwithstanding anything contained in clause (1) of article 269A, be levied and collected by the Government of India for a period of two years or such other period as the Goods and Services Tax Council may recommend, and such tax shall be assigned to the States in the manner provided in clause (2).

2.134 Sub-clause (2) of this clause seeks to provide that the net proceeds of additional tax on supply of goods in any financial year, except the proceeds attributable to the Union territories, shall not form part of the Consolidated Fund of India and be deemed to have been assigned to the States from where the supply originates.

2.135 Sub-clause (3) of this clause seeks to provide that the Government of India may, where it considers necessary in the public interest, exempt such goods from the levy of tax under clause (1).

2.136 Sub-clause (4) of this clause seeks to provide that Parliament may, by law, formulate the principles for determining the place of origin from where supply of goods take place in the course of inter-State trade or commerce.

2.137 Some Members of the Committee proposed to delete this clause because under clause 19, 100 percent compensation be provided for a period not less than five years. In view of guaranteed compensation for any loss incurred by any State or Union Territory, there is no need to levy a market-distorting 1% additional levy.

Views of the Government

2.138 In this regard the Ministry of Finance, Department of Revenue has explained that since GST is a destination based tax, the manufacturing States were apprehensive of their loss in revenues. To allay their fears, and to bring them on board, a provision has been made for the levy of 1% additional tax on the supply of goods. This tax shall be credited to the exporting State. Since it is expected that in the medium and long run, the revenues of all the States would increase due to better compliance and enforcement under GST, this provision of 1% additional tax has been made only for the first two years. The GST Council would have the power to recommend continuation of this tax at the end of 2 years, if it so deems fit. This was decided in view of the consultations with State Finance Ministers by FM on 15.12.2014. It is also in line with the recommendations made by the Empowered Committee in their various meetings for the protection of the revenues of the manufacturing States. Clause 18 in itself does not make any distinction of a “manufacturing state” and this tax shall be levied by all States who send their produce outside the State.

Views of the Stakeholders

- o In place of “An Additional Tax” in Clause 18 (1) and “additional tax” in Clause 18(2), it may be “Central Sales Tax.” Instead of introducing a new additional tax, the same purpose may be served by “Central Sales Tax,” which is already known to the Centre, the States, in industry, trade and others.
- o 1% levy against the spirit of GST.
- o Any specific reference to a period of two years would be arbitrary and unnecessary. The portion, “a period of two years”, may therefore be considered for deletion.
- o It is important to recognize that GST is a destination based tax levied at the point of consumption. Introduction of an additional tax on

supply of goods, not exceeding one per cent for two years would make the tax partly origin based and partly destination based. Allowing continuation of origin based tax system would be a major distortion and continuation of significant tax exportation from the richer producing states to the poorer consuming states.

- o In fact, this method of compensating the manufacturing states through one percent origin based tax is not at all necessary, since in any case the Bill itself envisages compensation by Centre for the states in case of revenue loss. Therefore, the view is that this provision would need to be deleted.
- o Since, the Bill already contains a provision for compensating the States for any losses under GST for five years, it would result in no net revenue gain to the States where they indeed suffer a revenue loss under the GST and are recipient of compensation from the Centre. It would effectively mean an extra profit to the States who gain revenues from the GST. If so, it does not serve its intended purpose. These concerns warrant a removal of the 1% origin based tax.
- o Restricting the levy only to 2 years, with no powers to extend the same for any further period. Restricting levy only to interstate sale and purchase of goods. This means that no such additional tax should be levied on interstate supply of goods otherwise than by way of sale and purchase.

Recommendation

2.139 The Committee feels that the provision of 1% additional tax in its present form is likely to lead to cascading of taxes. Therefore, the Committee strongly recommends that in the concerned GST law, an explanation should be given that for the purpose of Clause 18, the word ‘supply’ would mean:

Supply: "All forms of supply made for a consideration".

Clause 19

2.140 This clause seeks to provide that Parliament may, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for such period which may extend to five years.

In this clause some Members proposed amendments by adding the words “100 per cent” in the second line between “provide for” and “compensation to the States” and by **deleting** “such period which may extend to five years” and **substituting** with “a period not less than five years” **and to insert a new clause in clause 19 that–**

2.141 19(1) To this end, there shall be established a Goods and Services Compensation Fund under the administrative control of the Goods and Services Tax Council into which the Central Government shall deposit the Goods and Services Tax Compensation.

2.142 **By inserting** the words, “as well as the panchayats and Municipalities through States” between the words “to the States” between the words “to the States” and “for the loss of the revenue”

2.143 Further, some of the Members proposed amendments that for the words “Parliament may”, the words “Parliament shall” should be substituted.

2.144 Some Members proposed the addition of the words “as well as the Panchayats and the Municipalities through State Legislatures” so as to ensure the “sound finances” of the local bodies while respecting the Constitutional order that as local bodies are in the State List it is for State Legislatures, by law, to “authorise a Panchayat/Municipality to levy, collect and appropriate” such taxes.

Views of the Government

2.145 Regarding the said amendments the Ministry of Finance, Department of Revenue has stated that it may not be appropriate to stipulate that States would compensate the local bodies for any losses caused to them. 73rd Amendment of the Constitution provides for setting up of State Finance Commissions which have been given responsibility to make recommendations on principles which would govern distribution of finances between the States and local bodies i.e., Panchayats and Municipalities. Deficiencies, if any, in the functioning of State Finance Commissions in individual States may have to be dealt with separately.

2.146 Further, one of the Members proposed amendments that for the words “Parliament may”, the words “Parliament shall” should be substituted.

2.147 Regarding the proposed amendment to substitute the words “for a period of not less than five years”, in place of the words “which may extend to five years”, the Ministry of Finance, Department of Revenue has stated that to bridge the trust deficit with the States, and to ensure no revenue loss to them, it has been Constitutionally provided that the States shall be compensated for five years for their losses caused due to introduction of GST. This has also been recommended by the 14th Finance Commission.

Views of the Government

2.148 Regarding substitution of word 'may' by 'shall', the Legislative Department has clarified that under the Constitution, wherever law making power is conferred on Parliament, the language used is “may” in view of the fact that within the constitutional parameters Parliament is supreme. However, in contrast, wherever, the power to make law is subject to certain contingency, then in such situation like Proclamation of Emergency, the provisions of the Constitution, uses the word “shall”. (as used in article 250 below). In view of this, it may not be necessary to substitute the word "may" with the word "shall"

2.149 In this connection, it would be appropriate to reproduce the provisions of the following articles, namely:—

2.150 “2. Admission or establishment of new States.—Parliament may by law admit into the Union, or establish, new States on such terms and conditions as it thinks fit.

2.151 Formation of new States and alteration of areas, boundaries or names of existing States.—Parliament may by law—

(a) form a new State by separation of territory from any State or by uniting two or more States or parts of States or by uniting any territory to a part of any State....

2.152 Art 245. Extent of laws made by Parliament and by the Legislatures of States.—(1) Subject to the provisions of this Constitution, Parliament may make laws for the whole or any part of the territory of India, and the Legislature of a State may make laws for the whole or any part of the State.

2.153 Art 247. Power of Parliament to provide for the establishment of certain additional courts.—Notwithstanding anything in this Chapter, Parliament may by law provide for the establishment of any additional courts for the better administration of laws made by Parliament or of any existing laws with respect to a matter enumerated in the Union List.

2.154 Art 250. Power of Parliament to legislate with respect to any matter in the State List if a Proclamation of Emergency is in operation.—(1) Notwithstanding anything in this Chapter, Parliament shall, while a Proclamation of Emergency is in operation, have power to make laws for the whole or any part of the territory of India with respect to any of the matters enumerated in the State List.

2,155 Art 368. Power of Parliament to amend the Constitution and procedure therefor.— (1) Notwithstanding anything in this Constitution, Parliament may in exercise of its constituent power amend by way of addition, variation or repeal

any provision of this Constitution in accordance with the procedure laid down in this article.”.

2.156 On the issue of period of GST Compensation, Department has stated that:-

"It is expected that the revenues of the Central and State Governments will not be impacted in the long run. However, due to a shift from origin-based to destination-based indirect tax structure, some States might face drop in revenue in the initial years. To help the States in this transition phase, a number of provisions have been incorporated in the Bill as enumerated in Para I, points (a) to (e), above. In the medium and long run, the revenues of all States and Centre are expected to grow due to widening of tax base, better tax compliance and enforcement, and growth in the economy".

2.157 Further, the smaller and weaker States will benefit from GST from the start. Since these are primarily consuming States, all SGST collected on goods and services will flow to the consuming States under the GST regime. Hence, the revenue of these States will increase and they are not likely to suffer any loss even during initial years.

Views of the Stakeholders

- Parliament shall, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for a period not less than five years.
- In place of “protection to,” it may be ‘protection of 100 percent to’. This will provide required comfort fully to the States and shield against anxiety during the initial phase of introduction of GST.
- On the basis of past experience, the need for timely payment of compensation, without delay, in every financial year.

- As the Bill made a provision for compensation in the event of revenue loss to the States after the introduction of GST, on the recommendations of the GST council, for such period which may extend to five years, this should provide comfort to the States. Since Union government eventually by law would be committed to compensation for revenue loss, it may be proper to eliminate tax on interstate supply of goods as proposed in the new Bill during the first two years of GST regime to introduce a destination based tax system.
- Having agreed to give compensation, there is no harm in Centre agreeing to give 100% compensation for all five years, in case of loss of revenue; – that would raise the comfort level of the States, and bridge the evident trust-deficit between Centre and the States.

2.158 **In view of the clarifications given by the Legislative Department, the Committee feels that there is no justification for substitution of the word ‘may’ with ‘shall’.**

2.159 **Having regard to the concerns expressed by the various States and some of the Members of the Committee in their submissions made before the Select Committee, the Committee recommends amendment in clause 19. The amended clause 19 should read as follows:**

“19. Parliament may, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for the loss of revenue arising on account of implementation of the Goods and Services Tax for a period of five years.”

Clause 20

2.160 This clause seeks to provide for transitional provisions which provides that notwithstanding anything in this Act, any provision of any law relating to tax on goods or services or on both in force in any State immediately before the

commencement of this Act, which is inconsistent with the provisions of the Constitution as amended by this Act shall continue to be in force until amended or repealed by a competent Legislature or other competent authority or until expiration of one year from such commencement, whichever is earlier.

2.161 This clause prescribe a timeframe within which the subsuming of different indirect taxes into GST would take place and enable the competent Legislature to amend or repeal their existing laws to pave the way for imposition of SGST in the States.

Recommendation

2.163 This clause has been adopted with no change.

Clause 21

2.164 This clause seeks to provide that if any difficulty arises in giving effect to the provisions of the Constitution as amended by this Act (including any difficulty in relation to the transition from the provisions of the Constitution as they stood immediately before the date of assent of the President to this Act to the provisions of the Constitution as amended by this Act), the President may, by order, make such provisions, including any adaptation or modification of any provision of the Constitution as amended by this Act or law, as appear to the President to be necessary or expedient for the purpose of removing the difficulty.

2.165 However, no such order shall be made after the expiry of three years from the date of such assent. It also seeks to provide that every order made under sub-clause (1) shall, as soon as may be after it is made, be laid before each House of Parliament.

Recommendation

2.166 This clause has been adopted with no change.

CHAPTER -III

OTHER RELATED ISSUES IN CONTEXT OF THE BILL

3.1 The Committee, thereafter, discussed plethora of inter-connected issues like source of revenue of Panchayats and Municipalities, Losses to Municipalities on account of deletion of Entry 52, creation of National Compensation Fund, non-functioning of State Finance Commissions, provision of Dispute Settlement Authority, inclusion of enabling clause to bring alcohol at a later stage to avoid constitutional amendment, GST Rate and Revenue Neutral Rate (RNR), etc. which have been dealt separately in the succeeding paras.

Issue of Legislative Competence

3.2 Concerns were raised before the Committee on the adverse impact which the Constitution (122nd Amendment) Bill, 2014, may have on the finances of local bodies.

3.3 *Competence of States to authorize local bodies to levy, collect and appropriate taxes, duties, tolls and fees*

3.4 The Constitution makes elaborate provisions to deal with powers, authority and responsibilities of Panchayats, their power to impose taxes and Constitution of Finance Commission to review their financial position (articles 243G, 243H and 243-I). Similar provisions exist in case of Municipalities (articles 243W, 243X

and 243Y). These provisions speak of powers, functions, responsibilities, power to levy and collect tax by Panchayats and Municipalities. The powers to levy and collect taxes is delegated by State Legislatures by enacting law for the purpose and thus enabling them to perform the Constitutional functions and duties entrusted to them.

3.5 Articles 243H and 243X speak of power that the State Legislatures may give to Panchayats and Municipalities to levy collect and appropriate taxes, duties, tolls and fees and also of assigning such of them as are levied and collected by the State Government and to provide grants-in-aid from the Consolidated fund of the States.

3.6 From the provisions, it may be seen that the State's power to levy taxes is derived from the Constitution and the Panchayats and Municipalities power to tax is derived from the State Legislature which it would delegate in the manner Constitution permits. Those articles make it clear that the concerned State Legislature has to pass a law to confer taxing power on Panchayats and Municipalities. Further, it may be seen that the source of power rests with State Legislatures and the Constitution has not empowered the Panchayats and the Municipalities to impose taxes on their own. In the present set up there are State laws which enable the Panchayats and Municipalities to levy and collect the taxes.

3.7 In conclusion, it can be submitted that the provisions of articles 243H and 243X bestow a Constitutional obligation and responsibility on the State to enable revenue generation of Panchayats and Municipalities by enacting laws; which shall continue to apply when the States get the simultaneous power to levy GST under the proposed article 246A once the indirect taxes are subsumed into GST. The present Constitutional Amendment also requires enactment of State laws on the basis of Model GST Laws recommended by the GST Council and while making such laws States would abide by the Constitutional provisions relating to Panchayats and Municipalities.

Subsuming of Entry 52 under GST

3.8 Thereafter, the Committee discussed the rationale for deletion of Entry 52, State List and its possible impact on the revenue sources of the local bodies. Entry 52, State List provides for “Taxes on the entry of goods into a local area for consumption, use or sale therein.”

3.9 The Committee felt that municipal-level taxes are an important source of revenue for many local bodies. If, we take the example of city of Mumbai, municipalities’ main source of revenue is octroi. The revenue collection in 2014-15 on octroi in the city of Mumbai was somewhere around Rs. 6733 crores which is individually around 42% of the entire finance generated there. If that is taken away how development would be ensured. Although the Government of India is assuring that compensation would be given to State Governments for the losses incurred by them but that too would be through State Government.

3.10 In his submission, Secretary, Department of Revenue stated that ‘Entry tax is an impediment to the free flow of goods and services in India. It creates inefficiencies in the supply chain. Further, in many States, Entry tax is not VATable, and hence, results in compounding and cascading of taxes. Therefore, 13th Finance Commission headed by Dr Vijay Kelkar, had recommended that Entry tax should be fully subsumed under GST. The same view was endorsed by the Standing Committee on Finance, while examining the Constitutional 115th Amendment Bill, 2011. Keeping that in mind, in the proposed Bill, a provision of “floor rate with bands” has been made, under which the States may levy additional SGST within the band to raise additional resources for passing on to the local bodies.

Impact of subsuming of Entry Tax on the financial independence of local bodies

3.11 He further stated that ‘It has been seen that Entry tax in lieu of octroi or Octroi is only collected by local bodies in Maharashtra. Most States like Gujarat,

Karnataka, and Punjab already levy and collect Entry tax for distribution to local bodies. As stated above, under the GST regime, provision of “floor rate with bands” has been provided in the Bill which shall enable the States to raise additional resources through levy of additional SGST within the band, for passing it on to the local bodies.

3.12 Since Mumbai is the largest beneficiary of revenue collected from octroi, the case of Mumbai has been presented in detail. All other local bodies in the country are not so dependent on Entry tax or octroi for their revenue. In their 2015-16 budget, the Municipal Corporation of Greater Mumbai (MCGM) has estimated that they would earn about Rs. 7900 crores from octroi, out of a total revenue income of Rs. 19,255 crores, or about 41%. The other sources of revenue for MCGM are property tax, receipts from development plan, various user fees and charges, etc, which are not being affected by the Constitutional Amendment, and will continue to accrue to MCGM.

3.13 Further, in their 2015-16 budget, the MCGM has identified that they would need to introduce new taxes such as property tax on slums, transport cess, conservancy cess and fire cess. Incidentally, Mumbai is expected to yield very high revenues from service tax to the State of Maharashtra. It is open to the State to devolve suitable amount there from to the MCGM. Further, under Articles 243 H and 243 X of the Constitution, the State Government can also empower the local bodies to collect certain other levies such as profession tax or other taxes in the State List in the concerned Jurisdiction.

Devolution of funds to the local bodies by the State Government

3.14 The issue of devolution of funds to the local bodies and Municipalities by the respective State Government engaged the attention of the Committee from the day the Bill was referred to the Select Committee. Apprehensions and concerns were expressed from all quarters, even after the clarifications given by the Department of Revenue and Legislative Department, that the bodies which were

actually doing the work at the ground level may find it difficult to cope up with their requirements in the post GST era. Concerned over the availability of funds to them, several points were raised i.e how much funds would be allocated to them, how it would be done, whether the funds would ultimately be passed on to them, whether the amount so received would be enough to run their day today activities, there has to be a mechanism in the Bill to protect their interests, how constitutional provisions related to them would be protected and taken care of, etc. otherwise these bodies where actual activity is done would be at the sheer mercy of the Governments in their States. Here, the role of the State Finance Commissions becomes all the more important because while submitting their report they have to give due impetus to this fact that these bodies may not be deprived of their legitimate right guaranteed by the Constitution of India

3.14 The Committee felt that there is no question at all that the concerned State Governments have to devolve funds to the local bodies for their smooth functioning, and in order to do that they have to accept the recommendations of the State Finance Commissions, but what concerned most of the Members was that, either the State Finance Commissions are non-existent or even when they exist their recommendations were not followed in right spirit/ accepted. So, ultimately the local bodies suffer and this in turn hampers the various development works to be undertaken by them.

3.15 In his clarifications, Secretary Revenue stated that Constitution 73rd Amendment provides for setting up of State Finance Commissions which have been given responsibility to make recommendations on principles which would govern distribution of finances between the States and local bodies i.e. Panchayats and Municipalities. Deficiencies, if any, in the functioning of State Finance Commissions in individual States may have to be dealt with separately.

Recommendation

3.16 The Committee feels that the concerns expressed by all the Members of the Committee related to local bodies and Municipalities are not

unwarranted. Based on the years of experience and being witnessed to their work in their respective constituencies they were of the view that their interest needs to be protected. The same view was also endorsed by nearly all the stakeholders who have either submitted their memorandum or appeared before the Committee on the Bill.

3.17 But, at the same time we may not forget that the Constitution of India clearly defines the ambit under which the Centre and each of the State has to function. Any encroachment into the State List would disturb the whole system and could strain the Centre-State relations.

3.18 The Committee feels that although the issues raised by the Members to protect and preserve the interest of local bodies are valid, it would not be appropriate for the Committee to advise, recommend and guide the State Governments what they have to do with regard to the interests of the local bodies.

3.19 As per the provisions of the Bill, while the Parliament would pass law relating to CGST, every State Government has to pass a similar law relating to SGST. Hence, while drafting the SGST, the role of the drafters and the concerned State Governments becomes all the more important as they have a duty to protect the revenue sources of the Panchayats, Municipalities, etc, enshrined under Constitution of India. The Committee also feels that here the role of the GST Council is also very important, because while recommending to the Centre and State Governments for subsuming of the taxes, cesses and surcharges levied by the Union, the States and the local bodies in the goods and services tax under article 279 (4) (a), it may also ensure protection of revenue sources of local bodies under provisions of article 279 (4) (c) and (h).

3.20 In the light of the above, the Committee feels that in a cooperative federalism, each unit of it interacts cooperatively and collectively resolves their problems by taking appropriate action at their end. On the same

analogy, Government at the helm of the affairs is duty bound both morally and constitutionally to protect the interest of local bodies by giving them suitable space of functioning and power to levy and generate taxes for their day today functioning. Having full faith in our Constitution from where each tier of the Government draws its powers, the Committee believes that all the State Governments would enact laws on the basis of Model GST Laws recommended by the GST Council and while making such laws States would abide by the constitutional provisions relating to Panchayats and Municipalities.

3.21 Concerned about the very existence and survival of local bodies, the Committee feels that Local government is a State subject figuring as item 5 in List II of the Seventh Schedule to the Constitution. Article 243 G of the Indian Constitution enshrines the basic principle for devolution of power to the local bodies. In the nation's journey towards becoming an economic power, local bodies play an important part in enabling infrastructure availability to the citizens. Local bodies are institutions of the local self governance, which look after the administration of an area or small community such as villages, towns, or cities. The local bodies in India are broadly classified into two categories. The local bodies constituted for local planning, development and administration in the rural areas are referred as Rural Local Bodies (Panchayats) and the local bodies, which are constituted for local planning, development and administration in the urban areas are referred as Urban Local Bodies (Municipalities) and the Constitution of India gives protection to them through various articles, so while drafting the SGST laws due consideration should also be given to this fact. In that backdrop, the Committee strongly recommends that while drafting the SGST laws due consideration to the third tier of the Government as has been guaranteed by the Constitution be given and provisions of devolution of taxes to the local bodies be made.

3.22 The Committee is perturbed to know that State Finance Commissions (SFC) in some of the States are either non-existent or even when exist their recommendations were not accepted by the respective State Governments. The Committee understands that each tier of the Government draws its powers through the Constitution and there is a clear demarcation of fields through List I, II and III within which each tier has to function. Any encroachment by any of them would paralyze the whole system and defeat the very foundation of our Constitution. Hence, the Committee while not venturing into the domain of the State List desires that for the betterment of our States in general and country in particular it would be prudent to abide by the recommendations of the SFCs.

Creation of National Compensation Fund

3.23 The issue of creation of National Compensation Fund on the lines of National Calamity Fund also engaged the attention of the Committee. One of the Members opined that once the Government of India has decided to compensate the State Governments for any losses incurred by them after the introduction of GST, it would be judicious enough to make National Compensation Fund be part of the Bill. This would act as a confidence building measure and allay their fears as well to a great extent. The Standing Committee on Finance had in their report recommended for creation of such fund.

3.24 In their response, Secretary, Department of Revenue stated that to bridge the trust deficit of the States vis-à-vis the Centre, and to ensure that there is no revenue loss to them, a provision has been made in the Bill to provide compensation to States through a Central Legislation for loss of revenue arising on account of implementation of GST for a period which may extend up to five years on the recommendation of GST Council.

3.25 He further stated that as noted by the Fourteenth Finance Commission, GST Compensation would be a temporary feature, and hence, there is no need to create

a GST Compensation Fund through Constitutional Amendment. It is therefore proposed to consider creation of a GST Compensation Fund through Central Legislation.

Recommendation

3.26 Endorsing the view envisaged by Fourteen Finance Commission, the Committee feels it would be wise to keep the GST Compensation Fund out of the purview of the Bill as has been done in the present case, because it is a temporary component and that too only for five years.

Dispute Settlement Authority

3.27 Some of the Members were of the opinion that disputes arising out of the recommendations of the GST Council will be decided by a system to be evolved by GST Council. They were of the view that as the principles of natural justice hold that a party to a dispute cannot be a judge in its own cause, leaving disputes to be settled in accordance with the directives of the GST Council would be tantamount to allowing all disputes, which would necessarily involve one or more members of the GST Council as judges in disputes to which they are party.

3.28 With regard to the Dispute Settlement Authority, the Ministry of Finance (Department of Revenue) clarified that the States were apprehensive that the earlier proposed GST Dispute Settlement Authority under proposed new Article 279B will have powers of overriding the supremacy of the Parliament and the State Legislatures and will, thus, affect the fiscal autonomy of the States. The Parliamentary Standing Committee had, therefore, recommended that proposed Article 279B be omitted. On the recommendations of the Parliamentary Standing Committee on Finance and the Empowered Committee, it was decided to delete this provision, and instead, clause (11) in the proposed Article 279A was inserted to enable the GST Council to decide the modalities to resolve disputes arising out of its recommendations.

3.29 In the proposed Bill, every State would enjoy one vote in the GST Council. Thus there would be no possibility of ‘crowding out’ of small States in the GST Council.

Recommendation

3.30 The Committee feels that each and every State is being represented in the GST Council by their Revenue/Finance/Taxation Minister. Be it a small State or a big State, in the GST Council, all of them enjoy equal status and power to cast one vote. In the event of difference, it can very well be presumed that the GST Council will try to evolve consensus on contentious issues before going for casting of votes, as all the States are members of the Council. Thus, modality to resolve any differences internally lies with the Council. If any Dispute Settlement Authority is created separately it will certainly hamper the functioning of the GST Council in general and Legislatures (Parliament and States) in particular. Thus, it would be judicious not to have a separate and distinct authority having far reaching powers and which could preempt and supersede the powers of Parliament and State Legislatures in the long run.

3.31 The Committee also feels that when concept of Empowered Committee (EC) was coined for the first time, it may not have been presumed how it would function, whether it would serve the purpose for which it would be created, how States would be represented/heard, how issues would be taken up and resolved, etc. But experience has shown that the faith with which the concept of EC was coined has actually delivered. Empowered Committee headed by one among the State Finance/ Revenue Ministers of all States deliberate meticulously on each of the issues raised by its Members and with the passage of time it had taken the shape of arbitration centre where disputes related to them or between two or many States are raised, deliberated and settled amicably without any arbitration charges or fees borne by the disputant States. It would not be over exaggeration of facts if the Committee would say that on the one hand EC had worked as a forum

where any issue of State importance could be raised and on the other hand it had gained the confidence of States in solving their problems and allaying their fears. Such confidence building measure had been initiated by the EC that it could well be termed as a forum where disputes are settled broadly with consensus.

Benefit to Consumers

3.32 GST will largely eliminate cascading of taxes and this will benefit the consumers because manufacturers, traders and service providers are expected to be forced to pass on the benefit to ultimate consumers due to operation of market forces and competition. Simplification and automation under GST regime will reduce transaction cost, improve compliance and transparency and will curb undue rent seeking and profiteering in the long run. Such efficiency gains are expected to have beneficial effects on prices which will also ultimately benefit the consumers.

Results of studies conducted in other countries like Australia, Canada and New Zealand on the impact of GST on consumer prices

3.33 Ministry of Finance (Department of Revenue) in their written submission before the Committee stated that ‘Results of studies conducted in other countries cannot be directly applied to the Indian economy as India is at a different stage of development and has its own unique features. A study by National Council of Applied Economic Research (NCAER) commissioned by the Thirteenth Finance Commission has projected that after introduction of GST, the overall price levels will go down due to more efficient allocation of factors of production. It also projects that introduction of GST would lead to GDP growth in the range of 0.9 to 1.7 percent and export growth of between 3.2 and 6.3 percent’.

Recommendation

3.34 The Committee feels that it would be too early to presume as to whether the price levels will go down or up in the post GST era. What has to be seen and watched by the Government with eyes open is whether the

benefit, if any, arises would certainly be passed on to the consumers or not. Hence, the Committee feels that at the most if price stability is achieved it would serve the very purpose of GST in the entire country as inflation, nowadays has not left even a single field untouched.

Role of Financial Institutions in post GST era

3.35 The Committee was of the considered opinion that concerns of the Financial Institutions must be given due weightage as their views would be equally important as those expressed by other stakeholders in forming an opinion on the Bill.

3.36 In that backdrop, the Committee interacted with the representatives of various Financial Institutions during its study visit to Chennai, Kolkata and Mumbai. When the question was raised by the Committee as to whether the financial institutions were willing to play the role of nodal bank, receive the CGST and SGST and act as a 'clearing house' for the tax, all the financial institutions expressed their willingness to do so. The public Sector Banks informed the Committee that they should given a greater role under GST. The Committee asked the financial institutions to submit their written views on it.

3.37 In response thereto, the views received from United Bank of India and State Bank of India are as under:-

United Bank of India

3.38 GSTN which is a special purpose vehicle set up under u/s 125 of the Companies Act to provide IT infrastructure and service support to the Central and State Governments for implementation of GST has shareholders other than Government of India and State Government, three Banks, viz. ICICI Bank HDFC Ltd., HDFC Bank constitute 30% of the total shareholding of the company. No public sector bank is a stakeholder in the company. As the bulk of tax collection is undertaken by public sector banks, including State Bank of India, we hereby

submit to kindly consider inducting at least one of the public sector banks as stakeholder in the GSTN. However, if the same is not possible due to any administrative reason, at least a representation of public sector bank should be given in the Board of GSTN.

Since the fee earned on services being provided by the banks to customer may also be covered under the proposed GST, we submit before the Committee that filing of return and deposit of GST so collected be made applicable in the centralized manner as is being currently done by the Bank while levying service tax on the fees earned on services rendered to the customer.

State Bank of India

3.39 (i) Financial services are exempt from GST/VAT in almost all countries. However, In India, service tax is leviable on fee based services provided by the banks and financial institutions. Presently, the tax is applicable on all fee based activities including the services provided to weaker section of society, whose accounts were opened for financial inclusion to achieve the social goal of the Government. Retail transactions, in terms of volume, constitute more than 90% in banks. The value of service for most of these transactions does not exceed Rs. 100/- considering the larger goal of the Government, it is requested that GST should not be applicable on services rendered to retail depositors. In case the Government wishes to levy GST on such services, some abatement may be considered so that the cost of services to retail customers does not go up, as GST rate is likely to be substantially higher than the present service tax rate. This will go a long way in continuing with affordable banking services to all.

3.40 (v) Considering the huge network of branches/ATM and also considering the complexities involved, we request that banks should be permitted to have a single registration and discharge GST liability centrally and credits of SGST should be available across States.

3.41 (xi) Newspaper reports that the GST rate is likely to be 20-22% as against service tax rate of 14%. Considering that in most of the countries, banking

services are outside GST, the increase in the tax rate will further increase the cost of banking services. This results into cost of doing business to be much higher in India as compared to other competing countries. To be internationally competitive, the GST rate for banking industry should be minimum and in no case should it be more than what is being levied today.

3.42 We request that the best practices followed internationally may be followed and banking services are kept outside GST. If this is not possible then, interest, trading in securities and foreign currency and services to retail customers should not be liable to GST and suitable provision should be there to avail of CenVAT credit of input services taken to provide activities involved in such services. Further, single registration coupled with IGST provision should be made available to enable CenVAT credit for consumers of banking services.

Recommendation

3.43 The Committee feels GSTN shall play a crucial role in implementation of GST as it shall provide the IT infrastructure for implementation of GST. It noted that Non Government shareholding of GSTN is dominated by private banks. This is not desirable because of two reasons . Firstly, public sector banks have more than 70% share in total credit lending in the country. Secondly, GSTN's work is of strategic importance to the country and the firm would be a repository of a lot of sensitive data on business entities across the country. In light of above, the Committee strongly recommends that Government may take immediate steps to ensure Non Government financial institution shareholding be limited to public sector banks or public sector financial institutions.

3.44 Endorsing the views of the SBI, the Committee having same feeling as the bank recommends that the best practices followed internationally may be followed and if possible banking services may be kept outside GST. Furthermore, if this is not possible then, interest, trading in securities and foreign currency and services to retail customers should not be liable to GST

and suitable provision should be there to avail of CenVAT credit of input services taken to provide activities involved in such services. Further, single registration coupled with IGST provision should be made available to enable CenVAT credit for consumers of banking services.

3.45 The Committee is of the considered opinion that if the GST rate is more than the service tax rate of 14%, the increase in the tax rate will further increase the cost of banking services. This results into cost of doing business to be much higher in India as compared to other competing countries. Therefore, the Committee recommends that to be internationally competitive, the GST rate for banking industry should be minimum.

3.46 On a point raised during the meetings about the differential treatment to alcoholic liquor for human consumption, efforts made to encourage manufacturing activity and Floor Rates with Bands, the Department of Revenue in their written submission stated that:

Treatment of alcoholic liquor for human consumption

3.47 Only alcoholic liquor for human consumption has been excluded from the ambit of GST Constitutionally. All other forms of alcohol like alcohol for industrial use and medicinal and toilet preparation containing alcohol which falls in the taxing domain of the Central Government have been included in GST. This exclusion has been done to address the strong concern of the states regarding loss of revenue if potable alcohol was to be subsumed under GST.

Incentives to State Government to encourage manufacturing activities

3.48 The very nature of GST has features to incentivize manufacturing activity. As GST is a destination based consumption tax, higher the consumption of goods and services in a state, higher would be tax collection. It is well known that higher level of manufacturing activity results in a host of ancillary benefits such as creation of more jobs, higher earnings and higher standard of living, all of which

encourage higher consumption of goods and services within the state leading to higher tax collection.

Floor Rates with Bands

3.49 To give flexibility to the States, the provision of ‘bands’ over the GST floor rates, to be recommended by the GST Council, has been introduced. Depending on the local situations and requirements, the States have the option to levy slightly higher tax within this band.

GST Rate

3.50 I. On the aforesaid issue, experts in their written comments stated the following:

3.51 Once the enabling framework is created for the levy of GST, the next most crucial step in its implementation is the determination of the tax base and tax rate. This issue has been discussed in detail in the “Report of the Task Force on GST” that was submitted to the 13th Finance Commission. The Report recommends a broad base for the GST, and a combined Centre and State revenue neutral rate of 12%.

3.52 A broad base and moderate rate is an essential feature of a good tax system. Multiplicity of tax rates is also to be avoided. A majority of the VAT/GST system introduced in the last three decades embrace these features. For example, VAT/GST in New Zealand is levied on a comprehensive base at a single rate of 12.5% (at inception), in Singapore at 3%, Japan at 3%, Australia at 10%, South Africa at 16%, and Malaysia at 6% (most recent, implemented in 2015). Levy of GST on a comprehensive base makes it an economically efficient and productive source of revenue. In each of the examples cited, the revenue yield as a percent of GDP is estimated to be 0.5% or more for each percentage point of the GST rate. In New Zealand, the GST yield was the highest, at 0.74% of GDP (i.e., 12.5% GST was yielding revenues in excess of 9% of GDP).

3.53 The Centre and State revenues in India to be replaced by GST are a little less than 6% of GDP. The international benchmark revenue productivity of 0.5% of GDP yields a target revenue neutral rate for India of less than 12%. In their view, this remains a realistic option for India, which would be politically appealing, catalyse voluntary compliance, and provide a significant boost to investment and economic growth. While the tax base and rates are to be decided by the GST Council, the Bill should not create any barriers to levy of such a tax, i.e., it should allow the levy of tax to the broadest possible base.

GST Rate – it must not be inflationary

3.54 II. In terms of the proposed Article 279A (4)(e), the GST Council shall make recommendations to the Union and the States on ‘the rates including floor rates with bands of goods and services tax’. The GST rate is a very important factor in earning the trust of the tax payers. Howsoever efficient the GST machinery may be, the tax-payers won’t welcome GST happily if the GST rate is kept high because that will lead to high inflation. Even in developed countries like Australia and Canada, GST was opposed by the poorer sections of the taxpayers because of high GST rate.

GST and Revenue Neutral Rate (RNR)

3.55 The GST rate would normally be based on the Revenue Neutral Rate (RNR). In the present circumstances, the RNR is expected to be high because Petroleum and its products and Alcohol have been kept out of GST and consequently, the tax base would shrink. But, a high GST rate in line with high RNR would definitely lead to high inflation. India cannot afford to have high inflation at this stage of the economy. Therefore, it is submitted that **not to go strictly by the RNR while fixing the GST rate**. The newspaper reports suggested first a RNR of around 27%, and later it was reported to be somewhere between 20 and 23%. Internationally, GST rate normally varies between 16 to 20%, with exceptions like Australia at 10%, New Zealand at 15%, Japan at 8%,

Germany at 23% and Malaysia at 6%. France has four rates, the highest 20% and lowest 2.1%, while UK has two rates 20% and 5%. To start with, **India's GST rate should not go beyond 20% for standard rate and perhaps 14% for reduced rate.**

Recommendation

3.56 The Committee feels that although the GST Council has been entrusted with the task of fixing the rate including floor rates with bands in mutual consent with other State Governments who are part and parcel of the Council. But implementation of GST in other countries has shown GST rate is a very important factor in earning the trust of the consumers. If the GST rate is kept high, it will surely erode the confidence of the consumers badly and may lead to high inflation. Therefore, the Committee is of the considered view that while fixing the rate, the GST Council may opt for a broad base and moderate rate as it is an essential feature of a good tax system and as far as possible multiplicity of tax rates may be avoided.

Non-Interference in the State Governments powers stated in Concurrent List

3.57 The issue as to whether the proposed Article 246A intends to interfere in the State Governments powers mentioned under in the Concurrent List was also raised during the meeting of the Committee held on 3rd July, 2015. Replying to the Query, the Secretary, Department of Revenue informed the Committee that *“GST is a composite tax. Both the Centre and the States will have the power to levy it. Therefore, a separate specific provision is being made in Article 246A to enable both the Parliament and the State Legislatures to enact a proposal to levy and collect this tax. In no way this is diluting the powers of the States.”* This will in no way interfere with the powers of the States under the Concurrent list.

IT Preparedness

3.58 Building IT infrastructure and developing IT services through GSTN: Central and State Governments have jointly registered Goods and Services Tax Network (GSTN) as a not-for-profit, non-Government Company to provide shared IT infrastructure and services to Central and State Governments, tax payers and other stakeholders for implementation of GST. GSTN was incorporated in March 2013. GSTN is working on creating a GST portal and related ICT infrastructure together with an interface with State IT systems. To support the States, GSTN will prepare the necessary software for front-end modules which would include Registration and Returns. GSTN would also prepare back end processing modules like assessment, audit, etc. which would be required by the various States. In case the States want to develop their own software for backend modules, they shall be free to do so and in case they want to use the backend modules prepared by GSTN, they shall be provided the same.

3.59 The Committee was given to understand that an 'As-Is' Study was conducted by the NSDL to assess the capacities of the existing State IT systems and operational procedures, and to identify gaps with respect to the envisaged GST system. It is also expected that development of IT infrastructure and services is to complete by March, 2016.

3.60 The Committee is aware that Goods and Services Tax Network (GSTN) a not-for-profit, non-Government Company has been jointly set up by the Central and State Governments and it will provide shared IT infrastructure and services to the Central and State Governments, tax payers and other stakeholders. Further, it is expected that GSTN would complete the development of IT infrastructure and services by March, 2016 i.e. exactly one month before the date from which the Government of India intends to implement it throughout the country.

3.61 Apprehensions related to level of IT preparedness have been expressed at various fora together with concerns related to its implementation. There are many questions to be answered and many more will arise at the time of its implementation and how it is to be linked with the system available with states,

but at the very same time what has to be seen is its long lasting benefits that would accrue to the nation in the years to come.

3.62 The Committee feels that together with IT preparedness, training would be a crucial element to look for. Our is a society where most of the population is not techno savvy and there would be hitch in using it by those who are at the helms of affairs. Hence, to overcome all these apprehensions it would be imperative to impart training to the personnel's at all levels and at the very onset so that their fear about its usage, implementation, affects, etc may be removed and results in building their confidence in doing or performing various tasks.

Recommendation

3.63 **In that backdrop, the Committee recommends that all out effort should be made to improve upon the IT preparedness of the States, so that the apprehensions related to its level of preparedness may gets addressed. For its smooth implementation, the Committee immediately recommends implementation of comprehensive training programmes at all levels to allay the fears of consumers, stakeholders, organisations, etc. A message should go loud and clear to all that we as a country are ready to adopt tax reform of unparallel nature. The Committee also recommends that for having no discernible blemishes in the implementation of GST, it is imperative that not only IT preparedness is at very high level but also prerequisites like IT infrastructure, unified tax credit clearing mechanism, etc may be put in place for its implementation.**

Apprehension among State Governments

3.64 Many State Governments/UTs either submitted their written views or appeared before the Committee on the Bill. Doubts clubbed with apprehensions of numerous types were raised and brought to the notice of the Committee. Apprehensions were cast over the losses in revenue and their sources after the implementation of Goods and Services Taxes in India. Similarly, there were apprehensions relating to/ demands from all corners that whether States may be

empowered to levy higher taxes on tobacco and tobacco products, 100% compensation for a period of 5 years should be given, Abrupt deletion of entry 52 from the state list may financially cripple the local bodies, Flexibility may be given to the states to fix SGST rates as per their needs from time to time, to protect the revenue of the local bodies special category states may be allowed to levy entry tax, Inclusion of petroleum products in the present bill with the safeguard that it shall be operationalised on the recommendation of GST Council on a date later than five years, In clause 19 of the Bill, instead of the words “for such period which may extend to five year” words “for a period not less than five years” may be replaced. Similarly, for the words “Parliament may” the words “Parliament shall” be substituted, Amend the entry 62 to read it as under 62 taxes on entertainment, betting and gambling”. Similar demands in respect of Entertainment, Amusement, Betting & Gambling that proposed Amendment by way of insertion of clause 16 (e) be omitted, Taking into consideration of adverse impact on environment, proposes for levy of an additional non-rebatable cess subject to suitable framing of guidelines, “Taxes on food grains contributed by the States to National Food Grains Pool subject to any limitations imposed by Parliament by law”, etc.

Recommendation

3.65 Having heard the views of the main stakeholders i.e. State Governments/UTs, the Committee feels that States are like the arteries of the India and if the arteries find themselves choked the whole body will fall. Hence, for the sake of our survival, what needs to be done is to protect and preserve our arteries. Based on that analogy, the Committee feels that although the apprehensions brought to the notice of the Committee are not unwarranted but due care have been taken constitutionally to overcome any constraints come in their way. All these initiatives ushered by the Government of India having been evolved and brought in the form of current Bill are based on the views expressed in the Empowered Committee meetings. To allay the fear of all State Governments in general and manufacturing

states in particular, safeguards like 1% additional tax on supply of goods, compensation to States/UTs for losses in the revenue, States have been given the voting weightage of 2/3rd , decision in GST Council to be arrived at by the majority of not less than 3/4th , etc on the recommendation of the GST Council have been provided. More so, all this has been done constitutionally so that there may not be any doubt in the minds of the States/UTs.

3.66 Therefore, the Committee feels due consideration has been given by the Government of India to the aforesaid apprehensions raised by the States/UTs while coming forward with this comprehensive Constitutional Amendment Bill. The Committee feels that apprehensions cast over the introduction of goods and services taxes are early hiccups and with the introduction of it, the States/UTs would realise that they have many more options available to them to generate and augment their revenue source. Survival of the Union is on the States, the Committee close by saying that would the body (Centre) survive if arteries get choked, so vibrancy of the States comes first for the survival of the Centre.

THE CONSTITUTION (ONE HUNDRED AND TWENTY-SECOND
AMENDMENT) BILL, 2014

AS REPORTED BY THE SELECT COMMITTEE
No.- of 2015

	THE CONSTITUTION (ONE HUNDRED AND FIRST AMENDMENT) BILL, 2015 [Words underlined indicate the amendments suggested by the Select Committee and asterisks indicate omissions]	
	A BILL	
	<i>further to amend the Constitution of India.</i>	
	BE it enacted by Parliament in the Sixty-sixth Year of the Republic of India as follows:—	
	1. (1) This Act may be called the Constitution (One Hundred -----Amendment) Act, 2015.	Short title and commencement.
	(2) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint, and different dates may be appointed for different provisions of this Act and any reference in any such provision to the commencement of this Act shall be construed as a reference to the commencement of that provision.	
	2. After article 246 of the Constitution, the following article shall be inserted, namely:—	Insertion of new article 246A.
	"246A. (1) Notwithstanding anything contained in articles 246 and 254, Parliament, and, subject to clause (2), the Legislature of every State, have power to make laws with	Special provision with respect to goods and services tax.

	respect to goods and services tax imposed by the Union or by such State.	
	(2) Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce. <i>Explanation.</i>—The provisions of this article, shall, in respect of goods and services tax referred to in clause (5) of article 279A, take effect from the date recommended by the Goods and Services Tax Council."	
	3. In article 248 of the Constitution, in clause (1), for the word "Parliament", the words, figures and letter "Subject to article 246A, Parliament" shall be substituted.	Amendment of article 248.
	4. In article 249 of the Constitution, in clause (1), after the words "with respect to", the words, figures and letter "goods and services tax provided under article 246A or" shall be inserted.	Amendment of article 249.
	5. In article 250 of the Constitution, in clause (1), after the words "with respect to", the words, figures and letter "goods and services tax provided under article 246A or" shall be inserted.	Amendment of article 250.
	6. In article 268 of the Constitution, in clause (1), the words "and such duties of excise on medicinal and toilet preparations" shall be omitted.	Amendment of article 268.
	7. Article 268A of the Constitution, as inserted by section 2 of the Constitution (Eighty-eighth Amendment) Act, 2003 shall be omitted.	Amendment of article 268A.
	8. In article 269 of the Constitution, in clause (1), after the words "consignment of goods", the words, figures and letter "except as provided in article 269A" shall be inserted.	Amendment of article 269.
	9. After article 269 of the Constitution, the following article shall be inserted, namely:—	Insertion of new article 269A.

	"269A. (1) Goods and services tax on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council. <i>Explanation.</i>—For the purposes of this clause, supply of goods, or of services, or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-State trade or commerce.	Levy and collection of goods and services tax in course of inter-State trade or commerce.
	(2) Parliament may, by law, formulate the principles for determining the place of supply, and when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce."	
	10. In article 270 of the Constitution,—	Amendment of article 270.
	(i) in clause (1), for the words, figures and letter "articles 268, 268A and article 269", the words, figures and letter "articles 268, 269 and article 269A" shall be substituted;	
	(ii) after clause (1), the following clause shall be inserted, namely:—	
	"(1A) The goods and services tax levied and collected by the Government of India, except the tax apportioned with the States under clause (1) of article 269A, shall also be distributed between the Union and the States in the manner provided in clause (2)."	
	11. In article 271 of the Constitution, after the words "in those articles", the words, figures and letter "except the goods and services tax under article 246A," shall be inserted.	Amendment of article 271.
	12. After article 279 of the Constitution, the	Insertion of new

	following article shall be inserted, namely:—	article 279A.
	'279A. (1) The President shall, within sixty days from the date of commencement of the Constitution (One Hundred ----- Amendment) Act, 2015, by order, constitute a Council to be called the Goods and Services Tax Council.	Goods and Services Tax Council.
	(2) The Goods and Services Tax Council shall consist of the following Members, namely:—	
	(a) the Union Finance Minister Chairperson; (b) the Union Minister of State in charge of Revenue or Finance.....Member; (c) the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government.....Members.	
	(3) The Members of the Goods and Services Tax Council referred to in sub-clause (c) of clause (2) shall, as soon as may be, choose one amongst themselves to be the Vice-Chairperson of the Council for such period as they may decide.	
	(4) The Goods and Services Tax Council shall make recommendations to the Union and the States on— (a) the taxes, cesses and surcharges levied by the Union, the States and the local bodies which may be subsumed in the goods and services tax; (b) the goods and services that may be subjected to, or exempted from the goods and services tax; (c) model Goods and Services Tax Laws, principles of levy, apportionment	

	of Integrated Goods and Services Tax and the principles that govern the place of supply; (d) the threshold limit of turnover below which goods and services may be exempted from goods and services tax; (e) the rates including floor rates with bands of goods and services tax; (f) any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster; (g) special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand; and (h) any other matter relating to the goods and services tax, as the Council may decide.	
	(5) 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.	
	(6) While discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.	
	(7) One half of the total number of Members of the Goods and Services Tax Council shall constitute the quorum at its	

	meetings.	
	(8) The Goods and Services Tax Council shall determine the procedure in the performance of its functions.	
	(9) Every decision of the Goods and Services Tax Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the Members present and voting, in accordance with the following principles, namely:— (a)the vote of the Central Government shall have a weightage of one-third of the total votes cast, and (b)the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast,in that meeting.	
	(10) No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of— (a)any vacancy in, or any defect in, the constitution of the Council; or (b)any defect in the appointment of a person as a Member of the Council; or (c)any procedural irregularity of the Council not affecting the merits of the case.	
	(11) The Goods and Services Tax Council may decide about the modalities to resolve disputes arising out of its recommendations."	
	13. In article 286 of the Constitution,—	Amendment of article 286.
	(i)in clause (1),— (A)for the words "the sale or purchase of goods where such sale or purchase takes place", the words "the supply of goods or of	

	services or both, where such supply takes place" shall be substituted; (B)in sub-clause (b), for the word "goods", at both the places where it occurs, the words "goods or services or both" shall be substituted; (ii)in clause (2), for the words "sale or purchase of goods takes place", the words "supply of goods or of services or both" shall be substituted; (iii)clause (3) shall be omitted.	
	14. In article 366 of the Constitution,—	Amendment of article 366.
	(i)after clause (12), the following clause shall be inserted, namely:— '(12A) "goods and services tax" means any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption;'; (ii)after clause (26), the following clauses shall be inserted, namely:— '(26A) "Services" means anything other than goods; (26B) "State" with reference to articles 246A, 268, 269, 269A and article 279A includes a Union territory with Legislature;'.	
	15. In article 368 of the Constitution, in clause (2), in the proviso, in clause (a), for the words and figures "article 162 or article 241", the words, figures and letter "article 162, article241 or article 279A" shall be substituted.	Amendment of article 368.
	16. In the Sixth Schedule to the Constitution, in paragraph 8, in sub-paragraph (3),— (i)in clause (c), the word "and" occurring at	Amendment of Sixth Schedule.

	the end shall be omitted; (ii)in clause (d), the word "and" shall be inserted at the end; (iii)after clause (d), the following clause shall be inserted, namely:— "(e) taxes on entertainment and amusements."	
	17. In the Seventh Schedule to the Constitution,—	Amendment of Seventh Schedule.
	(a)in List I — Union List,— (i)for entry 84, the following entry shall be substituted, namely:— "84. Duties of excise on the following goods manufactured or produced in India, namely:— (a)petroleum crude; (b)high speed diesel; (c) motor spirit (commonly known as petrol); (d)natural gas; (e) aviation turbine fuel; and (f) tobacco and tobacco products."; (ii)entries 92 and 92C shall be omitted;	
	(b)in List II — State List,— (i) entry 52 shall be omitted; (ii) for entry 54, the following entry shall be substituted, namely:— "54. Taxes on the sale of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption, but not including sale	

	in the course of inter-State trade or commerce or sale in the course of international trade or commerce of such goods."; (iii)entry 55 shall be omitted; (iv)for entry 62, the following entry shall be substituted, namely:— "62. Taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council."	
	18. (1) An additional tax on supply of goods, not exceeding one per cent. in the course of inter-State trade or commerce shall, notwithstanding anything contained in clause (1) of article 269A, be levied and collected by the Government of India for a period of two years or such other period as the Goods and Services Tax Council may recommend, and such tax shall be assigned to the States in the manner provided in sub-section (2).	Arrangement for assignment of additional tax on supply of goods to States for two years or such other period recommended by Council.
	(2) The net proceeds of additional tax on supply of goods in any financial year, except the proceeds attributable to the Union territories, shall not form part of the Consolidated Fund of India and be deemed to have been assigned to the States from where the supply originates. (3) The Government of India may, where it considers necessary in the public interest, exempt such goods from the levy of tax under sub-section (1). (4) Parliament may, by law, formulate the principles for determining the place of origin from where supply of goods take place in the course of inter-State trade or commerce. (5) For the purposes of this section, "State" shall have the meaning assigned to it in clause (26B) of article 366 of the Constitution.	

	19. Parliament may, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for a* period **** of five years.	Compensation to States for loss of revenue on account of introduction of goods and services tax.
	20. Notwithstanding anything in this Act, any provision of any law relating to tax on goods or services or on both in force in any State immediately before the commencement of this Act, which is inconsistent with the provisions of the Constitution as amended by this Act shall continue to be in force until amended or repealed by a competent Legislature or other competent authority or until expiration of one year from such commencement, whichever is earlier.	Transitional provisions.
	21. (1) If any difficulty arises in giving effect to the provisions of the Constitution as amended by this Act (including any difficulty in relation to the transition from the provisions of the Constitution as they stood immediately before the date of assent of the President to this Act to the provisions of the Constitution as amended by this Act), the President may, by order, make such provisions, including any adaptation or modification of any provision of the Constitution as amended by this Act or law, as appear to the President to be necessary or expedient for the purpose of removing the difficulty: Provided that no such order shall be made after the expiry of three years from the date of such assent. (2) Every order made under sub-section (1) shall, as soon as may be after it is made, be laid before each House of Parliament.	Power of President to remove difficulties.

**RAJYA SABHA SELECT COMMITTEE ON THE GOODS AND SERVICES
TAX**

**NOTE OF DISSENT BY
MADHUSUDAN MISTRY, MANI SHANKARAIYAR, BHALCHANDRA
MUNGEKAR**

New Delhi, 20 July 2015

We are in favour of a Goods and Services Tax that is simple and comprehensive. The Constitution (122nd) Amendment Bill, 2015 is neither. It is pitted with compromises, exclusions and exceptions that make it impossible for us to extend our support to the Bill in the absence of the amendments we have proposed being incorporated in the Bill, as drafted at present.

First, to ensure that GST rates are moderate and reasonable and do not impose an unfair burden on consumers, particularly poor consumers, it is necessary that a ceiling rate be specified in Article 246A so that, in the pursuit of higher revenues, the GST Council desists from crossing the ceiling. We have proposed a ceiling of 18% as a reasonable, moderate, adequately revenue-generating GST rate.

Second, we find the proposal to levy an additional 1% tax to be market-distorting, especially in view of the fact that we have proposed 100% compensation for a minimum of five years to States that might lose revenues. Further, in our view, the compensation should be deposited in a GST Compensation Fund, under the administrative control of the GST Council, as proposed by the Standing Committee on Finance

Third, the single most crucial word in the Bill is "supply lies", which is used in clause 9 and clause 18 without being defined. We have, therefore, sought to amend clause 9 through two provisos to article 269 (A) to clarify that goods moving from one unit to another unit of a firm in

different States under the same ownership, or when two or more firms are collaborating in units located in different States for the manufacture of the same end-product, should be excluded from the term "supply Isupplies". This would also apply to the same term used in clause 18. However, representatives of the Government have failed to define this term in the Committee on the ground that three governmental committees are engaged in defining the term in preparing Bills fro GST, SGST and IGST. We believe that a Select Committee of the Rajya Sabha cannot be subordinated to bureaucratic committees and that it would not be proper for the Select Committee to commend a draft Constitution amendment to Parliament without a proper agreed definition of this key term.

Fourth, given that the fundamental aim of GST is to establish a common market for the whole country, we are unable to support a GST Bill that excludes indefinitely from the purview of the GST tobacco and tobacco products, alcohol for human consumption and electricity supply and consumption. We propose that all three be included in clause 12 of the Constitution amendment bill with the condition that the GST Council take a decision for their inclusion in GST within a period of five years.

Fifth, we cannot support a GST Council that is unduly weighted in favour of the Centre. In the interests of true "cooperative federalism", the share of the States in voting in the GST Council must be enhanced to 75% and the share of the Centre brought down to 25%.

Sixth, we cannot support a Bill that transgresses the elementary principle of law that parties to a dispute cannot be judges in their own cause. The failure to incorporate a GST Disputes Settlement Authority, as was provided

for in the 2011 Bill, is a serious lacuna that must be filled. The GST Council, comprising members who will necessarily be party to any dispute relating to the implementation of GST, must be supplemented and reinforced with a GST Disputes Settlement Authority in toto as provided for in the 2011 Bill.

Seventh, the sources of revenue of the Panchayats and Municipalities, as provided for in Parts IX and IXA of the Constitution, must be safeguarded and they must be assured of their due share in the revenue buoyancy that is expected to arise from the enactment and implementation of the GST. It is only with such assurance, through the amendments we have suggested in this regard to the Bill, that we might find it possible to support the proposed legislation.

Eighth, special consideration might be given by the GST Council to any State or Union territory, with or without a Legislature, such as Goa and Puducherry, whose population does not exceed twenty lakh.

Further, we strongly protest the failure to include in the Report of the Committee the detailed rationale for the various amendments we have moved to the Constitution (One Hundred and Twenty Second) Amendment Bill, 2015, while providing ample space for the Government to explain its rationale. Accordingly, we attach in the Annexure to this Note of Dissent the amendments we have moved to the draft Report of the Select Committee.

This Note of Dissent is submitted in view of the failure of the Select Committee to take our points adequately into account.

..L;

117 ~

911\r6}J.EYJ

~

(Madhusudan Mistry) Mani Shankar Aiyar (Bhalchandra Munekar)

Annexe

to

Note of Dissent submitted by
Madhusudan Mistry, Mani Shankar Aiyar and Bhalchandra Mungekar

**Text of amendments to the draft Report submitted by
Madhusudan Mistry, Mani Shankar Aiyar, Bhalchandra Mungekar**

Clause 2

Paragraph 5.4

In the third line, after "concerned" and before "the Ministry of Finance"
add:

"the members moving the amendment stressed the need to keep GST rates moderate and reasonable so that consumers, particularly poor consumers, are not excessively burdened, and to this end proposed that the GST Council be bound by the Constitution to not exceed 18% as the rate for an adequately revenue-generating GST. They clarified that there is the precedent of a specific rate of taxation provided for

in article 276(2) as also in clause 18 of the Bill before the committee."

Clause 9

Paragraph 32.3A

Add new paragraph to read as follows:

"These members rejected the argument made by Government representatives that as the definition of the term was being decided by three government committees working on GST, SGST and IGST there was no need to define the term in the Constitution, stating that a Select Committee of Parliament cannot be subordinated to ongoing work of governmental committees and, therefore, it would be improper to commend a Bill to Parliament that did not adequately define so crucial a term as "supply /supplies".

Clause 12

Paragraph 35.3A

Add new paragraph to read as follows:

Some members proposed that under clause 4(c), among the "principles" to be considered by the GST Council while preparing GST laws the principle of "share of local bodies in revenue buoyancy and compensation for losses sustained through taxes subsumed" should be included as articles 243H and 243X provide for State Legislatures to, by law, ensure the "sound finances" of the local bodies. This would also enable State Finance Commissions set up under articles 243 I and 243 Y to provide for augmenting the share of local bodies in revenue buoyancy generated by the adoption of GST.

Paragraph 35.38

Add a new paragraph to read as follows:

With reference to sub-clause (4) (g) which provides for "special consideration" to certain States, some members proposed, in keeping with article 243B (2), that "special consideration" may also be extended to States like Goa and Union territories like Puducherry by adding at the end of 4(g) "and any State or Union territory having a population not exceeding twenty lakhs". This proposal was made in response to the specific request of Goa and Puducherry to be given special consideration in view of their small size and limited sources of revenue.

Paragraph 35.4

Amend the last sentence to read: "These items have been kept out of GST **for the present** to protect the revenue interest of the States"

Paragraph 35.4A

Add the following paragraph to read as follows:

Some members sought the inclusion in clause 12(5) of highly revenue-generating products like tobacco and tobacco products, alcohol for human consumption and electricity supply and consumption within a period not later than five years so that India, within a few years, fulfills the fundamental GST objective of making

the entire nation a single common market for all products.

Clause 13

Paragraph 39.3A

Add the following new paragraph to read as follows:

Some members sought the definition in the Constitution amendment Bill itself of the term "supply" in proposed clause I(A) of article 286

Clause 14

Paragraph 40.1

Add at the end of the draft sentence the words: "so as to progressively ensure a true common market for all goods"

Paragraph 40.2

Add at the end of the draft sentence the words: "so as to avoid the circular definition of ,services' meaning 'anything other than goods'."

Clause 16

Paragraph 46.1

Amend the opening line to read as follows: "With a view to progressively promoting a common market in all goods and services," before "Some members"

Paragraph 46.2

Add at the end of the present draft sentence the following words: "as it does not figure in the Constitution?"

Paragraph 46.8A

Add the following new paragraph:

Some members did not accept Government's views as set out under paragraphs 46.6, 46.7 and 46.8 as the overarching objective of GST is to progressively render India a common market for all goods and services, including so-called 'demerit' goods. If a higher rate of tax has to be imposed on such goods, the GST Council may be authorised to do so.

Clause 18

Paragraph 52.5

Add at the end of the draft sentence the following words: "because these members have proposed that, under clause 19, 100 percent compensation be provided for a period not less than five years. In view of guaranteed compensation for any loss incurred by any State or Union territory, there is no need to levy a market-distorting 1% additional levy"

Clause 19

Paragraph 53.4A

Add the following new paragraph:

Some members proposed the addition of the words: ", as well as The Panchayats and The Municipalities through State Legislatures" so as to ensure the "sound finances" of the local bodies while respecting the Constitutional order that as local bodies are in the State List it is for State Legislatures, by law, to "authorise a Panchayat/Municipality to levy, collect and appropriate" such taxes. They held that a mere recommendation to this effect by the Select Committee would not be binding in the sense that an appropriate provision in the Constitution would be.

Chapter IV

Dispute Settlement Authority

Paragraph 62.1

Amend the second sentence to read as follows:

They were of the view that as the principles of natural justice hold that a party to a dispute cannot be a judge in its own cause, leaving disputes to be settled in accordance with the directives of the GST Council would be tantamount to allowing all disputes, which would necessarily involve one or more members of the GST Council as judges in disputes to which they are party.

A.
NAVANEETHAKRISHNAN.
ME'~BER OF PARLIAMENT
(RAJYA SABRA)

9, OLD TAMIL NADU HOUSE,
UTIL YA MARG,
ANAKYAPURI, NEW DELHI.

LEADER,
AIADMK PARTY IN RAJYA SABHA.
DELHI,

NEW

21.07.2015.

The Hon'ble Chairman,
Select committee on Constitution (One Hundred and Twenty -
Second Amendment) Bill,2014, Rajya Sabha, New Delhi

Resected Sir, Vanakkam,

A Dissent Note by AIADMK party on the report of
the Select Committee on the Constitution (One Hundred
and Twenty-Second Amendment) Bill,2014 is submitted after
having gone through the report.

Than
king
You,

Yours Sincerely,

~~eaJ~VO)I'~
(A. NAVANEETHAKRISHNAN)

**DISSENT NOTE BY AIADMK PARTY ON THE REPORT OF
THE SELECT COMMITTEE ON THE CONSTITUTION
(ONE HUNDRED AND TWENTY-SECOND AMENDMENT)
BILL, 2014**

The views of the AIADMK Party on the Constitution (One Hundred and Twenty-Second Amendment) Bill, 2014 on Goods and Services Tax (GST) passed by the Lok Sabha on 6th May, 2015, and which is presently under consideration of the Select

Committee by the Rajya Sabha, are in consonance with the letters dated 17.8.2014 and 19.12.2014 addressed by our Leader and the Hon'ble Chief Minister of Tamil Nadu to the Hon'ble Prime Minister and the letter dated 10.9.2014 addressed to the Union Finance Minister, in so far as they impinge upon the fiscal autonomy of States, and are as follows: -

I. PROVISIONS RELATING TO GOODS AND SERVICES TAX COUNCIL:

GST Council as a constitutional body impinges on the legislative sovereignty of both Parliament and the State Legislatures.

It also completely jeopardizes the autonomy of the States in fiscal matters. In spite of our repeated objections, the present Bill also envisages the formation of the GST Council. We strongly object to the provision for the GST Council.

Ideally it should not exist. The existing mechanism of the Empowered Committee of State Ministers which dealt with VAT issues is adequate. No statutory GST Council is required.

Furthermore, the decision making rule and voting weightage in the proposed Council are completely unacceptable. They give the Government of India an effective veto in the GST Council and no distinction is sought to be made amongst the States in weightage. Hence, if at all a Council is formed, the weightage of the vote of the Central Government should be reduced to **one-**

fourth of the total votes cast and that of the States should be increased to **three-fourths** of the total votes cast. Further, the weightage of each State's vote should be in proportion to the representation of each State in the Council of the States. This is important as the changeover to GST has different implications for different States based on their size and reliance on own tax revenues.

However, the Select Committee has not considered these views on the GST Council and has not recommended appropriate amendments. Hence the AIADMK Party dissents from the report of the Select Committee.

II. PROVISIONS RELATING TO PETROLEUM AND PETROLEUM PRODUCTS:

Petroleum and Petroleum products, which are currently outside the purview of State VAT in most States, are proposed to be covered under GST in the Constitution Amendment Bill though the date on which such tax will be levied on these products has been left to the recommendation of the GST Council. Bringing these products under the ambit of GST will entail huge revenue loss to the States as Input Tax Credit will have to be provided eventually. Further, there is no guarantee that GST will not be prematurely imposed on these products. Hence, considering the limited revenue resources of the State, as has been repeatedly insisted upon by our Leader, the Hon'ble Chief Minister of Tamil Nadu Puratchi Thalaivi Amma, Petroleum and Petroleum products should be totally kept outside GST.

However, the Select Committee has not considered these views on the provisions relating the petroleum and petroleum products and has not recommended appropriate amendments. Hence the AIADMK Party dissents from the report of the Select Committee.

III. PROVISIONS RELATING TO TOBACCO AND TOBACCO PRODUCTS:

States should also be empowered to levy higher taxes on Tobacco and Tobacco products over and above SGST similar to what has been allowed to the Centre.

However, the Select Committee has not considered these views on the provisions relating to tobacco and tobacco products and has not recommended appropriate amendments. Hence the AIADMK Party dissents from the report of the Select Committee.

IV. PROVISIONS RELATING TO ADDITIONAL LEVY OF 10/0 IN THE COURSE OF INTER-STATE TRADE OR COMMERCE:

Manufacturing States like Tamil Nadu stand to permanently lose substantial revenue if GST is implemented, as GST will be based on the destination principle. Though the Bill envisages that an additional tax on supply of goods to the extent of 1% in the course of inter-State trade or commerce for a period of 2 years or such other period as the GST Council may recommend, it also empowers the Government of India to exempt goods from this additional levy of 1%. The Select Committee has recommended that this additional levy of 1 per cent shall be restricted to "all forms of supply made for a consideration".

None of these formulations relating to the levy of 1 per cent additional tax really meet the requirements of a manufacturing State

like Tamil Nadu. **Instead, the States should be permitted to retain 4% of CGST part of the IGST on all inter-State sales/transfer of both goods and services.** This will enable a substantial reduction in the compensation payable to the States. At the same time, since it would come out of the CGST part of the IGST, hence it would not place the destination States at any disadvantage with regard to revenue flow.

However, the Select Committee has not considered these very valid views on the issue of taxation of interstate rate and has not recommended appropriate amendments. Hence the AIADMK Party dissents from the report of the Select Committee.

V. PROVISIONS RELATING TO COMPENSATION OF REVENUE LOSS TO THE STATES:

The Bill provides for Parliament to enact a law to provide for compensation to the States for such period which may extend to 5 years on the recommendation of the GST Council.

The Select Committee has suggested a modification indicating provision of compensation for a period of five years. While this removes the uncertainty regarding the period for which the compensation would be provided, it still falls short of the demands of the States regarding the extent of compensation.

In the 14th Finance Commission's Report it has been recommended that 100% compensation may be provided for the first 3 years, 75% for the 4th year and 50% for the 5th year. In discussions it appears that the Government of India is in line with this view.

However, taking into account the permanent loss that would accrue to the States, the AIADMK party suggests that **1000/0 compensation should be provided for a period of not less than 5 years** and a consensus should be arrived at on the methodology of computation of compensation and the mechanism to administer the compensation. As the Select Committee's report falls short of the expectations of the AIADMK Party we dissent from the report of the Select Committee.

VI. CONSENSUS ON IMPORTANT ISSUES RELATING TO GOODS AND SERVICES TAX:

As our Leader, the Hon'ble Chief Minister of Tamil Nadu has pointed out, it would be appropriate to arrive at a **broad consensus** on a number of other important issues relating to GST like revenue neutral rates, floor rates with bands, commodities to be excluded from GST, IGST model and clarity on dual administrative control before proceeding further with the enactment, so as to allay the genuine fears of the States over loss of fiscal autonomy and permanent revenue loss.

The Select Committee has also gone beyond its brief on the issue of Revenue Neutral Rate (RNR) and recommended that to start with, India's GST rate should not go beyond 20% for standard rate and perhaps 14% for reduced rate. This is a matter for the Empowered Committee of State Finance Ministers/ GST Council on which to take an appropriate view. Hence the AIADMK Party is unable to accept this recommendation in the Select Committee's report.

On behalf of the AIADMK Party, the Select Committee of the Rajya Sabha was requested to duly take into account the above serious concerns relating to the Constitution (One Hundred and Twenty-second

Amendment) Bill, 2014 while finalizing the report of the Committee.

As these views have not been duly considered by the Select Committee, this note may be appended to the Report as a dissent note containing the views of the AIADMK Party.

Dissent Note to the Select Committee Report on Constitution 122nd Amendment (GST) Bill

Some provisions of the Constitution (One Hundred and Twenty Second Amendment) Bill i.e. Goods and Services Tax Bill are likely to adversely impact the federal structure of the country.

There is a need for decentralization of powers and devolution of the taxes in favour of the States and further to the Local bodies. Fiscal Federalism and protection of the powers of the states is important while a frame work is created for a Pan Indian Common Economic Zone and market through goods and services Tax Structure.

The key issue arises in Clause XII of the Bill is the formation of a GST Council. According to the Clause, every decision of the Goods and Services Tax Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the members present and voting, in accordance with the following principles, namely:-

- (a) the vote of the Central Government shall have a weightage of one-third of the total votes cast, and
- (b) the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast. Naturally, the Centre will have enormous power in the GST Council, given its structure prescribed in the Bill. So, the weightage of the Centre in the council should be reduced to at least one-fourth of the total votes cast and that of the States should be increased to at least three-fourth of the total votes cast. The clauses are designed in a way that the Centre will have absolute powers in deciding tax proposals. This is likely to harm the concept of Union and States. It will be turning into a structure of Union alone.

While special provision with respect to the states of Arunachal Pradesh, Assam, Jammu & Kashmir, Manipur, Mizoram, Nagaland,

Sikkim, Tripura, Himachal Pradesh and Uttarakhand is made. Similar provision could have been made in case of Puducherry.

For protecting a particular local brand of MSME product and protecting Agri-based products, for promoting farmers and industry, States should have leverage.

GST should not be in the interest of big corporate houses, who want a free flow of goods and services with the technology promoted and owned by them. With the Centre having an absolute say over the decision making process on the GST, the States will lose its financial independence in the long run and corporate will dictate the policies of even the local Governments. So, these concerns must be given due consideration in the Bill.

21.7.15

(K.N.BALAGOPAL)

Nfia:t4 ~
Div.

(D~~

Div. No. 133

Recommendations/Observations at a Glance

1. **CLAUSE 1 TO CLAUSE 8 : THESE CLAUSES HAVE BEEN ADOPTED WITH NO CHANGE.**
2. **Clause 9 - The Committee feels that since imposition of GST on the supplies of goods and services in the course of inter-State trade would not lead to cascading of taxes, the Clause may be adopted with no change.**
3. **CLAUSE 10 & CLAUSE 11 : THESE CLAUSES HAVE BEEN ADOPTED WITH NO change.**
4. **Clause 12 - After having deliberated on the issue of finances of local bodies, the Committee strongly feels that the revenues of local bodies need to be sustained and protected for ensuring that standards of local governance are maintained. The Committee, thus, strongly recommends that the State Governments take adequate measures to ensure that adequate revenues flow to the local bodies, and their resources are not adversely affected. The Committee noted that Article 243H and 243X contain provisions for State Legislatures to authorize Panchayats and Municipalities to collect and appropriate taxes in the State list. The Committee further noted that Article 243I and 243Y provide for setting up of State Finance Commissions to make recommendations regarding devolution of funds to local bodies. The Committee noted that the above provisions notwithstanding, local bodies find managing their resource requirements quite challenging.**

In light of above, with respect to Article 279A 4(e), the Committee strongly recommends that the word ‘band’ used in the proposed Article may be defined in GST laws. The Committee recommends the following definition of ‘band’:

“Band” : Range of GST rates over the floor rate within which Central Goods and Service Tax (CGST) or State Goods and Services Tax (SGST) may be levied on any specified goods or services or any specified class of goods or services by the Central or a particular State Government as the case may be.

With respect to Article 279A(5), taking note of the provision that inclusion of petroleum products into GST can take place only on recommendation of GST Council which could happen only with the consent of both the Centre and the States, the Committee recommended that the clause be adopted with no change.

The Committee is aware that while discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

In view of the clarifications submitted by the Department of Revenue and Legislative Department, the Committee finds no merit in disturbing the voting pattern proposed in the Bill, as the same has been worked out on a formula where no one is at an disadvantageous or dominating position be it Centre or States. Moreover, under clause 2 Parliament and the Legislature of every State shall have power to make laws with respect to GST simultaneously.

In the GST Council, all the decisions have to be taken collectively by the Centre and States and in order to take decision on any issue 75% votes are necessary. So, in order to strike a fine balance Centre vote share has been kept at 1/3rd and that of the States at 2/3rd. In that backdrop, the Committee recommends that these amendments may not be necessary since our Constitution is a federal Constitution and so, it is necessary to make the provisions providing for a manner

that disallow the dominance of one over the other. Keeping this in view, the voting formula has been worked out. Hence, the clause may be adopted with no change.

The Committee, having noted the point mentioned by the Department of Revenue that the GST Council shall decide only the 'modalities' to resolve disputes, did not agree to recommend inclusion of Article 279B as was proposed in Constitution(115th Amendment) Bill, 2011.

5. Clause 13 - The term 'supply' would be defined in the various GST laws relating to CGST and SGST. Hence, the Committee feels that it would not be appropriate to insert the definition of supply in this clause. This clause has been adopted with no change.

6. Clause 14 - Endorsing the view of the Department, the Committee feels that 'services' has been so defined in order to give it wide amplitude so that all supplies that are not goods can potentially be covered within the ambit of services and no activity remains outside the taxable net. This would also minimize disputes. Further, having noted the points mentioned by the Department of Revenue regarding inclusion of petroleum products under GST, the clause may be adopted with no change.

7. Clause 15 & Clause 16 -These clauses have been adopted with no change.

8. Clause 17- 2.108 Regarding the aforesaid Entry, the Committee is of the view that Entry 92C was inserted by the Constitution (Eighty-Eighth Amendment) Act, 2003 to empower the Union to impose service tax on certain services read with article 268A of the Constitution.

Notwithstanding, the service tax levied under the Finance Act, 1994 were continuing as such. The amendment was carried out in the Constitution but the provision was never brought into force. Since Parliament has enacted the said

constitutional provision and as such the provision stands as the part of Constitution; and therefore, unless it is omitted by a Constitution Amendment Act by Parliament, it will continue to sit in the Constitution. On the need for formal repeal, the Law Commission, in its One Hundred and Forty-eighth Report on “Repeal of Certain Pre-1947 Central Acts”, has observed that “the statutes, unlike human beings, do not die a natural death, with the possible exception of statute whose life is pre-determined by the Legislature at the time of their enactment. A statute, unless it is expressly enacted for a temporary period, survives until it is killed by repeal. To this extent, statutes enjoy immortality.” Therefore, it is necessary to omit the said provision to ward off any future doubts about GST.

The Committee is of the view that the entry in the list II- State List empowers the State Government to make laws in respect of the subjects mentioned therein. The Committee is also of the considered view that taxes on electricity and water have been treated separately from taxes on other goods and services in the Constitution. Entry 53 of the List II (State List) deals with taxes on sale or consumption of electricity, and this entry is not being touched by the Constitution (122nd Amendment) Bill, 2014. The Committee also noted the rationale for the provisions relating to alcohol for human consumption and tobacco as provided by the Department of Revenue. Hence, the clause may be adopted with no change.

9. Clause 18- 2.139 The Committee feels that the provision of 1% additional tax in its present form is likely to lead to cascading of taxes. Therefore, the Committee strongly recommends that in the concerned GST law, an explanation should be given that for the purpose of Clause 18, the word ‘supply’ would mean:

Supply: "All forms of supply made for a consideration".

10. Clause 19 - 2.158 In view of the clarifications given by the Legislative Department, the Committee feels that there is no justification for substitution of the word ‘may’ with ‘shall’.

Having regard to the concerns expressed by the various States and some of the Members of the Committee in their submissions made before the Select Committee, the Committee recommends amendment in clause 19. The amended clause 19 should read as follows:

“19. Parliament may, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for the loss of revenue arising on account of implementation of the Goods and Services Tax for a period of five years.”

11. Clause 20 & Clause 21 : This clause has been adopted with no change.

12. The Committee feels that the concerns expressed by all the Members of the Committee related to local bodies and Municipalities are not unwarranted. Based on the years of experience and being witnessed to their work in their respective constituencies they were of the view that their interest needs to be protected. The same view was also endorsed by nearly all the stakeholders who have either submitted their memorandum or appeared before the Committee on the Bill.

But, at the same time we may not forget that the Constitution of India clearly defines the ambit under which the Centre and each of the State has to function. Any encroachment into the State List would disturb the whole system and could strain the Centre-State relations.

The Committee feels that although the issues raised by the Members to protect and preserve the interest of local bodies are valid, it would not be

appropriate for the Committee to advise, recommend and guide the State Governments what they have to do with regard to the interests of the local bodies.

As per the provisions of the Bill, while the Parliament would pass law relating to CGST, every State Government has to pass a similar law relating to SGST. Hence, while drafting the SGST, the role of the drafters and the concerned State Governments becomes all the more important as they have a duty to protect the revenue sources of the Panchayats, Municipalities, etc, enshrined under Constitution of India. The Committee also feels that here the role of the GST Council is also very important, because while recommending to the Centre and State Governments for subsuming of the taxes, cesses and surcharges levied by the Union, the States and the local bodies in the goods and services tax under article 279 (4) (a), it may also ensure protection of revenue sources of local bodies under provisions of article 279 (4) (c) and (h).

In the light of the above, the Committee feels that in a cooperative federalism, each unit of it interacts cooperatively and collectively resolves their problems by taking appropriate action at their end. On the same analogy, Government at the helm of the affairs is duty bound both morally and constitutionally to protect the interest of local bodies by giving them suitable space of functioning and power to levy and generate taxes for their day today functioning. Having full faith in our Constitution from where each tier of the Government draws its powers, the Committee believes that all the State Governments would enact laws on the basis of Model GST Laws recommended by the GST Council and while making such laws States would abide by the constitutional provisions relating to Panchayats and Municipalities.

Concerned about the very existence and survival of local bodies, the Committee feels that Local government is a State subject figuring as item 5 in List II of the

Seventh Schedule to the Constitution. Article 243 G of the Indian Constitution enshrines the basic principle for devolution of power to the local bodies. In the nation's journey towards becoming an economic power, local bodies play an important part in enabling infrastructure availability to the citizens. Local bodies are institutions of the local self governance, which look after the administration of an area or small community such as villages, towns, or cities. The local bodies in India are broadly classified into two categories. The local bodies constituted for local planning, development and administration in the rural areas are referred as Rural Local Bodies (Panchayats) and the local bodies, which are constituted for local planning, development and administration in the urban areas are referred as Urban Local Bodies (Municipalities) and the Constitution of India gives protection to them through various articles, so while drafting the SGST laws due consideration should also be given to this fact. In that backdrop, the Committee strongly recommends that while drafting the SGST laws due consideration to the third tier of the Government as has been guaranteed by the Constitution be given and provisions of devolution of taxes to the local bodies be made.

The Committee is perturbed to know that State Finance Commissions (SFC) in some of the States are either non-existent or even when exist their recommendations were not accepted by the respective State Governments. The Committee understands that each tier of the Government draws its powers through the Constitution and there is a clear demarcation of fields through List I, II and III within which each tier has to function. Any encroachment by any of them would paralyze the whole system and defeat the very foundation of our Constitution. Hence, the Committee while not venturing into the domain of the State List desires that for the betterment of our States in general and country in particular it would be prudent to abide by the recommendations of the SFCs.

13. Endorsing the view envisaged by Fourteen Finance Commission, the Committee feels it would be wise to keep the GST Compensation Fund out of the purview of the Bill as has been done in the present case, because it is a temporary component and that too only for five years.

14. The Committee feels that each and every State is being represented in the GST Council by their Revenue/Finance/Taxation Minister. Be it a small State or a big State, in the GST Council, all of them enjoy equal status and power to cast one vote. In the event of difference, it can very well be presumed that the GST Council will try to evolve consensus on contentious issues before going for casting of votes, as all the States are members of the Council. Thus, modality to resolve any differences internally lies with the Council. If any Dispute Settlement Authority is created separately it will certainly hamper the functioning of the GST Council in general and Legislatures (Parliament and States) in particular. Thus, it would be judicious not to have a separate and distinct authority having far reaching powers and which could preempt and supersede the powers of Parliament and State Legislatures in the long run.

The Committee also feels that when concept of Empowered Committee (EC) was coined for the first time, it may not have been presumed how it would function, whether it would serve the purpose for which it would be created, how States would be represented/heard, how issues would be taken up and resolved, etc. But experience has shown that the faith with which the concept of EC was coined has actually delivered. Empowered Committee headed by one among the State Finance/ Revenue Ministers of all States deliberate meticulously on each of the issues raised by its Members and with the passage of time it had taken the shape of arbitration centre where disputes related to them or between two or many States are raised, deliberated and settled amicably without any arbitration charges or fees borne by the disputant States. It would not be over exaggeration of facts if the

Committee would say that on the one hand EC had worked as a forum where any issue of State importance could be raised and on the other hand it had gained the confidence of States in solving their problems and allaying their fears. Such confidence building measure had been initiated by the EC that it could well be termed as a forum where disputes are settled broadly with consensus.

15. The Committee feels that it would be too early to presume as to whether the price levels will go down or up in the post GST era. What has to be seen and watched by the Government with eyes open is whether the benefit, if any, arises would certainly be passed on to the consumers or not. Hence, the Committee feels that at the most if price stability is achieved it would serve the very purpose of GST in the entire country as inflation, nowadays has not left even a single field untouched.

16. The Committee feels GSTN shall play a crucial role in implementation of GST as it shall provide the IT infrastructure for implementation of GST. It noted that Non Government shareholding of GSTN is dominated by private banks. This is not desirable because of two reasons . Firstly, public sector banks have more than 70% share in total credit lending in the country. Secondly, GSTN's work is of strategic importance to the country and the firm would be a repository of a lot of sensitive data on business entities across the country. In light of above, the Committee strongly recommends that Government may take immediate steps to ensure Non Government financial institution shareholding be limited to public sector banks or public sector financial institutions.

Endorsing the views of the SBI, the Committee having same feeling as the bank recommends that the best practices followed internationally may be followed and if possible banking services may be kept outside GST. Furthermore, if this is not possible then, interest, trading in securities and foreign currency and services to

retail customers should not be liable to GST and suitable provision should be there to avail of CenVAT credit of input services taken to provide activities involved in such services. Further, single registration coupled with IGST provision should be made available to enable CenVAT credit for consumers of banking services.

The Committee is of the considered opinion that if the GST rate is more than the service tax rate of 14%, the increase in the tax rate will further increase the cost of banking services. This results into cost of doing business to be much higher in India as compared to other competing countries. Therefore, the Committee recommends that to be internationally competitive, the GST rate for banking industry should be minimum.

17. The Committee feels that although the GST Council has been entrusted with the task of fixing the rate including floor rates with bands in mutual consent with other State Governments who are part and parcel of the Council. But implementation of GST in other countries has shown GST rate is a very important factor in earning the trust of the consumers. If the GST rate is kept high, it will surely erode the confidence of the consumers badly and may lead to high inflation. Therefore, the Committee is of the considered view that while fixing the rate, the GST Council may opt for a broad base and moderate rate as it is an essential feature of a good tax system and as far as possible multiplicity of tax rates may be avoided.

Non-Interference in the State Governments powers stated in Concurrent List

18. In that backdrop, the Committee recommends that all out effort should be made to improve upon the IT preparedness of the States, so that the apprehensions related to its level of preparedness may gets addressed. For its smooth implementation, the Committee immediately recommends implementation of comprehensive training programmes at all levels to allay the fears of consumers,

stakeholders, organisations, etc. A message should go loud and clear to all that we as a country are ready to adopt tax reform of unparallel nature. The Committee also recommends that for having no discernible blemishes in the implementation of GST, it is imperative that not only IT preparedness is at very high level but also prerequisites like IT infrastructure, unified tax credit clearing mechanism, etc may be put in place for its implementation.

19. Having heard the views of the main stakeholders i.e. State Governments/UTs, the Committee feels that States are like the arteries of the India and if the arteries find themselves choked the whole body will fall. Hence, for the sake of our survival, what needs to be done is to protect and preserve our arteries. Based on that analogy, the Committee feels that although the apprehensions brought to the notice of the Committee are not unwarranted but due care have been taken constitutionally to overcome any constraints come in their way. All these initiatives ushered by the Government of India having been evolved and brought in the form of current Bill are based on the views expressed in the Empowered Committee meetings. To allay the fear of all State Governments in general and manufacturing states in particular, safeguards like 1% additional tax on supply of goods, compensation to States/UTs for losses in the revenue, States have been given the voting weightage of 2/3rd , decision in GST Council to be arrived at by the majority of not less than 3/4th , etc on the recommendation of the GST Council have been provided. More so, all this has been done constitutionally so that there may not be any doubt in the minds of the States/UTs.

Therefore, the Committee feels due consideration has been given by the Government of India to the aforesaid apprehensions raised by the States/UTs while coming forward with this comprehensive Constitutional Amendment Bill. The Committee feels that apprehensions cast over the introduction of goods and services taxes are early hiccups and with the introduction of it, the States/UTs

would realise that they have many more options available to them to generate and augment their revenue source. Survival of the Union is on the States, the Committee close by saying that would the body (Centre) survive if arteries get choked, so vibrancy of the States comes first for the survival of the Centre.

8. Message from Lok Sabha - Reported

Secretary-General reported to the House, a message from the Lok Sabha informing the Rajya Sabha that the Lok Sabha at its sitting held on the 12th May, 2015, had adopted a Motion informing that the Lok Sabha concurs in the recommendation of the Rajya Sabha that the Lok Sabha do agree to leave being granted to withdraw the Motor Vehicles (Amendment) Bill, 2014, which was passed by the Lok Sabha on the 18th of December, 2014 and laid on the Table of the Rajya Sabha on the 19th of December, 2014.

1-01 p.m.

The House adjourned and re-assembled at 2-01 p.m.

2-01 p.m.

9. Government Bill — Motion for Reference of the Bill to a Select Committee — Adopted.

The Constitution (One Hundred and Twenty-second Amendment) Bill, 2014.

Shri Arun Jaitley, Minister of Finance, Corporate Affairs and Information and Broadcasting, moved the following motion:—

“That the Bill further to amend the Constitution of India, as passed by Lok Sabha, be referred to a Select Committee of the Rajya Sabha consisting of the following Members:—

1. Shri Bhupender Yadav
2. Dr. Chandan Mitra
3. Shri Ajay Sancheti
4. Shri Madhusudan Mistry
5. Shri Mani Shankar Aiyar
6. Dr. Bhalchandra Munekar
7. Shri Naresh Agrawal
8. Shri K. C. Tyagi

9. Shri Derek O'Brien
10. Shri A. Navaneethakrishnan
11. Shri Satish Chandra Misra
12. Shri K.N. Balagopal
13. Shri Dilip Kumar Tirkey
14. Shri C.M. Ramesh
15. Shri Praful Patel
16. Shrimati Kanimozhi
17. Shri Anil Desai
18. Shri Naresh Gujral
19. Mir Mohammad Fayaz
20. Shri D. Raja
21. Shri Rajeev Chandrasekhar

with instructions to report to the Rajya Sabha by the last day of the first week of the next Session.”

2-03 p.m.

The motion was adopted.

2-21 p.m.

10. Statement by Minister

Shri Nitin Jairam Gadkari, Minister of Road Transport, Highways and Shipping, made a statement regarding certain allegations against him made by some Members in the context of a CAG Report laid on the Table of the Rajya Sabha on the 30th of April, 2015

Thereafter, some Members sought clarifications.

2-57 p.m.

The House adjourned and re-assembled at 3-12 p.m.

List of Organisations heard during the visit of the “The Constitution
(One Hundred and Twenty-Second Amendment) Bill, 2014”.

1. Gail (India) Limited
2. Oil India Limited
3. Oil and Natural Gas Corporation
4. Indian Overseas Bank
5. Indian Bank
6. UCO Bank
7. United Bank of India
8. Bank of Baroda
9. State Bank of India
10. Chambre de Commerce
11. Tamil Nadu Vanigar Sangankalin Peramaippu
12. Puducherry Trader's Federation
13. Karaikal Chamber of Commerce
14. Pondicherry Chamber of Industries
15. Tamil Nadu Chamber of Commerce & Industry
16. The Bengal Chamber
17. Tamil Nadu Small & Tiny Industries Association
18. The Tamil Nadu Automobile & Allied Industries Federation
19. The Tamil Nadu Food Grains Merchants Association Ltd
20. Tamil Nadu Chamber Brick Manufacturers Association
21. The Southern India Mills' Association
22. Salem City Chamber of Commerce
23. The Southern India Chamber of Commerce and Industry
24. FICCI
25. All India Federation of Tax Practitioners
26. The Film & Television Producers Guild of India Ltd
27. CII
28. Indian Broadcasting Foundation
29. Advertising Agencies Association of India
30. Express Industry Council of India
31. ASSOCHAM
32. SIAM
33. Indian Foundation of Transport Research and Training
34. All India Confederation of Commercial Taxes Associations

Comparative Study of Select Committee Report & Original 122nd Constitutional Amendment Bill

	Constitution (122nd Amendment) Bill, 2014	Select Committee recommendations, 2015	Notes of Dissent in Committee Report, 2015
GST Council (Clause 12)	- Functions to include: Model GST laws, principles of levy and place of supply, rates including floor rates with bands of GST, apportionment of IGST, etc. - Voting: 3/4th weighted votes, 1/3 weightage to centre & 2/3 to states.	- Define 'bands' (of GST) to include the range of GST rates (over the floor rate) within which CGST and SGST may be levied on specific goods or services or class of goods or services. - Voting: No Changes Proposed	- A statutory GST Council is not required. A body like Empowered Committee of state Finance Ministers is adequate. - A ceiling of 18% must be imposed on GST rates. - Special consideration to be given to states or Union Territories whose population does not exceed 20 lakhs, (ex. Goa or Puducherry). - Voting: States must have 3/4 of the weighted votes, and the centre must have 1/4.
Dispute resolution (Clause 12)	GST Council to decide upon the modalities to resolve disputes.	No Changes Proposed	Separate GST Disputes Settlement Authority, as provided for in the 2011 Bill, must be included.
Definition of Service (Clause 14)	In 26A delete "anything other than goods" & substitute with "Commercial Transaction in Intangibles" so as to avoid the circular definition of 'Service' meaning 'anything other than goods'.	Endorsing the view of the department, the committee feels that 'service' has been so defined in order to give it wide amplitude so that all supplies that are not goods can potentially be covered within the ambit of service and no activity remain outside the taxable net. This would be minimise dispute.	Support the Select Committee recommendation.
Coverage of GST (Clauses 12 and 17)	- Alcoholic liquor for human consumption to be exempt from GST. - GST is to be levied on petroleum crude, high speed diesel, motor spirit, natural gas, aviation turbine fuel at a later date. - GST to be imposed on tobacco. Centre to impose additional levy on tobacco.	No Changes proposed	- Tobacco and tobacco products, alcohol for human consumption, and electricity supply and consumption must be brought within the purview of GST within five years. - States must also be permitted to levy taxes on tobacco. - Petroleum Product to be kept out of GST

Additional Tax (in interstate trade) (Clause 18)	• An additional tax of up to 1% on the supply of goods will be levied by centre in the course of inter-state trade or commerce. • The tax will be assigned to the states from where the supply originates. • This will be for two years, or longer, as recommended by GST Council.	• The 1% additional tax in its present form is likely to lead to cascading of taxes. • Add an explanation to the clause to define "supply" to mean all forms of supply made for a consideration (Clause 13).	• The 1% additional tax is market distorting, especially since 100% compensation for five years to states has been proposed. • Instead of the additional 1% tax, states should be permitted to retain 4% of centre's share of IGST on all inter-state supplies of goods.
Compensation to states (Clause 19)	• Parliament may provide for compensation to states for a maximum period of five years.	• Compensation to be for a five year period.	• 100% compensation to be provided for five years. • Compensation must be deposited in a GST Compensation Fund, under the GST Council.

Bill No. 192 of 2014

THE CONSTITUTION (ONE HUNDRED AND TWENTY-SECOND
AMENDMENT) BILL, 2014

A

BILL

further to amend the Constitution of India.

BE it enacted by Parliament in the Sixty-fifth Year of the Republic of India as follows:—

1. (1) This Act may be called the Constitution (One Hundred and Twenty-second Amendment) Act, 2014.

Short title and
commencement.

(2) It shall come into force on such date as the Central Government may, by notification
5 in the Official Gazette, appoint, and different dates may be appointed for different provisions
of this Act and any reference in any such provision to the commencement of this Act shall
be construed as a reference to the commencement of that provision.

2. After article 246 of the Constitution, the following article shall be inserted, namely:—

Insertion of
new article
246A.

10 "246A. (1) Notwithstanding anything contained in articles 246 and 254,
Parliament, and, subject to clause (2), the Legislature of every State, have power to
make laws with respect to goods and services tax imposed by the Union or by such
State.

Special
provision
with respect
to goods and
services tax.

(2) Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

Explanation.—The provisions of this article, shall, in respect of goods and services tax referred to in clause (5), of article 279A, take effect from the date recommended by the Goods and Services Tax Council.”. 5

Amendment of article 248. 3. In article 248 of the Constitution, in clause (1), for the word "Parliament", the words, figures and letter "Subject to article 246A, Parliament" shall be substituted.

Amendment of article 249. 4. In article 249 of the Constitution, in clause (1), after the words "with respect to", the words, figures and letter "goods and services tax provided under article 246A or" shall be inserted. 10

Amendment of article 250. 5. In article 250 of the Constitution, in clause (1), after the words "with respect to", the words, figures and letter "goods and services tax provided under article 246A or" shall be inserted.

Amendment of article 268. 6. In article 268 of the Constitution, in clause (1), the words "and such duties of excise on medicinal and toilet preparations" shall be omitted.

Omission of article 268A. 7. Article 268A of the Constitution, as inserted by section 2 of the Constitution (Eighty-eighth Amendment) Act, 2003 shall be omitted. 15

Amendment of article 269. 8. In article 269 of the Constitution, in clause (1), after the words "consignment of goods", the words, figures and letter "except as provided in article 269A" shall be inserted.

Insertion of new article 269A. 9. After article 269 of the Constitution, the following article shall be inserted, namely:— 20

Levy and collection of goods and services tax in course of inter-State trade or commerce. “269A. (1) Goods and services tax on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council. 25

Explanation.—For the purposes of this clause, supply of goods, or of services, or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-State trade or commerce.

(2) Parliament may, by law, formulate the principles for determining the place of supply, and when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.”. 30

Amendment of article 270. 10. In article 270 of the Constitution,—

(i) in clause (1), for the words, figures and letter "articles 268, 268A and article 269", the words, figures and letter "articles 268, 269 and article 269A" shall be substituted; 35

(ii) after clause (1), the following clause shall be inserted, namely:—

“(1A) The goods and services tax levied and collected by the Government of India, except the tax apportioned with the States under clause (1) of article 269A, shall also be distributed between the Union and the States in the manner provided in clause (2).” 40

Amendment of article 271. 11. In article 271 of the Constitution, after the words “in those articles”, the words, figures and letter “except the goods and services tax under article 246A,” shall be inserted.

12. After article 279 of the Constitution, the following article shall be inserted, namely:—

Insertion of
new article
279A.

“279A. (1) The President shall, within sixty days from the date of commencement of the Constitution (One Hundred and Twenty-second Amendment) Act, 2014, by order, constitute a Council to be called the Goods and Services Tax Council.

Goods and
Services Tax
Council.

5 (2) The Goods and Services Tax Council shall consist of the following members, namely:—

(a) the Union Finance Minister..... Chairperson;

(b) the Union Minister of State in charge of Revenue or Finance..... Member;

10 (c) the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government.....Members.

(3) The Members of the Goods and Services Tax Council referred to in sub-clause (c) of clause (2) shall, as soon as may be, choose one amongst themselves to be the Vice-Chairperson of the Council for such period as they may decide.

15 (4) The Goods and Services Tax Council shall make recommendations to the Union and the States on—

(a) the taxes, cesses and surcharges levied by the Union, the States and the local bodies which may be subsumed in the goods and services tax;

20 (b) the goods and services that may be subjected to, or exempted from the goods and services tax;

(c) model Goods and Services Tax Laws, principles of levy, apportionment of Integrated Goods and Services Tax and the principles that govern the place of supply;

25 (d) the threshold limit of turnover below which goods and services may be exempted from goods and services tax;

(e) the rates including floor rates with bands of goods and services tax;

(f) any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster;

30 (g) special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand; and

(h) any other matter relating to the goods and services tax, as the Council may decide.

35 (5) 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.

40 (6) While discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

(7) One half of the total number of Members of the Goods and Services Tax Council shall constitute the quorum at its meetings.

(8) The Goods and Services Tax Council shall determine the procedure in the performance of its functions.

(9) Every decision of the Goods and Services Tax Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the members present and voting, in accordance with the following principles, namely:—

(a) the vote of the Central Government shall have a weightage of one-third of the total votes cast, and

(b) the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast,

in that meeting.

(10) No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of—

(a) any vacancy in, or any defect in, the constitution of the Council; or

(b) any defect in the appointment of a person as a member of the Council; or

(c) any procedural irregularity of the Council not affecting the merits of the case.

(11) The Goods and Services Tax Council may decide about the modalities to resolve disputes arising out of its recommendation.”.

Amendment of
article 286.

13. In article 286 of the Constitution,—

(i) in clause (1),—

(A) for the words "the sale or purchase of goods where such sale or purchase takes place", the words "the supply of goods or of services or both, where such supply takes place" shall be substituted;

(B) in sub-clause (b), for the word “goods”, at both the places where it occurs the words “goods or services or both” shall be substituted;

(ii) in clause (2), for the words "sale or purchase of goods takes place", the words "supply of goods or of services or both" shall be substituted;

(iii) clause (3) shall be omitted.

Amendment of
article 366.

14. In article 366 of the Constitution,—

(i) after clause (12), the following clause shall be inserted, namely:—

“(12A) “goods and services tax” means any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption;”;

(ii) after clause (26), the following clauses shall be inserted, namely:—

“(26A) “Services” means anything other than goods;

(26B) “State” with reference to articles 246A, 268, 269, 269A and article 279A includes a Union territory with Legislature;”.

Amendment of
article 368.

15. In article 368 of the Constitution, in clause (2), in the proviso, in clause (a), for the words and figures “article 162 or article 241”, the words, figures and letter “article 162, article 241 or article 279A” shall be substituted.

Amendment
of Sixth
Schedule.

16. In the Sixth Schedule to the Constitution, in paragraph 8, in sub-paragraph (3),—

(i) in clause (c), the word "and" occurring at the end shall be omitted;

(ii) in clause (d), the word "and" shall be inserted at the end;

(iii) after clause (d), the following clause shall be inserted, namely:—

"(e) taxes on entertainment and amusements.”.

17. In the Seventh Schedule to the Constitution,—

Amendment of
Seventh
Schedule.

(a) in List I — Union List,—

(i) for entry 84, the following entry shall be substituted, namely:—

"84. Duties of excise on the following goods manufactured or produced in India, namely:—

(a) petroleum crude;

(b) high speed diesel;

(c) motor spirit (commonly known as petrol);

(d) natural gas;

(e) aviation turbine fuel; and

(f) tobacco and tobacco products.";

(ii) entries 92 and 92C shall be omitted;

(b) in List II — State List,—

(i) entry 52 shall be omitted;

(ii) for entry 54, the following entry shall be substituted, namely:—

"54. Taxes on the sale of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption, but not including sale in the course of inter-State trade or commerce or sale in the course of international trade or commerce of such goods.";

(iii) entry 55 shall be omitted;

(iv) for entry 62, the following entry shall be substituted, namely:—

"62. Taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council.".

18. (1) An additional tax on supply of goods, not exceeding one per cent. in the course of inter-State trade or commerce shall, notwithstanding anything contained in clause (1) of article 269A, be levied and collected by the Government of India for a period of two years or such other period as the Goods and Services Tax Council may recommend, and such tax shall be assigned to the States in the manner provided in clause (2).

Arrangement
for assignment
of additional
tax on supply
of goods to
States for two
years or such
other period
recommended
by the
Council.

(2) The net proceeds of additional tax on supply of goods in any financial year, except the proceeds attributable to the Union territories, shall not form part of the Consolidated Fund of India and be deemed to have been assigned to the States from where the supply originates.

(3) The Government of India may, where it considers necessary in the public interest, exempt such goods from the levy of tax under clause (1).

(4) Parliament may, by law, formulate the principles for determining the place of origin from where supply of goods take place in the course of inter-State trade or commerce.

19. Parliament may, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for such period which may extend to five years.

Compensation
to States for
loss of
revenue on
account of
introduction
of goods and
services tax.

Transitional provisions.

20. Notwithstanding anything in this Act, any provision of any law relating to tax on goods or services or on both in force in any State immediately before the commencement of this Act, which is inconsistent with the provisions of the Constitution as amended by this Act shall continue to be in force until amended or repealed by a competent Legislature or other competent authority or until expiration of one year from such commencement, whichever is earlier. 5

Power of President to remove difficulties.

21. (1) If any difficulty arises in giving effect to the provisions of the Constitution as amended by this Act (including any difficulty in relation to the transition from the provisions of the Constitution as they stood immediately before the date of assent of the President to this Act to the provisions of the Constitution as amended by this Act), the President may, by order, make such provisions, including any adaptation or modification of any provision of the Constitution as amended by this Act or law, as appear to the President to be necessary or expedient for the purpose of removing the difficulty: 10

Provided that no such order shall be made after the expiry of three years from the date of such assent. 15

(2) Every order made under sub-section (1) shall, as soon as may be after it is made, be laid before each House of Parliament.

STATEMENT OF OBJECTS AND REASONS

The Constitution is proposed to be amended to introduce the goods and services tax for conferring concurrent taxing powers on the Union as well as the States including Union territory with Legislature to make laws for levying goods and services tax on every transaction of supply of goods or services or both. The goods and services tax shall replace a number of indirect taxes being levied by the Union and the State Governments and is intended to remove cascading effect of taxes and provide for a common national market for goods and services. The proposed Central and State goods and services tax will be levied on all transactions involving supply of goods and services, except those which are kept out of the purview of the goods and services tax.

2. The proposed Bill, which seeks further to amend the Constitution, *inter alia*, provides for—

(a) subsuming of various Central indirect taxes and levies such as Central Excise Duty, Additional Excise Duties, Excise Duty levied under the Medicinal and Toilet Preparations (Excise Duties) Act, 1955, Service Tax, Additional Customs Duty commonly known as Countervailing Duty, Special Additional Duty of Customs, and Central Surcharges and Cesses so far as they relate to the supply of goods and services;

(b) subsuming of State Value Added Tax/Sales Tax, Entertainment Tax (other than the tax levied by the local bodies), Central Sales Tax (levied by the Centre and collected by the States), Octroi and Entry tax, Purchase Tax, Luxury tax, Taxes on lottery, betting and gambling; and State cesses and surcharges in so far as they relate to supply of goods and services;

(c) dispensing with the concept of ‘declared goods of special importance’ under the Constitution;

(d) levy of Integrated Goods and Services Tax on inter-State transactions of goods and services;

(e) levy of an additional tax on supply of goods, not exceeding one per cent. in the course of inter-State trade or commerce to be collected by the Government of India for a period of two years, and assigned to the States from where the supply originates;

(f) conferring concurrent power upon Parliament and the State Legislatures to make laws governing goods and services tax;

(g) coverage of all goods and services, except alcoholic liquor for human consumption, for the levy of goods and services tax. In case of petroleum and petroleum products, it has been provided that these goods shall not be subject to the levy of Goods and Services Tax till a date notified on the recommendation of the Goods and Services Tax Council.

(h) compensation to the States for loss of revenue arising on account of implementation of the Goods and Services Tax for a period which may extend to five years;

(i) creation of Goods and Services Tax Council to examine issues relating to goods and services tax and make recommendations to the Union and the States on parameters like rates, exemption list and threshold limits. The Council shall function under the Chairmanship of the Union Finance Minister and will have the Union Minister of State in charge of Revenue or Finance as member, along with the Minister in-charge of Finance or Taxation or any other Minister nominated by each State Government. It is further provided that every decision of the Council shall be taken by a majority of

not less than three-fourths of the weighted votes of the members present and voting in accordance with the following principles:—

(A) the vote of the Central Government shall have a weightage of one-third of the total votes cast, and

(B) the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast in that meeting.

Illustration:

In terms of clause (9) of the proposed article 279A, the "weighted votes of the members present and voting" in favour of a proposal in the Goods and Services Tax Council shall be determined as under:—

$$WT = WC + WS$$

Where,

$$WT = WC + WS = \left(\frac{WST}{SP} \right) \times SF$$

Wherein—

WT = Total weighted votes of all members in favour of a proposal.

WC = Weighted vote of the Union = $\frac{1}{3}$ i.e., 33.33% if the Union is in favour of the proposal and be taken as "0" if, Union is not in favour of a proposal.

WS = Weighted votes of the States in favour of a proposal.

SP = Number of States present and voting.

WST = Weighted votes of all States present and voting i.e., $\frac{2}{3}$ i.e., 66.67%

SF = Number of States voting in favour of a proposal.

(j) Clause 20 of the proposed Bill makes transitional provisions to take care of any inconsistency which may arise with respect to any law relating to tax on goods or services or on both in force in any State on the commencement of the provisions of the Constitution as amended by this Act within a period of one year.

3. the Bill seeks to achieve the above objects.

NEW DELHI;
The 18th December, 2014

ARUN JAITLEY

PRESIDENT'S RECOMMENDATION UNDER ARTICLE 117 OF THE
CONSTITUTION OF INDIA

[Copy of letter No. S-31011/07/2014-SO(ST), dated the 18th December, 2014 from Shri Arun Jaitley, Minister of Finance to the Secretary-General, Lok Sabha.]

The President, having been informed of the subject matter of the proposed Bill, recommends under clauses (1) and (3) of article 117, read with clause (1) of article 274, of the Constitution of India, the introduction of the Constitution (One Hundred and Twenty-second Amendment) Bill, 2014 in Lok Sabha and also the consideration of the Bill.

FINANCIAL MEMORANDUM

Clause 12 of the Bill seeks to insert a new article 279A in the Constitution relating to Constitution of Goods and Services Tax Council. The Council shall function under the Chairmanship of the Union Finance Minister and will have the Union Minister of State incharge of Revenue or Finance as member, along with the Minister in-charge of Finance or Taxation or any other Minister nominated by each State Government.

2. The creation of Goods and Services Tax Council will involve expenditure on office expenses, salaries and allowances of the officers and staff. The objective that the introduction of goods and services tax will make the Indian trade and industry more competitive, domestically as well as internationally and contribute significantly to the growth of the economy, such additional expenditure on the Council will not be significant.

3. At this stage, it will be difficult to make an estimate of the expenditure, both recurring and non-recurring on account of the Constitution of the Council.

4. Further, it is provided for compensation to the States for loss of revenue arising on account of implementation of the Goods and Services Tax for such period which may extend to five years. The exact compensation can be worked out only when the provisions of the Bill are implemented.

MEMORANDUM REGARDING DELEGATED LEGISLATION

Clause 12 of the Bill seeks to insert a new article 279A relating to the constitution of a Council to be called the Goods and Services Tax Council. Clause (1) of the proposed new article 279A provides that the President, shall within sixty days from the date of the commencement of the Constitution (One Hundred and Twenty-second Amendment) Act, 2014, by order, constitute a Council to be called the Goods and Services Tax Council. Clause (8) of the said article provides that the Council shall determine the procedure in the performance of its functions.

2. The procedures, as may be laid down by the Goods and Services Tax Council in the performance of its functions, are matters of procedure and details. The delegation of legislative power is, therefore, of a normal character.

ANNEXURE

EXTRACTS FROM THE CONSTITUTION OF INDIA

*	*	*	*	*
248. (1) Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent List or State List.				
*	*	*	*	*
249. (1) Notwithstanding anything in the foregoing provisions of this Chapter, if the Council of States has declared by resolution supported by not less than two-thirds of the members present and voting that it is necessary or expedient in the national interest that Parliament should make laws with respect to any matter enumerated in the State List specified in the resolution, it shall be lawful for Parliament to make laws for the whole or any part of the territory of India with respect to that matter while the resolution remains in force.				
*	*	*	*	*
250. (1) Notwithstanding anything in this Chapter, Parliament shall, while a Proclamation of Emergency is in operation, have power to make laws for the whole or any part of the territory of India with respect to any of the matters enumerated in the State List.				
*	*	*	*	*
<i>Distribution of Revenues between the Union and the States</i>				
268. (1) Such stamp duties and such duties of excise on medicinal and toilet preparations as are mentioned in the Union List shall be levied by the Government of India but shall be collected—				
(a) in the case where such duties are leviable within any Union territory, by the Government of India, and				
(b) in other cases, by the States within which such duties are respectively leviable.				
*	*	*	*	*
268A. (1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the States, in the manner provided in clause (2).				
(2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be—				
(a) collected by the Government of India and the States;				
(b) appropriated by the Government of India and the States,				
in accordance with such principles of collection and appropriation as may be formulated by Parliament by law.				
269. (1) Taxes on the sale or purchase of goods and taxes on the consignment of goods shall be levied and collected by the Government of India but shall be assigned and shall be deemed to have been assigned to the States on or after the 1st day of April, 1996 in the manner provided in clause (2).				
<i>Explanation.</i>—For the purposes of this clause,—				

Residuary powers of legislation.

Power of Parliament to legislate with respect to a matter in the State List in the national interest.

Power of Parliament to legislate with respect to any matter in the State List if a Proclamation of Emergency is in operation.

Duties levied by the Union but collected and appropriated by the States.

Service tax levied by Union and collected and appropriated by the Union and the States.

Taxes levied and collected by the Union but assigned to the States.

(a) the expression "taxes on the sale or purchase of goods" shall mean taxes on sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce;

(b) the expression "taxes on the consignment of goods" shall mean taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce.

* * * * *

Taxes levied and distributed between the Union and the States.

270. (1) All taxes and duties referred to in the Union List, except the duties and taxes referred to in articles 268, 268A and 269, respectively, surcharge on taxes and duties referred to in article 271 and any cess levied for specific purposes under any law made by Parliament shall be levied and collected by the Government of India and shall be distributed between the Union and the States in the manner provided in clause (2).

* * * * *

Surcharge on certain duties and taxes for purposes of the Union.

271. Notwithstanding anything in articles 269 and 270, Parliament may at any time increase any of the duties or taxes referred to in those articles by a surcharge for purposes of the Union and the whole proceeds of any such surcharge shall form part of the Consolidated Fund of India.

* * * * *

Restrictions as to imposition of tax on the sale or purchase of goods.

286. (1) No law of a State shall impose, or authorise the imposition of, a tax on the sale or purchase of goods where such sale or purchase takes place—

(a) outside the State; or

(b) in the course of the import of the goods into, or export of the goods out of, the territory of India.

(2) Parliament may by law formulate principles for determining when a sale or purchase of goods takes place in any of the ways mentioned in clause (1).

(3) Any law of a State shall, in so far as it imposes, or authorises the imposition of,—

(a) a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce; or

(b) a tax on the sale or purchase of goods, being a tax of the nature referred to in sub-clause (b), sub-clause (c) or sub-clause (d) of clause (29A) of article 366,

be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify.

* * * * *

PART XX

AMENDMENT OF THE CONSTITUTION

Power of Parliament to amend the Constitution and procedure therefore.

368. (1) * * * * *

(2) An amendment of this Constitution may be initiated only by the introduction of a Bill for the purpose in either House of Parliament, and when the Bill is passed in each House by a majority of the total membership of that House and by a majority of not less than two-thirds of the members of that House present and voting, it shall be presented to the President who shall give his assent to the Bill and thereupon the Constitution shall stand amended in accordance with the terms of the Bill:

Provided that if such amendment seeks to make any change in—

(a) article 54, article 55, article 73, article 162 or article 241, or

- (b) Chapter IV of Part V, Chapter V of Part VI, or Chapter I of Part XI, or
- (c) any of the Lists in the Seventh Schedule, or
- (d) the representation of States in Parliament, or
- (e) the provisions of this article,

the amendment shall also require to be ratified by the Legislatures of not less than one-half of the States by resolutions to that effect passed by those Legislatures before the Bill making provision for such amendment is presented to the President for assent.

* * * * *

SIXTH SCHEDULE

[Articles 244(2) and 275(1)]

Provisions as to the Administration of Tribal Areas in the States of Assam, Meghalaya, Tripura and Mizoram

* * * * *

8. (1) * * * * * *

(3) The District Council for an autonomous district shall have the power to levy and collect all or any of the following taxes within such district, that is to say—

Powers to assess and collect land revenue and to impose taxes.

* * * * *

(c) taxes on the entry of goods into a market for sale therein, and tolls on passengers and goods carried in ferries; and

(d) taxes for the maintenance of schools, dispensaries or roads.

* * * * *

SEVENTH SCHEDULE

(Article 246)

List I- Union List

* * * * *

84. Duties of excise on tobacco and other goods manufactured or produced in India except—

(a) alcoholic liquors for human consumption;

(b) opium, Indian hemp and other narcotic drugs and narcotics,

but including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry.

* * * * *

92. Taxes on the sale or purchase of newspapers and on advertisements published therein.

* * * * *

92C. Taxes on services.

* * * * *

List II-State List

* * * * *

52. Taxes on the entry of goods into a local area for consumption, use or sale therein.

* * * * *

54. Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of List I.

55. Taxes on advertisements other than advertisements published in the newspapers and advertisements broadcast by radio or television.

* * * * *

62. Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling.

* * * * *

LOK SABHA

A

BILL

further to amend the Constitution of India.

(Shri Arun Jaitley, Minister of Finance)

LOK SABHA

CORRIGENDA

to

**THE CONSTITUTION (ONE HUNDRED AND TWENTY-SECOND AMENDMENT)
BILL, 2014**

[To be/As introduced in Lok Sabha]

1. Page 2, line 32, -
for "Contitution,—"
read "Constitution,—"
2. Page 4, line 16, -
for "of its recommendation"."."
read "of its recommendations"."."
3. Page 5, in the marginal citation against clause 18, -
for "by the Council."
read "by Council."
4. Page 8, *omit* line 11.

NEW DELHI;

December 19, 2014
Agrahayana 28, 1936 (Saka)

Salient features of GST Constitutional Amendment Bill

1. Insertion of new Article 246A conferring simultaneous power to the Union and the State legislatures to legislate on GST.
2. Insertion of new Article 279A for the creation of a Goods & Services Tax Council, which will be a joint forum of the Centre and the States. This Council would function under the Chairmanship of the Union Finance Minister.
3. Central Taxes like Central Excise Duty, Additional Excise Duties, Service Tax, Additional Customs Duty (CVD) and Special Additional Duty of Customs (SAD), etc. will be subsumed in GST.
4. At the State level, Taxes like VAT/ Sales Tax, Central Sales Tax, Entertainment Tax, Octroi and Entry Tax, Purchase Tax and Luxury Tax, etc. would be subsumed in GST.
5. All Goods and services, except alcoholic liquor for human consumption, will be brought under the purview of GST. However, it has also been provided that petroleum and petroleum products shall not be subject to the levy of GST till notified at a future date on the recommendation of the GST Council. The present taxes levied by the States and the Centre on petroleum and petroleum products, i.e., Sales Tax/VAT, CST and Excise duty only, will continue to be levied in the interim period.
6. Both Centre and States will simultaneously levy GST across the value chain. The Centre would levy and collect Central Goods and Services Tax (CGST), and States would levy and collect the State Goods and Services Tax (SGST) on all transactions within a State.
7. Integrated GST (IGST): However, only the centre may levy and collect GST on supplies in the course of inter-state trade or commerce. The tax collected would be divided between the centre and the states in a manner to be provided by Parliament, by law, on the recommendations of the GST Council.
8. GST Council: The President must constitute a Goods and Services Tax Council within sixty days of this Act coming into force. The GST Council aim to develop a harmonized national market of goods and services.
9. Composition of the GST Council: The GST Council is to consist of the following three members: (i) the Union Finance Minister (as Chairman), (ii) the Union Minister of State in charge of Revenue or Finance, and (iii) the Minister in charge of Finance or Taxation or any other, nominated by each state government.
10. Functions of the GST Council: These include making recommendations on: (i) taxes, cesses, and surcharges levied by the centre, states and local bodies which may be subsumed in the GST; (ii) goods and services which may be subjected to or exempted from GST; (iii) model GST laws, principles of levy, apportionment of IGST and principles that govern the place of supply; (iv) the threshold limit of turnover below which goods and services may be exempted from GST; (v) rates including floor rates with bands of GST; (vi) special rates to raise additional resources during any natural calamity; (vii) special provision with respect to Arunachal Pradesh, Jammu and Kashmir, Manipur,

Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand and (viii) any other matters.

11. Resolution of disputes: The GST Council may decide upon the modalities for the resolution of disputes arising out of its recommendations.
12. Restrictions on imposition of tax: The Constitution imposes certain restrictions on states on the imposition of tax on the sale or purchase of goods. The Bill amends this provision to restrict the imposition of tax on the supply of goods and services and not on its sale.
13. Additional Tax on supply of goods: An additional tax (not to exceed 1%) on the supply of goods in the course of inter-state trade or commerce would be levied and collected by the centre. Such additional tax shall be assigned to the states for two years, or as recommended by the GST Council.
14. Compensation to states: Parliament may, by law, provide for compensation to states for revenue losses arising out of the implementation of the GST, on the GST Council's recommendations. This would be up to a five year period.
15. Goods exempt: Alcoholic liquor for human consumption is exempted from the purview of the GST. Further, the GST Council is to decide when GST would be levied on: (i) petroleum crude, (ii) high speed diesel, (iii) motor spirit (petrol), (iv) natural gas, and (v) aviation turbine fuel.
16. GST rates will be uniform across the Country. However, to give some fiscal autonomy to the Centre and States, there will a provision of a narrow tax band over and above the floor rates of CGST and SGST.
17. The term "Services" is proposed to be exhaustively defined as "anything other than goods".

Analysis of 122nd Constitutional Amendment Bill

Article No.	Original Article	Amendments	Analysis
246A	Insertion of new Article 246A.	Special provision with respect to goods and services tax. [Article 246A]: (1) Notwithstanding anything contained in articles 246 and 254, Parliament, and, subject to clause (2), the Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by such State. (2) Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce. Explanation— The provisions of this article, shall, in respect of goods and services tax referred to in clause (5), of article 279A, take effect from the date recommended by the Goods and Services Tax Council.	<u>Insertion of clause 246A – To facilitate the Parliament & states to make laws in regard to Goods & Service tax imposed by Union or such State:</u> Article 246 of Constitution of India establishes the law making jurisdiction of Central and State governments over Union List, State List and the concurrent list of Schedule VII to the Constitution. Article 254 establishes that the law enacted by Central government shall prevail over the state government where the laws are conflicting on subject matter of concurrent list (except that the state law may prevail in that state subject to Hon'ble President Assent). The article 246A(1) shall empower goods and service tax law framing with both the central and state government unlike in the current case where the service tax / excise was centre's domain in union list and sales tax on goods was state's domain except in case of interstate transactions. Article 246(2) re-establishes the centre's exclusive control on interstate supply of goods & services. Importantly interstate supply of services will mark its separate significance in the proposed GST regime. Article 279A is proposed for setup of GST Council within 60 days of commencement of this Act, 2014. The items proposed in article 279A(5) includes petroleum crude, high speed diesel, motor spirit (petrol), natural gas and aviation turbine fuel. The

Analysis of 122nd Constitutional Amendment Bill

			date on which GST is to be levied on these items is to be recommended by GST council.
248	Residuary powers of legislation [Article 248].— (1) Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent List or State List. (2) Such power shall include the power of making any law imposing a tax not mentioned in either of those Lists.	In article 248 of the Constitution, in clause (1), for the word " Parliament ", the words, figures and letter " Subject to article 246A, Parliament " shall be substituted.	<u>Facilitative amendments in Article 248(1), 249(1), 250(1), 268(1), 269(1), 270(1), 286. Omitting Article 268A.</u> Article 248(1) empowers the parliament to make laws on any matters not covered in state list and concurrent list. Hence in a sense this article is giving powers on residual matters to parliament. Now, this has been made subject to 246A since GST shall be both centre's and state's domain.
249	Power of Parliament to legislate with respect to a matter in the State List in the national interest [Article 249].— (1) Notwithstanding anything in the foregoing provisions of this Chapter, if the Council of States has declared by resolution supported by not less than two-thirds of the members present and voting that it is necessary or expedient in the national interest that Parliament should make laws with respect to any matter enumerated in the State List specified in the resolution, it shall be lawful for Parliament to make laws for the whole or any part of the territory of India with respect to that matter while the resolution remains in force. (2) A resolution passed under clause (1) shall remain in force for such period not exceeding one year as may be specified therein: Provided that, if and so often as a resolution approving the continuance in force of any such resolution is passed in	In article 249 of the Constitution, in clause (1), after the words " with respect to ", the words, figures and letter " goods and services tax provided under article 246A or " shall be inserted.	Article 249(1) empowers the parliament to make laws even of state list where it is in national interest and the council of states have passed a resolution to this effect of 2/3rd members or more. Now, GST has been also covered in this provision. Article 250(1) empowers the parliament to make laws even of state list in pursuance to proclamation of emergency being in operation. Now, GST has been also covered in this provision. Article 268(1) governs levy of duties of excise on medicinal and toilet preparations as mentioned in union list but are collected by state. Now, the duties of excise on medicinal and toilet preparations is being omitted. Apportioning of taxes between centre and state is facilitated by Article 268A

Analysis of 122nd Constitutional Amendment Bill

	the manner provided in clause (1), such resolution shall continue in force for a further period of one year from the date on which under this clause it would otherwise have ceased to be in force. (3) A law made by Parliament which Parliament would not but for the passing of a resolution under clause (1) have been competent to make shall, to the extent of the incompetency, cease to have effect on the expiration of a period of six months after the resolution has ceased to be in force, except as respects things done or omitted to be done before the expiration of the said period.		(Services) will be dispensed away. Article 269 facilitates levy and collection of interstate tax on sale of goods (not services) or consignment of goods but the same to be assigned to states. Now, the interstate supply of goods and services has been made an exception to this pure assignment to states since service now covered. A separate article 269A has been inserted to apportionate the taxes.
250	Power of Parliament to legislate with respect to any matter in the State List if a Proclamation of Emergency is in operation [Article 250]— (1) Notwithstanding anything in this Chapter, Parliament shall, while a Proclamation of Emergency is in operation, have power to make laws for the whole or any part of the territory of India with respect to any of the matters enumerated in the State List. (2) A law made by Parliament which Parliament would not but for the issue of a Proclamation of Emergency have been competent to make shall, to the extent of the incompetency, cease to have effect on the expiration of a period of six months after the Proclamation has ceased to operate, except as respects things done or omitted to be done before the expiration of the said period.	In article 250 of the Constitution, in clause (1), after the words "with respect to", the words, figures and letter "goods and services tax provided under article 246A or" shall be inserted.	

Analysis of 122nd Constitutional Amendment Bill

268	Duties levied by the Union but collected and appropriated by the States [Article 268] — (1) Such stamp duties and such duties of excise on medicinal and toilet preparations as are mentioned in the Union List shall be levied by the Government of India but shall be collected— (a) in the case where such duties are leviable within any Union territory, by the Government of India, and (b) in other cases, by the States within which such duties are respectively leviable. (2) The proceeds in any financial year of any such duty leviable within any State shall not form part of the Consolidated Fund of India, but shall be assigned to that State.	In article 268 of the Constitution, in clause (1), the words "and such duties of excise on medicinal and toilet preparations" shall be omitted.	
268A	Service tax levied by Union and collected and appropriated by the Union and the States [Article 268A]- (1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the States in the manner provided in clause (2). (2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be— (a) collected by the Government of India and the States; (b) appropriated by the Government of India and the States, in accordance with such principles of	Article 268A of the Constitution, as inserted by section 2 of the Constitution (Eighty-eighth Amendment) Act, 2003 shall be omitted.	

Analysis of 122nd Constitutional Amendment Bill

	collection and appropriation as may be formulated by Parliament by law.		
269	Taxes levied and collected by the Union but assigned to the States [Article 269]- (1) Taxes on the sale or purchase of goods and taxes on the consignment of goods shall be levied and collected by the Government of India but shall be assigned and shall be deemed to have been assigned to the States on or after the 1st day of April, 1996 in the manner provided in clause (2). Explanation—For the purposes of this clause,— (a) the expression “taxes on the sale or purchase of goods” shall mean taxes on sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce; (b) the expression “taxes on the consignment of goods” shall mean taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce. (2) The net proceeds in any financial year of any such tax, except in so far as those proceeds represent proceeds attributable to Union territories, shall not form part of the Consolidated Fund of India, but shall be assigned to the States within which that tax is leviable in that year, and shall be distributed among those States in	In article 269 of the Constitution, in clause (1), after the words “consignment of goods”, the words, figures and letter “except as provided in article 269A” shall be inserted.	

Analysis of 122nd Constitutional Amendment Bill

	accordance with such principles of distribution as may be formulated by Parliament by law. (3) Parliament may by law formulate principles for determining when a sale or purchase of, or consignment of, goods takes place in the course of inter-State trade or commerce.		
269A	Insertion of new Article 269A.	Levy and collection of Goods and Services Tax in course of inter-State trade or commerce [Article 269A].- (1) Goods and services tax on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council. Explanation.— For the purposes of this clause, supply of goods, or of services, or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-State trade or commerce. (2) Parliament may, by law, formulate the principles for determining the place of supply, and when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.	<u>Insertion of Article 269A – apportionment of Inter-state taxes on supply of Goods and Services based on GST council's recommendations.</u> With the beginning of GST, now taxes on supply of goods and service in course of interstate trade or commerce would also required to be made a commodity of due apportionment between union and states instead of pure assignment as in cases of goods. This article 269A is inserted precisely to mitigate this aspect. The apportionment shall be undertaken pursuant to GST Council's recommendation. To understand what transaction would constitute interstate trade, the rules of supply, origin and point of incidence would be required to be framed. The same would be in parliament's domain.
270	Taxes levied and distributed between the Union and the States [Article 270] -	In Article 270 of the Constitution,— (i) in clause (1), for the words, figures	Article 270 provides for apportionment of taxes and duties between Union and

Analysis of 122nd Constitutional Amendment Bill

	(1) All taxes and duties referred to in the Union List, except the duties and taxes referred to in articles *[268 and 269], respectively, surcharge on taxes and duties referred to in article 271 and any cess levied for specific purposes under any law made by Parliament shall be levied and collected by the Government of India and shall be distributed between the Union and the States in the manner provided in clause (2). (2) Such percentage, as may be prescribed, of the net proceeds of any such tax or duty in any financial year shall not form part of the Consolidated Fund of India, but shall be assigned to the States within which that tax or duty is leviable in that year, and shall be distributed among those States in such manner and from such time as may be prescribed in the manner provided in clause (3). (3) In this article, "prescribed" means,— (i) until a Finance Commission has been constituted, prescribed by the President by order, and (ii) after a Finance Commission has been constituted, prescribed by the President by order after considering the recommendations of the Finance Commission.	and letter "Articles 268, 268A and Article 269", the words, figures and letter "Articles 268, 269 and Article 269A" shall be substituted; (ii) after clause (1), the following clause shall be inserted, namely:— "(1A) The goods and services tax levied and collected by the Government of India, except the tax apportioned with the States under clause (1) of Article 269A, shall also be distributed between the Union and the States in the manner provided in clause (2)."	State. The Interstate GST has been kept out of this by inserting necessary exception. The reason for this exception is since the apportionment in interstate's case is not to be undertaken as per Article 270 laid mechanism but on recommendations of GST council as facilitated under Article 269A. In other cases of GST levied by government of India, a new clause 270(1A) is inserted and apportionment to be in accordance with normal provisions of Article 270 only.
271	Surcharge on certain duties and taxes for purposes of the Union [Article 271] - Notwithstanding anything in articles 269 and 270, Parliament may at any time increase any of the duties or taxes referred to in those articles by a surcharge for	In article 271 of the Constitution, after the words "in those articles", the words, figures and letter "except the goods and services tax under article 246A," shall be inserted.	<u>Surcharge by Parliament not to apply to GST</u> Article 271 empowers the parliament to increase taxes and duties on articles. The GST has been made an exception to power of parliament. Hence, the

Analysis of 122nd Constitutional Amendment Bill

	purposes of the Union and the whole proceeds of any such surcharge shall form part of the Consolidated Fund of India.		parliament cannot impose surcharge on GST.
279A	Insertion of new Article 279A.	Goods and Services Tax Council [Article 279A].- (1) The President shall, within sixty days from the date of commencement of the Constitution (One Hundred and Twenty-second Amendment) Act, 2014, by order, constitute a Council to be called the Goods and Services Tax Council. (2) The Goods and Services Tax Council shall consist of the following members, namely:— (a) the Union Finance Minister.....Chairperson; (b) the Union Minister of State in charge of Revenue or Finance.....Member; (c) the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government.....Members. (3) The Members of the Goods and Services Tax Council referred to in sub-clause (c) of clause (2) shall, as soon as may be, choose one amongst themselves to be the Vice-Chairperson of the Council for such period as they may decide. (4) The Goods and Services Tax Council shall make recommendations to the Union and the States on— (a) the taxes, cesses and surcharges levied by the Union, the States	<u>Constituting the 'GST council' vide Article 279A:</u> Article 279A is to be inserted to empower the Hon'ble President of India to constitute 'GST Council'. Brief features shall be :- ➤ To be incorporated within 60 days of Commencement of Act. ➤ Members shall include:- - FM – Chairperson • Union Minister of state in charge of revenue Members • State FM's / Nominated State Ministers – Members ➤ Members to choose Vice Chairperson ➤ Recommendations on :- • the taxes, cesses and surcharges levied by the Union, the States and the local bodies which may be subsumed in the goods and services tax; • the goods and services that may be subjected to, or exempted from the goods and services tax • model Goods and Services Tax Laws, principles of levy, apportionment of integrated Goods and Services Tax and the principles that govern the place of supply • the threshold limit of turnover below which goods and services may be exempted from goods and services tax • the rates including floor rates with

Analysis of 122nd Constitutional Amendment Bill

		and the local bodies which may be subsumed in the goods and services tax; (b) the goods and services that may be subjected to, or exempted from the goods and services tax; (c) model Goods and Services Tax Laws, principles of levy, apportionment of Integrated Goods and Services Tax and the principles that govern the place of supply; (d) the threshold limit of turnover below which goods and services may be exempted from goods and services tax; (e) the rates including floor rates with bands of goods and services tax; (f) any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster; (g) special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand; and (h) any other matter relating to the goods and services tax, as the Council may decide. (5) 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,	bands of goods and services tax - any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster - special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur; Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand; and - Any other matter relating to the goods and services tax, as the Council may decide. ➤ Date of levy of GST on items like petrol, diesel and natural gas. ➤ Quorum shall be 50% of members ➤ Decision by 75% of total weighted votes of members present and voting. Centre to have 1/3rd of weight of total votes and states to have 2/3rd of total votes cast. ➤ Dispute resolution modalities.

Analysis of 122nd Constitutional Amendment Bill

		motor spirit (commonly known as petrol), natural gas and aviation turbine fuel. (6) While discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services. (7) One half of the total number of Members of the Goods and Services Tax Council shall constitute the quorum at its meetings. (8) The Goods and Services Tax Council shall determine the procedure in the performance of its functions. (9) Every decision of the Goods and Services Tax Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the members present and voting, in accordance with the following principles, namely:— (a) the vote of the Central Government shall have a weightage of one-third of the total votes cast, and (b) the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast, in that meeting. (10) No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of— (a) any vacancy in, or any defect in,	

Analysis of 122nd Constitutional Amendment Bill

		the constitution of the Council; or (b) any defect in the appointment of a person as a member of the Council; or (c) any procedural irregularity of the Council not affecting the merits of the case. (11) The Goods and Services Tax Council may decide about the modalities to resolve disputes arising out of its recommendation.	
286	Restrictions as to imposition of tax on the sale or purchase of goods [Article 286].- (1) No law of a State shall impose, or authorise the imposition of, a tax on the sale or purchase of goods where such sale or purchase takes place— (a) outside the State; or (b) in the course of the import of the goods into, or export of the goods out of, the territory of India. (2) Parliament may by law formulate principles for determining when a sale or purchase of goods takes place in any of the ways mentioned in clause (1). (3) Any law of a State shall, in so far as it imposes, or authorises the imposition of,— (a) a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce; or (b) a tax on the sale or purchase of goods, being a tax of the nature referred to in sub-clause (b), sub-clause (c) or sub-clause (d) of clause	In Article 286 of the Constitution,— (i) in clause (1),— (A) for the words "the sale or purchase of goods where such sale or purchase takes place", the words "the supply of goods or of services or both, where such supply takes place" shall be substituted; (B) in sub-clause (b), for the word "goods", at both the places where it occurs the words "goods or services or both" shall be substituted; (ii) in clause (2), for the words "sale or purchase of goods takes place", the words "supply of goods or of services or both" shall be substituted; (iii) clause (3) shall be omitted.	Article 286 imposes restrictions for imposition of taxes on sale or purchases of goods in case of interstate trade, imports or exports or trade outside the state. It empowers the parliament for the same. Now, this is extended to GST.

Analysis of 122nd Constitutional Amendment Bill

	(29A) of article 366, be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify.		
366	Definitions [Article 366] Insertion of New Definitions	In Article 366 of the Constitution,— (i) after clause (12), the following clause shall be inserted , namely:— ‘(12A) “goods and services tax” means any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption.’ (ii) after clause (26), the following clauses shall be inserted , namely:— ‘(26A) “Services” means anything other than goods; (26B) “State” with reference to articles 246A, 268, 269, 269A and article 279A includes a Union territory with Legislature;	<u>New Definitions – Article 366:</u> (12A) “goods and services tax” means any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption (26A) “Services” means anything other than goods. The definition of services being other than goods raises the concern of whether it would also cover Immovable property transactions.
368	Power of Parliament to amend the Constitution and procedure therefore [Article 368].- (1) Notwithstanding anything in this Constitution, Parliament may in exercise of its constituent power amend by way of addition, variation or repeal any provision of this Constitution in accordance with the procedure laid down in this article. (2) An amendment of this Constitution may be initiated only by the introduction of a Bill for the purpose in either House of Parliament, and when the Bill is passed in each House by a majority of the total membership of that House and by a	In Article 368 of the Constitution, in clause (2), in the proviso, in clause (a), for the words and figures “ Article 162 or Article 241 ”, the words, figures and letter “ Article 162, Article 241 or Article 279A ” shall be substituted.	

Analysis of 122nd Constitutional Amendment Bill

	majority of not less than two-thirds of the members of that House present and voting, it shall be presented to the President who shall give his assent to the Bill and thereupon the Constitution shall stand amended in accordance with the terms of the Bill: Provided that if such amendment seeks to make any change in— (a) article 54, article 55, article 73, article 162 or article 241, or (b) Chapter IV of Part V, Chapter V of Part VI, or Chapter I of Part XI, or (c) any of the Lists in the Seventh Schedule, or (d) the representation of States in Parliament, or (e) the provisions of this article, the amendment shall also require to be ratified by the Legislatures of not less than one-half of the States by resolutions to that effect passed by those Legislatures before the Bill making provision for such amendment is presented to the President for assent. (3) Nothing in article 13 shall apply to any amendment made under this article. (4) No amendment of this Constitution (including the provisions of Part III) made or purporting to have been made under this article whether before or after the commencement of section 55 of the Constitution (Forty-second Amendment) Act, 1976 shall be called in question in any court on any ground. (5) For the removal of doubts, it is hereby		

Analysis of 122nd Constitutional Amendment Bill

	declared that there shall be no limitation whatever on the constituent power of Parliament to amend by way of addition, variation or repeal the provisions of this Constitution under this article.		
Schedule VI	<u>Amendment of Sixth Schedule - Para 8(3):-</u> 8. Powers to assess and collect land revenue and to impose taxes.— (1) The Regional Council for an autonomous region in respect of all lands within such region and the District Council for an autonomous district in respect of all lands within the district except those which are in the areas under the authority of Regional Councils, if any, within the district, shall have the power to assess and collect revenue in respect of such lands in accordance with the principles for the time being followed by the Government of the State in assessing lands for the purpose of land revenue in the State generally. (2) The Regional Council for an autonomous region in respect of areas within such region and the District Council for an autonomous district in respect of all areas in the district except those which are under the authority of Regional Councils, if any, within the district, shall have power to levy and collect taxes on lands and buildings, and tolls on persons resident within such areas. (3) The District Council for an autonomous district shall have the power to levy and collect all or any of the following taxes within such district, that is to say—	In the Sixth Schedule to the Constitution, in paragraph 8, in sub-paragraph (3),— (i) in clause (c), the word "and" occurring at the end shall be omitted; (ii) in clause (d), the word "and" shall be inserted at the end; (iii) after clause (d), the following clause shall be inserted, namely:— "(e) taxes on entertainment and amusements."	<u>Amendments in Union, State List of Schedule VII of Constitution. Also, amendment in Sixth Schedule:</u> Schedule VI Para 8(3) of Schedule VI empowers the district councils to levy and collect taxes on certain items. One insertion is further proposed in the same i.e. "Taxes on entertainment and amusements"

Analysis of 122nd Constitutional Amendment Bill

	(a) taxes on professions, trades, callings and employments; (b) taxes on animals, vehicles and boats; (c) taxes on the entry of goods into a market for sale therein, and tolls on passengers and goods carried in ferries; and (d) taxes for the maintenance of schools, dispensaries or roads. (4) A Regional Council or District Council, as the case may be, may make regulations to provide for the levy and collection of any of the taxes specified in sub-paragraphs (2) and (3) of this paragraph and every such regulation shall be submitted forthwith to the Governor and, until assented to by him, shall have no effect.		
Schedule VII	<u>Amendment of Seventh Schedule:-</u> <u>List I (Union List)-</u> <u>Entry 84:</u> Duties of excise on tobacco and other goods manufactured or produced in India except— (a) alcoholic liquors for human consumption; (b) opium, Indian hemp and other narcotic drugs and narcotics, but including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry. <u>Entry 92:</u>	In the Seventh Schedule to the Constitution,— (a) in List I — Union List,— (i) for Entry 84, the following entry shall be substituted, namely:— "84. Duties of excise on the following goods manufactured or produced in India, namely:— (a) petroleum crude; (b) high speed diesel; (c) motor spirit (commonly known as petrol); (d) natural gas; (e) aviation turbine fuel; and (f) tobacco and tobacco products."; (ii) Entries 92 and 92C shall be omitted;	Schedule VII – Union List a) Duties of excise on goods manufactured in India done away except petroleum, High speed diesel, petrol, natural gas, aviation turbine fuel and tobacco or tobacco products. (No. 84) b) Taxes on the sale or purchase of newspapers and on advertisements published therein – Done Away (No. 92) c) Entry related to interstate purchase and sale of goods (92C) – Done Away

Analysis of 122nd Constitutional Amendment Bill

	Taxes on the sale or purchase of newspapers and on advertisements published therein. <u>Entry 92C:</u> Taxes on services. <u>List II (State List) –</u> <u>Entry 52:</u> Taxes on the entry of goods into a local area for consumption, use or sale therein. <u>Entry 54:</u> Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of List I. <u>Entry 55:</u> Taxes on advertisements other than advertisements published in the newspapers and advertisements broadcast by radio or television. <u>Entry 62:</u> Taxes on luxuries, including taxes on entertainments, amusements, betting and	(b) in List II — State List,— (i) Entry 52 shall be omitted; (ii) for Entry 54, the following entry shall be substituted, namely:— "54. Taxes on the sale of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption, but not including sale in the course of inter-State trade or commerce or sale in the course of international trade or commerce of such goods. (iii) Entry 55 shall be omitted; (iv) for Entry 62, the following entry shall be substituted, namely:—	Schedule VII – State List a) Entry Tax – Done Away (No. 52) b) Taxes on advertisements – Done away (No. 55) c) Taxes on entertainment and amusements (Entry No. 62) – Applicable to the extent levied and collected by district / regional councils. d) Entry No. 54 on sale of goods, now scope reduced to petroleum, High speed diesel, petrol, natural gas, aviation turbine fuel and tobacco or tobacco products except in case of interstate trade or international trade or commerce.

Analysis of 122nd Constitutional Amendment Bill

	gambling.	"62. Taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council.	
	Other Modalities - Newly Inserted		
	Clause 18 of The Constitutional (One Hundred and Twenty-second Amendment) Bill, 2014.	Arrangement for assignment of additional tax on supply of goods to States for two years or such other period recommended by the Council. (1) An additional tax on supply of goods, not exceeding one per cent. in the course of inter-State trade or commerce shall, notwithstanding anything contained in clause (1) of article 269A, be levied and collected by the Government of India for a period of two years or such other period as the Goods and Services Tax Council may recommend, and such tax shall be assigned to the States in the manner provided in clause (2). (2) The net proceeds of additional tax on supply of goods in any financial year, except the proceeds attributable to the Union territories, shall not form part of the Consolidated Fund of India and be deemed to have been assigned to the States from where the supply originates. (3) The Government of India may, where it considers necessary in the public interest, exempt such goods from the levy of tax under clause (1). (4) Parliament may, by law, formulate the principles for determining the place	<u>Other Modalities:</u> a) An additional tax on supply of goods, not exceeding one per cent. in the course of inter-State trade or commerce shall, notwithstanding anything contained in clause (1) of Article 269A, be levied and collected by the Government of India for a period of two years or such other period as the, Goods and Services Tax Council may recommend and such tax shall be assigned to the states in manner as provided hereunder in (b). b) The net proceeds of additional tax on supply of goods in any financial year, except the proceeds attributable to the Union territories, shall not form part of the Consolidated Fund of India and be deemed to have been assigned to the States from where the supply originates. c) The Government of India may, where it considers necessary in the public interest, exempt such goods from the levy of tax under clause (1). This is exemption pertaining to the additional tax as referred above. d) Parliament may, by law, formulate the

Analysis of 122nd Constitutional Amendment Bill

		of origin from where supply of goods take place in the course of inter-State trade or commerce.	principles for determining the place of origin from where supply of goods take place in the course of inter-State trade or commerce.
	Clause 19 of The Constitutional (One Hundred and Twenty-second Amendment) Bill, 2014.	Compensation to States for loss of revenue on account of introduction of goods and services tax. Parliament may, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for such period which may extend to five years.	e) Parliament may, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for such period which may extend to five years.
	Clause 20 of The Constitutional (One Hundred and Twenty-second Amendment) Bill, 2014.	Transitional provisions. Notwithstanding anything in this Act, any provision of any law relating to tax on goods or services or on both in force in any State immediately before the commencement of this Act, which is inconsistent with the provisions of the Constitution as amended by this Act shall continue to be in force until amended or repealed by a competent Legislature or other competent authority or until expiration of one year from such commencement, whichever is earlier.	f) Necessary provisions for transition and power of president to remove difficulties incorporated.
	Clause 21 of The Constitutional (One Hundred and Twenty-second Amendment) Bill, 2014.	Power of President to Remove difficulties (1) If any difficulty arises in giving effect to the provisions of the Constitution as amended by this Act (including any difficulty in relation to the transition from the provisions of the Constitution as they stood immediately before the date of assent of the President to this Act to the	

Analysis of 122nd Constitutional Amendment Bill

		provisions of the Constitution as amended by this Act), the President may, by order, make such provisions, including any adaptation or modification of any provision of the Constitution as amended by this Act or law, as appear to the President to be necessary or expedient for the purpose of removing the difficulty: Provided that no such order shall be made after the expiry of three years from the date of such assent. (2) Every order made under sub-section (1) shall, as soon as may be after it is made, be laid before each House of Parliament.	

The IT Strategy for GST

Empowered Group on IT Infrastructure on GST headed by
Shri Nandan Nilekani

Preface

The broad IT plan for enabling GST was presented to the Government of India and the Empowered Committee of State Finance Ministers under the Chairmanship of Dr. Asim Dasgupta on July 21, 2010. This document is a follow-up to that presentation and feedback thereon and describes the IT strategy for GST implementation.

This document is at the draft stage, and will evolve as various stakeholders and experts are consulted.

1. Table of Contents

Preface.....	1
1. Introduction	2
1.1 The merits of GST.....	2
1.2 Urgency.....	2
2. An IT infrastructure for GST	3
2.1 Desirable features of Goods & Service Tax Network (GSTN).....	3
2.2 Stakeholders.....	4
2.3 Workflows	5
3. The solution architecture	6
3.1 A common GST portal	6
3.2 Basic solution architecture	7
3.3 Information Flow	8
3.4 Funds flow	9
4. Tax Booster.....	10
4.1 Tax computation and accounting.....	10
4.2 Tax booster.....	11
5. Implementation plan	12
6. Current Status of GSTN implementation.....	12

1. Introduction

1.1 The merits of GST

GST will bring about a change in the tax system by redistributing the burden of taxation equitably between manufacturing and services. GST will enable broadening of the tax base, which will further result in reduction in effective rate of tax. It will reduce distortions by applying the destination principle for levy of taxes. It will foster a common market across the country, reduce compliance costs and promote exports. It can provide a fiscal base for local bodies to enable them to fulfill their obligations. It will facilitate investment decisions being made on purely economic concerns independent of tax considerations.

1.2 Urgency

The broad framework of GST is now clear, with the model being approved by the Government of India and Empowered Committee of State Finance Ministers. The GST will be a dual tax with both Central and State GST component levied on the same base. The IGST framework will be used for goods and services that are exported across state boundaries. Thus, all goods and services, barring a few exceptions, will be brought into the GST base. For reasons of simplicity for the taxpayer, ease of tax administration, and bringing about a national common market, a common PAN-based taxpayer ID, a common return, and a common challan for tax payment have been agreed to by all stakeholders.

A number of issues still remain to be resolved. These are presently under the consideration of the Empowered Committee of State Finance Ministers under the Chairmanship of Dr Asim Dasgupta. Such issues include: the rates of taxation, the revenue sharing between States and Centre, and a framework for exemption, thresholds and composition.

On the IT front, there has been consensus that there will be a common portal providing three core services (registration, returns and payments). The broad services framework of the portal has been discussed with the Sub Working group for IT. Various technology issues have been addressed including solution architecture and selection of likely service provider. However many other related issues need to be addressed which are on the critical path for GST going live by April 2011. Some of these issues include incubation, ownership and governance structures, development, deployment, and integration of existing systems, and change management procedures, among others. An update on some of these issues is provided in Section 6 of this document.

Without a well-designed and well-functioning IT system, the benefits of GST will remain elusive. It is important that the design and implementation of the GST IT systems start without any further delay, and consensus is achieved on the unresolved policy issues in the earliest possible timeframe.

2. An IT infrastructure for GST



Figure 1: Desirable features of GSTN

2.1 Desirable features of Goods & Service Tax Network (GSTN)

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

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

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

Enable digitization and automation of the whole chain: All the business processes surrounding GST should be automated to the extent possible, and all documents processed electronically. This will lead to faster processing and reconciliation of tax information and enable

risk based scrutiny by tax authorities. For small taxpayers, facilitation centres can be set up to ease the migration.

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

Leverage existing investments: Existing IT investments of states should be leveraged. The Mission Mode Project on Commercial Tax should be aligned with the GST implementation going forward.

2.2 Stakeholders

The design of an IT infrastructure should serve all stakeholders and their business processes. The various stakeholders in a GST IT implementation are as follows (Figure 2):



Figure 2: Stakeholders

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

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

State tax authorities: The state tax authorities would be responsible for collecting SGST. Common file formats, interfaces, and policy administration will enable accurate and timely

assessment, and risk-based investigations resulting in enhanced productivity and revenues.

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

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

Banks: Banks will accept duty from the taxpayers and process challans. All tax collections (whether physical or electronic) will happen at bank branches, or through the banks' IT systems. Banks will route the tax collected to the concerned authorities through the RBI channel.

Other Stakeholders include CAG, GSTN, TRPs and facilitation agencies.

2.3 Workflows

The following three processes constitute the most important workflows of the GST administration and would be covered in the first phase:

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

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

Challans: Challans are the payment instruments used by taxpayers to actually pay their taxes. Challans are deposited at collecting banks and are forwarded by them to the tax administrations.

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

In addition, there are several other workflows such as processing refunds, taxpayer audits, and appeals. It is reiterated that the **core services** envisaged through common portal are limited to registration, payments and returns in the first phase. Other value added services will be added subsequently based on the needs of the Stakeholders. The IT infrastructure should be designed taking into account all stakeholders (Figure 2), and all related workflows (Figure 3)



Figure 3: Workflows

3. The solution architecture

3.1 A common GST portal

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

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

Figure 4 shows the solution architecture, the role of the common GST portal, and its connections with other systems.

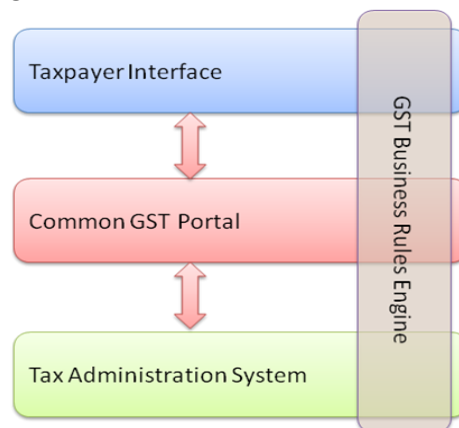


Figure 4: Solution Architecture

A common GST portal, operated by GSTN, is the fastest and most cost-effective way to provide common PAN-based registration, common returns, and common challans for all stakeholders. It can marry the taxpayers standard interface with the varied systems of the tax administrations. Each tax authority will have full flexibility in using this data for in-house automation, integration, and enforcement.

3.2 Basic solution architecture

Given the need for a common GST portal, the basic solution architecture is as follows:

1. Taxpayer files through a standardized taxpayer interface.
2. States and CBEC implement tax administration systems for assessments, audits, and enforcement within their domain. This is desirable but not a pre-condition since the GSTN can provide support for states that do not have the necessary IT systems in place.
3. The taxpayer and tax authority systems are connected with a Common GST Portal, operated by GSTN.
4. Policy decisions are captured in GST Business Rules Engine that defines the tax rates, revenue sharing rules, and exceptions for all parties.

The Business Rules Engine is a component of the solution architecture that spans all entities. It codifies policies and business rules such as the rates of taxation, the revenue sharing between states and centre, a framework for exemption, and thresholds, among other things. All systems in the rest of the solution architecture will be designed so that they load business rules from the Business Rules Engine. This decoupling of the business rules from the rest of the solution architecture allows for a great deal of flexibility. At a later date, if rates are changed or new items are added to the list of taxable items, or if existing items are exempted; these changes can be reflected in the Business Rules Engine, without affecting the rest of the system. This also makes it possible to start the design and implementation of all IT systems, even while policies and rates are debated. Once the policies and rates are fixed, they can simply be reflected in the Business Rules Engine.

In addition to common registration, returns, and challans, the Common GST portal will provision for selected information needs of states.

3.3 Information Flow

Information flows unmodified through Common GST Portal to states and CBEC
Common GST Portal will also integrate with systems of CBDT, MCA, etc.

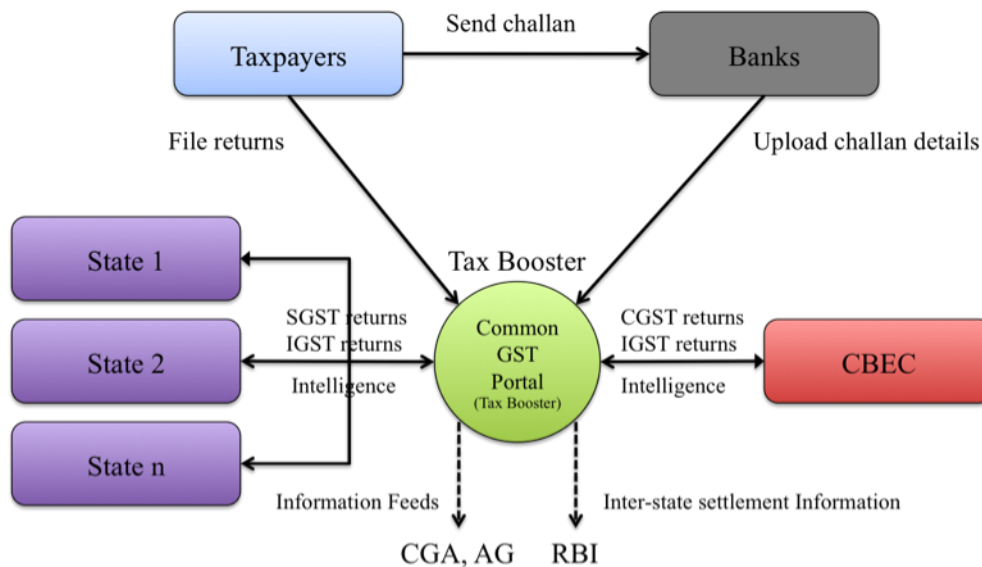


Figure 5: Information flow

The information flows are shown in Figure 5 are designed keeping the constitutional autonomy of states in mind, while simultaneously building intelligence in the system to plug leakages. The common GST portal is simply a pass-through device. The taxpayer files the return with GSTN, which keeps a copy of the return for analysis, and forwards it in near real-time to the respective state and CBEC. The taxpayer pays the actual duty in the bank, which uploads only the challan details into the GSTN. Actual funds never pass through the GSTN.

The common GST portal reconciles the returns and the challans. In addition to its pass-through role, the common GST portal also plays two other critical roles:

1. It acts as a tax booster, matching the input tax credits in the returns to detect tax evasion. It can also integrate with various other systems at MCA, CBDT for verification of PAN or other corporate information and perform data mining and pattern detection to detect tax fraud. It sends this information as alerts/ reports to the respective tax authorities.
2. It also computes inter-state settlement, netting IGST across states.

3.4 Funds flow

State funds flow directly from taxpayers to the states
Centre funds flow directly from taxpayers to centre

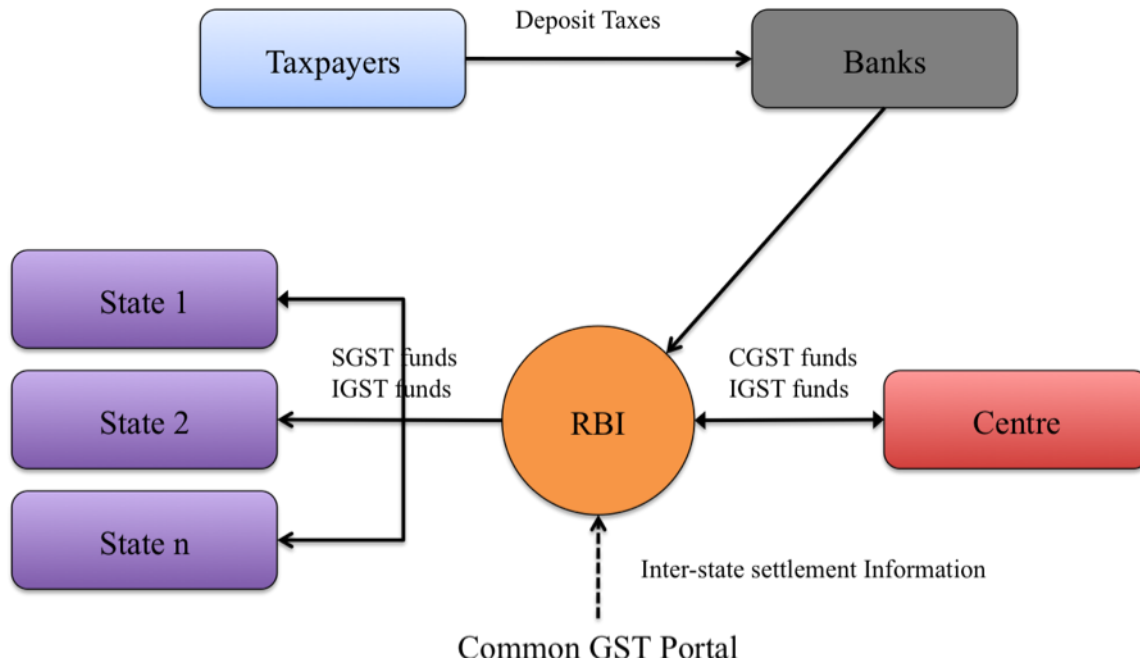


Figure 6: Funds flows

Just like the information flows, the funds flows (Figure 6) are also designed keeping the constitutional autonomy of states in mind. The design ensures smooth and timely availability of funds as soon as they are deposited. The SGST funds that are intended for the states directly go from the taxpayer to the state treasuries. Similarly, the CGST funds go directly to the centre. With the help of information from GSTN, IGST will be settled between states and centre by RBI.

4. Tax Booster

4.1 Tax computation and accounting



Figure 7: Levels of granularity for returns

The tax returns can be filed at various levels of granularity, as shown in Figure 7.

1. **Aggregate level:** A taxpayer aggregates all his sales and purchases made across all the customers/ vendors and files one return.
2. **Dealer level:** A taxpayer aggregates all his sales and purchases made across all the customers/ vendors and files one return along with the transactions consolidated customer/ vendor wise.
3. **Invoice level:** A taxpayer aggregates all his sales and purchases made across all the customers/ vendors and files one return along with the transactions details provided invoice wise.
4. **Line item level:** A taxpayer aggregates all his sales and purchases made across all the customers/ vendors and files one return along with the invoice wise transactions capturing item wise details as well.

Invoice level detail is necessary for the reconciliation of tax deposits, and the end-to-end reconciliation of ITC. An effective IGST implementation may also require invoice-level details. A number of states are capturing invoice details even in the existing VAT systems. It is proposed to follow a two-pronged approach with Dealer level granularity of returns in the first phase followed by invoice level in the next phase. This issue is currently being discussed in the IT sub-

working group for evolving consensus.

There has been some concern around reconciliation of ITC at invoice-level detail due to the sheer volume of data. However, this scale is no different than what organizations such as NSE, NSDL, RBI, and banks handle on a daily basis. Experience at states that have implemented this also shows that match quality is low initially, but improves significantly over time.

4.2 Tax booster

Type of fraud	Common GST Portal: Intelligence based deterrence
Fraudulent bills	Matching
Improper Input Tax Credit	Matching
Fraudulent use of 'exempt' rules	Electronic returns
False payment proofs	Electronic challans
Unrecorded sales	Data mining
Misuse of composition method	Data mining
Wrongful application of lower tax	Data mining
Under-invoicing	Data mining
Non-existent dealers	Data mining

Figure 8: Types of frauds

As taxpayers start filing invoice level returns, the common GST portal can start analysing the data for tax evasion and fraud. Common formats for returns and payments, combined with electronic filing and electronic payments, and a standardized PAN-based registration makes the data consistent, and amenable to mining.

Some of the common frauds, and how they may be combated are shown in Figure 8. Assuming VAT collections of Rs.1,50,000 crores across all states, and a potential for a 20% increase in collections, the common GST portal can lead to additional revenues of up to Rs.30,000 crores.

5. Implementation plan

Owner	Component
Taxpayer	User registration (PAN-based) File returns Tax payments
GSTN	User registration (PAN-based) Acceptance and Consolidation of returns Challan reconciliation Matching of Input Tax Credit Dashboard and MIS Helpdesk and facilitation centres
Tax Authorities	Assessment, audits, and enforcement Refunds Dispute resolution Helpdesk and facilitation centres
Banks and RBI	Tax payments and reconciliation
Accounting Authorities	Reconciliation

Figure 9: Owners of various components

The GST IT implementation requires various stakeholders to implement new IT systems, or modify existing systems. All these stakeholders are on the critical path for GST readiness in April 2011. Implementation plans for various stakeholders, and interfaces between stakeholders should be frozen, and agreed to by all before implementation can commence. Figure 9 lists the components to be implemented by various stakeholders to go live in April 2011.

6. Current Status of GSTN implementation

The Ministry of Finance, with the concurrence of the Empowered Committee of State Finance Ministers, has set up an *Empowered Group on IT Infrastructure for GST* with, inter alia, the mandate of approving the Solution architecture of the Common GST portal to be set up, Suggesting the modalities for setting up of a National Information Utility (NIU / SPV) and evaluating the suitability of the existing NIUs namely NSDL & NPCL for incubating the NIU/SPV for GST portal.

The 'Empowered Group on IT Infrastructure for GST' in its first meeting evaluated the feasibility of incubating the NIU, called GSTN, in NSDL and came to the conclusion that NSDL is well suited for this purpose. The scope of the project and implementation strategy is being worked out with the NSDL.

73

**STANDING COMMITTEE ON FINANCE
(2012-13)**

FIFTEENTH LOK SABHA

**MINISTRY OF FINANCE
(DEPARTMENT OF REVENUE)**

**THE CONSTITUTION
(ONE HUNDRED FIFTEENTH AMENDMENT) BILL, 2011**

SEVENTY THIRD REPORT



**LOK SABHA SECRETARIAT
NEW DELHI**

August, 2013, Sravana, 1935 (Saka)

SEVENTY THIRD REPORT

**STANDING COMMITTEE ON FINANCE
(2012-2013)**

(FIFTEENTH LOK SABHA)

THE CONSTITUTION (ONE HUNDRED FIFTEENTH AMENDMENT) BILL, 2011

Presented to Lok Sabha on 7 August, 2013

Laid in Rajya Sabha on 7 August, 2013



**LOK SABHA SECRETARIAT
NEW DELHI**

August, 2013, Sravana, 1935 (Saka)

CONTENTS

Page Nos.

Composition of the Committee.....

Introduction.....

REPORT

PART -I

I.	GST Design	1
II.	Salient features of the Bill	7
III.	Impact of GST on :	
	(a) Economy	11
	(b) Prices	15
	(c) Consumer prices – International experiences	17
	(d) Producing States and Consuming States	18
	(e) MSME and Employment Generation	19

PART-II

IV.	Issues relating to Amendment Bill	22
	(a) Power to make laws with respect to Goods & Services Tax	22
	(b) Integrated Goods and Services Tax (IGST)	24
	(c) GST Council	26
	(d) Goods & Services Tax Dispute Settlement Authority	32
	(e) Declared Goods (Article 286)	35
	(f) Goods and Services Tax (Article 366)	36
	(g) Amendment of Sixth Schedule to the Constitution	40
	(h) Amendment of Seventh Schedule to the Constitution	41
	(i) Transitional Provision	44
V.	Administration and IT Mechanism	45
VI.	Compensation Mechanism	46
VII.	GST Monitoring Cell	47
VIII.	Alternative to GST Model	48
IX.	Latest position of the Empowered Committee of State Finance Ministers on the provisions of the Bill	50
X.	Consensus between Centre and States on GST Design and CST Compensation	53

Part-III

Observations / Recommendations	55

APPENDICES

- I. Notes of Dissent submitted by Shri Naresh Agrawal , MP.....
- II. Minutes of sittings of the Committee held on 8 June, 2012, 15 June, 2012,
27 June, 2012, 6 July, 2012, 13 July, 2012, 20 July, 2012, 27 July, 2012
21 January, 2013, 28 June, 2013 and 19 July, 2013.....
- III. The Constitution (One Hundred Fifteenth Amendment) Bill, 2011

COMPOSITION OF STANDING COMMITTEE ON FINANCE (2012-13)

Shri Yashwant Sinha - Chairman

MEMBERS

LOK SABHA

2. Shri Suwendu Adhikari
3. Dr. Baliram
4. Shri Sudip Bandyopadhyay*
5. Shri Udayanraje Bhonsle
6. Shri Nishikant Dubey
7. Shri Gurudas Dasgupta
8. Shri Rahul Gandhi
9. Shri Deepender Singh Hooda
10. Shri Chandrakant Khaire
11. Shri Bhartruhari Mahtab
12. Dr. Chinta Mohan
13. Shri Sanjay Brijkishorlal Nirupam
14. Shri Prem Das Rai
15. Shri S.S. Ramasubbu
16. Vacant**
17. Shri Adv. A. Sampath
18. Shri Thakur Anurag Singh
19. Dr. M. Thambidurai
20. Shri Shivkumar Udasi
21. Shri Dharmendra Yadav

RAJYA SABHA

22. Shri Naresh Agrawal
23. Shri Rajeev Chandrasekhar
24. Smt. Renuka Chowdhury
25. Shri Piyush Goyal
26. Shri Satish Chandra Misra
27. Dr. Mahendra Prasad
28. Shri Ravi Shankar Prasad
29. Shri P. Rajeeve
30. Shri Praveen Rashtrapal
31. Dr. Yogendra P. Trivedi

SECRETARIAT

1. Shri A.K. Singh	- Joint Secretary
2. Shri Ramkumar Suryanarayanan	- Additional Director
3. Shri Kulmohan Singh Arora	- Under Secretary

* *Nominated as Member of the Standing Committee on Finance w.e.f 13th December, 2012*

** *Dr. Kavuru Sambasiva Rao, MP ceased to be the Member of the Committee w.e.f 17.06.2013 consequent upon his induction to the Union Council of Ministers*

INTRODUCTION

I, the Chairman of the Standing Committee on Finance, having been authorized by the Committee, present this Seventy-third Report on the Constitution (One Hundred Fifteenth Amendment) Bill, 2011.

2. The Constitution (One Hundred Fifteenth Amendment) Bill, 2011 introduced in Lok Sabha on 22 March, 2011, was referred to the Committee on 29 March, 2011 for examination and report thereon, by the Speaker, Lok Sabha under rule 331E of the Rules of Procedure and Conduct of Business in Lok Sabha.

3. The Committee took briefing/oral evidence of the representatives of the Ministry of Finance (Department of Revenue) at their sitting held on 8th June, 2012.

4. The Committee, at their sitting held on 8th June, 2012 heard the views of Dr. Asim Kumar Dasgupta, Former Finance Minister, West Bengal and Former Chairman, Empowered Committee of the State Finance Ministers. At the sitting held on 15th June, 2012, Shri Sushil Kumar Modi, Deputy Chief Minister, Bihar & Chairman, Empowered Committee of the State Finance Ministers, representative of Federation of Indian Chamber of Commerce and Industry (FICCI), Confederation of Indian Industry (CII), Petroleum Federation of India (PETROFED) and International Spirits & Wines Association of India (ISWAI) presented their views before the Committee. On 27th June, 2012, the Committee heard the views of the representatives of Indian Merchants' Association (IMA), Film and Television Producers Guild of India, All India Federation of Tax Practitioner (AIFTP) and Bhartiya Udyog Vyapar Mandal (BUVM). The Committee at their sitting held on 6th July, 2012 heard the views of the representatives of Government of Madhya Pradesh. On 13th July, 2012, the Committee heard the views of Dr. Parthasarathi Shome, Director & Chief Executive, Indian Council for Research on International Economic Relations (ICRIER), Dr. Vijay L. Kelkar, Chairman, National Stock Exchange of India Ltd. (NSE) & Former Chairman Thirteenth Finance Commission, and the

representatives of Governments of Odisha, Tamil Nadu and Maharashtra. The Committee also heard the views of the representatives of Government of Gujarat at their sitting held on 20th July, 2012. The Committee once again heard the views of Dr. Vijay L. Kelkar at their sitting held on 27th July, 2012.

5. The Committee considered and adopted the draft report and authorized the Chairman to finalise the same and present it to the Parliament at their sittings held on 28 June, 2013 and 19 July, 2013.

6. The Committee wish to express their thanks to the officials of the Ministry of Finance (Department of Revenue) concerned with the Bill for their cooperation and all the State Governments, Organisation, Associations and Experts for their valuable suggestions on the amendment Bill.

7. For facility of reference, the observations/recommendations of the Committee have been printed in thick type in the body of the Report.

**New Delhi;
25 July, 2013
03 Sravana, 1935 (Saka)**

**YASHWANT SINHA,
Chairman,
Standing Committee on Finance.**

REPORT

Part - I

The Constitution (One Hundred and Fifteenth Amendment) Bill, 2011, which has been referred to the Standing Committee on Finance of Parliament for detailed examination and Report seeks to bring fundamental systemic reforms in the indirect taxes dispensation prevailing in the country by integrating and harmonizing the tax structure across the country in the form of Goods and Services Tax (GST). The proposed amendments in the Constitution are targeted to achieve the objective of conferring simultaneous power on Parliament and State legislatures to make laws for levying GST simultaneously on every transaction of supply and goods & services. In addition, the proposed amendments would allow subsuming of a number of indirect taxes presently being levied by Central & State Governments into GST and thus will remove cascading of taxes and provide a common national market for goods and services. Before discussing at length the various issues emanating from the provisions of the Constitution (One Hundred and Fifteenth Amendment) Bill, 2011, it would be useful to have a brief overview of the proposed amendment Bill.

I. GST Design

2. GST is recognized internationally as a destination based consumption tax which is least distortionary. The broad objectives of introducing the Goods and Services Tax (GST) in India are to expand the tax base through wider coverage of economic activities and reduction in exemptions; mitigate cascading and double taxation and enable better compliance through the lowering of overall tax burden on goods and services. By removing hidden or embedded taxes, it would improve the competitiveness of domestic industry vis-à-vis imports and in international markets. By harmonizing the tax structure across States, this reform would also lead to the development of a common national market for goods and services.

3. The indirect tax system in the country has been going through a series of reforms over the last two decades. At the Central level, a Value Added Tax called, CENVAT, providing credit of tax paid on inputs and capital goods was introduced upto the manufacturing stage. Subsequently, in 1994, a tax on services (commonly known as Service Tax) was introduced by the Centre. The Service Tax has grown consistently in scope to cover more services and now applies to about 115 service categories with commensurate growth in revenue from this tax. In 2004, the input tax credit scheme for CENVAT and Service Tax was merged to permit cross flow of credit across these taxes. As for the States, they have switched over from a multiple point Sales tax to a Value Added Tax (VAT) covering all transactions of sale of goods within the State up to the retail stage in a phased manner starting from 2005-06.

4. Despite these measures, goods and services continue to be burdened with multiple indirect taxes at different stages of the value chain with significant tax cascading under the present indirect tax regime. The important reasons for this are as under:

- a) In respect of taxation of goods, CENVAT is confined to the “manufacturing” stage and does not extend to the distribution chain beyond the factory gate. As such, CENVAT paid on goods cannot be neutralized against State VAT payable on subsequent sale of goods. This is true both for CENVAT collected on domestically produced goods as well as that collected as additional duty of customs on imported goods.
- b) CENVAT is itself made up of several components in the nature of cesses and surcharges such as the National Calamity Contingency Duty (NCCD), education and secondary and higher education cess, additional duty of excise on tobacco and tobacco products etc. This multiplicity of duties complicates the tax structure and often obstructs the smooth flow of tax credit.
- c) While input tax credit of CENVAT or additional duty of customs paid on goods is available to service providers paying Service Tax, they

are unable to neutralize the State VAT or other State taxes paid on their purchase of goods.

- d) State VAT is payable on the value of goods inclusive of CENVAT paid at the manufacturing stage so that the VAT liability of a dealer gets inflated by this component without compensatory set-off.
- e) Inter-State sale of goods attracts the Central Sales Tax (CST) levied by the Centre and collected by the States. This is an origin-based tax and cannot be set-off against VAT in many situations.
- f) State VAT and CST do not directly apply to the import of goods on which special additional duties of customs are levied at a uniform rate of 4% by the Centre. Input tax credit of these duties is available only to those manufacturing excisable goods. Other importers have to claim refund of this duty as and when they pay VAT on subsequent sales.
- g) VAT dealers are unable to set-off any Service Tax that they may have paid on their procurement of taxable input services.
- h) State Governments also levy and collect a variety of other indirect taxes such as luxury tax, entertainment tax, entry tax etc. for which no set-off is available.

5. Introduction of GST is a logical culmination of the tax reform process involving the switch over to CENVAT; levy of service tax and the transition from sales tax to state VAT. By replacing a large number of taxes levied both by the Centre and the States, GST would integrate the tax base and allow seamless flow of input tax credit across the value chain of goods and services. This would eliminate multiplicity of taxes, cascading of taxes and overall simplification of indirect taxation regime. Seamless input tax credit chain will lead to reduced cost of goods and services. As the credit chain will function only if all the transactions are recorded, GST environment would lead to improved disclosure of economic transactions which may have a positive impact on direct tax collections also.

6. It is in the context of India's federal structure that a dual GST, wherein both the Centre and the States concurrently levy and collect the tax, has been envisaged. It would be mutually beneficial to both by allowing an expansion of their respective fiscal space; and better tax compliance.
7. Internationally, comprehensive Goods & Services tax has already been introduced in more than 100 countries across the world. The Empowered Committee of State Finance Ministers (EC) has visited and studied the best practices of many countries like Australia, Brazil, etc. which has similar political structure as that of India. At the same time, the Indian model would have to be unique owing to the quasi-federal nature of its polity.
8. Under the GST regime, both the Centre and the State would have the powers to tax the "supply" of goods and services right from their primary stage to final consumption. Such a regime with IGST on inter-state supplies would result in establishing a seamless Input Tax Credit (ITC) chain from the primary to the tertiary stage. Such seamless credit chain and the removal of differential in tax rates on inter-state and intra-state transactions are likely to lower costs for the consumers and will result in better tax compliance.
9. In addition since all the dealers will be given PAN based registration number under GST regime and will be required to file returns on a common portal, more robust information sharing and analysis between the Centre and the States as also amongst States would be feasible. This will definitely help in checking evasion and boost revenues of the Centre as well as States since currently, there is no systematic sharing of information between Central and State tax administrations allowing sufficient scope for wrong reporting by dealers and thus the tax evasion. Under the existing system, Centre and States have been granting relief from payment of tax to promote investments. This leads to a lot of inefficiency in the taxation system. It is expected that in Centre as well as States will not grant such tax relief in the GST regime to make taxation system more efficient.

10. The benefits of GST can be summarized as under :

- For business and industry
 - Easy compliance
 - Removal of cascading
 - Improved competitiveness
- For Central and State Governments
 - Simple and easy to administer
 - Better controls on leakage
 - Consolidation of tax base
 - Higher revenue efficiency
- For the consumer
 - Single and Transparent tax proportionate to the value of goods and services
 - Reduction of prices

11. GST, by its design, encourages the system to be transparent. There is an inbuilt system of Input Tax Credit i.e. the tax paid at earlier stage of the production distribution chain will be set off at the final stage of sale of goods and services. Also the rate arbitrage between the inter-state and intra-state supplies will get eliminated. This is because it is proposed to equalize the total rate of tax applicable to intra- and inter-state supplies unlike the present regime where the CST rate is 2% while the normal VAT rate is either 5% or 12.5%. Thus it is expected that tax evasion would be largely reduced. The Centre and States today fix rate of tax and grant exemptions many times not in sync with each other. States also try to compete with each other to attract investment etc. and offer reduced rate of tax on select goods, which leads to tax rate war between States and ultimately hurts them. The affected State today has no forum to go to get its grievance redressed. The Bill proposes to set up GST council which after discussion will recommend rate of tax etc. to Centre as well as States. Centre and States will be expected to follow the recommendations of the GST Council and State and Centre will have a forum in the form of GST Dispute Settlement Authority for seeking redressal of grievances related to loss of revenue because

of such deviating action of the other State which may have affected their revenue. This will bring transparency, accountability and efficiency in the tax administration and reduce the arbitrage opportunities available to tax avoidance and evasion.

II. Salient Features of Constitution (Amendment) Bill

12. The Constitution (One Hundred and Fifteenth Amendment) Bill, 2011 was introduced in Lok Sabha on 22 March, 2011 and subsequently referred by the Hon'ble Speaker, Lok Sabha to the Standing Committee on Finance on 29 March, 2011 for examination and Report thereon. The Salient features of the Bill are outlined below:

- (a) The term 'Goods and Services Tax (GST)' is proposed to be defined in the main body of the Constitution and no new entry is proposed to be added in any Union, State or Concurrent list.
- (b) A new Article 246A is proposed to be added, which will confer simultaneous power to Union and State legislatures to legislate on GST.
- (c) A Goods & Services Tax Council (Article 279A) will be created, which will be a joint forum for the Centre and the States to discuss important issues relating to GST so that the objective of having a harmonized structure for GST and a harmonized national market can be achieved. This Council would function under the Chairmanship of the Union Finance Minister and will have Minister in charge of Finance/Taxation or Minister nominated by each of the States & UTs with legislatures, as members. The Council will make recommendations to the Union and the States on important parameters like rates, exemption list, threshold limits, etc. The Recommendations made by this Council will act as benchmark or guidance to Union as well as State Governments. The Parliament as well as State Legislatures will be free to exercise their power on all issues recommended by the Council. One-third of the total number of Members of the Council will constitute the quorum of GST council. It is further provided that the decisions of the GST Council shall be with the consensus of all members present at the

meeting. This is to protect the interests of each State and the Centre when the Council takes a decision.

- (d) In exercise of their powers, these legislative bodies may deviate from the recommendations of the Council and may act in a manner which is prejudicial to the harmonious working of GST or which adversely impacts the revenue of some other State/Central Government. Such deviations or actions are required to be kept to the minimum, if the objective of having a common national market and smooth working of GST is to be achieved. It is accordingly proposed to set up Goods & Services Tax Dispute Settlement Authority (Article 279B), which may be approached by the affected Government (whether the Centre or the States) seeking redressal for any loss caused by any action due to a deviation from the recommendations made by the Goods & Services Tax Council or for adversely affecting the harmonious structure and implementation of the GST.
- (e) Subsuming of various Central and State indirect taxes and levies in GST is proposed to be ensured through this set of Constitutional amendments.
- (f) Power to levy Integrated GST on inter-State supply of goods & services is to be given to Centre.
- (g) Certain goods like Crude Petroleum, Diesel, Petrol, Aviation Turbine Fuel, Natural Gas and alcohol for human consumption etc. are proposed to be kept out of the ambit of GST.

Background

13. The Empowered Committee of State Finance Ministers (EC) was requested to prepare a design of the proposed GST. After several years of effort and constant interaction with the Department of Revenue, Government of India, the Empowered Committee of State Finance Ministers released the “First Discussion Paper on GST in India” in November, 2009. Following several rounds

of discussion between the EC and the Central Government, certain important design parameters of GST have been agreed as follows:

- (a) There will be a dual GST model for the country, wherein the first component, namely, Central GST will be levied and collected by the Central Government and the second component, namely, the State GST will be levied, collected and appropriated by each of the States. The proceeds of the Central GST would be shared between the Centre and the States on the basis of the devolution formula recommended by the Finance Commission and accepted by the Government.
- (b) The proposed Central and State GST would be levied on all transactions involving supply of goods and services except those that are exempt or kept out of the purview of the GST.
- (c) Central and State indirect taxes and levies listed below would be subsumed under the proposed GST:

Central tax/levies to be subsumed

- (i) Central Excise Duty;
- (ii) Additional Excise Duties;
- (iii) The excise Duty levied under the Medicinal and Toiletries Preparation Act;
- (iv) Service Tax;
- (v) Additional Customs Duty, commonly known as Countervailing Duty (CVD);
- (vi) Special Additional Duty of Customs – 4% (SAD);
- (vii) Surcharges; and
- (viii) Cesses.

State taxes and levies to be subsumed

- (i) VAT/Sales tax;
- (ii) Entertainment tax (unless it is levied by the local bodies);
- (iii) Luxury tax;

- (iv) Taxes on lottery, betting and gambling;
 - (v) State Cesses and Surcharges in so far as they relate to supply of goods and services; and
 - (vi) Entry tax not in lieu of Octroi.
- (d) Integrated GST (IGST) would be levied on inter-State transactions of Goods and Services. This IGST would be equivalent to the sum of CGST and SGST. 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. The IGST system would ensure that intended destination based system is followed under GST regime.
- (e) GST will also be levied on imports. The incidence of tax will generally follow the destination principle and the tax revenue corresponding to SGST will accrue to the State where the imported goods and services are consumed. Input Tax Credit will be available of the GST paid on the import of goods and services.
- (f) In terms of coverage of goods, the proposed Goods and Services Tax will not apply to five specified petroleum products viz. crude petroleum, diesel, aviation turbine fuel and natural gas. On these items, the Centre would continue to levy Central Excise duty (CENVAT) while the States would continue to levy Sales tax. State excises on alcohol for human consumption and electricity duty on sale and consumption of electricity would not be subsumed under GST to begin with. Tobacco and its products would be subject to

GST, but, they would continue to bear Central Excise duty over and above the GST.

- (g) The proposed GST would thus be leviable on all transactions involving supply of goods and services except for exempted transactions. Consequently, the existing levies of CENVAT by the Centre and VAT by the States which apply to the 'manufacture' and 'sale' of goods respectively would be replaced. The taxable event for GST would thus no longer be manufacture or sale of goods but the 'supply of goods and services'.

III. Impact of GST on :

(a) Economy

14. A National Council of Applied Economic Research (NCAER) study, commissioned by the Thirteenth Finance Commission has stated that Implementation of a comprehensive GST across goods and services is expected, *ceteris paribus*, to provide gains to India's GDP somewhere within a range of 0.9 to 1.7 per cent. The corresponding change in absolute values of GDP over 2008-09 is expected to be between Rs. 42,789 crore and Rs. 83,899 crore, respectively. The comparable dollar value increment is estimated to be between \$ 18, 550 million, respectively.

15. The additional gain in GDP, originating from the GST reform, would be earned during all years in future over and above the growth in GDP which would have been achieved otherwise. The present value of the GST-reform induced gains in GDP may be computed as the present value of additional income stream based on some discount rate. Assuming a discount rate as the long-term real rate of interest at about 3 per cent, the present value of total gain in GDP has been computed as between Rs.1,469 thousand crores and 2,881 thousand crores. The corresponding dollar values are \$325 billion and \$637 billion.

16. Gains in exports are expected to vary between 3.2 and 6.3 per cent with corresponding absolute value range as Rs. 24,669 crore and Rs. 48,661 crore.

The comparable dollar value increment is estimated to be between \$5,427 million and \$10,704 million, respectively. Imports are expected to gain somewhere between 2.4 and 4.7 per cent with corresponding absolute values ranging between Rs. 31,173 crore and Rs. 61,501 crore. The comparable dollar value increment is estimated to be between \$6,871 million and \$13,556 million, respectively.

17. GST would lead to efficient allocation of factors of production. The overall price level would go down. It is expected that the real returns to the factors of production would go up. Our results show gains in real returns to land ranging between 0.42 and 0.82 per cent. Wage rate gains vary between 0.68 and 1.33 per cent. The real returns to capital would gain somewhere between 0.37 and 0.74 per cent.

18. Based on certain computations, the revenue neutral GST rate across goods and services is expected to be positioned somewhere in the range of 6.2 per cent and 9.4 per cent, depending on various scenarios of sectoral exemptions.

19. In sum, implementation of a comprehensive GST in India is expected to lead to efficient allocation of factors of production thus leading to gains in GDP and exports. This would translate into enhanced economic welfare and returns to the factors of production, viz. land, labour and capital.

20. When asked as to how GST would help fiscal consolidation, Dr. Vijay L. Kelkar, Ex-chairman, Thirteenth Finance Commission in his post-evidence replies stated as under :

“The changeover to GST is designed to be revenue neutral at existing levels of compliance. Given the design of the ‘flawless’ GST, the producers and distributors will only be pass through for the GST. Further, given the single and low rate of tax the benefit from evasion will significantly reduce. Therefore, there will be little incentive for the producers and distributors to evade their turnover. Accordingly, this policy initiative should witness a higher compliance and an upsurge in revenue collections. This will also have an indirect positive impact on direct tax collections. Further, given the fact that GST will trigger an increase in the GDP, this in turn would yield higher revenues even

at existing levels of compliance. Another important source of gain for the Government would be the savings on account of reduction in the price levels of a large number of goods and services consumed by the Government.

However, to the extent, the Central Government will be required to incentivise the States to adopt the GST, there will be an increase in the budgetary outgo. Given the smallness of the size of the compensation, it is expected that there would be a net gain in the tax revenues. This should enable the Central Government to better manage its finances.

As regards the State Governments, the design and the road map of the GST recommended by us would lead to substantial gain in revenues. While the revenue neutral rate for the States is estimated to be 6 percent, we have recommended that the states should be allowed to impose GST at the rate of 7 percent. An increase in the RNR of the States by 1 percent implies a revenue gain of Rs. 31381 crores per annum in the base year 2007-08 (i.e. 16.67 percent increase in the revenues). This gain will be further augmented by better compliance.

Therefore, overall the implementation of GST should enable the Government at both levels to better meet the challenges of fiscal correction.

GST will positively impact the common man in many ways. **Firstly**, it will add to the overall economic growth by removing economic distortions. It will create new employment opportunities (about 20 million high end jobs over a period of time) thereby increasing the levels of income across a large section of the society. **Secondly**, it will reduce inflation if GST is levied at the combined rate of 12 percent as recommended by the Thirteenth Finance Commission. **Thirdly**, it will decentralize production to areas enjoying comparative advantage so more jobs can be expected to be created in rural areas. This will in turn slow down the pace of migration to urban areas. **Fourthly**, it will improve governance since the introduction of a comprehensive GST will bring about more transparency and an end to crony capitalism. **Finally**, GST can create further opportunities for relief under direct taxes over time since it is viewed as a revenue generating machine. Alternately, it will facilitate fiscal consolidation thereby reducing the debt burden of citizens in general”.

21. However, the representatives of Gujarat and Madhya Pradesh Government disagreed with the assessment of Dr. Vijay L. Kelkar and submitted as under :

(i) **Views of Government of Gujarat :**

22. The most critical aspect of the proposed Amendment and introduction of GST in the country related to the expected revenue losses to the states. While the loss of revenue is expected due to removal of cascading effect, unacceptable revenue losses would arise mainly on account of the inability to achieve Revenue neutral rates, the loss of CST revenues and the sub-optimal collections from services sector.

23. The Task Force on GST of Thirteenth Finance Commission (TFC0 has worked out a Revenue-Neutral Rate (RNR) of 12% (5% CGST and 7% SGST) assuming there is a single GST rate and stamp duty & electricity duty are also subsumed in the GST. It is not clear whether services and goods will have the same rate or be subjected to tax at different rates. The proposed RNR by the NIPFP does not match the rates suggested by thirteenth Finance Commission. Our calculations show that RNR will be as high as 19.68%. Such high rates cannot be levied on all goods and services and therefore revenue losses will certainly occur. The anticipated revenue losses to the State of Gujarat would be around Rs. 9,000 crore.

(ii) **Views of Government of Madhya Pradesh :**

24. Fiscal health of States is likely to be deteriorate because of the substantial tax revenue loss, they will not be able to mobilize additional resources for development as they cannot change the rates structure of the most important tax instrument available to them and they cannot raise additional resources through borrowing as their borrowing limit is determined by the Centre and has been fixed at 3% of GSDP.

25. Backward States generally have poor fiscal health and are more dependent on Central Devolution and Grants. The share of taxable services in the

“consumption basket” of the poor is always smaller as compared to the better off sections off the society. Therefore, the additional revenue accruing to backward States from “final consumption of services” in GST will be meager to compensate the loss of tax revenue from taxation of primary commodities only on the “Destination Principle”.

26. When asked as to how GST will affect the fiscal health of the states Shri Sushil Kumar Modi, Chairman, Empowered Committee of State Finance Ministers in his post-evidence reply has stated as under :

“With the introduction of GST, 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, 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 on the stakeholders. Hence, implementation of GST will provide a better environment for growth and possibly may result in the increase of the GDP. Therefore, in long run implementation of GST is not likely to affect the fiscal health of the States. On the contrary, it may improve the generation of the revenue of the States. However, in the initial few years of the implementation of GST, because of subsumation of several State Taxes, removal of the cascading affect, provision of additional set-offs may result in some State specific losses and, therefore, there may be a need for provision of GST compensation to such States in the initial few years”.

(b) Prices

27. When asked as to how GST will impact prices, Dr. Vijay L. Kelkar, Ex-Chairman, Thirteenth Finance Commission in his post-evidence reply stated as under :

“Prices of agricultural commodities and services are expected to rise. Most of the manufactured goods would be available at relatively low prices especially textiles and readymade garments.

There are two opposing forces which determine the changes in price levels. First, increased payments to the primary factors of production, viz. land, labour and capital, increase the cost of production and hence tend to have upward pull on prices. Second, sectors under imperfect competition (manufacturing sectors) get benefits of cost reduction through increasing returns to scale which are not reaped by sectors assumed to be in perfect competition. The relative impact of the force determines the overall price change. It may also be noted that the share of primary inputs (land, labour and capital) in total output is relatively high in agricultural and services sectors.

Another factor that impacts the price levels refers to the quantum of intermediate input purchases from sectors under perfect competition versus imperfect competition. Relatively low proportions of intermediate inputs purchased by agriculture and service sectors (i.e. sectors under perfect competition) are sourced from manufacturing sectors and hence these sectors do not reap the benefit of relatively low cost inputs from manufacturing sectors. Therefore, fall in prices of manufactured goods should benefit agriculture and services sectors.

Further, the terms of trade can also be expected to improve in favour of agriculture vis-a-vis manufactured goods. The prices of agricultural goods would increase between 0.61 percent and 1.18 percent whereas the overall prices of all manufacturing sector would decline between 1.22 percent and 2.53 percent. Consequently, the terms of trade will move in favour of agriculture between 1.9 percent and 3.8 percent.

The increase in agricultural prices would benefit millions of farmers in India. Similarly, the urban poor will also benefit from new employment opportunities. With regard to the food crops the poor would continue to remain secured through the public distribution system. The prices of many other consumer goods are expected to decline. These include sugar; beverages; cotton textiles; wool, silk and synthetic fibre textiles; and textile products and wearing apparel.

Further, moving forward, the combined lower rate of Union Excise Duty (UED) and State level VAT on inputs and goods consumed by vulnerable section of the society is already 11 percent which will be marginally increased to 12 percent when GST is introduced. Similarly, the present rate of Service Tax of 12 percent is already aligned to the 12 percent combined GST rate recommended by the Thirteenth Finance Commission. However, the combined standard rate of 25.5 percent under the UED and State-VAT is substantially higher than the 12 percent. With the introduction of GST the 25.5 percent will have to be reduced to 12 percent which will have a strong downward effect on inflation. In addition, the service tax coverage has also been extended to all services except a negative list. Therefore, overall inflationary

impact of GST will be negative through lower prices, lower fiscal deficit and higher output”.

(c) Consumer prices – international experiences

28. In a note submitted to the Committee, the Government of Madhya Pradesh has cited some studies illustrating adverse impact of GST upon consumer prices which has been reproduced as below :

- (a) The empirical data relating to the consumer price changes in Australia, Canada and New Zealand is given by (Bolton & Dollery, 2004). On the issue of the effect of GST on consumer price inflation Tom Bolton and Brian Dollery have drawn the following conclusion from the empirical data :

“It seems useful to frame the comparison of the macroeconomic inflationary effect in terms of Alston’s (1996) case study methodology. At the time of New Zealand’s GST introduction all three countries had roughly 4% to 6% annual consumer price inflation rates. In the year following the introduction of the GST in Canada, the average of the three countries had dropped to between 1% and 2%. The average was still low in the year before the introduction of the GST in Australia. Accordingly, the observed spike in price levels that occurred in all three countries should not be compared directly inter temporally with regards to economic performance since almost all the other factors impinging on the rate of inflation were different. However, while all three countries did exhibit a spike in price level, there was nonetheless no indication of subsequent wage-price spirals”.

- (b) Ruggeri and Wart have examined the effects of GST in Canada. They have come to the following conclusion :

“The GST has contributed substantially to higher inflation and has seriously weakened the Canadian economy in 1991. Statistics Canada has estimated that the GST is responsible for most of the first-quarter 1991 increase in the consumer price index (CPI) of 1.5 percent and has contributed to a decline of 1.2 percent in real GDP (which is equivalent to an annual compound decline of 4.6 percent). The CPI jumped by 2.6 percent from December 1990 to January 1991, with 1.6 percentage points of that rise attributed by Statistics Canada to the GST.

The introduction of the GST has added to the inflation rate, first because it entails a tax rise of about \$1.5 billion over what the MST would have yielded in 1991, 7 and, second, because not all the savings from the elimination of the MST were passed forward immediately. In the medium term, the effect of the initial price shock depends upon the degree of competition on affected industries, the price sensitivity of demands for affected good, the state of labour relations, and aggregate demand. The inflationary pressure generated by this rise in consumption taxation has restricted the ability of the Bank of Canada to soften the impact of the current recession through lower interest rates, and as a result it has taken a prolonged and deep economic slide to bring interest rates down to the levels experienced before 1989”.

- (c) Tom Bolton and Brian Dollery have drawn the following conclusions regarding the effect on GDP of New Zealand, Canada and Australia.

“It is immediately apparent that the economic impacts of the GST package were quite varied across countries, suggesting no common denominator. For example, the dramatic jump in GDP in 1987 in New Zealand can hardly be attributed to GDP growth since both Australia and Canada experienced a simultaneous boom period. For the same reason, the Canadian recession could not have been induced by the introduction of the GST because it formed part of the (then) global recession”.

29. The Ministry of Finance in their post-evidence reply inter-alia stated that however, in most of the countries it has been a success though each one of them has been carrying out changes post rollout. In Europe, New Zealand, South Africa, Canada, Australia etc. the effects of GST/VAT have been encouraging and have led to buoyancy in collections and moderation of rates.

(d) Producing States and Consuming States

30. Some States like Gujarat and Madhya Pradesh in their memoranda have stated that public investments in infrastructure are a critical factor in inducing and sustaining economic growth. Infrastructure such as roads, power and water supply do not only promote industrial growth, but also agricultural development, services sector, and enhanced quality of life. GST is proposed as a destination

based tax, with tax revenues moving to the consuming states. The states which consume the most shall be the importing states and the states like Gujarat which are having a large manufacturing base, will be one of the net exporting states. This will lead to a situation where the net exporting states which have made heavy investments in infrastructure and industrial promotion measures will lose their tax revenues to the net consuming states as the tax will be destination based and the CST would be done away with. There will not be incentive to the net exporting states to invest further in industrial infrastructure. It may be appreciated that this is likely to lead to de-acceleration in public investments in infrastructure, across the states. On the other hand, net exporting states that have already invested heavily in such infrastructure, would be hard pressed to recover the investment from tax revenues. It is required to be examined, whether this is a healthy condition to create.

31. The Ministry of Finance in their post-evidence reply stated that there is no scientific data yet available to gauge the impact of the proposed GST on the producing States viz-a-viz consuming States. However, under GST the states which are net importers of goods and services will gain while the states which are net exporters (manufacturing states) may lose on account of destination based IGST. However, this is in consonance with the basic philosophy of the GST that the burden of taxes should not be imposed on non-residents of a State.

(e) MSMEs and Employment Generation

32. The Government of Gujarat in their memorandum submitted to the Committee has stated that at present threshold under Central Excise is Rs. 1.5 crore. The proposed threshold limit of Rs. 10 lakhs under CGST would bring many of the Micro Small and Medium Enterprises (MSMEs) under the central tax net. This is likely to adversely affect the employment generating units under MSME sector. Some of the units may become financially unviable and lose competitiveness due to additional burden of tax, cost of compliance and dual

control. Around 30,000 MSME s will be affected in Gujarat alone and this contributes to employment of 2.18 lakh families.

33. The importance of the MSME sector in the economic arena cannot be under-estimated. Not only is the direct employment generated per unit of capital deployed generally much higher, but the MSME also provide ancillary and support services to large industries, in a cost-efficient manner. The spirit of innovation and enterprise thrives in the MSME sector. The contribution of MSMEs in export competitiveness of the country is considerable. These aspects are likely to be adversely affected, by bringing in the MSME into the central tax net.

34. When asked to comment upon the impact of GST on MSMEs, Dr. Vijay L. Kelkar in his post-evidence reply stated as under :

“At present small scale industries are entitled to exemption from payment of CENVAT in respect of their turnover upto Rs.1.5 crores. However, there is no such threshold exemption in respect of state level VAT. The main reason for exemption from payment of CENVAT is to liberate them from the onerous compliance burden under the CENVAT regime particularly in the context that, in general, the small scale industries are managed by one or two entrepreneurs with the support of a handful of semi-skilled office staff.

In the context of the GST, it has been recommended that the reporting of payment and transaction information of both CGST and SGST should be allowed through a combined Form. Therefore, in any case the small scale industry has to comply with the reporting of payment and transaction information of SGST. No additional burden is cast upon the small scale industry for compliance with the CGST. Hence, the case for continuing with the existing exemption upto Rs.1.5 crores of turnover is extremely weak. Accordingly, it is recommended that this exemption should not be continued under the GST framework.

Further, the small scale industries are generally wary of dealing with multiple tax administrations. Therefore, in order to inspire confidence of the small scale industry in the new GST framework, it is also recommend that the scrutiny/audit of the small scale industry should be conducted only by the state tax administration. However, the State tax administration may seek the assistance of the central tax administration or any other state tax administration if the operations of the small scale industry transcend the state boundaries. Since the CGST and the SGST are proposed to be levied on an identical GST

tax base, the outcome of any investigation impacting SGST will also have a corresponding impact on CGST. Therefore, enforcement by the State tax administration would be adequate to even deal with CGST evasion.

Further, it must be noted that the combined GST rate of 12 percent recommended by the Thirteenth Finance Commission will be less than the 13.5 percent liability under State VAT and the burden of embedded input tax under Union Excise duty and Service Tax. Therefore, withdrawal of exemption will not be onerous for the MSME sector. In fact the liability will substantially reduce”.

PART-II

IV. Issues relating to Amendment Bill

34. Certain key issues emanating from some of the provisions of the Amendment Bill were raised by the Committee and discussed with the representatives of Ministry of Finance (Department of Revenue) State Governments experts, associations, organizations and Empowered Committee of the State Finance Ministers. Written information /replies was also obtained from the Ministry.

(a) Power to make laws with respect to Goods and Services Tax

(Insertion of new Article 246 A)

35. Clause 2 of the Amendment Bill reads as :

After article 246 of the Constitution, the following article shall be inserted, namely:—

‘246A. Notwithstanding anything contained in articles 246 and 254, Parliament and the Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by that State respectively:

Provided that Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

Explanation.— For the purpose of this article, “State” includes a Union territory with Legislature.’

36. On the above amendment, the Empowered Committee of the State Finance Ministers have expressed their views as under :

“Most of the States agree to this amendment. Gujarat and Madhya Pradesh are, however, of the opinion that this amendment will take away the fiscal autonomy of the States given by the Constitution since 1950 and also the proposed Article 246A inflicts severe blow on provision of distribution of legislative powers by introducing a separate category. States of Himachal Pradesh and Jharkhand feel that it should be ensured that the Constitutional Amendments should not affect the fiscal autonomy of the States as enshrined in the Indian

Constitution. Jammu & Kashmir basically have no objection to the proposed Article 246A except they feel that keeping in view the special Constitutional status of Jammu & Kashmir, adequate safeguards need to be incorporated in the Constitutional Amendment Bill with respect to Jammu & Kashmir. Madhya Pradesh, Mizoram and Rajasthan feel that proposed Article 246A provides for concurrent jurisdiction for both Union and the States and, therefore, in case of conflict of interests between them, it should be clarified which legislative power shall prevail. West Bengal is of the opinion that the proviso in the proposed Article 246A should refer to “supply or receipt of goods or of services, or both”.

37. The Ministry of Finance (Department of Revenue) have clarified their position as under :

“It is true that both Centre and States will have power to simultaneously levy GST on supply of goods and services but this power is not being given through an entry in the Concurrent List but through insertion of an Article in the main body of the Constitution itself. It is correct that the proposed Article 246A does not limit the legislative power of the States as the intention is to allow autonomy to the State legislature on the basis of the recommendations of the GST Council until it affects the harmonized working of GST”.

38. In this regard during the course of oral evidence Dr. Vijay L. Kelkar, Ex-chairman, Finance Commission further elaborated that the existing independent power of the State has yielded a distortionary tax system. Autonomy has neither served the objective of collection of revenue nor sub-served the attainment of any socio-economic objective. There is widespread tax evasion, poverty, malnutrition, and social and economic inequity. The ability of a State to achieve its socio-economic policies is determined by its expenditure policies. At present, the distortionary tax system in States has limited its ability to raise sufficient resources for its residents thereby severely undermining its ability to pursue an independent expenditure policy. Tax policy is only a means to an end. The proposed harmonized tax system will help mobilize larger resources and enhance the power of the States to pursue an independent expenditure policy. The proposed GST regime will lead to harmonization of tax base, tax rate and tax infrastructure. This will promote economic efficiency, and reduce compliance and administrative cost.

(b) Integrated Goods and Services tax (IGST)

Insertion of Article 269A

39. Clause 9 reads as under :

‘269A. (1) Goods and services tax on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be prescribed by Parliament by law. *Explanation I.* — For the purposes of this clause, supply of goods or of services or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-State trade or commerce. *Explanation II.* — For the purpose of this article, “State” includes a Union territory with Legislature. (2) Parliament may, by law, formulate the principles for determining when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

40. The Chairman, Empowered Committee of State Finance Ministers has submitted to the Committee as under on the above clause :

“This amendment is generally acceptable to the States except some observations made by some of the States. Assam, Himachal Pradesh and Kerala feel that Article 269A should, in clear terms, provide for levy of GST on “Destination Principle” on supply of goods and services. Gujarat and West Bengal feel that the word “apportioned” should be replaced by the word “distributed” or “assigned”. Several States like Himachal Pradesh, Jharkhand and Uttar Pradesh feel that the revenue received from IGST should be under the divisible pool. Gujarat opposes inclusion of GST on import of goods within the purview of Union Government as it goes against the consensus of delegating the powers to the States on VAT on imports on “Destination Principle”. He further added that :

“This amendment can be retained in view of the fact that there should be an institutional mechanism to extend the GST credit chain in the course of inter state trade and commerce and the proposed Article 269A contemplates providing just such a legal framework. However, the word “apportioned” used in Article 269A(1) should be replaced by the word “distributed”. The word “distributed” has also been used in Article 270”.

41. On the above clause, the Ministry of Finance (Department of Revenue) in their written submission commented as under :

“It is correct that terms “distribution” and “assignment” have been used in the Constitution. The distribution has been used in terms of one way flow from Centre to the States like devolution of funds from Central pool of taxes. The assignment has been used for taxes like Central Sales Tax, where tax is collected and kept by the State from where the trade originates. The IGST will follow a system under which money would move from Centre to the States or vice-versa, depending upon the fact whether the State is net exporter or net importer for the given period of settlement. That is why a different word “apportioned” has been used in the proposed amendment to denote a two-way flow of funds, post settlement”.

42. The Ministry further clarified that IGST proceeds will not follow the devolution formula nor would get assigned to the States.

43. When asked about the modalities of the IGST model and its revenue implications, the Ministry of Finance in a written reply stated as under :

“IGST model envisages that the Centre will levy tax at a rate approximately equal to (CGST+SGST) rate on inter State supply of goods and services. IGST will be levied and collected by the Centre. This levy will basically meet the objective of providing a continuous credit chain across States. The funds under the mechanism will required to be transferred from one State to another by the Centre depending upon the goods supplied to and from the State during the settlement period under consideration. The settlement of accounts will be done by the Centre that would function as a clearing house for this purpose. The model would obviate the need for refunds to exporting dealers (to enable full neutralization of input taxes) as well as the need for every State to settle accounts with every other State. To the extent, goods or services are supplied from one State to another for further distribution, IGST transactions would be revenue neutral (the tax paid in the exporting State would be available as credit to the buyer in the importing State). Since GST will follow destination principle, the net importing States will be the gainers while net exporting States will be the losers after this system is put in place. For the Centre, IGST will not have any revenue implication, either positive or negative”.

44. While submitting his suggestions on this clause, Dr. Vijay L. Kelkar during the course of oral evidence deposed as under :

“There is no reason why the Centre should get involved in the collection of inter-sate trade tax. The proposed IGST is extremely complex and therefore place a very high level of compliance burden on the taxpayer and the clearing house agency. A simpler Model is the Modified bank

Model as recommended by the Task Force on GST set-up by the Thirteenth Finance Commission. It does not require any involvement of the Central Government”.

(c) GST Council

(Insertion of new Article 279A)

45. Clause 12 of the amendment Bill reads as under :

“After article 279 of the Constitution, the following articles shall be inserted, namely: -

‘279.A(1) The President shall, within sixty days from the date of commencement of the Constitution (One Hundred and Fifteenth Amendment) Act, 2011, by order, constitute a Council to be called the Goods and Services Tax Council.

(2) The Goods and Services Tax Council shall consist of the following members, namely:-

(a) the Union Finance Minister Chairperson;

(b) the Union Minister of State in charge of Revenue Member;

(c) the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government Members

(3) The Members of the Goods and Services Tax Council referred to in sub-clause(c) of clause (2) shall, as soon as may be, choose one amongst themselves to be the Vice-Chairperson of the Council for such period as they may decide.

(4) The Goods and Services Tax Council shall make recommendations to the Union and the States on-

(a) the taxes, cesses and surcharges levied by the Centre, the States and the local bodies which may be subsumed in the goods and services tax;

(b) the goods and services that may be subjected to or exempted from the goods and services tax;

(c) the threshold limit of turnover below which goods and services tax may be exempted;

(d) the rates of goods and services tax; and

(e) any other matter relating to the goods and services tax, as the Council may decide.

(5) While discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

(6) One-third of the total number of members of the Goods and Services Tax Council shall constitute the quorum at its meetings.

(7) The Goods and Services Tax Council shall determine the procedure in the performance of its functions.

(8) Every decision of the Goods and Services Tax Council taken at a meeting shall be with the consensus of all the members present at the meeting.

(9) No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of –

(a) any vacancy in, or any defect in, the constitution of the Council; or

(b) any defect in the appointment of a person as a member of the Council; or

(c) any irregularity in the procedure of the Council not affecting the merits of the case.

Explanation.- For the purposes of this article, “State” includes a Union Territory with Legislature.

46. On the above clause, Shri Sushil Kumar Modi, Chairman, Empowered Committee of State Finance Ministers while stating the concerns expressed by some State Governments submitted as under :

“Most of the States agree to the setting up of a GST Council. Gujarat and Nagaland, however, feel that there is no need of creation of a new body as the Empowered Committee of State Finance Ministers is working for last several years on consensus basis and may be converted into GST Council. Following views have also been expressed by different States on the various provisions of proposed Article 279A.

(i) Flexibility should be provided to the States in time of economic exigencies, disasters and natural calamities.

- (ii) Special schemes for the North-Eastern States and the Special Category States should be provided.
- (iii) Harmonization of the GST structure should be in line with the 'destination principle' and should be clearly defined.
- (iv) The quorum of 1/3rd provided is not adequate and it should be somewhere half to 3/4th of the total number of members of the GST Council.
- (v) The mention of local bodies in sub-clause 4(a) should not be there as the revenues of the local bodies are not to be subsumed under GST.
- (vi) The recommendations under clause 4 to be made by the Council should be subject to the provisions of Article 246A.
- (vii) Sub-clause 4(d) should be amended so as to provide for a system of floor rates and rate band instead of fixing a uniform rate of tax and the prescribed floor rate should apply to inter-state transactions.
- (viii) Issue of GST compensation should also be one of the issues on which the Council should be in a position to make its recommendations.
- (ix) Keeping in view the special position of the State of Jammu & Kashmir, suitable provisions need to be kept in Article 279A and 279B so that no decision of the Council should be applicable to Jammu & Kashmir without expressed consent of the State.

47. On the issue of achieving consensus (Clause 8) during the meeting of the Committee, the Chairman, Empowered Committee of State Finances elaborated as under :

“It is a fact that sometimes it may be difficult to achieve consensus and it may lead to stalemate in the functioning of the GST Council. Therefore, the word “consensus” has to be properly defined. One alternative could be that “every decision of the Goods and Services Tax Council taken at the meeting should be with a majority of 2/3rd or 3/4th of the members present at the meeting. Every decision regarding Central Goods and Services Tax may also require the agreement of the Union Finance Minister”.

48. On the flexibility to be given to the States in times of economic exigencies, the Ministry have stated that Article 279A (4)(e) allows Council to make recommendations on any matter related to GST in addition to the threshold rate of tax etc. The flexibility is available to the GST Council depending upon the need and mentioning in the body of the Bill that flexibility will be available only in case of economic exigencies, disasters and natural calamities, will only limit the flexibility already intended to be provided to the GST Council.

49. On the Special Scheme for North Eastern States and Special Category States, the Ministry have commented that the flexibility to GST Council is available in the existing formulation also. The mention of flexibility only in certain situations as proposed will limit the flexibility available to the Council unintentionally. The special schemes for NE and special category States have been launched under the concerned tax laws and not through the Constitution, and therefore, the same cannot be mentioned in the Constitution itself.

50. On the tax incentives available to North Eastern States and Special Category States, the Ministry of Finance in their post-evidence reply stated that since it is proposed to subsume Central Excise Duty within GST, it would not be possible to continue with area-based exemptions (from central excise duty) operating in Jammu & Kashmir, Himachal Pradesh, Uttarakhand, Sikkim, North East and Kutch in their present form. Besides, such exemptions are incompatible with the concept of GST that presupposes a moderate neutral tax across the entire value chain and seamless flow of credit. As such, it is envisaged to convert these schemes into cash subsidy schemes. This would not have any adverse impact on the units currently availing of the area based exemption benefits.

51. On subsuming of taxes levied by the local bodies, Ministry stated that It appears appropriate to empower GST Council to make recommendations with respect to subsuming of taxes levied by the local bodies also so that at later point of time when it is decided to subsume taxes like Octroi, it could be done with a recommendation of the GST Council. The subsuming of any tax will anyway

involve a long drawn process of Constitution amendment during which States will have sufficient opportunity to present their views.

52. On the harmonized structure of the GST, the Ministry have commented that harmonized structure of the GST will mean that there is no serious conflict between the systems followed by Centre and the States during GST regime. Harmonized national market means that there would not be unnecessary preferences available to anyone to set up a business or industry in a particular part or a States because of tax related concessions. These words are clearly understood and may be further detailed by the GST Council, depending upon the need from time to time.

53. On the issue of Quorum and consensus the Ministry clarified that the various options in this regard have been discussed. The Central revenue being subsumed in the GST is almost equal to all the States revenue proposed to be subsumed in it. In the GST Council, however, 2/3rd of the States will be able to take a decision against the interests of the Centre if the given formulation is accepted. It has accordingly been proposed that decision in the GST Council be taken on the basis of consensus.

54. Regarding formula for compensation to the States, the Ministry clarified that GST Council would be able to make recommendation on any matter only when all the States and Union Finance Minister agree to the proposal. If such a formulation of compensation formula can be worked out, there appears to be no difficulty in Union Government accepting the same even if it is not recommended by the Council. The Council is generally expected to make recommendations on matters related to GST to both Union and States to ensure harmonization.

55. On floor rate the Ministry have stated that GST Council may decide to make recommendations about the floor rate or a band within which tax rates may be kept depending upon the discussions in its meeting. The proposed amendment will allow such flexibility. However, in their post evidence reply the Ministry of Finance on floor rate/band stated that a high level of harmonization helps in minimizing the aberrations in the implementation of the GST. Dispersal in rates across various States compromises the objectives of a single common market

significantly. The matter becomes even more complex if such variation in rates is permitted in the case of services. Services, being intangible, are difficult to be related to geographical locations and pose significant challenges in deciding the precise place where they are liable to be taxed. If the autonomy is permitted only in respect of goods, (and not services), it leads to different problems of distinguishing between goods and services, which is not easy in a modern economy where such distinctions are withering away fast. Moreover, variations in rates across States lead to arbitrage opportunities, resulting in evasion and distortion in production and supply chain. Thus the benefits of keeping harmonized structure far outweigh the desire to provide unrestricted autonomy.

56. On floor rates, Dr. Parthasarathi Shome, Director & Chief Executive, Indian Council & Research on International Economic Relations in his memorandum submitted to the Committee has stated that states should be allowed to have floor rates under SGST allowing them to move up the rate if they wished. The reason presumably is that some advanced economies do this. It is important to keep India's SGST rate structure as simple as possible. The states have performed this task well so far under their VAT structure where they essentially have one general rate and one lower rate, with a list of goods of local importance from which they can select about a dozen commodities to exempt to suit local conditions. There is no reason why they should sacrifice under the SGST the uniformity that they have already achieved under the VAT. Otherwise, in practice, the SGST would become unmanageable; and administration and monitoring of interstate trade may become untenable.

57. On the threshold limit of turnover below which goods and services tax may be exempted, the Government of Madhya Pradesh in their post-evidence reply have stated that "low threshold for both CGST and SGST will increase the tax incidence on the products of small producers and adversely affect the employment in small scale industries. The threshold for taxation in Central Excise regime at present is Rs. 1.5 crore. This threshold should continue in CGST otherwise the tax burden on small producers will adversely affect them. A

relatively high threshold for CGST will also protect small business from dual tax administration”.

58. On the threshold limit, the Government of Gujarat added further that States are of the view that the threshold for Central GST should be Rs. 1.5 crore or more, but the Union Government wants Rs. 10 lakhs turnover as the threshold for Central GST. This will bring about additional 30 lakh dealers approximately, under levy of CGST, which in turn, will increase the transaction costs and impact competitiveness.

(d) Goods and Services Tax Dispute Settlement Authority (Article 279 B)

59. Clause 12, Article 279 B reads as under :

“279B. (1) Parliament may, by law, provide for the establishment of a Goods and Services Tax Dispute Settlement Authority to adjudicate any dispute or complaint referred to it by a State Government or the Government of India arising out of a deviation from any of the recommendations of the Goods and Services Tax Council constituted under article 279A that results in a loss of revenue to a State Government or the Government of India or affects the harmonised structure of the Goods and Services Tax.

(2) The Goods and Services Tax Dispute Settlement Authority shall consist of a Chairperson and two other members.

(3) The Chairperson of the Goods and Services Tax Dispute Settlement Authority shall be a person who has been a judge of the Supreme Court or Chief Justice of a High Court to be appointed by the President on the recommendation of the Chief Justice of India.

(4) The two other members of the Goods and Services Tax Dispute Settlement Authority shall be persons of proven capacity and expertise in the field of law, economics or public affairs to be appointed by the President on the recommendation of the Goods and Services Tax Council.

(5) The Goods and Services Tax Dispute Settlement Authority shall pass suitable orders including interim orders.

(6) A law made under clause (1) may specify the powers which may be exercised by the Goods and Services Tax Dispute Settlement Authority and provide for the procedure to be followed by it.

(7) Notwithstanding anything in this Constitution, Parliament may by law provide that no Court other than the Supreme Court shall exercise

jurisdiction in respect of any such adjudication or dispute or complaint as is referred to in clause (1).

Explanation- For the purposes of this article, “State” includes a Union Territory with Legislature’.

60. On the GST Dispute Settlement Authority, the Chairman, Empowered Committee of State Finance Ministers stated that most of the States have expressed the view that the provision pertaining to the GST Dispute Settlement Authority should be omitted as this authority shall have powers of overriding the supremacy of the Parliament and the State Legislatures. It shall affect the fiscal autonomy of the States.

61. The Constitution confers autonomy on the Parliament and the State Legislatures to legislate within the respective fields assigned to them and the fact that a statute enacted by a competent Legislative body can be called into question on grounds of deviations from the recommendations of an essentially executive body, albeit Constitutional, is being construed as undermining the supremacy of the Legislature. Keeping in view the concerns expressed by the States, and the fact that the proposed provision of GST Dispute Settlement Authority will affect the fiscal autonomy of the Parliament and the State Legislatures, the proposed Article 279B providing for GST Dispute Settlement Authority may be omitted. However, any dispensation involving multiple partners does require a mechanism to resolve disputes. A provision can be made in Article 279A itself empowering the GST Council to decide about the mechanism to resolve the disputes arising out of its recommendations.

62. The Ministry have clarified their position on this issue as under :

“The Law of Natural Justice says that nobody should be Judge in its own cause. Since the GST Council is to make recommendations only with consensus, making the Council responsible for adjudicating disputes will not be feasible as the State against which a complaint will be expected to be filed may block it in the GST Council itself. Moreover, GST Council is not supposed to decide the amount of compensation to be paid by the deviating State but to make recommendations about the key GST parameters and, therefore, the suggestion cannot be accepted”.

Legality of Goods and Services Tax Council (GSTC) and Dispute Settlement Authority (DSA)

63. When asked about the legality of the setting up of Goods and Services Tax Council (GSTC) and Dispute Settlement Authority (DSA) and whether the setting up of a DSA would be unconstitutional, the Ministry of Finance (Department of Revenue) sought the opinion of the Attorney General of India on the matter through Department of Legal Affairs which is as under :

“This is an important point which has been raised and the short answer to it is that it is certainly open to Parliament to approve any recommendation. However, this does not mean that the GSTC recommendations will have no value. Having regard to the nature of the Constitution of GSTC, the Council would have performed useful role in making recommendations but the ultimate authority whether to accept such recommendations can and must rest only in the Legislatures, namely, Parliament and the State Legislatures.

In this view of the matter, the setting up of the GSTC does not strike at the root of the legislative powers over Finance. The powers of the legislature over Finance are sacrosanct and are not affected by the setting up of the GSTC”.

64. On the legality of DSA, the Attorney General of India further stated which is as under :

“Here again, I wish to state that the question of the Parliament and the State Legislatures becoming mute spectators does not arise. The Dispute Settlement Authority is primarily with regard to the aspect of disputes in relation to deviation from any recommendation of the GSTC, and it is not just any deviation but a deviation which results in loss of revenue to a State Government or the Government of India, or affects the harmonized structure of the Goods and Service Tax. Notwithstanding the decision on the DSA, the ultimate control over finance will always be that of the legislatures.

In the premises, my answer to the two queries are as above. The supremacy of the legislatures over Finance are not affected by the proposed amendments”.

(e) Declared Goods (Article 286)

65. Clause 13 Article 286 reads as under :

“In article 286 of the Constitution -

(i) in clause (1),-

(A) for the words “the sale or purchase of goods where such sale or purchase takes place”, the words “the supply of goods or of services or both, where such supply takes place” shall be substituted;

(B) in sub-clause (b), for the word “goods”, at both the places where it occurs, the words “goods or services or both” shall be substituted;

(ii) in clause (2), for the words “sale or purchase of goods takes place”, the words “supply of goods or of services or both” shall be substituted;

(iii) for clause (3), the following clauses shall be substituted, namely:-

“(3) Any law of a State shall, in so far as it imposes, or authorises the imposition of a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of tax as Parliament may by law specify.

(4) Nothing in clause (3) shall apply to a law of a State insofar as it imposes or authorises the imposition of goods and services tax”.

66. On the above amendment, Shri Sushil Kumar Modi, Chairman, Empowered Committee of State Finance Ministers has submitted as under :

“Most of the States are opposed to the clauses (3) and (4) of this amendment. Clauses (3) and (4) allow the Union Government to take a unilateral decision of restricting the rates of petroleum products and alcoholic liquor for human consumption which may substantially affect the revenues of the States without their consent. In some cases, the Union Government had taken such decisions in past. It bears mention at this stage that the first three drafts of the Amendment Bill did not contain such a provision which suddenly appeared for the first time in the Amendment Bill introduced in the Lok Sabha. In terms of the proposed sub-clause (4), such restrictions will apply only to goods kept out of the ambit of GST viz. Crude oil, Petrol, Diesel, Aviation Turbine Fuel, Natural gas and alcoholic liquor for human consumption. The aforesaid items are major revenue earners for the States and any

restriction on the authority to tax the same will be inimical to the interests of the States.

In view of above, I feel that clauses (3) and (4) should be omitted. Alternatively, in clause (3), after the words, “subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of tax as Parliament by law specify”, the words “on the recommendation of the Goods and Services Tax Council constituted under article 279A” may be added”.

67. The Madhya Pradesh Government in their written submission on the above amendment have stated as under :

“The revised draft imposes the restriction on the States with respect to imposition of tax on sale or purchase of declared goods (not supply of declared goods). This can’t be acceptable as inter-state supply of declared goods are zero-rated and any restriction on the State to levy of tax on declared goods adversely affects the fiscal autonomy of the State in the GST regime”.

68. The Ministry on the above amendment have furnished their comments as under :

“The Central Government today has power under the Constitution to restrict rate of tax a State can levy on sale of a good. The proposal here is to restrict the Centre’s existing power to the goods kept outside the GST as it is expected that rate of tax on goods brought within GST will be decided on the basis of consensus between the Centre and the States and will follow a discipline. No new power is being sought by the Centre through the proposed amendment and in fact, the existing power available in the Constitution is proposed to be restricted”.

(f) Goods and Service Tax (Article 366)

69. Clause 14 in the amendment Bill reads as under ;

14. In article 366 of the Constitution, -

(i) after clause (12), the following clause shall be inserted, namely:-

‘(12A) “goods and services tax” means any tax on supply of goods or services or both except taxes on the supply of the following goods, namely:-

- (i) petroleum crude;
- (ii) high speed diesel;
- (iii) motor spirit (commonly known as petrol);

- (iv) natural gas;
- (v) aviation turbine fuel; and
- (vi) alcoholic liquor for human consumption.’;

(ii) clause (29A) shall be omitted

70. On the definition aspect of Goods and Services Tax, Dr. Vijay L. Kelkar, Ex-Chairman, Thirteenth Finance Commission, during the course of oral evidence submitted before the Committee that the proposed definition of GST in Clause 14 of the Constitutional Amendment Bill is incomplete. It is essential that it is defined as a sales tax rather than a VAT-type tax.

71. On the proposed definition of GST, the Ministry of Finance in their written reply stated that the detailed contours of the GST will be worked out by the GST Council who will take a decision on the extent to which input tax credits will be allowed. It does not seem necessary to define the GSTT as a VAT-type tax, as that word is capable of being understood in a variety of manners. The existing entries in the Constitution pertaining to Excise and State VAT also define the tax in terms of its taxable event even though they are both VAT type of taxes. Likewise, GST has been defined in terms of its taxable event namely the supply of goods and services.

72. On the exclusion of petroleum crude, high speed diesel, motor spirit, natural gas, aviation turbine fuel; and alcoholic liquor for human consumption from the purview of Goods and Services Tax, Shri Sushil Kumar Modi, the Chairman, Empowered Committee of State Finance Minister's in his post evidence reply stated as under :

”The States are in agreement that petroleum products, alcohol liquor for human consumption and electricity should not be, for the time being, brought within the ambit of GST. Mainly this decision has been taken as petroleum products and alcoholic liquor for human consumption are major revenue earner for the States. Regarding electricity, the decision has been taken to keep ‘electricity’ outside the GST for the time being only. At present ‘Coal’ is under VAT, and, therefore, it has been kept under the purview of the GST.

However, Federation of Indian Chambers of Commerce and Industry (FICCI), Confederation of Indian Industry (CII), Petroleum Federation of India (PetroFed), International Spirits & Wines Association of India (ISWAI) and Confederation of Indian Alcoholic Beverage Companies (CIABC) have represented before the Committee that the petroleum products and alcoholic liquor for human consumption should be kept under the ambit of GST and specific levies can be imposed by the Centre and the States to address their revenue concerns. In case, it is decided not to bring them immediately under GST, then these products should not be “Constitutionally” debarred from bringing them under GST. Exclusion of specific goods by way of Constitutional Amendment would dilute the flexibility for levy of GST on these products in the future, even if the Centre and the States were to reach a consensus later. It will also remove flexibility to cover these goods in stages as their subsequent inclusion would require another Constitutional Amendment which could be a long drawn process.

There is considerable ground for concurring with the views expressed by the Trade and Industry Associations that the petroleum products and alcoholic liquor for human consumption should not be Constitutionally debarred from the ambit of GST. The decision to extend GST to any category of goods should, vest with the GST Council. The said goods may be kept under GST and the revenue shortfall (on account of their being taxed at the standard rate, which is expected to be lower than the current tax rate on such goods, and also on account of providing input tax credit on these goods) can be made good by having recourse to additional non-creditable levies, in line with the best practices being followed internationally vis a vis such goods. Excluding goods from the Constitutional definition of “goods and service tax” would call for another Constitutional amendment, if, at some time in the future, a consensus emerges to bring these goods in the GST fold, and we are all aware that a Constitutional amendment may be a difficult proposition. Therefore, the clause (12A) may be re-worked as “ ‘Goods and Services Tax’ means any tax on supply of goods and services or both” and the remaining portion of the clause (12A) may be omitted and the word “supply” should be clearly defined in article 366.”

73. On the issue of coal to be kept outside the purview of GST, the representatives of Odisha Government during the oral evidence submitted that Coal should be kept out of GST along with natural gas. According to them, Excise duty was not levied on coal and it was subjected to only VAT at 4%. Bringing coal into the purview of excise duty may escalate the prices of coal. If coal is brought under GST, the tax rate of coal will be 12 to 16%, which will

further escalate the price of coal. Coal is an important input for generation of electricity. As Electricity Duty is not going to be subsumed under GST, there will be no set off available for generation of power. So if coal is brought into GST purview, the cost of electricity generated by the coal based thermal power stations will go up which will adversely affect the industries as well as general consumer.

74. When asked as to what will be the impact on economy if petroleum and electricity are kept out of GST. Dr. Vijay L. Kelkar, Ex-chairman, Thirteenth Finance Commission in his post-evidence reply has stated as under :

“To the extent, petroleum and electricity are kept out of GST, the cascading effect of commodity taxation will increase. This will add to the economic distortions and hence impact economic growth. A lower economic growth will lead to lower growth in GST collections”.

75. On this question, the Ministry have submitted their comments as under :

“Centre wanted all the items to be subsumed in the GST but States have insisted that certain goods be kept out of GST and an explicit provision to this effect be made in the Constitution itself. Article 366(12A) has been drafted accordingly. If these exclusions are not enumerated, States would enjoy the power to levy GST on these goods in addition to the powers to levy Sales tax, State excise etc. which are being separately retained. This would neither be desirable nor is it the intention”.

76. On the question of exclusion of certain items from the purview of GST, Dr. Asim Kumar Dasgupta, Ex-Chairman, Empowered Committee of State Finance Minister's deposed as under before the Committee :

“Clause 14 basically invokes article 366. It basically gives the definitions and categories. In doing so, it says, “except taxes on petroleum, high speed diesel, alcohol, liquor”. If we want just say, “as may be recommended by the GST Council”. That is because today we may keep these things out of the GST. After some time we may like to have a formulation. So, for each thing you have to come back for constitutional amendment. So, if we have just this clause because normally the names of the commodities do not find place in the constitutional amendment. It normally should not. It should be in the CST laws”.

(g) Amendment of Sixth Schedule to the Constitution

77. Clause 16 of the Amendment Bill reads as under :

In the Sixth Schedule to the Constitution, in paragraph 8, in sub-paragraph (3), -

- (i) in clause (c), the word “and” occurring at the end shall be omitted;
- (ii) in clause (d), the word “and” shall be inserted at the end;
- (iii) after clause (d), the following clause shall be inserted, namely:-

“(e) taxes on entertainment and amusements”.

78. On the above clause Confederation of Indian Industry (CII) and the Film and Television Producers Guild of India Limited furnished the following views :

“Clause 16 of the Bill proposes to insert a new clause (e) in Paragraph 8, sub paragraph 3 of the Sixth Schedule to the Constitution to empower District Councils and Regional Councils to levy tax on entertainment and amusement. Further, Clause 17 of the Bill proposes to amend the Seventh Schedule to the Constitution and substitute a new entry 62 for the current entry 62, to retain the States’ power to levy taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council.

One of the basic objectives of the GST is to replace the current multiplicity of taxes with a single, comprehensive tax. Continuation of levies such as the entertainment tax levied by the local bodies would defeat this objective. Such specific taxes balkanize the common market and give rise to significant controversies about the scope of taxes.

The current entertainment tax structure is a patchwork of many taxes and the entertainment tax rates are abnormally high. The impact of cascading taxes on the industry is significant. Exclusion of entertainment tax from GST would lead to cascading in many instances and impose a serious burden on the industry.

Supplementary levies in addition to the GST are warranted only for products that are harmful to health (e.g. alcohol) or give rise to negative externalities (e.g. petroleum products). However, there are no negative externalities associated with entertainment and it deserves to be treated at par with other goods and services.

Imposing a separate tax on entertainment outside GST would pose serious practical difficulties. Entertainment is not well defined and includes

a large variety of activities. With the advent of modern technology, entertainment has assumed many diverse forms and has become highly mobile. Already many disputes have arisen about the scope of entertainment tax.

A recent example is that of the entertainment tax levied by the State of Madhya Pradesh that covers a wide range of telecom and other activities. The provisions of the MP Entertainment tax Act could be interpreted to include even the non-entertainment value added services offered by telecom operators such as news updates, messenger/ email services, money transfers and bill payment services to name a few. Moreover, the entire telecom business is structured based on the telecom circle jurisdictions and not for individual State within the circle. Thus, the jurisdiction of levy (only the State of Madhya Pradesh) does not coincide with the telecom jurisdiction (both Madhya Pradesh and Chhattisgarh) thus raising serious compliance issues.

A separate tax at the national or State level is bad enough, it would be worse at the local or municipal level, as evident from the above example. Businesses do not maintain records / books of accounts that identify transactions at the local level.

Moreover, the quantum of revenues earned by States from entertainment tax is not significant and constitutes less than one percent of their total revenue from the indirect taxes. The revenue apportioned to / collected by the local bodies is an even smaller proportion. It is expected that the States' revenue would witness an overall increase. The States would have enough scope to provide funds to the local/municipal bodies."

(h) Amendment of Seventh Schedule to the Constitution

79. Clause 17 (b) reads as under :

(b) in List II – State List, -

(i) for entry 52, the following entry shall be substituted, namely:-

"52. Taxes on the entry of goods into a local area for consumption, use or sale therein to the extent levied and collected by a Panchayat or a Municipality.";

(ii) for entry 54, the following entry shall be substituted, namely:-

"54. Taxes on the sale, other than sale in the course of inter-State trade or commerce or sale in the course of international trade and commerce of, petroleum crude, high speed diesel, natural gas, motor spirit (commonly

known as petrol), aviation turbine fuel and alcoholic liquor for human consumption.”;

(iii) entry 55 shall be omitted;

(iv) for entry 62, the following entry shall be substituted, namely:-

“62. Taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council.”

80. The Chairman, Empowered Committee of State Finance Ministers in his written memorandum submitted his views on the above amendments in the Seventh Schedule to the Constitution as follows :

“Entry 52 : Most of the States are strongly opposed to this amendment. The Empowered Committee had unanimously decided that the Entry Tax will be subsumed under GST except Entry Tax levied in lieu of Octroi. However, as per new proposed Entry 52, the levy of Entry Tax by local bodies would create barriers to trade and commerce and would induce complexities in the business environment by distorting the tax structure and raising compliance burdens. In fact, at present States have introduced Entry Tax in lieu of Octroi for obviating certain fundamental problems with the levy and collection of Octroi by the local bodies and proceeds are distributed to the local bodies. It will not, therefore, be desirable to go back to the earlier system of levy and collection of Octroi by local bodies, as it will bring back the old issues and hinder free movement of goods as well as free flow of trade. The revised draft seeks to take away the Legislative powers of the States to levy and collect “Entry Tax in lieu of Octroi. Therefore, the proposed formulation of Entry 52 of the State list is not acceptable to most of the States”.

81. In view of this, he has suggested that the following formulation may be considered :

“The Entry 52 may read as “Taxes on the entry of goods into a local area for consumption, use or sale therein, in lieu of octroi”. In case, in the Constitution, the word “octroi” has not been used, then the same could be suitably defined. Alternatively, following formulation can be considered:

52. Taxes on the entry of goods into a local area for consumption, use or sale therein when such taxes are collected by or for the Panchayats or Municipalities or District Councils / Regional Councils constituted under the Sixth Schedule of the Constitution and are assigned to them”.

82. He further explained on this point as follows :

“Several States like Bihar, Gujarat, Haryana, Jharkhand, Maharashtra, Rajasthan and Tamil Nadu feel that since Central Government has retained the power to tax ‘tobacco and tobacco products’, therefore, suitable provision should also be made under Entry 54 for States to levy tax on tobacco and tobacco products in addition to GST. In the original Entry 54, after the taxes on sale the word “or purchase” was used and, therefore, several States are of the view that “or purchase” word should be added after ‘sale’. States like Odisha, Chattisgarh, Jharkhand and Meghalaya feel that ‘coal’ should be included in the list while a few States like West Bengal want that ‘light diesel oil’ should be included. Some States like Karnataka want that ‘Natural Gas’ should be out of the list.

I feel that Entry 54, as suggested, can be agreed after adding the words “or purchase” after the word “sale”.

“Several States namely Andhra Pradesh, Assam, Karnataka, Jharkhand, Chhattisgarh, Uttar Pradesh and West Bengal are objecting to omitting Entry 55. Under Entry 55, tax is levied by the local bodies on the advertisements through hoardings etc. If Entry 55 is omitted, the source of revenue for the local bodies will diminish which will create difficulty for them in discharging their responsibilities. Hence, it is not appropriate to omit Entry 55.

I feel that this entry should not be either omitted or alternatively modified as indicated below:-

“55. Taxes on advertisements, other than advertisements published in the newspapers and advertisements broadcast by radio or television, to the extent levied and collected by the Panchayats or Municipalities or other local bodies or by the District Councils or Regional Councils constituted under the Sixth Schedule of the Constitution.”

“States of Andhra Pradesh, Assam, Kerala and West Bengal wanted that “taxes on Betting and Gambling” should be kept outside GST, while the States namely Himachal Pradesh, Jharkhand, Karnataka, Rajasthan and Uttarakhand feel that local bodies do not have capability to levy entertainment and amusement tax and, therefore, power should be given to the States to levy these taxes and distribute them to the local bodies.

In the First Discussion Paper, it was decided by the Empowered Committee that Entertainment Tax (unless it is levied by the local

bodies) and taxes on Lottery, Betting and Gambling should be subsumed under GST. Therefore, I feel that the Entry 62, as proposed, can be retained”.

83. On this issue of entry tax the Confederation of Indian Industry (CII) have furnished their views as follows :

“Clause 17 of the Bill proposes to amend the Seventh Schedule to the Constitution and substitute a new entry 52 for the current entry 52, to retain the States’ power to levy taxes on the entry of goods into a local area for consumption, use or sale therein to the extent levied and collected by a Panchayat or a Municipality.

Entry tax imposes a major cost burden on the industry and is a deterrent for their operations and expansion plans. The problems get compounded when entry taxes levied on the industrial inputs and on transit sales. Such taxes go against the concept of the common market. Further, Entry tax has been a subject of protracted litigation at all levels. Article 301 of the Constitution provides for freedom of trade and commerce throughout the territory of India and precludes the States from taxing inter-state transactions to prevent/minimize barriers to inter-state trade. On the other hand, Article 304 of the Constitution allows the legislature of the State to impose tax on goods imported from other States or the Union territories, in line with the tax imposed on similar goods produced in that State, to avoid any discrimination between imported goods and locally manufactured goods.

Continuation of entry tax outside the GST would perpetuate such complexities and litigation and impose barriers to trade. It is therefore suggested that entry tax should be fully subsumed in the GST”.

(i) Transitional Provision

84. Clause 18 of the Bill reads as under :

“Notwithstanding anything in this Act, any provision of any law relating to tax on goods or services or on both in force in any State immediately before the commencement of this Act, which is inconsistent with the provisions of the Constitution as amended by this Act shall continue to be in force until amended or repealed by a competent Legislature or other competent authority or until expiration of one year from such commencement, whichever is earlier”.

85. On the above clause, Dr. Asim Kumar Dasgupta, Ex-chairman, Empowered Committee of State Finance Minister's expressed his following views before the Committee :

"On Clause 18, I would say that the commencement period has been kept at one year. Suppose a State election is declared, then that State would not be able to implement the GST. So, we need to be a little more tolerant. Instead of 'one year' if it is 'two years', then it would be better".

V. Administration and IT Mechanism

86. In their memorandum submitted to the Committee, the Government of Gujarat has stated that to implement flawless GST design, the basic prerequisites are seamless IT infrastructure, uniform administrative paradigms (threshold, common list of exemptions) unified tax credit clearing mechanism and provision of compensation for revenue losses.

87. Establishment of a seamless value chain and tax credit mechanism on such a chain, would presuppose a common IT platform where all the e>Returns, e-payments and e-registration are received and processed. With the threshold limit being proposed at Rs. 10 lakh, the total number of dealers would be at least 30-35 lakhs. The quantum of data exchange that would be required for adjusting credits available under SGST and CGST against IGST, would be enormous. At present, the states which are getting 100 percent e>Returns, e-payments and e-registrations are Kerala and Maharashtra. Gujarat has achieved 90% e-compliance in payments, returns and 100% e-registrations. Gujarat has been making steady progress in use of IT in tax administration and has done process re-engineering to facilitate quick and efficient service delivery and at the same time use of IT as a tool to plug leakages.

88. On IT infrastructure, the Ministry of Finance clarified as under :

"An Empowered Group on IT Infrastructure (EG) headed by Shri Nandan Nilekani has been constituted to put in place a strong IT infrastructure for GST. The group is working to achieve this objective in a time bound manner. Further, in order to IT enable commercial

tax administrations of States/UTs, a Mission Mode Project has been launched to provide financial support to the States and UTs”.

VI. Compensation Mechanism

89. Shri Sushil Modi, Chairman, Empowered Committee of State Finance Ministers in his post-evidence reply has stated that there is a trust deficit between the Centre and States on account of non-payment of CST compensation to the States. The States feel that they have to go with a begging bowl for the CST compensation to the Centre asking for compensation. So the States want that in Article 279A for GST Council itself, there should be a provision for the GST compensation mechanism so that GST compensation can be recommended by the GST Council.

90. The Gujarat Government in their written memorandum has stated that given that service tax alone would not be able to compensate loss of revenue in many states, and that Revenue Neutral Rate (RNR) will not be achieved, the issue of GST compensation becomes paramount to maintain fiscal balances in these states. There is no clarity about the GST compensation package for loss to the States. The experience of CST compensation has been very painful. Any compensation-based system is a blow to the fiscal self-reliance of the states and is open to disputes on eligibility, calculation and amount of outstanding claims. Statutory devolution of compensation is not provided for under the proposed GST model. Total losses to all the States are estimated by the National Institute of Public Finance and Policy (NIPFP) at a level of Rs. 32,000 crore based on calculations taking 2007-08 as the base year. On the other hand, Task force under 13th Finance Commission has suggested a provision of Rs. 50,000 crore as compensation for 5 years. Thus, adequate amount of compensation needs to be planned for.

91. Thirteenth Finance Commission in their Report (Volume 1) on GST have stated that states had requested that an objective compensation mechanism to support possible revenue losses after implementing GST be put in place. In this regard, they recommended the following :

- i. The present Empowered Committee be transformed into a statutory Council of Finance Ministers with representation from the Centre and states. A GST Compensation Fund should be created under the administrative control of this Council.
- ii. The Central Government shall transfer to the GST Compensation
- iii. The amounts in the Fund should be used for compensating states for any revenue loss on account of adoption of the model GST.
- iv. The amount will be disbursed in quarterly instalments on the basis of the recommendations made by a three-member Compensation Committee comprising of the Secretary, Department of Revenue, Government of India; Secretary to the EC and chaired by an eminent person with experience in public finance. This person would be appointed by the Union Government.

92. To a specific query as to whether compensation to the States should be made a part of the Constitution Amendment, the Ministry of Finance in their post-evidence reply stated that the proposed model of the GST, in particular the RNR that will be finally decided, is expected to ensure that there is no loss because of the CST or any other aspect of the GST. States are expected to gain substantial revenue on account of the power to tax services and to obtain the share of taxes by the levy of GST on importation of goods. Nevertheless, the Centre has assured compensation for a specified period if there is a loss. The detailed understanding on the same would be worked out in the run up to the GST. There is no need to build the same in the Constitution Amendment Bill. In any case, the Constitution provides for the setting up of a Finance Commission every five years or earlier if required, to examine the issue of fiscal transfers from the Centre to the States and their distribution among the States.

VII. GST Monitoring Cell (GMC)

93. Dr. Parthasarathi Shome, Director & Chief Executive, Indian Council for research on International Economic Relations in his memorandum stated that the GST introduction must be accompanied by a strong GST Monitoring Cell (GMC). This was not done adequately for the VAT in terms of requisite post-introduction monitoring and analysis. At least for the GST, the GMC, with an adequate

allocation of qualified staff, should follow closely the immediate impact of the GST, for example, on inflation and any possible hoarding, as well as the unfolding ramifications for tax administrative ease, lowering of compliance costs for taxpayers, elimination of moral hazard for both taxpayer and tax administrator, and the success of the ICT mechanism put in place for interstate trade to assess whether India becomes a truly common market.

VIII. Alternative to GST Model

94. The State Governments of Madhya Pradesh and Gujarat have offered alternatives to GST model which is enunciated as under :

Gujarat Model

The GST model as proposed by the Central Government and being introduced through the Constitution (115th Amendment) Bill, 2011 suffers from imbalance in the division of resources and functions between the union and States, absence of reliable and accurate State-wise data on services, different, contradictory reports / estimates, adverse impact on prices and employment generation, etc. pending transition / operational issues. An alternative model to achieve the major objectives of reforms in indirect taxes was therefore, proposed by Gujarat in January, 2010, as follows :

- States retain the subject of CGST in Centre's list and SGST in State list under Constitution as is the case of VAT now.
- Collection by States of CGST and SGST as is being done now for CST. Transfer of CGST amount collected by the respective State tax authorities to Central Government. States collect and retain SGST and CGST. Subsequently CGST to be transferred to the Centre.
- Revenue Neutral Rate (RNR) to be finalized jointly by the Centre and States in the Empowered Committee.
- The principle of protection of revenue of the States, in the base year and subsequent projection as per CGAR, would be followed.

Views of Madhya Pradesh Government on GST

95. It is understood that need for GST is driven by the need to have common national market and to reduce the number of indirect taxes. However, this cannot be done at the cost of reducing revenues of the States and rendering them bereft of financial autonomy. The better way to achieve this end would be to help States integrate most of the State taxes and bring them on an IT platform, which would reduce the problems for tax payers. The payment of VAT should also be on IT platform and national and inter-State transactions should be freely shared. This would not only reduce malpractice but also help in seamless movements of goods. States have already made substantial progress in this direction.

96. Regarding services, Centre should consider the transfer of the administration of tax on services as provided in Article 268A. States can integrate administration of tax on services with State VAT just as has been done with CST through the mechanism of ITR. Centre can retain administration of certain services like financial services, railways and air services which can pose difficulties at the State level. It can progressively reduce excise duties and custom duties so as to keep industries more competitive as is the case in US. This scheme can be implemented with minor amendments in CST Act and the Service Tax legislation.

97. The Ministry of Finance has submitted their following comments on the above alternative models of GST :

“This model is unacceptable to the Centre for the following reasons:

- Domestic taxes still account for a very high proportion of total tax revenues of the Centre for the collection of which it cannot be dependent on 32 States/UT Governments.
- In the proposed arrangement, the “assignment” to the Union is envisaged on the basis of the devolution formula stipulated by the Finance Commission. But the final share of the State may not correspond to the amount it retains in this manner. This implies that each State would be required to settle accounts with every other State for final settlement.

- For inter-state supply of goods and services, centralized agency would still be required for levy and collection.

The alternative model of Gujarat and Madhya Pradesh have not been accepted by the Empowered Committee of State Finance Ministers itself”.

IX. Latest position of the Empowered Committee of State Finance Ministers on the provisions of the Bill

98. When asked to indicate the latest position of the Empowered Committee on the provision of the Bill, the Chairman, Empowered Committee vide his communication has stated that the views of the States and his own observations on the Bill furnished to the Standing Committee on Finance in the year 2012 may be treated as valid and taken into consideration. However, the Chairman, Empowered Committee furnished the following supplementary observations on the Bill :-

SUPPLEMENTARY OBSERVATIONS

Option to the States to join GST

- ☐ States may be given option to join GST from the date of implementation or even at a later date by making suitable amendments in the Constitution (One Hundred and Fifteenth Amendment) Bill, 2011.
- ☐ States may be provided incentives/compensation by the Central Government to encourage them to join GST regime.
- ☐ Obligations and flexibilities of the Central Government and States may be properly defined and a common forum for discussion on GST between the States and the Central Government should be established (The Bill already provides for setting up of a GST Council).
- ☐ Appropriate legislation to determine precise place of supply rules and the taxability of inter-state transactions would also need to be prepared by the Central Government in consultation with the States.

Fiscal Autonomy of the States

- Fiscal autonomy of the States is required to be ensured. This can be achieved by giving some flexibility to the States in deciding GST rates, exempted items and thresholds, keeping in view the local needs of each State.
- A State may be allowed to exempt few additional items subject to the condition that the total revenue implication of the same is limited to certain percentage of its GST revenue.
- Floor rates in fairly narrow band are workable and that should be allowed. [As suggested in earlier observation for Clause 12 of the Bill].

Consultation with and Education of the Stakeholders

- The general public and the stakeholders have to be properly educated and made aware of the benefits of the GST to ensure their acceptability. Support of the key associations of trade and industry is also necessary.
- The rules and procedures should be simple and unambiguous so that confusion and litigations could be avoided. Significant stakeholder consultation is required in finalising the rules and procedures. Practical guidelines should be provided by the Central and the State Governments to the stakeholders and there should be a mechanism with the law makers and administrators to solve matters as they arise on the new rules and procedures.
- Adequate lead time is required to be provided to the trade and industry so that they are able to change their accounting systems and other procedures well in time.
- Tax officials and personnel have to imparted adequate training to manage the transition smoothly.
- Precise rules of transition need to be evolved and publicised much in advance.
- These are legislative and administrative matters and are required to be undertaken at the time of implementation of GST.

Rates and Special Provisions

- Efforts should be made to have standard rate as low as possible to reduce the burden on the consumers. To ensure this, possibilities of tax-evasion are required to be minimized and the Central Government may have to adequately compensate the States, in case, they suffer losses on account of implementation of GST during the initial years.
- To ensure that small scale industries/traders are not affected adversely due to the implementation of GST, special provisions are required to be made for them. This may also include income tax incentives to be given by the Central Government in this regard.
- Keeping in view the psychology of the consumers, possibility of making the GST as 'invisible tax' and merging it with MRP may have to be considered.

Avoidance of Dual Control

- One of the lessons learned from the visit is that it is always preferable that only one agency collects the tax. In case, it is not feasible then at least new areas of dual control should be avoided. It has, therefore, been suggested by the Empowered Committee that the Government of India should retain their existing threshold of Rs.1.5 crores for goods in GST regime also so that those small dealers and manufacturers who are not subjected to CENVAT at present, are also not subjected to the dual control in the GST regime.
- The GSTN portal should be made to go live as soon as possible so that common front end solutions like registration, returns and payments can roll out in order to lessen the impact of dual control in core functions.

Taxation of Tobacco & Tobacco Products

- As per the existing provisions of 'The Constitution (One Hundred and Fifteenth Amendment) Bill, 2011', States can only impose GST on Tobacco and Tobacco Products while the Centre can impose both GST and Excise Duty. Keeping in view the requests received from several States and the fact that the States are already levying VAT at very high rate on Tobacco and Tobacco Products, therefore, the States may also be allowed to levy State Excise Duty or any other tax in addition to GST on Tobacco and Tobacco Products. This could be achieved by making

amendment in Entry 51 in the State List of Seventh Schedule of the Constitution by incorporating “(c) tobacco and tobacco products.”

X. Consensus between Centre and States on GST Design and CST Compensation

99. In a written communication, the Ministry of Finance (Department of revenue) informed the Committee that the Hon’ble Finance Minister held a meeting with the State Finance Ministers on 8th November, 2012 where issues relating to GST were discussed. In accordance with the decision taken in the meeting with the State Finance Ministers, two Committees have been constituted to finalise the GST design and to consider the issue of CST compensation to the States for the revenue loss on account of reduction of CST rate from 4% to 2%. These two Committees are likely to submit their Reports by 31st December, 2012. Ministry of Finance (Department of Revenue) intends to finalise its views after the Reports of these two Committees are received.

100. In the meantime the two Committees constituted by the Ministry have submitted their reports to the Ministry on 21st January, 2013. These two reports were considered by the Empowered Committee (EC) of State Finance Ministers in its meetings held in Bhubaneswar on 28th - 29th January, 2013.

101. Subsequently, the Ministry of Finance (Department of Revenue) through a written communication have informed the Committee that the recommendation of Empowered Committee as contained in the minutes of the meetings held on 28th – 29th January, 2013 (as reproduced below) on the reports of the Committees on GST Design and CST Compensation are being examined in the Ministry of Finance (Department of Revenue) and a Committee has been constituted to look into the changes required in the Constitution (One Hundred and Fifteenth Amendment) Bill, 2011. Also an amount of Rs. 9,000 crore has been allocated in the Budget for the year 2013-14 payment of the first installment of balance amount of CST compensation for the State:

Suggestions made during meetings of Empowered Committee (EC)
held at Bhubaneswar on 28-29 January, 2013

- “(i) A change of drafting nature in Article 249 - The Amendment proposed in Article 249 reads as follows: **In article 249 of the Constitution, in clause (1), after the words ‘with respect to’, the words ‘goods and services tax or’ shall be inserted.** As, ‘with respect to’ appears twice in clause (1) of Article 249, it therefore needs to be clarified whether the words ‘goods and services tax or’ should be inserted after the first or second or both places where ‘with respect to’ appears in the Article.
- (ii) Amendment to sub-clause (d) of clause (4) of Article 279 to provide for floor rates with bands. The present formulation envisages a single rate of GST.
- (iii) Insertion of a new sub-clause in clause (4) Article 279A to provide States and Centre flexibility to raise additional resources during the time of natural calamities and disasters.
- (iv) The need for amendment to clause (4) of Article 279A to provide for special schemes, for North-Eastern State and the State of J&K.
- (v) Amendment to clause (6) of Article 279A, for increasing the proposed quorum to half from the present proposed one-third.
- (vi) Changes to clause (8) of Article 279A to provide for voting instead of ‘consensus’ for decisions of the GST council with Central representatives **present in the Council meeting** having one-third weightage and State representatives having two-thirds weightage, with the decision being taken **with more than three-fourths weightage votes of the representatives present in the meeting.**
- (vii) Deletion of Article 279B to omit the **GST Dispute Settlement Authority.** Simultaneously, a reference to Article 279B in the proposed amendment to Article 368, will need to be deleted.
- (viii) Amendment in Article 286 for doing away with the concept of **declared goods** in case it is proposed to include petroleum products under the GST.
- (ix) Amendment to clause (12A) of Article 366 to delete petroleum products from the list of goods on which GST will not apply.
- (x) Including a definition of ‘Service’ in the Constitution itself.
- (xi) Modifying the proposed amendment to entry 52 in the State List to allow only ‘entry tax in lieu of octroi’.”

PART- III
OBSERVATIONS / RECOMMENDATIONS

Background

1. The Constitution (115th Amendment) Bill, 2011 relating to GST was referred to the Standing Committee on Finance of Parliament on 29 March, 2011 for detailed examination and Report thereon. A Press Communiqué was issued in May, 2011 inviting comments / suggestions. More than hundred memoranda comprising of several suggestions were received in response to the Press Communiqué. Since then, the Committee, while apportioning their limited time between various other Bills referred to them, including the ones the Government wanted returned urgently held regular meetings conducting several oral hearings on this Bill on a regular basis involving the Ministry of Finance and various stakeholders like Federation of Indian Chamber of Commerce and Industry (FICCI), Confederation of Indian Industry (CII), Petroleum Federation of India (PETROFED), International Spirits & Wines Association of India (ISWAI), Indian Merchants' Association (IMA), Film and Television Producers Guild of India, All India Federation of Tax Practitioner (AIFTP), Bhartiya Udyog Vyapar Mandal (BUVM), etc. The Committee also heard experts like Dr. Asim Kumar Dasgupta, Dr. Vijay Kelkar and Dr. Parthasarathy Shome. The Committee also took special permission of the Hon'ble Speaker to call representatives of various State Governments like Odisha, Maharashtra, Tamil Nadu, Madhya Pradesh and Gujarat in order to have a cross-section of opinion on the Bill. The Committee thus made it a point to hear

divergent views on certain complex issues related to the Bill. During this period, the Committee also had extensive interaction with the Empowered Committee of State Finance Ministers and heard the views of their Chairman, Shri Sushil Kumar Modi. The Committee also gathered useful inputs from the overseas tours undertaken by the Empowered Committee.

2. The various points raised by the Members during their sitting held in June, 2012, were sent to the Ministry for their reply. The Committee were keen to submit their report in the monsoon session of Parliament , 2012. However the Ministry submitted their interim replies only in August, 2012. Subsequently, the Committee requested the Ministry of Finance to submit their final views on the Bill and sought clarification as to whether any review was being conducted with regard to any of the provisions of the Bill with a view to arriving at a consensus since there were reports to that effect in the media. The Ministry informed the Committee that the position of the Ministry would be communicated by the end of January, 2013 on submission of the reports of the Committees on GST design and CST compensation issues. Further, during the month of March, 2013, the Ministry informed the Committee that the recommendations of the Empowered Committee made in their meetings held on 28th-29th January, 2013 on the reports on GST Design and CST Compensation were being examined in the Ministry and a Committee had been constituted to look into the changes required in the Bill. They also informed that in the meantime, an amount of Rs. 9,000 crore had been allocated in the Budget

for 2013-14 for payment of first instalment of balance amount of CST Compensation for the States. The Committee were also given to understand that a conclusive view on the changes to be made in the Bill would, however be taken only after taking into account the observations and recommendations of the Standing Committee on Finance. The Committee are surprised however, to note that there was no finality in the thinking of the Ministry during the whole period the Committee were engaged in the examination of the Bill with the result that it remained work in progress *simultaneously* at both ends. The matter continues to be in a state of flux. However, the Committee have decided to pronounce their views on the Bill and fulfill their mandate, so that they are not *blamed* for stalling the Bill. The Committee have thus sought to finalise and present their Report on the far-reaching Constitution (Amendment) Bill after thorough deliberations involving as many stakeholders as possible so that a fair consensus can be achieved on the provisions of the Bill and issues connected therewith.

GST Design

3. The Committee note that the proposed Bill envisaged harmonization of the indirect tax regime by subsuming a variety of taxes levied by the Centre and the States. The implementation of GST would allow the Centre and State Governments to avoid multiple layers of taxation that currently exists in India leading to the creation of a single market. The most important aspect of the Bill is the consensus required with all the States in

the design of the GST structure and all the other contours. The Committee note that there has been divergence in views amongst States, who have serious apprehensions on erosion of state autonomy. A fine balance is therefore required to be maintained between the imperatives of a common market with unified tax structure vis-à-vis the fiscal requirements of States. The Centre needs to play a pro-active role in this regard.

The Committee are of the view that any tax reform should have an objective of improving economic efficiency, encouraging economic activity and benefiting the common man and should be put in place giving due regard to the Constitutional Scheme of distribution of powers and fiscal autonomy of the States. In a federal set up, implementation of a comprehensive tax reform like GST hinges on mutual trust and cooperation between Centre and State Governments. The Committee are of the opinion that before proceeding to enact 'The Constitution (One Hundred and Fifteenth Amendment) Bill, 2011, broad consensus on key issues concerning the implementation of GST should be arrived at between the Centre and the State Governments. While designing the desired tax reforms, the Government should also learn from the experience in other countries, while taking into account the political, social and economic variations obtaining in our country. Adequate groundwork would thus be essential before setting upon to operationalise the proposed GST regime. Keeping in view the apprehensions expressed by States, a credible study would also be required to evaluate the impact of the GST regime on the

revenues of States. If the success of VAT in States has to be replicated, it may be necessary to leave enough flexibility and fiscal space for the States. It may also be made optional for States as was done in the case of VAT. In the succeeding paras, the Committee have commented upon specific issues arising out of some of the clauses in the Constitution (Amendment) Bill and have suggested changes, wherever required.

Compensation Mechanism

4. The Committee note that differences had emerged between the Centre and States on account of CST compensation to the States arising out of phasing out of CST. Further, during their interactions with State Governments, the Committee observed that one of the major concerns over implementation of GST is Revenue Neutrality Rate (RNR). Some States generating high tax revenue have expressed apprehensions on the possibility of suffering revenue losses after the implementation of GST. The Committee note with concern that no structured mechanism has been formulated so far *to attend to this problem*. The Committee would, therefore, recommend that a well-defined automatic compensation mechanism may thus be built in, which would ensure that trajectories of revenues being contemplated are maintained at least in the short turn. Suitable amendments may accordingly be made in the Bill providing for a built-in permanent compensation mechanism with a view to addressing the legitimate revenue concerns of States. For this purpose, a GST

Compensation Fund may be created under the administrative control of the GST Council.

Administration and Information Technology (IT) Mechanism

5. The Committee concur with the view that for flawless implementation of GST, the basic prerequisites are seamless IT infrastructure, uniform administrative paradigms, unified tax credit clearing mechanism etc. The Committee note that in this regard an Empowered Group on IT Infrastructure headed by Shri Nandan Nilekani has been constituted to put in place a strong IT infrastructure on GST in a time bound manner. For smooth and effective implementation of GST, the Committee would urge the Central Government to provide technical assistance and capacity building at State level, which would help in developing robust IT practices, ranging from overall procedure of e-filing of tax return to audit of tax and result in enhanced GST collections at the State level. Without well-designed IT infrastructure across the country, the benefits of GST may remain elusive. It is also imperative that although a dual GST regime has been proposed, a situation of trade / business dealing with a dual administration and multiplicity of authorities should be avoided, as it may create more hassles rather than ease them. Though not part of the Constitutional Amendment Bill, this issue needs clarity, so that dual GST regime becomes acceptable to trade and commerce at large and fosters tax compliance.

Integrated Goods and Services Tax (IGST)

6. The IGST model envisages that the Centre will levy tax at a rate approximately equal to (CGST + SGST) rate on inter-State supply of goods and services. It will be collected by the Centre and transferred to States depending upon whether the State is net exporter or net importer for the given period of settlement. The Committee note that the settlement of accounts will be done by the Centre that would function as a clearing house for this purpose. The proceeds of the IGST arising out of inter-state trade or commerce shall thus be used for the settlement of accounts among the States for the flow of input tax credit in the course of Inter-State transactions based on 'destination principle' thereby providing a continuous credit chain across States. The Committee further note that to the extent, goods or services are supplied from one State to another for further distribution, IGST transactions would be revenue neutral. However, in practice, there may be a possibility of a positive balance in the proceeds of IGST at the end of a fiscal year. The Committee, therefore, desire that a suitable proviso in the Article 269A in both Clause 9 and Clause 10 of amendment Bill may be made for distribution of remaining proceeds of IGST when the accounts of the fiscal year have been settled.

It has also been submitted to the Committee by some experts that the IGST model could be onerous in terms of compliance and administrative burden and that since it is meant for effectively tax inter-state trade on destination principle, the Central Government need not get

involved in this process. A simpler model (Modified Bank Model) as recommended by the Task Force on GST set up by Thirteenth Finance Commission has been suggested for settlement of proceeds arising out of inter-state trade. The Committee note that the Central Government will only act as a clearing agent with regard to IGST, which remains in effect a clearing mechanism between States for inter-State transactions. The Committee would thus suggest that the alternate model, suggested by the Task Force on GST constituted by the 13th Finance Commission could be considered with a view to simplifying and easing compliance and administrative burden and ensuring a smooth clearing house mechanism between States for facilitating the process of IGST after consideration by the GST Council.

Further, as the destination-based IGST model favours predominantly consumer States more than producer States, the revenue concerns of these States also needs to be factored in and duly addressed. The proposed model should not thus act as a dampener or dis-incentive for States with a strong manufacturing base.

GST Dispute Settlement Authority

7. In concurrence with the views expressed by State Governments and the Chairman, Empowered Committee, the Committee believe that the proposed provision of GST Dispute Settlement Authority would affect the fiscal powers of Parliament and the State Legislatures. The Committee, therefore, desire that the proposed Article 279B providing for GST Dispute

Settlement Authority should be omitted, as this body would have the effect of overriding the supremacy of Parliament and the State Legislatures. However, since any dispensation involving several entities / interests requires a mechanism to resolve disputes / differences, it may be expedient to make a provision in Article 279A itself empowering the GST Council to decide about the modalities to resolve disputes arising out of its recommendations.

Harmonized Tax Structure

8. The Committee note that Clause 5 of the proposed Article 279A require the GST Council to be guided by the need for a harmonized structure of goods and service tax and for the development of a harmonized market for goods and services. However, since the words have not been defined in the proposed Bill, the Committee are of the view that such ambiguity should not remain in the Bill. They would therefore recommend that the word 'harmonized structure' may be clearly amplified or defined. It should also be clarified that the provisions contained in Clause 5 are in the nature of guiding principles for the Council and not mandatory or obligatory in nature.

Consensus

9. The Committee note that the decisions in the GST Council, would be taken, based on consensus which implies that all the members present would have to agree to a proposal; even if one State differs, the decision

cannot be passed. The Committee feel that keeping in view the diversity in socio-economic interests of the States, achieving such a consensus is likely to be very difficult. As it would be critical in ensuring that all the valid interests are properly reflected in the recommendations of the GST Council, the Committee would therefore recommend amendments to Clause (8) of Article 279 A so as to provide for voting instead of consensus for decisions of the GST Council. Accordingly, as agreed upon by the Empowered Committee, one-third weightage for central representatives and two-thirds weightage for state representatives may be provided with the decision taken by the Council being passed with more than three-fourths votes of the representatives present in the meeting. Similarly, amendment to Clause (6) of Article 279A may also be made for increasing the quorum to half from the proposed one-third. In this context, the Committee would recommend that in tune with the spirit of cooperative federalism, it would be in order if the proposed GST Council functions like the present Empowered Committee, which has had a good track record of not only reforming the tax system but also resolving differences amicably in an institutional mode.

Declared Goods

10. In order to ensure that there is no unilateral decision by the Centre regarding taxation of 'declared goods' kept outside the purview of GST (clauses 3 and 4 of amendment proposed in Article 286) and also to uphold the spirit of cooperative federalism, which is crucial for the structure of

dual GST, the Committee recommend that Clause 3 may be amended so that in place of “subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of tax as Parliament may by law specify”, the phrase “subject to such restrictions and conditions of tax as Parliament may by law specify on the recommendations of the GST Council constituted under 279A” may be substituted. This change is expected to allay the fears of States to some extent on loss of fiscal autonomy.

In this context, it would also be expedient to insert a new sub-clause in Clause (4) of Article 279A to provide both States and Centre the requisite flexibility to raise additional resources during period of natural calamities and disasters. The proposed Clause 4 of Article 279A may also be suitably amended to provide for special schemes for North-Eastern States, the State of J & K and other special category States. Similarly, the Central Government should also have the flexibility to levy surcharge or cess whenever required or during extra-ordinary circumstances.

Entry Tax

11. The Committee note that entry 52 of Seventh Schedule is worded in the Bill as “taxes on the entry of goods into a local area for consumption, use or sale therein to the extent levied and collected by a Panchayat or Municipality”. As most of the States seem to be opposed to this proposed amendment, the Committee do not agree with this formulation. It will not be desirable to go back to the earlier system of levy and collection of octroi by local bodies and this will be a retrograde step, which would hinder free

flow of trade and increase compliance burden. The Committee therefore desire that entry tax in general should be subsumed in GST. The relevant Clause / sub-clause in the Bill may be modified accordingly so as to empower the States to collect entry tax for distribution to local bodies instead of leaving it to be collected by different local bodies.

Floor Rate

12. Tax on sale of goods is the biggest and most buoyant source of revenue for States. The Committee are of the opinion that the States should have some limited leverage to vary the rate of tax depending on exigencies. The Committee, therefore, desire that a system of band with floor rate should be adopted while introducing GST, so that States have some elbow-room within stipulated limit to calibrate the rate of tax depending on needs of the situation and the dynamics of circumstances. The Committee are of the view that based on the European model, there could be a floor rate and a ceiling rate within which the States will have the freedom to have a high or a low rate. Taking into account the need for State autonomy, the States may thus be allowed to increase their GST rate within a narrow band. There could however be provision to levy higher rates on demerit goods, whenever necessary. The proposed Article 279 (A) may accordingly be modified *providing for* such a flexibility in rate.

Threshold of limits of turnover etc. for exempting certain class of taxpayers like small traders / manufacturers / service-providers may also be left to the wisdom of the GST Council. Although it is ideally desirable that the GST regime is made comprehensive and all encompassing for the present, the existing exemption for small business may continue in line with the Government policy to encourage and promote small enterprises including self-employed sector.

Exclusions

13. Article 366 of the Constitution is proposed to be amended vide Clause 14 in the Bill, wherein taxes on the supply of specified goods is proposed to be excluded from the purview of GST. The Committee believe that such specific exclusions need not be provided in a Constitution (Amendment) Bill, as this will needlessly make the GST regime very rigid. Since the ultimate goal is to have an integrated, comprehensive and seamless GST regime subsuming various Central and State indirect taxes and levies, the Committee recommend that the above-mentioned exclusion provision may be omitted from the Constitution (Amendment) Bill. In any case, the proposed provision inserting Article 279A in the Constitution empowers the GST Council vide Clause 4(a) and (b) to make recommendations on subsuming or exempting or excluding certain goods / services from the purview of GST. The Committee thus believe that the constitutional mandate being provided to the GST Council is resilient enough to address emerging situations.

GST Monitoring

14. Considering the fluidity and uncertainties involved in ushering in radical changes in the tax system, the Committee believe that there is a need to set up a GST Monitoring / Evaluation Cell, which should closely follow on a continuous basis the immediate impact of GST on key aspects such as growth in GDP, inflation, hoarding, compliance costs for taxpayers, administrative bottlenecks and, last but not the least, the retail prices paid by the ultimate consumer. The efficacy of the proposed GST model in lieu of the existing CST dispensation with regard to inter-state trade / transactions and the requirement for a robust, error-free IT platform also needs to be monitored with a view to assessing and ensuring that India becomes a truly common market. Certain pro-consumer measures should be initiated as well, such as, passing on tax credit benefit to retail consumers for cushioning them against possible increase in prices post-GST and ensuring that cascading effect on consumer prices is well and truly avoided as envisaged. The GST Monitoring / Evaluation Cell may function under the aegis of the proposed GST Council. This may be incorporated as a clause / sub-clause in the proposed Article 279A of the Bill so as to put monitoring of GST on a firmer footing.

Conclusion

15. In conclusion, the Committee are of the considered view that fears expressed in some quarters about the proposed GST Council being made a constitutional body and infringing upon or even overriding the supremacy of Parliament or State Legislature is not correct as it is envisaged as a recommendatory body. The fruitful experience with the Empowered Committee of State Finance Ministers so far does not seem to give any credence to such apprehensions. This body has provided a useful platform for consensus-building between Centre and States and has evolved democratic practices over time to discuss and resolve issues. The Committee would thus expect the proposed GST Council to follow the principles of cooperative federalism and democratic governance. As this will be a political and a recommendatory body, it would be in a position to play a constructive and enabling role vis-à-vis the Legislature, which needless to emphasise, would remain supreme in matters of legislation including taxation. In the Committee's view the mandate entrusted to the GST Council under the proposed Article 279A of the Constitution (Amendment) Bill does not in any way alter the existing constitutional scheme in so far as the Legislature, both Union and State, is concerned.

On the whole, the Committee are of the view that the Constitutional (Amendment) Bill should not ideally include specific aspects relating to rates, exemptions, exclusions, thresholds, administrative arrangements etc. What should be included in the laws and rules should not form part of

the Constitution of India. The present Bill relating to GST, in the Committee's view, has not been well-drafted from this perspective and, therefore, requires amendments as suggested above.

New Delhi;
25 July, 2013
Shravana 03, 1935 (Saka)

YASHWANT SINHA
Chairman
Standing Committee on Finance

NOTE OF DISSENT

Naresh Agrawal, MP (RS)
01/07/2013

The Standing Committee on Finance is sending its report on GST to Government. Whereas the Prime Minister and Finance Minister are continuously giving statements that Union Government are reconsidering over this issue. I have objected but you were adamant on sending your report.

Sir, I am sending my objections as well as of Uttar Pradesh Government. Please attach the annexure to the report to be sent to the Union Government so that our objects are also registered.

Objections:

- ❖ The way by which taxes collected by Union Government through GST will be allocated to the States and what will be its time limit?
- ❖ Initially huge resources are needed for GST collection and for this purpose, how Union Government is going to provide assistance to the States?
- ❖ How Union Government is going to compensate the States in the next five years of the financial loss suffered by the States due to implementation of GST?
- ❖ Municipal Corporation, Municipality, Town Area, Zila Prishad etc. impose taxes at local level, so what is the provision in GST regarding this.
- ❖ Uttar Pradesh Government is totally against GST because due to this Union Government will have direct interference in State Governments head, which will be direct interference in sovereignty of States.
- ❖ There are 11 States in total having special status. Whether those States will retain the reliefs which they were receiving even after implementation of GST? If so, the manner in which this will be done.

Sd/
(NARESH AGRAWAL)

MINUTES OF THE TWENTY SECOND SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)

The Committee sat on Friday, the 8th June, 2012 from 1130 hrs to 1600 hrs.

PRESENT

Shri Yashwant Sinha – Chairman

MEMBERS

LOK SABHA

2. Shri Shivkumar Udasi
3. Shri Bhakta Charan Das
4. Shri Gurudas Dasgupta
5. Shri Bhartruhari Mahtab
6. Shri Anjan Kumar Yadav M.
7. Shri Prem Das Rai
8. Shri R. Thamaraiselvan

RAJYA SABHA

9. Shri Vijay Jawaharlal Darda
10. Shri Piyush Goyal
11. Dr. Mahendra Prasad

SECRETARIAT

1.	Shri A.K. Singh	-	Joint Secretary
2.	Shri R.K. Jain	-	Director
3.	Shri Ramkumar Suryanarayanan	-	Deputy Secretary
4.	Shri Kulmohan Singh Arora	-	Under Secretary

Part I

(1130 hrs. to 1345 hrs.)

WITNESSES

Ministry of Finance (Department of Revenue)

1. Shri R.S. Gujral, Finance Secretary & Secretary (Revenue)
1. Shri S.K. Goel, Chairman, CBEC
2. Shri Laxman Das, Chairman, CBDT
3. Shri Shashi Shekhar, Addl. Secretary (Rev)
4. Smt. Sreela Ghosh, Member (CX)
5. Shri M.S. Badhan, Member (Customs)
6. Ms. Praveen Mahajan, Member (P&V), CBEC
7. Ms. Sheila Sangwan, Member (Service Tax)
8. Ms. J.M. Shanti Sundharam, Member (L&J, Budget)
9. Shri M.L. Meena, Joint Secretary (Rev)

10. Shri V.K. Garg, Joint Secretary (TRU-II)
11. Shri Vivek Johri, Joint Secretary (TRU-I)
12. Shri Arun Sahu, Director General (Systems)

2. The Secretary, Ministry of Finance (Department of Revenue) briefed the Committee on the provisions of 'The Constitution (One Hundred Fifteenth Amendment) Bill, 2011' (GST). Members sought clarifications from the witnesses on the issues pertaining to the Bill, which inter-alia included objectives behind the Bill, rationale of dual GST model for the country, Integrated GST (IGST) to be levied on Inter-State Transaction of Goods and Services, exemption of specified petroleum products, electricity and alcohol for human consumption from the purview of GST, Constitution of proposed Goods and Services Tax Council and Goods and Services Tax Dispute Settlement Authority. Other issues discussed included impact of GST on the fiscal autonomy of the States, provision of compensation to States for loss related to introduction of GST. The Chairman directed the witnesses to send written replies in response to the queries posed by the Members at the earliest.

The witnesses then withdrew.

Part II
(1415 to 1600 hrs.)

WITNESS

Dr. Asim Kumar Dasgupta, Former Finance Minister, West Bengal and Former Chairman, Empowered Committee of the State Finance Ministers.

1. The Committee then heard Dr. Asim Kumar Dasgupta on 'The Constitution (One Hundred Fifteenth Amendment) Bill, 2011'. The major issues discussed broadly related to empowerment of the States and Centre to levy tax on Goods and Services and tax on inter-state transactions, the setting up of GST council with representation of the Centre and the States, for recommending the GST rates and other matters of GST with a view to uphold the need for a harmonized tax structure and the development of a harmonized national market for goods and services. The other issues discussed included the setting up of a GST Dispute Settlement Authority for necessary adjudication and to uphold the

proposed dual GST structure. Dr. Asim Kumar Dasgupta replied to the queries raised by the Members during the sitting.

A verbatim record of the proceeding was kept.

The witness then withdrew.

The Committee then adjourned.

MINUTES OF THE TWENTY THIRD SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)

The Committee sat on Friday, the 15th June, 2012 from 1130 hrs to 1630 hrs.

PRESENT

Shri Yashwant Sinha – Chairman

MEMBERS

LOK SABHA

2. Shri Shivkumar Udasi
3. Shri Bhakta Charan Das
4. Shri Gurudas Dasgupta
5. Shri Bhartruhari Mahtab
6. Shri Prem Das Rai
7. Shri Sarvey Sathyanarayana

RAJYA SABHA

9. Shri Naresh Agrawal
10. Shri Piyush Goyal
11. Dr. Mahendra Prasad
12. Shri P. Rajeeve

SECRETARIAT

1.	Shri A.K. Singh	-	Joint Secretary
2.	Shri R.K. Jain	-	Director
3.	Shri Ramkumar Suryanarayanan	-	Deputy Secretary
4.	Shri Kulmohan Singh Arora	-	Under Secretary

Part I

(1130 hrs. to 1330 hrs.)

WITNESSES

The Empowered Committee of State Finance Ministers

1. Shri Sushil Kumar Modi, Chairman & Deputy CM, Bihar
2. Shri Satish Chandra, Member Secretary

2. The Chairman, Empowered Committee of State Finance Ministers briefed the Committee on the provisions of the 'The Constitution (One Hundred Fifteenth Amendment) Bill, 2011' (GST). Members sought clarification on issues like article

269 (A), CGST and on GST Dispute Settlement Authority. Members also deliberated upon the quality of collection agency and how a particular transaction of goods and services would be taxed simultaneously under CGST and SGST. Members also deliberated upon taxes (Central and State) to be subsumed under GST, cascading effect i.e. tax on tax and how to remove it. Some topics like positive balance proceed at the year end with the IGST, positive impact because of the integration of markets, reduction in prices and treatment of North Eastern States and special category States were also raised. Clarification on the definition of 'harmonized structure' was also sought. Concern were also raised on Central GST and State GST being separate and complication thereon and securing the fiscal autonomy of the State Governments. The Chairman, Empowered Committee also informed the Members about increase in growth of revenue post VAT implementation. The Chairman directed the witness to send written replies in response to the queries posed by the Members at the earliest.

The witnesses then withdrew.

Part II
(1430 hrs. to 1600 hrs.)

WITNESSES

Federation of Indian Chambers of Commerce and Industry (FICCI)

1. Dr. Rajiv Kumar, Secretary General
2. Shri S. Madhavan, Co-Chairman, GST Task Force
3. Shri Sachin Menon, Co-Chairman, GST Task Force
4. Shri J.K. Batra, Advisor-Taxation

Confederation of Indian Industry (CII)

1. Shri Sunil K. Munjal, Past President CII, Chairman, CII Economic Policy and Jt. Managing Director, Hero Autocorp. Ltd.
2. Shri D.D. Goyal CGM-Finance, Maruti Udyog
3. Shri Rajiv Khandelwal, Head-Taxation, ICICI Bank

3. The Committee then heard the representatives of Federation of Indian Chambers of Commerce and Industry (FICCI) and Confederation of Indian Industry (CII) on the provisions of the 'The Constitution (One Hundred Fifteenth

Amendment) Bill, 2011' (GST). The major issues discussed broadly related to the GST Council, the Dispute Settlement Authority (DSA), exclusion of certain sectors like petroleum, alcohol, real estate from the purview of GST, issues regarding the positive effect on growth, taking onboard the North Eastern States, special category States and public policy of getting rid of regional imbalances under this particular regime were also discussed. Questions were also raised on the impact of introduction of GST on the creation of jobs and livelihoods in the country and on social sector. Members also enquired about GST and effect of exclusion or inclusion of particular products on Indian economy. Members also took into account the plight of special category States especially the North Eastern States and the issue of integration of market, effect on social sector, tax structure and frivolous disputes. The Chairman directed the witnesses to send written replies in response to the queries posed by the Members at the earliest.

The witnesses then withdrew.

Part III
(1600 hrs. to 1615 hrs.)

WITNESSES

Petroleum Federation of India (PETROFED)

1. Shri B.C. Tripathi, Chairman & Managing Director, GAIL (India) Ltd.
2. Shri S.K. Srivastava, Chairman & Managing Director, Oil India Ltd.
3. Shri A.K. Hazarika, Director (Onshore), ONGC

3. The Committee then heard the representatives of Petroleum Federation of India (PETROFED) on 'The Constitution (One Hundred Fifteenth Amendment) Bill, 2011'. The major issues discussed related to cascading effect of non-inclusion of petroleum products under the proposed amendment Bill. Moreover, they were also advised by the Committee to look into strengthening of awareness campaign regarding conservation of petroleum products for which they promised to look into. The Chairman directed the witnesses to send written replies in response to the queries posed by the Members at the earliest.

The witnesses then withdrew.

Part IV
(1620 hrs. to 1630 hrs.)

WITNESSES

International Spirits & Wines Association of India (ISWAI)

1. Shri I.P. Suresh Menon, Executive Director, UB Group
2. Shri S. Madhvan, Executive Director, PriceWaterhouse Coopers
3. Shri Ajit Jha, Director, SAB Miller, India

4. The Committee then heard the representatives of International Spirits & Wines Association of India (ISWAI). They submitted that the ISWAI has been pursuing with the States and presenting the GST for alcoholic beverages as a win-win situation for the States too. When asked by the Committee, the representatives of ISWAI promised to send in hard copies of relevant information and international experience regarding implementation of GST on this sector. The Committee advised the representatives of ISWAI that at this stage only the issues pertaining to Constitution Amendment Bill might be raised and other matters could be taken after the GST Council had been constituted.

A verbatim record of the proceeding was kept.

The witnesses then withdrew.

The Committee then adjourned.

MINUTES OF THE TWENTY FOURTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)

The Committee sat on Wednesday, the 27th June, 2012 from 1130 hrs to 1430 hrs.

PRESENT

Shri Yashwant Sinha - Chairman

MEMBERS

LOK SABHA

2. Shri Gurudas Dasgupta
3. Shri Chandrakant Khaire
4. Shri Bhartruhari Mahtab
5. Shri Anjan Kumar Yadav M.
6. Shri Prem Das Rai
7. Dr. Kavuru Sambasiva Rao
8. Shri Rayapati S. Rao
9. Shri Magunta Sreenivasulu Reddy
10. Shri G.M. Siddeswara
11. Shri Yashvir Singh

RAJYA SABHA

12. Shri Naresh Agrawal
13. Smt. Renuka Chowdhury
14. Shri Piyush Goyal
15. Dr. Mahendra Prasad
16. Shri Ravi Shankar Prasad
17. Dr. K.V.P. Ramachandra Rao

SECRETARIAT

1.	Shri A.K. Singh	-	Joint Secretary
2.	Shri R.K. Jain	-	Director
3.	Shri Ramkumar Suryanarayanan	-	Deputy Secretary
4.	Shri Kulmohan Singh Arora	-	Under Secretary

Part I
(1130 hrs. to 1330 hrs.)
WITNESSES

Indian Merchants' Association (IMA)

Shri Arvind Pradhan, DG, IMA

2. DG, Indian Merchants' Association (IMA) briefed the Committee on the provisions of 'The Constitution (One Hundred Fifteenth Amendment) Bill, 2011' (GST). Members sought clarifications from the witness on the issues pertaining the Bill, which inter-alia included subjects and issues like Articles 279(A), 279(5), 279(a)(8) which gives the functions of the GST Council, its composition, coverage of taxes on items like electricity, renewable energy sector, stamp duty on shares / contracts, toll taxes, entertainment tax etc. Other issues discussed included effect on income of local bodies, effect of GST on industrial development, economic growth, harmonisation and increase in tax and its effect on the economic scenario of the country. The Chairman directed the witnesses to send written replies in response to the queries posed by the Members at the earliest.

The witness then withdrew.

Part II
(1130 hrs. to 1330 hrs.)
WITNESSES

Film & Television Producers Guild of India

1. Shri Ramesh Sippy, President
2. Shri Mukesh Bhatt, Vice President
3. Shri Uday Singh, Member
4. Shri Shibasish Sarkar, Member
5. Shri Srinivas Shenoy, Member
6. Shri Kulmeet Makkar, CEO

3. The Committee then heard the views of Film & Television Producers Guild of India (FTPGI) on 'The Constitution (One Hundred Fifteenth Amendment) Bill, 2011' (GST). The major issues discussed broadly related to remaining taxation power of the States after GST (like entertainment tax) and its effect on the growth of the film industry. There were also discussion of films being taxed at a punitive rate similar to alcohol and tobacco. The other issues discussed included topic of investment of black money in film industry, the effect of inclusion of entertainment tax in GST on local bodies and how taxes will be transferred to the local bodies. The representatives of the Film & Television Producers Guild of India replied to the queries raised by the Members during the sitting.

The witnesses then withdrew.

Part III
(1130 hrs. to 1330 hrs.)
WITNESSES

All India Federation of Tax Practitioners (AIFTP)

1. Shri J.D. Nankani, Deputy National President
2. Shri Mukul Gupta, Chairman, central GST Committee, AIFTP
3. Shri Narendra Kumar Arora, Chairman, North Zone
4. Shri P.S. Sarin, Past Chairman, North Zone
5. Shri Sandeep Goel, Member National Executive

3. The Committee then heard the views of All India Federation of Tax Practitioners (AIFTP) on 'The Constitution (One Hundred Fifteenth Amendment) Bill, 2011' (GST). The came up with suggestions that under Article 279-B, in addition to dispute referred or complaints referred to Dispute Settlement Authority by State Government or Government of India, the dispute or complaint referred by any Industrial/Trade Association or Professional Association or Institutions or Organisations of national repute must also be added. They further suggested for appropriate definition of Goods and Services, inclusion of Petroleum and electricity

sectors under the proposed GST regime, prevention of artificial credit restrictions, no restriction over moratorium for large infrastructure projects etc. However, under due guidance and brainstorming, the representatives of AIFTP withdrew certain submissions made before the Committee. Moreover, they were directed by the Chairman to send a comprehensive written replies to the questions asked by the Chairman and Members. The representatives of AIFTP promised to comply and send the same at the earliest.

The witnesses then withdrew.

Part IV
(1130 hrs. to 1330 hrs.)
WITNESSES

Bhartiya Udyog Vyapar Mandal (BUVM)

1. Shri Babu Lal Gupta, Senior Vice President
2. Shri Vijay Prakash Jain, Secretary General
3. Shri Kishor C Mehta, General Secretary
4. Shri Hemant Gupta, Organising Secretary

4. The Committee then heard the representatives of Bhartiya Udyog Vyapar Mandal (BUVM) who came for advocating the cause of small and medium level traders. Primarily, they requested for a single and unified GST model. However, upon seeing their misinterpretation of certain clauses in the proposed amendment Bill and divergent views of the representatives over the implementation of GST, the Committee directed the concerned representative to send a comprehensive and unified text with proper suggestions, observations and answers to the questions raised by the Members of the Committee. The representatives of Bhartiya Udyog Vyapar Mandal (BUVM) promised to comply and send the same at the earliest.

A verbatim record of the proceeding was kept.

The witnesses then withdrew.

The Committee then adjourned.

MINUTES OF THE TWENTY FIFTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)

The Committee sat on Friday, the 6th July, 2012 from 1130 hrs to 1330 hrs.

PRESENT

Shri Yashwant Sinha - Chairman

MEMBERS

LOK SABHA

2. Shri Harishchandra Deoram Chavan
3. Shri Bhakta Charan Das
4. Shri Gurudas Dasgupta
5. Shri Nishikant Dubey
6. Shri Chandrakant Khaire
7. Shri Bhartruhari Mahtab
8. Shri Prem Das Rai
9. Dr. Kavuru Sambasiva Rao
10. Shri Rayapati S. Rao
11. Shri Yashvir Singh

RAJYA SABHA

12. Shri Naresh Agrawal
13. Smt. Renuka Chowdhury
14. Dr. Mahendra Prasad
15. Shri P. Rajeeve
16. Dr. K.V.P. Ramachandra Rao
17. Shri Yogendra P. Trivedi

SECRETARIAT

1.	Shri R.K. Jain	-	Director
2.	Shri Ramkumar Suryanarayanan	-	Deputy Secretary
3.	Shri Kulmohan Singh Arora	-	Under Secretary

WITNESSES

Government of Madhya Pradesh

1. Shri Raghavji, Finance Minister, Government of Madhya Pradesh
2. Shri A.P. Shrivastava, Principal Secretary, Commercial Tax Department
3. Shri Amit Rathore, Commissioner, Commercial Tax

2. At the outset, the Chairman welcomed the Hon'ble Finance Minister, Government of Madhya Pradesh and his colleagues to the sitting of the Committee. The Chairman then asked them to present their views on the Constitution (One Hundred Fifteenth Amendment) Bill, 2011 to the Committee. The representatives of Government of Madhya Pradesh in their presentation before the Committee strongly opposed the proposed GST model and advocated for an alternate model which is similar to present VAT regime but with more seamlessness. They put forth their argument in light of the fact that though VAT system being quite novel, their State is doing well with the system and generating adequate resources. Moreover, they raised certain apprehensions regarding Dispute Settlement Authority that it might turn into a super-legislature thereby eroding the basic structure of our Constitution, cooperative federalism and especially the fiscal autonomy of the States. However, the Committee enlightened them that the institutions similar to or even with lesser Constitutional mandate than Dispute Settlement Authority viz. Finance Commission, Planning Commission etc. are effectively functioning in our political set up. And if GST mechanism is not in the interest of the Country, the States have full opportunity to pull down the proposed Constitution Amendment Bill in their respective Assemblies. The representatives of the State of Madhya Pradesh further submitted that the proposed GST is nothing but VAT plus service tax and a better Information Technology platform holds the key for better and seamless tax structure. The Committee directed them to send their written replies at the earliest, which they promised to comply with.

A verbatim record of the proceeding was kept.

The witnesses then withdrew.

The Committee then adjourned.

MINUTES OF THE TWENTY SIXTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)

The Committee sat on Friday, the 13th July, 2012 from 1100 hrs to 1600 hrs.

PRESENT

Shri Yashwant Sinha – Chairman

MEMBERS

LOK SABHA

2. Shri Shivkumar Udasi
3. Shri Jayant Chaudhary
4. Shri Nishikant Dubey
5. Shri Chandrakant Khaire
6. Shri Bhartruhari Mahtab
7. Shri Prem Das Rai
8. Dr. Kavuru Sambasiva Rao
9. Shri Rayapati S. Rao
10. Shri Manicka Tagore
11. Shri R. Thamaraiselvan
12. Dr. M. Thambiduarai

RAJYA SABHA

13. Shri Naresh Agrawal
14. Shri Satish Chandra Misra
15. Dr. Mahendra Prasad
16. Shri Ravi Shankar Prasad
17. Shri P. Rajeeve
18. Dr. K.V.P. Ramachandra Rao

SECRETARIAT

1.	Shri A.K. Singh	-	Joint Secretary
2.	Shri R.K. Jain	-	Director
3.	Shri Ramkumar Suryanarayanan	-	Deputy Secretary
4.	Shri Kulmohan Singh Arora	-	Under Secretary

Part I
(1100 hrs. to 1230 hrs.)

WITNESSES

Indian Council For Research On International Economic Relations (ICRIER)

Dr. Parthasarathi Shome - Director & Chief Executive, ICRIER

2. Dr. Parthasarathi Shome, Director & Chief Executive, Indian Council For Research On International Economic Relations (ICRIER) briefed the Committee on the provisions of the 'Constitution (One Hundred Fifteenth Amendment) Bill, 2011' (GST). Members heard the views and sought clarifications from the witness on the issues pertaining the Bill, which inter-alia included issues like States relation with Centre, problems in raising sufficient funds for States, direct relationship of GST with GDP growth, effect on trade, relevance of appellate body, Revenue Neutral Rates (RNR), effects on common man and on federal system of the constitution. Other issues discussed included distinction between zero rating and exemption, effect on revenue base, the need for dual GST, time period for its (GST) implementation and taxation of inter-state transactions of Goods and services. The Chairman directed the witnesses to send written replies in response to the queries posed by the Members at the earliest.

The witness then withdrew.

Part II
(1230 hrs. to 1400 hrs.)

WITNESSES

1. Shri Vijay L. Kelkar, Chairman, National Stock Exchange of India Limited (NSE)
2. Shri Arbind Modi, Consultant, Planning Commission and
Ex-Chairman of the Task Force on GST (Set up by the 13th Finance Commission)
3. The Committee then heard the views of Dr. Vijay L. Kelkar, Chairman, National Stock Exchange (NSE) on 'the Constitution (One hundred fifteenth Amendment) Bill, 2011' (GST). Major issues discussed broadly related to bypassing of the State legislatures, mechanism in place to solve problems between two States on issues like

taxation, surcharge and collecting benefit for the common man, dual tax system, illegal transaction and tax evasion. Other issues discussed included concern of States on exclusion of petrol and diesel, co-operative federalism, role of GST in fiscal consolidation, impact of GST on GDP and inflation. Also, GST's effect on rural economy (especially agriculture) in a State was also raised. Dr. Vijay L. Kelkar replied to the queries raised by the Members during the sitting. The Chairman directed the witnesses to send written replies to the queries raised by the Members at the earliest. The Committee desired to hear the views of Shri Kelkar once again after they have received and read the written replies from him to which Shri Kelkar agreed.

The witnesses then withdrew.

**Part III
(1430 hrs. to 1600 hrs.)**

WITNESSES

Government of Odisha

1. Shri Prafulla Chandra Ghadai, Minister, Finance, Excise & Public Enterprises
2. Shri J.K. Mohapatra, Principal Secretary, Finance Department

Government of Tamil Nadu

Shri Sunil Paliwal, Secretary, Commercial Taxes Department

Government of Maharashtra

Shri Sudhir Srivastava, Principal Secretary (Finance), Finance Department

4. Welcoming the Hon'ble Minister from the Government of Odisha and other officials, Hon'ble Chairman then opened the floor for their submissions. The representatives of the Government of Odisha focused their deliberations on impact on the autonomy of States due to Dispute Settlement Authority, non subsumption of entry tax and exclusion of Coal from the proposed GST regime

and a range or band within which the States will have power to levy tax in case of any exigency.

5. Moreover, the representative of Government of Maharashtra advocated for more clarity in jurisdiction of Dispute Settlement Authority, calculation of revenue neutral rates, well defined automatic compensation mechanism., avoidance of dual administration for GST and requirement of massive computerization.

6. Furthermore, the representative of Government of Tamil Nadu appended the issues of exclusion of petroleum products and alcoholic beverages out of the proposed Bill, cascading effect of taxes, encroachment on the mandates of the State Governments by the GST Council, assigning power to levy tax on tobacco to the State Governments or excluding it as petroleum and alcoholic beverages, and impact assessment of GST on the revenue of State Government and the Central Government.

7. Further the Committee also enquired and discussed about the apprehensions of the representatives regarding the GST Council becoming the super-legislature body, plight of states having low tax base, the smaller and poorer States, inconsistency in stand of States over GST Council vis-à-vis Dispute Settlement Authority, trust deficit between the States and the Centre etc. The Committee directed them to send their written replies at the earliest which they promised to comply with.

A verbatim record of the proceeding was kept.

The witnesses then withdrew.

The Committee then adjourned.

MINUTES OF THE TWENTY SEVENTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)

The Committee sat on Friday, the 20th July, 2012 from 1500 hrs to 1715 hrs.

PRESENT

Shri Yashwant Sinha – **Chairman**

MEMBERS

LOK SABHA

2. Shri Shivkumar Udasi
3. Shri Jayant Chaudhary
4. Shri Bhakta Charan Das
5. Shri Gurudas Dasgupta
6. Shri Nishikant Dubey
7. Shri Bhartruhari Mahtab
8. Shri Anjan Kumar Yadav M.
9. Shri Prem Das Rai
10. Dr. Kavuru Sambasiva Rao
11. Shri Rayapati S. Rao
12. Shri G.M. Siddeswara
13. Shri Yashvir Singh
14. Shri R. Thamaraiselvan

RAJYA SABHA

15. Shri Naresh Agrawal
16. Smt. Renuka Chowdhury
17. Shri Piyush Goyal
18. Dr. Mahendra Prasad
19. Shri Ravi Shankar Prasad
20. Shri P. Rajeeve
21. Dr. K.V.P. Ramachandra Rao

SECRETARIAT

1. Shri A.K. Singh	-	Joint Secretary
2. Shri R.K. Jain	-	Director
3. Shri Ramkumar Suryanarayanan	-	Deputy Secretary
4. Shri Kulmohan Singh Arora	-	Under Secretary

WITNESSES

Government of Gujarat

1. Shri Saurabh Patel, Minister of State for Finance, Government of Gujarat
2. Shri M.M. Srivastava, Additional Chief Secretary
3. Ms. S. Aparna, Secretary (Economic Affairs)

2. At the outset, the Hon'ble Chairman, welcomed the Hon'ble Minister of State for Finance, Government of Gujarat and his colleagues to the sitting of the Committee. The Chairman then requested them to present their views on the Constitution (One hundred fifteenth Amendment) Bill, 2011' (GST). Thereafter, Shri Saurabh Patel, MOS Finance, Government of Gujarat, briefed the Committee on the provisions of the 'Constitution (One Hundred and Fifteenth Amendment) Bill, 2011' (GST). The representatives of Government of Gujarat opposed the proposed GST model and advocated for an alternate to GST model to achieve the major objectives of reforms in indirect taxes in the Country. Members heard the views and sought clarifications from the witnesses on issues pertaining to the Bill, which included issues like effect of GST on GDP especially on agriculture, farming community, employment generation and balance of payment. Questions of Cooperative Fiscal federalism, increase in threshold limit for MSME, effect on consumers especially farmers and people below poverty line (BPL), meaning of the word "consensus" with respect to the GST Council, administrative difficulties regarding CGST and SGST operability were also discussed. The Chairman directed the witnesses to send written replies in response to the queries posed by the Members at the earliest.

A verbatim record of the proceeding was kept.

The witnesses then withdrew.

The Committee then adjourned.

MINUTES OF THE TWENTY EIGHTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)

The Committee sat on Friday, the 27th July, 2012 from 1100 hrs to 1620 hrs.

PRESENT

Shri Yashwant Sinha – Chairman

MEMBERS

LOK SABHA

2. Shri Shivkumar Udasi
3. Shri Jayant Chaudhary
4. Shri Bhakta Charan Das
5. Shri Gurudas Dasgupta
6. Shri Nishikant Dubey
7. Shri Bhartruhari Mahtab
8. Dr. Kavuru Sambasiva Rao.
9. Shri Rayapati S. Rao
10. Shri Sarvey Sathyanarayana
11. Shri Yashvir Singh
12. Shri R. Thamaraiselvan

RAJYA SABHA

13. Shri Naresh Agrawal
14. Smt. Renuka Chowdhury
15. Shri Piyush Goyal
16. Dr. Mahendra Prasad
17. Shri Ravi Shankar Prasad
18. Dr. K.V.P. Ramachandra Rao
19. Shri Y.P. Trivedi

SECRETARIAT

1. Shri A.K. Singh	-	Joint Secretary
2. Shri R.K. Jain	-	Director
3. Shri Ramkumar Suryanarayanan	-	Deputy Secretary
4. Smt. Reena Gopalakrishnan	-	Deputy Secretary
5. Shri Kulmohan Singh Arora	-	Under Secretary

Part I (1100 hrs. to 1230 hrs.)

WITNESSES

1. Shri Vijay L. Kelkar, Chairman, National Stock Exchange of India Limited (NSE)
2. Shri Arbind Modi, Consultant, Planning Commission and
Ex-Chairman of the Task Force on GST (Set up by the 13th Finance Commission)

2. The Hon'ble Chairman welcomed and thanked Dr. Vijay L. Kelkar and Shri Arbind Modi for once again presenting themselves before the Committee. Giving cue to the representatives, the Committee streamlined certain crucial topics for their deliberations, viz. Centre-State fiscal relationship, fiscal autonomy of States, fiscal federalism, voting rights in the GST Council and flexibility in taxation etc. The Committee also invited views from them on alternative model of GST as suggested by the Government of Gujarat and Madhya Pradesh.
3. Apart from the above-mentioned issues the Committee was briefed and discussed issues regarding harmonizing impact of GST over Indian economy and coming up of a common market, impact of GST Council on legislative process, impact of proposed GST regime on role of Finance Commission, international experiences with respect to GST, role and need of sufficient Information Technology mechanism for effective implementation of GST, inclusion of various sectors such as, petroleum, real estate, electricity, railways and telecommunication etc. under proposed GST regime, abolition of octroi, rural exemptions in GST, crony capitalism etc.
4. Moreover, issues such as impact of GST on prices, agriculture, common man, international trade, MSMEs and fiscal consolidation were also discussed elaborately.

The witnesses then withdrew.

Part II
(1230 hrs. to 1620 hrs.)

5	XX	XX	XX	XX
	XX	XX	XX	XX

A verbatim record of the proceedings was kept.

The witnesses then withdrew.

The Committee then adjourned.

MINUTES OF THE NINTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2012-13)

The Committee sat on Monday, the 21th January, 2013 from 1130 hrs to 1230 hrs.

PRESENT

Shri Yashwant Sinha – Chairman

MEMBERS

LOK SABHA

2. Dr. Baliram
3. Shri Nishikant Dubey
4. Shri Bhartruhari Mahtab
5. Dr. Chinta Mohan
6. Shri Sanjay Brijkishorlal Nirupam
7. Shri Prem Das Rai
8. Shri S.S. Ramasubbu
9. Shri Adv. A. Sampath
10. Shri Thakur Anurag Singh
11. Shri Shivkumar Udasi

RAJYA SABHA

12. Shri Naresh Agrawal
13. Smt. Renuka Chowdhury
14. Shri Piyush Goyal
15. Shri Satish Chandra Misra
16. Shri P. Rajeeve
17. Dr. Yogendra P. Trivedi

SECRETARIAT

1. Shri P.C. Tripathy	–	Director
2. Shri Ramkumar Suryanarayanan	–	Additional Director
3. Shri Sanjay Sethi	–	Under Secretary

2. At the outset, Hon'ble Chairman welcomed the Members to the sitting of the Committee. Thereafter, he briefed the Members on the work done so far on 'The Constitution (One Hundred and Fifteenth Amendment) Bill, 2011' (GST) and the latest communication received from the Ministry of Finance in this regard, wherein they have stated that they will report back to the Committee about the findings of the two Committees set up by them and the views of the Ministry thereon. Members expressed the view that draft Report may be attempted on the Bill based on the deliberations made thus far. In the meantime, the Ministry may be asked to furnish

the latest position at their end at the earliest so that the Report of the Committee is not held up on this count.

The Committee then adjourned.

MINUTES OF THE NINETEENTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2012-13)

The Committee sat on Friday, the 28th June, 2013 from 1100 hrs to 1300 hrs.

PRESENT

Shri Yashwant Sinha – Chairman

LOK SABHA

2. Dr. Baliram
3. Shri Nishikant Dubey
4. Shri Gurudas Dasgupta
5. Shri Deepender Singh Hooda
6. Shri Chandrakant Khaire
7. Shri Sanjay Brijkishorlal Nirupam
8. Shri Prem Das Rai
9. Shri Adv. A. Sampath
10. Dr. M. Thambidurai
11. Shri Shivkumar Udasi
12. Shri Dharmendra Yadav

RAJYA SABHA

13. Shri Naresh Agrawal
14. Shri Rajeev Chandrasekhar
15. Shri Piyush Goyal
16. Dr. Mahendra Prasad
17. Shri Ravi Shankar Prasad
18. Shri P. Rajeeve
19. Shri Praveen Rashtrapal

SECRETARIAT

1. Shri Ramkumar Suryanarayanan – Additional Director
2. Shri Kulmohan Singh Arora – Under Secretary

2. The Committee took up draft report on 'the Constitution (One Hundred and Fifteenth) Amendment Bill, 2011' relating to GST for consideration and adoption. After long deliberations, the Members suggested some changes in the draft report. The Chairman then directed that the changes as suggested by the Members may be incorporated in the body of the draft report and the same may be circulated to the Members. The Committee then decided to consider and adopt the draft Report at their next sitting scheduled to be held on 19 July, 2013.

The Committee then adjourned.

MINUTES OF THE TWENTIETH SITTING OF THE STANDING COMMITTEE ON FINANCE (2012-13)

The Committee sat on Friday, the 19th July, 2013 from 1100 hrs to 1330 hrs.

PRESENT

Shri Yashwant Sinha – Chairman

LOK SABHA

2. Shri Nishikant Dubey
3. Shri Gurudas Dasgupta
4. Shri Deepender Singh Hooda
5. Shri Chandrakant Khaire
6. Shri Bhartruhari Mahtab
7. Shri Sanjay Brijkishorlal Nirupam
8. Shri S.S. Ramasubbu
9. Shri Adv. A. Sampath
10. Dr. M. Thambidurai
11. Shri Shivkumar Udasi

RAJYA SABHA

12. Shri Naresh Agrawal
13. Smt. Renuka Chowdhury
14. Shri Piyush Goyal
15. Shri Satish Chandra Misra
16. Dr. Mahendra Prasad
17. Shri Ravi Shankar Prasad
18. Shri P. Rajeeve

SECRETARIAT

1. Shri A.K. Singh	–	Joint Secretary
2. Shri Ramkumar Suryanarayanan	–	Additional Director
3. Shri Sanjay Sethi	–	Deputy Secretary

2. At the outset, the Chairman informed the members that the changes suggested by them in the draft report on 'the Constitution (One Hundred and Fifteenth) Amendment Bill, 2011' relating to GST at the sitting of the Committee held on 28 June, 2013 had been suitably incorporated. The Committee then considered the

draft report and adopted the same without any changes. The Committee authorised the Chairman to present the same to Hon'ble Speaker/Parliament.

3.	XX	XX	XX	XX
	XX	XX	XX	XX

WITNESS

Shri Vinod Dhall, Consultant & Former Secretary, Ministry of Corporate Affairs

4.	XX	XX	XX	XX
	XX	XX	XX	XX

A verbatim record of the proceedings was kept.

The witness then withdrew.

The Committee then adjourned.

TAXATION OF SERVICES BASED ON A NEGATIVE LIST OF SERVICES

CONCEPT PAPER FOR PUBLIC DEBATE

1.0 Background:

1.1 In the Parliament, while presenting the Union Budget 2011, the Finance Minister proposed that:

“Many experts have argued that it will be desirable to tax services based on a small negative list, so that many untapped sectors are brought into the tax net. Such an approach will be very conducive for a nationwide GST. I propose to initiate an informed public debate on the subject to help us finalize the approach to GST.”

1.2 Pursuant to the announcement made by the Honourable Finance Minister, it has become imperative to initiate an informed public debate on widening the tax base by introducing a negative list of services

2.0 What is a negative list?

2.1 To a lay person, not initiated into the rigors of tax policy, a negative list of services implies two things: firstly, a list of services which will not be subject to service tax; secondly, other than the services mentioned in the negative list, all other services will become taxable which fall within the definition of the ‘supply of services’. This can be contrasted from the present method of taxation that has detailed description for each taxable service and all other unspecified services are not liable to tax. The latter method of taxation is also referred to as taxation by way of a positive list.

2.2 The selective taxation of services by way of incremental additions over the years served well in the past in acclimatizing both the tax payers and tax administrators to the new levy. However, with considerable expansion of the list, the administrative challenge has multiplied manifold. Service tax has now gained considerable maturity and many practitioners of the subject believe that incremental approach to taxation is not suitable for providing a stable system for taxation of services that is at the threshold of getting subsumed into a comprehensive GST.

3.0 Contours of public debate:

3.1 Broadly the following questions can arise in a public debate on introduction of a negative list based comprehensive approach to taxation of services. Feedback based on

these questions from all stakeholders can further enlighten Government's approach to this important tax reform initiative:

- Negative vs positive list: should the country adopt a negative list? What will be the proper timing: at the time of GST or even earlier?
- How to define 'service', for the purpose of taxation?
- What are the services which should be placed in the negative list?
- How comprehensive the coverage should be while drawing the negative list? What should therefore be the policy on taxation of important sectors e.g. education, health, public services, charitable and NGOs, infrastructure etc.?
- What are the likely revenue implications?

4.0 Negative vs Positive list

4.1 The issue that which of the two lists is more desirable can be argued both ways with each having its own pros and cons. Positive list has the advantage of definitiveness, which is an essential pre-requisite for a good taxation law. However this very advantage starts getting eroded as the number of services increase. The possibilities of overlaps amongst definitions lead to innumerable administrative issues resulting in litigation and higher compliance costs. Some of the definitions could be so wide that they lead to unintended taxation requiring either clarifications or exemptions.

4.2 On the other hand the fact that many services are outside the tax net invariably leads to unintended exemptions, thus keeping the tax base narrow with all the accompanying consequences. Such unintended exemptions at intermediate stages lead to breakage of the input tax chain adding costs for the tax-payers and end-users. This will be clear from the following illustration:

Situation 1: No exemption					
	Taxable Inputs	Output	Input tax credit	Output tax@ 10%	Net liability
Origin Suppliers	0	100	0	10	10
Service provider I	100	200	10	20	10
Service provider II	200	400	20	40	20
Total					40

Situation 2: With exemption					
	Taxable Inputs	Output	Input tax credit	Output tax@ 10%	Net liability
Origin Suppliers	0	100	0	10	10
Service provider I	100	200	10	exempted	0
Service provider II	200	400	0	40	40
Total					50

4.3 It is evident from the illustration that when the Service Provider I is kept outside the tax chain the effective tax on the total supply goes up from 40 to 50 as the taxes paid at the previous stages are not available as tax credit at the subsequent stage.

4.4 As the untaxed supplies are treated exempt for the purpose of input tax credit rules, taxes paid on the inputs used in their supplies are required to be reversed under the prescribed rules. This further adds complexities both for the tax-payers and the administrators.

4.5 Such exclusions also lead to distortion of economic neutrality across similar or substitute supplies e.g. road vs. rail transportation or discourage outsourcing by incentivizing self-supplies, and are thus not conducive to making the optimal choices in the economy. Moreover the one-time taxation of the service sector obviates the need for year-after-year incremental changes.

4.6 On the other hand there are significant advantages of positive list in so far it has already attained a certain level of awareness and stability in administration. The categorizations of services is also useful for a variety of purposes e.g. import and export rules, Cenvat Rules and Point of Taxation Rules or where ever any differential treatment is required to be given to any service as also for statistical purposes.

4.7 The proper timing for the launch of negative list can also be argued either way. GST will give the advantage of a wider constitutional mandate for comprehensive taxation of goods and services. Undoubtedly that will be far more conducive for the launch of taxation based on a negative list. On the other hand there are advantages in moving towards negative list at an earlier time in order to gain useful experience in its implementation and minimize the impact of the mammoth changes that GST may usher.

5.0 Definition of Service:

5.1 As the new concept envisages taxation of the whole, unless otherwise something is excluded, it is necessary to capture that universe such that it does not infringe upon either the powers to tax of another legislature in a specific area or taxes such areas as are subjected to like taxes as goods. To initiate a public debate and obtain feedback, a definition of 'service' is proposed as follows:

5.2 A "service" means anything which does not constitute supply of goods, money or immovable property-

and includes-

- A. *right to use an immovable property;*
- B. *construction of a complex, building, civil structure or a part thereof, including a complex or building intended for sale to a buyer, wholly or partly, except where the entire consideration is received after issuance of certificate of completion by a competent authority;*
- C. *temporary transfer or permitting the use or enjoyment of any intellectual property right;*
- D. *obligation to refrain from an act, or to tolerate an act or a situation, or to do an act;*
- E. *service in relation to lease or hire of goods; and*
- F. *right to enter any premises-*

but excludes a supply-

- A. *by an employee to an employer in the course of or in relation to the employment of the person;*
- B. *by a constitutional authority under the Indian Constitution or a member of an Indian legislature or a local self-government in that capacity;*
- C. *that amounts to manufacture of excisable goods or is chargeable as part of the value of goods to a duty in terms of the provisions of Central Excise Act, 1944;*

5.3 In the attempted definition, a supply of service is defined as 'anything which does not constitute supply of goods, money or immovable property'. The key words are goods, money and immovable property. Tax will be imposed on supply of services. A supply is a transaction and transaction involves two persons. Transaction involving goods, money and immovable property is excluded from the meaning of supply of service. Inclusions and exclusions support and clarify the above definition of supply of services.

6.0 Exclusions:

6.1 Supplies of goods, money and immovable property are the principal exclusions, in the proposed scheme. The expression ‘goods’ as defined in *clause (7) of section 2 of the Sale of Goods Act, 1930*, can continue to be part of the service tax framework as at present. According to the Sale of Goods Act, 1930:

“Goods” means every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass, and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale.

6.2 It is important to mention that supplies which are deemed to be sale of goods in terms of Article 366 (29A) of the Constitution in the case of specified contracts will stand excluded as goods. These relate to goods portion of the supplies in a works contract, contracts of hire purchase and catering. The remaining portion of the supply in the specified composite contracts shall be considered as supply of service. Under the proposed negative list approach, where supplies of services are bundled alongwith supply of goods in situations other than those stated in Article 366 of the constitution, nature of the transaction will have to be judged by what the Honorable Supreme Court has called the “dominant nature test” in the case of *Bharat Sanchar Nigam Ltd. Vs UOI [2006(2) STR 161 (SC) para 43]*. The test requires: “did the parties have in mind or intend separate rights arising out of the sale of goods. If there was no such intention there is no sale (of goods) even if the contract could be disintegrated.”

6.3 The expression “money” is meant to capture transactions where Indian legal tender is exchanged from one form to another.

6.4 The expression ‘Immovable property’ as defined in clause 26 of section 3 of the General Clauses Act, 1897 can be borrowed to support the proposed scheme:

“Immovable property” shall include land, benefits arising out of land and things attached to the earth, or permanently fastened to anything attached to the earth.”

6.5 In addition to the above, certain exclusions are provided to clarify the concept of ‘supply of service’. For instance, it is provided in the definition of ‘supply of service’ that, sale of immovable property in fully complete form i.e. after issuance of the completion certificate, will not be counted as supply of service. However, all agreements to sell a complex, building, civil structure or a part thereof to intending buyers, wholly or partly, where a part of the consideration is received before the completion certificate is

obtained shall constitute service, as is the case even at present. Similarly, it is proposed that a transaction involving right to use immovable property e.g. renting shall constitute a supply of service.

6.6 A transaction takes place between two persons. Therefore self-supplies will not constitute a service. The word “*Person*” shall include any company or association or body of individuals, whether incorporated or not (section 2(42) of the General Clauses Act, 1897) and hence services by or to unincorporated associations and joint ventures will constitute a valid transaction.

6.7 Supply of services by an employee to an employer in the course of or in relation to the employment of the person is an important exclusion. However any service rendered by an employee in another capacity will constitute a supply of service. Similar position is proposed in respect of constitutional functionaries, some of whom may not be strictly in the position of an employee, as also members of Union and State legislatures and local self-government.

6.8 Any supply that amounts to manufacture or is includible in the value of the goods under the Central Excise Act is also kept outside the purview of the definition of service as this is liable to Central Excise duty as goods.

7.0 Inclusions:

7.1 A number of specific entries have been specified in the inclusive portion to provide greater clarity to the new approach to taxation of services. Right to use immovable property falls within the domain of services. Also temporary transfer or permitting the use or enjoyment of any intellectual property will constitute supply of service. The obligation to refrain from an act, or to tolerate an act or a situation, or to do an act will also constitute service. Delivery of goods by way of hire purchase or installments is declared by the Constitution to be deemed sale of goods. But services provided in relation to lease or hire of goods have been held to be a service [Association of Leasing & Financial Services Companies vs UOI (2010-TIOL-87-SC-ST-LB)]. Right to enter any premises e.g. museums; art galleries or botanical gardens will also constitute service.

7.2 To bring certainty and clarity in certain areas where goods and services aspects may overlap, it is proposed to empower the Central Government to specify certain supplies as supply of service or otherwise, whether in full or part. Services so declared will be taxed as a supply of service notwithstanding anything to the contrary. This is not meant to be unbridled power and shall operate within the existing legal restraints on the subject.

7.3 In the light of the discussions in the previous paragraph, supplies of electricity, power, heat, refrigeration and ventilation may be specified as not comprising supply of services. Sale of SIM card with talk time [Idea Mobile Communication Ltd Vs CCEC, Cochin (2011-TIOL-71-SC-ST)], downloadable on-site software and similar supplies through the internet may be specified as services. Service element involved in the supplies in respect of works contracts, restaurants, outdoor catering may be subject to tax as services at the prescribed rates, so that goods portion falling within the taxation powers of state governments, will stand excluded.

8.0 Negative list of services:

8.1 An indicative negative list is given in the Annexure. This is only a proposition to initiate a discussion. While drawing the indicative negative list some of the considerations found relevant are as follows:

- (i) Administrative considerations: taxation of Government, difficult to tax sectors e.g. margin-based financial services.
- (ii) Under contractual obligations: Specified international bodies and diplomatic missions
- (iii) Welfare considerations: welfare of vulnerable sections of society, essential education, public health; public transport, services by non-profit entities, religious services, promotion of art, culture and sports.
- (iv) Economic considerations: transport of export goods, services meant for agriculture, animal husbandry and infrastructure development.
- (v) Explicit activities in the nature of services, which are within the taxing powers of States: betting and lotteries, tolls.

8.2 Most of the services provided by government are provided without a specific charge to the recipient and thus shall not be liable to tax. However the other supplies could be classified as follows:

- i. Where services are provided at market rates and compete with private entities;
- ii. Where services are provided at concessional rates but compete with private entities;
- iii. Where services are provided exclusively or predominantly by government.

8.3 When Government is engaged in providing services in purely commercial areas or where similar services are provided by private enterprise, it is necessary to provide equitable tax treatment. When government supplies compete with the supplies made by

private enterprise, if tax is levied only on supplies made by private enterprise, it amounts to discrimination and economic distortions will be inevitable.

8.4 Where services are provided by Government or its extended agencies more or less exclusively many experts argue that such services should also be subjected to tax. The counter argument is that such taxation would lead to increase in administrative work load without commensurate increase in net revenue when the same amount can be collected by increased user charges. With increasing privatization and outsourcing the dividing line between government functions for a fee or charge and somewhat similar functions elsewhere is diminishing. For example the driving licenses in many states are now issued by private bodies though the approval continues to be given by government agencies. It is thus proposed to confine negative list only to services provided in select few areas and the matter is left open at this stage for public debate as to what precise exclusions should be made.

8.5 Even though the definition of goods includes stocks and shares, the sale and purchase of securities and debts on a principal-to-principal basis is also separately excluded by a specific entry in the proposed negative list. This may require discussion whether mere exclusion at the definition stage of stocks and shares will capture all the various instruments that are sold and purchased on principal-to-principal basis in financial markets. However, services in relation to sale and purchase of securities e.g. stock broking will come under the tax net.

8.6 Renting of personal dwellings for the residential use of any person is commonly included in negative list in most parts of the world. Due to wide divergence in income levels in India a case is made for bringing opulent living within the tax net. A reasonably high threshold will ensure that the effect is felt largely by the very well to do sections of the society.

8.7 On the subject of taxation of health services, diverse views have been expressed in the recent past. While appreciating that health services are absolutely essential for all persons, some tax policy experts do argue that only the basic or public health services should be kept in the negative list. All health and medical services other than these health services, particularly the high-end medical services provided by private enterprise, should be brought within the tax fold. Among other arguments they justify the same on grounds of the sanctity of the tax-chain so that taxes paid at the previous stage are allowed to be set off at the subsequent stages of consumption (in particular for the health insurance sector) and the need to use the resources so made available for upgrading the facilities for the poor in the public health system. Another model of taxation could be to exempt health care up to a decent threshold so as to confine it to large entities that are commonly accessed by persons with insurance cover or other

affluent sections of society. Services provided by such establishments to needy and economically weaker sections could be exempted as per agreed criteria. Public hospitals could be kept outside the levy as they largely address the needs of the weaker sections. The issue thus requires a well-rounded debate on all the various aspects. For the moment two options are indicated but there can be many varied variants for the treatment of this sector.

8.8 Similar arguments are also made in respect of certain streams of education. Services provided by international schools and expenses recovered by certain educational institutions over and above the prescribed charges, including capitation fees or donations are areas that are often cited for the purpose of levy of service tax.

8.9 It is acknowledged that some of the areas specified in the proposed negative list require greater elaboration. However the same has not been attempted at this stage in order to obtain diverse and unbiased views during the course of the public debate.

9. Revenue Impact

9.1 It is well known that nearly 57% of India GDP comes from services. After including construction, the contribution from services will come to about 63%. At current prices the contribution from services during 2010-11 comes to about Rs 50 lakh crore.

9.2 The national income statistics do not capture the break-up of the service sector in the manner it is being taxed or sought to be taxed. However some broad indications are available of the contribution of services from certain sectors. Based on these indications contribution from services that are proposed to be kept in the negative list e.g. trading of goods, transportation of passengers, education and health sectors as also portions of construction, real estate and financial sectors can be estimated. In addition to exclusions by way of negative list, export of services valued at about nearly US\$ 130 billion at present will also remain exempt. The import of services meant for direct consumptions by individuals are at present not largely subjected to tax. Remaining services from abroad may not make any major net contribution to tax being available for credit set off.

9.3 On a rough estimate nearly 40% of the total services will come into the tax net as a result of the proposed negative list. However a large part of the informal sector would also remain outside the tax net due to the threshold exemption. This would leave only about 60% of the sector not covered by negative list actually available for tax payment. Thus the potential for effective taxation of services may be confined to about 20-25% of the service sector contribution. This is still a sizable number and will add significant numbers to the revenue though may not sound astounding as some sections believe it to be.

10.0 Conclusion:

10.1 For the purpose of operationalizing the proposed negative list, certain changes will be necessary in the current service tax framework, importantly in the rules relating to import and export of services and to a lesser extent Cenvat Credit Rules, 2004, Service Tax Rules, 1994 and Point of Taxation Rules, 2011.

10.2 Exemptions which are operational within the current positive list regime have not been discussed in this paper. It is possible that some of these may be retained by the Government of India in public interest and some others may be withdrawn as not necessary, being covered by the negative list. In this connection, remarks column of the annexure may be perused.

(This Concept Paper is placed in the public domain for the widest possible consultation, extensive debate and to seek views and feedback of all stakeholders. The Paper has been prepared by a team of officers with inputs from CII, FICCI, ASSOCHAM and PHDCI. Views expressed here do not reflect the position of the Government of India in any manner. Any comments, suggestions or feedback may be given by September 30, 2011 to Shri Shobhit Jain, OSD (TRU) at shobhit.jain@nic.in, Tel: 011-23095590; fax: 011-23093037)

Possible Negative List of Services

Sector	S. No.	Negative List	Remarks
1. By specified persons	1.	Notified services provided by: a. Government* and Judiciary; b. RBI; and c. government regulatory bodies	List of these services or the principle for exclusions will be worked out based on the outcome of the debate
	2.	Services provided by individuals to Government in relation to their representation on any council, commission or similar body set up by the Government	
	3.	Service by UN, international bodies, diplomatic missions under diplomatic and consular arrangements as per laid down conditions (details to be specified)	Services provided to such entities to remain exempt as at present.
2. Social welfare and public utilities	4.	Services provided by organizations registered as non-profit entities in matters relating to public and social welfare activities-excluding education and health (covered separately)-including charitable fund-raising events, sponsorships to charitable events and voluntary donations to charity	Public and social welfare activities will be suitably defined and may be restricted to specified fields only
	5.	Funeral, burial, crematorium and mortuary services	
3. Agriculture & animal husbandry	6.	Services directly used for growing, cultivation, harvesting of the agricultural produce, horticulture, animal husbandry, forestry, dairy, poultry farming and pisciculture (including renting of vacant land exclusively or predominantly for any such purpose)	Certain support services in relation to agriculture and allied activities may be separately exempted
4. Financial Sector	7.	Sale, purchase or acquisition of securities and debts on principal-to-principal basis	Acquisition of shares in lieu of services will be liable to tax
	8.	Interest	
	9.	Dividend on investments	
	10.	Inter-bank sale and purchase of foreign currency	

5. Transport	11	Transport of passengers by: a) public transport buses on a point-to-point basis (except tourist buses) and stage-carriage basis; b) public transport in ship or vessel of less than 15 net tonnage on a point-to-point basis; d) by metered taxis or three-wheeler auto rickshaw plying within the precincts of a city	
	12	Transport of goods to a destination outside India by any means of transport	
	13	Supply of goods carriage to a person engaged in the business of transportation of goods	
6. Construction & Real Estate	14	Construction, works-contract, repair, alteration, renovation or restoration of: a) roads, airports, railways, transport terminals, bridges, tunnels, dams, canals, irrigation and flood control waterworks including watershed development and water-bodies, water treatment plants and water supply pipelines; b) buildings owned by Government, other than meant predominantly for industrial or commercial use, including government hospitals and educational institutions c) residential building comprising of a single dwelling unit; d) homeless shelter, orphanage, old-age home, rehabilitation & de-addiction centre, child day-care home or place of worship	
	15	Renting of personal dwelling for residential use of a person below a threshold (to be finalized after debate) and when used otherwise as a hotel, inn, guest house, club or campsite or similar accommodation	
7. Education	16	Pre-school, school and recognized education** and vocational training recognized by NCVT except as capitation fee, donations or similar charges in relation to admission	

8. Health	17	Option 1: Services provided by a clinical establishment with a turnover below Rs 4 crore in the previous year Option 2: Hospital, medical care, diagnostic, para-medical services except in relation to preventive health check-up within the precincts of a clinical establishment, cosmetic or plastic surgery	Services to specified sections and by public hospitals may be exempted under option 1.
9. Others	18	Copyright services of original literary, dramatic, musical and artistic works.	
	19	Services provided by independent journalists, PTI & UNI for providing news	
	20	Services provided by sportspersons, as a player, coach or referee/umpire and performing artists in that capacity (excluding as brand ambassadors)	
	21	Religious services provided by any person.	
	22	Services provided by a political party recognized by Election Commission of India	
	23	Services provided by a trade union to its members	
	24	Representational services provided by an advocate to individuals	
	25	National or international prize/award in recognition of achievement in the field of art, literature, science, sport, economics or public life	
	26	Tolls except services in relation to collection of tolls	
	27	Betting and gambling except services in relation to promoting, marketing or organizing games of chance, including lottery services	

***Government** means the Union, State and local self government but shall not include any entity established under the Companies Act 1956 or any other law for the time being in force.

****Recognized education** means education leading to the award of a certificate or degree recognized by a body established by an Indian law.

Revised Concept Paper on Taxation of Services based on Negative List

November, 2011 • CBEC; Ministry of Finance

1.0 Background

1.1 A Concept Paper on the “Taxation of Services Based on a Negative List” was circulated on August 31, 2011 to seek feedback from all stakeholders. Many chambers, service providers’ associations, professional institutes, business entities and individuals have provided valuable inputs.

1.2 The feedback received indicates an overwhelming support for the taxation of services based on a Negative List. It has been mentioned that a long positive list is neither conducive from the point of tax administration nor tax compliance and adds to legal disputes.

1.3 As to the timing for the introduction of the Negative List, the opinion is divided. While some feel that it should be introduced at the time of GST, with a wider Constitutional mandate, there are others who feel that the introduction of Negative List should be done independently of the GST. In fact, it has been added that such introduction at an earlier stage will pave the way for the smooth transition to the GST, and significantly ease the challenges arising out of implementing the GST. It has been further stated that the issues relating to some transactions being considered services by the Central Government and goods or luxury or entertainment by some of the State Governments are independent of the issue whether the taxation is based on positive or negative list.

1.4 Many suggestions have been made on the contents of the negative list also. This revised Concept Paper has been drafted to consider all the relevant issues that may arise if the Negative List is to be introduced either under the existing regime of taxation or at the time of GST.

2. Definition of Service and Taxability

2.1 The earlier Paper had given the definition of service to “mean anything which does not constitute supply of goods, money or immovable property” A number of specific inclusions or exclusions were further elaborated. Suggestions have been made that the “service” should be confined to economic transactions or transactions

for consideration. These suggestions have arisen primarily because the provisions relating to charging section were not indicated in the earlier Paper. Taking note of all the various considerations, it is felt that the definition of “service” need not be revised in any manner and retained.

2.2 However the essence of the suggestions can be captured in the charging section somewhat as follows:

“There shall be levied a tax (hereinafter referred to as service tax) at the rate of ... per cent of the value of services provided or to be provided by a taxable person to another person and collected in such manner as may be prescribed.”

2.3 The above charging section is illustrative in terms of the present scheme of taxation and the same will naturally look quite different if the negative list is introduced alongwith the GST, capturing all the various activities that will be brought within the purview of the GST.

2.4 Taxable person may be defined as: “any person who independently carries out any economic activity, whether or not for a pecuniary profit”.

2.5 Thus the impact of all the proposed charging section will be to confine taxation to transactions in services carried out with another person by a person engaged in an economic activity on his own account.

2.6 A taxable person will not include wage earners as employees or others under a contract to their employers while acting in that capacity as they do not carry out economic activities independently but only on behalf of the organization they work for. This will also exclude members of legislatures likewise, which were covered by a specific exclusion in the previous Concept Paper. It is further clarified that this will apply only in so far as employees are bound to an employer by a contract of employment or by any other legal arrangement creating that relationship. It will in no case stretch to services rendered beyond the demand of the contractual arrangement. Thus an employee agreeing to serve after normal office hours against additional remuneration in terms of another arrangement beyond the terms of employment will not be construed as working in the said contractual relationship e.g. a teacher taking private tuition classes while the additional charges may be paid by the school from the amounts so collected from the students.

2.7 Economic activities are such activities as are carried out for consideration, whether or not the consideration is adequate or provided by the recipient of the service, or leads to profit at the end of a period. The taxable activities will thus exclude transactions carried out free of charge or gratis, without any direct or indirect commercial advantage, or as recreation or hobby. Statutory fines and penalties will also not constitute “economic activities”. However, commercial demurrages, by whatever name called, for extended use of a service will be taxable. Moreover the presence of profit motive is not necessary while carrying out economic activity. Thus the activities of political parties, religious bodies, in so far as they carry out religious activities, decorations and awards for excellence and not as reward in lieu of recognition for services rendered, will fall outside the charging section.

2.8 It is further clarified that by virtue of Article 366 of the constitution certain supplies are deemed to be supply of goods. They will thus be excluded from the definition of “service” but only to the extent of the value of goods.

2.9 As stated in the previous Paper, having regard to its characteristics and with a view to remove any ambiguity, the Central Government shall have powers to declare an activity as a provision of service or otherwise and such activity, notwithstanding anything to the contrary, be considered as a provision of service. The inclusions and exclusions given under the definition of service in the earlier Concept Paper can be clarified under this provision and need not form a part of the main definition.

3.0 Negative List of Services

3.1 The revised Negative List of services is given in the Annexure.

3.2 A number of deletions have been made from the previous Paper and are as follows:

1. Services provided directly in relation to agriculture, horticulture and animal husbandry: These services are largely provided by the small scale sector below the threshold. The words “directly in relation to” are capable of very wide interpretation and thus prone to abuse. However, agriculture and animal husbandry would remain priority sectors for the Government and the impact of taxes on input services, wherever justified, would be considered for neutralization appropriately through other means.

2. Transport of goods to a destination outside India: Same may not be liable to taxation by virtue of the Place of Taxation/Supply rules.
3. Services provided by individuals serving on government councils and commissions and supply of goods carriage with driver.
4. Services by religious entities, political parties, decorations and awards have also been taken off as they are rendered by persons who may not be engaged in “economic activities”.

3.3 Many other valuable suggestions have been incorporated and are as follows:

1. Taxation of services provided by government in areas where it competes with private sector unquestioningly finds support. However there are significant problems in defining what will comprise such activities. Moreover it will also keep changing over time as private sector gets increasingly involved in rendering services that might today be in the exclusive domain of the government. Taxation of all services provided by government for a fee or surcharge, while resolving this problem, will add administrative costs and could be more appropriately handled by revising user-charges, wherever necessary. It is thus felt that these services could be defined by way of specific entries. However, in the context of GST the issue could be revisited.
2. Exemptions in the financial sector have been expanded to cover transactions and instruments akin to the instruments and transactions indicated in the earlier Negative List.
3. In the case of transport sector, it is proposed to include passenger travel by non-AC second class as also travel in all classes of metro and monorail so as to address the needs of a common man and encourage public transport system.
4. The entry relating to construction has been revisited. It is felt that the tax paid on construction activities is not available as credit under the existing rules except as sub-contractor. Thus a case is made for keeping certain infrastructure projects within the negative list, particularly those that are meant for larger public good. At the same time construction of such projects together with projects meant for social welfare and for non-commercial use of the government will create definitional issues and amount to end-use exemption. Normally construction activities are not included in negative list

worldwide. It is now for public debate to what extent construction should be covered in the negative list.

5. Renting of personal dwellings is included in the negative list only to the extent of Rs.1 lakh per month per dwelling to cover high-end apartments.
6. Option 2 relating to health sector indicated in the earlier Paper is proposed to be kept in the Revised Concept Paper at this stage. The taxability under any other option could be considered under the GST.
7. A new entry is proposed relating to services to own members by way of reimbursement of charges by an exempt entity. This has been done to obviate the burden of taxes in case of unincorporated associations engaged in non-taxable activities which get funded by own members.
8. Advertisements, other than advertisements in newspapers or broadcast on radio or TV or displayed in other electronic media have also been added as this entry is covered under the State List in the Constitution.

4.0 Place of Taxation Rules

4.1 In order to operationalize the Negative List, it will be necessary to move towards Place of Taxation/Supply Rules that will determine the principles for the determination of location at which services shall be deemed to be provided. These are also intended to be released for public debate shortly.

(This Revised Concept Paper is placed in the public domain for the widest possible consultation, extensive debate and to seek views and feedback of all stakeholders. Views expressed here do not reflect the position of the Government of India in any manner. Any comments, suggestions or feedback may be given by December 15, 2011 to Shri Shobhit Jain, OSD (TRU) at shobhit.jain@nic.in, Tel: 011-23095590; Fax: 011-23093037)

Revised Negative List of Services

Sector	S. No.	Negative List
1. By specified persons	1.	All services other than notified services provided by government <u>Proposed notified services:</u> 1. Business promotion or <u>business support services</u> 2. Construction/works contract 3. Insurance services 4. Port or airport services 5. Postal services other than under Universal Service Obligations (post card, inland letter and money order) 6. Renting of an immovable property or right to enter or use an immovable property 7. Security 8. Trade fairs and exhibitions 9. Transport of goods and passengers 10. Warehousing
	2.	Services by international bodies and diplomatic missions under diplomatic and consular arrangements as per laid down conditions
2. Social welfare and public utilities	3.	Services by organizations registered as non-profit entities under the Income Tax Act 1961 (DTC 2012) in matters relating to public and social welfare activities substantially at or below the costs (excluding health & education)
	4.	Funeral, burial, crematorium and mortuary services
3. Financial Sector	5.	Sale, purchase or acquisition of securities, debts, mutual funds and actionable claims on principal-to-principal basis excluding (1) services in relation to such transactions and (2) when acquired in lieu of a service
	6.	Interest or discount on cheques, promissory notes, bills of exchange or debt instruments
	7.	Dividend on investments
	8.	Sale and purchase of foreign currency amongst banks and/or authorized dealers of foreign exchange
4. Transport	9	Transport of passengers with accompanied belongings by: a) Non-AC second class of passenger travel by railway and any class by metro and mono-rail; b) Public transport buses on a point-to-point basis (except tourist buses) and stage-carriage basis; c) Public transport in ship or vessel of less than 15 net tonnage on a point-to-point basis (except tourist purposes); d) Metered cabs or three-wheeler auto-rickshaw

5. Construction & Real Estate	10	Construction, works-contract, repair, alteration, renovation or restoration of: a) <u>Specified infrastructure for larger public good</u> ; b) Residential building comprising a single dwelling unit
	11	Renting of personal dwellings in excess of Rs 1 lakh per month per dwelling
6. Education	12	Pre-school, school and recognized education** and vocational training recognized by NCVT except placement services and donations or similar charges in relation to admission
7. Health	13	Services by <u>clinical establishments</u> except in relation to health & fitness, weight reduction programmes, health check-up and cosmetic or plastic surgery;
8. Others	14	Copyright services of original literary, dramatic, musical and artistic works.
	15	Services provided by independent journalists, PTI & UNI for providing news
	16	Services provided by sportspersons, as a player, coach or referee/umpire and performing artists in that capacity (excluding as brand ambassadors)
	17	Services provided by a trade union to its members
	18	Representational services provided by an advocate to individuals
	19	Services to own members by an exempt entity by way of reimbursement of charges
	20	Tolls except services in relation to collection of tolls
	21	Betting and gambling except services in relation to promoting, marketing or organizing games of chance, including lottery services
	22	Advertisements other than advertisements published in newspapers or broadcast by radio or TV or displayed in other electronic media

***Government** means the Union, State and local self government and government regulatory bodies established under an act but shall not include any other entity established under the Companies Act 1956 or any other law for the time being in force.

****Recognized education** means education leading to the award of a certificate or degree recognized by a body established by an Indian law.

Bill No. 22 of 2011

**THE CONSTITUTION (ONE HUNDRED AND FIFTEENTH
AMENDMENT) BILL, 2011**

A

BILL

further to amend the Constitution of India.

BE it enacted by Parliament in the Sixty-second Year of the Republic of India as follows:—

1. (1) This Act may be called the Constitution (One Hundred and Fifteenth Amendment) Act, 2011. Short title and commencement.

5 (2) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint, and different dates may be appointed for different provisions of this Act and any reference in any such provision to the commencement of this Act shall be construed as a reference to the commencement of that provision.

2. After article 246 of the Constitution, the following article shall be inserted, Insertion of new article 246A.
namely:—

10 '246A. Notwithstanding anything contained in articles 246 and 254, Parliament and the Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by that State respectively: Special provision with respect to goods and services tax.

Provided that Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

Explanation.— For the purpose of this article, “State” includes a Union territory with Legislature.’

5

Amendment of article 248. **3.** In article 248 of the Constitution, in clause (1), for the word “Parliament”, the words, figures and letter “Subject to article 246A, Parliament” shall be substituted.

Amendment of article 249. **4.** In article 249 of the Constitution, in clause (1), after the words “with respect to”, the words “goods and services tax or” shall be inserted.

Amendment of article 250. **5.** In article 250 of the Constitution, in clause (1), after the words “with respect to”, the words “goods and services tax or” shall be inserted.

10

Amendment of article 268. **6.** In article 268 of the Constitution, in clause (1), the words “and such duties of excise on medicinal and toilet preparations” shall be omitted.

Omission of article 268A. **7.** Article 268A of the Constitution [as inserted by section 2 of the Constitution (Eighty-eighth Amendment) Act, 2003] shall be omitted.

15

Amendment of article 269. **8.** In article 269 of the Constitution, in clause (1), after the words “consignment of goods”, the words, figures and letter “except as provided in article 269A” shall be inserted.

Insertion of new article 269A. **9.** After article 269 of the Constitution, the following article shall be inserted, namely:—

Levy and collection of goods and services tax in course of inter-State trade or commerce. ‘269A. (1) Goods and services tax on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be prescribed by Parliament by law.

20

Explanation I. — For the purposes of this clause, supply of goods or of services or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-State trade or commerce.

25

Explanation II. — For the purpose of this article, “State” includes a Union territory with Legislature.

(2) Parliament may, by law, formulate the principles for determining when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.’

30

Amendment of article 270. **10.** In article 270 of the Constitution,—

(i) in clause (1), for the words, figures and letter “articles 268, 268A and 269”, the words, figures and letter “articles 268, 269 and 269A” shall be substituted;

(ii) after clause (1), the following clause shall be inserted, namely:—

“(1A) Goods and services tax levied and collected by the Government of India shall also be distributed between the Union and the States in the manner provided in clause (2).”.

35

Amendment of article 271. **11.** In article 271 of the Constitution, after the words “in those articles”, the words “except the goods and services tax” shall be inserted.

Insertion of new articles 279A and 279B. **12.** After article 279 of the Constitution, the following articles shall be inserted, namely:—

40

‘279A. (1) **The President shall, within sixty days from the date of commencement of the Constitution (One Hundred and Fifteenth Amendment) Act, 2011, by order, constitute a Council to be called the Goods and Services Tax Council.**

(2) **The Goods and Services Tax Council shall consist of the following members, namely:—**

45

(a) **the Union Finance Minister Chairperson;**

(b) **the Union Minister of State in charge of Revenue Member;**

(c) **the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government Members.**

50

Goods and Services Tax Council.

(3) The Members of the Goods and Services Tax Council referred to in sub-clause (c) of clause (2) shall, as soon as may be, choose one amongst themselves to be the Vice-Chairperson of the Council for such period as they may decide.

(4) The Goods and Services Tax Council shall make recommendations to the Union and the States on—

(a) the taxes, cesses and surcharges levied by the Centre, the States and the local bodies which may be subsumed in the goods and services tax;

(b) the goods and services that may be subjected to or exempted from the goods and services tax;

(c) the threshold limit of turnover below which goods and services tax may be exempted;

(d) the rates of goods and services tax; and

(e) any other matter relating to the goods and services tax, as the Council may decide.

(5) While discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

(6) One-third of the total number of members of the Goods and Services Tax Council shall constitute the quorum at its meetings.

(7) The Goods and Services Tax Council shall determine the procedure in the performance of its functions.

(8) Every decision of the Goods and Services Tax Council taken at a meeting shall be with the consensus of all the members present at the meeting.

(9) No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of—

(a) any vacancy in, or any defect in, the constitution of the Council; or

(b) any defect in the appointment of a person as a Member of the Council; or

(c) any irregularity in the procedure of the Council not affecting the merits of the case.

Explanation.—For the purposes of this article, “State” includes a Union territory with Legislature.

279B. (1) Parliament may, by law, provide for the establishment of a Goods and Services Tax Dispute Settlement Authority to adjudicate any dispute or complaint referred to it by a State Government or the Government of India arising out of a deviation from any of the recommendations of the Goods and Services Tax Council constituted under article 279A that results in a loss of revenue to a State Government or the Government of India or affects the harmonised structure of the goods and services tax.

Goods and
Services Tax
Dispute
Settlement
Authority.

(2) The Goods and Services Tax Dispute Settlement Authority shall consist of a Chairperson and two other members.

(3) The Chairperson of the Goods and Services Tax Dispute Settlement Authority shall be a person who has been a Judge of the Supreme Court or Chief Justice of a High Court to be appointed by the President on the recommendation of the Chief Justice of India.

(4) The two other members of the Goods and Services Tax Dispute Settlement Authority shall be persons of proven capacity and expertise in the field of law, economics or public affairs to be appointed by the President on the recommendation of the Goods and Services Tax Council.

(5) **The Goods and Services Tax Dispute Settlement Authority shall pass suitable orders including interim orders.**

(6) **A law made under clause (1) may specify the powers which may be exercised by the Goods and Services Tax Dispute Settlement Authority and provide for the procedure to be followed by it.**

(7) **Notwithstanding anything in this Constitution, Parliament may by law provide that no Court other than the Supreme Court shall exercise jurisdiction in respect of any such adjudication or dispute or complaint as is referred to in clause (1).**

Explanation.— For the purpose of this article, “State” includes a Union territory with Legislature.’.

Amendment of
article 286.

13. In article 286 of the Constitution,—

(i) in clause (1),—

(A) for the words “the sale or purchase of goods where such sale or purchase takes place”, the words “the supply of goods or of services or both, where such supply takes place” shall be substituted;

(B) in sub-clause (b), for the word “goods”, at both the places where it occurs, the words “goods or services or both” shall be substituted;

(ii) in clause (2), for the words “sale or purchase of goods takes place”, the words “supply of goods or of services or both” shall be substituted;

(iii) for clause (3), the following clauses shall be substituted, namely:—

“(3) Any law of a State shall, in so far as it imposes, or authorises the imposition of a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of tax as Parliament may by law specify.

(4) Nothing in clause (3) shall apply to a law of a State insofar as it imposes or authorises the imposition of goods and services tax.”.

Amendment of
article 366.

14. In article 366 of the Constitution,—

(i) after clause (12), the following clause shall be inserted, namely:—

‘(12A) “goods and services tax” means any tax on supply of goods or services or both except taxes on the supply of the following goods, namely:—

(i) petroleum crude;

(ii) high speed diesel;

(iii) motor spirit (commonly known as petrol);

(iv) natural gas;

(v) aviation turbine fuel; and

(vi) alcoholic liquor for human consumption.’;

(ii) clause (29A) shall be omitted.

Amendment of
article 368.

15. In article 368 of the Constitution, in clause (2), in the proviso, in clause (a), for the words and figures “article 162 or article 241”, the words, figures and letters “article 162, article 241, article 279A or article 279B” shall be substituted.

Amendment of
Sixth Schedule.

16. In the Sixth Schedule to the Constitution, in paragraph 8, in sub-paragraph (3),—

(i) in clause (c), the word “and” occurring at the end shall be omitted;

(ii) in clause (d), the word “and” shall be inserted at the end;

(iii) after clause (d), the following clause shall be inserted, namely:—

“(e) taxes on entertainment and amusements.”.

17. In the Seventh Schedule to the Constitution,—Amendment
of Seventh
Schedule.**(a) in List I — Union List,—****(i) for entry 84, the following entry shall be substituted, namely:—**“84. Duties of excise on the following goods manufactured or
produced in India, namely:—

(a) petroleum crude;

(b) high speed diesel;

(c) motor spirit (commonly known as petrol);

(d) natural gas;

(e) aviation turbine fuel; and

(f) tobacco and tobacco products.”;

(ii) entries 92 and 92C shall be omitted;**(b) in List II — State List,—****(i) for entry 52, the following entry shall be substituted, namely:—**“52. Taxes on the entry of goods into a local area for consumption,
use or sale therein to the extent levied and collected by a Panchayat or a
Municipality.”;**(ii) for entry 54, the following entry shall be substituted, namely:—**“54. Taxes on the sale, other than sale in the course of inter-State
trade or commerce or sale in the course of international trade and commerce
of, petroleum crude, high speed diesel, natural gas, motor spirit (commonly
known as petrol), aviation turbine fuel and alcoholic liquor for human
consumption.”;**(iii) entry 55 shall be omitted;****(iv) for entry 62, the following entry shall be substituted, namely:—**“62. Taxes on entertainments and amusements to the extent levied
and collected by a Panchayat or a Municipality or a Regional Council or
a District Council.”.

18. Notwithstanding anything in this Act, any provision of any law relating to tax on
goods or services or on both in force in any State immediately before the commencement of
this Act, which is inconsistent with the provisions of the Constitution as amended by this
Act shall continue to be in force until amended or repealed by a competent Legislature or
other competent authority or until expiration of one year from such commencement, which-
ever is earlier.

Transitional
provision.

19. (1) If any difficulty arises in giving effect to the provisions of the Constitution as
amended by this Act (including any difficulty in relation to the transition from the provisions
of the Constitution as they stood immediately before the date of assent of the President to
this Act to the provisions of the Constitution as amended by this Act), the President may,
by order, make such provisions, including any adaptation or modification of any provision
of the Constitution or law, as appear to the President to be necessary or expedient for the
purpose of removing the difficulty:

Power of the
President to
remove
difficulties.

Provided that no such order shall be made after the expiry of three years from the date
of such assent.

(2) Every order made under sub-section (1) shall, as soon as may be after it is made,
be laid before each House of Parliament.

STATEMENT OF OBJECTS AND REASONS

The scheme of the Constitution does not provide for any concurrent taxing powers to the Union as well as the States. It is proposed to introduce the goods and services tax and for this purpose to amend the Constitution conferring simultaneous power on Parliament as well as the State Legislatures including every Union territory with Legislature to make laws for levying goods and services tax on every transaction of supply of goods or services or both. The goods and services tax would replace a number of indirect taxes presently being levied by the Central Government and the State Governments and is intended to remove cascading of taxes and provide a common national market for goods and services. The proposed Central and State goods and services tax would be levied on all transactions involving supply of goods and services except those that are exempt or kept out of the purview of the goods and services tax.

2. The proposed Bill which seeks further to amend the Constitution, *inter alia*, provides for—

(a) subsuming of various Central and State indirect taxes and levies like Central Excise Duty, Additional Excise Duties, Excise Duty levied under the Medicinal and Toilet Preparations (Excise Duties) Act, 1955, Service Tax, Additional Customs Duty commonly known as Countervailing Duty (CVD), Special Additional Duty of Customs (SAD), Central Surcharges and Cesses (excluding those applicable to income-tax, customs duties and to excise duties so far as they relate to goods outside the purview of the goods and services tax;

(b) subsuming of State VAT/Sales Tax, entertainment tax (unless it is levied by the local bodies), Luxury Tax, Taxes on lottery, betting and gambling, tax on advertisements, State Cesses and Surcharges insofar as they relate to supply of goods and services and Entry Tax, not levied by local bodies;

(c) levy of Integrated GST (IGST) on inter-State transactions of goods and services;

(d) conferring simultaneous power upon Parliament and the State Legislatures to make laws governing goods and services tax;

(e) coverage of goods other than crude petroleum, diesel, petrol, aviation turbine fuel, natural gas and alcohol for human consumption under the goods and services tax for the levy of goods and services tax;

(f) creation of a Goods and Services Tax Council to examine issues relating to goods and services tax and make recommendations to the Union and the States on parameters like rates, exemption list and threshold limits;

(g) enabling the setting up of a Goods and Services Tax Dispute Settlement Authority, which may be approached by the affected Government (whether the Centre or a State) seeking redressal for any loss caused by any action due to a deviation from the recommendations made by the Goods and Services Tax Council or for adversely affecting the harmonious structure and implementation of the goods and services tax;

(h) empowering District Councils and Regional Councils also to levy tax on entertainment and amusement;

(i) enabling the levy of goods and services tax on sale or purchase of newspapers and advertisements published therein;

(j) permitting only Municipalities and Panchayats to levy and collect tax on entry of goods in a local area for consumption, use or sale therein;

(k) allowing States to levy tax on intra-State sale of goods kept outside the purview of the goods and services tax, namely, Petroleum crude, High Speed Diesel, Natural Gas, Motor Spirit (Petrol), Aviation Turbine Fuel and Alcoholic Liquor for human consumption.

3. The Bill seeks to achieve the above objects.

NEW DELHI;

PRANAB MUKHERJEE

The 16th March, 2011.

PRESIDENT'S RECOMMENDATION UNDER ARTICLE 117 OF THE
CONSTITUTION OF INDIA

**[Copy of letter No. 31011/04/2009, dated 16.3.2011 from Shri Pranab Mukherjee,
Minister of Finance to the Secretary-General, Lok Sabha]**

The President, having been informed of the subject matter of the proposed Bill, recommends, under clauses (1) and (3) of article 117, read with clause (1) of article 274, of the Constitution of India, the introduction of the Constitution (One Hundred and Fifteenth Amendment) Bill, 2011 in Lok Sabha and also the consideration of the Bill.

FINANCIAL MEMORANDUM

Clause 12 of the Bill seeks to insert new articles 279A relating to constitution of Goods and Services Tax Council and 279B relating to establishment of Goods and Services Tax Dispute Settlement Authority in the Constitution. The proposed new article 279A seeks to empower the President to constitute a Council to be called the Goods and Services Tax Council consisting of the Union Finance Minister as its Chairperson and Union Minister of State in-charge of Revenue and the State Minister in-charge of Finance or Taxation or any other Minister nominated by each State Government as their Members.

The proposed new article 279B seeks to provide for the establishment of a Goods and Services Tax Dispute Settlement Authority to adjudicate dispute or complaint referred to it by a State Government or the Government of India arising out of a deviation from any of the recommendations of the Goods and Services Tax Council constituted under the proposed article 279A that results in a loss of revenue to a State Government or the Government of India or affects the harmonised structure of the goods and services tax.

There are no direct financial implications on account of the proposal. However, the creation of the Goods and Services Tax Council and the Goods and Services Tax Dispute Settlement Authority will involve creation of some posts. Given that the introduction of goods and services tax will make the Indian trade and industry much more competitive, domestically as well as internationally and contribute significantly to the growth of the economy, such additional expenditure on these bodies would be miniscule.

It is not practicable to make an estimate of the expenditure, both recurring and non-recurring on account of the above. However, such expenditure would be considerably marginal.

MEMORANDUM REGARDING DELEGATED LEGISLATION

Clause 12 of the Bill seeks to insert a new article 279A relating to the constitution of a Council to be called the Goods and Services Tax Council and another article 279B establishing the Goods and Services Tax Disputes Settlement Authority. Clause (1) of the proposed new article 279A provides that the President shall, within sixty days from the date of the commencement of the Constitution (One Hundred and Fifteenth Amendment) Act, 2011, by order, constitute a Council to be called the Goods and Services Tax Council. Clause (7) of the said article provides that the Council shall determine the procedure in the performance of its functions.

2. The procedure, as may be laid down by the Goods and Services Tax Council in the performance of its functions, are matters of procedure and details. The delegation of legislative power is, therefore, of a normal character.

ANNEXURE
EXTRACTS FROM THE CONSTITUTION OF INDIA

	*	*	*	*	*
Residuary powers of legislation.	248. (1) Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent List or State List.				
	*	*	*	*	*

Power of Parliament to legislate with respect to a matter in the State List in the national interest.	249. (1) Notwithstanding anything in the foregoing provisions of this Chapter, if the Council of States has declared by resolution supported by not less than two-thirds of the members present and voting that it is necessary or expedient in the national interest that Parliament should make laws with respect to any matter enumerated in the State List specified in the resolution, it shall be lawful for Parliament to make laws for the whole or any part of the territory of India with respect to that matter while the resolution remains in force.				
	*	*	*	*	*

Power of Parliament to legislate with respect to any matter in the State List if a Proclamation of Emergency is in operation.	250. (1) Notwithstanding anything in this Chapter, Parliament shall, while a Proclamation of Emergency is in operation, have power to make laws for the whole or any part of the territory of India with respect to any of the matters enumerated in the State List.				
	*	*	*	*	*

Distribution of Revenues between the Union and the States

Duties levied by the Union but collected and appropriated by the States.	268. (1) Such stamp duties and such duties of excise on medicinal and toilet preparations as are mentioned in the Union List shall be levied by the Government of India but shall be collected—				
	(a) in the case where such duties are leviable within any Union territory, by the Government of India, and				

(b) in other cases, by the States within which such duties are respectively leviable.

	*	*	*	*	*

Service tax levied by Union and collected and appropriated by the Union and the States.	268A. (1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the States in the manner provided in clause (2).				

(2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be—

(a) collected by the Government of India and the States;

(b) appropriated by the Government of India and the States,

in accordance with such principles of collection and appropriation as may be formulated by Parliament by law.

Taxes levied and collected by the Union but assigned to the States.	269. (1) Taxes on the sale or purchase of goods and taxes on the consignment of goods shall be levied and collected by the Government of India but shall be assigned and shall be deemed to have been assigned to the States on or after the 1st day of April, 1996 in the manner provided in clause (2).				

Explanation.—For the purposes of this clause,—

(a) the expression “taxes on the sale or purchase of goods” shall mean taxes on sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce;

(b) the expression “taxes on the consignment of goods” shall mean taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce.

* * * * *

270. (1) All taxes and duties referred to in the Union List, except the duties and taxes referred to in articles 268, 268A and 269, respectively, surcharge on taxes and duties referred to in article 271 and any cess levied for specific purposes under any law made by Parliament shall be levied and collected by the Government of India and shall be distributed between the Union and the States in the manner provided in clause (2).

Taxes levied and distributed between the Union and the States.

* * * * *

271. Notwithstanding anything in articles 269 and 270, Parliament may at any time increase any of the duties or taxes referred to in those articles by a surcharge for purposes of the Union and the whole proceeds of any such surcharge shall form part of the Consolidated Fund of India.

Surcharge on certain duties and taxes for purposes of the Union.

* * * * *

286. (1) No law of a State shall impose, or authorise the imposition of, a tax on the sale or purchase of goods where such sale or purchase takes place—

Restrictions as to imposition of tax on the sale or purchase of goods.

(a) outside the State; or

(b) in the course of the import of the goods into, or export of the goods out of, the territory of India.

(2) Parliament may by law formulate principles for determining when a sale or purchase of goods takes place in any of the ways mentioned in clause (1).

(3) Any law of a State shall, in so far as it imposes, or authorises the imposition of,—

(a) a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce; or

(b) a tax on the sale or purchase of goods, being a tax of the nature referred to in sub-clause (b), sub-clause (c) or sub-clause (d) of clause (29A) of article 366,

be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify.

* * * * *

366. In this Constitution, unless the context otherwise requires, the following expressions have the meanings hereby respectively assigned to them, that is to say—

Definitions.

* * * * *

(29A) “tax on the sale or purchase of goods” includes—

(a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;

(b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;

(c) a tax on the delivery of goods on hire-purchase or any system of payment by instalments;

(d) a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;

(e) a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;

(f) a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration,

and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made;

* * * * *

PART XX

AMENDMENT OF THE CONSTITUTION

Power of
Parliament to
amend the
Constitution
and procedure
therefor.

368. (1) * * * * *

(2) An amendment of this Constitution may be initiated only by the introduction of a Bill for the purpose in either House of Parliament, and when the Bill is passed in each House by a majority of the total membership of that House and by a majority of not less than two-thirds of the members of that House present and voting, it shall be presented to the President who shall give his assent to the Bill and thereupon the Constitution shall stand amended in accordance with the terms of the Bill:

Provided that if such amendment seeks to make any change in—

(a) article 54, article 55, article 73, article 162 or article 241, or

(b) Chapter IV of Part V, Chapter V of Part VI, or Chapter I of Part XI, or

(c) any of the Lists in the Seventh Schedule, or

(d) the representation of States in Parliament, or

(e) the provisions of this article,

the amendment shall also require to be ratified by the Legislatures of not less than one-half of the States by resolutions to that effect passed by those Legislatures before the Bill making provision for such amendment is presented to the President for assent.

* * * * *

SIXTH SCHEDULE

[Articles 244 (2) and 275 (1)]

Provisions as the Administration of Tribal Areas in the States of Assam, Meghalaya, Tripura and Mizoram

8. Powers to assess and collect land revenue and to impose taxes.—(1) * * * *

(3) The District Council for an autonomous district shall have the power to levy and collect all or any of the following taxes within such district, that is to say—

* * * * *

(c) taxes on the entry of goods into a market for sale therein, and tolls on passengers and goods carried in ferries; and

(d) taxes for the maintenance of schools, dispensaries or roads.

* * * * *

SEVENTH SCHEDULE*(Article 246)***List I—Union List**

* * * * *

84. Duties of excise on tobacco and other goods manufactured or produced in India except—

(a) alcoholic liquors for human consumption;

(b) opium, Indian hemp and other narcotic drugs and narcotics,

but including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry.

* * * * *

92. Taxes on the sale or purchase of newspapers and on advertisements published therein.

* * * * *

92C. Taxes on services.

* * * * *

List II—State List

* * * * *

52. Taxes on the entry of goods into a local area for consumption, use or sale therein.

* * * * *

54. Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of List I.

55. Taxes on advertisements other than advertisements published in the newspapers and advertisements broadcast by radio or television.

* * * * *

62. Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling.

* * * * *

LOK SABHA

A

BILL

further to amend the Constitution of India.

(Shri Pranab Mukherjee, Minister of Finance)

Report of the Technology Advisory Group for Unique Projects

Ministry of Finance
New Delhi, India

January 31, 2011



January 31, 2011

To,
Shri Pranab Mukherjee,
Honourable Minister of Finance,
Government of India.

Sir,
We submit herewith the Report of the Technology Advisory Group on
Unique Projects (TAGUP).

Shri Nandan Nilekani
Chairman, UIDAI

Shri C.B. Bhawe
Chairman, SEBI

Shri R. Chandrasekhar
Secretary, DoT

Shri Dhirendra Swarup
Former Chairman, PFRDA

Shri S.S. Khan
Former Member, CBDT

Shri P.R.V. Ramanan
Former Member, CBEC

Dr. Nachiket Mor
Chairman, IFMR Trust

Members

Chairman

Nandan Nilekani	Chairman, UIDAI

Members

C. B. Bhav	Chairman, SEBI
R. Chandrasekhar	Secretary, Department of Telecommunications
Dhirendra Swarup	Former Chairman, PFRDA
S. S. Khan	Former Member, CBDT
P. R. V. Ramanan	Former Member, CBEC
Dr. Nachiket Mor	Chairman, IFMR Trust

Secretariat

Amal Pushp	Additional Director of Income Tax, CBDT, DoR
Krishnan Dharmarajan	Director, National e-Governance Division, DIT
Parama Sen	Director, DoE
Ravi Agarwal	Director of Income Tax (Systems), CBDT, DoR
Ritesh Kumar Singh	Private Secretary to Minister for Petroleum and Natural Gas
Ritvik Pandey	Deputy Secretary, DEA
Satyajit Suri	General Manager (Program Development and Management), NISG
Somya Dave	Additional Director General, CBEC, DoR
Srikar M.S.	Private Secretary to Chairman, UIDAI
Dr. Viral B. Shah	Manager, UIDAI

Preface

The Finance Minister in his Budget Speech of 2010–2011 had announced the setting up of a Technology Advisory Group for Unique Projects. Para 104 of the Budget speech reads as follows:

Technology Advisory Group for Unique Projects

104. An effective tax administration and financial governance system calls for creation of IT projects which are reliable, secure and efficient. IT projects like Tax Information Network, New Pension Scheme, National Treasury Management Agency, Expenditure Information Network, Goods and Service Tax, are in different stages of roll out. To look into various technological and systemic issues, I propose to set up a Technology Advisory Group for Unique Projects under the Chairmanship of Shri Nandan Nilekani.

In recent years, Government functioning in general and specific projects in particular have come to involve complex Information Technology (IT) system development. Five projects stand out:

1. Goods and Services Tax (GST)
2. Tax Information Network (TIN)
3. Expenditure Information Network (EIN)
4. National Treasury Management Agency (NTMA)
5. New Pension System (NPS)

In addition, there are numerous other settings in Government where IT systems are mission critical.

These five projects alone have immense transformative power and can change India's growth trajectory. This justifies efforts in increasing the probability of project success. The challenge is to find ways to rapidly roll out these complex systems, to achieve project objectives and sustain high levels of reliable performance. Issues of project management for complex IT-intensive systems in Government need to be addressed on a priority. This report is an effort in this direction.

The Group held consultations with various experts within Government and outside. The consultations were held with Department of Economic Affairs, Department of Expenditure, Department of Revenue, PFRDA, CGA, CBDT, CBEC, NIC, CRIS, NSDL, NPCI, NASSCOM, and representatives of various State Governments.

Although the primary audience of this report are decision makers and the management teams of projects such as GST, TIN, EIN, NTMA, and NPS, the Group believes that

the framework put forth in this report is more generally applicable to the complex IT-intensive systems which are increasingly coming to prominence in the craft of Indian public administration.

The Group also recognises that various existing IT-intensive projects in Government are at different stages of implementation and with differing models. The adoption of the key recommendations of the Group to such projects should be done in a way that ensures minimal disruption to existing functioning.

List of abbreviations

BPR	Business Process Re-engineering
CBDT	Central Board of Direct Taxes
CBEC	Central Board of Excise and Customs
CVC	Central Vigilance Commission
DEA	Department of Economic Affairs
DIT	Department of Information Technology
DoR	Department of Revenue
DoE	Department of Expenditure
DoT	Department of Telecommunications
EIN	Expenditure Information Network
GFR	General Financial Rules
GOI	Government of India
GST	Goods and Services Tax
GSTN	Goods and Services Tax Network
IT	Information Technology
ITD	Income Tax Department
KYC	Know Your Customer
MoU	Memorandum of Understanding
MSP	Managed Services Provider
NISG	National Institute for Smart Government
NPCI	National Payments Corporation of India
NPS	New Pension System
NSDL	National Securities Depository Limited
NSE	National Stock Exchange
NTMA	National Treasury Management Authority
NIU	National Information Utility
PAN	Permanent Account Number
PFRDA	Pension Fund Regulatory and Development Authority
RFP	Request for Proposal
RTI	Right to Information
SEBI	Securities and Exchange Board of India
SLA	Service Level Agreement
TAGUP	Technology Advisory Group for Unique Projects
TIN	Tax Information Network
UIDAI	Unique Identification Authority of India

Executive summary

In the last two decades, the Government of India (GOI) and many State Governments have initiated several e-Governance projects many of which have brought about significant changes in the way the concerned Departments and Agencies had conducted their business in the past.

The Finance Ministry in the GOI has been in the forefront of such initiatives and has successfully implemented large, complex projects involving extensive use of IT Systems, such as the TIN for Income Tax applications, ICES for Customs, and ACES for Excise and Service Tax. Similarly, the vision of organized financial trading (stock exchanges, depositories, and clearing corporations) has been implemented successfully using IT systems through the joint efforts of various stakeholders.

Undoubtedly, all of them have to be built on sound and durable IT systems for better management. Considering the complex nature of these projects, it is necessary to not only get the design and implementation of such systems right, but it is also essential that institutional capacity be built up to support these projects and sustain them on an ongoing basis. The challenge is thus that of finding ways to rapidly roll out these systems, to achieve and then to sustain high levels of reliable performance on an ongoing basis.

The Group reviewed these five projects along various dimensions. The challenges faced in implementing ongoing projects like TIN, ICES and ACES have been a valuable guide. The most important lesson that needs to be acted upon is that business change¹ should drive the design and implementation of these projects. IT is essentially an enabler and a powerful tool to achieve the expected business change. In this sense, IT is a means to an end.

In the course of these reviews, the Group observed similar patterns and challenges across all projects, and a common framework for evaluation evolved naturally. Thus, this report starts out by addressing the challenges faced by large complex IT projects in Government, and then applies this framework to the evaluation of the five projects at hand. Part I discusses the public policy challenges. Technology challenges are discussed in Part II. All projects are then evaluated within this framework in Part III.

Public policy challenges

Chapter 1 analyzes the first of the public policy challenges, namely, the appropriate placement of tasks. IT projects in Government, if small, are typically implemented in-house, and if large, or contracted out to Managed Service Providers (MSP) or vendors. Taking into account the complex nature of 5 projects in view, and the

project management challenges, the adoption of a National Information Utility (NIU) framework, where the Government focuses on policy formulation and enforcement, and the NIU on implementation of IT systems to enable the proposed business changes is recommended. Besides, the recommendations cover the aspects of ownership and governance structure of the NIU, strategic control by the Government, and allocation of responsibilities between the Government and the NIU.

Considering the importance of investment in *peopleware* in the successful implementation of complex projects and the need to nurture talent to sustain continuous improvement, Chapter 2 discusses the second challenge, namely, human resource issues. The recommendations herein cover aspects such as setting up of a dedicated Mission Team headed by Mission Leader, a five year tenure for the team to ensure continuity, revising Deputation schemes within Government, induction of talent from outside the Government, wider use of contractual appointments, capacity building through induction and advanced training programs, grant of incentives to retain in-service officers on projects, creation of conducive work environment and improving methods of performance appraisal methods, especially for personnel appointed to key projects. Similarly, the NIU must also have a dedicated management team that mirrors the team within Government.

Chapter 3 discusses the issues that are relevant for giving shape to the contractual relationship between the Government and the NIU in a vendor-customer mode. In line with the recommendations for the adoption of NIU framework, wherein NIUs will work in the spirit of partnership with the Government, detailed recommendations have been made on the aspects to be touched in the agreement with NIU, such as scope of work, activities to undertaken by the NIU, financial arrangement, obligations of the NIU and the Government, SLAs, and business continuity plan upon exit.

The challenges faced by projects from startup to going concern are addressed in Chapter 4. The needs of a project in the startup phase are quite different from its needs in steady State. These may vary from mundane issues such as office space, to complex issues such as legal frameworks and bringing all stakeholders on board. The recommendations focus therefore on issues such as, incubation process before the NIU comes into being, need to set up dedicated teams within the Government as well as the NIU, need for consultations with stakeholders, preparation of a Mission Strategy Document, rapid roll out based on the experience of pilots and the relationship during the start-up phase.

Chapter 5 discusses specific challenges faced by projects that span multiple levels of Government. The Group is of the view that the seemingly opposite characteristics of federal, decentralized governance and the need for a unified approach through a single software application with common functionality can be resolved with the right solution architecture evolved through a process of consensus. Incentive compatible solutions for all levels of Government are necessary to bring about a coalition for change and ensure full participation and success for such projects.

Technology challenges

Chapter 6 points out some key design considerations for the solution architecture. The solution architecture should be designed to be flexible, reusable, extensible by stakeholders, and free of vendor lock-in. Given that many Government projects touch end-users such as citizens and firms, the Government should also play an active role in promoting banking and accessibility for all. This can form the basis of a platform for delivery of services.

Chapter 7 addresses openness in implementation of Government IT projects. It describes the relevance of open standards, open data, and open source. The Government

should not only be a consumer, but also strive to produce and facilitate open standards, open data, and open source. It also suggests the creation of an open source foundation for open sourcing software from Government projects.

Chapter 8 discusses security for systems of strategic importance. Today, attacks on IT systems are getting increasingly sophisticated. Systems such as those that are the focus of this report are likely to be targeted. Compromise may also happen from within the organization. Security must be taken seriously, and should be one of the topmost concerns of the management team.

Chapter 9 describes mechanisms of accountability and transparency that should be built into the design of IT systems in Government. Transparency cannot be an afterthought. It is essential to define what data will be released early on, so that the IT system can be architected accordingly.

Chapter 10 describes safeguards in technology and processes that should be built into the design of IT systems to protect the privacy of individuals. Privacy, like transparency cannot be an afterthought. Privacy and transparency are also not at odds with each other, and a well-planned system can easily achieve both.

Recommendations on Ministry of Finance projects

Chapter 11 discusses the strategy and implementation of the GST project. The recommendations, take note of the impending implementation of GST and cover the setting up of GST Network as an NIU, incubation of the project in NSDL, the need to set up a dedicated Mission Team on a priority basis, the placement of tasks in the NIU, the setting up of a continuing consultation process among the stakeholders, the broad features of the solution architecture of the GSTN, and the way forward from the pilot stage to steady state.

Chapter 12 discusses the working of the TIN project and the IT systems within the Income Tax Department for processing the information flowing from the TIN. The Group notes that with the impending operationalisation of the Direct Taxes Code, major changes in the application solutions are called for. The way forward would be to set up an NIU to design, develop and manage its IT related infrastructure on long-term basis and also to replace the existing application of diverse implementation methodologies. The recommendations to achieve project objectives have also been set out.

Chapter 13 discusses the Expenditure Information Network. The existing system of expenditure has some limitations. Today, measurement of plan implementation is on the basis of outlay rather than outcome. Government follows hierarchical and multiple patterns for allocation and release of funds to the implementing agencies and beneficiaries. It is difficult to track the flow of funds to actual beneficiaries, and equally difficult to evaluate the performance of agencies based on spending and project implementation. The Group recommends that a Mission Team be set up within Government along with an NIU for implementing the EIN. A high level solution architecture for the EIN is also described in this chapter.

Chapter 14 discusses the way forward for NTMA. It is seen that the Internal Working group on Debt Management (WG) has provided detailed steps for incubating the project, setting up of IT systems, the need for creation of databases on debts and contingent liabilities and change management for transferring the functions from RBI to NTMA. The Group commends the approach suggested by the WG, and recommends that an NIU approach be adopted for the implementation of IT systems for NTMA.

Chapter 15 discusses the status of IT systems set up to meet the requirements of the New Pension System. The suggested way forward is to work towards convergence of all pension and provident fund streams, rationalization of tax treatment of NPS to provide



more even treatment with other retirement products and providers and creation of awareness among the subscribers. Recommendations for implementation have also been indicated.

The report concludes with a summary of recommendations in Part [IV](#).

Contents

Contents	2
I Public policy challenges	7
1 The appropriate placement of tasks	9
1.1 Background	9
1.2 National Information Utilities (NIU)	10
1.3 Institutional framework and strategic control	11
1.3.1 Independent management	11
1.3.2 Strategic control within Government	11
1.3.3 A flexible institutional framework	12
1.4 Ownership	13
1.4.1 Desirable features	14
1.5 Allocation of tasks and responsibilities	15
2 Human resource policies	16
2.1 Background	16
2.2 Key recommendations	17
2.2.1 Leadership and active ownership	17
2.3 Recommendations for the Government team	17
2.3.1 A dedicated Mission Leader in Government	17
2.3.2 A dedicated Mission Execution Team in Government	17
2.3.3 Recruitment and tenure of the Mission Execution Team	18
2.4 Staffing of the NIU team	18
2.5 Database of IT Projects and Centres of Expertise	18
2.6 Capacity Building and retention of in-house staff	19
2.7 Conducive work environment	20
2.8 Performance Appraisal	20

3	Contracting	21
3.1	Background	21
3.2	Contracting with National Information Utilities	22
3.3	Aspects to be covered in the agreement with NIU	22
3.3.1	Scope of work	22
3.3.2	Activities to be undertaken by NIU	23
3.3.3	Obligations	23
3.3.4	Financial arrangement	23
3.3.5	Service Level Agreement	23
3.3.6	Business continuity plan upon exit	23
4	From startup to going concern	25
4.1	Background	25
4.2	Institutional framework for the project	25
4.3	Incubation of a new National Information Utility	25
4.4	Mission Strategy Document	26
4.5	The right team	27
4.6	Consultations with stakeholders	27
4.7	Legal framework	27
4.8	Incremental rollout	28
4.9	Government-NIU relationship during incubation	28
5	Multiple levels of Government	29
5.1	Background	29
5.2	Decentralized governance	29
5.3	Need for a single application	30
5.4	Solution design for multiple levels of Government	30
5.5	NIU approach to align incentives	31
5.6	Building a coalition for change	32
II	Technology challenges	33
6	Solution architecture	35
6.1	Background	35
6.2	Essential elements of a solution architecture	35
6.2.1	Map out a long term IT strategy	35
6.2.2	Structured change management	36
6.2.3	Reflection of policy changes in IT systems	36
6.2.4	Data quality	37
6.2.5	Vendor neutral solution	37
6.2.6	Interoperability and multiple providers	37
6.2.7	A platform strategy	37
6.3	Essential public goods	38
6.3.1	Connectivity	38
6.3.2	Banking system interface	39

7	Openness	40
7.1	Background	40
7.2	Open standards	40
7.3	Open data	41
7.4	Open source	41
7.4.1	An Open Source Foundation	42
8	Information security	43
8.1	Background	43
8.2	Institution-wide support for information security	43
8.2.1	Certification	44
8.2.2	Audits	45
8.3	Solution architecture and information security	45
8.4	Threat to information security from insiders	46
8.5	Legal framework governing information security	46
8.6	National level considerations	47
9	Accountability, transparency, and self-corrective forces	48
9.1	Background	48
9.2	What to share	48
9.3	Solution architecture and transparency	48
9.4	Self-corrective forces	49
9.5	Contact centre	49
9.6	Crowd-sourcing	49
9.7	International experiences	50
10	Protection of the individual	52
10.1	Background	52
10.2	Solution architecture and privacy	52
10.2.1	Personal identifiable information	52
10.2.2	Anonymization	53
10.2.3	Data retention and usage policy	53
10.3	Balancing the right to privacy with public interest	53
III	Recommendations for Ministry of Finance projects	54
11	Goods and Services Tax	56
11.1	Introduction	56
11.2	Public policy challenges	56
11.2.1	Placement of tasks	56
11.2.2	Incubation of the project	57
11.2.3	Human resources	57
11.2.4	Agreement with NSDL	58
11.2.5	Multiple levels of Government	58
11.3	Technology challenges	58
11.3.1	Solution architecture for GSTN	58
11.4	The way forward	59

12 Tax Information Network	61
12.1 Introduction	61
12.2 Public policy challenges	62
12.2.1 Placement of tasks: NSDL as the MSP	62
12.2.2 Human Resources	62
12.2.3 Contracting	62
12.2.4 Incubation	63
12.3 Technology challenges	63
12.3.1 Solution architecture	63
12.3.2 Openness	63
12.3.3 Security	64
12.3.4 Transparency and Privacy	64
12.4 The way forward	64
12.4.1 TIN only a component in IT infrastructure of Income Tax Department	64
12.4.2 Recommendations	65
13 Expenditure Information Network	67
13.1 Introduction	67
13.1.1 Challenges with expenditure tracking today	67
13.1.2 Setting up an Expenditure Information Network	68
13.2 Public policy challenges	69
13.3 Technology challenges	69
13.4 The way forward	70
14 National Treasury Management Agency	71
14.1 Introduction	71
14.2 Public policy challenges	71
14.3 Technology challenges	71
14.4 The way forward	72
15 New Pension System	73
15.1 Introduction	73
15.2 Public policy challenges	73
15.2.1 Placement of tasks: NSDL as the MSP	73
15.2.2 Human resources	73
15.2.3 Contracting	74
15.2.4 Incubation	74
15.2.5 Multiple levels of Government	74
15.3 Technology challenges	75
15.3.1 Solution architecture	75
15.4 The way forward	76

IV Summary of recommendations	78
16 Recommendations for public policy challenges	80
16.1 The appropriate placement of tasks	80
16.2 Human resource policies	81
16.3 Contracting	83
16.4 From startup to going concern	83
16.5 Multiple levels of Government	84
17 Recommendations for technology challenges	86
17.1 Solution architecture	86
17.2 Openness	87
17.3 Information security	87
17.4 Accountability, transparency, and self-corrective forces	88
17.5 Protection of the individual	88
18 Recommendations for Ministry of Finance projects	90
18.1 Goods and Services Tax	90
18.2 Tax Information Network	92
18.3 Expenditure Information Network	93
18.4 National Treasury Management Agency	94
18.5 New Pension System	95

Part I

Public policy challenges

1

The appropriate placement of tasks

1.1. Background

Over the years, several projects, both large and small, have been implemented in the Government sector in India with varying degrees of success. Some of these projects are yet to meet the expectations of the ultimate users as well as the departments that conceived these projects. While reasons for the same are many, one that has been a recurring theme in all the projects has been the inability of the concerned departments to implement and manage them efficiently and effectively in a sustained manner.

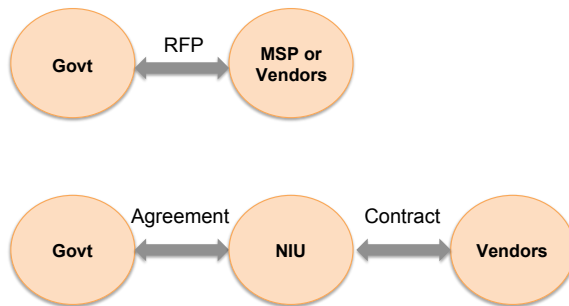
Typically, IT projects supporting Government functions are developed within Government for small projects, or outsourced to a Managed Services Provider (MSP) or one or more vendors for larger projects. In the MSP/vendor model, the Government Department puts a project team in place, which carefully studies the business requirements and writes a Request for Proposal (RFP). An MSP/vendor is then selected through a competitive bidding process. In the case of highly specialised projects, Government has also followed the route of selection of service providers on nomination basis after rigorous evaluation of alternatives and negotiation of price by an expert group consisting of resources from within and outside.

Invariably, managing such projects has been a great challenge. Often, the implementation team has had to face serious problems due to lack of financial independence, inability to get the right personnel and retain them, technological obsolescence, lack of speed and productivity in implementation, lack of ownership on the part of the user community within the department, leading to cost and time overruns and failure to fulfill the requirements.

The Group is of the view that for complex projects that depend on mission-critical IT systems, like the GST project, there is a clear need to move away from the above mentioned implementation models. A robust and flexible institutional framework, combined with a strong dedicated team is necessary to successfully implement such projects in Government. Alongside, appropriate placement of tasks and allocation of responsibilities as between the Government and the supporting institutions are essential to achieve the goals and objectives of the projects.

The Group recommends that a class of institutions called *National Information Utilities (NIU)* may be put in place to handle all aspects of IT systems for such complex

Figure 1.1: Role of NIU



projects. These institutions would work in the spirit of partnership with Government, helping to overcome some of the challenges of a pure MSP/vendor model. They would participate in high-level design, specification of requirements, proof-of-concept studies, while strategic control is retained within Government. For actual implementation, the NIU then contracts with vendors from the market for specialised services while being completely responsible to the Government for committed deliverables and service levels. The proposed structure is depicted in Figure 1.1. It is believed that the NIU model would substantially overcome the problems faced by the Government in implementing the projects with in-house skills or through the MSP/vendor model.

Projects that can benefit from an NIU structure may have one or more of the following characteristics:

1. Projects that span multiple levels of Governments — Central, State, Local (Chapter 5)
2. Projects that span multiple Government departments
3. Projects that span multiple stakeholders, where the network externalities of a thriving ecosystem around the Government developed platform is essential for success
4. Projects that require significant business process re-engineering to leverage technology
5. Projects that aid a sovereign function of Government

1.2. National Information Utilities (NIU)

As conceived by the Group, NIUs would be *private companies with a public purpose*: profit-making, but not profit maximizing. This concept is not a new one; some comparable examples are NSDL (Box 1.1), NPCI (Box 1.2), and CRIS (Box 1.3).

An NIU would make available essential infrastructure for public service. Such institutions can make it possible for Government functions to be carried out efficiently, allow feasible projects to be designed, and thus foster economic development. Well functioning NIUs have a net positive effect on society, like other infrastructure institutions.¹

For projects in Government, at a high level, the two major tasks are *policy making* and *implementation*. The policy related tasks such as policy formulation and policy

¹Market Infrastructure Institutions (MIIs) described in the Report of the Committee (chaired by Bimal Jalan) are a closely related concept: <http://www.sebi.gov.in/commreport/ownershipreport.pdf>

Box 1.1: National Securities Depository Limited (NSDL)

1. NSDL is a company incorporated under the Companies Act, 1956, and regulated by SEBI.
2. The principal sponsors UTI, IDBI, and NSE are required to hold a minimum of 51% stake. Principal sponsors give an undertaking that they stand responsible for all operations carried out by NSDL.
3. Other stakeholders include SBI, banks, and depository participants.
4. Paid-up equity of Rs.80 crores; Net worth above Rs.100 crores, as required by SEBI regulations.
5. There are no Stated restrictions on listing NSDL in the stock exchange, other than the 5% maximum stake requirement for any shareholder; but only depository participants can be shareholders.
6. NSDL is managed by a Board of Directors; it is governed by its bye-laws, and its business operations are regulated by business rules.
7. Though NSDL is a profit-making company, it does not have quarterly targets and does not work towards maximizing profits. Windfall profits and increase in revenue volumes are adjusted through reduction in tariffs and charges.
8. Operating model involves:
 - (a) Outsourcing to external vendors/ service providers. Certain activities like system administration, DB administration, UAT, regression and volume testing, requirements gathering, system analysis are done by in-house functional analysts and engineers
 - (b) Operating expenditure based contracts with Government customers
 - (c) Capital expenditure based / fixed price/ time-material contracts with vendors/ suppliers
 - (d) NSDL has the autonomy to pay market-linked salaries to its employees. The compensation levels are benchmarked with financial services sector and IT sector.
 - (e) NSDL is not bound by Government procurement regulations

enforcement should be carried out by Government. The NIU would be primarily responsible for technology-related aspects of implementation, bound by tight service level agreements (SLA), and subject to periodic audits. The project must be designed so that strategic control is retained within Government.

1.3. Institutional framework and strategic control

1.3.1. *Independent management*

The structure of the NIU should be such that it should be able to work without the need for day-to-day guidance and advisory from the shareholders/members/Board. The management should be independent and empowered to take quick and efficient business decisions pertaining to attracting and retaining talent, procurement, rapid response to business exigencies, adopting new technologies etc. The independence of the management is linked to the financial independence of the NIU. Therefore, the NIU should be able to get funding independently and have a self-sustaining financial model (for e.g. levy user charges/ charge for services or a combination). The entity should be empowered to commit and sign appropriate SLAs with customers and vendors.

1.3.2. *Strategic control within Government*

Given the sensitivity of the role that the NIU will play, it is necessary that strategic control be retained within Government. Strategic control primarily should be focussed

Box 1.2: National Payments Corporation of India (NPCI)

1. Incorporated as Section 25 company under Companies Act, 1956
2. Ten promoter banks (State Bank of India, Punjab National Bank, Canara Bank, Bank of Baroda, Union bank of India, Bank of India, ICICI Bank, HDFC Bank, Citibank, and HSBC).
3. Authorized capital is Rs.300 crore; paid up capital is Rs.30 crores. Equity contribution in NPCI is not considered as an exposure to financial markets.
4. Board composition: Chairman, nominee from RBI, nominees from promoter banks, MD and CEO.
5. Intent was to involve the top banking community as shareholders to the company.
6. The core business of NPCI is *inter-bank transaction processing*
7. NPCI termed as Deemed public sector; it falls within the ambit of CVC and RTI due to its public sector status.
8. Challenges faced by NPCI include:
 - (a) Pricing pressure from competition
 - (b) Service management expectations
 - (c) Restrictions on scaling the organization due to Section 25 status
 - (d) Having customers as board members

on the vision and outcomes of the project, rather than controlling the functioning and management of the day to day affairs of the NIU. Providing flexibility to the NIU is not necessarily against achieving the broad objectives and outcomes of the project.

Strategic control can be achieved by having a strong dedicated team within Government *inter alia* to drive policies, design a suitable solution architecture, supervise execution, frame appropriate contracts, adopt outcome based pricing, evolve SLAs, and conduct independent audits.

1.3.3. A flexible institutional framework

In order to evolve an operational model that would help in achieving the twin objectives of independent management within the NIU, and retention of strategic control within Government, the Group evaluated two alternatives; namely a Society (registered under *The Societies Registration Act, 1860*) and a Company (registered under *Companies Act, 1956*).

A Society is governed by its bylaws, which are specifically defined for each Society. The Societies Registration Act, 1860, provides full flexibility to the members of the Society to define the bylaws based on which the society is to be governed and managed. A Company is governed by Companies Act, 1956. Under the Act, there is a clear distinction between Management and the Governing Body (Board of Directors). The Act also lays down the roles and responsibilities of Directors, including the Managing Director.

A society can be created with bylaws that allow for independence of the management team with regard to operations, including HR policies and compensation norms, procurement process, and financial decisions. However, in order to retain strategic control, the society needs to be controlled by Government and its processes may have to be aligned with Government processes.

Box 1.3: Centre for Railway Information Systems (CRIS)

1. CRIS has been formed as a society governed by its own bye-laws. It was registered as a society under the Societies Registration Act, 1986.
2. CRIS's interface with the Ministry of Railways is managed through a Directorate at the Ministry. It is headed by a dedicated Managing Director.
3. The society's structure requires it to approach the Ministry of Railways for financial approval.
4. CRIS has avenues to raise resources through levy of 10% service charge with respect to the procurement of goods and services it undertakes with respect to various projects. However, in recent times, even this service charge is being reduced / eliminated due to cost cutting by the Ministry.
5. Challenges faced by CRIS include:
 - (a) Constraints on financing of projects
 - (b) Limited business continuity due to staffing by officers on deputation for short periods
 - (c) Interfacing with the Ministry through the Directorate can sometimes be sub-optimal and slow

On the other hand, a company's management is provided with the requisite empowerment to operate independently with regard to day to day operations and yet be accountable to the Board. The Companies Act, 1956, provides for more elaborate and rigid norms (as compared to a society) with respect to accountability and transparency. The governance structure of a Company allows for Government to retain strategic control (by virtue of being a shareholder and also a customer), without impeding the independence of its management.

In the context of executing complex projects in Government, a company structure is preferable over a society due to greater ability to raise funds and it allows for financial independence, operational flexibility, quicker decision making, greater accountability, and transparency. In the context of a society, the ability to attract different kinds of capital is limited and the structure is not viable for the public-private nature as envisioned in the long term.

The Group therefore recommends that the NIU should be structured as a company with limited liability and be subject to sound corporate governance norms, such as those required for listed companies. While the company should not be listed on a stock exchange, the board composition, accountability, and transparency norms for NIUs should be the same as prescribed for listed companies.

1.4. Ownership

The following characteristics would be appropriate for NIUs:

1. Total private ownership within NIUs should be at least 51%. As a paying customer, the Government would be free to take its business to another NIU, if necessary. At the same time, the Government could moderate the functioning of the NIU by virtue of being the owner, through its position on the Board.
2. The ownership share of the Government in an NIU should be at least 26%.
3. No single private entity should own more than 25% of the shares in an NIU. Institutions that have a direct conflict of interest (eg. IT companies) should not be permitted to be shareholders.

4. An NIU should not go for an initial public offering or list itself on public exchanges.
5. NIUs should be dispersed-shareholding corporations with a professional management team who are not owners.
6. A re-mutualisation approach may be thought of, wherein the shareholders of an NIU are the entities who stand to greatly benefit indirectly from its success. This would help align their incentives to the impact of the NIU upon society, as opposed to a focus on dividends and valuation.
7. An NIU should preferably have a net worth of Rs.300 crore. This will ensure that the NIU is well-capitalized, can hire the best people at competitive salaries, and invest adequately in infrastructure, so that it can manage large-scale national projects.
8. The articles of association of the NIU may include a cap on dividend payouts, to ensure that the incentives of the owners do not drive it towards profit-maximization.

1.4.1. *Desirable features*

NIUs are important institutions, since they aid the functioning of Government. Due to various factors such as a large upfront sunk-cost, economies of scale, and network externalities from a surrounding ecosystem, they are essentially set up as *natural monopolies*. It is thus essential that a monopolistic operator is obliged to provide access to a competing NIU, when one emerges. For example, the Depositories Act, 1996, requires full interoperability among all depositories. NSDL was initially set up as the first depository, whose creation was facilitated by Government. However, when CDSL emerged, the customers benefited from interoperability across depositories.

The following are desirable features for effective functioning of an NIU:

1. **Self-financing:** The NIU should be capable of self-financing its operations and providing for its sustenance in the near future.
2. **Make reasonable profits:** The NIU should endeavor to generate reasonable profits in order to be self-sustaining. The NIU should levy reasonable charges on its users without abusing its dominant position. The NIU must not maximise profit or valuation. Salaries of employees should not be linked to profits. The salaries should be competitive and market driven, to ensure that the best quality of people for the job can be hired.
3. **Net worth:** The net worth of the NIU should be available as a last resort to meet exigencies and ensure that it is able to remain as a going concern.
4. **Professional standards and competitive practices:** The NIU must maintain the same professional standards in all its dealings including dealings with its competitors, its technology providers and related entities. It must be able to maintain its integrity by being unbiased while dealing with all such entities.
5. **Transparency:** The NIU should maintain utmost transparency in its operations. The NIU on its website should at least make disclosures that are mandated for a listed company.
6. **Technology:** The NIU should be willing to invest in technology for increasing efficiency, reach and economies of scale.
7. **Competition:** NIUs would have characteristics similar to those of monopolies. Hence, it is essential to create enabling conditions that allow new entrants to enter the market, with necessary safeguards in place.

1.5. Allocation of tasks and responsibilities

The Government-NIU relationship must be in the spirit of a partnership, rather than that of a vendor and customer. The relationship may be defined by an Agreement, which contains the allocation of tasks and responsibilities between the Government and the NIU, financials, and SLAs.

In the early phases of a project, during incubation, the Government may also have to be actively involved with implementation of technology. The NIU should also engage the services of domain experts from within and outside the Government during incubation and subsequent stages of implementation. Both, the Government and the NIU should have teams that are dedicated to the project, which will facilitate smooth decision making.

The concerned Department that owns the project and is responsible for its successful implementation should lay down clearly the project goals and charter. Business change is the driving force, and technology is an enabler. Therefore, a Mission Strategy Document for the project that *inter alia* details the functions, and capabilities of the IT system, which would assist in bringing about the desired business change, should be prepared.

The Department should recognize the capabilities and limitations of the technology solution, while the NIU should perceive its responsibility as extending beyond merely meeting a technical or legal requirement under the Agreement, but as providing a holistic service to achieve the projected business change.

2

Human resource policies

2.1. Background

All projects that aim at effecting a business change through enhanced use of IT systems, are first of all, governance projects. The success of a complex project with multiple objectives and multiple stakeholders requires a strong Mission Execution Team that is capable of driving all business and technology issues.

This team should get the total support and involvement of the top management within Government, acceptance of change and use of IT systems by all, particularly, the host of end users. Investment in *peopleware* and effective harnessing of human capital deployed for conceiving, designing, implementing, maintaining, and running of such systems is indeed a clear need in the context of large projects such as those under study by this Group.

These projects require a diverse mix of skills, ranging from domain specific knowledge on business issues and managing large decentralized organizations, to specialised skills in domains such as technology design, vendor development and informed buying, contract facilitation and monitoring, law, relationship building, communication and outreach. Today, Departments have officers who are business specialists, with a deep understanding of the Department's business and domain knowledge as well as officers who are generalists, who manage the running of a large decentralized organization. For the execution of large complex projects that include mission-critical IT systems, it is important to complement the skills within Government with specialised skills from the private sector.

The Group had the benefit of interaction with officers of Departments that have implemented large projects with a significant IT component and based on the same, the following human resource challenges within Government have been identified as requiring consideration:

1. Absence of leadership and active ownership of projects
2. Outdated recruitment processes and methodology
3. Inability to pay market salaries for specialised skills
4. Lack of diverse opportunities and variety in assignments
5. Lack of avenues of continued enhancement of professional skills and career growth opportunities

6. Non-conducive work environment
7. Outdated performance evaluation and preference for seniority over merit
8. Untimely transfers of officers posted to handle certain project functions

2.2. Key recommendations

2.2.1. *Leadership and active ownership*

The Group is of the view that strong support from the top management within Government, leadership at the level of project implementation, and ownership and commitment at various operational levels are necessary concomitants of success of any project. The concerned Department should put in place a high level body that will review the progress of the project during its implementation and later evaluate the realization of benefits and objectives on a periodic basis.

Further, every project should have:

1. A dedicated **Mission Leader** within the Government Department responsible for the project
2. A dedicated **Mission Execution Team** should support the Mission Leader
3. The Mission Leader should have the freedom to choose the Mission Execution Team from within or outside the Government

2.3. Recommendations for the Government team

2.3.1. *A dedicated Mission Leader in Government*

Typically, complex mission-critical projects in Government are anchored under an officer of the level or seniority of a Joint Secretary. Often, this Joint Secretary has a number of other responsibilities also that they may have to attend to on a daily basis. While this model works well for projects that are already on course and only day-to-day operations have to be managed, it does not work well for new and complex projects that are getting off the ground.

Every mission-critical project in Government should therefore have a dedicated Mission Leader who holds the rank of a Joint Secretary or Additional secretary or above in the Government of India. If the project is being implemented within a Department, the Mission Leader should directly report to the Secretary. The Mission Leader should be fully responsible and empowered for all aspects of the project: policy, decision-making, human resources, finance, procurement, and all other aspects of implementation. The Mission Leader must have skills and expertise (including experience with IT projects) specific to the project, which must be corroborated by a quantifiable track record. The selection of the Mission Leader should be open to all officers within Government, and through open advertisement.

2.3.2. *A dedicated Mission Execution Team in Government*

The Mission Execution Team is a dedicated team that is focussed on project implementation. A diverse set of skills are required for successful execution of complex projects. These skills include intimate familiarity with the Government processes, specialisation in verticals such as technology, outreach, law, as well as the ability to manage a large decentralized organization, among others. The Mission Leader should have full flexibility in hiring the Mission Execution Team, combining people from the public and private sectors. This team, including the Mission Leader, should have adequate tenure (at least 5 years) for purposes of continuity, so that institutional memory can be created and retained.

2.3.3. *Recruitment and tenure of the Mission Execution Team*

Professionals may be hired from within the Government, or from the private sector into the Mission Execution Team in a number of ways as indicated below:

1. Posting suitable officers to the project from the same cadre;
2. Inducting officers on deputation from other departments at suitable compensation under the Central Staffing Scheme; persons selected through this process should be given a tenure co-terminus with the project timelines, and be given all benefits of promotion while working on the project, so that they will not suffer on account of non-reversion to their cadre at the time of promotion; and
3. Infusion of talent from the private sector by way of lateral entry.

Other modes of staffing the Mission Execution Team that could be considered are as follows:

1. Hiring professional resources on contract basis;
2. Appointing consultants at market rates on contractual basis;
3. Recruiting sabbaticals from industry, who continue to be employed by the parent organization, but spend all their time on the Government project;
4. Recruiting volunteers who come from various walks of life through a well-defined volunteer selection process; and
5. Recruiting students from various colleges and universities as interns through a well-defined internship program

Given that a diverse mix of people may be inducted into a project, it is essential that all recruits should be made familiar with Government rules and procedures, perhaps through a short training course. With the exception of recruiting volunteers and sabbaticals¹, the rest of the methods of recruitment are provided for even now. The recommendations of the Sixth Pay Commission on contractual appointments² may be referred to in this context. These provisions should be more widely used for the five projects in view, and also other projects that may be launched in the future.

2.4. **Staffing of the NIU team**

An NIU, on the other hand, can hire professionals from the market at market salaries. Just as the Government team will have business specialists, and experts from other domains, so should the NIU have a management team with the right domain knowledge, and other essential expertise in areas such as technology, law, and outreach. The NIU should also take on its staff, professionals from the Department, who have the requisite business domain knowledge, so that the IT systems they develop and implement is backed by people with relevant domain experience.

2.5. **Database of IT Projects and Centres of Expertise**

The Group is of the view that the Government should set up a Database of all IT projects implemented in the public sector, including the PSUs. This database should contain comprehensive details of the individual projects and the key personnel associated with the project. Such a database will assist in identifying the IT talent available in the country, which can be tapped to meet the specific or general requirements of any

¹Hiring sabbaticals, volunteers, and interns at UIDAI: http://uidai.gov.in/index.php?option=com_content&view=article&id=154&Itemid=15

²Sixth Pay Commission (Paragraph 1.2.6): <http://india.gov.in/govt/paycommission.php>

similar project of national importance. Further, the task of drawing IT professionals on deputation from different departments and PSUs as also on contract basis from the private sector would be facilitated. Secondly, *Centres of Expertise* within the country would need to be identified for providing assistance by way of project consultancy through accredited professionals and advanced training in the field of IT management.

2.6. Capacity Building and retention of in-house staff

The Group suggests the following measures for capacity building in the departments embarking on large, complex projects with mission-critical IT systems:

1. The training curriculum for the existing workforce of various services should include training on the technical aspects of IT systems, project management and evaluation, procurement management, governance issues, and change management.
2. Mid-career programs should also be designed in such a way that senior officers are not only able to provide the required leadership but also coach and mentor junior managers.
3. All induction programs and furbisher programs for employees should include basic knowledge of IT systems, hands-on training in departmental IT projects and effective use of information flowing from Computer applications.
4. In-service personnel, who already possess technical knowledge should be trained in the latest technologies and in fields in which they like to specialize.

As regards retention of in-house staff on IT projects the following measures are suggested:

1. In-service officers deployed in IT functions should be provided with *IT professional allowance* on the lines of the training allowance at the rate of 30% of their remuneration. Such a provision is justified for the following reasons:
 - (a) In-service officers deployed in IT functions are entrusted with the important task of preparation of operation manuals and conducting of training programs for end users and the ICT aware staff on a continuing basis.
 - (b) These professionals are expected to possess specialised skills in evaluation, procurement, and management of technologies, and maintain communications with various stakeholders. The IT skills of these teams require regular refresh to enable them to engage meaningfully with IT vendors, optimize investment in IT infrastructure, and ensure that systems development remains aligned with business requirement.
 - (c) Such officers are part of the Mission Execution Team and have to put in long hours of work.
 - (d) Strong IT and domain skills in Government teams ensure that strategic control remains within the Government.
2. The Performance Linked Increment Scheme as suggested by the Sixth Pay Commission for Central Government employees, should be implemented supplementing the same with performance linked training programs in special skills.
3. A scheme of non-monetary incentives such as public acknowledgement of their contributions, certificates of outstanding performance etc. should be instituted with a view to motivating both in-service officers and contracted personnel.

4. Full opportunity should be provided for every individual to equip himself for higher levels of responsibility through individual and group assignment and training programs to ensure that his/her needs are satisfied. In order to enable employees to develop multiple IT skills, both technical and managerial, they should be provided with work diversity in different application areas and different technology. This would enlarge the opportunity spectrum available to the employees.

2.7. Conducive work environment

Other measures suggested for consideration for creating a conducive work environment are as follows:

1. The in-house end users of information systems, who are at the front end, are generally the least prepared to handle the change that is sought to be effected by extensive automation and e-governance techniques. Without user participation in planning the overall strategy of implementation and in-systems development and testing, it is difficult to buy their support and ownership of the system. End users should be able to assist in on line processing of work, get information from the system and also provide inputs for improvement. Such end users should be provided appropriate training and support and encouraged to make their own contribution to the success and continuous improvement of the project outcomes.
2. With a view to raising the motivation levels of in-house employees, creation of a proper work environment is a clear necessity. Towards this end, team formations should be done with care and thought so that those who are in the initial phase of their careers are placed along with supportive co-workers, who are willing to coach and mentor them. Managers should also be trained in coaching. Employees should be sensitized about the vision and values of the organization and encouraged to contribute towards realizing the same. Access to learning by choice in areas of interest to the employees and also useful to the organization and availability of feedback from managers in order to measure their contributions and gain greater control over their work should be part of creation of the right work environment.

2.8. Performance Appraisal

The discussions held by the Group have revealed that the present appraisal system within Government has several salutary aspects, such as filing of a resume by the employee and review by the higher authority. There are detailed instructions explaining the way the appraisal should be conducted. Yet, there is a widespread perception that the system is beset with shortcomings.

The Group is of the view that the method of performance appraisal has to be reconsidered, by redefining the purpose and principles, conducting a job analysis, obtaining employee feedback, reviewing standards of objectivity, conducting training for both managers and employees and reviewing/evaluating the results of the system. Greater objectivity and according appropriate weight to the overall contribution of the individual has to be given due consideration. Since increasingly, Government is undertaking tasks which demand greater professional skills, such as IT skills, merit should be given primacy over seniority within a given band of eligible appointees. Adoption of performance management techniques would be particularly relevant for appraising the performance of in-service officers entrusted with the task of implementation of mission-critical projects.

3

Contracting

3.1. Background

Many an IT project fails due to shortcomings in contracting. The contracting process defines the placement of tasks; which tasks are kept within Government, and which are outsourced. As discussed in Chapter 1, a contract for large complex project is likely to suffer from over-specification or under-specification, especially if there exists no precedent or proof-of-concept study. This chapter provides general recommendations for good contracting

A study on *E-Governance & IT Services Procurement: Issues, Challenges, and Recommendations*¹ has been published by NASSCOM. This includes a review of Government procurement guidelines, and highlights challenges from the Government's perspective as well as the industry perspective.

Contracting is a well-understood subject within Government. Nevertheless, the following general aspects that impinge on the relationship between the supplier and the Government merit a mention as they have equal relevance for a relationship in the nature of partnership or vendor customer model.

1. The solutions proposed by the supplier should focus on and meet the business needs spelt out by the Department owning the project and not just the technical/operational requirements.
2. Through the lifecycle of the project the supplier should produce realistic plans, including timeframes, resources, technology, mode of delivery and financials, and align the same with the business needs.
3. The supplier should as far as possible ensure continuity in employing trained personnel on the project from start to the steady State.
4. Both should share in a timely manner all information about technical/financial/personnel problems.
5. Both should set up a mechanism for co-operation and dialogue.
6. Both should agree and document change control processes, address risk factors and avoid informal and cosmetic changes.

¹E-Governance & IT Services Procurement: Issues, Challenges, and Recommendations (NASSCOM): <http://egovreach.in/index.php/pages/national>

7. Both should recognize that estimates of price, timeframes should be realistic and achievable.

3.2. Contracting with National Information Utilities

The success and timely completion of a project depends a great deal on the completeness of the contract. The ideal contract defines all requirements exactly, and addresses all possible contingencies — it is a risk management tool. Based on this ideal contract, the ideal firm can bid perfectly, and execute the contract as specified.

However, it is not always possible to achieve the ideal of specifying all requirements/contingencies with respect to complex IT projects right at the time of inception. Both over-specification or under-specification should be avoided.

As described in Chapter 1, NIUs work in the spirit of partnership with Government. The NIU is an intermediary of sorts, between the Government, and the IT vendors that build the project. An NIU-based approach is an incremental approach. An NIU approach also leads to a clean separation of roles in the steady State, where the Government focuses on policy, and the NIU focuses on implementation and execution.

The Government-NIU relationship can be defined through an Agreement. The Agreement outlines the broad project goals, placement of tasks, financials, SLAs, and most importantly, embodies the spirit of partnership. The Agreement should include the following:

1. Scope of work
2. Activities to be undertaken by NIU
3. Obligations of the Government and NIU
4. Financial Arrangement
5. Service Level Agreement
6. Business continuity plan upon exit

This relationship is further defined through ownership and governance structures for NIUs, which are set up as private companies with a public purpose. Even though the NIU is set up as a natural monopoly, the ownership and governance structures combined with the fact that it is set up to service just one customer at a pre-defined service level, act as the right checks and balances.

An example of the risk management methodologies adopted in the TIN Agreement is provided in Box 3.1.

3.3. Aspects to be covered in the agreement with NIU

The Agreement between the Government and the NIU should cover in clear terms all the aspects discussed in the succeeding paragraphs in this section.

3.3.1. *Scope of work*

The scope of work is a high-level functional (but complete) description of the project at hand. It clearly defines the tasks to be undertaken by the NIU, and defines the milestones and deliverables. Further details may be provided in other detailed specifications documents.

Box 3.1: Risk management in TIN

Income Tax Department (ITD) provided for adequate measures to ensure the quality of service in TIN. These measures included:

1. An Agreement signed with NSDL that covered:
 - (a) Scope of services by NSDL
 - (b) Responsibilities of NSDL and ITD
 - (c) Regular MIS to ITD
 - (d) ISO 9001-2000 certification for TIN processes
 - (e) ISO 27001 certification for NSDL Information Systems security practices
 - (f) Periodic Review of TIN operations jointly by ITD and NSDL
 - (g) Third party audit to monitor quality and security of the systems and processes established by NSDL
2. Service Level Agreement signed with NSDL to ensure that NSDL continues to provide services as required by the department.

3.3.2. *Activities to be undertaken by NIU*

In order to accomplish the tasks assigned to it, the NIU may be required to set up infrastructure and implement supporting processes. These activities should be defined at a functional level to the extent possible under this head.

3.3.3. *Obligations*

The obligations of both, the Government and the NIU should be articulated as clearly as possible in the Agreement. These obligations are necessary conditions for the success of the project, and will be monitored through SLAs.

3.3.4. *Financial arrangement*

Typically fixed-cost pricing is preferred for systems that have reached their steady State. However, the Agreement between the Government and the NIU is at a functional level, unlike traditional tendering, which is often at an implementation level. As a result, it is essential that outcome-oriented pricing be adopted. The pricing should be for the accomplishment of the business objectives on a per transaction basis. The onus is then on the NIU to figure out sizing, scaling, storage, capacity etc.

3.3.5. *Service Level Agreement*

Very strict and detailed SLAs are essential when Government contracts out a project to an NIU on the basis of an Agreement. It is only through SLAs that the obligations can be monitored, and the financial arrangement implemented. The agreement should allow for strict penalties if SLAs are violated. The Government should also appoint Independent auditors to ensure that the NIU continues to provide services as agreed upon.

3.3.6. *Business continuity plan upon exit*

In the event that the Government wishes to terminate the relationship with the NIU, there should be a business continuity plan outlined in the agreement. There should be

an elaborate continuity plan as per industry best practices to ensure that the project process does not get halted during exit of the vendor or during transition. For this purpose, the contract should lay down a clear handover/transition plan, the required logistics for transfer of hardware/software, migration of data, provision of a transition team, data security and confidentiality, among other things.

4

From startup to going concern

4.1. Background

The startup phase of a project may be defined as the phase from incubation to the point where a long-term institutional capacity is set up to manage operations on a regular basis. The challenges faced by a project during the incubation phase are very different than challenges faced in steady-state operations. The Government may have to play an active role during incubation, shifting to a largely regulatory role in steady-state.

Effective incubation can help the project rapidly get off the ground. The incubation phase includes issues that range from mundane issues such as setting up an office and hiring staff to devising incentive compatible solutions that are agreeable to all stakeholders.

This chapter presents a broad framework for incubation that can help projects get off the ground rapidly. An example of incubation recommendations made in the context of the NTMA is presented in Box 4.1.

4.2. Institutional framework for the project

One of the first steps in the incubation of a project is the creation of a suitable institutional framework. Depending on the nature of the project, it may either be housed within a Department, or in a new institution created with the specific purpose of executing the project. Various institutional frameworks that were examined in the context of NTMA are described in Box 4.2.

4.3. Incubation of a new National Information Utility

While a project itself may be housed within one of various available institutional frameworks, an NIU that serves the project should necessarily follow the structure as described in Chapter 1.

In the case that a new NIU is being created to support a particular project, it can be incubated within an existing NIU. Subsequently, when the project achieves some level of maturity, the project team and project assets (tangible and intangible) can be spun off

Box 4.1: Incubation of National Treasury Management Agency

A committee headed by Dr. Jehangir Aziz has proposed **Establishing a National Treasury Management Agency (NTMA)**. The report has been shared with regulators, State Governments and other relevant agencies for their comments. The report is essentially a Mission Strategy Document that discusses the need for the NTMA, the legal framework, stakeholders, and the process of incubation. It also includes a draft of the National Treasury Management Agency Bill. Chapter 8 of the report outlines the following steps for incubation:

1. The NTMA would commence operation as a non-statutory office of the Ministry of Finance, as was done in the early days of SEBI, IRDA and PFRDA. A mechanism will need to be arranged for MOF to give the NTMA a budget in this phase. The key tasks that need to be put into place at the outset are:
 - (a) Office premises
 - (b) Setting up an organisation chart
 - (c) Establishing an HR process; recruiting key individuals into this organisation chart
 - (d) Establishing the advisory board
 - (e) Setting up a series of outsourcing relationships
2. Establish databases about the Central Government's debt and contingent liabilities, along with a website
3. Establish a research and analytical capability
4. Plan out bond market processes and market mechanisms for bond issuance and trading
5. Stakeholder analysis and reaching out to market participants
6. Linkage of the NTMA IT platform with IT platforms of Government, exchanges, depositories, and investors
7. After the NTMA is set up, the core debt management functions can be transferred from RBI to the NTMA.

into the new NIU. The original NIU, in this case, should be compensated appropriately for the resources it deploys.

4.4. Mission Strategy Document

At the outset, the project should publish a Mission Strategy Document that describes the project, the stakeholders, the broad legal framework, the solution architecture, the nature of the platform and role of the ecosystem, and potential pricing. The strategy may evolve over time, but the guiding principles should be sound and remain unchanged. The process of creating such a document also helps set and manage the expectations of stakeholders, and ensures that the solution is designed in a way that is acceptable to all stakeholders.

The report of the Working Group on *Establishing a National Treasury Management Agency*¹ can serve as the Mission Strategy Document for the NTMA. The UIDAI published early on, the *UIDAI Strategy Overview*² that described the strategic vision, from which many aspects of implementation have been derived.

¹Establishing a National Treasury Management Agency: http://finmin.nic.in/reports/Report_Internal_Working_Group_on_Debt_Management.pdf

²The UIDAI Strategy Overview: http://uidai.gov.in/UID_PDF/Front_Page_Articles/Documents/Strategy-Overview-001.pdf

Box 4.2: Institutional frameworks considered for NTMA

In the report on **Establishing a National Treasury Management Agency (NTMA)**, the Working Group (WG) considered various institutional frameworks:

1. **An Executive Agency:** The WG recommends an Executive Agency as a sound interim step, but suggests that such a structure would face resource constraints, and risk being perceived as closer to the Centre rather than a neutral agent of Central and State Governments.
2. **A Company:** While providing flexibility and independence, the WG noted that regulatory certainty and predictability are crucial when an agency implements the Government's decisions on a core sovereign function such as debt management, and that judicial decisions on company law may affect this regulatory certainty.
3. **A Society or Trust:** These structures were rejected as impractical as they would limit the range of financial instruments that NTMA could deploy.
4. **A Statutory Body:** The WG recommended that the NTMA be a Statutory Body for the purposes of operational flexibility, accountability to Central and State Governments and to Parliament, financial expertise, and for the ability to prioritise public policy objectives rather than tactical trading objectives.

4.5. The right team

It is essential that the best teams be put in place within Government and within the NIU. This should be the first and foremost priority of all projects. The chapter on human resource issues (Chapter 2) describes general principles for putting a project team in place within Government and in the NIU.

4.6. Consultations with stakeholders

Consultations with stakeholders early on in a project is crucial to set it along the right trajectory. At a minimum, stakeholders include:

1. Multiple levels of Government, or other Government Departments
2. NIU
3. Banking system (if funds are involved)
4. Service providers whose services are essential for the project
5. Customers and end-users

Depending on the nature of the project, it may be necessary to hold consultations with various other Departments, trade associations, marginalized groups, etc. These consultations are necessary to ensure that an incentive compatible solution is designed, which is acceptable to all stakeholders.

4.7. Legal framework

A legal framework, with enabling policies may be necessary for a project to go live. This may require passing a Bill, modifying subordinate regulation in Central and State Acts, or in some cases, a constitutional amendment. A strong legal team working with all stakeholders is a must for every project.

4.8. Incremental rollout

The project should be rolled out as soon as possible, and iterated rapidly, rather than waiting to roll out a perfect system. This represents a recent shift in the way large IT projects are implemented today; the style having been popularized by modern internet firms processing millions of transactions daily. Such a rapid iterative rollout process makes it possible to get customer feedback early on, and allowing mid-course corrections as necessary. It also helps keep the project teams motivated and excited.

4.9. Government-NIU relationship during incubation

1. The Government should have a dedicated Mission Execution Team as described in Chapter 2. The Government's role is to set policy, co-ordinate with other departments, and provide strategic direction, whereas the NIU focuses on execution and implementation.
2. In the early stage, the Government agency / Department works alongside the NIU in an entrepreneurial spirit of trying to understand the challenges and design a system that will deliver results. Many research and development sub-projects and proof-of-concept studies may get initiated at this stage. The Government and NIU jointly define the requirements post these learnings.
3. As the system starts falling into place, the role of Government changes to:
 - (a) Conducting proof-of-concept studies
 - (b) Giving feedback on misfeatures, bugs and additional specifications
 - (c) Setting up the institutional capability for scaling
4. Once the rollout is completed, the Government's role shifts largely to that of a customer. It should compute metrics of performance of the system in all respects such as performance, cost, accuracy, and release these into the public domain. Quarterly reviews of the performance of the system should be undertaken at the highest levels. A variety of external experts should be brought in on a regular basis to study the functioning of the system, and to critique it along with proposals for improvement.
5. Even after these complex IT systems are fully running, none of these systems ever stand still. The very success of a project generates an array of areas where extensions are possible, and the magnitude of scale-up that can arise out of success can be quite dramatic given the size of India. A consultative process needs to be established for agreeing on new features of the system and ongoing change management.

5

Multiple levels of Government

5.1. Background

A class of national infrastructure projects have been implemented successfully today, which include a stock exchange (NSE), depository and Tax Information Network (NSDL) etc. This class of applications has typically had a single owner and could be Centrally implemented. A new class of applications such as GST, NPS, and EIN will span multiple levels of Government where Central, State, and Local Governments will all have jurisdiction and some role to play in successful implementations. This chapter deals with the concerns in the implementation of IT projects within a federal structure with multiple stakeholders, and recommendations to address those concerns.

5.2. Decentralized governance

Decentralisation of Government is a healthy feature of democracies when it produces a tighter link between accountability through elections and the delivery of local public goods. States have constitutional autonomy in certain areas under the Indian constitution. IT systems designed as a single application may be perceived to shift the balance of power within the federal structure.

Every Government at every level that is touched by an IT project is a stakeholder. Thus, a project such as GST that requires buy-in from all States, or EIN, which spans all levels of Government, is unlikely to succeed, if the IT systems are designed and operated by one of the Governments. There is always the fear that a non-transparent system, with control concentrated with some of the stakeholders may affect the autonomy of the others. This may happen in subtle ways due to inefficiencies, delays, and errors, which are not uncommon in complex IT systems in early stages. A critical aspect of the success of such IT projects is that the solution must be incentive compatible for all stakeholders. Common functions should be included in a single application shared by all stakeholders.

IT projects that span multiple levels of Governments may be classified into two types:

1. Projects such as GST, NTMA, and EIN where the NIU aids the core function, or aids carrying out a sovereign function of multiple levels of Government.

Box 5.1: Solution design for GST

The Common GST Portal has been designed as follows:

1. Common minimum functionality (PAN registration, standardized return filing, and standardized challans for payments) is built into the Common GST Portal
2. Only information flows through the Common GST Portal, whereas funds flow through the banking system
3. Given that GST will be an important source of revenue, the funds arrive in almost real-time from the taxpayer, through the banking system, into the State and Central Government treasuries. Thus, the constitutional autonomy of all Governments is respected by the IT system design.
4. The Common GST Portal passes the information on returns and challans immediately to the tax administration systems, while enhancing this information with intelligence gathered from matching returns
5. The design and implementation of the Common GST Portal has started while policies such as tax rates are being debated and the legal framework is being put in place

2. Projects such as NPS, where the core function is carried out by a Central agency, but co-operation among Government agencies is required for the purposes of uniformity, standardization, interoperability to maintain levels of service and drive economies of scale.

5.3. Need for a single application

IT systems naturally lend themselves to development as a single application developed by one team. A single application may be deployed in a decentralized environment, but its development must necessarily be centralized.

IT systems developed as a single application encourage standardization, drive economies of scale, higher efficiency and increased productivity. Systems thus developed are efficient in the use of public funds, which otherwise may be spent on multiple platforms implementing similar but incompatible technologies multiple times. Such systems can be developed so that they can be customized at every deployment point, but it still operate as a unified application. This also offers a uniform customer experience for all interactions with Government.

As communication networks become more pervasive, technology solutions are getting increasingly centralized. As an example, rather than storing email on their PCs, people prefer to have their email on the web, and find it convenient to access it anywhere. Banks have moved from distributed branch automation software to Core Banking Solutions (CBS) over the last twenty years. This does not necessarily mean that the software runs in one data centre only. On the contrary, every branch runs an extension of the CBS software itself.

5.4. Solution design for multiple levels of Government

Solutions for projects that involve multiple levels of Government need to be designed carefully. Not only is it necessary to manage stakeholder concerns and incentives, but it is also necessary to ensure that the solution respects the constitutional autonomy of all levels of Government involved in the project. Increasingly, projects that span Central

and State Governments are being undertaken, and going forward, projects that span Central, State, and Local Governments will be undertaken.

Projects spanning multiple levels of Government require consensus building that may take time. Various Governments may also have to create the right legal framework for the project to operate in. The design and implementation of the solution itself takes a long time. These two activities, consensus building and solution design need not necessarily be sequential. The basic design and the nuts and bolts of the implementation can be put in place while policy details are being debated. Eventually, the policies agreed upon are only an input to the solution, and will change from time to time. Work on actually building the IT systems should thus start at the earliest possible date, while policies are reflected within the solution as consensus is achieved.

As mentioned earlier, such projects should also be implemented as a single application while respecting the constitutional autonomy of all Governments involved. Common minimum functionality can be built into a Common Portal, in such a way that its basic functionality can be enhanced by local customizations such as look and feel, local languages, and local policies, to mention a few. Such a design allows for low cost, scale, interoperability, speed, simplicity, a uniform customer experience, and portability of service. The application of these design principles for the Common GST Portal are described in Box 5.1.

5.5. NIU approach to align incentives

The committee recommends the following for projects that span multiple levels of Government:

1. Clearly identify all stakeholders.
2. Form an Empowered Committee of representatives drawn from every stakeholder for all decision making. If this Empowered Committee is large, a smaller Empowered Group may be appointed for carrying out the day-to-day business.
3. Form an NIU for implementation of the IT system.
4. All levels of Government that are participating in the project may become owners of the NIU, so that they have an equal say in the way the NIU conducts its business.

A joint ownership structure as described above helps align incentives across stakeholders and build consensus by giving them an equal say in decision making, and insuring against an uneven distribution of control favouring one stakeholder over another. A common single application also saves costs and dramatically reduces complexity for all stakeholders, while allowing customization and extension as necessary. An example of this strategy in the case of GST is described in Box 5.2.

In the case that all State Governments and Central Government are owners, the Board of the NIU may end up having too many members. The Board may be, in such cases, comprised of about ten members, with equitable representation of Centre and States. The States may also be represented by rotation and by a body that represents all States. Various committees are also necessary to overlook various aspects of the project, and nominees of all States should be co-opted into these committees.

Getting the governance structure of the NIU right calls for a delicate balance. On one hand, Governments by virtue of their shareholding, are owners. On the other hand, the same Governments are customers. For a typical firm, owners and customers are not the same. Thus, if owners are unhappy with the management team, they can terminate the relationship. If customers are unhappy with the service, they take their business elsewhere. However, if one of the owners is also the customer, these checks and balances may not be as effective as otherwise. The recommendations in Chapter 1 on ownership and governance structures of NIUs take these issues into account.

Box 5.2: Goods and Services Tax Network (GSTN)

GSTN is an NIU that is being set up to serve multiple levels of Governments (Central and State) in GST:

1. The Empowered Committee of State Finance Ministers (EC) has appointed an Empowered Group on IT (EG-IT) to oversee the IT implementation at an operational level. The group has created high-level IT plan: **The IT Strategy for GST**, which has been embraced by all stakeholders
2. The IT strategy for GST called out for the need of a Common GST Portal to implement common functionality
3. A team within Ministry of Finance is working on the legal framework necessary for GST
4. A new NIU (GSTN) has been proposed to operationalize GST
5. Upon evaluating current NIUs such as NSDL and NPCI, the Ministry of Finance has decided to incubate GSTN within NSDL
6. It has been proposed by the EG-IT that GSTN be set up as a Section 25 Company
7. The EG-IT has also recommended that Centre and States would have equitable representation on the Board which should comprise of about ten members. The States could be represented by rotation and also by EC (or its successor). In case the funding of the States was routed through EC (or its successor), the Empowered Committee would be considered as the representative of all the States, for all compliance purposes. To ensure participation of a larger number of States in the governance of GSTN, the Board would be supported by additional Committees in which nominees of other States could be co-opted.

5.6. Building a coalition for change

The execution of large complex projects such as GST, EIN, NPS etc. require building a coalition of change. IT, although a major component, is not the only component. Such large scale computerization often involves business process re-engineering. When such sweeping changes are being carried out, inevitably enough, in the larger interests of certainty and uniformity, some of the stakeholders may have to give up some restrictive practices, while some others may have to adopt certain regulation as against their existing regime. Particularly in the context of GST, an additional consideration may be that of encouraging a common market and freer movement of goods and services. With a successful coalition for change, such large and complex projects are more likely to succeed.

Stakeholder analysis is an important step in building such a coalition. Once stakeholder analysis is conducted, incentive-compatible solutions can be built. It is recommended that the project release a Mission Strategy Document that guides the implementation going forward. The process laid out for incubation of Government projects and NIUs in Chapter 4 is designed to foster a coalition of change early on in the life cycle of a project.

Success of large complex projects such as the five unique projects under consideration depends on much more than getting the IT right. Building a coalition for change greatly increases the odds of success, especially in projects involving multiple levels of Government. Some of these approaches are being tried in the implementation of GST (Box 5.2).

Part II

Technology challenges

6

Solution architecture

6.1. Background

The solution architecture of a complex IT project is an important factor for the success of the project. This chapter focuses on retaining strategic control of the project within Government, by working closely with the implementation team on designing the right solution architecture.

The Group deliberated on good software development practices such as project planning, milestones, development frameworks, quality assurance, and user acceptance testing, among others. Given that many of these are implementation level details, which are well understood within industry, and may vary from project to project, the Group is of the opinion that individual projects should make their own choices on software development processes. The Group also does not touch upon common and well defined practices for mission-critical applications such as disaster recovery centres, high availability, 24-by-7 operation, and fault tolerance; these architectural design principles are well understood by software designers and architects. Some of these issues are discussed in the *Guidelines for Strategic Control in Outsourced Projects* released by the Department of Information Technology, Government of India¹.

6.2. Essential elements of a solution architecture

6.2.1. Map out a long term IT strategy

At the outset of a project, the IT strategy should be conceived and published as part of the Mission Strategy Document as described in Chapter 4. A functional system diagram should be created that captures the following at a conceptual level:

1. Role of multiple levels of Government
2. Key business processes and workflows (information flow, funds flow, etc.)
3. Integration with various stakeholders

This forms the basis of the solution architecture, and serves as a guide for implementation level details.

¹Guidelines for Strategic Control in Outsourced Projects: http://www.mit.gov.in/sites/upload_files/dit/files/Guidelines_Strategic_Control_Outsorced_Projects_251110.pdf

Box 6.1: Change management in TIN

The project was subdivided into a number of small components and specific milestones were identified for these components so that the project could be monitored on a regular basis against specific deliverables.

1. **Compulsion to File Returns in Electronic form:** When the new scheme was introduced in FY 02–03, only corporate deductors were required to file returns in electronic form. From FY 04–05, it was made mandatory for the Government deductors to file the returns in electronic form. More segments of deductors were brought in to the mandatory list in due course of time.
2. **Quoting of PAN and TAN in tax payment instrument:** To begin with, taxpayers were allowed to deposit their taxes even without quoting of TAN/ PAN in their challan. Once the system for issuance of TAN and PAN stabilized, ITD made it mandatory for the taxpayers to quote TAN / PAN in the tax payment challan. Today, more than 98% of TDS challan have valid TAN and 95% of non-TDS challan have valid PAN.
3. **Preparation of e>Returns:** A simple ASCII text-based file format for submission of e>Returns was published. Any software designer or platform provider could prepare returns in this format. A free return preparation utility was launched, so that small deductors would not have to incur a cost in buying software. A platform independent file validation tool was made freely available, so that filers could verify their returns before submission.
4. **Return Acceptance:** The filers could either upload the returns directly to the TIN system on the internet or submit the return to any of the TIN facilitation centres across the country.
5. **Upload of challan details by banks:** ITD also prescribed a standard ASCII text-based file format for upload of challan details to TIN. A platform independent file validation utility for challan files was provided to the banks. Banks were provided the flexibility to upload the challans through leased line connections that they had with NSDL for depository operations, or use dial-up PSTN/ISDN links, or use the internet.

This approach is being followed for the implementation of GST, where *The IT Strategy for GST was defined and accepted within Government even before the NIU was selected. The report of the Working Group on Establishing a National Treasury Management Agency*¹ and the *UIDAI Strategy Overview*² are also examples of Mission Strategy Documents that describe the solution architecture at a high level.

6.2.2. Structured change management

Business process re-engineering (BPR) is essential to the success of an IT project. When a large number of organizations and disparate user segments are involved, it is important to phase the re-engineering. Changes that are most critical for efficiency can anchor the transformation process. A structured change management process should be put in place, so that the process is incremental. A principle of least surprise to the user, so that minimal change in user behaviour is required, is a good principle to guide the change management process. Box 6.1 describes an example from TIN.

6.2.3. Reflection of policy changes in IT systems

Changes in policy should be accompanied by the corresponding changes in IT systems; the two should go hand-in-hand. For projects that depend on mission-critical IT systems, if policies cannot be implemented using the IT system, it may be difficult to enforce

¹Establishing a National Treasury Management Agency: http://finmin.nic.in/reports/Report_Internal_Working_Group_on_Debt_Management.pdf

²The UIDAI Strategy Overview: http://uidai.gov.in/UID_PDF/Front_Page_Articles/Documents/Strategy_Overview-001.pdf

Box 6.2: Interoperability among depositories

Depositories are established under the Depositories Act, 1996. Initially, there was only one depository, NSDL. Over time, as the concept was accepted, and markets took off, CDSL (another depository) was created. Even though NSDL started out as the only depository, competition emerged over time. The fact that the Securities and Exchanges Board of India (SEBI) required interoperability among various depositories ensures that the customers and the ecosystem are not affected when competing depositories are created.

them practically. Thus, when a change in policy is planned, the teams responsible for the IT systems should be consulted. The policy change should then be announced when the modifications in the IT system have been completed.

6.2.4. Data quality

As the saying goes “garbage in, garbage out”; an IT system is only as good as the data it consumes. The system design should have a self-cleaning mechanism. For example, the UIDAI proposes to authenticate the identity of a resident based on data they have provided during enrollment. The system is self-cleaning, because it is in the resident’s interest to ensure that the system has correct data, in absence of which he cannot authenticate his own identity. Similarly, TIN has seen a gradual increase in data quality over time, as taxpayers realized the benefits of electronic filing and electronic payments.

Further, clean data can be ensured by standardisation of processes, matching and verifying information in workflows, simple and well defined open data formats, electronic payments and processing, instant feedback to customers, incentives for compliance, and penalisation for non-compliance. It is through incentives that data quality can be managed, rather than micromanagement of stakeholders.

6.2.5. Vendor neutral solution

The solution architecture should be vendor neutral. Open standards should be adopted and open source should be used as prudent. In the case that specialised software components are used, the project should define an open standard and require vendors to comply. Multiple vendors can also be selected for such components. Issues relating to openness are discussed further in Chapter 7. It is for this purpose that both, the teams within Government and in the NIU, should include technology experts. A vendor neutral solution architecture also makes it easy to change NIUs or vendors if necessary. A credible threat of migration also ensures competitive pricing.

6.2.6. Interoperability and multiple providers

Interoperability among multiple service providers is essential to foster competition in the long run. This can only be achieved if interoperability is built into the system architecture from the outset. Projects that are implemented with NIUs essentially establish natural monopolies in the early stage. Once the requirements are well understood and the ecosystem has formed, there may be justification for competing firms. The example from depositories (Box 6.2) illustrates this point quite well.

6.2.7. A platform strategy

A large complex IT project touches a number of stakeholders. It is desirable that such projects employ a *Service Oriented Architecture* in their design. This makes it possible for

Box 6.3: A platform strategy in banking

A bank account is a great example of a platform strategy. A bank keeps a bank account in its core banking platform. This account may be accessed in a number of ways:

1. At the bank branch
2. Through mobile phones using m-banking
3. Through phones using IVR systems and call centres
4. Through the internet using computers, smart phones, and tablets
5. Through ATMs
6. Through debit cards
7. By payment processors to enable merchant transactions
8. By billers for the purposes of automatic billing

If bank accounts were not designed following a platform approach, it would not have been possible to access them through so many channels.

an ecosystem to evolve around standards and services provided by Government. The example of open file formats published by NSDL for e>Returns and e-challans in TIN (Box 6.1) are a good example here. It ensured that the end customer had multiple options to prepare returns. There was no lock-in of a particular software or service provider. Many independent software providers could create new software bringing in competition. At the same time, existing financial accounting software packages could support the new file formats effortlessly. An example from banking is described in Box 6.3.

6.3. Essential public goods

Almost all projects within Government, and the citizens at large will benefit from the essential public goods of connectivity and payments. The Group recommends that Government should make it a top priority to provide connectivity and banking facilities ubiquitously.

6.3.1. Connectivity

The Group's conceptualisation of a platform approach to service delivery entails that at the front-end, the data entry and retrieval architecture must be real-time and ubiquitous. In order to enable this, data connectivity at the front-end is critical. The front-end would include Government offices in tier 3 and tier 4 locations as well as Local Governments in rural locations for services such as e-procurement and payroll. For services such as TIN, PAN, and other Government-to-citizen services, the front-end would also include non-Government facilitation centers.

Connectivity in the country has improved by leaps and bounds. The Government has launched various initiatives to ensure last mile connectivity across the country. The recent acceptance of Aadhaar for satisfying proof of identity and address for all telecom connections by Department of Telecommunications will also ensure greater telecom inclusion².

²Aadhaar as proof of identity and address for telecom connections: http://uidai.gov.in/images/FrontPageUpdates/2011117_114142_telco_notification.pdf

6.3.2. Banking system interface

For all services that entail payments to citizens, the last mile interface is the weakest link. An efficient payments and transfers system warrants bank connectivity to every individual and institution, including those in remote rural areas. In the absence of bank accounts, payments have to be effected via an intermediary, which in turn creates room for leakages. With a universal bank account, it can be mandated that payments are made directly into bank accounts. In order to achieve this vision of all payments being universally routed through a bank account, the following are proposed:

1. **Account opening:** Access to bank accounts should be universal. Although the KYC guidelines are largely enabling, more effort in account opening needs to be undertaken. The recent acceptance of Aadhaar as proof of identity and address for opening bank accounts can help accelerate financial inclusion³. In the absence of a bank account for every individual, the ability to accurately ascertain individual level outcomes of payments made is not there.
2. **Unique identification of individuals and firms:** We need to minimise errors in identifying individuals (as beneficiaries under various schemes) and firms and ensure foolproof ways for transactions to be authenticated. Dovetailing efforts with the Aadhaar initiative can ensure that payments can be sent electronically by various Governments directly to beneficiaries on the basis of their Aadhaar using an *Aadhaar payments bridge*. Further, microATM and mobile-based person-to-person payments can be simplified by giving concrete shape to the approved framework of the *Inter-Ministerial Group for delivery of Basic Financial Services*⁴. For firms, the PAN has emerged as the unique identifier. All submissions by individuals and non-individuals that involve money transfer and payments should be made electronically and they should be authenticated and validated immediately, to the extent possible.

The Government should closely work with all stakeholders to define a uniform banking interface for Government, so that inter-Government payments may be tightly integrated with internal processes within Government.

³Aadhaar as proof of identity and address for opening bank accounts: http://uidai.gov.in/images/FrontPageUpdates/notification_regarding_aadhaar.pdf

⁴Report of the Inter-Ministerial Group for delivery of Basic Financial Services: <http://www.mit.gov.in/content/Government-approves-framework-provision-basic-financial-services-through-mobile-phones>

7

Openness

7.1. Background

Openness should be an integral part of Government projects. This chapter refers to openness of technology. Openness in technology can refer to the open standards, open data, and open source. The project management team should actively pursue openness at all stages of the project implementation.

Openness is a two-way street. On the one hand, Government, as the producer of public goods funded by taxpayers should define open standards, and release open data in open file formats, along with open source software to the extent possible. On the other hand, the use of open standards, open data, and open source within large complex IT projects brings down costs, leads to higher competition, and increased transparency in implementation.

The Mission team within Government should be committed to the principle of openness to the extent possible. The Department of IT has also released a *Policy on Open Standards for e-Governance*¹, which can serve as a guide for openness.

7.2. Open standards

The use of open standards in the design and implementation of open standards is highly desirable in IT systems. Multiple vendors provide competing solutions that can be used interchangeably with open standards. For example, all major database vendors provide databases that can be used interchangeably. However, most vendors will also provide proprietary extensions that lead to vendor lock-in. The system design must be done carefully, fully adhering to open standards.

While Department of Information Technology notifies national policies on standards from time to time, a project should publish domain specific open standards to cultivate an ecosystem. It is important to note that these new open standards are not devised in a top-down approach, but are created out of necessity, and from practical experience. Examples from UIDAI on publishing new open standards are mentioned in Box 7.1.

¹Policy on Open Standards for e-Governance: http://egovstandards.gov.in/approved-standards/egscontent.2010-11-12.9124322046/at_download/file

Box 7.1: Open standards at UIDAI

The UIDAI has deployed open standards in the design and implementation of its IT systems, as well as released open standards relevant to its core mission. For the core mission of UIDAI of collecting demographic and biometric data of residents to issue Aadhaar numbers, the following standards have been published:

1. **Demographic data standards:** The UIDAI published standards for the collection and storage of demographic data in the **Demographic Data Standards and Verification Procedure Committee Report^a**, under the chairmanship of Mr. Vittal^d. This includes standardization of the data fields to collect and store name, address, date-of-birth, and gender.
2. **Biometric data standards:** The UIDAI published standards for the collection and storage of biometric data in the **Report on Biometrics Design Standards for UID Applications**, under the chairmanship of Dr. Gairola^b.

^aDemographic Data Standards and Verification procedure Committee Report: http://uidai.gov.in/UID_PDF/Committees/UID_DDSVP_Committee_Report_v1.0.pdf

^bReport on Biometrics Design Standards for UID Applications: http://uidai.gov.in/UID_PDF/Committees/Biometrics_Standards_Committee_report.pdf

7.3. Open data

The Government, as a producer of public goods should release data in well-defined formats electronically, when possible, as prescribed by the *Right to Information Act, 2005*. Open data can become a foundation for a number of transformational IT projects in Government. Innovative firms and individuals can combine various types of data to glean new information that may not have been possible from the individual datasets.

Open data is already released by various Government agencies. One example is the Department of Statistics, under the Ministry of Statistics and Program Implementation, which releases various statistics based on surveys and compiling the national accounts. This can be emulated throughout Government. There is a need of a much greater scale of release of unencumbered data, placed into the public domain, of information created within Government.

There can be economic data, map data, census data, pollution data, water data, soil quality data, climate data, PIN code data, administrative boundaries data, health data, Government accounts data, etc., which is released by the relevant ministries. Early international experiences¹ of releasing open data using open file formats have resulted in mashups, which combine data from multiple sources and present it in ways that yield new insight, have been encouraging.

Open data can become the foundation of a transparent and accountable Government. Thus, it is important that the designers of IT systems keep open data in mind. This point is elaborated further in Chapter 9.

7.4. Open source

Open source refers to providing the source code of a computer program in the public domain, for others to examine and use. Today, entire operating systems, desktop software, office productivity suites, and server software are examples of software that are available as open source.

¹Release of open data using open file formats: US (<http://www.data.gov>) and UK (<http://data.gov.uk>).

There are some who believe that in cases where open source software is available, no commercial software should be used. This can sometimes be counter-productive, since there may be cases when commercial software is better suited than the open source versions. It is not a good idea to force the use of specific software of any type; instead, the focus should be on adopting open standards, and using open source as prudent.

The Mission Execution Team in Government should also ensure that components of a project that may be reusable by other projects are released as open source software. While some may argue that the Government should open source the entire project, the Group recognizes the intellectual property of the NIU. The committee also recognizes that it may be counter-productive to the business planning and profitability of the NIU to release all source code as open source. The Government and NIU should work together from the early phases of the project in deciding what components can be open sourced.

In summary, there are enormous benefits from both using open source that is available off the shelf, from participating in the development process of existing open source software so as to extend existing open source systems into superior functionality (while feeding these extensions back into the public domain), and from releasing new open source systems. Every IT system in Government will benefit from pushing in all these three directions. At the same time, these three approaches should not become an inflexible dogma.

7.4.1. *An Open Source Foundation*

Today, the major impediment to Government projects releasing source code is the lack of a proper process for open-sourcing applications and housing them. The existence of an open source foundation, along with a well-defined process to release open source software can help drive the creation of an effective e-governance software stack.

The Group suggests that the Government in partnership with concerned stakeholders should set up an open source foundation² to host open source software released by Government projects.

²Some examples of open source foundations are the Apache software foundation (<http://www.apache.org/foundation/>) and Eclipse foundation (<http://www.eclipse.org/org/>).

8

Information security

8.1. Background

As the use of mission-critical IT systems becomes widespread within Government, the growing connectivity between these information systems, the Internet and other infrastructure, create opportunities for increasingly sophisticated attacks on such systems. Such attacks may be made by individuals, non-state players, as well as by hostile Nations. It is therefore essential to ensure that any disruptions of critical Government information systems are contained and managed effectively to minimize their impact. The security team for important projects must be best in class, and the security solutions must always be cutting edge at all times.

Information security breach may include consequences such as financial losses, systems being rendered unusable, intellectual property theft, damage to the organization's brand and reputation, and legal exposure or lawsuits, among others. These consequences may be on account of: confidential records or sensitive information being compromised or being made unavailable, identity theft due to customer or employee information being stolen, modification or alteration of the operating system programs, software applications, files, data etc., or crippling of infrastructure such as networks and applications.

These concerns are heightened when aspects of national security also come to the fore, an example of which is described in Box 8.1.

8.2. Institution-wide support for information security

Security is widely regarded as a hygiene factor which comes to fore only in times of disaster, while in organizations that manage security well, the ownership of security vests at the highest levels of governance. Without the visible support of senior management it may not be possible to actually implement the required security framework, ensure compliance by users and elicit co-operation.

Implementing security is often considered a one-time activity, which is effectively discharged when funding approvals are accorded for a technology stack. It is often perceived that having a set of information security tools will ensure adequate protection for a reasonable period of time. Even as implementing teams close all the known

Box 8.1: Geo-political nature of attacks on IT systems

Stuxnet is an Internet worm that infects Microsoft Windows computers. It primarily spreads via USB sticks, which allows it to get into computers and networks not normally connected to the Internet. Once inside a network, it uses a variety of mechanisms to propagate to other machines within that network and gain privilege once it has infected those machines.

Stuxnet doesn't actually do anything on those infected Microsoft Windows computers, because they are not the real target. What it looks for is a particular model of Programmable Logic Controller (PLC) made by Siemens. These are small embedded industrial control systems that run all sorts of automated processes: on factory floors, in chemical plants, in oil refineries, at pipelines, and in nuclear power plants.

If it does not find one, it does nothing. If it does, it infects the PLC using what was then an unknown and unpatched vulnerability in the controller software. The changes made by Stuxnet are very specific, targeting a specific group of PLCs, leading many to believe that Stuxnet's authors had a specific purpose in mind.

Stuxnet does not act like a criminal worm. It does not spread indiscriminately. It does not steal credit card information, or account login credentials, nor does it herd infected computers into a botnet. It does not threaten sabotage, like a criminal organization intent on extortion might; it performs sabotage. The damages due to Stuxnet have also been compared to a military operation.

Analysis of the worm suggests that it was expensive to create. It is estimated that a team of talented programs developed it over a period of six months, in a laboratory setting.

Source: Forbes magazine (Oct 2010), New York Times (Jan 2011)

weaknesses and gaps, intruders develop new and more sophisticated methods of attacks. Thus the information security landscape is dynamic in nature and techniques that worked at one point may not suffice for the current year. Often a regular high level review and monitoring framework is not in place, leading to a reactive rather than proactive approach to information security.

Within the NIU framework suggested in this report, security should be given utmost importance by the Mission Team within Government, and by the management team at the NIU. A Chief Information Security Officer (CISO) should be appointed who is empowered and fully responsible for all aspects of information security: technology, processes, and people (Figure 8.1).

Security must be part of the ethos of the organization, and can only be achieved when the entire organization (right from senior management to field personnel) is geared for it. This requires training and awareness on basic facts about information security (strong passwords, how systems are hacked, denial-of-service attacks, social engineering, de-mystifying jargon etc.) all levels.

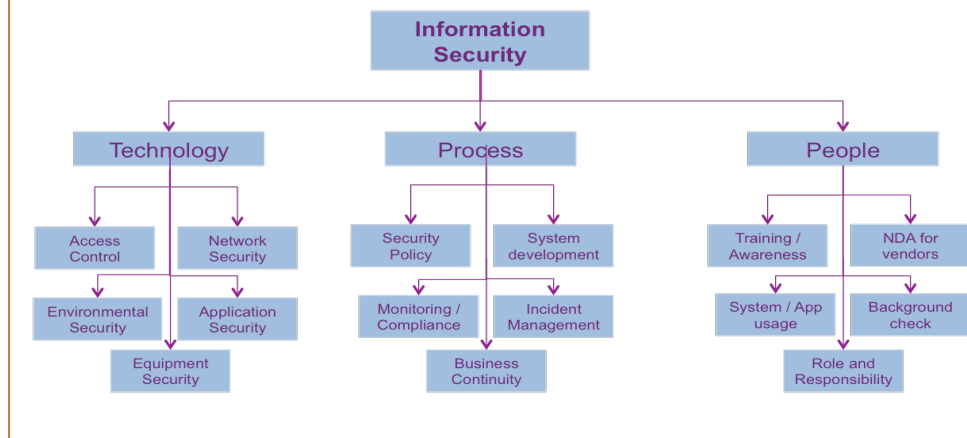
Getting certified for various standards, and audited by independent security auditors help provide the CISO with a basic understanding of the level of security within the organization. It is essential, that as problems are identified, not only the symptoms are treated, but the root cause of the problems are also identified and processes are put in place to avoid them in the future.

8.2.1. Certification

Various international standards and best practices can be customized to define a comprehensive certification framework:

1. The ISO 27001 is a formal management system that brings information security under explicit management control.
2. ISO 15048 (Common criteria) provides a basis for verifying security functionality of IT products as well as ensuring that they are free of trap-doors etc.

Figure 8.1: Controls for information security



3. BS 25999 provides guidelines for the implementation of disaster recovery and business continuity management framework.

Some of these certifications are expensive to achieve, and although they provide a broad framework to evaluate security of an IT system at large, they are by no means sufficient.

8.2.2. Audits

Audits are performed by an independent third party, and thus provide an independent evaluation of the security of an IT system. The scope of audits may include:

1. **Technology review:** which covers all the technology components of the IT project such as
 - (a) **Ethical hacking:** Vulnerability assessment and Penetration testing of the network
 - (b) **Application Security:** Application security audit to identify known vulnerabilities and source code review:
 - (c) **Design Review:** Review the IT architecture from security point of view and identify single point of failure.
2. **Process Review:** Review should cover all the process related to security adopted by the IT project such as change management, Log review, access control etc
3. **Third party review:** Review the security controls deployed by the third parties on the Government data/information

8.3. Solution architecture and information security

Security should be an integral of the solution architecture, and not an afterthought. The following ideas can help guide the design of the solution architecture from a security perspective:

1. **Identity, access and entitlement management:** Providing authentication and authorization services are the core objectives of this control. It ensures that right people have access to right resources. Having access to fewer resources than necessary for a particular task hampers productivity, while access to more resources than necessary introduces risk.

2. **Host access management:** A dedicated host access management solution greatly strengthens the security of mission-critical servers. Such a solution can improve security, simplify and reduce the cost of server administration, and provide significantly improved audit capability needed to address regulatory compliance and security best practice requirements.
3. **Data encryption:** Encryption of data ensures that information stored in the system (referred to as plaintext) is transformed into an unreadable form using an algorithm (called ciphertext) for anyone except those possessing special knowledge, usually referred to as a key. This helps in providing assurance of confidentiality of information, even in cases of unauthorized access.
4. **Data hashing:** Hashing of data ensures that any alteration to even a bit of data drastically changes a special fixed length code called hash, created from the original data stream. This helps in providing integrity assurance to trusted set of information. Passwords and other sensitive information are often stored only as hashes, so that access is granted only if the generated hash matches a stored hash.
5. **Data classification and data loss prevention:** : Data Loss Prevention (DLP) systems are designed to detect and prevent the unauthorized use and transmission of confidential information. DLP increases the effectiveness of existing controls by minimizing inadvertent and malicious data loss, and will empower the organization to comply with various data protection regulations. It provides a customizable level of control at critical areas throughout the Organization — at the endpoint, the network, the message server and for stored data.
6. **Transaction audit:** It is imperative to analyse transactions for anomalous behaviour as well as to collect sufficient forensic data for each transaction so as to enable the monitoring engine to establish the difference between a normal transaction and a fraudulent transaction.
7. **Interaction security:** At interaction level, it is necessary to ensure that security is taken care of at each interaction point that includes people-system interaction as well as system-system interaction. All workflows and business processes should be developed keeping security in mind. All the interactions must be under audit and audit trails should be secured. There must be clear and specific security policies that define roles and responsibilities for all interaction in the organization.

8.4. Threat to information security from insiders

Projects that depend upon mission-critical IT systems may have a number of employees, and an order of magnitude larger number of customers. Employees are given privileges within the system to enable them to carry out their daily functions. It has been observed in a number of cases that security is often at risk due to insiders having authorized access, but use this authority in ways that are malafide. A security-conscious design of the solution architecture, combined with a dedicated CISO and security team are essential to combat not only external security threats, but also security threats emanating from within the organization.

8.5. Legal framework governing information security

In order to deal with information security crimes, the Information Technology Act, 2000 (hereinafter, referred to as IT Act, 2000) was passed, covering inter alia:

1. Legal Recognition of Electronic Documents
2. Legal Recognition of Digital Signatures

3. Offenses and Contraventions
4. Justice Dispensation Systems for Cyber crimes

The Information Technology Act, 2000, was further amended through the Information Technology Amendment Act, 2008 (ITAA 2008). ITAA 2008 addresses the emergence of various types of cyber-crime, such as identity theft and the creation of malicious computer code. This Act provides the legal framework to promote IT in the country and:

1. Empowers Government to accept filing, creating and retention of official documents in the digital format.
2. Provides for legal effect, validity and enforceability of electronic records.
3. Provides for the authentication and origin of electronic records and communications through digital signature.
4. Provides a more exhaustive coverage of cyber crimes in law.

Some other Acts (and their associated regulations) which Government organizations are required to comply with (apart from the statutes governing the concerned Departments), include Indian Evidence Act 1872, Official Secrets Act 1923, Indian Copyright Act 1957, and Right to Information Act, 2005.

8.6. National level considerations

The Group has suggested a security-conscious design of the solution architecture, a dedicated security team headed by a CISO, and basic security training for all employees to tackle internal and external security threats to a project. There is merit in sharing information and learnings across various Government projects, and co-ordinating across projects in case of large-scale attacks on various systems. The security teams of individual projects should integrate with existing agencies set up by the Government such as CERT-In¹, and with other frameworks that evolve over time.

¹Cert-In (<http://www.cert-in.org.in/>) is the national nodal agency for responding to computer security incidents as and when they occur.

9

Accountability, transparency, and self-corrective forces

9.1. Background

The passage of the *Right to Information Act, 2005* (RTI Act) that guarantees citizen access to nearly all Government information not deemed to be critical for national security, has caused a sea change in how citizens interact with, and monitor, Government.

If deployed effectively, information technology has the potential to serve as a powerful tool to bring about transparency and accountability of Government services. Yet, increased transparency and accountability is by no means a guaranteed outcome of a Government IT project. IT projects which are not designed with an explicit objective of increasing transparency, which lack a clear channel through which the IT system will increase transparency, or which fail to take into account the interests of the various stakeholders in the IT system will fail to increase transparency or accountability.

9.2. What to share

The Group recommends that designers of Government IT systems take a pro-active stance in deciding which information to share publicly. As a large share of the information collected by the Government must be provided according to the provisions of the RTI Act, proactively sharing data can obviate the need for responding to RTI requests on an individual basis, while also making it easier for citizens to access this data.

9.3. Solution architecture and transparency

The architecture of an IT project must be designed keeping a transparency portal in mind. A large IT project produces large volumes of data daily. If a transparency portal is designed as an afterthought, the end result may be lack-lustre.

Typically, the same software architecture for data warehousing, data mining and business intelligence required within an IT project for policy support and analysis can

also support the operations required for a transparency portal. Even though a portal is created with basic analytical capabilities, all the data should be made available in simple, well-defined, machine-readable formats.

9.4. Self-corrective forces

A transparency portal for an IT project in Government works as a positive feedback loop. The fact that such a portal is implemented, means that analytics about the performance of the project are generated immediately. As a result, any deviation from expected behaviour is detected quickly and rectified.

In case such a portal is not well thought out, potential problems may manifest themselves much later, and may turn out to be difficult to fix. A transparency portal leads to monitoring and feedback at various levels: within the service provider, within Government, and by citizens at large. The NREGA MIS portal is an example of such a transparency portal (Box 9.1).

9.5. Contact centre

The contact centre closes the feedback loop of self-corrective forces. It establishes multiple channels of communication with all stakeholders, including end-users, for purposes of gathering information and reporting grievances. An effective contact centre is tightly integrated with the IT systems, so that queries and complaints can be dealt with effectively, and information is recorded and updated on a real-time basis. Some of the key features of such a contact centre¹ are as follows:

1. Provide services in multiple languages
2. Provide inbound channels of communication such as voice, fax, letters, e-mail, and a web portal
3. Provide outbound channels such as voice, fax, letter, e-mail, and SMS messages
4. Available during working hours, or on a 24-by-7 basis, depending upon the nature of the project
5. Deploy key technologies such as a Customer Relationship Management application (CRM), Interactive Voice Response System (IVRS), Automatic Call Distribution (ACD), Computer Telephony Integration (CTI), call logging, quality management system, email response system, and scanning solutions for letters and faxes.

9.6. Crowd-sourcing

Enabling citizens and beneficiaries of public schemes to directly provide feedback using web and mobile phone-based platforms is a powerful way of involving citizens in improving public accountability. It unlocks the potential of collective wisdom². In addition, the ability to combine spatial and financial data can provide very powerful maps to track the progress of various initiatives and schemes.

¹An example of a contact centre from UIDAI: http://uidai.gov.in/UID_PDF/Front_Page_Articles/Recent_Tenders/CONTACT_CENTERS/RFP_for_setting_up_and_operating_contact_centers_for_UIDAI_Ver3.pdf

²Examples of technology platforms that have successfully used crowd-sourcing are Ushahidi, Transparent Chennai, Environment Sustainability Index, Pollution Index, and e-Government's foundation projects.

Box 9.1: NREGA MIS portal

The National Rural Employment Guarantee Act (NREGA) aims at enhancing the livelihood security of the people in rural areas by guaranteeing hundred days of wage employment in a financial year, to a rural household whose members volunteer to do unskilled manual work. The Act contains specific provisions for public accountability. Based on the statutory directives, the guidelines stipulate a three-pronged strategy for public accountability: proactive disclosure, social audit, and a grievance redressal mechanism.

The Ministry of Rural Development has set internal and external systems to closely monitor NREGA both physical and financial performance of States.

1. **Management Information System (MIS):** A web enabled public MIS^a has been developed. The village level household database has internal checks for ensuring consistency and conformity to normative processes. All critical parameters get monitored in public domain: a) workers' entitlement data and documents such as registration, job cards, muster rolls, (b) shelf of approved and sanctioned works, works under execution, measurement (c) employment provided (d) financial indicators including wage payment. Till FY 2008-09, 6 crore Job Cards and 1.2 crore muster rolls have been placed on MIS.
2. **Statutory institutional mechanisms:** At the national level, a Central Employment Guarantee Council has been set up with the statutory mandate of monitoring and reviewing the Act. The Ministry also invited the CAG to conduct a concurrent audit of the program in the very first year of implementation to assess gaps in program implementation by States, so as to initiate remedial measures at an early stage.
3. **Other mechanisms:** Other mechanisms include National Level Monitors and Area Officers, and officials of the ministry who undertake annual field visits, quarterly performance review with States. A Professional Institutional Network (PIN) has also been constituted for steady, sustainable interventions that enhance the quality of the program. These institutions will conduct impact assessment, concurrent monitoring and appraisal, research, capacity building to identify both good practices factors that have or will limit the optimal performance of the scheme. Currently, the network has 18 member institutions, including Indian Institute of Technology (IITs), Indian Institute of Management (IIMs), Administrative Staff College of India (ASCI), Indian Institute of Forest Management (IIFM), Agriculture Universities and other professional institutions. In its first phase, 13 institutions have conducted an NREGA appraisal.

^aNREGA MIS portal: <http://www.nrega.nic.in>

9.7. International experiences

Various Governments are now leveraging the capabilities of IT platforms to democratize public data, to drive innovation, and provide transparency in the operations of Government. Some of the notable examples of portals that aggregate Government data and make it available in common data formats are as follows:

1. USA:

- (a) The Federal Funding Accountability and Transparency Act (FFATA) of 2006 requires that the Office of Management and Budget (OMB) establish a single searchable website, accessible to the public at no cost, which includes for each Federal award: the name of the entity receiving the award; the amount of the award; information on the award including transaction type, funding agency, etc; the location of the entity receiving the award; and a unique identifier of the entity receiving the award. <http://USAspending.gov> was first launched in December 2007 to fulfill these requirements.
- (b) A primary goal of <http://Data.gov> is to improve access to Federal data and expand creative use of those data beyond the walls of Government by encouraging innovative ideas (e.g., web applications). Data.gov strives to make Government more transparent and is committed to creating an unprecedented level of openness in Government.

- (c) <http://ITDashboard.gov> is a website enabling federal agencies, industry, the general public and other stakeholders to view details of federal information technology investments. The purpose of the Dashboard is to provide information on the effectiveness of Government IT programs and to support decisions regarding the investment and management of resources. The Dashboard is now being used by the Administration and Congress to make budget and policy decisions.
2. **Brazil:** The Government of Brazil provides a transparency portal for expenditure data at <http://www.portaldatransparencia.gov.br/>. This Transparency Portal was created in November 2004 for the purpose of making it possible for public managers and citizens at large to follow up on the financial execution of all programs and actions of the Federal Government more easily. The information available in it includes: funds transferred by the Federal Government to States, municipalities and the Federal District; funds directly transferred to citizens; direct spending of the Federal Government with procurement or contracts for projects and services, including the spending of each agency with per diems, office supplies, equipment, projects and services; as well as spending through Payment Cards of the Federal Government.
 3. **UK:** The Government is releasing public data to help people understand how Government works and how policies are made. Some of this data is already available elsewhere, but <http://data.gov.uk> brings it together in one searchable website. Making this data easily available means it will be easier for people to make decisions and suggestions about Government policies based on detailed information. There are currently over 5,400 datasets available, from all Central Government departments and a number of other public sector bodies and local authorities.

The enabling framework for an Expenditure Information Network (EIN) is slowly coming into place. There is a need for an effective monitoring, evaluation and accounting system for the large sums of money that are disbursed by the Central Government to State Governments, district level agencies and other implementing agencies. While there are various stand-alone efforts in this direction, there is as yet no consolidated Expenditure Information Network (EIN). This Group recommends details of the proposed EIN in Chapter 13.

10

Protection of the individual

10.1. Background

As IT systems become commonplace in governance, issues related to the protection of the individual's right to privacy come to the fore. With paper records, the risk of unauthorized access of large quantities of data has been limited due to the difficulty of aggregating and accessing the data. When data is stored in electronic format, the risk is greater. Data protection provisions already exist in existing legislations like the Information Technology Act, 2000.

The Department of Personnel and Training (DoPT) is currently engaged in preparing a legislative framework on data protection, which would also address issues pertaining to an individual's data in the context of IT systems¹. These recommendations may serve as useful guidelines for designers of IT systems until such a date that formal legislation on privacy is passed.

10.2. Solution architecture and privacy

Just as the solution architecture of a project should be designed taking security (Section 8.3) and transparency (Section 9.3) into account, it should also be designed from the ground up to support privacy of end-users. The privacy framework for a project should be defined early on, which translates the legislation on privacy into implementable rules for IT systems.

10.2.1. *Personal identifiable information*

The design of the solution architecture should ensure that any Personal Identifiable Information (PII) is stored safely, and access is carefully monitored. To the extent possible, workflows should be designed so that access to PII is avoided. Also, PII should be stored in encrypted form, and separately from other data. Separate access controls may be defined, with strict access control, monitoring, and logging of all access to PII data.

¹Approach paper for a legislation on privacy: http://persmin.gov.in/WriteReadData/RTI/aproach_paper.pdf

Stringent penalties must be in place to address the issue of unauthorized access of personal data by outside agencies as well as by personnel within the organization. Strict protocols and processes must be in place to detect such access in order that they are dealt with swiftly and in a deterrent manner. This is not only desirable from a privacy perspective, but also from a security perspective.

10.2.2. *Anonymization*

Anonymization of data is an important aspect of privacy. Data should be carefully anonymized when released publicly, or when shared with other organizations that do not require access to PII, as allowed within the data protection and privacy framework. Careful thought should be given to anonymization, since naive approaches to de-identifying data are prone to attacks that combine the data with other publicly available information to re-identify individuals. The concept of k -anonymity has been defined in the academic literature on privacy, where each record within the system is at least indistinguishable from $k - 1$ other records in the released dataset. Thus, privacy is protected by guaranteeing that every released record will relate to at least k other individuals in the dataset, even if the records are directly linked with other external information. Translating this theory into practice may not be easy, but designers of the solution architecture should try to approximate such concepts in their design to the extent possible.

10.2.3. *Data retention and usage policy*

Data retention and usage policies should be well-defined, especially for PII. It may be necessary to retain transaction logs for long periods of time for purposes of analysis and research, but PII should be scrubbed from these logs after a pre-defined period. In case the legal framework of the project provides for it, an individual should be able to access data stored in the IT system about themselves, after appropriate authentication of their identity.

10.3. **Balancing the right to privacy with public interest**

The right balance between the individual's right to privacy and the larger public interest should be achieved by the data protection framework. While personal information relating to the individual must be strictly protected from unauthorized access, there may be a need for Government agencies to access or share this data for purposes of national security, economic offenses, tax evasion and other specified circumstances. Hence, authorized sharing of information under specified circumstances, ipso facto, should not be considered as a violation of an individual's right to privacy. However, detailed processes, systems and guidelines need to be put in place to ensure that authorized access and sharing is within the parameters set by law.

Part III

Recommendations for Ministry of Finance projects

11

Goods and Services Tax

11.1. Introduction

The Goods and Services Tax (GST), which will replace the State VAT, Central Excise, Service Tax and a few other indirect taxes will be a broad-based, single, comprehensive tax levied on goods and services. It will be levied at every stage of the production-distribution chain by giving the benefit of Input Tax Credit (ITC) of the tax remitted at previous stages. GST is based on a destination-based taxation system, where tax is levied on final consumption. It is expected to broaden the tax base, foster a common market across the country, reduce compliance costs, and promote exports. The GST will be a dual tax with levy by both Central and State tax administrations on the same base. The GST demands a well-designed and robust IT system for realizing its potential in reforming indirect taxation in India. The IT system for GST would be a unique project, which will integrate the Central and State tax administrations.

11.2. Public policy challenges

11.2.1. *Placement of tasks*

11.2.1.1. *Governance bodies*

The following governance bodies have been constituted for realizing the vision of GST and implementing it:

1. The Empowered Committee of State Finance Ministers (EC) set up to work with the Central Government to lay down the features of GST and oversee its implementation.
2. The Joint Working Group (JWG) constituted by the Empowered Committee in consultation with the Central Government to prepare the roadmap for GST implementation.
3. The Empowered Group on IT for GST (EG-IT) formed in July 2010 for devising the IT strategy for GST and monitoring its implementation.

11.2.1.2. *GSTN as the NIU*

The EG-IT has recommended setting up of an NIU — Goods and Services Tax Network (GSTN), for managing the IT systems for GST implementation, including the Common GST Portal. GSTN will perform the following functions:

1. Provide common infrastructure and services to Central and State Governments
2. Ensure integration of the Common GST Portal with existing tax administration systems of Central and State Governments
3. Build efficient and convenient interfaces with tax payers and tax administrators
4. Facilitate, implement and set standards for providing common GST services to the Central and State Governments
5. Carry out research, study global best practices and provide training to the stakeholders.

The Group endorses the above approach and recommends that the GSTN should be set up as an NIU as envisaged in Chapter 1 of this report.

11.2.2. *Incubation of the project*

The EG-IT has suggested that the GSTN project may be incubated within NSDL and this suggestion has been generally accepted. The preliminary work of conducting a proof-of-concept is being undertaken by NSDL and it has been planned to run a GST pilot with selected State Governments participating in it along with the CBEC. The Group commends this approach and recommends that the infrastructure for the GSTN should be based on latest technology and ring fenced, so that whenever the *spin-off* takes place, the GSTN infrastructure is smoothly transferred to the proposed NIU being set up as GSTN.

The IT strategy document for GST prepared by the EG-IT, which defines the contours of the IT implementation in respect of the GST Common Portal and its interface with all stakeholders, could form the basis for taking forward the implementation of GSTN.

11.2.3. *Human resources*

The Group recommends that a dedicated Mission Leader and a dedicated Mission Execution Team be appointed for GST. The NIU for the implementation of GST — GSTN — should be set up with the highest priority.

The Group further recommends that an implementation team, comprising of officers drawn from the CBEC and some of the State Governments (pending the appointment of a full-fledged Mission Team and during the pilot stage) should be set up at the earliest. This team would work along with the teams that would be set up by NSDL for implementing the project. The two teams should together initiate the implementation of the GSTN including such as acquisition of necessary infrastructure, design and development of the application, etc. The personnel selected to man the implementation team should be trained in the tasks mentioned above. Hiring of talent on contract basis should also be explored as necessary. This team should later be part of the Mission Execution Team.

The implementation of GST is based on a substantive change contemplated in the relevant laws and procedures of Central and State Governments. It is essential that the GST Mission Execution Team includes professionals with legal expertise.

11.2.4. *Agreement with NSDL*

The Agreement with NSDL should be drawn carefully and with clarity. It should include aspects such as financials, responsibilities of the Government side and NSDL at the incubation stage, acquisition of infrastructure, development of application software, ownership of source code, spin-off to the NIU, and the process of transfer of assets (both tangible and intangible).

Further, though NSDL is assisting the Government in incubating the GSTN, once GSTN is set up as an NIU, the latter may continue to procure services from NSDL in the initial phases of GST implementation, as it considers necessary.

The GSTN may, as and when it commences its full-fledged operations, adopt a business outcome based, per-transaction pricing model. Even during the period when NSDL is providing such services, a similar approach is recommended.

11.2.5. *Multiple levels of Government*

The Central and State Governments have accepted in principle the setting up of GSTN as an NIU, as a way to align incentives of all stakeholders. The joint ownership of GSTN by all States and Central Government ensures that no stakeholder loses strategic control. GSTN will develop and operate the Common GST Portal, which will have common minimal functionality, but will be customizable and extensible by various Governments.

GSTN will render the following services through the Common GST Portal:

1. Dealer registration (including existing dealer master migration and issue of PAN based registration number)
2. Payment management including payment gateways and integration with banking systems
3. Return filing and processing
4. Taxpayer management, including account management, notifications, information, and status tracking
5. Tax authority account and ledger Management
6. Computation of settlement (including IGST settlement) between the Centre and States
7. Processing and reconciliation of import GST and integration with EDI systems of Customs
8. MIS including need based information and business intelligence
9. Maintenance of interfaces between the Common GST Portal and tax administration systems
10. Provide training to stakeholders

The CBEC and State Governments may design and develop their own applications to meet requirements for effective tax administration such as audit, intelligence gathering, enforcement, and risk management.

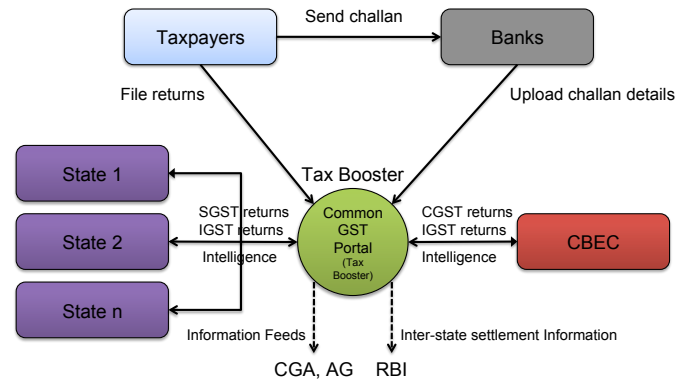
11.3. **Technology challenges**

11.3.1. *Solution architecture for GSTN*

The solution architecture for information flow (Figure 11.1) and funds flow (Figure 11.2) is designed to ensure timely delivery of information through the Common GST Portal, and timely delivery of funds directly through the banking system.

Figure 11.1: GST solution architecture: information flow

Information flows unmodified through Common GST Portal to states and CBEC
Common GST Portal will also integrate with systems of CBDT, MCA, etc.



The Common GST Portal is simply a pass-through device for information, while enhancing it with intelligence to plug leakages. The taxpayer sends the return with GSTN, which keeps a copy of the return for analysis, and forwards it in near real-time to the respective State and CBEC. The taxpayer pays the actual duty in the bank, which uploads only the challan details into the GSTN. Actual funds never pass through the GSTN.

The Common GST Portal reconciles the returns and the challans. In addition to its pass-through role, the portal would also play two other critical roles:

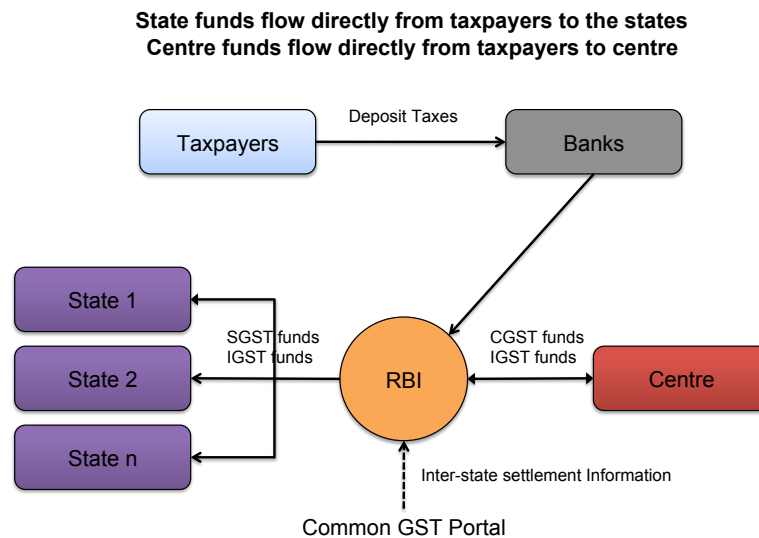
1. It would act as a tax booster, matching the input tax credits in the returns to detect tax evasion. It can also integrate with various other systems at MCA and CBDT for verification of PAN or other corporate information and perform data mining and pattern detection to detect tax fraud. It would send this information as alerts/ reports to the respective tax authorities.
2. It would also compute inter-State settlement, netting IGST across States.

11.4. The way forward

The GST project not only presents several public policy changes, but also requires adherence to tight timelines. In terms of implementation of the IT systems for the administration of the GST, the following important milestones that would facilitate timely implementation should be kept in view:

1. Finalisation of business processes registrations, returns, payments
2. Commencement of GST pilot project by NSDL with identified States and Centre.
3. NSDL to set up core functionalities of common portal in pilot and provide APIs for all stakeholders. Limited testing of APIs by participating stakeholders.
4. Engaging with participating entities for pilot including dealers, banks and other Government agencies.
5. Completing the impact analysis for GST and initiating steps to align existing tax systems at Center and all States for GST. This would include changes to business and IT infrastructure. Timely financial approvals and procurements would also be critical.

Figure 11.2: GST solution architecture: funds flow



6. Evaluation of Pilot Project resulting in iterative review of processes/ IT implementation.
7. Finalisation of detailed project report for actual implementation of GST
8. Attaining clarity on NIU engagement and structure of GSTN.
9. Creation of GSTN and formalising the involvement of NSDL in GST implementation.
10. Finalisation of IGST legal framework and business process.
11. Implementing the stakeholder outreach program
12. Scaling up to GST implementation:
 - (a) Administration and organisational restructuring
 - (b) Training and testing of applications by tax payers and all tax authorities

The Group notes that the CBEC has set up data centers to run centralized applications for Central Excise, Service Tax and Customs purposes. With the implementation of GST, these and other facilities should be leveraged to the extent possible. An in-depth study (either by an in-house team or by a consultant) of the reusability of the existing ACES project components should be undertaken and necessary steps should be initiated to refashion the same and integrate it with the GST solution.

12

Tax Information Network

12.1. Introduction

Successful tax administration is about making tax compliance painless and tax evasion painful. In order to modernize the systemic processes of tax administration, the Task Force on Direct Taxes, set up by Government of India under the Chairmanship of Dr. Vijay Kelkar, recommended in 2002 establishment of an electronic national Tax Information Network (TIN). Today, this network integrates primary information of tax payments made in designated banks, Tax Deduction at Source (TDS) Returns and information on high value transactions through Annual Information Returns (AIR) into a central database, which gives a 360 degree view of the taxpayer.

Income Tax Department (ITD) established TIN in 2003 through NSDL as a Managed Services Provider model providing the following services:

1. To receive information relating to tax payments coming from banks and enable necessary reconciliations between ITD, banks and accounting agencies in the Government of India
2. To receive TDS returns, digitize the same and enable reconciliation of information in these returns with the payment details received from the banks
3. To collate Information relating to TDS and compile Permanent Account Number (PAN) ledgers reflecting TDS and payment details for each of the taxpayer entities
4. To receive, compile and collate information relating to high value financial transactions coming through Annual Information Returns (AIR)

TIN has helped ITD to ensure that tax credit is given to a taxpayer only against tax reported to Government account. Further, this revised process and automation has enhanced convenience in record keeping relating to TDS returns, linking of returns with TDS particulars and has reduced cost of compliance for the taxpayers. The system is designed in a way that it is in the taxpayer's interest to ensure a high level of data quality and compliance. It is reported that the data quality in TIN has dramatically improved over the years, and continues to improve. Thus, TIN has contributed to reduction in leakage, increase in tax base, improvement in process efficiency and transparency, enabled speedy reconciliation, facilitated faster transfer of tax collected to Government and help in data mining to identify trends and making projections.

12.2. Public policy challenges

12.2.1. *Placement of tasks: NSDL as the MSP*

The ITD decided to outsource the technology-centric part of tax collection and TDS data as well as high value financial information on an MSP model to NSDL. The Department could, therefore, focus on its core functions in the areas of policy making, policy administration, tax assessment, and detection of tax evasion. NSDL was engaged for its expertise in data collection and consolidation, rather than establishing the infrastructure in-house. This placement of tasks is similar to that of an NIU, as described in Chapter 1. Outcome based per-transaction pricing was agreed upon, enforced through strict SLAs. Since it also provides for a reasonable return on investment (ROI) to the Service Provider over the tenure of the contract, the Service provider has a continued interest in successful running of the project. The ITD has developed an element of partnership with the service provider, and thus is able to meet its requirement of additional optional services based on changing or upcoming business needs. Automation of the processes and services through TIN has reduced the cost of compliance for the taxpayers, resulting into better voluntary compliance. At the same time, automation of the process of collection and collation of information has resulted into a more effective deterrence against tax evasion.

The Group takes note of this aspect and is of the view that to the extent possible keeping in view the sensitivity of the data, such model could be replicated in other aspects of ITD and other Government Departments, wherein technology driven data capturing processes are entrusted to specialized entities who would enable the processes with none or limited or pre-specified rights towards access and usage of data. Such entities may act as enablers to strengthen the information flow to the concerned departments.

12.2.2. *Human Resources*

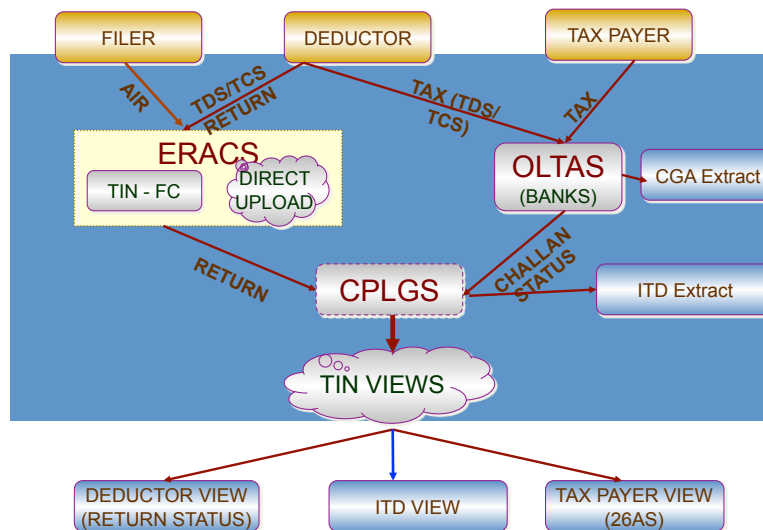
The Directorate of Income Tax (Systems) has acted as the dedicated agency responsible for defining the specifications, contracting with the service provider, getting the project up and running in partnership with NSDL, monitoring and controlling the implementation, and planning change management on the basis of feedback from various stakeholders. An officer in the rank of Joint Secretary (known as Director in the Directorate of Income Tax (Systems)) has played the role of the Mission Leader and he is being assisted by in-house technical staff to supervise this project. Now that the project has reached steady State, the Mission Leader has certain additional responsibilities.

NSDL has separate heads of Department for systems and business operations who are assisted by a team of functional and domain experts. The TIN team has separate process and sub-process owners for various modules like TDS, OLTAS, PAN Ledger Generation, data extraction etc. both in systems and operation areas. NSDL uses its common pool of resources only for support functions like personnel, administration, finance, and computer operation.

12.2.3. *Contracting*

Establishing TIN required initial capital investment, regular operating expenditure, and periodic investment for capacity upgrade and modification to accommodate increase in volume and changes in the Income Tax Laws. The Department realized that the normal Government procurement may require lengthy procedure for administrative approval, resulting in delays in implementation. Therefore, the Department developed a financial model wherein the payment is made on the basis of usage of the system. To suit this

Figure 12.1: Information security



business model, the Department also evolved a special Agreement that dened the expected outcome for each module, and risk management policies that included third party audits, SLAs and exit management policies.

12.2.4. Incubation

NSDL did not need to be incubated, since it was already operating the depository successfully when the TIN agreement was signed.

12.3. Technology challenges

12.3.1. Solution architecture

The modules of TIN as shown in Figure 12.1 are as follows:

1. **OLTAS (Online Tax Accounting System):** A system for all tax collecting banks to consolidate challan level information in the TIN central system
2. **ERACS (Electronic Return Acceptance and Consolidation System):** This consists of an online facility and a network of facilitation centers to accept TDS returns from the deductors' Annual Information Reports from specified agencies.
3. **CPLGS (Central Pan Ledger Generation System):** This is the central system maintained by NSDL where the returns uploaded by filers and challan details uploaded by the banks are consolidated and matched. Subsequently, these systems generate the specified extracts of challan data for ITD and the Office of CGA and the return and PAN ledgers of data for ITD in a manner that will enable processing of returns and provide input for assessment of Income Tax Return. This system also provides a dashboard to various stakeholders for status tracking, monitoring, and control.

12.3.2. Openness

TIN has published a plain text ASCII file format for submission of returns by filers and submission of challan data by banks. TIN also provided a free file validation utility that

users could use to verify the correctness of their files before uploading. This approach has proved beneficial to all stakeholders:

1. This open data format helped deductors build functionality in their in-house systems to generate a TDS return on their own.
2. There is no lock-in: of software, or service provider, or even the technology platform for preparation of returns.
3. Many independent software providers built return preparation software in the market, encouraging competition and innovation.
4. Existing financial accounting software packages seamlessly integrated return preparation.
5. Banks also provided similar flexibility for upload of their challan details

12.3.3. *Security*

TIN has put extensive security infrastructure and policies in place to ensure that the security and privacy of data is safeguarded. These are continuously reviewed and upgraded to keep up with challenges in the environment. Periodic audits are conducted by third party auditors, which include security audits.

12.3.4. *Transparency and Privacy*

The Department holds the personal and financial data of the taxpayers in a fiduciary capacity and carries out a sovereign function of the State. Therefore, it needs to have control on strategic assets including the software, hardware and the databases as well as exclusive control over use and dissemination of data. It is recommended, therefore, that TIN should adopt the best practices for transparency and privacy as discussed in this report.

12.4. **The way forward**

12.4.1. *TIN only a component in IT infrastructure of Income Tax Department*

ITD is a large organisation dealing with tax matters of over 3 crore taxpayers. Its PAN database now exceeds 10 crore records. It annually receives 2.75 crore tax challans, 3 crore returns of income, and 40 lakh TDS returns with information of over 29 crore transactions, besides the AIRs. This is a large and recurring data volume growing every year.

ITD handles its main IT-related functions through a National Data Center (NDC) with its backup sites, connected to offices across the country through a VPN. These have been set up on an outsourced model with three different service providers for Software Solution, Network Service and System Integration. These Service Providers are mainly paid against SLA based contracts, though ITD has also acquired ownership of critical hardware of NDC.

TIN provides ITD's major interface with its customers (taxpayers, TDS Deductors etc) and constituents (Banks, AIR filers etc). Several other taxpayer service functionalities have been set up by ITD using different methodologies and at different times. Thus, hosting and maintenance of its website has been outsourced to two agencies on per transaction basis - a RFP for appointment of a new agency is in progress. Helpdesk support Aayakar Sampark Kendra has been outsourced to another agency. The facility for e-filing of returns of income has been set up departmentally though a RFP for appointment of an agency has been issued recently. A RFP for providing web-enabled services is also in process.

For data processing within the department, the ITD is following multiple approaches. E-filed returns of income and paper returns of Karnataka region are being processed through a Centralised Processing Center (CPC) at Bangalore set up recently on MSP model. The number of these returns has risen to over 60 lakh but the remaining returns of income (2.5 crore) and TDS returns are being processed departmentally on NDC. It is proposed to set up two more CPCs at Pune and Manesar on MSP model. The risk management system is run departmentally on NDC. Data mining of AIR and TDS returns is being done regionally through a customised solution developed departmentally and managed through yet another Service Provider. Computer Forensic labs at Delhi and Mumbai are being run through C-DAC. A Record Management System, Workflow Management System, Judicial Reference System and a Data Warehousing project have been conceived but are yet to be set up. ITD proposes to set up a Special Purpose Vehicle for its IT needs though its exact contours are to be worked out.

It is thus apparent that various IT-related initiatives have been developed or are proposed on different models of implementation for historical reasons. TIN, conceptualised way back in 2003, is only one component of ITD's taxpayer interface. Though it has several features of a NIU with consequent advantages, it is not exactly a NIU in the sense contemplated in this report. The MoU between NSDL and ITD has undergone two renewals and is to now expire in 2011.

The Group notes that the Department is at the crossroads of important strategic decisions as the new Direct Taxes Code is to be operationalised from April 2012 requiring major changes in its application system - which itself was developed in late 1990s, its functional needs in terms of growth of revenues/ number of taxpayers/service standards etc, and required deterrence levels are going to grow significantly over next 5-7 years. The data volumes have grown exponentially. The existing contracts with various service providers are nearing expiry. Although the existing IT related instrumentalities have served the department's needs admirably it may not be advisable to continue with these diverse implementation methodologies.

Considering that its technology needs are large, dynamic, and sensitive from the point of both, security and privacy, the Department clearly needs a dedicated and efficient NIU type organization to set up, manage and run its IT-related infrastructure on long term basis.

12.4.2. Recommendations

1. The Group is of the view that time has come for the department to have a fresh and holistic look at its overall IT-related and functional needs over next 5-7 years and to devise a new and comprehensive IT plan keeping in mind the recommendations in foregoing chapters of this report. In its Vision document 2020 the Department has proposed to *meet the challenges of technology by formulating a Strategic Technology Plan*. The Group recommends that this may be done forthwith along with a time bound roadmap for implementation, and all new initiatives should be implemented only in accordance with this Plan.
2. As part of the Strategic Technology Plan ITD must clearly identify IT-related activities and services that it can actively outsource to a NIU and those which it must necessarily handle departmentally. Ideally ITD should directly handle only matters involving policy making, quasi-judicial decision making, exception handling, risk management and enforcement functions. The IT systems required to assist and enable its functionaries in discharge of these should be set up, managed, and run by a NIU.
3. There is a strong case for a separate well-capitalised and professionally run NIU to handle the IT-related needs of ITD. This should be set up on priority

and in accordance with the recommendations in the foregoing chapters. While ITD should retain Board level strategic control, the NIU should have financial autonomy and operational freedom and its affairs should be managed by an eclectic mix of IT experts, management professionals and domain experts.

4. Such a NIU would necessarily need services of a few departmental officers as domain experts at different levels to enable it to discharge its mandate. It should therefore be possible for suitable departmental officers to be deputed to the NIU for a defined period while retaining lien on their cadre posts. The relevant Rules may be accordingly modified to enable deputation/secondment of a few officers to the proposed NIU.
5. Action points 4 and 5 of ITD's Vision 2020 document require it to *resolve multiplicity of platforms in favour of uniform holistic rule based application matrix* and to *integrate all the elements of tax collection process through technology with information seamlessly flowing to the users for informed decision making*. This Group entirely endorses these and recommends that these should be implemented at the earliest.
6. The Ministry of Finance should develop the next generation Risk Information Network to enhance the effectiveness and impact of tax collection using functionalities such as comprehensive taxpayer profiling, trend analysis, pattern recognition, and data mining of the information gathered in ITD, GST, and Customs systems.
7. Simultaneously the Department needs to restructure and reorganise the Directorate of Systems and re-define its role as the department's single point interface with the NIU so as to take full advantage of the NIU model. As part of this exercise it may also re-determine the strength of its technical cadres and restructure the same.

13

Expenditure Information Network

13.1. Introduction

In the mid 1980's, the then Prime Minister Shri Rajiv Gandhi had estimated that of every rupee spent on development only 15 paise reached the poor. Apart from administrative inefficiencies, poor targeting, and high implementation costs, there is often a big hiatus between the release of funds by the GoI and actual expenditures on the ground.

As a 2007 Planning Commission Working Paper ¹ pointed out:

The connection between release of funds by the Central Government and actual expenditures for physical inputs by the implementing agencies is currently, very obscure.

The office of the Controller General of Accounts is already implementing the Central Plan Scheme Monitoring System (CPSMS), which aims to establish a suitable on-line Management Information System and Decision Support System for the Plan Schemes of the GOI. A lot of work has been done in this area. However, moving forward, the vision of the EIN as articulated in this report should be the next priority of the Government.

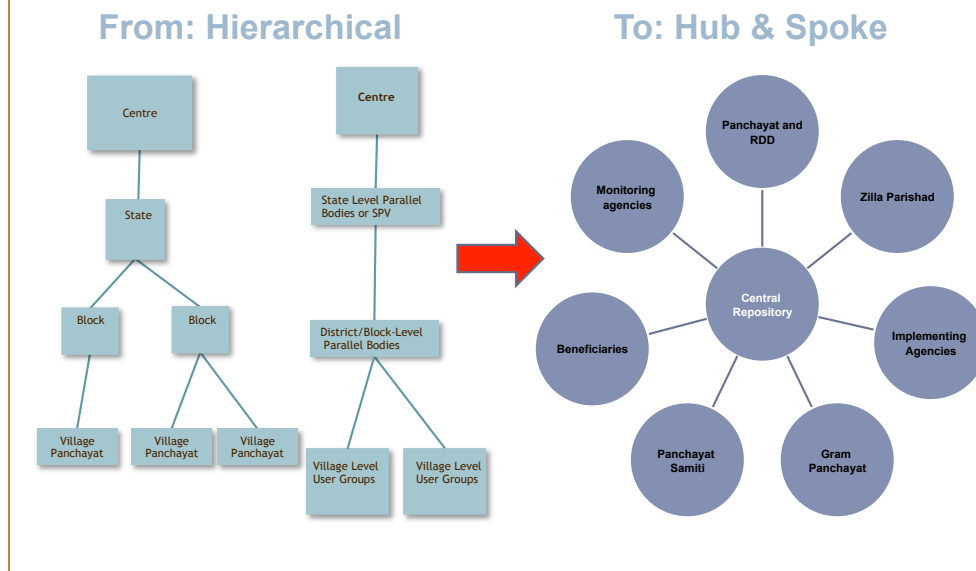
13.1.1. *Challenges with expenditure tracking today*

Today, the GoI's budget documents do not report on actual expenditures at the level of implementation. Data on expenditures can be found in the annual audited accounts of the Government but these have nearly a two year time lag. Disaggregated expenditure data is often only available up to the district level and not below. This makes it difficult to perform data analysis for program evaluation. A well functioning system that makes this information available in real-time will greatly improve transparency, policy-making, and eventually lead to more effective governance.

The existing system of transfer and monitoring of funds has some limitations. Today, measurement of plan schemes and programs is largely on the basis of outlays rather than outcomes. Government follows hierarchical and multiple patterns for allocation and release of funds to the implementing agencies and beneficiaries. It is difficult to

¹Virmani Arvind (2007), Planning for Results, Planning Commission Working Paper No. 1/207-PC.

Figure 13.1: EIN: From hierarchical to hub-and-spoke reporting



track the flow of funds to actual beneficiaries, and equally difficult to evaluate the performance of agencies based on spending and project implementation.

Apparently, there is significant float of funds in the system, the cost of which due to inefficient use is eventually borne by the taxpayer.

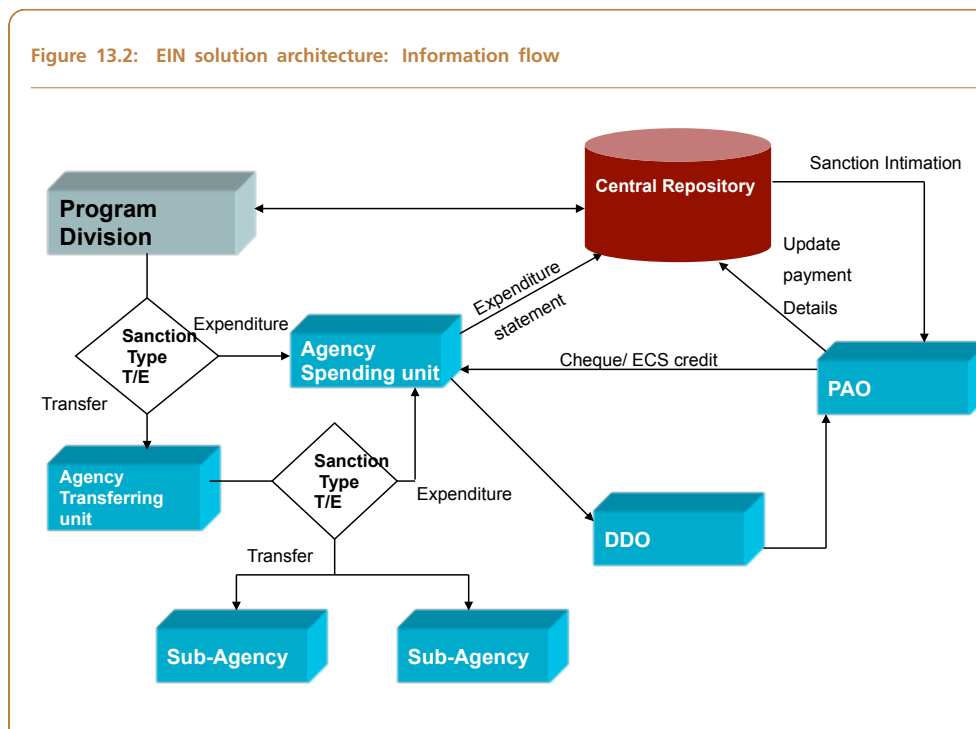
13.1.2. Setting up an Expenditure Information Network

There is a need for effective monitoring, evaluation and accounting system for the funds that are disbursed by the Central Government to State Governments, district level agencies and other implementing agencies as Plan Expenditure².

The establishment of an integrated Expenditure Information Network is a step in this direction, and can help achieve the following objectives:

1. Monitoring scheme-wise release of funds and outcomes
2. Helping in budgeting, planning and decision making based on the evaluation of all plan schemes
3. Maintaining time-series information related to each implementing agency, which will enable in evaluating performance
4. Ensuring disbursement of funds to intended beneficiaries
5. Ensuring timely disbursement of funds
6. Reducing float of funds within the system
7. Up-to-date and near real-time information on utilization of funds
8. Monitoring of outcomes up to the last mile
9. Transparency in disbursement and utilization of funds by making information available in public domain by way of a transparency portal

²Finance Minister's Budget speech in 2008–09 (Paragraph 115): <http://indiabudget.nic.in/ub2008-09/bs/speecha.htm>; Economic Survey 2007–08: <http://indiabudget.nic.in/es2007-08/esmain.htm>



13.2. Public policy challenges

The Group recommends that the NIU framework as described in Chapter 1 be followed. Aspects such as allocation of tasks between the Government and the NIU, appointment of a dedicated Mission Leader and a dedicated Mission Execution Team (Chapter 2) may be along the lines of the recommendations contained in this report.

Some of the challenges anticipated in the implementation of EIN are similar to those being faced in the context of GST. The relationship between the Government and the NIU may be defined by an Agreement as described in Chapter 3. EIN may be incubated as per the recommendations in Chapter 4 of this report. Learnings from the experience of setting up GSTN should be adopted in setting up the NIU for the implementation of EIN.

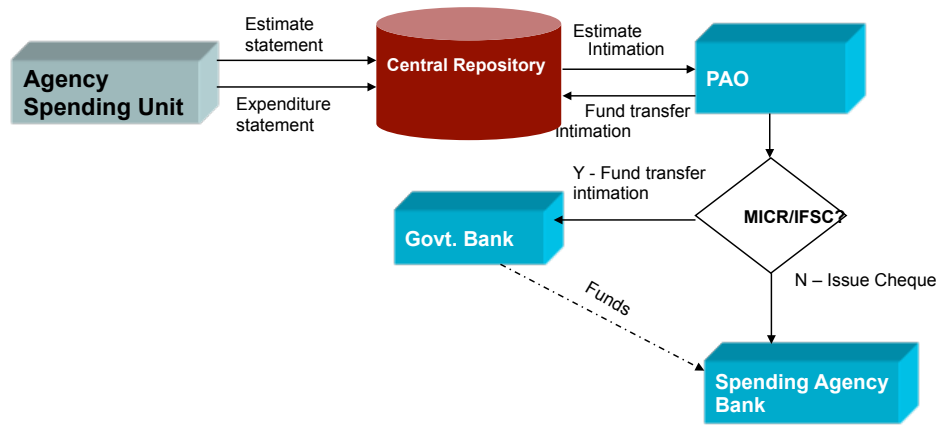
The EIN solution should provide for tracking of expenditure at Central, State, and Local levels. Therefore, the solution should ensure balance between standardisation of features and autonomy of States as provided in Chapter 5. Appropriate incentives should also be devised for full participation at all levels of Government.

13.3. Technology challenges

The solution architecture for EIN should have the following features:

1. The hierarchical functions of allocation, authorization, disbursement, and utilization may continue as at present, but the reporting mechanism should be based on a hub and spoke model as shown in Figure 13.1. This arrangement will help in correct and prompt capturing of expenditure information.
2. The Central Expenditure Repository (CER) is a key ingredient of the design of the EIN. EIN will handle the information flow through this repository (Figure 13.2).
3. The flow of funds will be managed through the banking system (Figure 13.3). Banks can make an electronic transfer in case the account is available in a CBS

Figure 13.3: EIN solution architecture: funds flow



branch, or issue a cheque. Banks would then report the details of disbursements to EIN for reconciliation purposes.

4. EIN will track all authorizations and forward electronic instructions to banks, so that funds move only against actual expenditure to service providers.
5. Planning Commission, Ministries, Departments, and Program Divisions can be linked to CER and should be able to monitor the outcomes, utilization and fund status through near real-time availability of information about all entities and programs.
6. Pay And Accounts Office (PAO) should be able to view the payment authorizations marked in EIN and release funds to spending agencies.
7. Program Divisions at various ministries should be able to set first leg of fund flow transaction (allocation of funds to parent agency). Funds disbursed to States should be marked as *Transfer* and not *Expenditure* if the funds are meant for further distribution to implementing agencies.
8. All the agencies such as State bodies, district bodies, village panchayats, block level bodies, and beneficiaries should have access to EIN with appropriate access controls. These agencies can view the funds sanctioned for them and also update the status of utilization of funds by them.
9. For greater transparency, citizens should also have access to a transparency portal and information from the ground can be crowd-sourced.
10. All financial information made public through a transparency portal should be machine-readable and format-neutral.
11. EIN should enable easy download of data and reports to facilitate the evaluation of the impact of public expenditure.

13.4. The way forward

The EIN project is similar to the GST project in many ways. Some of the processes touch more agencies and involve more steps. The Group recommends that the measures suggested for GST (Section 11.4) may be suitably adapted for the implementation of EIN.

14

National Treasury Management Agency

14.1. Introduction

In the 2007–08 Budget speech, the Honourable Minister of Finance announced that a Debt Management Office would be set up¹. This drew on the recommendations of the HPEC Report on Mumbai: An International Financial Centre². In light of these developments, the Ministry of Finance formed an Internal Working Group to analyse how best to move forward on establishing a Debt Management Office. The report of the Internal Working Group on Debt Management — Establishing a National Treasury Management Agency (WG)³ — lays down a framework on setting up the NTMA. The NTMA will manage debt for the Centre and States, with the overarching objectives of meeting their financing needs, while minimising borrowing costs within acceptable levels of risk.

14.2. Public policy challenges

The Group recommends following the NIU framework as described in Chapter 1 for NTMA. As recommended in the Report of the Internal Working Group on Debt Management, NTMA should have a dedicated team to manage its operations. The Group recommends that the HR structure for Government teams (consisting of a Mission Leader and Mission Execution Team) as recommended in Chapter 2 should be adopted for NTMA.

14.3. Technology challenges

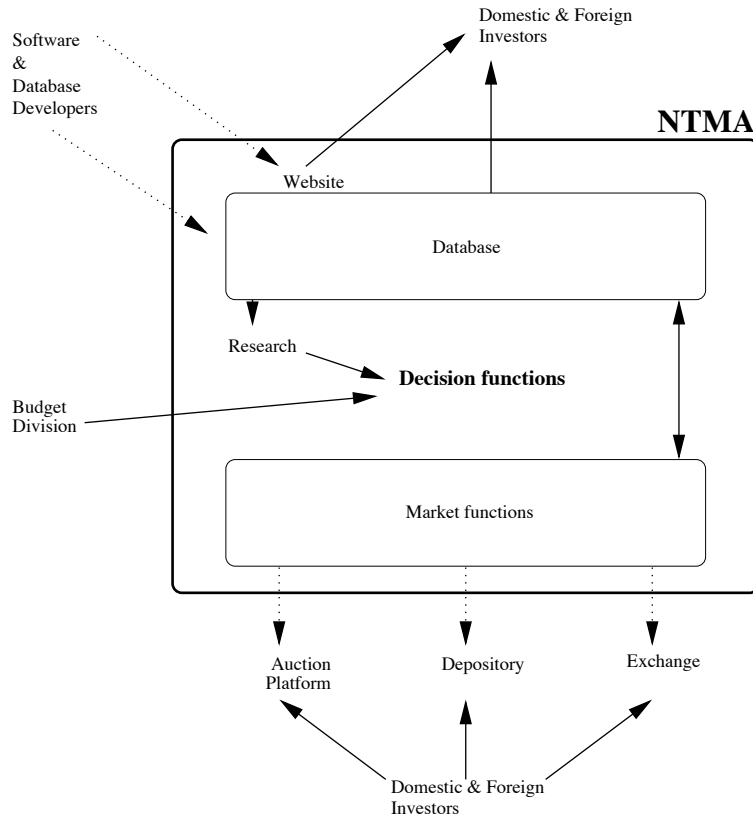
The WG has recommended the solution architecture for NTMA, which is shown in Figure 14.1. The Group commends this approach.

¹Finance Minister's Budget speech in 2007–08: <http://indiabudget.nic.in/ub2007-08/bs/speecha.htm>

²Report of the High Powered Expert Committee on Making Mumbai an International Financial Centre: http://finmin.nic.in/the_ministry/dept_eo_affairs/capital_market_div/mifc/fullreport/execsummary.pdf

³Establishing a National Treasury Management Agency: http://finmin.nic.in/reports/Report_Internal_Working_Group_on_Debt_Management.pdf

Figure 14.1: NTMA solution architecture



The WG has a strong focus on openness, transparency, and developing a strong research capability. The Group recommends that NTMA should also adopt the best practices for solution architecture, openness, transparency, security, and privacy as described in this report.

14.4. The way forward

The WG provides detailed steps for incubation, which span legal issues, setting up of IT systems, and change management for transferring the functions from RBI to NTMA. The Group recommends that the incubation framework, and creation of the platform described in the WG report may be adopted.

15

New Pension System

15.1. Introduction

In 2004, the Government of India introduced a new defined contribution pension scheme known as the New Pension System (NPS), replacing the existing system of defined benefit pensions. The NPS was envisioned to provide financial security to its subscribers after retirement while ensuring that the costs of pensions account administration, fund management charges and other expenses are low.

The Government established the Pension Fund Regulatory and Development Authority (PFRDA), as the apex body to regulate and develop the pension sector in India, to provide old age income security for all individuals, including those in the unorganised sector.

PFRDA has put in place an institutional framework with a set of Intermediaries who have experience in their respective areas of operations such as record keeping, fund transfers, fund management, custodial services etc. The relationships between various stakeholders are shown in Figure 15.1.

15.2. Public policy challenges

15.2.1. *Placement of tasks: NSDL as the MSP*

PFRDA is responsible for designing the institutional architecture, framing the policies for functioning of NPS, selecting and regulating various intermediaries for record keeping, fund management etc. The record keeping function is performed by NSDL, who runs the Central Record keeping Agency (CRA). The current placement of tasks is similar to that of an NIU as described in Chapter 1.

15.2.2. *Human resources*

The PFRDA provides for a Chairperson and not more than five members, of whom at least three shall be whole-time members, to be appointed by the Central Government.

The other officials include two Executive Directors who have their team of officers drawn from various Government departments. PFRDA is in the process of enhancing its

team by infusing talent from outside. The Group recommends infusing the team at PFRDA with market professionals.

For each of the major intermediaries like CRA, Pension Fund Managers, etc., PFRDA has prescribed establishment of exclusive business units to perform the functions related to NPS. Each of these intermediaries is regulated by PFRDA and is assisted by process owners for each key process.

15.2.3. *Contracting*

PFRDA engaged external consultants to assist in developing the RFP for the solution architecture, system specifications and contracts. The contracts with intermediaries prescribe the roles, responsibilities, charge structure, service level agreement, penalty structures, exit management mechanisms, etc.

15.2.4. *Incubation*

Various intermediaries such as the CRA, Fund Managers etc were selected on the basis of an open and transparent competitive bidding process managed by PFRDA. Subsequently, PFRDA has been actively monitoring the establishment of each of these agencies.

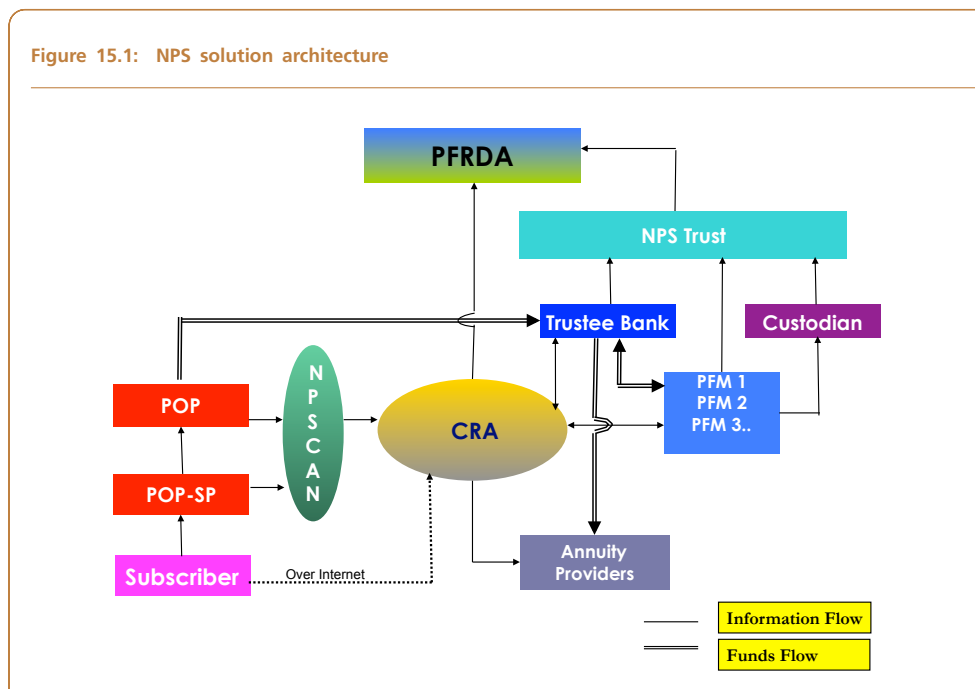
The various stakeholders in NPS are as follows:

1. **CRA:** In the NPS architecture, the CRA forms the foundation on which the long-term success and stability of NPS rests. CRA maintains complete records of all clients with respect to their subscription, scheme choice, units allocation, scanned copies of their documents etc.
2. **Fund Managers:** They handle the investment of the funds collected within the contours of the prescribed guidelines.
3. **Custodian:** Custodian handles the back office functions for the fund managers.
4. **Annuity Providers:** They will provide monthly pay-outs to individuals after retirement based on the accumulated pension wealth.
5. **Trustee Bank:** The Trustee Bank consolidates the funds uploaded by the subscribers (directly or through intermediaries) and forwards them to the fund managers, based on the input consolidated by CRA.
6. **Entities for servicing the subscribers:** In case of Government employees, the accounts officers (Pay and Accounts Officer / CDDO for Central ministries or treasury officers for State Government) handle the consolidation of subscriber contribution, transfer of the funds to the trustee bank, and uploading the subscriber contribution files to CRA. In case of subscribers in the unorganised sector, the client servicing is handled by Points of Presence (PoPs) registered by PFRDA.

15.2.5. *Multiple levels of Government*

Central Government has adopted the basic architecture designed by PFRDA for all Central Government departments, with a few exceptions. State Governments have the freedom to adopt the NPS architecture and the associated institutional infrastructure or to establish their own mechanism and infrastructure, or to continue with their current pension system.

All States joining the NPS are required to sign separate agreements with intermediaries such as the CRA. However, PFRDA strives to ensure that the solution and contract remains standard for all entities that participate in NPS.



15.3. Technology challenges

15.3.1. Solution architecture

The detailed solution architecture for NPS is shown in Figure 15.1. The salient features of the NPS are:

1. NPS has already been operationalised for new Central Government employees through a notification with effect from January 1, 2004.
2. Every NPS subscriber has an individual pension account with a unique Personal Retirement Account Number (PRAN), which will be portable across jobs and locations. NPS will also offer seamless transfer of accumulations in case of change of employment and/or location.
3. NPS offers a basket of investment choices and pension fund managers. The subscriber can choose any fund manager and scheme and has the option of switching schemes and fund managers
4. Provides services for opening of Individual Retirement Account (IRA), and issuing PRAN Card, I-PIN, and T-PIN to account holders, through the CRA.
5. Offers Tier-I (pension, non-withdrawable) and Tier-II (withdrawable) accounts.
6. Implementation framework allows a combination of retailers, pension funds and multiple recordkeepers.
7. Uses existing network of bank branches and post offices to collect contributions and deliver services to customers across the country.

Though the CRA system was developed on the basis of a standard specification evolved by PFRDA, the operationalisation of CRA services to Central, State and all India segments threw up a number of challenges in terms of the way data is maintained by accounting offices at various ministries, issues related to discipline in handling pension contribution deductions, and quality of the data maintained by them.

PFRDA and CRA have been making continuous refinements to the basic solution and business processes to meet the varying requirements on the basis of the feedback

received from the users. Some examples of these enhancements and improvements include:

1. Facilitates easy adoption through registration of nodal offices and subscribers and enabling them to commence the subscriber contribution quickly.
2. Multiple interface models to accommodate the requirements of various State Governments and Central Autonomous Bodies (CAB) who have joined NPS.
3. Utilities for contribution processing to accommodate varying requirements relating to fund transfer and interfacing models across organizations.
4. Enhanced features to help the various oversight bodies and to satisfy the special requirements of various entities like Points of Presence (POP), States etc.
5. Exception handling in case of mismatch in Subscriber Contribution File and funds transfer for streamlining process compliance by nodal offices.
6. System stabilization and exception handling in case of poor data quality.
7. Management reports and dashboards
8. Grievance management to analyse the grievance patterns and bring about systemic improvements in CRA systems and processes
9. SMS alerts to IRA compliant subscribers

15.4. The way forward

1. In order for a well-ordered and mature pension business to develop in the country, there is a need for:
 - (a) All pension and provident fund streams to converge in the medium term;
 - (b) Costs to go down dramatically due to competition and economies of scale; and
 - (c) Rule-based regulations need to give way to principles / risk-based supervision.
2. An enabling legal framework that provides the necessary impetus for NPS should be provided.
3. The tax treatment of the NPS also needs to be rationalized to provide for, at least equal treatment with other retirement products and providers.
4. There is an imminent need to create a certain level of awareness amongst the NPS subscribers that will eventually empower them to make well informed investment choices to protect and further their own interests.
5. As the broader mandate of the PFRDA is to regulate the pension sector in the country, this may eventually necessitate the separation of the NPS administration, including marketing and distribution strategies, from the PFRDA.

Recommendations

1. NPS needs to create a daily MIS with facts about number of subscribers, assets under management, the breakdown of number of subscribers and assets under management under various heads of Government, the number of switches made by customers from one fund manager to another, the returns of the various schemes of various pension fund managers, and summary statistics about the returns obtained by NPS members. The daily release of this information base is essential for policy analysis and the creation of self-correcting forces.

2. NPS should create an audit mechanism whereby every year, for randomly chosen customers in a statistically meaningful way, a comprehensive review is undertaken about correctness of data, about whether contributions came in on time, and about whether each member was notified about every contribution. The results of this audit should be released into the public domain. This will yield a regular check upon the quality of performance of NPS.
3. There is a need to avoid splitting the functionality of NPS across multiple variants of the same product, since the existence of variants reduce portability for customers and increase cost.
4. While significant strides in IT implementation have been undertaken in the NPS, there is a need to further leverage recent technological innovations in e-Governance, banking, and financial networks to develop greater efficient mechanisms that leverage use of IT in an end-to-end manner – from the post office interacting with the customer to the CRA to the fund manager and annuity providers.
5. More specifically, initiatives may be taken in the following areas to develop a comprehensive integrated pension administration system:
 - (a) Enabling linkages with HR and payroll systems of the Central and State Governments to obtain subscriber contribution details, among other things.
 - (b) Revamping and automating all pension administration processes.
 - (c) Re-engineering in the context of the user departments, especially in areas related to Government accounting formations
 - (d) Providing process linking between Government accounting systems and the pensions administration system
 - (e) The implementation of these initiatives should be accompanied by extensive skill enhancements, learning and change management efforts, in conjunction with nationwide public awareness campaigns.
6. As the Aadhaar implementation becomes ubiquitous across the country, there is a need to establish the platform for linking Aadhaar with the PRAN number, which can enable Aadhaar-linked KYC for pension scheme enrollment. In this aspect, the NPS should also explore opportunities for future integration with the identification and authentications systems of the Unique Identification Authority of India (UIDAI).

Part IV

Summary of recommendations

16

Recommendations for public policy challenges

16.1. The appropriate placement of tasks

1. For complex projects that depend on mission-critical IT systems, National Information Utilities (NIU) working in the spirit of partnership with Government may be put in place to handle all aspects of IT systems. They would participate in high-level design, specification of requirements, proof-of-concept studies, while strategic control would remain with Government. (1.1)
2. NIUs would be set up as private companies with a public purpose: profit-making, but not profit maximizing. The NIUs should be financially independent and empowered to take quick and efficient business decisions pertaining to attracting and retaining talent, procurement, rapid response to business exigencies, adopting new technologies etc. They should be able to get funding independently and have a self-sustaining financial model. (1.3.1)
3. Strategic control can be achieved by having a strong dedicated team within Government inter alia to drive policies, design a suitable solution architecture, supervise execution, frame appropriate contracts, adopt outcome based pricing, evolve strict service level agreements (SLA), and conduct independent audits. (1.3.2)
4. An NIU should be structured as a company with limited liability and be subject to sound corporate governance norms, such as those required for listed companies though the company may not be listed. The board composition, accountability, and transparency norms for NIUs should be the same as prescribed for listed companies. (1.3.3)
5. Other characteristics of an NIU should, inter alia, be:
 - (a) ownership share of the Government in it should be at least 26%;
 - (b) total private ownership within it should be at least 51%;
 - (c) no single private entity should own more than 25% of the shares in an NIU;
 - (d) institutions that have a direct conflict of interest (e.g. IT companies) should not be permitted to be shareholders;

- (e) an NIU should not go for an initial public offering or list itself on public exchanges;
 - (f) an NIU should be dispersed-shareholding corporations with a professional management team;
 - (g) an NIU should preferably have a net worth of Rs.300 crore. (1.4)
6. NIUs, though set up initially as natural monopolies, would be obliged to provide access to a competing NIU, when one emerges. (1.4.1)
 7. For effective functioning, an NIU should be, self-financing, making reasonable profits, and having sufficient net worth' to meet exigencies. It should maintain high professional standards and competitive practices, utmost transparency in its operations, be willing to invest in technology for increasing efficiency, reach and economies of scale. (1.4.1)
 8. Government-NIU relationship may be defined by an Agreement, which covers allocation of tasks and responsibilities between the Government and the NIU, financials, and SLAs. (1.5)
 9. In the early phases of a project, during incubation, both, the Government and the NIU should have teams that are dedicated to the project, which will facilitate smooth decision making. (1.5)
 10. Business change is the driving force, and technology is an enabler. Therefore, a Mission Strategy Document for the project that inter alia details the functions, and capabilities of the IT System which would assist in bringing about the desired business change, should be prepared. (1.5)
 11. While the Department should recognize the capabilities and limitations of the technology solution, the NIU should perceive its responsibility as extending beyond merely meeting a technical or legal requirement under the Agreement with Government. (1.5)

16.2. Human resource policies

1. Strong support from the top management within Government, leadership at the level of project implementation, and ownership and commitment at various operational levels are necessary concomitants of success of any project. The concerned Department should put in place a high level body that will review the progress of the project during its implementation and later evaluate the realization of benefits and objectives on a periodic basis. (2.1)
2. Every project should have a dedicated Mission Leader within the Government Department, of the rank of Joint or Additional Secretary, fully responsible for the project. This person should possess necessary technical and managerial skills. This post should be open to all eligible officers of the Government. The Mission Leader should have the freedom to choose the Mission Execution Team from within or outside the Government. (2.3.1)
3. The Mission Execution Team should be manned by personnel, who possess a diverse set of skills including intimate familiarity with the Government processes, specialisation in verticals such as technology, outreach, law, as well as the ability to manage a large decentralized organization, among others. This team, including the Mission Leader, should have adequate tenure (at least 5 years) for purposes of continuity, so that institutional memory can be created and retained. (2.3.2)

4. Professionals may be hired into the Team by posting suitable officers to the project from the same cadre; inducting officers on deputation from other departments at suitable compensation under the Central Staffing Scheme; infusion of talent from the private sector by way of lateral entry; hiring professional resources on contract basis; by appointing consultants at market rates on contractual basis; recruiting sabbaticals from industry, who continue to be employed by the parent organization; recruiting volunteers who come from various walks of life through a well-defined volunteer selection process; and recruiting students from various colleges and universities as interns through a well-defined internship program. (2.3.3)
5. Just as the Government team will have business specialists, and experts from other domains, so should the NIU have a management team with the right domain knowledge, and other essential expertise in areas such as technology, law, and outreach. The NIU should also take on its staff, professionals from the Department, who have the requisite business domain knowledge, so that the IT systems they develop and implement is backed by people with relevant domain experience. (2.4)
6. Government should set up a database of all IT projects implemented in the public sector, containing comprehensive details of the individual projects and the key personnel associated with the project. Centres of Expertise within the country may be identified for providing assistance by way of project consultancy and advanced training in the field of IT management. (2.5)
7. With a view to building capacity within the Departments embarking on large, complex projects with mission-critical IT systems, the training curriculum for the existing workforce of various services should include training on the technical aspects of IT systems, project management and evaluation, procurement management, governance issues, and change management. Mid-career programs should also be designed in such a way that senior officers are not only able to provide the required leadership but also coach and mentor junior managers. In-service personnel, who already possess technical knowledge should be trained in the latest technologies and in fields in which they like to specialize. (2.6)
8. As a measure to retain in-service staff deployed in IT functions they should be provided with IT professional allowance on the lines of the training allowance at the rate of 30% of their remuneration. (2.6)
9. The Performance Linked Increment Scheme as suggested by the Sixth Pay Commission for Central Government employees, should be implemented along with performance linked training programs in special skills. (2.6)
10. A scheme of non-monetary incentives such as public acknowledgement of their contributions, certificates of outstanding performance etc. should be instituted with a view to motivating both in-service officers and contracted personnel. (2.6)
11. Full opportunity should be provided for every individual to equip himself for higher levels of responsibility through individual and group assignment and training programs to ensure that his/her needs are satisfied. (2.6)
12. For creating a conducive work environment, end users should be provided appropriate training and support and encouraged to make their own contribution to the success and continuous improvement of the project outcomes. (2.7)
13. The method of performance appraisal has to be reconsidered, by redefining the purpose and principles, conducting a job analysis, obtaining employee feedback, reviewing standards of objectivity, conducting training for both managers and employees and reviewing/evaluating the results of the system. Greater objectivity

and according appropriate weight to the overall contribution of the individual has to be given due consideration. Merit should be given primacy over seniority within a given band of eligible appointees. Adoption of performance management techniques would be particularly relevant for appraising the performance of in-service officers entrusted with the task of implementation of mission-critical projects. (2.8)

16.3. Contracting

1. In general, the relationship between the supplier and the Government should ensure that:
 - (a) the solutions proposed by the supplier focus on and meet the business needs spelt out by the Department owning the project and not just the technical, operational, or legal requirements;
 - (b) through the lifecycle of the project the supplier should produce realistic plans, including timeframes, resources, technology, mode of delivery and financials, and align the same with the business needs;
 - (c) the supplier should as far as possible maintains continuity in employing trained Personnel;
 - (d) both should share in a timely manner all information about technical, financial, and personnel problems, set up a mechanism for co-operation and dialogue;
 - (e) both should agree and document change control processes, address risk factors and avoid informal changes.
 - (f) both should recognize that estimates of price, timeframes should be realistic and achievable. (3.1)
2. The Agreement between an NIU and the Government should clearly set out all aspects relating to the scope of work, activities to be undertaken by NIU, obligations of the Government and NIU, the financial arrangement, Service Level Agreement, and business continuity plan upon exit. (3.2)

16.4. From startup to going concern

1. While a project itself may be housed within one of various available institutional frameworks, an NIU that serves the project should necessarily follow the structure as described in Chapter 1. In the case that a new NIU is being created to support a particular project, it can be incubated within an existing NIU. Subsequently, when the project achieves some level of maturity, the project team and project assets (tangible and intangible) can be spun off. (4.3)
2. The project should prepare a Mission Strategy Document that describes the project, the stakeholders, the broad legal framework, the solution architecture, the nature of the platform, role of the ecosystem, and potential pricing. (4.4)
3. Best teams should be put in place within Government and within the NIU. (4.5)
4. Consultations with stakeholders e.g. multiple levels of Government, other Government Departments, NIU, Banking system (if funds are involved), service providers, and customers and end-users. (4.6)

5. A legal framework, with enabling policies may be necessary for a project to go live. This may require passing a Bill, modifying subordinate regulation in centre and State Acts, or in some cases, a constitutional amendment. A strong legal team working with all stakeholders is a must for every project. (4.7)
6. The project should be rolled out as soon as possible, and iterated rapidly, rather than waiting to roll out a perfect system. (4.8)
7. The Government's role is to set policy, co-ordinate with other Departments, and provide strategic direction, whereas the NIU focuses on execution and implementation. In the early stage, the Government agency / Department works alongside the NIU and as the system starts falling into place, the role of Government changes to:
 - (a) Conducting proof-of-concept studies
 - (b) Giving feedback on mis-features, bugs and additional specifications, and
 - (c) Setting up the institutional capability for scaling. (4.9)
8. Once the rollout is completed, the Government's role shifts largely to that of a customer. It should compute metrics of performance of the system in all respects such as performance, cost, accuracy, and release these into the public domain. Quarterly reviews of the performance of the system should be undertaken. (4.9)

16.5. Multiple levels of Government

1. IT projects that span multiple levels of Governments may be classified into two types:
 - (a) Projects such as GST, NTMA, and EIN where the NIU aids the core function, or aids carrying out a sovereign function of multiple levels of Government.
 - (b) Projects such as NPS, where the core function is carried out by a Central agency, but co-operation among Government agencies is required for the purposes of uniformity, standardization, interoperability to maintain levels of service and drive economies of scale. (5.2)
2. A critical aspect of the success of such IT projects that the solution must be incentive compatible across stakeholders. Common functions should be included in a single application shared by all stakeholders. Such a single application, while respecting the constitutional autonomy of all Governments involved, may be deployed in a decentralized environment, but its development must necessarily be centralized. (5.3)
3. The two activities, consensus building and solution design need not necessarily be sequential. The basic design and the details of the implementation can be put in place while policy details are being debated. (5.4)
4. Common minimum functionality can be built into a Common Portal, in such a way that its basic functionality can be enhanced by local customizations such as look and feel, local languages, and local policies, to mention a few. Such a design allows for low cost, scale, interoperability, speed, simplicity, a uniform customer experience, and portability of service. (5.4)
5. The following steps could be adopted for projects that span multiple levels of Government:
 - (a) identification of all stakeholders;



- (b) formation of an Empowered Committee of representatives drawn from every stakeholder;
 - (c) appointment for all decision making, a smaller Empowered Group;
 - (d) creation of an NIU for the execution of the project. (5.5)
6. The project should release a Mission Strategy Document that guides the implementation. The process laid out for incubation of Government projects and NIUs would foster a coalition for change early on in the life cycle of a project. (5.6)

17

Recommendations for technology challenges

17.1. Solution architecture

1. At the outset of a project, the long term IT strategy should be conceived and published as part of the Mission Strategy Document. A functional system diagram should be created that captures the following at a conceptual level:
 - (a) Role of multiple levels of Government
 - (b) Key business processes and workflows (information flow, funds flow, etc.)
 - (c) Integration with various stakeholders (6.2.1)
2. A structured change management process should be put in place, so that the process is incremental. A principle of least surprise to the user, so that minimal change in user behaviour is required, is a good principle to guide the change management process. (6.2.2)
3. Changes in policy should be accompanied by the corresponding changes in IT systems; the two should go hand-in-hand. (6.2.3)
4. Clean data should be ensured by standardisation of processes, matching and verifying information in workflows, simple and well defined open data formats, electronic payments and processing, instant feedback to customers, incentives for compliance, and penalisation for non-compliance. It is through incentives that data quality can be managed, rather than micromanagement of stakeholders. (6.2.4)
5. Interoperability among multiple service providers is essential to foster competition in the long run. This can only be achieved if interoperability is built into the system architecture from the outset. (6.2.5)
6. The solution architecture should be designed as a Service Oriented Architecture that allows stakeholders to integrate with the IT platform of the project. (6.2.6)
7. conceptualisation of a platform approach to service delivery entails that at the front-end, the data entry and retrieval architecture must be real-time and ubiquitous. In order to enable this, data connectivity at the front-end is

critical. The Government should make it a top priority to provide connectivity ubiquitously. Implementation of Aadhaar for proof of identity and address for telecom connections across all stakeholders should be rolled out for greater telecom inclusion. (6.3.1)

8. In order to minimise errors in identifying individuals (as beneficiaries under various schemes) and firms and ensure foolproof ways for transactions to be authenticated,

- (a) Efforts should be dovetailed with the Aadhaar initiative for unique identification of individuals

- (b) PAN numbers should be used for unique identification of institutions. (6.3.2)

9. Access to bank accounts should be universal, so that Government payments can be made seamlessly. Implementation of Aadhaar for proof of identity and address for opening bank accounts across all stakeholders should be rolled out for greater financial inclusion. (6.3.2)

10. An Aadhaar Payments Bridge should be designed by all stakeholders to ensure seamless delivery of Government payments to beneficiaries. (6.3.2)

11. The Government should closely work with all stakeholders to define a uniform banking interface for Government, so that inter-Government payments may be tightly integrated with internal processes within Government. (6.3.2)

17.2. Openness

1. The use of open standards in the design and implementation of open standards is highly desirable in IT systems. Multiple vendors provide competing solutions that can be used interchangeably with open standards. (7.2)
2. All projects should be active producers and consumers of open data. (7.3)
3. Open source software should be adopted in projects as prudent. (7.4)
4. The Government in partnership with concerned stakeholders should set up an open source foundation to host open source software released by Government projects. (7.4.1)

17.3. Information security

1. As use of mission-critical IT systems becomes widespread within Government, the growing connectivity between these information systems, the Internet and other infrastructure, create opportunities for increasingly sophisticated attacks on such systems. Such attacks may be made by individuals, non-state players, as well as by hostile Nations. It is therefore essential to ensure that any disruptions of critical Government information systems are contained and managed effectively to minimize their impact. (8.1)
2. The security team for important projects must be best in class, and the security solutions must always be cutting edge at all times. (8.1)
3. A Chief Information Security Officer (CISO) should be appointed who is empowered and fully responsible for all aspects of information security: technology, processes, and people. (8.2)

4. Security must be part of the ethos of the organization, and can only be achieved when the entire organization (right from senior management to field personnel) is geared for it. This requires training and awareness on basic facts about information security (strong passwords, how systems are hacked, denial-of-service attacks, social engineering, de-mystifying jargon etc.) all levels. (8.2)
5. Various international standards and best practices can be customized to define a comprehensive certification framework (8.2.1)
6. Technology reviews, process reviews and third party reviews should be conducted on an ongoing basis. (8.2.2)
7. Security should be an integral of the solution architecture, and not an afterthought. As part of the security architecture, the following ideas should be considered: identity, access and entitlement management, host access management, data encryption, data hashing, data classification and data loss prevention, transaction auditing, and interaction security. (8.3)
8. Protections must be put in place to address the threat to security from insiders. (8.4)
9. The security teams of individual projects should integrate with existing agencies set up by the Government such as CERT-In1, and with other frameworks that evolve over time. (8.6)

17.4. Accountability, transparency, and self-corrective forces

1. The architecture of an IT project must be designed keeping a transparency portal in mind. A large IT project produces large volumes of data daily. If a transparency portal is designed as an afterthought, the end result may be lack-lustre. (9.3)
2. The same software architecture for data warehousing, data mining and business intelligence required within an IT project for policy support and analysis can also support the operations required for a transparency portal. (9.3)
3. All the data should be made available in simple, well-defined, machine-readable formats. (9.3)
4. A transparency portal leads to monitoring and feedback at various levels: within the service provider, within Government, and by citizens at large. It is an essential part of self-corrective forces that lead to greater accountability and transparency. (9.4)
5. contact centre closes the feedback loop of self-corrective forces. It establishes multiple channels of communication with all stakeholders, including end-users, for purposes of gathering information and reporting grievances. It should provide service in multiple languages, through multiple channels, and be integrated with the solution architecture of the project. (9.5)
6. Enabling citizens and beneficiaries of public schemes to directly provide feedback using web and mobile phone-based platforms is a powerful way of involving citizens in improving public accountability. It unlocks the potential of collective wisdom. (9.6)

17.5. Protection of the individual

1. The solution architecture of a project should be designed for data protection and privacy from the ground up. (10.2)

2. The privacy framework for a project should be defined early on, which translates the legislation on privacy into implementable rules for IT systems. (10.2)
3. The design of the solution architecture should ensure that any Personal Identifiable Information (PII) is stored safely, and access is carefully monitored. Stringent penalties must be in place to address the issue of unauthorized access of personal data by outside agencies as well as by personnel within the organization. Strict protocols and processes must be in place to detect such access in order that they are dealt with swiftly and in a deterrent manner. This is not only desirable from a privacy perspective, but also from a security perspective. (10.2.1)
4. Anonymization of data is an important aspect of privacy. Data should be carefully anonymized when released publicly, or when shared with other organizations that do not require access to PII, as allowed within the data protection and privacy framework. (10.2.2)
5. Careful thought should be given to anonymization, since naive approaches to de-identifying data are prone to attacks that combine the data with other publicly available information to re-identify individuals. (10.2.2)
6. Data retention and usage policies should be well-defined, especially for PII. In case the legal framework of the project provides for it, an individual should be able to access data stored in the IT system about themselves, after appropriate authentication of their identity. (10.2.3)
7. The right balance between the individuals right to privacy and the larger public interest should be achieved by the data protection framework. While personal information relating to the individual must be strictly protected from unauthorized access, there may be a need for Government agencies to access or share this data for purposes of national security, economic offenses, tax evasion and other specified circumstances. Hence, authorized sharing of information under specified circumstances, ipso facto, should not be considered as a violation of an individuals right to privacy. However, detailed processes, systems and guidelines need to be put in place to ensure that authorized access and sharing is within the parameters set by law. (10.3)

18

Recommendations for Ministry of Finance projects

18.1. Goods and Services Tax

1. The recommendation of EG-IT for the setting up of an NIU Goods and Services Tax Network (GSTN), for managing the IT systems for GST implementation, including the Common GST Portal is endorsed. GSTN will:
 - (a) provide common infrastructure and services to Central and State Governments;
 - (b) ensure integration of the Common GST Portal with existing tax administration systems of Central and State Governments;
 - (c) build efficient and convenient interfaces with tax payers and tax administrators;
 - (d) facilitate, implement and set standards for providing common GST services to the Central and State Governments;
 - (e) carry out research, study global best practices and provide training to the stakeholders. (11.2.1.2)
2. The GSTN project may be incubated within NSDL and the preliminary work of conducting a proof-of-concept is being undertaken by NSDL and it has been planned to run a GST pilot with selected State Governments participating in it along with the CBEC. The infrastructure for the GSTN should be based on latest technology and ring fenced, so that whenever the spin-off takes place, the GSTN infrastructure is smoothly transferred to the proposed NIU being set up as GSTN. (11.2.2)
3. The IT strategy document for GST prepared by the EG-IT, which defines the contours of the IT implementation in respect of the GST Common Portal and its interface with all stakeholders, could form the basis for taking forward the implementation of GSTN. (11.2.2)

4. A dedicated Mission Leader and a dedicated Mission Execution Team should be appointed for GST. An implementation team, comprising of officers drawn from and some of the State Governments (pending the appointment of a full-fledged Mission Team and during the pilot stage) should be set up at the earliest. This team would work along with the teams that would be set up by NSDL for implementing the project. The two teams should together initiate the implementation of the GSTN including such as acquisition of necessary infrastructure, design and development of the application, etc. (11.2.3)
5. The personnel selected to man the implementation team should be trained in the tasks mentioned above. Hiring of talent on contract basis should also be explored as necessary. This team should later be part of the Mission Execution Team. This Team should include professionals with technology and legal expertise. (11.2.3)
6. The Agreement with NSDL should be drawn carefully and with clarity. It should include aspects such as financials, responsibilities of the Government side and NSDL at the incubation stage, acquisition of infrastructure, development of application software, ownership of source code, spin-off to the NIU, and the process of transfer of assets (both tangible and intangible). (11.2.4)
7. Though NSDL is assisting the Government in incubating the GSTN, once GSTN is set up as an NIU, the latter may continue to procure services from NSDL in the initial phases of GST implementation, as it considers necessary. (11.2.4)
8. The GSTN may, as and when it commences its full-fledged operations adopt a business-outcome based, per-transaction pricing model. Even during the period when NSDL is providing such services, a similar approach is recommended. (11.2.4)
9. GSTN will develop and operate the Common GST Portal, which will have common minimal functionality, but will be customizable and extensible by various governments. (11.2.5)
10. GSTN will render the following services through the Common GST Portal:
 - (a) Dealer registration (including existing dealer master migration and issue of PAN based registration number)
 - (b) Payment management including payment gateways and integration with banking systems
 - (c) Return filing and processing
 - (d) Taxpayer management, including account management, notifications, information, and status tracking
 - (e) Tax authority account and ledger Management
 - (f) Computation of settlement (including IGST settlement) between the Centre and States
 - (g) Processing and reconciliation of import GST and integration with EDI systems of Customs
 - (h) MIS including need based information and business intelligence
 - (i) Maintenance of interfaces between the Common GST Portal and tax administration systems
 - (j) Provide training to stakeholders (11.2.5)
11. The CBEC and State Governments may design and develop their own applications to meet requirements for effective tax administration such as audit, intelligence gathering. (11.2.5)

12. The Common GST Portal is a pass-through device for information, while enhancing it with intelligence to plug leakages. It would also act as a tax booster, matching the input tax credits in the returns to detect tax evasion. It can also integrate with various other systems at MCA and CBDT for verification of PAN or other corporate information and perform data mining and pattern detection to detect tax fraud. It would send this information as alerts and reports to the respective tax authorities. It would also compute inter-State settlement, netting IGST across States. (11.3.1)
13. The following important milestones that would facilitate timely implementation should be kept in view:
 - (a) Finalisation of business processes of registrations, returns, and payments
 - (b) Commencement of GST pilot project by NSDL with identified States and Centre.
 - (c) NSDL to set up core functionalities of common portal in pilot and provide APIs for all stakeholders. Limited testing of APIs by participating stakeholders.
 - (d) Engaging with participating entities for pilot including dealers, banks and other Government agencies.
 - (e) Completing the impact analysis for GST and initiating steps to align existing tax systems at the Centre and all States for GST. This would include changes to business and IT infrastructure. Timely financial approvals and procurements would also be critical.
 - (f) Evaluation of Pilot Project resulting in iterative review of processes and IT implementation.
 - (g) Finalisation of detailed project report for actual implementation of GST
 - (h) Attaining clarity on NIU engagement and structure of GSTN.
 - (i) Creation of GSTN and formalising the involvement of NSDL in GST implementation.
 - (j) Finalisation of IGST legal framework and business process.
 - (k) Implementing the stakeholder outreach program
 - (l) Scaling up to GST implementation with administration and organisational restructuring, and training and testing of applications by tax payers and all tax authorities (11.4)
14. The CBEC has set up data centers to run centralized applications for Central Excise, Service Tax and Customs purposes. With the implementation of GST, these and other facilities should be leveraged to the extent possible. An in-depth study (either by an in-house team or by a consultant) of the reusability of the existing ACES project components should be undertaken and necessary steps should be initiated to refashion the same and integrate it with the GST solution. (11.4)

18.2. Tax Information Network

1. The department is at the crossroads of important strategic decisions as the new Direct Taxes Code is to be operationalized from April 2012, requiring major changes in its application system. Although the existing IT related instrumentalities have served the departments needs admirably it may not be advisable to continue with these diverse implementation methodologies. (12.4.1)
2. Considering that its technology needs are large, dynamic, and sensitive from the point of both, security and privacy, the Department clearly needs a dedicated and efficient NIU type organization to set up, manage and run its IT-related infrastructure on long term basis. (12.4.1)

3. The IT Department should prepare a Mission Strategy Document forthwith along with a time bound roadmap for implementation, and all new initiatives should be implemented only in accordance with this Plan. (12.4.2)
4. As part of the preparation of the Mission Strategy Document, the Department must clearly identify IT-related activities and services that it can actively outsource to an NIU and those which it must necessarily handle departmentally. (12.4.2)
5. ITD should directly handle only matters involving policy making, quasi-judicial decision making, exception handling, risk management and enforcement functions. The IT systems required to assist and enable its functionaries in discharge of these should be set up, managed, and run by an NIU. (12.4.2)
6. There is a strong case for a separate well-capitalised and professionally run NIU to handle the IT-related needs of ITD. This should be set up on priority and in accordance with the recommendations in the foregoing chapters. While ITD should retain Board level strategic control, the NIU should have financial autonomy and operational freedom and its affairs. (12.4.2)
7. Such an NIU would necessarily need services of a few departmental officers as domain experts at different levels to enable it to discharge its mandate. It should therefore be possible for suitable departmental officers to be deputed to the NIU for a defined period while retaining lien on their cadre posts. The relevant Rules may be accordingly modified to enable deputation/secondment of a few officers to the proposed NIU. (12.4.2)
8. The multiplicity of platforms should be replaced by a uniform, holistic, rule-based application matrix so as to integrate all the elements of tax collection process through technology with information seamlessly flowing to the users for informed decision making. (12.4.2)
9. The Ministry of Finance should develop the next generation Risk Information Network to enhance the effectiveness and impact of tax collection using functionalities such as comprehensive taxpayer profiling, trend analysis, pattern recognition, and data mining of the information gathered in IT Department, GST, and Customs systems. (12.4.2)
10. Simultaneously, the IT Department needs to restructure and reorganise the Directorate of Systems and re-define its role as the department's single point interface with the NIU so as to take full advantage of the NIU model. As part of this exercise, it may also re-determine the strength of its technical cadres and restructure the same. (12.4.2)

18.3. Expenditure Information Network

1. The establishment of an integrated Expenditure Information Network can help achieve the following objectives:
 - (a) monitoring scheme-wise release of funds and outcomes;
 - (b) helping in budgeting, planning and decision making based on the evaluation of all plan schemes;
 - (c) maintaining time-series information related to each implementing agency, which will enable in evaluating performance;
 - (d) ensuring disbursement of funds to intended beneficiaries;
 - (e) ensuring timely disbursement of funds;
 - (f) reducing float of funds within the system;

- (g) up-to-date and near real-time information on utilization of funds;
 - (h) monitoring of outcomes up to the last mile; and
 - (i) transparency in disbursal and utilization of funds by making information available in public domain by way of a transparency portal. (13.1.2)
2. The NIU framework should be followed in setting up the EIN. Aspects such as allocation of tasks between the Government and the NIU, appointment of a dedicated Mission Leader and a dedicated Mission Execution Team may be along the lines of the recommendations contained in this report. (13.2)
 3. The relationship between the Government and the NIU may be defined by an Agreement as described in this report.
 4. EIN may be incubated as per the recommendations in Chapter 4 of this report. Lessons from the experience of setting up GSTN should be adopted in setting up the NIU for the implementation of EIN. (13.2)
 5. The EIN solution should ensure balance between standardisation of features and autonomy of States
 6. Appropriate incentives should also be devised for full participation at all levels of Government. (13.2)
 7. The Central Expenditure Repository (CER) will handle the information flow. The flow of funds will be managed through the banking system. EIN will track all authorizations and forward electronic instructions to banks, so that funds move only against actual expenditure to service providers. (13.3)
 8. Planning Commission, Ministries, Departments, and Program Divisions can be linked to CER and should be able to monitor the outcomes, utilization and fund status through near real-time availability of information about all entities and programs. (13.3)
 9. All the agencies such as State bodies, district bodies, village panchayats, block level bodies, and beneficiaries should have access to EIN with appropriate access controls. These agencies can view the funds sanctioned for them and also update the status of utilization of funds by them. (13.3)
 10. For greater transparency, citizens should also have access to a transparency portal and information from the ground can be crowd-sourced. (13.3)
 11. All financial information made public through a transparency portal should be machine-readable and format-neutral. (13.3)
 12. The EIN project is similar to the GST project in many ways. Some of the processes touch more agencies and involve more steps. The Group recommends that the measures suggested for GST may be suitably adapted for the implementation of EIN. (13.3)

18.4. National Treasury Management Agency

1. The NIU framework as described in this report is recommended for the administration of NTMA. (14.2)
2. As recommended in the Report of the Internal Working Group on Debt Management, NTMA should have a dedicated team to manage its operations. The HR structure for Government teams (consisting of a Mission Leader and Mission Execution Team) as recommended in this report should be adopted for NTMA. (14.2)

3. The WG has recommended a solution architecture for NTMA, which may be adopted. (14.3)
4. The WG has also provided detailed steps for incubation, which span legal issues, setting up of IT systems, and change management for transferring the functions from RBI to NTMA. The incubation framework, and creation of the platform described in the WG report may be adopted. (14.3)

18.5. New Pension System

1. In order for a well-ordered and mature pension business to develop in the country,
 - (a) All pension and provident fund streams should converge in the medium term;
 - (b) Costs to go down dramatically due to competition and economies of scale; and
 - (c) Rule-based regulations need to give way to principles / risk-based supervision. (15.4)
2. An enabling legal framework that provides the necessary impetus for NPS should be provided. (15.4)
3. The tax treatment of the NPS also needs to be rationalized to provide for, at least equal treatment with other retirement products and providers. (15.4)
4. There is an imminent need to create a certain level of awareness amongst the NPS subscribers that will eventually empower them to make well informed investment choices to protect and further their own interests. (15.4)
5. As the broader mandate of the PFRDA is to regulate the pension sector in the country, this may eventually necessitate the separation of the NPS administration, including marketing and distribution strategies, from the PFRDA. (15.4)
6. NPS should to create a daily MIS with facts about number of subscribers, assets under management, the breakdown of number of subscribers and assets under management under various heads of Government, the number of switches made by customers from one fund manager to another, the returns of the various schemes of various pension fund managers, and summary statistics about the returns obtained by NPS members. The daily release of this information base is essential for policy analysis and the creation of self-correcting forces. (15.4)
7. NPS needs to create an audit mechanism whereby every year, for randomly chosen customers in a statistically meaningful way, a comprehensive review is undertaken about correctness of data, about whether contributions came in on time, and about whether each member was notified about every contribution. The results of this audit should be released into the public domain. This will yield a regular check upon the quality of performance of NPS. (15.4)
8. There is a need to avoid splitting the functionality of NPS across multiple variants of the same product, since the existence of variants reduce portability for customers and increase cost. (15.4)
9. While significant strides in IT implementation have been undertaken in the NPS, there is a need to further leverage recent technological innovations in e-Governance, banking, and financial networks to develop greater efficient mechanisms that leverage use of IT in an end-to-end manner (15.4)
10. More specifically, initiatives may be taken in the following areas to develop a comprehensive integrated pension administration system:

- (a) Enabling linkages with HR and payroll systems of the Central and State Governments to obtain subscriber contribution details, among other things
 - (b) Revamping and automating all pension administration processes
 - (c) Re-engineering in the context of the user departments, especially in areas related to Government accounting formations
 - (d) Providing process linking between Government accounting systems and the pensions administration system
 - (e) The implementation of these initiatives should be accompanied by extensive skill enhancements, learning and change management efforts, in conjunction with nationwide public awareness campaigns. (15.4)
11. As the Aadhaar implementation becomes ubiquitous across the country, there is a need to establish the platform for linking the Aadhaar with the PRAN number, which can enable Aadhaar-linked KYC for pension scheme enrollment. In this aspect, the NPS should also explore opportunities for future integration with the identification and authentications systems of the Unique Identification Authority of India (UIDAI). (15.4)



Report of the Task Force on Goods & Services Tax

Thirteenth Finance Commission

15th December, 2009

Task Force

Chairman

Arbind Modi, IRS
Joint Secretary
Department of Revenue

Members

V. Bhaskar, IAS
Joint Secretary
Thirteenth Finance Commission

B.S. Bhullar, IAS
Joint Secretary
Thirteenth Finance Commission

Dr Rathin Roy
Economic Advisor
Thirteenth Finance Commission

Dr Ajay Shah
Senior Fellow
National Institute of Public Finance and Policy

Dr. Kavita Rao,
Senior Fellow
National Institute of Public Finance and Policy

Ritvik Pandey, IAS
Deputy Secretary
Thirteenth Finance Commission

Convener

R.N. Sharma
Jt. Director
Thirteenth Finance Commission

Acknowledgements

We would like to convey our sincere thanks to the Thirteenth Finance Commission, Government of India for having granted us this opportunity to make our recommendations on various issues relating to the design and implementation of the Goods and Services Tax (GST).

During our study over more than 18 months, we interacted with large number of experts and officials from both the Central Government and State Governments. We have immensely benefited from their advice and thoughtful inputs. In particular, we would like to thank Dr. Vijay Kelkar, Prof. Atul Sarma, Prof. Indira Rajaraman, Shri B. K. Chaturvedi, Dr. Sanjiv Misra and Shri Sumit Bose for their constant guidance and insightful suggestions. We are also thankful to Dr. Parthasarathi Shome for guiding us in this endeavor.

Our sincere thanks are also due to Shri P. V. Bhide, Shri K. Jose Cyriac, Shri Vivek Johri, Shri Gautam Bhattacharya, Shri R. Sekar and Shri Sushil Solanki for their comments and views on various aspects of our work.

Shri Satya Poddar was extremely helpful in providing us with all the intellectual resources and framing the issues on various aspects of the Goods and Services Tax. He was extremely generous with his time and resources in making numerous presentations to the Task Force on various design and implementation issues relating to GST. We would like to convey our sincere thanks to him.

We are also grateful to Dr. Asim Dasgupta, Shri Satish Chandra and other officials in the Empowered Committee of State Finance Ministers and other officials of various State Governments.

This Report could not have been completed without the assistance of Shri K. Ravi, Smt. Geetha Govind and Shri Ranjan Giri. We would like to place on record our deep appreciation of their painstaking and continued support through this period of 18 months.

Contents

Executive Summary	i
CHAPTER – I	1
Introduction	1
CHAPTER-II	4
Goods and Services Tax: The Model	4
a. Single GST versus Dual GST	4
b. Type of GST – Consumption, income or production.....	5
c. Origin versus Destination Principle	9
d. Method of Computation	10
e. Treatment of capital goods.....	12
f. Exemption from GST	13
g. Treatment of petroleum products.....	17
h. Treatment of tobacco goods and alcohol	19
i. Treatment of natural gas	19
j. Treatment of the power sector.....	20
k. Treatment of transport services	21
l. Treatment of financial services.....	22
m. Treatment of immovable properties	23
n. Place of supply rules	27
o. Threshold Limit for registration of GST dealers	31
p. Treatment of Small Scale Industries	32
q. Area based exemptions	33
r. Treatment of Special Economic Zones.....	35
CHAPTER – III	36
Treatment of Inter-State transactions	36
CHAPTER - IV.....	48
Administrative Structure.....	48
a. Registration of taxpayers	48

**Report of the Task Force on Goods and Services Tax
Thirteenth Finance Commission**

b. GST invoice.....	50
c. Periodicity of GST Payment.....	51
d. Administrative structure	51
CHAPTER - V	54
Rates of Tax.....	54
I. Single or Multiple Rates	54
II. Determination of the rate of GST	60
a. Taxes to be subsumed in the GST	61
b. Estimation of the GST base	62
1. Subtractive – indirect method (SI method)	63
• Exempt sectors.....	71
• Taxable sectors.....	72
2. Consumption Method.....	75
i. Task Force Estimate.....	75
ii. NCAER Estimate	78
3. Shome Index Method.....	80
4. Revenue Method.....	82
c. The Revenue Neutral Rate(RNR)	85
Chapter - VI	87
Revenue Performance of GST	87
CHAPTER - VII.....	92
Implications of the Goods and Services Tax	92
a. GST and economic growth	92
b. GST and International Trade	96
c. GST: Equity and Poverty reduction	97
d. GST and Prices.....	100
e. GST and informal sector.....	101
f. GST and Fiscal management	102
g. GST and vertical balance of power	103
CHAPTER - VIII.....	104
“Flawless” Goods and Services Tax and the autonomy of States	104

**Report of the Task Force on Goods and Services Tax
Thirteenth Finance Commission**

CHAPTER - IX	109
Incentivising States to adopt GST	109
CHAPTER - X	112
Goods and Services Tax - The way forward	112
Chapter-XI	117
Conclusion.....	117
Annexures	121
Terms of Reference of the Task Force	136
References	137

Executive Summary

1. The taxation of goods and services in India has, hitherto, been characterised as a cascading and distortionary tax on production resulting in mis-allocation of resources and lower productivity and economic growth. It also inhibits voluntary compliance. Therefore, it is necessary to replace the existing indirect tax system by a new regime which would foster the achievement of the following objectives:

- (a) The incidence of tax falls only on domestic consumption;
- (b) The efficiency and equity of the system is optimized;
- (c) There should be no export of taxes across taxing jurisdictions;
- (d) The Indian market should be integrated into a single common market;
- (e) It enhances the cause of cooperative federalism. **(Para 2.1)**

2. A well designed 'value added tax on all goods and services (GST) is the most elegant method of eliminating distortions and taxing consumption. Under this structure, all different stages of production and distribution can be interpreted as a mere tax pass-through, and the tax essentially 'sticks' on final consumption within the taxing jurisdiction.

(Para 2.2)

3. The 'flawless' GST recommended by us comprises of the following elements:

- i. It should be a dual levy imposed concurrently by the Centre and the States, but independently to promote cooperative federalism. **(Para 2.4)**
- ii. Both the Central Goods and Services Tax (CGST) and the State Goods and Services Tax (SGST) should be levied on a common and identical base. **(Para 2.4)**
- iii. The Centre and the States should adopt a consumption-type GST¹, that is, there should be no distinction between raw materials and capital goods in allowing input tax credit. **(Para 2.7)**

¹ Reference to GST in this Report includes both CGST and SGST

- iv. The tax base should comprehensively extend over all goods and services upto the final consumer point. **(Para 2.7)**
- v. There should be no classification between goods and services in law so as to ensure that there is no classification dispute. **(Para 2.7)**
- vi. The GST should be structured on the destination principle. As a result, the tax base will shift from production to consumption whereby imports will be liable to both CGST and SGST and exports should be relieved of the burden of goods and service tax by zero rating. Consequently, revenues will accrue to the State in which the consumption takes place or is deemed to take place; **(Para 2.13)**
- vii. The computation of the CGST and SGST liability should be based on the invoice credit method i.e., allow credit for tax paid on all intermediate goods or services on the basis of invoices issued by the supplier. As a result, all different stages of production and distribution can be interpreted as a mere tax pass-through, and the tax will effectively 'stick' on final consumption within the taxing jurisdiction. This will facilitate elimination of the cascading effect at various stages of production and distribution. **(Para 2.16)**
- viii. The CGST and SGST should be credited to the accounts of the Centre and the States separately. Since the CGST and SGST are to be treated separately, taxes paid against the CGST should 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. Cross utilization of ITC between the CGST and the SGST should not be allowed. **(Para 2.16)**
- ix. Full and immediate input credit should be allowed for tax paid (both CGST and SGST) on all purchases of capital goods (including GST on capital goods) in the year in which the capital goods are acquired. Similarly, any kind of transfer of the capital goods at a later stage should also attract GST liability like all other goods and services. **(Para 2.18)**
- x. Ordinarily, there should not be any exemption from CGST or SGST. However, if for some reason, it is considered necessary to provide exemption, the Centre and the

States should draw up a common exemption which should be restricted to the following:-;

- a. All public services of Government (Central, State and municipal/panchayati raj) including Civil administration, health services and formal education services provided by Government schools and colleges, Defence, Para-military, Police, Intelligence and Government Departments. However, public services will not include Railways, Post and Telegraph, other commercial Departments, Public Sector enterprises, banks and Insurance, health and education services;
 - b. Any service transactions between an employer and employee either as a service provider, recipient or vice versa;
 - c. any **unprocessed food article** which is covered under the public distribution system should be exempt regardless of the outlet through which it is sold; and
 - d. **education services** provided by non-Governmental schools and colleges; and
 - e. **health services** provided by non-Governmental agencies. **(Para 2.26)**
- xi. The SIN –goods comprising of emission fuels, tobacco products and alcohol should be subject to a dual levy of GST and excise. No input credit should be allowed for excise. However, industrial fuels should be subjected only to GST (both Central and State) with the benefit of input credit like any other intermediate good.
(Paras 2.27 to 2.32)
- xii. all inter-state transactions in goods and services should be effectively zero rated by adopting the Modified Bank Model. **(Paras 3.1 to 3.19)**
- xiii. the consignment sales and branch transfers across states should be subject to treatment in the same manner as if it was a inter-state transaction in the nature of sale between two independent dealers. **(Para 3.20)**
-

- xiv. the function of all state border check posts should be reduced to checking contrabands by setting up large scanners for trucks to pass through without any need for physical verification. The cost of the scanners should be entirely borne by the Central Government. All check-posts should be jointly manned by both States so as to reduce the number of check-posts and enhance efficiency in the road movement of goods. **(Para 3.20)**
- xv. Keeping in view the compliance cost and administrative feasibility, small dealers (including service providers) and manufacturers should be exempted from the purview of both CGST and SGST if their annual aggregate turnover (excluding both CGST and SGST) of all goods and services does not exceed Rs.10 lakh. However, like in most other countries, those below the threshold limit may be allowed to register voluntarily to facilitate sales to other registered manufacturers/dealers, limit competitive distortions and avoid inequities. Further, the threshold exemption limit should be uniform for both CGST and SGST and across States. **(Paras 2.61 and 2.62)**
- xvi. Further, with a view to reduce administrative and compliance burden, small dealers with annual aggregate turnover of goods and services between Rs.10 lakh to Rs.40 lakh² may be allowed to opt for a compounded levy of **one percent**, each towards CGST and SGST. However, no input credit should be allowed against the compounded levy or purchases made from exempt dealers. **(Para 2.63)**
- xvii. Certain high value goods comprising of (i) gold, silver and platinum ornaments; (ii) precious stones; and (iii) bullions (hereafter referred to as “high value goods”) are prone to smuggling due to high tax incidence thereby generating negative externalities in terms of social and economic disorder. Therefore, we recommend that dealers in such high value items may, subject to the threshold exemption but without the ceiling of Rs. 40 lakh, also be allowed to opt for the compounded levy of **one percent**, each towards CGST and SGST. **(Para 2.64)**

² The limit of Rs 40 lakh is based on the consideration that dealers with turnover of Rs 40 lakh or more are subject to tax audit under the Income Tax Act, 1961 and therefore they would suffer from many additional burden in terms of documentation under the GST.

- xviii. The existing **exemption upto Rs.1.5 crores of turnover for small-scale industries should not be continued under the GST framework**. However, in order to inspire confidence of the small scale industry in the new GST framework, the scrutiny/audit of the small scale industry should be conducted only by the state tax administration. The enforcement by the State tax administration would be adequate to even deal with CGST evasion. **(Paras 2.66 and 2.67)**
- xix. The area based exemption in respect of CENVAT **should not be continued** under the GST framework. In case it is considered necessary to provide support to industry for balanced regional development, it would be appropriate to provide direct investment linked cash subsidy. **(Para 2.74)**
- xx. Since the GST is designed to ensure that all producers and distributors are treated as complete pass-through and exports are zero-rated, there **should be no exemption for the developers of, or units in, the Special Economic Zones**. **(Para 2.75)**
- xxi. The tax regime for power sector, vehicles, goods and passengers, financial services and the real estate and housing services sector should be reformed and integrated into the GST framework along the lines summarized in the paragraphs 4 to 7 and explained in detail in Chapter-II.
- xxii. The rate of CGST and SGST on all non-SIN goods and services should be fixed at a single positive rate of 5 per cent and 7 per cent, respectively. In addition, there should be a zero rate applicable to all goods and services exported out of the country. **(Paras 5.9 and 5.79)**
- xxiii. The following central taxes should be subsumed in the CGST³:
- a. Central Excise Duty (including Additional Excise Duties);
 - b. Service Tax;
 - c. Additional Customs Duty (commonly referred to as 'CVD');
 - d. Surcharges and all cesses

(Para 2.11)

³ This is consistent with the proposal of the EC in their Discussion paper dated 30th April, 2008.

xxiv. The following State level taxes, as also recommended by the Empowered Committee (EC) in its discussion paper dated 30th April, 2008, should be subsumed in the SGST:-

- a. VAT/Sales Tax (including Central Sales Tax and Purchase tax);
- b. Entertainment tax (other than levied by local bodies);
- c. Entry taxes not in lieu of Octroi;
- d. Other Taxes and Duties (includes Luxury Tax, Taxes on lottery, betting and gambling, and all cesses and surcharges by States);

Since all taxes on goods and services, levied by the Centre or the States, should be subsumed in the GST, the following other taxes levied by the States on goods and services should also be subsumed:

- i. Stamp duty;
- ii. Taxes on Vehicles;
- iii. Taxes on Goods and Passengers; and
- iv. Taxes and duties on electricity. **(Para 2.11)**

xxv. Any amount collected through these taxes on the SIN goods should not be subsumed either in the CGST or the SGST. Similarly any amount which is collected as tax/fee/charge/cess which is essentially in the nature of a user charge for supply of goods and services (including environmental goods and services) also should not be subsumed under the CGST or SGST. Further, both Centre and the States should take steps to consolidate all taxes (other than proposed GST) on the SIN goods as a single levy termed as Central Excises and State Excises, respectively. **(Para 2.11)**

xxvi. All entry and Octroi duties levied by the third-tier of Government must be abolished. **(Para 2.11)**

4. The **power sector** must form an integral part of the comprehensive GST base recommended by us over which both the Central and State Governments would have concurrent jurisdiction. The tax regime for the power sector should be the same as in the case of any other normal good. The electricity duty levied by the States should be subsumed

in the SGST. Article 278 and Article 288 of the Constitution should be amended to enable levy of GST on supply of electricity to Government at all levels like any other normal goods.

(Para 2.35)

5. The **tax on vehicles and the tax on goods and passengers** levied by the State Governments should be subsumed in the GST. All transport equipments and all forms of services for transportation of goods and services by railways, air, road and sea must form an integral part of the comprehensive GST base recommended by us over which both the Central and State Governments would have concurrent jurisdiction. The tax regime for the transport equipments and transport services should be the same as in the case of any other normal goods.

(Para 2.38)

6. The **consumption of financial services** should be comprehensively taxed under the GST framework on the basis of the full taxation method.

(Paras 2.39 to 2.41)

7. The **real estate sector** should be integrated into the GST framework by subsuming the stamp duty on immovable properties levied by the States to facilitate input credit and eliminate cascading effect. The new GST regime for immovable property transactions and real estate services should be designed on the lines of the comprehensive taxation method. Therefore, the new regime would comprise of the following elements: -

- a. The GST should apply for all newly constructed property (both residential and commercial). If it is self-used by the person who constructed it, the GST should be applied on the cost of construction. If it is sold or transferred, the GST should be applied on the consideration received at first transfer or sale. In both cases, credit should be allowed in respect of input tax paid on raw materials used in construction.
- b. Rental charges received (excluding imputed rental values) in respect of leasing of immovable property used for both residential and commercial purposes should be charged to GST. Input tax credit would be allowed only in

respect of input tax paid on goods and services used for maintenance. No input tax credit should be allowed in respect of tax paid on construction or acquisition of the property or tax paid on improvements thereto. All secondary market transactions in immovable properties (whether constructed before or after the introduction of GST) should be liable to GST. However, if the property has been constructed after the introduction of GST, the GST should be levied on the resale value and input tax credit should be allowed in respect of the GST paid upon construction or purchase of the property after making adjustment for inflation. If the property has been acquired by the seller before the introduction of GST, the GST should be levied on the difference between the sale price and the cost of acquisition and improvements thereto. In such cases, no input tax credit would be allowed.

- c. The adjustment for inflation may be made on the basis of the same inflation index as provided for the purposes of determination of capital gains under the Income-tax Act, 1961.
- d. The new regime will also be subject to the threshold exemption of Rs.10,00,000/- for small businesses thereby eliminating the problem of excessively large number of landlords seeking GST registration.
- e. Immovable property will also include land and, therefore, the new regime will also be applicable to land transactions. However, where land is used for construction of a property, it will be treated as an input. In such cases, the GST paid in respect of land will be allowed as input tax credit in the same manner as other inputs used in construction.
- f. The State Governments would continue to perform essential asset registry functions, and enforces property rights associated with them. These functions are comparable to those of a depository on the markets. The registration fees can be interpreted as user charges for these records keeping functions – which justify small charges. The imposition of large scale

indirect taxes through registration and stamp duties constitutes a case of erroneous tax policy. Therefore, States may continue to levy a registration fee at a specific rate not exceeding Rs 1000 per transaction in immovable property, which is merely a user charge for the IT systems used in property registration.

Since the new regime will impart greater transparency through market mechanism, it will also strike a major blow to the underground economy. Therefore, it is imperative that the reform of the present system of taxation of immovable property transaction and real estate services forms an integral part of the proposed GST design. **(Paras 2.42 to 2.48)**

8. In the context of the GST, it is necessary to resolve the problem relating to the **treatment of inter-state sales/transfers** in a manner that the incidence of the tax falls on the consumption of commodities without any distortionary cascading effect and the revenue accrues to the State where the final consumer is located. After analysing the various Models, we recommend a Modified Bank Model, which comprises, inter alia, of the following functional components:-

- (i) In the course of inter-state B2B supply, the seller in the origin State shall collect the SGST leviable on the transaction from the buyer in the destination State as if the sale was within the origin State.
- (ii) The seller would issue an invoice to the buyer indicating the details of the transaction (including the date of the transaction) and his business identification number (BIN).
- (iii) The seller shall use the input SGST for payment of the output SGST on both intra-state and inter-state transactions. To the extent total output SGST is in excess of the input SGST, the same shall be paid into any of the authorised bank in the prescribed manner. This will ensure a self-adjustment mechanism for input credit thereby minimizing the need for issue of refunds.

- (iv) The buyer in the destination State shall make use of the SGST so paid in the State of origin for making payment of output SGST in the destination State.
- (v) All registered dealers across the country shall pay the sum due as CGST and SGST to the credit of the Central Government and all other States within one week from the end of the month to which the sale transactions relate.
- (vi) The Central Government and State Governments shall jointly identify a nodal bank to receive the collection of CGST and SGST by collecting banks. The nodal bank will also receive all information relating to purchase and sale by registered dealers.
- (vii) The nodal bank shall host the IT infrastructure, provide payment gateway to all banks in India and provide screen-based upload or file upload facility for receiving payment and transaction information.
- (viii) It would be mandatory for all registered dealers to make the payment by electronically furnishing Form No. GST-I, which would be a combined monthly payment and return form for all intra-state and inter-state transactions..
- (ix) As far as the registered dealer is concerned, he would be required to make a **single payment** of the aggregate of all sums due to the Centre and all other States. Even though he would have collected tax in the Origin State for inter-state transactions with buyers in a number of destination States, he can fulfil his obligation of directly remitting the tax so collected to all the destination states through a single payment made along with the electronic furnishing of Form No. GST-I. This mechanism will have the benefit of extremely low compliance cost.
- (x) It would be mandatory for all registered dealers to make electronic payment of CGST and the SGST by electronically remitting it in to the RBI, SBI or any authorized bank.

- (xi) The procedure for making payment of CGST and SGST and furnishing information relating to transactions of both purchases from and sales to registered dealers in Form No. GST-I shall be as explained in para 3.12.

9. It is now well-recognised that **tax administration** is tax policy. An inefficient tax administration will not be able to provide the requisite level of deterrence thereby leading to non-compliance and under performance of the tax regime. Therefore, the full potential of the pure tax regime will remain unrealised. Hence, the structure, design and the business process of the tax administration is an important factor in the determination of the revenue performance. The Central Board of Excise & Customs (CBEC) shall be responsible for implementing the CGST and the State Tax administrations will be separately responsible for implementing the SGST. The various tax administrative functions such as assessment, enforcement, scrutiny and audit should be undertaken by the CBEC in respect of the CGST and by the State tax administration in respect of the SGST subject to our recommendation on small-scale industries. However, from a taxpayer's perspective all compliance and enforcement procedures under CGST and SGST should be uniform. The Central Government shall establish a common IT infrastructure which will serve the needs of both CGST and SGST. **(Para 4.8)**

10. The jurisdiction between the CBEC and the State Administration may be divided between the two in such manner that the interface of the taxpayer is confined to one tax administration only. The basis for division could be turnover or any other criteria which is considered reasonable so that the compliance and administrative burden is minimized. **(Para 4.8)**

11. All persons with annual aggregate turnover of goods and services exceeding Rs.10 lakh (excluding CGST and SGST) should be required to register and obtain a GST registration number. Persons with lower turnover may be allowed an option to register. The GST registration number should be a twelve digit alpha numeric number. The first ten digits should be the alpha-numeric Permanent Account Number (PAN) followed by a space and

two more digits indicating the state code. This number scheme should be publicised widely and should be self-generated after obtaining a PAN. (Para 4.4)

12. The unit of taxation for the purposes of GST should be persons as defined under the Income Tax Act. Consequently, for the purposes of CGST, all production units/branches of a person located anywhere in the country will be treated as a single taxable entity eligible for CGST input credit across units/branches. Similarly, for the purposes of SGST, all production units/branches of a person located anywhere within the State will be treated as a single taxable entity eligible for SGST input credit across units/branches in that State.

13. The payment of tax and the transaction reporting should be made through a combined payment and transaction reporting statement in Form No. GST-I. This statement should detail all business to business transactions relating to sales. This statement should be common for both CGST and SGST compliance and it should be mandatory to file this statement electronically on a monthly basis while making payment of taxes. The VAT period should be a calendar month. (Para 4.8)

14. The administration of this **levy should be based on audited accounts** and not on the basis of any form of physical controls. Since the tax base will be common, there should be a **common appellate authority**. Similarly, the Authority for Advance Ruling should also be common. Best international practices should be embedded in the Central-GST, particularly in respect of laws relating to levy of penalties, and circumstances and method of prosecution. No authority should have any power to make preventive detention for the purposes of CGST and SGST. Procedures for collection of both the CGST and SGST should be uniform. (Para 4.8)

15. Another important element of the taxpayer information base is the **VAT invoice**, which forms the primary source of information and therefore a crucial control document of VAT. In an invoice based VAT system, the issue of invoices in the proper form is an essential part of the procedure for imposing and enforcing the VAT. Therefore, it should be mandatory for a supplier making a taxable supply to another taxable person to provide a

VAT invoice with that supply or the payment for it. The requirement should be enforceable by some penalty. The VAT invoice should be standardised across all states so as to contain a minimum of information about the supply being invoiced. **(Para 4.6)**

16. The choice of a single or a multiple VAT rates is extremely critical to the efficiency and performance of the GST. In terms of best international practice, recent experience shows that the preference of the policymakers is for adoption of a single rate as it is more efficient. Therefore, we recommend one **positive rate**, each for CGST and SGST on all goods and services. In addition, there should be a **zero rate** applicable to all goods and services exported out of the country. **(Para 5.9)**

17. One of the crucial issues relates to the determination of the rate of CGST and SGST. Since the GST is primarily intended as an exercise in reforming the consumption tax in India and not an exercise for additional resource mobilisation through discretionary changes, the CGST and SGST rates should be such rates which would yield the same revenue as collected from the various taxes which will be subsumed in the CGST and SGST, that is, it should be a '**revenue neutral rates**' or '**RNR**'). **(Para 5.17)**

18. Using **the fiscal year 2007-08 as the base year for calculation of the RNR, we first estimate the GST base under five different methods**. These methods are (i) Subtraction-Indirect Method; (ii) Consumption Method-Task Force Estimate; (iii) Consumption Method-NCAER Estimate; (iv) Shome Index Method; and (iv) Revenue Method. The various estimates of the GST Base for 2007-08 are summarized in Table-10. The Task Force estimate of the GST Base using the Consumption method is the highest (Rs.37,43,077 crores) whereas the Shome Index method provides the lowest estimate. All other estimates fall within this range. Since the five estimates are different, we use their average (Rs 31,25,325 crores) as the size of the comprehensive GST base for 2007-08 for the purposes of estimating the RNR. Since the tax base for both the CGST and the SGST are proposed to be identical, we use the same tax base for calculating the RNR for both levies. **(Paras 5.22 to 5.75)**

19. Given the estimate of the GST Base and the level of central taxes which are intended to be subsumed in the GST, we estimate the RNR for the CGST at 5.0 percent. Similarly, the RNR in respect of the state level TF-taxes which are proposed to be subsumed in the SGST is estimated to be 6.0 percent. **Therefore, the combined RNR is estimated to be 11 percent.** Incidentally, this estimate is the same as estimated by Poddar and Bagchi in their pioneering study published in November, 2007. These estimates do not factor in the revenue gains from increased compliance and GDP. To the extent, the flawless GST will reduce cascading effect, there will be significant increase in the corporate profits and hence corporate tax collections. Hence, in actual practice, the RNR of 11 percent will be revenue positive. However, all entry and Octroi taxes by state governments and other sub-national Governments are also proposed to be abolished. Accordingly, it is imperative to provide for an alternate buoyant source of revenue to the third-tier of Government. Hence, we recommend the following:-

- i. The rate of CGST and SGST on all non-SIN goods should be fixed at the **single rate of 5 percent and 7 percent, respectively;**
- ii. A formula-based devolution of an amount equivalent to collection of SGST at **2 percentage points** should be made to the third-tier of Government after an appropriate Constitutional Amendment;
- iii. The formula should be based on the recommendations of the State Finance Commission.
- iv. Pending Constitutional Amendment, the collection from 7 percent SGST shall accrue to the State Government and devolution to the third-tier Government should continue to be made on the basis of the recommendations of the State Finance Commission.
- v. Both the Central and the State Governments may continue to levy taxes, in addition to the CGST and SGST, on the various non-SIN goods as at present.

(Paras 5.76 to 5.79)

20. High import tariffs, excises and turnover tax on domestic goods and services have enormous cascading effects, leading to a distorted structure of production, consumption and exports. The existing tax system introduces myriad distortions which favour some goods and services at the expense of others. These distortions yield inefficient resource allocation and consequently, inferior GDP growth. The introduction of the GST will bring about a macroeconomic dividend by reducing what have been called the “negative grey area dynamic effects” of cascading taxation. As a result it reduces the overall incidence of indirect taxation by removing the many distortionary features of the present indirect tax system. The switchover to a flawless GST will have significant macroeconomic effects. The overall macroeconomic effect of reduction in economic distortions due to GST would be to It would provide an impetus to economic growth. Using CGE Model, the NCAER study commissioned by the Thirteenth Finance Commission estimates the impact of the introduction of a GST which would eliminate all taxes on production and distribution and rest on final consumption only. The study is based on two important assumptions of full employment and that 50 percent of indirect taxes remain embedded and ‘stick’ on production and distribution. The study concludes that ‘implementation of a comprehensive GST in India will lead to efficient allocation of factors of production thus leading to gain in GDP and exports. This would translate into enhanced economic welfare and returns to the factors of production, i.e. land, labour and capital. The gains in real returns to land range between 0.42 and 0.82 per cent. Wage rate gains vary between 0.68 and 1.33 per cent. The real returns to capital would gain in the range of 0.37 and 0.74 percent.’ Further, the study also shows that ‘implementation of GST across goods and services is expected, ceteris paribus, to provide gains to India’s GDP somewhere within a range of 0.9 to 1.7 per cent. The corresponding change in absolute values of GDP over 2008-09 is expected to be between Rs. 42,789 crore and Rs. 83,899 crore, respectively. **(Paras 7.1 to 7.5)**

21. These additional gains in GDP, originating from the GST reform, would be earned during all years in future over and above the growth in GDP which would have been achieved otherwise. The present value of the GST-reform induced gains in GDP may be computed as the present value of additional income stream based on some discount rate.

Assuming the long-term real rate of interest of about 3 per cent as the discount rate, the present value of total gain in GDP is computed as between Rs. 1,469 thousand crores and 2,881 thousand crores. The corresponding dollar values are \$325 billion and \$637 billion or as much as one-third to one-half of the country's GDP for the year 2009-10. **(Para 7.6)**

22. Gains in exports are expected to vary between 3.2 and 6.3 per cent with corresponding absolute value range as Rs. 24,669 crore and Rs. 48,661 crore. Imports are expected to gain somewhere between 2.4 and 4.7 per cent with corresponding absolute values ranging between Rs. 31,173 crore and Rs. 61,501 crore. **(Para 7.11)**

23. The benefit to the poor from the implementation of GST will flow from two sources: first through increase in the income levels and second through reduction in prices of goods consumed by them. The proposed switchover to the 'flawless' GST should, therefore, be viewed as pro-poor and not regressive. Hence, the switchover will improve the vertical equity of the indirect tax system. Similarly, to the extent it will impose a higher burden on the informal economy by reducing the cascading effect, the switchover will also improve horizontal equity. **(Para 7.22 and Para 7.29)**

24. Prices of agricultural commodities and services are expected to rise. Most of the manufactured goods would be available at relatively low prices especially textiles and readymade garments. The prices of agricultural goods would increase between 0.61 and 1.18 percent whereas the overall prices of all manufacturing sector would decline between 1.22 and 2.53 percent. Consequently, the terms of trade will move in favour of agriculture between 1.9 to 3.8 percent. The increase in agricultural prices would benefit millions of farmers in India. Similarly, the urban poor will also benefit from new employment opportunities. With regard to the food crops the poor would continue to remain secured through the public distribution system. The prices of many other consumer goods are expected to decline. These include sugar; beverages; cotton textiles; wool, silk and synthetic fibre textiles; and textile products and wearing apparel. **(Paras 7.24, 7.27 and 7.28)**

25. The changeover to GST is designed to be revenue neutral at existing levels of compliance. Given the design of the ‘flawless’ GST, the producers and distributors will only be pass through for the GST. Therefore, this policy initiative should witness a higher compliance and an upsurge in revenue collections. This will also have an indirect positive impact on direct tax collections. Further, given the fact that GST will trigger an increase in the GDP, this in turn would yield higher revenues even at existing levels of compliance. Another important source of gain for the Government would be the savings on account of reduction in the price levels of a large number of goods and services consumed by the Government. However, to the extent, the Central Government will be required to incentivise the states to adopt the GST, there will be an increase in the budgetary outgo. Given the smallness of the size of the compensation, it is expected that there would be a net gain in the tax revenues. This should enable the Central Government to better manage its finances. **(Para 7.31 and 7.32)**

26. As regards the State Governments, in the first year of implementation of GST and phasing out of the Stamp duty, the States should expect additional revenues to the extent of Rs 70,000 crores (excluding the incentive amount). However, in the subsequent years this gain would diminish on account of the phasing out of stamp duty but will be more than adequately compensated as compliance starts improving. **(Para 7.33)**

27. Under the proposed GST, the expansion in the power of the States is significantly larger than the Centre. Therefore, the proposed GST will alter the balance of power in favour of the states thereby reducing the vertical imbalance. **(Para 7.36)**

28. The GST envisages a mechanism whereby both the Centre and the States will cease to have any independent power to make changes in the design and structure once agreed upon. The existing mechanism for arriving at a collective decision on the structure of the GST should be permanently institutionalised so that changes in the initial design of the GST are collectively agreed and implemented by both the Centre and the States. The Empowered Committee of State Finance Ministers may, upon the introduction of the GST, be transformed into a permanent constitutional body known as the Council of Finance

Ministers. This Council shall comprise of the Union Finance Minister and all State Finance Ministers. The Union Finance Minister would be the Chairman of this Council.

(Paras 8.11 and 8.12)

29. The Council should be responsible for any modification in the initial design of the dual GST and regulating the indirect tax system in the country. The initial design of the dual GST should be approved by the Chairman and three-fourth of the State Finance Ministers. Thereafter, any change in the structure of the GST (both base and the rates) should be allowed to be carried out only if the Chairman **and** two-thirds of the State Finance Ministers agree to do so. Consequently, neither the Centre nor any State will have the authority to unilaterally make any change in the agreed design of the GST. However, in the event of a crisis, the Member State or the Centre may take immediate steps to impose a surcharge subject to ex-post facto approval by the Council within one month. Further, such surcharge should not be allowed to remain in force beyond a period of one year. **(Para 8.13)**

30. We do not expect any revenue loss to the States on account of the switch-over to GST. However, with a view to incentivising the States and establishing a credible mechanism for deciding on compensation claims, if any, we recommend the following:-

- i) A GST Compensation Fund should be created under the administrative control of the **Council of Finance Ministers**.
- ii) The Central Government shall transfer to the GST Compensation Fund a minimum sum of Rs 6000 crores per annum over the next five years (i.e. a total amount of Rs 30,000 crores) if, and only if, the States-
 - a. introduce the 'flawless' GST as recommended by us; and
 - b. follow the road map, as suggested by us, for its introduction;
- iii) The amounts in the Fund should be used only for the following purposes:-
 - a. To compensate the states for any revenue loss on account of the adoption of the 'flawless' GST;
 - b. The balance, if any in the Fund, to be carried forward to the subsequent year;

- c. The balance, if any remaining at the end of the fifth year, to be distributed amongst the states on the basis of the same formula used for distributing resources in the divisible pool.
- iv) The amount will be transferred in quarterly instalments.
- v) The amounts shall be disbursed by the Council on the basis of the recommendations by a three member Compensation Committee comprising of the Secretary, Department of Revenue, Government of India, Secretary to the Council and any fiscal expert appointed by the Central Government for this purpose.
- vi) No contribution to the Fund shall be made by the Central Government in any year in which the States fail to adhere to the roadmap for implementation of the GST.
- vii) The methodology to be used for estimating the revenue loss and the compensation shall be decided by the Council.

(Paras 9.3 to 9.6)

31. The States should also be liable to a penalty in case they deviate from the agreed design and structure of the GST. **(Para 9.8)**

32. Since the design of the GST will also impact the indirect tax system of the Central Government, it is necessary for the Central Government to play a more proactive role in this effort. Towards this, the leadership of the Union Finance Minister would be vital. This will provide the necessary impetus to the process of 'grand bargaining' for the GST. **(Para 10.4)**

33. On account of lack of adequate preparedness, the implementation of the GST scheduled for 1st April, 2010 should be postponed by six months to 1st October, 2010. However, the Council should release a timeline of various activities for introduction of GST simultaneously with the announcement for postponement. **(Para 10.6)**

34. All taxes on goods and services including cesses and surcharges levied at the State and sub-national level should be subsumed in the SGST. However, if for some political

economy reasons it is considered expedient to introduce the GST in a phased way, we recommend the phasing in the following manner:-

- a) In the year 2010-11, all elements of the Flawless GST recommended by us whereby
 - i. the single CGST rate should be 5 percent and the corresponding SGST rate should be 7 percent; and
 - ii. Transactions in immoveable property (i.e real estate and housing services) should be brought within the fold of GST; and
 - iii. Stamp duty may not be subsumed but the rate of stamp duty in all states should be calibrated so as not to exceed 4 percent. As a result, transactions in real estate will be subject to a dual levy like in the case of SIN-goods;
- b) In the year 2011-12, same as (a) above, with the modification that the rate of stamp duty should be reduced to 2 percent; and
- c) In the year 2012-13, same as (a) above, with the modification that-
 - i. Stamp duty should be eliminated and replaced by a Registration Fee at a specific rate;
 - ii. the revenues attributable to 2 percentage point out of the 7 percentage point of SGST should be set apart for devolution to the third-tier of Government and the revenues from the balance 5 percentage points will remain with the State Government so that the third-tier of Government have a interest in the efficient functioning of the GST and do not have to impose any cascading taxes like cess, entry tax or Octroi.

(Paras 10.3 to 10.10)

CHAPTER – I

Introduction

1.1 In 2004, analysing the structure of the prevailing indirect tax system both at the Central and State level, the Task Force on Implementation of the Fiscal Responsibility and Budget Management Act, 2003 observed that “high import tariffs, excises and turnover tax on domestic goods and services have enormous cascading effects, leading to a distorted structure of production, consumption and exports. This problem can be effectively addressed by shifting the tax burden from production and trade to final consumption, and from savings to consumption. The existing tax system introduces innumerable distortions resulting in inefficient resource allocation and adversely impacting GDP growth. It also provides an incentive to firms to engage in political lobbying for exemptions and favourable modifications in the tax schedule. The Indian consumer is known to be remarkably sensitive to apparently small changes in relative prices. The goal of a rational tax system is to *empower households* to engage in undistorted decision making, driven by their own needs and preferences.”. Accordingly, the Task Force recommended that “a well designed destination-based value added tax on all goods and services is the most elegant method of eliminating distortions and taxing consumption. Under this structure, all different stages of production and distribution can be interpreted as a mere tax pass-through, and the tax essentially ‘sticks’ on final consumption within the taxing jurisdiction⁴. Therefore, the Task Force recommended the introduction of a destination based VAT type dual Goods and Services Tax (hereafter referred to as ‘GST’).

1.2 In general, the recommendation was viewed as the ultimate goal but there was certain degree of scepticism about whether India should immediately move to a ‘flawless’

⁴ Report of the Task Force on Implementation of Fiscal Responsibility and Budget Management Act, 2003, Government of India (July, 2004)

GST⁵. Experts, in particular, were of the view that the dual GST was an idea whose time had not come.

1.3 By mid-2004, the State Governments were already at an advance stage of preparation for a switch over from the cascading type sales tax to a partial VAT regime which was eventually introduced with effect from the 1st April, 2005⁶. The VAT has two basic rates of 4 percent and 12.5 percent. There is an exempted category and a special rate of 1 percent for a few selected items. The items of basic necessities and goods of local importance are put under the exempted category. Special rate of 1 percent is applicable for Gold, silver and precious stones. The 4 per cent rate applies to other essential items and industrial inputs. The 12.5 percent is residual rate of VAT applicable to commodities not covered by other schedules. There is also a category with 20 percent floor rate of tax, but the commodities listed in this schedule will not be subjected to VAT. This category covers items like motor spirit (petrol, diesel, and aviation turbine fuel), liquor, etc. While input-credit is available for intra-state transactions, no such credit is available for inter-state transactions. Therefore, the VAT, like its predecessor the Sales tax, continues to be characterised by narrow base, plethora of exemptions, multiple rate structure and cascading effect on account of break in the input-credit chain. The introduction of VAT is, at best, a toddler's tentative step towards indirect tax reform.

1.4 As a step towards the eventual introduction of the GST, the Centre also took immediate steps to integrate the CENVAT and the services tax and expand the scope of the service tax in a phased manner. Recognising the need for a giant leap to cleanse the indirect tax system of its distortionary impact on the economy, the Finance Minister, while presenting the Union Budget 2006-07, set April 1, 2010 as the date for introducing GST and requested the Empowered Committee of State Finance Ministers to work with the Central Government to prepare a road map for introduction of GST in India.

⁵ "Flawless" GST means a GST which has all the elements described in para 3 of the Executive Summary.

⁶ Haryana was the first State to introduce the partial VAT regime in 2003.

1.5 The Thirteenth Finance Commission has been mandated to make recommendations after considering the impact of the proposed implementation of the GST with effect from the 1st April, 2010 including its impact on foreign trade. For this purpose, it is necessary to know the structure of the Goods and Services Tax which will be in place. The authority to design the structure of the GST Model jointly vests in the Empowered Committee of States' Finance Ministers and the Central Government. The Empowered Committee brought out its preliminary views on the design of the GST in a paper⁷ of April, 2008 and the Union Government gave its response to these proposals. After further consultations, the Empowered Committee presented the first discussion paper in November, 2009. The contours outlined in this paper do not adequately advance the cause of indirect of tax reforms due to a number of infirmities. This initiative seems to be an amalgam of compromises and continued fear of possible revenue losses and adverse impact on the low income groups. Clearly, there are a number of important unresolved issues relating to the design of the GST and resolving these will need further discussions between Central and State Governments. Hopefully, by providing comprehensive discussion of the issues, this Report of the Task Force will make useful contribution towards the Union and the State Governments reaching such a 'grand bargain' so that we have a world class GST regime in India.

⁷ "A Model and Road Map for Goods and Services Tax in India-Views of the Empowered Committee of State Finance Ministers", New Delhi, April 30, 2008.

CHAPTER-II

Goods and Services Tax: The Model

2.1 In the absence of a firm Model of the GST, it is necessary for us to construct a comprehensive Model in the light of the roadmap prepared by EC, the views expressed by the Central Government, the ongoing discussion on unresolved issues and best international practice. Therefore, the Group seeks to design the Model in such manner as would foster the achievement of the following objectives:

- (a) The incidence of tax falls only on domestic consumption;
- (b) The efficiency and equity of the system is optimized;
- (c) There should be no export of taxes across taxing jurisdictions;
- (d) The Indian market should be integrated into a single common market;
- (e) It enhances the cause of cooperative federalism.

2.2 With a view to attaining the objectives set out above, we recommend a VAT type Goods and Services Tax (GST). In the context of the design of the GST, some of the important issues are discussed in the following paragraphs.

a. Single GST versus Dual GST

2.3 In a federal country like India where the power to tax domestic trade is divided between the Central Government and the State Government, the designing of a destination based GST becomes extremely complicated. A conventional national GST⁸ cannot be implemented without the States losing their fiscal autonomy. However, this is not feasible since revenues from State VAT account for substantial proportion of State's revenues. Therefore, the solution has to be found within the existing federal framework where both levels of Governments have the concurrent powers to tax domestic trade in goods and services.

⁸ This refers to a single National level GST to be levied and collected by the Central Government.

2.4 In view of the above, we recommend the following:-

- (a) The GST will be a dual levy imposed concurrently by the Centre and the States, but independently. It will have two components: one levied by the Centre (hereinafter referred to as CGST), and the other levied by the States and Union Territories (UTs) [hereinafter referred to as SGST].
- (b) Both the CGST and SGST will operate over a common base. That is, the base will be identical.

b. Type of GST – Consumption, income or production

2.5 There are three possible variants of VAT, depending upon what macro-aggregate the government wants to tax: gross income, net income or consumption. A **gross product type VAT** treats both consumption and capital formation as final uses of the good; hence capital goods purchased by the dealer would not be treated as inputs. Input tax credit will not be available on taxes paid on capital goods. A **income type VAT** would give credit for tax paid on current inputs and tax paid on capital goods to the extent attributable to depreciation of capital goods, in any given year. Credit for tax on capital goods will therefore be spread over the life of the capital good. A **consumption type VAT** goes a step further in that only final consumption is treated as the final use of a good; full credit, therefore, is given for taxes paid on capital goods as well, in the year of purchase.

2.6 The consumption base has been a much favoured tax base from both the perspective of economic neutrality and ease of administration. It is also the only VAT that is equivalent to a retail sales tax, in that it restricts the burden of the tax to final consumption goods. In effect, the tax is only on the pure value added within the production stage in question. Consumption VATs are also the easiest to compute—all taxes previously paid on purchases from other firms to be simply subtracted from taxes due on sale. No distinction needs to be drawn between capital goods and other inputs, and no depreciation need be computed. Consumption, it is argued, is also a broad measure of the ability to pay taxes, much like income. Furthermore, it excludes savings from the base, hence does not discourage investment.

2.7 From an economic growth perspective, both the income and gross product VAT have an anti-investment bias. This is all the more significant in countries that impose substantial income taxes. An income tax taxes saved income and hence investment twice—one as the income is being earned and again as the rewards for saving appear as interest and profit, which are again taxed. Since income tax is fairly well established in India, we recommend that-

- (a) The Centre and the States should adopt a consumption type GST, i.e. there should be no distinction between raw materials and capital goods in allowing GST credit. Only this GST variant is equivalent to a retail sales tax.
- (b) The tax base of both CGST and SGST should comprehensively extend over **all goods and services** going up to the final consumer (retail level), reflecting the tax base of a typical consumption VAT.
- (c) Since the tax base will extend to all goods and services, no distinction will be maintained between goods and services. A registered dealer will be required to collect taxes on every invoice irrespective of whether the supply is for goods or services. Therefore, no classification of goods and services should be provided for in law. This will eliminate all classification disputes.

2.8 In the course of discussion with officials in the Department of Revenue a view was expressed that in the context of service tax, it should be levied on all services but there should be a positive list of such services. This view was based on the consideration that the assessing officer feels comfortable in levy and collection of tax if he knows exactly on which service the levy is being imposed.

2.9 In this context, we would like to point out that **firstly**, it is not possible to draw up a positive list which is all comprehensive. Invariably there would be gaps in the base. **Secondly**, it would lead to classification disputes thereby imposing higher compliance and administrative burden. **Thirdly**, with the introduction of the GST no distinction is required to be made between goods and services. Therefore, the issue relating to separate taxation of

services does not arise. **Fourthly**, under the GST regime, it is not necessary for the assessing officer to know what he should be taxing. The design should be so structured that he would need to know that all supply transactions will attract GST except those prescribed. Since the negative list is intended to be a very small list, it would not be difficult for him to administer. In the case of a positive list, the assessing officer must familiarize himself with a much longer list and any gap in his knowledge base could lead to erroneous judgement. Therefore, we are not inclined to agree with the view of the Department of Revenue officials that the taxation of services should be based on a positive list. Accordingly, we recommend that all goods and services should be subject to tax other than those specified in the negative list.

2.10 In view of the fact that the CGST and SGST are intended to be levied on consumption of all goods and services, these two taxes must subsume all taxes presently levied on various goods and services by the Centre and the States, respectively. For the purposes of identifying the taxes which needs to be subsumed in the CGST and SGST, we recommend that the following principles⁹ should be adopted:-

- (a) 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.
- (b) 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.
- (c) The sub-summation should result in free flow of tax credit at the intra and inter State levels.
- (d) Any tax/fee/charge which is in the nature of a user charge for supply of goods & services should not be subsumed under the GST.

⁹ In general, these principles are consistent with the principles laid down by the EC in their Discussion Paper dated 30th April, 2008.

2.11 Based on the aforesaid principles, we recommend the following:-

- a. The following central taxes should be subsumed in the CGST¹⁰:
 1. Central Excise Duty (including Additional Excise Duties);
 2. Service Tax;
 3. Additional Customs Duty (commonly referred to as 'CVD');
 4. Surcharges and all cesses
- b. The following State level taxes, as also recommended by the Empowered Committee (EC) in its discussion paper dated 30th April, 2008, should be subsumed in the SGST:-
 - i. VAT/Sales Tax (including Central Sales Tax and Purchase tax¹¹);
 - ii. Entertainment tax (other than levied by local bodies);
 - iii. Entry taxes not in lieu of Octroi;
 - iv. Other Taxes and Duties (includes Luxury Tax, Taxes on lottery, betting and gambling, and all cesses and surcharges by States)¹²;
- c. Since all taxes on goods and services, levied by the Centre or the States, should be subsumed in the GST, the following other taxes levied by the States on goods and services should also be subsumed:
 - i. Stamp duty;
 - ii. Taxes on Vehicles;
 - iii. Taxes on Goods and Passengers; and
 - iv. Taxes and duties on electricity.

¹⁰ This is consistent with the proposal of the EC in their Discussion paper dated 30th April, 2008.

¹¹ The Discussion Paper dated 30th April, 2008 released by the Empowered Committee indicates that Purchase Tax will be subsumed by the SGST. However, the Discussion Paper released on 10th November, 2009 indicates that Purchase Tax will not be subsumed by the SGST. This does not advance the cause of a 'flawless' GST and is a retrograde step in the reform of indirect taxes. We recommend that the purchase tax should be subsumed in the SGST.

¹² This does not include (i) Stamp Duty, (ii) Taxes on Vehicles, (iii) Taxes on Goods and Passengers, and (iv) Taxes and Duties on electricity.

- d. Any amount collected through these taxes on the SIN goods should not be subsumed either in the CGST or the SGST. Similarly any amount which is collected as tax/fee/charge/cess which is essentially in the nature of a user charge for supply of goods and services (including environmental goods and services) also should not be subsumed under the CGST or SGST. Further, both Centre and the States should take steps to consolidate all taxes (other than proposed GST) on the SIN goods as a single levy termed as Central Excises and State Excises, respectively.
- e. All entry and Octroi duties levied by the third-tier of Government must be abolished.¹³

2.12 For the purposes of this Report, the set of taxes which the EC has recommended for being subsumed in the SGST will be referred to as **“EC-taxes”**. Similarly, the larger set of taxes which we have recommended for being subsumed in the SGST will be referred to as **“TF-taxes”**.

c. Origin versus Destination Principle

2.13 A GST can be implemented under either the origin or the destination principle. Under the former, the GST is imposed on the value added of all taxable products that are produced domestically; under the latter, the GST is imposed on the value added of all taxable products that are consumed domestically. Obviously, the two principles are identical in a closed economy. In an open economy, the difference between them lies solely in their treatment of imports and exports: exports are taxed but imports are not under the origin principle, while just the converse holds under the destination principle. It is important to note that the distinction between the two principles is based on the location of production and consumption. In view of our recommendation for a consumption type GST and the need for increased international competitiveness, we recommend that -

¹³ This has already been done by all States other than Maharashtra.

- a. the GST should be structured on the destination principle. As a result, the tax base will shift from production to consumption whereby imports will be liable to tax and exports will be relieved of the burden of goods and service tax. Consequently, revenues will accrue to the State in which the consumption takes place or is deemed to take place;
- b. international exports should be zero rated;
- c. international imports should be subject to both CGST and SGST at the time of importation irrespective of whether or not the imported goods are produced domestically;
- d. SGST on B2B imports should be collected by the same agency which collects the CGST and should be remitted to the state in which the place of destination of the imports is located regardless of where the goods enter the country. However, the place of destination may be defined to mean the address of the importer on the import invoice; and
- e. SGST on B2C imports should be collected by the same agency which collects the CGST and should be remitted to the state in which the place of residence of the person importing the goods is located regardless of where the goods enter the country.

d. Method of Computation

2.14 There are essentially three methods of computing VAT liability: addition method, subtraction method and the credit method (also known as the invoice method). The principal debate concerning choice of methods in computing VAT liability is normally restricted to the credit and subtraction methods. The credit method requires that the amount of VAT charged be explicitly stated on the invoice associated with any taxable transaction. The amount of tax a dealer submits to tax authorities is simply the difference between the tax he collected on his sales and the tax he paid on his purchases. Under the subtraction method, each dealer's tax liability is computed by applying the applicable VAT rate to the difference between his total sales (inclusive of the VAT element in his sales price)

and his total purchases (inclusive of the VAT element in his purchase price). Hence, unlike the credit method, the amount of VAT connected with a taxable transaction is not required to be explicitly stated on the associated invoice.

2.15 The credit method therefore, is more transparent, whereby the effective tax rate on any commodity is easily identifiable as the rate applicable to the last transaction in that commodity. In the case of the subtraction method, the rate of VAT is not separately indicated and to this extent there is a loss of transparency. Further, since the effective rate under the subtraction method is a weighted average of the rates at the various stages, there could exist an incentive to shift value added to the stages with the lower tax rate. This kind of tax distortion needs to be avoided.

2.16 In view of the above, we recommend that-

- i. the credit method should be adopted for computation of the VAT liability.
- ii. The computation of the CGST and SGST liability will be based on the invoice credit method i.e., allow credit for tax paid on all intermediate goods or services on the basis of invoices issued by the supplier. As a result, all different stages of production and distribution can be interpreted as a mere tax pass-through, and the tax will effectively 'stick' on final consumption within the taxing jurisdiction. This will facilitate elimination of the cascading effect at various stages of production and distribution.
- iii. The CGST and SGST are to be credited to the accounts of the Centre and the States separately.
- iv. Since the CGST and SGST are to be treated separately, taxes paid against the CGST should 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.

- v. Cross utilization of ITC between the CGST and the SGST should not be allowed.

e. Treatment of capital goods

2.17 In the past, a number of countries, introduced accelerated depreciation or investment allowance to compensate for domestic trade taxes paid on capital goods. With the gradual introduction of VAT and the feasibility of extending credit for VAT on fixed assets,¹⁴ depreciation rates were rationalised. Later in some countries, VAT was used to slow down the development of capital intensive production processes. To this end, they disallowed the credit for the VAT on fixed assets (defined as all assets which are subject to depreciation) and non-material assets, like technical know-how. The case for allowing full and immediate credit for the VAT on capital goods rests on several arguments:

1. Depending on the capital intensity of the production process, the VAT on fixed assets enters into the price, causing uneven effects on consumer prices.
2. Any kind of restriction on full and immediate credit for VAT on fixed assets deters investment and hampers technological change, unless it can be fully shifted forward to consumers¹⁵.
3. Limiting the credit for VAT on fixed assets in any manner results in increased cost of exports thereby undermining international competitiveness. Hence, it serves as a disincentive to exports.
4. Capital goods need to be defined thereby creating scope for considerable disputes.
5. Denial of immediate credit for VAT on capital goods leads to implicit taxation. This is further aggravated if excess credits are not refunded but must be

¹⁴ Other reasons for rationalizing the depreciation rates were significant control over rate of inflation in the price of capital goods and reduction in corporate tax rates.

¹⁵ However, forward shifting is unlikely if competing imports can be sold without the element of tax on capital goods.

applied against VAT on future sales. Further, in the face of inflation, the real value of the tax credits carried forward declines rapidly becoming equivalent in effect to a tax on fixed assets. Any denial of full and immediate credit for the VAT on capital goods violates the neutrality of VAT.

2.18 Therefore, in recent years, most countries have introduced a full and immediate credit for the VAT on capital goods applied for the purpose of registered businesses. Under the Central Excise Act, credit for CENVAT paid on capital goods or CVD on imported capital goods is spread over two years resulting in the kind of distortions discussed above. The rationale for this spread over is essentially loss in revenues. The estimated total credit for CENVAT paid on capital goods and CVD on imported capital goods in 2002-03 was Rs. 8,500 crore and could be expected to increase to about Rs. 9,000 crore in 2004-05. Since the credit is allowed over a period of two years, the loss in revenues is, therefore, estimated to be Rs.4,500 crore and restricted to the transitional year only. However, in the context of revenue gain from reduction in depreciation rates proposed in the section on corporate tax, the impact on revenue could be fully absorbed. In the light of the arguments in support of full and immediate credit for VAT on capital goods and the revenue implications thereof, we recommend that-

- i. Full and immediate input credit should be allowed for tax paid (both CGST and SGST) on all purchases of capital goods (including GST on capital goods) in the year in which the capital goods are acquired; and
- ii. any kind of transfer of the capital goods at a later stage should also attract GST liability like all other goods and services.

f. Exemption from GST

2.19 Suppliers of goods and services are either taxable or tax exempt. By definition, exemption relieves the exempt trader's value added from the tax, but all his purchases including capital goods are taxed. Exemption will therefore increase the amount of tax finally paid on intermediate goods—the opposite effect that the exemption was supposed

to provide. In the case of final goods, exemption eliminates the tax on value added in the final stage only. In other words, if a commodity is exempt only at the retail level, then only the retail level is freed of VAT. Although the retailer would not charge VAT on its sale, the retailer would not be entitled to a credit for tax paid on the purchase of an exempt item. If a commodity or service is zero rated, the zero rated trader's value added is not taxed and the trader receives a credit for the tax paid on the purchase of materials and other inputs used. Zero rating, in theory, is the only way to ensure that a product is truly free of VAT, since any tax paid would be credited on the last sale. The considerations influencing the choice between zero rating and exemption are:

- (1) The desirability of freeing users of specific goods or services completely from VAT (as with zero rating), or only partially (as with exemption);
- (2) The merits of excluding certain firms from the registration and filing of returns. Even from the perspective of firms themselves, there are conflicting considerations. If a firm's goods are completely exempt, it is not required to register or file a return, but the prices of the goods sold by the exempt firm will include the tax incurred by the exempt firm on its purchases.

2.20 This may be particularly objectionable to the exempt firm's customers who cannot receive credit for the embedded tax. In this case, exemption would place the exempt firm at a competitive disadvantage.

2.21 If the objective is to have a broader tax base, however, exempting certain goods may become preferable to zero rating them. In addition, the administrative burden of the zero rating procedure can be onerous. Zero-rating implies build up or payout of refunds, which may entail huge administrative costs, requiring verification and disbursement of refund cheques. Furthermore, there is the issue of controlling evasion or fraud. Zero rating creates an incentive for sellers to exaggerate the values of their final sales and to correspondingly inflate the value of taxable inputs purchases, in order to avail themselves of the refund of a

larger input tax element. The resources needed to cross-check such claims can impose additional and perhaps unsustainable demands on prevailing systems.

2.22 Further, tax exemptions are economically inefficient, inequitable, lead to revenue loss, breed rent-seeking behaviour, increase compliance cost and enhance administrative burden. The case for tax incentives is further weakened in the existing tax regime of moderate tax rates.

2.23 In general, a case is often made for exempting **food** on the consideration that the levy of GST would have a significant impact on those living at or below the subsistence levels. Food constitutes a large variety of items and attempt at any definition will lead to complexity in legislation. If the exemption is extended to all categories of food items, the revenue base will shrink significantly and the standard rate would need to be substantially higher. This would trigger demands for other goods which form the consumption basket of the poor. To the extent the poor consume other goods also, any increase in the standard rate will also adversely affect them. Contrary to popular perception, food items are indeed subject to tax at the state level though at lower rates. As stated in earlier paragraphs, the distribution channel for unprocessed food in the rural sector is either a direct sale by the farmer to the final consumer in village hats or through small retail stores who would even otherwise remain exempt because of the threshold exemption for dealer registration. A lower rate for food in contrast to the relatively high standard rate would mean a two rate structure and gradual expansion of the lower rate category as is the international experience. As a compromise, we recommend that any food item which is covered under the public distribution system should be exempt regardless of the outlet through which it is sold. This principle may be applied to other non-food items also.

2.24 In the case of **health services**, there are two approaches. The first approach is the full taxation model whereby the health services form part of the comprehensive GST base. As a result, there is effectively zero tax liability in the case of publicly funded subsidised

health care facilities since input tax credit will be more than the output tax. As regards, health care availed in other health care facilities covered by insurance, there would be no additional burden on the consumer since the expenditure would be borne by the insurance company and can be claimed as input credit. Essentially, there would be zero incidence of GST on health care. Consequently, there would be opportunities for reduction in the price of health care. The second approach is the exemption approach which does not allow for full rebating of input taxes and therefore, effectively there is a significant element of GST embedded in the price of the final health care. Therefore, while public may prefer exemption, in reality it imposes a higher tax burden particularly on the publicly funded health care and for care provided in facilities covered by insurance. Since health services do not form part of our sample used for calculation of our RNR in the later part of this Report, the choice of the method of treatment of health services will not impact the estimation of the GST base and hence the RNR rate. Accordingly, we recommend that the choice may be made keeping in view the considerations discussed above.

2.25 The considerations discussed in the context of health services similarly apply to education services except that these services are not covered by insurance. In fact, the problem is more complex since the sector is more diverse covering child care facilities, formal education (both school and college levels), professional education, occupational programs, diploma programs and recreational programs. Therefore, defining educational services is more complex. However, given the multitude of schools and colleges in the country and the disproportionately large administrative burden, we recommend that the educational services may be exempted from the levy of GST and such exemption should be limited to formal education services provided by schools and colleges.

2.26 Keeping in view the above-mentioned economic and administrative implications of exemptions and zero rating, we summarize our recommendations on exemption from GST as under:-

- a. Ordinarily, there should not be any exemption from CGST or SGST. If for some reason, it is considered necessary to provide exemption, the Centre and the States should draw up a common exemption;
- b. The common list of exemption should be restricted to the following:-
 - i. All public services of Government (Central, State and municipal/panchayati raj) including Civil administration, health services and formal education services provided by Government schools and colleges, Defence, Para-military, Police, Intelligence and Government Departments. However, public services will not include Railways, Post and Telegraph, other commercial Departments, Public Sector enterprises, banks and Insurance, health and education services;
 - ii. Any service transactions between an employer and employee either as a service provider, recipient or vice versa;
 - iii. any **unprocessed food article** which is covered under the public distribution system should be exempt regardless of the outlet through which it is sold; and
 - iv. **education services** provided by non-Governmental schools and colleges; and
 - v. **health services** provided by non-Governmental agencies.

g. Treatment of petroleum products

2.27 One of the classes of products whose consumption needs to be checked to restrict negative externalities is petroleum products. The entire range of petroleum products is subject to multiple taxation at both the Central and State level. As a result, the incidence of tax on products essentially used as intermediate inputs cannot be estimated and leads to a cascading effect on downstream products. Consequently, it is necessary to rationalise the tax treatment of petroleum products.

2.28 The petroleum products can essentially be classified into two categories: (i) industrial inputs or fuels such as crude oil; (ii) transportation fuels comprising of HSD, MS and ATF; and (iii) household fuels comprising of kerosene and Liquefied Petroleum Gas (LPG). While industrial fuels are intermediate inputs, transportation fuels and kerosene (collectively referred to as “emission fuels”) are used both as intermediate inputs and in final consumption. The emission fuels generate negative externalities, whose consumption needs to be checked. Therefore, generally, such emission fuels are subject to an excise against which no input tax credit is allowed in respect of inputs (including capital goods) used in the manufacture of such fuels. However, in large number of cases, such emission fuels are also used as intermediates. As a result, the cascading effect of embedded input taxes is significant.

2.29 In view of the above, the Task Force recommends a dual levy of GST and excise on the entire range of emission fuels. As a general rule, no input credit will be allowed to any person in respect of GST on the emission fuels since emission fuels are predominantly used in final consumption and has the potential for creating a flourishing market in trading of invoice and input tax credit. However, this general rule should be relaxed in the case of consumption of transportation fuels by the Ministry of Railways, the State Road Transport Corporations, the Airlines, truckers, taxi operators and a dealer¹⁶ trading in these goods on the consideration that the consumption is essentially intermediate in nature and the unlikelihood of these entities indulging in purchase of bogus invoices. However, in the case of truckers and taxi operators, the benefit of input tax credit has the potential of misuse and therefore credit may be allowed through the abatement mechanism only. Further, no input tax credit in respect of excise would be allowed to any other person. (

2.30 We also recommend that the industrial fuels should be subjected only to GST (both Central and State) with the benefit of input credit like any other intermediate good.

¹⁶ For example, a dealer operating a petrol station will be allowed input credit in respect of GST on petrol purchased by him from an oil marketing company.

2.31 Both the Central and the State Governments may determine the appropriate revenue neutral rate of excise in the case of emission fuels.

h. Treatment of tobacco goods and alcohol

2.32 Like emission fuels, all tobacco goods and alcohol are also **SIN-goods**¹⁷. Therefore, on the same analogy, we recommend a dual levy of GST and excise on the entire range of these goods. As a general rule, no input credit will be allowed to any person in respect of GST on these goods since they are predominantly used in final consumption. However, this general rule should be relaxed in the case of a dealer trading in these goods on the consideration that the consumption is essentially intermediate in nature. Further, no input tax credit in respect of excise would be allowed to any person. Both the Central and the State Governments may determine the appropriate revenue neutral rate of excise in the case of these products. However, we would like to point out that excessively high rates of tax on tobacco and alcohol may encourage evasion and become a source for financing of undesirable activities.

i. Treatment of natural gas

2.33 Natural gas, like petroleum products, is derived from the same source. However, unlike petroleum products, natural gas does not generate negative externalities. Therefore, the tax regime for natural gas should be distinctively different from the regime applicable to petroleum products. Accordingly, natural gas should be subjected only to GST (both Central and State) with all the benefits of input credit as in the case of other normal goods. We recommend accordingly.

¹⁷ **SIN-goods** are goods whose consumption create negative externalities and for the purposes of this Report, collectively or severally, refers to emission fuels, tobacco goods and alcohol.

j. Treatment of the power sector

2.34 Power is one of the most important inputs in the process of production of goods and services. Hence, it is necessary to rationalise the tax treatment of the power sector so as to ensure that there is seamless flow of input tax credit across all the processes/activities in the power sector. At present, the power sector is subject to multiple taxation. At the Central Government level, power equipments are either exempt from CENVAT or subject to concessional rates. As a result, either no or partial input tax credit is available and the input taxes remain embedded in the cost of the power equipments. This problem is further compounded by the absence of a levy on power generation, distribution or consumption thereby denying input tax credit even for equipments and stores which are subject to CENVAT. Similarly, at the State level, there is no benefit of input tax credit in respect of the State VAT on inputs used in the process of power generation and distribution. The cumulative impact of the taxation regime at both the Central and State level is significant cascading effect¹⁸ of taxes when power is used as an intermediate input. This phenomenon partly explains the cause for high cost of power generation and distribution. As a result, the international competitiveness of Indian industry is significantly undermined.

2.35 In view of the above, we recommend the following:

- (i) The electricity duty levied by the States should be subsumed in the SGST.
- (ii) The power sector must form an integral part of the comprehensive GST base recommended by us over which both the Central and State Governments would have concurrent jurisdiction.
- (iii) The tax regime for the power sector should be the same as in the case of any other normal good.

¹⁸ The Task Force has not made any independent assessment of the impact of the embedded taxes in power generation and distribution. However, discussions with experts in the field suggest that the embedded taxes could account for as high as 30 per cent of the cost of power production and distribution.

- (iv) Article 278 and Article 288 of the Constitution should be amended to enable levy of GST on supply of electricity to Government at all levels like any other normal goods.

2.36 The inclusion of the power sector in the GST model would significantly reduce the cost of power projects and consequently the cost of generation and distribution of electricity. As a result, it will improve profitability of power projects thereby attracting new investments into the sector. To the extent the cost of power will witness reduction, downstream industries will also benefit from cost savings and thus become internationally more competitive.

k. Treatment of transport services

2.37 Transport services, like most other services, is used both as intermediate input and in final consumption. Further, the transport equipments are also subject to multiple taxation at both Central and State level. The present regime leads to cascading effect of embedded taxes on the downstream industry which do not get rebated thereby leading to enhanced cost for such industries. Hence, it is imperative to rationalise the taxation regime for transport services.

2.38 Accordingly, we recommend the following:

- (i) The tax on vehicles and the tax on goods and passengers levied by the State Governments should be subsumed in the GST.
- (ii) All transport equipments and all forms of services for transportation of goods and services by railways, air, road and sea must form an integral part of the comprehensive GST base recommended by us over which both the Central and State Governments would have concurrent jurisdiction.
- (iii) The tax regime for the transport equipments and transport services should be the same as in the case of any other normal good.

- (iv) It is not necessary to levy higher rates of taxes on vehicles as is the existing practice since it is proposed to subject the use of these vehicles to tax at higher rates through excise on emission fuels. Accordingly, the present practice of levying higher rates of taxes on vehicles should be done away.

I. Treatment of financial services

2.39 The financial sector constitutes a significant component of the gross domestic product and also private final consumption. Further, in developing countries, taxation of consumption of financial services is viewed as progressive because such services as banking, brokerage, property and casualty insurance and foreign exchange transactions are connected closely with those having higher income and wealth. The progressive revenue objective thus dictates as wide an application of VAT to financial services as possible. It also encourage countries to consider compensatory taxes where an exemption must be provided and even additional ad hoc taxes for revenue purposes. Therefore, given the progressive nature of taxation of financial services and the distortionary impact of compensatory and ad hoc taxes, we recommend that the consumption of financial services should be comprehensively taxed under the GST framework.

2.40 We recognise that there are predominantly three alternative methods for levying GST on financial services: the exemption method, the zero rating method and the full taxation method. While the exemption method and the zero rating method reduces the potential GST base and also distorts consumption across financial services and other business services, the full taxation method significantly enhances the tax base and also results in equal treatment of all services. Therefore, we recommend that the consumption of financial services should be taxed on the basis of the full taxation method.

2.41 There are alternative approaches to full taxation of financial services. These are the addition method, the subtraction method and the cash flow method. We recommend that the choice of the method may be based on administrative and compliance consideration.

m. Treatment of immovable properties

2.42 The **case for** including the real estate sector in the tax base for the GST rests on a number of competing reasons. **Firstly**, the construction and exploitation of real estate comprises one of the larger sources of gross domestic product. Therefore, any exclusion of the real estate sector would lead to significant reduction in the tax base. This would lead to an increase in the GST rate for other sectors thereby distorting economic efficiency and incentive for compliance.

2.43 **Secondly**, expenditure on housing also constitutes a significantly large proportion of total personal consumption expenditure. Therefore, the exemption of the housing sector from the GST base would distort the consumption pattern. Further, it would also undermine vertical equity in as much as consumption of housing services is relatively high in the case of the rich.

2.44 **Thirdly**, real estate is subject to multiple taxation at both levels of Government. At the Central Government level, there has been an attempt to introduce service tax on housing services and allow credit for inputs used for the supply of such services. However, at the State level input tax credit is not available for all taxes, thereby leading to significant cascading effect. Further, there is no incentive to the purchaser to obtain an invoice. Consequently, the audit trail of such transactions is lost and producers of inputs are also encouraged to suppress such transactions. The cumulative effect is to incentivise transactions in black money.

2.45 At the State level, the taxes on the real estate sector include 'sales tax' on works contract, state level VAT on various inputs used in the construction of real estate, stamp duty and registration fee. Registration and stamp duties exhibit the same distortionary cumulative and cascading effects as excises. The problem is further compounded by the fact that in most states, the statutory rates of stamp duty on immovable property transaction

are high. Therefore, the effective rate on value addition is exorbitant, thereby encouraging under-reporting of transactional value and evasion of stamp duty. Since stamp duties are directly or indirectly related to other taxes, any stamp duty evasion triggers a similar adverse response to compliance with other taxes. As with other transaction taxes, it generates a bias in favour of not selling, and inhibits the development of a liquid secondary market. In the context of a distortionary tax regime governing the real estate industry in India, there is a strong tendency for this industry to remain outside the organised sector and consequently the regulatory framework. Therefore, it serves as a breeding ground for tax evasion and criminal activities.

2.46 **Fourthly**, rationalisation of the tax regime governing the real estate industry could yield numerous benefits: improve tax compliance in the property tax which is critical for the revenue base of local government, a reduced role for black money, and a reduced role for the criminal element in the real estate sector and significantly lowering of costs by mass housing.

2.47 Keeping in view the implications of the different methods for taxing real estate and housing services discussed in Annexe-I, we recommend the following strategy for integrating the real estate sector into the GST framework:

- i. The stamp duty on immovable properties levied by the States should be subsumed in the GST to facilitate input credit and eliminate cascading effect.
- ii. The new GST regime for immovable property transactions and real estate services should be designed on the lines of the comprehensive taxation method. Therefore, the new regime would comprise of the following elements: -
 - (a) The GST should apply for all newly constructed property (both residential and commercial). If it is self-used by the person who

constructed it, the GST should be applied on the cost of construction. If it is sold or transferred, the GST should be applied on the consideration received at first transfer or sale. In both cases, credit should be allowed in respect of input tax paid on raw materials used in construction.

- (b) Rental charges received (excluding imputed rental values) in respect of leasing of immovable property used for both residential and commercial purposes should be charged to GST. Input tax credit would be allowed only in respect of input tax paid on goods and services used for maintenance. No input tax credit should be allowed in respect of tax paid on construction or acquisition of the property or tax paid on improvements thereto.
- (c) All secondary market transactions in immovable properties (whether constructed before or after the introduction of GST) should be liable to GST. However, if the property has been constructed after the introduction of GST, the GST should be levied on the resale value and input tax credit should be allowed in respect of the GST paid upon construction or purchase of the property after making adjustment for inflation. If the property has been acquired by the seller before the introduction of GST, the GST should be levied on the difference between the sale price and the cost of acquisition and improvements thereto. In such cases, no input tax credit would be allowed.
- (d) The adjustment for inflation may be made on the basis of the same inflation index as provided for the purposes of determination of capital gains under the Income-tax Act, 1961.

- (e) The new regime will also be subject to the threshold exemption of Rs.10,00,000/- for small businesses thereby eliminating the problem of excessively large number of landlords seeking GST registration.
 - (f) Immovable property will also include land¹⁹ and, therefore, the new regime will also be applicable to land transactions. However, where land is used for construction of a property, it will be treated as an input. In such cases, the GST paid in respect of land will be allowed as input tax credit in the same manner as other inputs used in construction.
- iii. The State Governments would continue to perform essential asset registry functions, and enforces property rights associated with them. These functions are comparable to those of a depository on the markets. The registration fees can be interpreted as user charges for these records keeping functions – which justify small charges. The imposition of large scale indirect taxes through registration and stamp duties constitutes a case of erroneous tax policy. Therefore, States may continue to levy a registration fee at a specific rate not exceeding Rs 1000 per transaction in immovable property, which is merely a user charge for the IT systems used in property registration.

2.48 The proposed new regime will lead to more efficient allocation of resources in as much as it will be comprehensive in its scope for taxation of immovable property transactions and real estate services. It will be neutral between old and new properties, and

¹⁹ The increase in the value of land is attributable to the direct or indirect improvements in the form of development of townships, landscaping, and construction of infrastructure that make it usable for agricultural, industrial, or residential purposes. Raw land is similar to the minerals underneath, which are of little or no value unless they can be extracted for commercial/industrial use or consumption. VAT is applied to the full selling price of minerals. In the same manner, VAT should apply to the full value of land.

between rented and self occupied properties. It will be administratively less burdensome since no distinction would be required to be made between residential and commercial properties. Similarly, the treatment of input tax credit will be relatively simple with the tax paid on construction/acquisition of the property being allowed as a set off, after inflation indexing, against the GST on resale of the property and any tax paid on minor repairs and maintenance being allowed as set off against the rental charges, if any, in the same year. Further, under the model, the real estate developer will also be entitled to set off input tax on all inputs (including land) used for the purposes of construction and development of the real estate. As a result, the distortionary cascading effect of the existing tax regime for immovable property transaction and real estate services will be fully eliminated. This would have significant downward effect on pricing of real estate. The new regime has the potential for creating an efficient secondary market in immovable property and real estate services which will facilitate better price discovery. The role of the underworld elements associated with this sector will be eliminated. Since the new regime will impart greater transparency through market mechanism, it will also strike a major blow to the underground economy. Therefore, it is imperative that the reform of the present system of taxation of immovable property transaction and real estate services forms an integral part of the proposed GST design.

n. Place of supply rules

2.49 The value added tax system is based on tax collection in a staged process, with successive taxpayers entitled to deduct input tax on purchases and account for output tax on sales. Each business in the supply chain takes part in the process of controlling and collecting the tax, remitting the proportion of tax corresponding to the margin realised on transactions, or the difference between the VAT paid out to suppliers and the VAT charged to customers.

2.50 In practice, most countries with value added taxes impose the tax at all stages and normally allow immediate deduction of taxes on purchases by all but the final consumer. These features give value added taxes their main economic advantage, that of neutrality.

The full right to deduction of input tax through the supply chain, with the exception of the final consumer, ensures the neutrality of the tax, whatever the nature of the product, the structure of the distribution chain and the technical means used for its delivery (stores, physical delivery, Internet).

2.51 Internationally, VAT is designed on the destination principle which allows the tax to keep its neutrality in cross-border trade. According to this principle, exports are exempt with refund of input taxes (“zero-rated”) and imports are taxed on the same basis and with the same rates as local production. This VAT on imports is generally collected at the same time as customs duties, although in some countries collection is postponed until declared on the importer’s next VAT return. Deduction of the VAT incurred at importation, in the same way as input tax deduction on domestic supply, ensures neutrality and no distortion of international trade. This implies that the total tax paid in relation to a commodity is determined by the rules applicable in the jurisdiction of its consumption and therefore all revenue accrues to the jurisdiction where the sale to the final customer occurs.

2.52 In the international trade in tangible goods, the place of taxation (or the place of supply) is the place of delivery, or shipment, of the goods to the recipient (buyer). In other words, a sale of goods is taxable in a jurisdiction if the goods are made available in, or delivered/shipped, that jurisdiction.

2.53 However, the nature of service and intangible products does not allow for the application of the same rules. In principle, the provider should account for the tax in the jurisdiction where the service or the intangible property is consumed or used, irrespective of the contract, payment, beneficial interest or the location of the supplier and customer at the time of the supply. Whether intangible property is used or a service is actually performed in a jurisdiction is essentially a matter of fact. However, it is not always easy to determine where services and intangibles are likely to be consumed. The increasing global nature of businesses and communication technologies makes it more difficult to apply a pure consumption test. The solution developed in most countries consists of identifying the place of consumption by reference to proxies rather than directly trying to identify the

actual or intended place of consumption. The nature of those proxies and the way they are used vary widely across jurisdictions since they result from local history and legal frameworks.

2.54 While the rules and approaches vary across countries, the basic criteria for determining the place of taxation (or place of supply) in the case of services is as follows:-

- a) In the case of a sale of real property, the place of supply is the jurisdiction in which the property is located. Similarly, services directly connected with real property (i.e services provided by real estate agents or architects) are also taxed in the place in which the property is located.
- b) In the case of mobile services (that is, passenger travel services, freight transportation services, telecommunication services, motor vehicles lease/rentals and E-commerce supplies), there is no fixed place of performance or use/enjoyment of the service. Therefore special rules need to be framed keeping in mind the basic destination principle.
- c) In the case of other services and intangible property, the place of supply is determined on the basis of one or more of the following proxies:
 - i. Place of performance of service;
 - ii. Place of use or enjoyment of the service or intangible property;
 - iii. Place of location/residence of the recipient; and
 - iv. Place of location/residence of the supplier.

2.55 In defining the place of supply of services and intangible property, a distinction is often made between supplies made to businesses (B2B) and final consumers (B2C). In general, the place of supply in the case of B2B transaction is the place where the recipient is located or established regardless of where the services are performed or used. This is particularly in the case of intangible services like advisory or consulting services for which the place of performance is not important. Therefore, all such services rendered to a non-resident are zero-rated. By contrast, many B2C services tend to be tangible or physical in nature, e.g. haircuts, hotel accommodation, local transportation and entertainment services

which are consumed in the place of their performance. Therefore, the place of supply in the case of B2C transaction is the place where the supplier is located. In some countries even such services to non-residents is zero-rated.

2.56 In addition to the above, there are a variety of other complex cross-border transactions for which supplementary rules are required to ensure uniformity and consistency across jurisdictions. They relate to global transactions (or master service agreements) for individual supplies to legal entities of a corporate group around the world, triangular transactions, supplies among branches and between branches and head office, and cost reimbursement/ allocation arrangements.

2.57 The place of supply rules indicated above relate to international transactions of goods and services. Ordinarily, these rules should also apply to inter-state supplies. However, in practice there are substantial deviations in these rules. The recipient of the services may be located in more than one state and there is no practice to determine the residency of the recipient unlike in the case of international transactions. Therefore, it is extremely difficult to identify the place in which the recipient is established/ located. In general, it would be desirable to tax B2B supplies of services and intangibles in the State of destination, and not of origin.

2.58 Given that any tax on B2B supplies would generally be fully creditable, excessive sophistication would not be warranted for defining the place of destination of such supplies. For multi-establishment business entities, the place of destination should be defined as the place of predominant use of the service. However, if there is no unique place of predominant use, the place of destination could be the mailing address of the recipient as stated on the invoice, which would normally be the business address of the contracting party. The risk of misuse of this rule would be minimal if it is limited to B2B supplies where the tax is fully creditable.

2.59 For B2C services, the place of supply should be the State in which the supplier is located, which, in turn, could be defined as the place where the services are performed. If there is no unique place of performance of the service, the place of supply could be defined

as the State where the supplier's establishment most directly in negotiation with the recipient is located.

2.60 The rules relating to the place of supply of goods and services, discussed above, are in conformity with best international practice and expert advice. Therefore, we recommend that the Centre and the States may consider framing the rules on the basis of the guidelines indicated above.

o. Threshold Limit for registration of GST dealers

2.61 Typically a small number of firms account for a large proportion of revenues from taxes on goods and services. Simultaneously, resources used in the collection of taxes are scarce and must therefore be deployed effectively; these need to be concentrated on the largest taxpayers as part of the risk management strategy. Further, the compliance burden under the invoice credit method is relatively high and it is uneconomical to collect revenues from a large number of small taxpayers. Hence, keeping in view the compliance cost and administrative feasibility, small dealers (including service providers) and manufacturers should be exempted from the purview of both CGST and SGST if their annual aggregate turnover (excluding both CGST and SGST) of all goods and services does not exceed Rs.10 lakh. However, like in most other countries, those below the threshold limit may be allowed to register voluntarily to facilitate sales to other registered manufacturers/dealers, limit competitive distortions and avoid inequities.

2.62 A case is made out that the states should be allowed to adopt different threshold limits keeping in view the size of the revenue base. Consequently, states with low revenue potential like the North-eastern states in particular must be allowed to adopt a lower threshold limit to protect their revenues. The objective of providing a threshold exemption is two-fold; firstly to mitigate the incidence of tax on the poor who generally make purchases of their goods and services from small dealers and secondly to reduce administrative burden of dealing with a multitude of small dealers who account for a dis-

proportionately low share in the revenues. Hence, allowing some states to adopt a lower threshold implies that the poor in these states will bear the incidence of tax on their consumption unlike those similarly placed in other states and therefore, would be inequitable. This will also have the potential to trigger tax-induced migration from these states. Accordingly, we recommend that the threshold exemption limit should be uniform for both CGST and SGST and across States.

2.63 Further, with a view to reduce administrative and compliance burden, we also recommend small dealers with annual aggregate turnover of goods and services between Rs.10 lakh to Rs.40 lakh²⁰ may be allowed to opt for a compounded levy of one percent, each towards CGST and SGST. However, no input credit should be allowed against the compounded levy or purchases made from exempt dealers.

2.64 The Group recognizes that certain high value goods comprising of (i) gold, silver and platinum ornaments; (ii) precious stones; and (iii) bullions (hereafter referred to as “high value goods”) are prone to smuggling due to high tax incidence thereby generating negative externalities in terms of social and economic disorder. Therefore, we recommend that dealers in such high value items may, subject to the threshold exemption but without the ceiling of Rs. 40 lakh, also be allowed to opt for the compounded levy of one percent, each towards CGST and SGST.

p. Treatment of Small Scale Industries

2.65 At present small scale industries are entitled to exemption from payment of CENVAT in respect of their turnover upto Rs.1.5 crores. However, there is no such threshold exemption in respect of state level VAT. The main reason for exemption from payment of CENVAT is to liberate them from the onerous compliance burden under the CENVAT regime particularly in the context that, in general, the small scale industries are managed by one or two entrepreneurs with the support of a handful of semi-skilled office staff.

²⁰ The limit of Rs 40 lakh is based on the consideration that dealers with turnover of Rs 40 lakh or more are subject to tax audit under the Income Tax Act, 1961 and therefore they would suffer from many additional burden in terms of documentation under the GST.

2.66 In the context of the GST, we have recommended the reporting of payment and transaction information of both CGST and SGST through the combined Form No. GST-I. Therefore, in any case the small scale industry has to comply with the reporting of payment and transaction information of SGST. No additional burden is cast upon the small scale industry for compliance with the CGST. Hence, the case for continuing with the existing exemption upto Rs.1.5 crores of turnover is extremely weak. Accordingly, we recommend that this exemption should not be continued under the GST framework.

2.67 Further, the small scale industries are generally wary of dealing with multiple tax administrations. Therefore, in order to inspire confidence of the small scale industry in the new GST framework, we also recommend that the scrutiny/audit of the small scale industry should be conducted only by the state tax administration. However, the State tax administration may seek the assistance of the central tax administration or any other state tax administration if the operations of the small scale industry transcend the state boundaries. Since the CGST and the SGST are proposed to be levied on an identical GST tax base, the outcome of any investigation impacting SGST will also have a corresponding impact on CGST. Therefore, enforcement by the State tax administration would be adequate to even deal with CGST evasion.

q. Area based exemptions

2.68 Under the CENVAT, industries set up in the North East, Jammu & Kashmir, Sikkim, Uttaranchal and Himachal Pradesh (hereinafter referred to as 'specified areas') enjoy exemption from payment of CENVAT. This area based exemption creates economic distortions and affect economic viability of units located in non-exempt areas. They are difficult to administer and prone to misuse. Moreover, durability of investment attracted by such measures beyond the exemption period is also doubtful.

2.69 The Prime Minister's Economic Advisory Council, which had recently examined the issue of area based exemption in the context of its impact on pharmaceutical industry, has observed that:-

"The policy of granting area based exemptions was ill advised. It created a host of distortions. We have to design and introduce subterfuges to neutralize those distortions. But such subterfuges make the tax administration needlessly clumsy and complex and run counter to our declared policy of simplifying the tax system. There is clearly a case for revisiting the whole issue of area based tax exemptions. If their premature withdrawal is not possible for political and business reasons, at the minimum such incentives should not be extended to fresh areas and the ones already in force should be extinguished when their applicability ends."

2.70 Further, the existing exemption for Uttranchal and Himachal has been objected to by many States. In particular, Chief Ministers of Haryana, Uttar Pradesh and Punjab have often expressed their opposition to such exemptions as these had the effect of diverting industries to Himachal Pradesh and Uttranchal.

2.71 Para 3.3.2.(viii) of the draft of "An Approach to the 11th Five Year Plan" has also commented on the undesirability of the area based exemptions. To quote :-

"The existing incentive programmes such as those available for the North East, J&K, Himachal Pradesh and Uttranchal need to be reviewed with a view to assessing their impact on industrialization in these regions. The extension of excise duty exemption to Himachal and Uttranchal has had an adverse impact on industrial investments in both the North Eastern region and the adjacent States. Consideration would need to be given to restricting these incentives to only hilly areas or to replacing these incentives by a special programme for roadways and railway development in these States."

2.72 The area based exemptions erode the tax base. The revenue foregone on account of area-based exemptions is estimated to be Rs. 8,073 crores in 2007-08.

2.73 Further, the case for providing area based exemption is extremely weakened in the face of our recommendation for a sharp reduction in the combined rates of CGST and SGST and the ease of compliance through a combined transaction reporting and payment Form No. GST-I.

2.74 In view of the above, we recommend that the area based exemption in respect of CENVAT should not be continued under the GST framework. In case it is considered necessary to provide support to industry for balanced regional development, it would be appropriate to provide direct investment linked cash subsidy.

r. Treatment of Special Economic Zones

2.75 Since the GST is designed to ensure that all producers and distributors are treated as complete pass-through and exports are zero-rated, there is no case for allowing any form of incentive to the developers of, or units in, the Special Economic Zones. We recommend accordingly.

CHAPTER – III

Treatment of Inter-State transactions

3.1 The Indian Constitution as it originally stood envisaged taxation of interstate sales only in the state where it was consumed. Unfortunately, this led some states to issue notices to dealers not resident within their jurisdictions to file returns. To bring some order in the matter, a law was enacted by the Parliament in 1956 authorising the central government to levy a tax on interstate sales called the central sales tax (CST). But the power to administer the tax was delegated by the Centre to the states of origin of the sales who were also allowed to retain the revenue. Initially, the tax was levied at the rate of only 1 per cent but it was raised successively to 4 per cent. In 2006-07, the Central Government and the State Governments came to an understanding to reduce CST in a phased manner and completely eliminate it by 1st April, 2010. Accordingly, the CST was reduced to 3 per cent. in 2007-08 and subsequently to 2 per cent. in 2008-09. However, on account of revenue implications, it has now been decided to continue with the CST at the present level of 2 per cent until GST is introduced.

3.2 The rate of CST is 2 per cent if the sale is between two registered dealers across states and the transaction is documented through the use of “C Forms”. The latter is issued by the importing state to the importing registered dealers within the state, and is submitted to the exporting dealer in order that the latter can avail himself of the concessional rate of tax. If the good is sold to unregistered dealers outside the state and is not a declared good, the transaction, by law attracts the rate applicable in the exporting state. If the rate applicable in the exporting state is less than the CST rate, the transaction is not required to be documented through the “C Form”. Since sales tax applies only when there is a sale, no tax is attracted when goods move from one state to another as transfer between branches of the same enterprise or on a ‘consignment’ basis.

3.3 The CST constitutes a distorting factor in the location of industries and the flow of internal trade, impeding the growth of a truly common market in the country. It also causes

inter-jurisdictional inequity and reduces the international competitiveness of exports. Further, the administration of and compliance with the CST is also beset with problems. The Department is constantly under pressure to monitor the exports to registered dealers. Similarly, the importers have to incur considerable transaction cost to procure “C Forms” from the department. The exporters are also burdened with the responsibility of obtaining the “C Forms” from the importers on time. Further, the treatment of branch transfers and consignment sale under the CST provides an easy avenue for evasion. In spite of the adverse economic implications of the CST, the States have come to acquire a vested interest in maintaining the status-quo since it account for about 15 per cent of their tax revenues.

3.4 In the context of the GST, it is necessary to resolve the problem relating to the treatment of inter-state sales/transfers in a manner that the incidence of the tax falls on the consumption of commodities without any distortionary cascading effect and the revenue accrues to the State where the final consumer is located.

3.5 The Empowered Committee of State Finance Ministers had set up a Working Group for designing the model. The following models for treatment of inter-state trade have been analysed by the Group:-

- i. Bank model
- ii. TDS model
- iii. SGST authority model
- iv. CGST authority model
- v. TINXSYS (De-matted C-form) model
- vi. TINXSYS with reverse charge model
- vii. Full De-mat model
- viii. Inter-State De-mat model
- ix. IGST model.

3.6 After a detailed analysis of the merits and demerits of all the models, the Group recognised that the success of every model depended on the following pre-requisites:-

- a. E-filing of return every month with dealer wise transaction details
- b. E-payment of taxes
- c. National Portal for access to information by member States and dealers
- d. National agency for overseeing the flow of information and taxes
- e. Strong IT infrastructure for the above issues
- f. The intra and inter state rates of tax should be equal to avoid evasion and camouflaging the intra state transactions as inter state transactions.

3.7 Based on its analysis, the Group has recommended the adoption of the IGST Model for implementation with the caveat that a *‘strong IT infrastructure and complete information of the interstate transactions is a precondition and essential prerequisite for considering the IGST model. Without addressing these fundamental concerns of IT infrastructure and information support systems, the adoption of IGST model which is still at a conceptual stage is far from realistic at this stage in adoption of GST in the course of interstate transaction in goods and GST for the nation.’*

3.8 The ‘Road Map to GST’ released by the Empowered Group of Ministers proposed the Bank Model as a mechanism to deal with inter-state transaction of goods and services. The functional components of the Model are :-

- a. Collection of SGST by the seller of the selling State.
- b. Remittance of SGST collected by the seller to the respective buying State’s Account in the designated bank, along with the details of buyers and invoices.
- c. Transfer of remitted tax amount by the designated bank to the respective buying State.
- d. Refund of input SGST by the selling state to the seller in the event of inter-state transactions
- e. Allowance of Input tax credit to the buyer in the buying State to the extent of the SGST received by remittance and transfer of tax amount.

3.9 The Bank Model was found to be more suitable Model, to monitor the interstate transactions of goods including stock transfer, on the following assumptions:

- i. This model would ensure evasion free tax environment and easy administration of credit flow to the buyers in the buying States.
- ii. This model envisages a level of automation that would ensure capturing all the information relating to interstate transactions in the exporting state and transferring the same to the importing state.
- iii. This model requires the bank to evolve an IT infrastructure to communicate electronically with all concerned in respect of interstate transaction of goods through a national level portal and to provide the related information to all concerned.

3.10 The Working Group recognised that the Bank Model is a ‘better system ensuring evasion free inter-state business environment’. However, the Group was of the view that it would entail higher cost of both compliance and administration. Further, it was also alarmed by the fact that ‘few members’ created an uproar by stating *“Why should the importing States permit their buyers to pay tax to the sellers of the exporting States and wait for the tax money so paid till remittance by the sellers and transfer by the bank to their exchequer?; and why can’t the Importing States levy SGST on the interstate purchases treating them as import from outside for commencement and flow of SGST credit in the importing States?”* Therefore, the Group abandoned the Bank Model.

3.11 We have also analysed the various Models presented in the Report of the Working Group. The IGST Model recommended by the Group, while requiring a IT and complex accounting infrastructure, would also require a separate legislation for levy of IGST on inter-state transactions. This will have to be similar to the present CST legislation. Further, the IGST Model envisages that the IGST may be paid either by using the CGST or the SGST. Similarly, credit for the IGST by the buyer can be claimed to make payment of either CGST or SGST. Rules would also be required to be framed for prioritising the set off against CGST, IGST and SGST. This implies a complex accounting of input tax credit and apportionment

between CGST and SGST which would considerably enhance both compliance and administrative burden. Further, the Centre and the States may also have to compensate each other at different points in time. It also envisages the establishment of a centralized agency for settlement of accounts between the Centre and the States. Therefore, we do not support the adoption of the IGST Model. We would recommend a modified version of the Bank Model (hereafter referred to as 'Modified Bank Model') for inter-state trade in goods and services.

3.12 The functional components of the **Modified Bank Model** would be as under :-

- (i) In the course of inter-state B2B supply, the seller in the origin State shall collect the SGST leviable on the transaction from the buyer in the destination State as if the sale was within the origin State.
- (ii) The seller would issue an invoice to the buyer indicating the details of the transaction (including the date of the transaction) and his business identification number (BIN).
- (iii) The seller shall use the input SGST for payment of the output SGST on both intra-state and inter-state transactions. To the extent total output SGST is in excess of the input SGST, the same shall be paid into any of the authorised bank in the prescribed manner. This will ensure a self-adjustment mechanism for input credit thereby minimizing the need for issue of refunds.
- (iv) The buyer in the destination State shall make use of the SGST so paid in the State of origin for making payment of output SGST in the destination State.
- (v) All registered dealers across the country shall pay the sum due as CGST and SGST to the credit of the Central Government and all other States within one week from the end of the month to which the sale transactions relate.
- (vi) The Central Government and State Governments shall jointly identify a nodal bank to receive the collection of CGST and SGST by collecting banks. The

nodal bank will also receive all information relating to purchase and sale by registered dealers.

- (vii) The nodal bank shall host the IT infrastructure, provide payment gateway to all banks in India and provide screen-based upload or file upload facility for receiving payment and transaction information.
- (viii) It would be mandatory for all registered dealers to make the payment by electronically furnishing Form No. GST-I, which would be a combined monthly payment and return form for all intra-state and inter-state transactions..
- (ix) As far as the registered dealer is concerned, he would be required to make a **single payment** of the aggregate of all sums due to the Centre and all other States. Even though he would have collected tax in the Origin State for inter-state transactions with buyers in a number of destination States, he can fulfil his obligation of directly remitting the tax so collected to all the destination states through a single payment made along with the electronic furnishing of Form No. GST-I. This mechanism will have the benefit of extremely low compliance cost.
- (x) It would be mandatory for all registered dealers to make electronic payment of CGST and the SGST by electronically remitting it in to the RBI, SBI or any authorized bank.
- (xi) The procedure for making payment of CGST and SGST and furnishing information relating to transactions of both purchases from and sales to registered dealers in Form No. GST-I shall be as under:-
 - (a) Seller will open Nodal Bank website or approach GST facilitation centre (which will provide Bank website access and also guide Seller) to submit Form No. GST-I. The Nodal Bank would only serve as the payment gateway to facilitate payment in any bank in which the dealer has an internet banking account.

- (b) Seller will enter his basic details such as his BIN, Name, Phone and email (Financial year will be current year by default and can be changed, date of deposit will be the current date) on Form No.GST-I.
- (c) In case the number of Invoices for sale to registered dealers and purchases from registered dealers is less than 10, the Seller shall enter the details of such individual invoices online (Invoice number, date of the invoice, BIN of the registered purchaser or seller and amount of GST collected or paid for the Invoice). If the number of invoices for sale or purchase to registered dealers is more than 10 , the seller can enter these details offline and upload the file.
- (d) The total of GST will be computed automatically and Seller can enter additional details for Interest, penalty or other amounts as applicable. The complete total will be calculated automatically and mentioned in figures and words.
- (e) Seller will have to submit this information for payment by direct debit to his bank account (as per his selection on the Nodal Bank website) as is the procedure for any e-payment.
- (f) Nodal Bank will transmit ONLY the total GST amount information, along with details of the Seller as per the challan information, to the bank for debit to the Seller's bank account. Nodal Bank will NOT transmit any information about the Invoices to the bank.
- (g) The Internet banking website of the bank will be opened automatically and the Seller will have to enter his login and password relevant for internet banking to access his bank account. Then the total GST amount

as per the challan will be debited to his account and credited to Government account by the bank.

- (h) The bank will confirm to Nodal Bank details of successful deposit of GST amount to Government account.
- (i) Nodal Bank, upon receipt of confirmation from bank of the GST payment by Seller, would generate the Form No. GST-I, which can be printed out by the Seller for his own record purposes.
- (j) The Seller would issue an Invoice to the Buyer with details of the Invoice Number and the GST amount for that Invoice. The Buyer can verify if the GST amount has been credited to the Government by using the Seller BIN, Invoice number, date of invoice and Invoice Amount to verify the corresponding entry from the nodal bank website.
- (xii) Input credit for GST would be available to the Buyer against that Invoice by using the combination of Seller BIN, Invoice Number, date of invoice and Amount of GST for that Invoice
- (xiii) All banks receiving payments from the registered dealers would be required to transfer the funds to the Nodal Bank on T+1 basis. The Nodal Bank in turn would credit the funds to the respective States.
- (xiv) The software can be designed in a manner which would have the capacity to allocate the amount paid by any registered dealer between the States on the basis of the business identification number of the buyer. The amounts so allocated can be automatically credited to the account of the destination States without any manual intervention. As a result, it would not be necessary to set up any clearing house mechanism whereby at any given point in time sums would be due to, or from, any other States. Therefore,

the destination State would not be dependent on any other State for collection of revenue.

- (xv) There will be no requirement for the buyer to make pre-payment of taxes separately for each transaction in the destination State. It will also eliminate the problem of extensive documentation like the 'C' Form in the case of CST.
- (xvi) Since every registered dealer would be required to furnish information relating to both the purchases and sales to registered dealers, this would enable automatic matching of input credit claims and identify all mismatches for follow up action. This will eliminate any possibility of fraudulent claim of input credit and evasion.
- (xvii) The Nodal Bank should be paid on per transaction record basis and the entire cost should be borne by the Central Government.
- (xviii) Further, in case of any default, the administrative responsibility and control over the collection and recovery of SGST should vest in the origin State.

3.13 As described above, the Modified Bank Model will continue to be evasion proof as the Bank Model. Since the Model envisages a single payment mechanism through a combined monthly payment-cum-return Form No. GST-I, the registered dealer can develop the data relating to the transactions on a real time basis over the entire month and eventually upload the file anytime in the first week of the following month. As a result the compliance cost would be minimal.

3.14 The IT infrastructure would be hosted by the Nodal Bank and the State tax administration would be required to establish a central computer server to download the data from the Nodal Bank. The data so downloaded can be allowed to be used by its officers through IT Network or through any other communication system. This will also reduce immediate pressure to set up the IT infrastructure in all States on or before 1st April,

2010. Further, the Model does not envisage the establishment of a clearing house mechanism. Therefore, the Model is also administratively efficient.

3.15 As stated above, the Bank Model was abandoned by the Working Group in view of an alarm set off by few States. In this context, it must be recognised that trade flow is, in general, a two way process between States. Buyers in the destination State have to pay tax to the sellers in the origin State in all cases. Therefore, if buyers in State 'A' have made payment to sellers in State 'B' and, therefore, certain amounts have become due to State 'A', there would be similar situations where sellers in State 'A' would be required to make good certain amounts to either State 'B' or any other State. Hence, it would result in almost no gain or loss to any State as they would mostly cancel each other over a period of time and over a number of transactions.²¹ The problem lies in the fact that the seller is allowed a float for a certain period before remitting the amounts to the destination States. The alternate remedy of collecting taxes like on imports at the State border check posts is fraught with severe economic inefficiency. It has been well documented that border check posts are extremely inefficient mechanisms for tax collection since they slow down the movement of goods across borders which in turn translates into high cost of inventory management. The deadweight loss on account of such economic inefficiencies far outweighs the loss on account of float allowed to the sellers in the origin State. Therefore, we are of the view that the apprehensions expressed by few States on the Bank Model are exaggerated in the absence of sufficient information and analysis.

3.16 The Modified Bank Model would not require large resources to be committed since the nodal bank would be paid on per transaction record basis. Further, since the cost would be entirely borne by the Central Government, it would not impose any additional burden on the States. In fact, the states will be able to save resources since input credit mismatches will be automatically detected thereby significantly improving its effectivity. This Model

²¹ This may not apply to States which are net exporters. However, in the Modified Bank Model proposed by us, the input tax which would be required to be refunded by these States to the registered dealers within their jurisdiction on account of inter-state transactions would be required to be paid directly to the importing State and not to the dealer.

does not require any separate clearing house mechanism as under the Bank Model. Under this Model, there is no possibility of default or failure on the part of the Sellers of the selling State to remit the SGST collected to the destination State since a single consolidated payment is required to be made in respect of all CGST and SGST liability.

3.17 In some quarters, doubts have been expressed about the efficacy of the Bank process in transfer and reconciliation of SGST remittances and its ability to handle and transfer the vast information of inter-state transactions of goods between millions of business entities across the State borders. In this context, it may be pointed out that, even today, all taxes of the Central and State Governments are collected by the banks, reconciled and transferred to the Government at different levels. Further, the large volume of data can be smoothly handled by creating appropriate IT structure. Such capacity has been developed by TCS for NSDL to handle the Income tax Department's database. We believe other large IT firms like Infosys and WIPRO also have similar software design and IT project executing capacity. The Nodal Bank can hire any such firm for developing the IT structure for GST payment and transaction information management. Therefore, such doubts are entirely misplaced.

3.18 Another apprehension expressed relates to the refund of accumulated Input tax credit on the basis of interstate transaction of goods which would continue to be a challenge and require high level of audit trails. The accumulated input tax credit on the basis of interstate transaction can be utilised to make payment of output SGST in respect of local transactions. In most cases the accumulated credit would be fully exhausted. In cases where accumulated credit remains unutilised, the same would have to be refunded. The number of such cases may not be very large. Nevertheless, the Government can establish a centralised processing centre (CPC) for processing of returns (Form No GST-I), along the same lines as the CPC established by the Income tax Department at Bangalore. This will fully meet the challenge of issuing refunds.

3.19 Another argument advanced against the Bank Model is that there is no international precedence (even in EU) in favour of adopting this model to the complexities of Indian situation. **Unlike in the EU, we have a common thread in the form of CGST which binds inter-state transactions.** This, coupled with the system of consolidated payment of CGST and SGST and transaction related information, ensures a fool proof compliance mechanism.

3.20 In view of the above, we recommend that-

- i. all inter-state transactions in goods and services should be effectively zero rated by adopting the Modified Bank Model along the lines discussed in the aforesaid paragraphs.
- ii. the consignment sales and branch transfers across states should be subject to treatment in the same manner as if it was a inter-state transaction in the nature of sale between two independent dealers.
- iii. the function of all state border check posts should be reduced to checking contrabands by setting up large scanners for trucks to pass through without any need for physical verification.
- iv. The cost of the scanners should be entirely borne by the Central Government.
- v. All check-posts should be jointly manned by both States so as to reduce the number of check-posts and enhance efficiency in the road movement of goods.

CHAPTER - IV

Administrative Structure

4.1 It is now well-recognised that tax administration is tax policy. An inefficient tax administration will not be able to provide the requisite level of deterrence thereby leading to non-compliance and under performance of the tax regime. Therefore, the full potential of the pure tax regime will remain unrealised. Hence, the structure, design and the business process of the tax administration is an important factor in the determination of the revenue performance.

4.2 In the context of the GST we are not embarking on an exercise of comprehensively designing all the elements of the tax administration. We intend to restrict our recommendations only to a few important issues.

a. Registration of taxpayers

4.3 The creation of an efficient taxpayer information system for the purposes of administering a VAT necessarily entails the creation of a taxpayer's master file through a mechanism of registration of all dealers liable to GST. Registration brings a person within the control of the tax authorities. Steps towards its compilation must be taken well in advance of the start of the GST.

4.4 Fortunately, there exists a unique taxpayers identification number at the central level in the Income Tax Department in the form of the Permanent Account Number (PAN). All persons who are liable to income tax or whose sales exceed Rs.5,00,000 are required to obtain a PAN. The Customs and the Central Excise Department has already adopted the PAN for registration of importers and exporters and manufacturers. Since the operation of a successful VAT entails coordination between the tax administrations at both the national and the state level through computerised information sharing we recommend the following:

- i. All persons with annual aggregate turnover of goods and services exceeding Rs.10 lakh (excluding CGST and SGST) should be required to register and obtain a GST registration number. Persons with lower turnover may be allowed an option to register.
- ii. The GST registration number should be a twelve digit alpha numeric number. The first ten digits should be the alpha-numeric Permanent Account Number (PAN) followed by a space and two more digits indicating the state code. This number scheme should be publicised widely and should be self-generated after obtaining a PAN²².
- iii. There will be a single GST registration number for all branches in a State. Therefore, a dealer having branches across States will have as many GST registration numbers as the number of States in which he operates.
- iv. The registrant dealer should be required to furnish a form, only by way of information, indicating the registration number for every State in which he operates. He should not be allowed to use the registration number, though self-generated, unless he has furnished the form.
- v. Since the number is PAN based, it is not necessary to have any pre-registration verification. However, the states may, if necessary, undertake post-registration verification to eliminate any potential abuse.
- vi. To begin with, on the eve of the introduction of GST, the dealer must furnish a consolidated form for all States in which he operates. If, at a later stage, the dealer extends his operation to a new State, he should be required to furnish a form for extension of activities and register the self-generated number for the new State.
- vii. Overtime, the string corresponding to PAN will be replaced by the Unique Identification Number (UIN) proposed to be issued to all residents.
- viii. It should be mandatory for all registrant dealers to obtain an e-mail ID and

²² At present, PAN has been allotted to more than 80 million people, including companies, firms and other business entities. Therefore, it is highly unlikely that there would be any existing business entity which would not have obtained a PAN.

also open an internet banking account with any bank. The form must capture the e-mail ID and the internet bank account number.

- ix. All persons with annual aggregate turnover of goods and services exceeding Rs.10 lakh (excluding CGST and SGST) would be required to compulsorily acquire the 18 digit identification number. Persons with lower turnover will have the option of obtaining the identification number.

4.5 These recommendations will enable the GST administration to save on considerable time for registration and also enable computerisation of transactions by distinguishing one record from another. Given the simplicity of the proposed registration system, the GST administration can begin registration of dealers from 1st January, 2010.

b. GST invoice

4.6 Another important element of the taxpayer information base is the VAT invoice, which forms the primary source of information and therefore a crucial control document of VAT. In an invoice based VAT system, the issue of invoices in the proper form is an essential part of the procedure for imposing and enforcing the VAT. Typically, under the VAT laws the allowance of a credit for input tax is conditional on the existence of a VAT invoice issued during the period for which the credit is claimed. An invoice is also required by the tax authorities to audit the collection of VAT. Further as indicated above, the VAT invoices form the primary source from which the return of VAT invoices will have to be prepared and furnished to tax authorities for third party information matching. Accordingly, we make the following recommendations relating to VAT invoices:

- i. The law should require a supplier making a taxable supply to another taxable person to provide a VAT invoice with that supply or the payment for it. The requirement should be enforceable by some penalty.
- ii. The VAT invoice should be standardised across all states so as to contain a minimum of information about the supply being invoiced.

c. Periodicity of GST Payment

4.7 Since the amount of VAT collected by a dealer is related to his turnover, the dealer is likely to accumulate a huge VAT liability within a very short period. Hence, it is necessary to minimise the risk of payment defaults by dealers, in particular fly-by-night operators. Given that the collection under VAT will serve as the dominant source of revenue for state governments it is imperative to provide for a collection mechanism which would ensure a periodic flow of revenue to the exchequer subject to a minimum compliance burden on taxpayers and risk of revenue loss. Therefore, we recommend that the VAT period should be a calendar month.

d. Administrative structure

4.8 The proposed GST will be a dual levy. Therefore, concern has been expressed at different fora on the administrative structure for implementing the CGST and the SGST consistent with the autonomy of the different levels of Government. Therefore, we recommend that the tax administration and procedures for the dual GST should be designed in the following manner:-

- (a) The Central Board of Excise & Customs (CBEC) shall be responsible for implementing the CGST and the State Tax administrations will be separately responsible for implementing the SGST²³. The various tax administrative functions such as assessment, enforcement, scrutiny and audit should be undertaken by the CBEC in respect of the CGST and by the State tax administration in respect of the SGST subject to our recommendation on small-scale industries.
- (b) All procedures under CGST and SGST should be uniform.

²³ The jurisdiction between the CBEC and the State Administration may be divided between the two in such manner that the interface of the taxpayer is confined to one tax administration only. The basis for division could be turnover or any other criteria which is considered reasonable so that the compliance and administrative burden is minimized.

- (c) Each taxpayer should be allotted a PAN based taxpayer identification number, as recommended above.
- (d) The unit of taxation for the purposes of GST should be persons as defined under the Income Tax Act. Consequently, for the purposes of CGST, all production units/branches of a person located anywhere in the country will be treated as a single taxable entity eligible for CGST input credit across units/branches. Similarly, for the purposes of SGST, all production units/branches of a person located anywhere within the State will be treated as a single taxable entity eligible for SGST input credit across units/branches in that State.
- (e) The Central Government shall establish a common IT infrastructure which will serve the needs of both CGST and SGST.
- (f) The Central Government will be responsible for establishing a taxpayers information network (TIN) keeping in view the information requirement of CBEC and the State tax administration. The TIN will be shared between the Centre and the States.
- (g) The payment of tax and the transaction reporting should be made through a combined payment and transaction reporting statement in Form No. GST-I. This statement should detail all business to business transactions relating to sales. This statement should be common for both CGST and SGST compliance and it should be mandatory to file this statement electronically on a monthly basis while making payment of taxes.
- (h) Taxpayers opting for the compounded levy may be required to pay their taxes and file their returns on a quarterly basis.
- (i) Electronic filing of all other returns, if any, should also be mandatory. Therefore, the return forms should be common for CGST and SGST compliance.

- (j) The information furnished shall be stored in a common database to which both the CBEC and the State tax administration will have access.
- (k) For the purposes of audit, both CBEC and the State tax administration can design an independent risk management strategy. However, both must coordinate to ensure that the same taxpayer is not subject to simultaneous audit under CGST and SGST.
- (l) The administration of this levy should be based on audited accounts and not on the basis of any form of physical controls.
- (m) Since the tax base will be common, there should be a common appellate authority. Similarly, the Authority for Advance Ruling will also be common.
- (n) Best international practices should be embedded in the Central-GST, particularly in respect of laws relating to levy of penalties, and circumstances and method of prosecution.
- (o) No authority should have any power to make preventive detention for the purposes of CGST and SGST.
- (p) Procedures for collection of both the CGST and SGST should be uniform.

4.9 The uniformity in the procedures recommended by us will considerably reduce compliance and administrative cost. This should undoubtedly result in improved voluntary compliance.

CHAPTER - V

Rates of Tax

I. Single or Multiple Rates

5.1 The choice of a single or a multiple VAT rates is highly controversial. There is a belief that the public will accept a VAT type GST more easily if products consumed by low-income households are taxed at lower rates than products consumed by those that are better off. Administrators who actually implement the tax know that every additional rate will significantly increase cost and complexity. The cost of auditing the classification of exempt and taxable items and the applicable rates thereon at every stage of production, distribution and sale is also extremely high. Therefore, they support the elegance of a single rate (other than the zero rates). Economists espouse the optimality of tax rates based on elasticity. In general, business and industry also espouse a single rate since it is simple to comply and eliminates the problem of classification which arises under the multiple rates regime leading to protracted legal disputes and taxpayers' grievances. Further, multiple rates also implies that the standard rate is relatively high. Since taxes result in economic distortion which increases exponentially with the increase in the applied tax rate, a relatively high standard rate creates much larger economic distortion. It also provides an incentive for evasion and frequent lobbying by trade and industry for favourable modifications in the tax schedule.

5.2 Early VAT systems were characterised by a progressive tax structure whereby basic necessities were taxed at lower rates, luxuries at higher rates and all other goods and services at a standard rate. The problem was further compounded by numerous exemptions. However, since the 1990s there is a growing trend towards a single positive rate, a zero rate and some, or no, exemptions.

5.3 The Task Force on Implementation of the Fiscal Responsibilities and Budget Management Act, 2003 sketched the elements of a reform strategy which would achieve the core economic policy goals of promoting efficiency, equity and high quality growth.

These elements, inter-alia, included low and few rates. The Task Force expressed the view that *“High tax rates distort economic decisions and fuel and deployment of resources into tax avoidance and tax evasion. A large number of rates of taxes exacerbates the problem of bracket creep and classification disputes. These arguments suggest that a rational tax system is one with very few rates and low rates. For example, debates on customs duties have universally argued that if customs tariffs have to exist, there should be a single uniform rate on all goods. Similarly, it is well accepted that there should be a single VAT rate covering all kind of production”*. In view of the fact that both the Centre and the States had multiple rates, the service tax base was extremely narrow, and the States had not moved to VAT, the Task Force, even while recognising the efficacy of a single VAT rate, recommended multiple rates as a transitory step towards a single VAT rate²⁴. The recommendation does not, in any way, undermine the efficacy of a single VAT rate²⁵.

5.4 Bogetic and Hassan (1993)²⁶ analysed a diverse group of 34 countries on a wide spectrum of VAT structures bases and revenues. In terms of VAT structure, two groups of countries were identified: single rate and multiple rate countries. Given the revenue performance data and the consensus preference of tax experts for single rates, they examined whether existing data on VAT support the contention that countries with single rate mobilise more revenue than those that have multiple rates. The empirical results confirm that the dispersion of rates if found to negatively affect VAT revenues. The results also confirm in other conventional view that VAT generates, other things being constant, higher revenue in single VAT rate countries than in multiple rates countries. The difference in the estimated models for the two country groups statistically significant indicating a structural change²⁷. Accordingly, they recommend that to generate superior revenues, a VAT should be levied in a single rate on as broad base as possible; it also must be accompanied by a strong tax administration to ensure enforcement and compliance.

²⁴ This has been ascertained from Dr. Vijay L. Kelkar, who headed the Task Force.

²⁵ The recommendation for multiple VAT rates was adversely commented upon by experts.

²⁶ Bogetic, Zeljko and Fareed Hassan (1993). Determinants of Value-Added Tax Revenue: A Cross-Section Analysis, The World Bank Working Paper No.1203.

²⁷ They also point out that the change in the pattern of VAT revenues cannot be exclusively explained in terms of difference in rate structures.

5.5 Mello (2008)²⁸ empirically analyses 38 OECD and non-OECD countries and concludes that VAT efficiency is inversely related to the statutory rate and the share of tax administration costs in tax revenue (proxying for tax administration efficiency)²⁹. The VAT efficiency is affected adversely by the level of the statutory rate. The co-efficient in the tax is small in magnitude, although it is highly significant, so that the loss in efficiency due to an increase in the VAT rate is relatively modest. The elasticity of VAT revenues to VAT rate is (-) 0.3 approximately. Silvani and Wakefield (2002) analyse a sample of 22 countries in the 1990s and show that, if the VAT tax rate is raised by one percentage point, productivity falls by 3.6 per cent.

5.6 The Group took note of the fact that, in 2007-08, the combined statutory incidence of CENVAT, CST and State level VAT on goods was in the range of 27 per cent and 30 per cent³⁰. This combined rate is one of the highest in the world and is not conducive to voluntary compliance. Further, it also underscores the need for multiple rates.

5.7 The Group also took note of the need to minimize the tax burden on consumption by low income households. However it does not recommend a low rate of tax, or exemption, for products consumed by low income households since the same products also form part of the consumption basket of the middle and high income households. As stated earlier, the introduction of a low rate or exemption for products commonly consumed by low income households also results in increase in the standard rate. Since low income households also consume goods liable to tax at the standard rate, the cumulative burden on the aggregate consumption by the low income households remains unaffected in spite of the exemption or

²⁸ Mello, Luiz de (2008). Avoiding the Value Added Tax: Theory and Cross-Country Evidence, OECD, Economics Department Working Paper No. 604.

²⁹ VAT efficiency also tends to be higher in countries where the regulatory framework in product markets is pro-business and governance (regulatory quality, rule of law and government effectiveness) is strong. Moreover, VAT productivity does not seem to differ in a statistically significant manner between OECD members and non-members. Finally, the ratio of administrative costs to tax revenue is the best-performing indicator of tax administration quality used in the empirical analysis, with other metrics, such as the ratio of audit and other non-audit verification assessments to net revenue having a much lower predictive power.

³⁰ This does not include the incidence of embedded taxes which are not vatiable. This combined statutory incidence has since reduced to a lower range of 18 per cent to 20 per cent in 2008-09 as a consequence of the sharp temporary cut in the CENVAT rate.

low rate for the common goods consumed by them. The Group also recognized that, in general, the low income households purchase their requirement of daily necessities from the small neighbourhood retail outlets whose turnover is generally low/moderate. Therefore, the burden of GST on consumption by low income households should be minimized, more appropriately, by providing a moderate threshold exemption for registration of dealers. Accordingly, the Group has, in para 2.61 above, recommended a threshold exemption limit of Rs.10 lakh.

5.8 Further, in terms of best international practice, recent experience shows that the preference of the policymakers is for adoption of a single rate as it is more efficient.³¹

5.9 In the light of the above, the Group recommends **one positive rate**, each for CGST and SGST on all goods and services. In addition, there should be a **zero rate** applicable to all goods and services exported out of the country.

5.10 A view has been expressed that a single rate of State GST for all goods and services will, in our country with its large low income population, be highly regressive. It is mainly the articles of common consumption which are in the lower rate bands of VAT. The single revenue-neutral rate will definitely be much higher than the rate now prevailing at the lower bands. In short, the incidence of taxation on the articles consumed by the common man will rise, while the rate of tax on luxuries will fall. The implementation of a regressive tax during an economic slowdown is even worse than doing so in a boom. In other countries where such a shift to a single rate has occurred, an increased propensity to evade has also been noticed. Those who argue for a single rate GST on grounds of economic efficiency and growth are ignoring the adverse distributional consequences. The implementation of a single rate will thus be highly unpopular with the common man.

5.11 Under the present Indirect Tax regime at the State level, the lower rate is generally 4 per cent. However, in the absence of a seamless flow of the input credit mechanism resulting in cascading of taxes **and** the CENVAT-inclusive tax base, the incidence on products

³¹ Michael Keen (2009): "What makes a successful VAT?", Presentation at the Workshop on September 30, 2009 at the National Institute of Public Finance and Policy (NIPFP), New Delhi.

liable to the lower rate of 4 per cent is substantially higher. Since we recommend in para 5.79 a single rate, which is extremely low in comparison to the existing standard rate of 12.5 per cent, there is little scope for providing a further lower rate. In addition, the proposed GST design structure envisages a comprehensive base with a seamless flow of the input credit mechanism. Consequently, the cascading effect would be negligible. Further, the tax base will be exclusive of CENVAT. The cumulative effect would be that the real tax incidence under the proposed GST model would approximate the statutory rate and would not be significantly different from the present levels of incidence on such products. The proposed single rate GST regime will be transparent in comparison to the present opaque system. A move to a single rate of GST is regressive if the initial point is a destination based VAT type regime across a comprehensive base and allowing for seamless flow of input credit where the cascading effect is either non-existent or negligible. Since the existing indirect tax structure is characterised by significant cascading effect, the move to a single rate of GST which approximates the real incidence, does not result in any adverse distributional consequences.

5.12 A tax on consumption can be regressive. The structure should be designed to alleviate the tax incidence on consumption by the relatively poorer section of the society. One of the methods could be to identify such items of consumption by the poor and either exempt them from GST or subject them to a lower rate. Under this method, consumption by the rich would also suffer the same level of tax since no distinction can be made between the rich and the poorer consumers at the point of sale. Therefore, this method is highly regressive. The second method is to provide for a moderate threshold exemption level for registration of dealers. Consequently, all small dealers would remain outside the purview of the GST and, therefore, the tax incidence on products sold through such dealers would be relatively lower. Since the poorer section of the society tend to make their purchases from such small and unregistered dealers, the consumption of any commodity by the poor would bear a relatively lower incidence of tax than the consumption of the same commodity by the relatively richer section of the society. In the aforesaid paragraphs, we have

recommended a modest threshold exemption level of Rs.10 lakh. This recommendation is aimed to address the issue.

5.13 The distributional consequences of the proposed GST should be analysed keeping in view its impact on economic growth and employment. To the extent it enhances economic efficiency, it will also create new opportunities for employment which would obviously benefit the relatively poorer section of the society and improve equity³². There is yet another instrument to improve the distributional outcome of this by direct cash transfer to the target groups. With the proposed UIN system such a policy is feasible and a more efficient option.

5.14 In view of the above, the apprehension that the move to a single rate would be regressive is misplaced.

5.15 It has been argued that the proposal to have a uniform rate of State GST reduces the autonomy of the States and, therefore, undermines the federal structure of our Constitution. Further, the States would lose the flexibility to swiftly respond to any crisis³³. In the present context, the design of the structure of the GST will be determined through the collective process of a 'grand bargain' between the Centre and all the States for the collective welfare of its people. The decision to have a uniform rate should, therefore, be viewed as a collective decision of all States and Centre to harmonize the tax rates, arrived on the basis of consensus in the Empowered Committee of State Finance Ministers. Further, the proposed GST structure would confer upon the States the power to tax services which accounts for about 54 per cent of the GDP. This would significantly improve the vertical imbalance in the federal fiscal relations in favour of the States³⁴. The States would also have the flexibility to impose surcharges to meet any financial need in an emergency-like situation.

³² Unemployment results in an implicit taxation of the poor at the rate of 100 per cent.

³³ Some States have argued that but for the flexibility, the Central Government would not have been able to reduce the CENVAT rate as a response to the economic slowdown witnessed in the second half of the fiscal year 2008-09.

³⁴ This would be so even after making appropriate adjustment for allowing the Centre to levy tax upto the retail stage.

5.16 It is now well recognised that the performance of GST is dependant, amongst others, on the ratio $\left[\frac{\text{Weighted average of statutory rates}}{\text{Standard rate}}\right]$ ³⁵. Therefore, the ratio is less than one if there are multiple rates. Hence, it is necessary to adopt a single rate so as to optimize the performance of the GST.

II. Determination of the rate of GST

5.17 One of the crucial issues relates to the determination of the rate of CGST and SGST. Since the GST is primarily intended as an exercise in reforming the consumption tax in India and not an exercise for additional resource mobilisation through discretionary changes, the CGST and SGST rates should be such rates which would yield the same revenue as collected from the various taxes which will be subsumed in the CGST and SGST (hereafter such rates shall be referred to as ‘**revenue neutral rates**’ or ‘**RNR**’).

5.18 The Thirteenth Finance Commission has been mandated to make its recommendations having regard to the basis of levels of taxation likely to be reached at the end of 2008-09. However, the fiscal year 2008-09 has been characterised by unprecedented economic meltdown necessitating immediate and temporary midyear corrections in the rates of CENVAT and Service Tax. Further, due to intra-year extreme volatility in the prices of various commodities, the levels of taxation achieved in 2008-09 are substantially lower than what would have been achieved if the trend of the preceeding five years had continued. Further, detail firm level data is required for the purposes of calculation of RNR. This is available only upto the fiscal year 2007-08. **Therefore, the Group has used the fiscal year 2007-08 as the base year for calculation of the RNR.**

³⁵ A **standard rate** is defined to mean the rate on supply of all general goods and services for which no other specific rate is provided. In effect, this is the rate applicable to the residuary category of goods and services. Further, detail analysis of this is presented in Chapter – VI.

5.19 The RNR for the CGST and the SGST is determined in accordance with the formula-

$$\text{RNR} = \frac{\text{R}}{\text{B}} \times 100$$

Where,

RNR : Revenue Neutral Rate for the Centre or the States as the case may be;

R : Collection from the Central or State taxes, as the case may be, which are proposed to be subsumed in the CGST and SGST;

B : Estimated Tax base of the GST

a. Taxes to be subsumed in the GST

5.20 The **Central taxes** which are proposed to be subsumed by the Empowered Committee in the CGST are indicated in Para 2.11 of Chapter-II of this Report. We concur in this proposal of the EC. Further, the SIN goods will be subject to a dual levy comprising of the CGST and Excises. The total collection from these central taxes in 2007-08 was **Rs 233435 crores** (including collection from petroleum and tobacco products) of which collection from non-SIN goods and services was **Rs 157733 crores only**. The breakup of the collections is presented in Table-1. Since the SIN-goods will continue to be subject to excises as at present, the RNR for the CGST is sought to be calculated only in respect of **Rs 157733 crores**, being the collections from non-SIN goods and services.

Table-1: Revenues from Central taxes to be subsumed in CGST					
Sl No	Nature of Tax	Non-SIN Goods	POL	Tobacco	Total
1	CVD	53510	5199	0	58709
2	Union Excise Duties	52922	60231	10272	123425
3	Service Tax	51301	0	0	51301
4	Total	157733	65430	10272	233435
Note: Union Excise Duties includes Additional Excise Duties and the various cesses listed out for subsumation in the CGST					

5.21 Similarly, the total collection from “**EC-taxes**” in 2007-08 was **Rs.118356 crores** (excluding collection from petroleum, alcohol and tobacco products). However, the total collection from “**TF-taxes**” (excluding collection from petroleum, alcohol and tobacco products) was **Rs 188285 crores** in 2007-08 as per details presented in Table-2. Since we are of the view that all the “**TF-taxes**” should be subsumed in the SGST, our RNR for the SGST is sought to be calculated in respect of an amount of **Rs 188285 crores**.

Table-2: Revenues from State taxes to be subsumed in SGST

Sl. No	Nature of Taxes	Non-SIN Goods	POL	Tobacco	Alcohol	Total
1	Stamp Duty	38473				38473
2	Taxes on Vehicles	15549				15549
3	Taxes on Goods & passengers	6719				6719
4	Taxes and Duties on Electricity	9188				9188
5	Sales Tax/VAT (incl. CST and Purchase Tax)	110826	56442	3000	11450	181718
6	Entertainment tax	1062				1062
7	Entry taxes not in lieu of Octroi	3914				3914
8	Other taxes and Duties*	2554				2554
9	Total (sum of 1 to 8)	188285	56442	3000	11450	259177
10	TF- Taxes (sum of 1 to 8)	188285				
11	EC- Taxes (sum of 5 to 8)	118356				

* This includes (i) taxes on lottery, betting and gambling; (ii)luxury tax; and (iii) cesses and surcharges by States

b. Estimation of the GST base

5.22 For the purposes of estimating the RNR, we need to first **estimate the GST base** in the light of the GST Model designed by us. There are essentially two methods of estimating the GST base. **One method** is to estimate the final consumption in the country and make appropriate allowance for leakage. However, the pre-GST indirect tax system is generally characterised by high leakage while the shift to a consumption-type GST is compliance

enhancing. Therefore, estimating the degree of leakage under the proposed GST is vexatious. The **second method** is to estimate the gross value addition by the producers of goods and services and make appropriate adjustments relating to imports and exports. The gross value addition by the producers can be estimated by either using the input-output table or the profit and loss account of the producers.

5.23 For the purposes of estimation of the GST base, we use the following methods/approaches:-

1. Subtractive – indirect method (SI method);
2. Consumption method
 - i. Task Force Estimate; and
 - ii. NCAER Estimate.
3. Shome Index method
4. Revenue method

5.24 We use the average of the estimates under these methods as the estimate of the GST Base for the purposes of calculating RNR.

1. Subtractive – indirect method (SI method)

5.25 At the producer level, the GST base is equivalent to the value added which is the value that a producer adds to his raw materials or purchases before selling the new or improved product or service. That is, the inputs (the raw materials, transport, rent, advertising, and so on) are bought, people are paid wages to work on these inputs and, when the final good or service is sold, some profit is left. So value added can be looked at from the additive side (wages plus profits) or from the subtractive side (output minus inputs).

5.26 Value added = wages + profits = output – input. If the tax rate on this value added is 't', there are four basic forms that can produce an identical result:

- (1) t (wages + profits) : the additive – direct (accounts) method;

- (2) $t(\text{wages}) + t(\text{profits})$: the additive – indirect method³⁶,
- (3) $t(\text{output} - \text{input})$: the subtractive – direct (accounts) method; and
- (4) $t(\text{output}) - t(\text{input})$: the subtractive – indirect (the invoice or credit) method.

5.27 While there are four possible ways of levying a VAT, in practice, the method used (number 4) never actually calculates the value added; instead, the tax rate is applied to a component of value added (output and inputs) and the resultant tax liabilities are subtracted to get the final net tax payable. This is sometimes called the “indirect” way to assess the tax on value added.

5.28 The Subtractive – indirect method (SI method) is based on the profit and loss account of producers. Since extensive producer level data was available with the Income Tax Department, the Group analysed the profit and loss accounts of **28, 51, 248 business entities** for the financial year ending on the 31st March, 2008 (financial year 2007-08) which have electronically filed their profit and loss account along with their return of income with the Income Tax Department for assessment year 2008-09. The activities of these entities are classified into 9 sectors and further sub classified into 74 sub-sectors (refer Annex - II). Further, the sample includes **3,50,894** companies and **3,84,425** partnership firms. Since it is mandatory for firms with an annual turnover of more than Rs.40 lakhs and all companies to electronically file their return of income, the dataset includes all companies and such firms, who have filed their return upto 15th August, 2009 for the financial year 2007-08 (assessment year 2008-09). In addition, it also includes other business entities which have voluntarily opted to electronically file their return. For the purposes of this exercise, we assume that these **28, 51,248** entities constitute the universe of the GST taxpayers. This sample does not include the multitude of taxpayers who have filed their tax returns in paper form. Charitable organizations are required to file their return only in paper form. Therefore, the sample does not include the tax returns of any charitable organization. Since

³⁶ This method is so called because value added itself is not calculated but only the tax liability on the components of value added is calculated.

most entities engaged in providing education and health services operate as charities, the sample does not include education and health services providers. Further, since agricultural income is exempt from income tax, the sample does not capture the data relating to the agricultural sector.

Table-3: Turnover based Distribution of sample entities			
Turnover* range	Number of cases	Amount of Output base (Rs in crores)	Share in the total turnover (in percent.)
Less than zero	2014	-719	-0.01
Between 0 to Rs 10 lakh	1616862	25761	0.28
Between 10 lakh to Rs 25 lakh	237333	38933	0.42
Between 25 lakh to Rs 40 lakh	146984	48061	0.51
Between 40 lakh to Rs 100 lakh	333047	219065	2.34
Between 1 crore to Rs 2 crore	199099	280778	3.00
Between 2 crore to Rs 5 crore	165385	519055	5.55
Between 5 crore to Rs 10 crore	71341	498382	5.33
Between 10 crore to Rs 100 crore	71332	1840605	19.68
Above 100 crore	8160	5884524	62.91
Gross Total	2851557	9354445	100
Less: Indirect Taxes		281168	
Turnover net of indirect taxes		9073277	
* Turnover is defined as total credits in the Profit and Loss Account as reduced by the value of closing stock. This is the same definition used for computing the GDP			

5.29 The distribution of taxpayers across turnover is shown in Table-3. For this purpose, “turnover” is defined to mean the aggregate of all income receipts credited to the Profit and Loss account so as to align it with the definition of “gross value of output” for the purposes of National Accounts by the CSO. The aggregate gross value of output of the sample entities

is Rs.90,73,277 crores³⁷ in 2007-08 as against the gross value of output of Rs.75,78,410 crores estimated by CSO for the non-agricultural sector³⁸. Therefore, it is obvious that the CSO estimation of gross value of output seems to be an under estimation.³⁹ Consequently, the estimation of GDP, private final consumption etc., by the CSO also appears to be understated. Therefore, the sample size is extremely large and any estimation of the GST base on the basis of this sample will be fairly representative of the actual GST base.

5.30 The computation of the GST base under the SI method involves the following steps:

- a. The receipt items on the credit side of the Profit and Loss Account, which would be liable to output tax, are identified and appropriately adjusted for indirect taxes to arrive at the **‘value of supply of domestically produced goods and services (net of indirect taxes)’** (hereinafter referred to as **‘net value of supply of domestically produced goods and services’**);
- b. Since imports are liable to GST at the point of importation, the **‘value of imports’** is aggregated with the **‘net value of supply of domestically produced goods and services’** to arrive at the **‘net value of domestically available goods and services’**.
- c. Since exports are zero rated in a GST regime, the value of exports is reduced from the **‘net value of domestically available goods and services’** to arrive at the **‘net value of goods and services available for domestic consumption’** or the **‘aggregate output tax base’**.
- d. Similarly, the expense items on the debit side of the Profit and Loss Account, in respect of which input tax credit would be potentially

³⁷ Since agricultural income is exempt from income tax and persons whose income is predominantly from agriculture are not required to file their tax returns, this does not include the gross value of output produced in the agricultural sector.

³⁸ This is derived by reducing the aggregate of the value of output of Rs.9,18,846 crores in agriculture, Rs 3,33,098 crores in Public Administration and Defense and Rs 2, 84, 953 crores being 50 percent of the value of the output under ‘Other services’ from the value of total output of Rs 91,89,784 crores in 2007-08 as reported by CSO.

³⁹ The turnover of the sample entities relate to the organised sector. The under reporting of the value of output by the CSO is further accentuated if we adjust for the unorganised sector.

available, are identified and appropriately adjusted for indirect taxes to arrive at the **'value of purchase of intermediate goods and services'**.

- e. Under the GST Model, full and immediate input credit is proposed to be allowed for GST paid on purchase of capital goods in the year of purchase. Therefore, the **'value of purchase of capital goods'** is aggregated with the **'value of purchase of intermediate goods and services'** to arrive at **'gross value of purchase of intermediate goods and services'**.
- f. Since no input tax credit would be available in respect of purchases made from unregistered dealers, the **'value of purchases from the unregistered dealers'** is reduced from the **'gross value of purchase of intermediate goods and services'** to arrive at the **'aggregate input tax base'**.
- g. The **'aggregate output tax base'** is reduced by the **'aggregate input tax base'** to arrive at the **'GST Base'**.

5.31 On the basis of the profit and loss accounts of the 28,51,248 business entities, the **"net value of supply of domestically produced goods and services"** is the aggregate of the value (net of indirect taxes) of (i) Sales/gross receipts from business; (ii) Commission; (iii) Profit on sale of fixed assets; and (iv) 'Any other income' since output tax would be charged only in respect of these four items credited to the profit and loss account.⁴⁰ This is estimated to be **Rs. 87,21,874 crores in the financial year 2007-08 for all sectors**. This constitutes 105.02 percent of the gross value of the output in the non-agriculture sector in 2007-08, as reported by CSO. However, the corresponding figure for the **taxable sectors (excluding financial, rail and real estate sectors)** is **Rs. 77,62,224 crores**.

5.32 The item 'any other income' as reported in the accounts does not include rent, dividend, interest, profit on sale of investments liable to STT, profit on other investment,

⁴⁰ In the case of rent, the expenditure on rent is reduced by the rental income reported. Therefore, we do not separately include this item in the 'net value of supply of domestically produced goods and services'.

profit on currency fluctuation and agricultural income. In practice, a large number of professional entities report their gross receipts under this item since they do not view themselves as carrying on business or engaged in sales. Since the Group has recommended a comprehensive GST base to include all goods and services, the value of supply of goods and services must therefore, include the item 'any other income'. As regards, rent, dividend, interest, profit on sale of investment liable to STT, profit on other investment, profit on currency fluctuation and agricultural income, these have been excluded from the value of the supply of goods and services since the source of these items of income is, in general, a business-to-business transaction and therefore, a wash transaction in the context of GST.

5.33 The various receipts which have been excluded from the item 'any other income' basically arise from transaction in financial services and immovable property. While the base for GST is proposed to include financial services and immovable property (real estate), the size of the base relating to these services is determined separately and not on the basis of the subtractive-indirect (invoice or credit) method.

5.34 Input tax base comprises of all goods and services used as intermediate inputs in the production of goods and services and on which output tax has been paid. The **'value of purchases of intermediate goods and services'** is the aggregate of the expenditure on items listed in Table-4. The aggregate of such expenditure by all the sample entities during the financial year 2007-08 is Rs.73,29,483 crores of which Rs 4,32,910 crores relates to purchase of agricultural commodities and the balance Rs 68,96,573 crores relates to purchases from the non-agricultural sector. However, the **'value of purchases of intermediate goods and services'** by the **taxable sectors (excluding financial, rail and real estate sectors)** is Rs. **67,12,418 crores.**

Table-4: Intermediate goods and services forming part of Input Tax Base

A	Purchases of trading goods and raw material	
B	Special services	
	1	Freight
	2	Consumable Stores
	3	Power & Fuel
	4	Building repair
	5	Machinery repair
	6	Total expenditure on insurance
	7	Workmen and staff welfare expenses
	8	Entertainment
	9	Hospitality
	10	Conference
	11	Sales promotion including publicity (other than advertisement)
	12	Advertisement
	13	Commission
	14	Hotel boarding and lodging
	15	Travelling expenses including foreign travelling
	16	Conveyance expenses
	17	Telephone expenses
	18	Guest house expenses
	19	Club expenses
	20	Festival celebration expenses
	21	Gift
	22	Audit fee
C	Miscellaneous Services	
		Other expenses

5.35 The aggregate of the purchases of trading goods and raw material by all the sample entities during the financial year 2007-08 is Rs.56,70,610 crores. However, the corresponding figure for the **taxable sectors (excluding financial, rail and real estate sectors)** is Rs. 51,80,108 crores. These purchases include purchase of trading goods and raw materials from registered and unregistered dealers in both the primary and secondary sector. To the extent these include purchases of trading goods and raw materials from the unregistered dealers, no input tax credit would be available since no output tax would have been paid by the unregistered dealers. In the case of primary articles like cereals and plantation crops, these would generally be purchased from agriculturists who would be

outside the scope of GST either by virtue of exemption or by virtue of their turnover being below the threshold limit. If for some reason, the agriculturist falls within the scope of the GST, he would be liable to collect GST for which the purchaser in our sample would be eligible to claim input credit. Since agriculturists do not ordinarily file an income tax return, his sales do not form part of the output base estimated above. Therefore, purchases of primary articles would not be entitled to any input credit. Such purchases are estimated to be Rs.4,32,910 crores. Further, we also estimate 10 percent of the purchases of trading goods and raw materials from the secondary sector to have been purchased from the unregistered dealers on which no input credit would be available. Such purchases amount to Rs.5,23,770 crores. Therefore, the aggregate purchases of trading goods and raw material from unregistered dealers is Rs 9,56,680 crores in 2007-08 for all sectors.

5.36 The value of **Special services** availed by all sample entities is Rs.7,25,657 crores. Given the nature of the services, we estimate 25 percent of the services to have been acquired from **unregistered dealers** and therefore, no input credit would be available. The **value of such services is estimated to be Rs.1,92,756 crores.**

5.37 Similarly, the value of **Miscellaneous Services** availed is Rs.8,67,077 crores which is charged to the profit and loss account under the head 'other expenses'. These are generally petty expenses in nature most of which are acquired from unregistered dealers. It is estimated that 60 percent of this amount would be from unregistered dealers. Accordingly, a sum of Rs. 5,32,709 crores will not be eligible for input credit.

5.38 Accordingly, the '**value of purchases from the unregistered dealers**' in 2007-08 for all sectors is computed at Rs.16,82,145 crores of which Rs 4,32,910 crores relate to purchases of agricultural commodities and the balance Rs .12,49,235 crores to non-agricultural goods and services. In the course of discussion in different fora on the estimated purchase from unregistered dealers, a view was expressed that this estimate may be upwardly biased. Therefore, it is important to undertake a validation check of the estimate.

5.39 In general, the unorganized sector in terms of the National Accounts Statistics is a good proxy for the unregistered dealers under the GST. The share of the unorganised sector in the non-agriculture Net Domestic Product in 2007-08 is 48.69 percent and 90.27 percent in the agricultural sector.⁴¹ Applying these ratios to the firm level profit and loss account, the purchases from the unorganised sector/unregistered dealers is estimated at Rs37,48,729 crores of which Rs 3,90,788 crores relates to agricultural commodities and the balance Rs 33, 57, 941 crores relate to purchase of non-agricultural goods and services from the unorganised sector. Our own estimate of Rs 16,82,145 crores is only 45 percent of the purchases from the unorganised sector estimated on the basis of the National Accounts Statistics. Therefore, there is no reason to doubt the veracity of our estimates.⁴²

5.40 On the basis of the above, the GST bases for the '**Taxable sectors**' and '**Exempt sectors**' (which comprises of the Food sector and health and education services) are computed separately.

- **Exempt sectors**

5.41 We have earlier recommended exemption from GST of unprocessed food articles. Producers of food grains do not file income tax returns. Similarly, most of the trading in food grains is undertaken by small traders with low turnover. Such traders, in general, file their income tax returns in paper form. However, the sample represents electronically filed returns only. The impact of the exemption for unprocessed food articles (rice and wheat) on our estimation of the GST base is not significant.

5.42 Similarly, we have also recommended exemption from GST in respect of health and education services. The health and the education sector is mostly organised as charitable trusts. The charitable trusts are required to file their returns in paper form and therefore do

⁴¹ See Statement 76.1 of National Accounts Statistics 2009

⁴² In reality, it is likely that the purchases from unregistered dealers would be substantially larger than our estimate. To the extent it is so, the GST base is likely to increase, and the RNR would be lower, than our estimate.

not form part of the sample. However, 3928 trusts with a total turnover of Rs 8133 crores have electronically filed their returns. Assuming that these trusts operate in the health and education sector, the volume of the total turnover is insignificant to make any material difference to the estimation of the GST base. Therefore, no separate adjustment is made to provide for the exemption for the health and education sector under the proposed GST.

5.43 Separate data relating to life-saving drugs is not available. Therefore, we estimate the GST base relating to this sector at Rs 5000 crores on the basis of anecdotal information.

5.44 Therefore, the GST base relating to the 'Exempt sectors' is estimated at **Rs 86, 575** crores.

- Taxable sectors

5.45 The '**Taxable sectors**' is sub-divided into two, namely, the '**General sectors**' and the '**Special sectors**'. The latter comprises of the Financial Sector, Rail Transport Sector and Real Estate Sector. The GST base relating to the '**General sectors**' is computed by using the **SI method**.

5.46 In terms of the proposed GST Model, the tax base will include real estate (land and buildings) and housing services. In the case of real estate transactions, the incremental value between two transactions will be subject to GST thereby, subsuming the stamp duty within the GST base. Further, rent, whether from residential or commercial property, will also form part of the GST base. However, rent in a business-to-business transaction will be a wash transaction. Since expenditure on rent is greater than the rental income in the case of sample entities, the net expenditure on rent is included in the '**value of purchase of intermediate goods and services**'. To the extent GST on rent will also be collected on business-to-consumer transactions, it is not feasible to make any estimate of the volume of such rental transactions. Therefore, the estimate of the tax base relating to real estate and housing services is limited to the estimated base in respect of real estate (land and

buildings) transactions. In 2007-08, the Gross Fixed Capital Formation by way of construction in the household sector is Rs 429260 crores. This does not include the value of land. Assuming that the land value accounts for 50 percent of the total value of the real estate, the GST base relating to land is estimated at Rs 429260 crores.

5.47 The comprehensive GST is intended to bring within its fold rail transport services also. However, this is intended to be confined to rail services provided for transportation of goods only. The rail transportation sector is entirely under the Ministry of Railways which is not required to file a tax return. Therefore, the sample does not include rail services. Accordingly, based on the information contained in the National Accounts (2009), the GST Base in respect of rail services is estimated at Rs 44,746 crores.

5.48 The GST Base in respect of the **‘General sectors’** is computed on the basis of the Profit and Loss Account of the entities who filed their income tax returns electronically by following the steps indicated in Para 5.30. The GST Base for 2007-08 is estimated at Rs 24,29,924 crores.

5.49 The **‘GST Base’** for all the sectors is summarized in Table-5. As would be noted, the **‘GST Base’** for the **‘Taxable sectors’** is estimated at Rs 30,50,228 crores.

Report of the Task Force on Goods and Services Tax
Thirteenth Finance Commission

Table-5 : Estimation of the GST Base under the SI Method

Sl.No	Description	Unit	All Sectors	Exempt Sector	Taxable Sector				
					Special Sectors			General Sectors	Total
					Financial Services	Rail Services	Land Sector		
					1	2	3	4	5
	Sample Size	Nos.	2851248	77851	100055			2673342	2773397
A.	Output Tax Base								
	1 Net value of supply of domestically produced goods and services	Rs. In crs	8721874	112713				7762224	
	2 Value of Imports	Rs. In crs	1200678					1200678	
	3 Net value of domestically available goods and services (1+2)	Rs. In crs	9922552	112713				8962902	
	4 Value of Exports	Rs. In crs	989505					989505	
	5 Aggregate Output Tax Base (3-4)	Rs. In crs	8933047	112713				7973397	
B.	Input Tax Base								
	1 Value of purchase of Capital Goods	Rs. In crs	457504	9743				431504	
	2 Value of purchase of Intermediate Goods and Services	Rs. In crs	7329483	98091				6712418	
	3 Gross value of purchase of intermediate goods and services (1+2)	Rs. In crs	7786987	107835				7143921	
	4 Value of purchases from Unregistered dealers	Rs. In crs	1682145	81696				1600449	
	5 Aggregate Input Tax Base (3-4)	Rs. In crs	6104842	26138				5543473	
C.	GST Base (A5-B5)	Rs. In crs	2828205	86575	193103	20750	429260	2429924	3073037

2. Consumption Method

i. Task Force Estimate

5.50 In addition to the SI method, we also estimate the GST Base by estimating the total final consumption.

5.51 For this purpose, we use the Input Flow Matrix 2006-07 at factor cost⁴³ published by the National Accounts Division of the CSO. The Input Flow Matrix or contains details of 130 commodities consumed as input in 130 industries, covering the entire range of economic activities. Commodities are recorded in columns and industries are recorded in rows in a square matrix form. The value of each commodity consumed by each industry is at factor cost. It also provides commodity-wise detail of Total final use, that is, private final consumption expenditure (PFCE), government final consumption expenditure (GFCE), gross fixed capital formation (GFCF), change in stock (CIS), export and import.

5.52 To estimate the GST base, we need to estimate the contribution of all commodities in the primary, secondary and tertiary sectors of economy to the value addition chain. Since GST will be applicable only on the output of registered dealers with a turnover of more than Rs 10 lakh, consumption of goods and services from unregistered dealers will not be subject to GST. Therefore, it is necessary to estimate the value of such purchases forming part of the Private Final Consumption Expenditure (PFCE). For this purposes, we assume that the share of purchases from the unregistered dealers is in the same ratio as the share of the unorganised sector in the total National Domestic Product (NDP). The contribution of the organized and unorganized sectors in the NDP for 2006-07 is calculated on the basis of information available in statement 76.1 of National Accounts Statistics, 2009. The PFCE on goods and services from registered dealers (organized sector) for inclusion in the GST base is estimated at **Rs 10,12, 609 crores** (Table-6).

⁴³ This matrix is also referred to as 'The Absorption Matrix'

5.53 Government Final Consumption Expenditure (GFCE) comprises of two elements, namely, compensation to employees and Net purchase of Goods and Services. Since compensation to employees will be outside the scope of the GST base, we exclude public administration in the Input Flow Matrix from the GFCE to arrive at the Net purchases of goods and services by Government.

5.54 Gross Fixed Capital Formation (GFCF) comprises of two broad components i.e., construction and machinery equipments. The machinery equipments component is in the nature of capital goods which, under the GST, are proposed to be treated as intermediate inputs. Therefore, this element is not included as part of the GST base. Similarly, expenditure on construction by the Public Sector and the Private Corporate Sector is also proposed as intermediate input by allowing full and immediate input credit on capital goods. Therefore, for the purposes of this exercise what is relevant is the estimate of the Gross fixed Capital Formation in the household sector.

5.55 The expenditure on construction as reported in Statement 19 of National Accounts Statistics, 2009 is Rs. 5,00,036 crores comprising of Rs. 3,66,855 crores towards construction and Rs. 1,33,181 crores towards plant and machinery. The household sector in general would be in the un-organised sector (unregistered dealers or final consumers) and therefore, the expenditure on plant and machinery and construction by the household sector would be in the nature of final consumption. The expenditure on construction in the household sector would comprise of two components, namely, material and labour. In general, tax would be payable on the material component only since the labour component being from the un-organized or own labour will not be captured under the GST. Accordingly, we estimate the labour component as one-third of Rs. 3,66,855 crores i.e. Rs. 1,22,285 crores. Hence, the final consumption component in the Gross Fixed Capital Formation in the household sector in 2006-07 is estimated at Rs. 3,77,751 crores.

5.56 Some element of the food sector, and education and health services are proposed to be exempt from the GST. Similarly, services categorised under the labels 'Other Commercial,

Social, Personal Services', 'Others Services' and 'Public Administration' are also proposed to be excluded since these would essentially be rendered by entities with turnover below the threshold limit or by government or by the non-profit sector.

5.57 The estimate of the non-land GST Base for 2006-07 is obtained by aggregating the PFCE on goods and services from registered dealers (organized sector), the net purchases of goods and services by the Government and the component relating to final consumption in the Gross Fixed Capital Formation in the household sector.

5.58 In Table-6, the size of the non-land **GST Base for 2006-07** is estimated at **Rs 28,98,520 crores**, which accounts for 76.69 percent of the GDP at factor cost at current prices (Rs. 3779385 crores). Applying the same ratio, the size of the non-land **GST Base in 2007-08** is estimated to be **Rs 33,13,817 crores**. The GST Base relating to land for 2007-08 is estimated to be **Rs. 4,29,260 crores** as computed under the SI method. **Therefore, the aggregate GST Base in 2007-08 is estimated at Rs. 37,43,077 crores.** This estimate is significantly higher than the size of the GST base estimated under the SI method.

Table-6: Task Force Estimate of the GST Base using the Consumption Method			
Sl. No.	Description	Units	Amount
1	Aggregate Private Final Consumption Expenditure	Rs. in crs	2260042
2	Private Final Consumption Expenditure relating to purchases from unregistered dealers (unorganised sector)	Rs. in crs	1247433
3	Private Final Consumption Expenditure (Organized sector) (Row 1 - Row 2)	Rs. in crs	1012609
4	Government Final Consumption Expenditure on goods and services	Rs. in crs	421059
5	Gross Fixed Capital Formation in household sector (excluding labour)	Rs. in crs	377751
6	Intermediate inputs from unregistered dealers	Rs. in crs	1713887
7	Gross Total (Row 3 + Row 4 + Row 5 + Row 6)	Rs. in crs	3525306
8	Exemption for food, health , education and some services	Rs. in crs	626786
9	Estimated non-land GST Base in 2006-07 (Row 7 - Row 8)	Rs. in crs	2898520
10	GDP at factor cost in 2006-07	Rs. in crs	3779385
11	Non-land GST base as a proportion of GDP (Row 9 divided by Row 10)	in percent	76.69
12	GDP at factor cost in 2007-08	Rs. in crs	4320892
13	Estimated non-land GST Base in 2007-08 (Row 11 * Row 12)	Rs. in crs	3313817
14	GST base relating to land for 2007-08 /1	Rs. in crs	429260
15	Estimated GST Base in 2007-08 (Row 13 + Row 14)	Rs. in crs	3743077
/1 The GST base relating to land in 2006-07 is estimated at Rs.366855 crores.			

ii. NCAER Estimate

5.59 The Thirteenth Finance Commission had assigned a study to Dr. Rajesh Chadha of the NCAER to carry out a study on the implication of GST for international study. Using CGE Model, NCAER has, inter alia, also estimated the RNR for a comprehensive GST factoring the impact of

exemption for the food sector, education and health services. However, it **does not** factor the impact of-

- a. exemption for small businesses (i.e. the threshold exemption of Rs 10 lakh for GST registration by dealers); and
- b. inclusion of land transactions within the scope of the GST.

5.60 The RNR for non-petroleum taxes of Rs 1,76,893 crores for the base year 2003-04 has been estimated to be 7.22 percent⁴⁴. Implicit in this estimate is the estimate of the GST Base at Rs 2450042 crores for 2003-04.

5.61 We use the purchases from the unorganized sector as a proxy for the purchases from the unregistered dealers. The private final consumption expenditure (PFCE) at market prices in 2003-04 was Rs 1699485 crores. We first adjust for the embedded net indirect taxes by applying the ratio of GDP at factor cost at current prices to the GDP at market prices at current prices for the financial year 2003-04 to the PFCE to arrive at the PFCE at factor cost at current prices. Thereafter, we estimate the purchases from the unorganised sector at Rs 894152 crores by applying the share of the unorganised sector in the net domestic product in the year 2007-08.

5.62 In 2007-08, the Gross Fixed Capital Formation by way of construction in the household sector is Rs 429260 crores. This does not include the value of land. Assuming that the land value accounts for 50 percent of the total value of the real estate, the GST base relating to land is estimated at Rs 429260 crores.

⁴⁴ NCAER has estimated the RNR for non-petroleum taxes at 6.20 percent under the **first scenario** that there will be no threshold exemption for registration and no specific goods and services based exemption. This scenario is not relevant for us since we intend to provide a threshold exemption and exemption for some specific goods and services. Under the **second scenario** of no threshold exemption but exemption of the same goods and services which we have recommended, the RNR is estimated to be 7.22 percent for non-petroleum taxes. Similarly, **the third and fourth scenarios** envisage that the GST will subsume all taxes including petroleum taxes and the scope of commodity specific exemptions will expand to larger baskets. The estimates of RNR under the third and fourth scenarios are 9.01 and 9.4 percent, respectively. However, the two latter scenarios are irrelevant for our purposes since we do not intend to subsume petroleum taxes within the scope of GST.

Table-7: NCAER Estimate of the GST Base			
Sl. No.	Description	Units	Amount
1	Estimated GST Base(excluding land and the threshold exemption) in 2003-04	Rs. in crs	2450042
2	Impact of the threshold exemption (purchases from the unorganised sector)	Rs. in crs	894152
3	Non-land GST Base in 2003-04 adjusted for threshold exemption (Row 1 - Row 2)	Rs. in crs	1555890
4	GDP at factor cost in 2003-04	Rs. in crs	2538170
5	Estimated non-land GST Base in 2003-04 (Row 3 divided by Row 4)	in percent	61.30
6	GDP at factor cost in 2007-08	Rs. in crs	4320892
7	Estimated non-land GST Base in 2007-08 (Row 5 * Row 6)	Rs. in crs	2648692
8	GST base relating to land for 2007-08 /1	Rs.in crs	429260
9	Estimated GST Base in 2007-08 (Row 7 + Row 8)	Rs. in crs	3077952
/1 The GST base relating to land in 2003-04 is estimated at Rs.197305 crores.			

5.63 After adjusting the NCAER estimates to reflect the design and structure of the GST recommended by us, the GST Base in 2007-08 is estimated at Rs 30,77,952 crores as per calculations indicated in Table-7. This estimate of the GST Base also approximates the estimate under the SI method.

3. Shome Index Method

5.64 Parthasarathi Shome, one of our leading fiscal economists, has written extensively on tax policy and revenue trends. Among his observations is one that pertains to the revenue productivity of the VAT. The relationship between VAT rate and its revenue implication in terms of GDP could be referred to as the Shome Index as has sometimes been reflected in the context of Latin America. Thus, if the general rate of the VAT is, say 10 percent, the revenue collection from the VAT can be expected to be 5 percent of GDP⁴⁵. This revenue achievement is possible if-

⁴⁵ This is calculated by the formula $(1/2) \times 10 \text{ percent} = 5 \text{ percent of GDP}$

- i. the VAT base is broad with few exemptions;
- ii. the general VAT rate is not impeded by other lower rates;
- iii. tax administration is transparent; and
- iv. social norms do not erode tax compliance.

5.65 This has been observed in Chile whose VAT bases were proverbially wide. With an 18% VAT rate, Chile's VAT revenue was almost 9% of GDP. Chile taxed even unprocessed food and fresh vegetables.

5.66 If the VAT base is narrow as is the case in the U.K., then the Shome Index would reveal a small percent collection in terms of GDP. Thus, in the U.K., with a VAT rate of 17.5%, the revenue intake has hovered around 6%. In terms of the Shome Index, at a VAT rate of 'X' percent, the VAT revenue in terms of GDP is nearly as low as $(1/3^{\text{rd}} * 'X')$ percent. In other countries, say with some other characteristic such as low compliance, a similar outcome would be experienced.

5.67 In most countries, as a thumb rule, VAT revenue hovers between $(1/3^{\text{rd}} * 'X')$ percent and $(1/2 * 'X')$ percent of GDP. The strategy for countries that have an x% VAT rate should invariably be to design the VAT structure and enhance its administration in a way that the achievement of $(1/2 * 'X')$ percent of GDP in revenue is feasible.

5.68 However, this Index is valid generally for countries which do not include real estate and housing services and financial services within the scope of VAT.

5.69 Based on the Shome Index, the GST Base is estimated in Table-8 at **Rs 27,82,809 crores**.

Table-8: Estimating the GST Base on the basis of the Shome Index

SI No.	Description	Amount [Rs in crs]
1	GDP at factor Cost at current prices	43,20,892
2	Estimated base on the basis of Shome Index [50 percent of row 1]	21,60,446

3	Estimated base relating to Financial Services	1,93,103
4	Estimated base relating to Real Estate	4,29,260
5	GST Base [Row 2+Row 3+ Row 4]	27,82,809

5.70 This estimation of the base is lower than the base estimated under the SI method primarily due to the fact that the estimates of GDP per se appears to be under reported since the value of output reported in the sample is substantially higher than the value of output as estimated from the National Accounts Statistics prepared by CSO for comparable sectors.

4. Revenue Method

5.71 A common method used by the revenue authorities both at the centre and state levels is to estimate the implicit GST base in the revenues actually collected and make such adjustments as are necessary to reflect the increase or decrease in the base on the basis of the recommended design and structure of the GST.

5.72 As would be seen, the output tax base is computed by estimating the implicit base underlying the aggregate of (i) the amount of collection by way of countervailing duty and Union excise duties for non-POL goods; and (ii) the estimated revenue foregone as reported in the Receipts Budget of the Union Government). This implicit base is calculated at the aggregate Union Excise Duty rate of 16.48 percent (inclusive of 3 percent of education cess). Similarly, the input tax base is computed by estimating the implicit base underlying the CENVAT credit allowed to producers at the same duty rate. The difference between the output tax base and the input tax base so calculated is the GST base relating to goods which is estimated at **Rs 11,77,706 crores** in 2007-08 (Table-9). Similarly the service tax base is estimated at **Rs 4,13,697 crores** for 2007-08 as shown in the said Table.

5.73 Since the proposed GST is comprehensive in its base, it will extend to a much larger base particularly in the financial services, rail transport, land, petroleum, tobacco and alcohol, trade and construction sectors. The estimated increase in the tax base in respect of each of these sectors is indicated separately in Table. The aggregate of the increase is estimated at Rs. 13, 58,344 crores for 2007-08 as shown in the said Table.

Table- 9 :Estimation of GST Base: Revenue Method				
A	Non-POL (Existing Base)	Units	Amount	
	Countervailing Duty	(Rs. In crs)	53510	
	Public Ledger Account (paid to Govt)	(Rs. In crs)	53108	
	Revenue foregone	(Rs. In crs)	87468	
	Cenvat	(Rs. In crs)	147447	
	Output Tax	(Rs. In crs)	341533	
	Output tax Base	(Rs. In crs)	2072409	
	Input Tax Base	(Rs. In crs)	894703	
	Existing GST Base (Goods)	(Rs. In crs)	1177706	
B	Services (Existing Base)	(Rs. In crs)	413697	
C	Additional Base			
	Financial Services	(Rs. In crs)	66835	
	Rail	(Rs. In crs)	20750	
	Land	(Rs. In crs)	429260	
	Trade	(Rs. In crs)	518102	
	Petroleum, Power and Tobacco	(Rs. In crs)	191513	
	Construction	(Rs. In crs)	131884	
	Sub-total	(Rs. In crs)	1358344	
D	GST Base	(Rs. In crs)	2949748	

5.74 Based on the above, the aggregate GST Base for 2007-08 is estimated at **Rs 29,49,748 crores** as shown in Table-9. As would be noted this estimate is larger than the estimate under the Shome Index Method but lower than the estimate under the SI method.

5.75 The various estimates of the GST Base for 2007-08 are summarized in Table-10. As may be noted, the Task Force estimate of the GST Base using the Consumption method is the highest (Rs.37,43,077 crores) whereas the Shome Index method provides the lowest estimate. All other estimates fall within this range. Since the five estimates are different, we adopt their average of Rs 31,25,325 crores⁴⁶ (row E of Table-10), as the size of the comprehensive GST base for 2007-08 for the purposes of estimating the RNR. Since the tax base for both the CGST and the SGST are proposed to be identical, we use the same tax base for calculating the RNR for both levies.

Table-10: Estimation of GST Base and the RNR			
Sl No	Description	Units	Amount
A	Subtraction-Indirect Method	(Rs in crs)	3073037
B	Consumption Method		
	i. Task Force Estimate	(Rs in crs)	3743077
	ii Chadha Estimate	(Rs in crs)	3077952
C	Shome Index Method	(Rs in crs)	2782809
D	Revenue Method	(Rs in crs)	2949748
E	Average of all estimated GST Base	(Rs in crs)	3125325
F	Centre's RNR	(in percent)	5.05
G	State's RNR	(in percent)	6.02

⁴⁶ The standard deviation of these estimates is calculated to be Rs 640977 crores.

c. The Revenue Neutral Rate(RNR)

5.76 Given the estimate of the GST Base and the level of central taxes which are intended to be subsumed in the GST, we estimate the RNR for the CGST at 5.0 percent. Similarly, the RNR in respect of the state level TF-taxes which are proposed to be subsumed in the SGST is estimated to be 6.0 percent. **Therefore, the combined RNR is estimated to be 11 percent.** Incidentally, this estimate is the same as estimated by Bagchi and Poddar in their pioneering study published in November, 2007⁴⁷.

5.77 These estimates do not factor in the revenue gains from increased compliance and GDP. To the extent, the flawless GST will reduce cascading effect, there will be significant increase in the corporate profits and hence corporate tax collections. Therefore, in actual practice, the RNR of 11 percent will be revenue positive.

5.78 As would be noted, we have, in para 2.11, recommended the abolition of all entry and Octroi taxes by state governments and other sub-national Governments. Therefore, it is imperative to provide for an alternate buoyant source of revenue to the third-tier of Government.

5.79 In view of the aforesaid, we recommend the following:-

- i. The rate of CGST and SGST on all non-SIN goods should be fixed at the **single rate of 5 percent and 7 percent, respectively;**
- ii. A formula-based devolution of an amount equivalent to collection of SGST at 2 percentage points should be made to the third-tier of Government after an appropriate Constitutional Amendment;
- iii. The formula should be based on the recommendations of the State Finance Commission.

⁴⁷ Poddar, Satya and Amaresh Bagchi (Nov 2007), "Revenue-neutral rate for GST", The Economic Times, 15th November, 2007, Delhi

- iv. Pending Constitutional Amendment, the collection from 7 percent SGST shall accrue to the State Government and devolution to the third-tier Government should continue to be made on the basis of the recommendations of the State Finance Commission.
- v. Both the Central and the State Governments may continue to levy taxes, in addition to the CGST and SGST, on the various non-SIN goods as at present.

Chapter - VI

Revenue Performance of GST

6.1 As is well-known, VAT is, potentially, a broad-based tax levied on all commodity sales with a view to, ultimately, taxing the whole of final consumption. VAT is not a progressive but a proportional tax. It was never designed to meet social or redistributive objectives. In theory, the tax is, therefore, most “efficient” when imposed on all goods and services at a single standard rate. The efficiency of the VAT system can be optimized depending on the ability of tax administration to collect the tax due effectively. In this respect, a single rate and a simpler tax system is easier for tax administrations to administer and for businesses to comply. In this perspective, a VAT system is, in absolute terms, “efficient” when it covers the whole of the potential tax base (consumption by end users) at a single rate and where all the tax due is collected by the tax administration. Therefore, the ratio of the revenues actually collected and the revenues that would arise from a theoretically “pure” VAT system with a single rate applied to all final consumption and 100 per cent compliance would be a good measure to evaluate the performance of VAT. In literature, this ratio is referred to as the VAT Revenue Ratio (VRR). This ratio gives an indication of the efficiency of the VAT regime in a country compared to a standard norm.

6.2 In theory, the closer the VAT system of a country is to the “pure” VAT regime, the more its VRR is close to 1. Any other value – higher or lower – indicates deviation from a single tax rate applied on all final consumption or a failure to collect all tax due. A VRR close to 1 is taken as an indicator of a VAT bearing uniformly on a broad base with effective tax collection. On the other hand, a low VRR may indicate an erosion of the tax base at the standard rate. This can result from exemptions, reduced rates, registration thresholds for small traders, poor compliance or poor tax administration or a combination of these.

6.3 The VRR is characterised by a number of deficiencies. The estimation of the potential VAT tax base (i.e. consumption by end users or national consumption) is difficult to assess with precision. In general, the figures of national consumption used to calculate the VRR are taken from the national accounts⁴⁸, but “consumption” within the meaning of national accounts does not exactly match the potential VAT tax base. For example, several investment goods (such as new buildings) are not considered as consumption in national accounts (where they are treated as “investments” or “gross fixed capital formation”) but they are subject to VAT in many countries. A combination of this factor together with the cascading effects of exemption in the value chain may lead to a VRR above one. Therefore, for the purposes of calculation of VRR in respect of the proposed ‘flawless’ GST, we compute the potential tax base by expanding the scope of final consumption within the meaning of National Accounts to include also the Gross fixed capital formation (including transaction (“consumption”) in land) in the household sector. Accordingly, the ‘**potential tax base**’ of a GST is estimated at Rs 39,49,907 crores as indicated in Table-11. However, the ‘**actual tax base**’ under the ‘flawless’ GST is estimated at a reduced amount of Rs 31, 25,325 crores. **Accordingly, VRR of the ‘flawless’ GST is calculated to be 0.79.**

6.4 The VRR is affected by both policy decisions – over the base and the number of rates – and compliance levels. The VRR is actually the product of a “**Policy efficiency ratio**” (comparing the theoretical revenue from actual VAT law and revenue from a pure VAT system) and a “**Compliance efficiency ratio**” (comparing actual VAT revenues with theoretical revenue from actual tax law). Therefore, mathematically expressed,-

$$\text{VRR} = \frac{\text{Weighted average of statutory rates}}{\text{Standard rate}} * (1 - \text{Exemptions}) * (\text{Compliance level})$$

The product of the two terms $\left[\frac{\text{Weighted average of statutory rates}}{\text{Standard rate}} * (1 - \text{Exemptions}) \right]$ denotes the “**Policy efficiency ratio**” and the term $(\text{Compliance level})$ denotes the “**Compliance efficiency ratio**”.

⁴⁸ There is currently no internationally agreed method to assess a VAT theoretical base.

6.5 Our recommendation is for a single rate for both CGST and SGST and zero rate is applicable only for international exports. Therefore, the weighted average of statutory rates is equal to the single rate (standard rate) and accordingly, the ratio $\frac{\text{Weighted average of statutory rates}}{\text{Standard rate}}$ is equal to 1 (one).

Table-11 : Computation of VAT Revenue Ratio (VRR) under the 'Flawless' GST*			
Sl. No	Description	Unit	Amount
A	Private Final Consumption Expenditure	Rs in crs	2605859
B	Government Final Consumption Expenditure	Rs in crs	479099
C	Gross Fixed Capital Formation(Household Sector)	Rs in crs	435689
D	Gross Fixed Capital Formation(Land)	Rs in crs	429260
E	Potential GST Base (A+B+C+D)	Rs in crs	3949907
F	Actual Tax Base	Rs in crs	3125325
G	VAT Revenue Ratio (F divided by E)	Nos	0.79
H	Standard Rate	in percent	12.00
I	Weighted Average of Statutory rates	in percent	12.00
J	Weighted average of Statutory rates as a ratio of Standard rate	Nos	1.00
K	Amount of Exemption**	Rs in crs	206830
L	Impact of exemption [K divided by (F+K)]	Nos	0.062
M	Policy Efficiency Ratio	Nos	0.938
N	Compliance Efficiency Ratio	Nos	0.84

* The estimates should be taken as approximates.
 **The exemptions relate only to exemptions for unprocessed food articles, health services and education services. This does not include the impact of threshold exemption

6.6 Similarly, the 'flawless' GST recommended by us envisages very limited number of exemptions. These are essentially restricted to food, education and health services, the threshold exemption for registration of small dealers and public administration. As regards the

threshold exemption for registration of small dealers, it has both a positive and a negative impact on revenues. To the extent sales by unregistered dealers is exempt, there is a revenue loss. However, part of the revenue loss is recouped since purchases from unregistered dealers are not eligible for input tax credit. Similarly, a large part of the food items is distributed by small dealers and therefore there is significant overlap in the revenue effect of the threshold exemption and the food sector. The same also holds well in the health and education sector. The net impact of the exemptions under the 'flawless' GST on the tax base is estimated to be Rs 206830 crores only. This accounts for **6.2 percent** erosion in the potential tax base. Hence, the ratio ($1 - \text{Exemptions}$) is calculated to be 0.938. Consequently, the '**Policy Efficiency Ratio**' is estimated to be **0.938**.

6.7 We do not have any method of making a direct estimate of compliance. However, compliance level is the ratio of the VRR to the 'Policy Efficiency Ratio'. Therefore, the implicit **compliance level is estimated to be 0.84**.

6.8 It has been pointed out by some that given the cross-country estimates of the VRR, our estimate of VRR is extremely high. It is argued that if the VRR is aligned to the international norm, the revenue neutral rate (RNR) would be substantially higher than the 11 percent estimated by us. In this context it would be useful to point out that given the deficiencies in the VRR as a measure of the revenue performance of VAT, it is difficult to draw typical profiles for "efficient" and "inefficient" countries in the collection of VAT revenues on the basis of this VRR. Since the VRR depends upon a number of factors, there is considerable variation in the VAT Revenue Ratio across countries. Therefore, it is best to use VRR as a tool to measure a single country's performance over a number of years rather than as a tool for comparison across countries. Nevertheless, 5 countries (i.e. Korea, Japan, Switzerland, Luxemburg and New Zealand) from amongst 29 OECD countries indeed have a VRR exceeding 0.7; another 17 countries have a VRR ranging between 0.5 and 0.7 and the balance 7 countries have a VRR of less than 0.5. Therefore, our estimate of VRR (and also the RNR) cannot be considered as an

outlier. The reason underlying such high VRR is the minimization of the exemptions and the elimination of the multiple rates.

6.9 The existing VRR in the case of Central Government levy on goods and services is extremely low. The current base is estimated to be as low as 0.36⁴⁹. Further, the factor $\frac{\text{Weighted average of statutory rates}}{\text{Standard rate}}$ is also estimated to be 0.75⁵⁰. Therefore, the 'Policy efficiency ratio' is estimated to be a low of 0.27⁵¹. We have no estimate of the compliance level but we have anecdotal information that there is substantial evasion. If we assume that the compliance is 0.84, the VRR for central taxes on goods and services is estimated to be 0.23⁵².

6.10 Given this estimate of an extremely low VRR, it is not surprising that the estimate of the GST Base by both Central Government and State Governments on the basis of the existing revenues is extremely low. As is well known, the existing tax structure is riddled with a plethora of incentives and multiple rates. Therefore, the 'Policy efficiency ratio' is extremely low. Once these policy deficiencies are removed the VRR would automatically increase to a substantially higher level of 0.76. The purpose of introducing the flawless GST is precisely to achieve this policy objective. Our calculation of the VRR of the 'flawless' GST is based on the existing level of compliance and not on the basis of any increase in the compliance level. Hence, any apprehension that given the existing compliance level, the high level of VRR cannot be achieved is totally misplaced. The VRR under the 'flawless' GST can be achieved by eliminating the policy deficiencies under the existing regime for taxation of goods and services. **What is required is a strong political consensus to do so.**

⁴⁹ The value of exemptions (excluding threshold exemption) from Table-9 is estimated to be Rs 18,89,096 crores (Rs 1358344 crores plus Rs 530752 crores) and the estimated potential base is Rs 29,49,748 crores. Therefore, the share of exemptions in the potential base is estimated to be 0.64. Hence, the share of the actual base is 0.36.

⁵⁰ The standard rate is 16.48 percent and the weighted average of statutory rates is estimated to be 12.28 percent. Therefore, the ratio of weighted average of statutory rates to standard rate is 0.75.

⁵¹ This is the product of 0.36 and 0.75.

⁵² This is the product of the 'Policy Efficiency Ratio' (0.27) and the 'Compliance Efficiency Ratio' (0.84).

CHAPTER - VII

Implications of the Goods and Services Tax

7.1 The economic case for a ‘flawless’ GST is straightforward: Income is taxed irrespective of source and use; therefore, consumption should also be taxed on the same principle. This is the feasible second-best solution, compared to the unattainable first best distortion-free world of lump sum taxation. The ‘flawless’ GST is rooted in this breathtakingly simple analytical proposition. In the Indian economic policy context, poverty reduction and inclusive growth are key policy objectives and will, undoubtedly, continue for some time. What, then, are the implications of the **switchover** from the cascading and distortionary taxation of goods and services to the the ‘flawless’ GST for, amongst others, economic growth, equity and poverty?

a. GST and economic growth

7.2 High import tariffs, excises and turnover tax on domestic goods and services have enormous cascading effects, leading to a distorted structure of production, consumption and exports. The existing tax system introduces myriad distortions which favour some goods and services at the expense of others. These distortions yield inefficient resource allocation and consequently, inferior GDP growth. In India, the motivation underlying the hugely differentiated scheme of indirect taxation of production and sales that has evolved over the country’s history was progressive and noble; the actual impact of such a structure is now widely acknowledged to be regressive, capricious, and sub optimal in terms of the efficiency of tax effort, leaving the door open for lobbyists and special pleading. The problem of the present distortionary indirect tax system can be effectively addressed by shifting the tax burden from production and trade to final consumption. The ‘flawless’ GST, which subsumes all indirect taxes on goods and services, is the most elegant method of taxing consumption. Under this structure, all different stages of production and distribution can be interpreted as a mere tax pass-through, and the tax essentially ‘sticks’ on final consumption within the taxing jurisdiction.

7.3 The introduction of the GST will also bring about a macroeconomic dividend by reducing what have been called the “negative grey area dynamic effects” of cascading taxation. As a result it reduces the overall incidence of indirect taxation by removing the many distortionary features of the present indirect tax system. There are seven important macroeconomic channels through which the ‘flawless’ GST minimises the distortions. **First**, the failure to tax all goods and services distorts consumption decisions; it weakens the signalling power of relative prices. GST will reduce these distortions and enable all economic agents to respond more effectively to price signals. This will improve the allocative efficiency of the tax system. **Second**, the failure to exempt all sales to business distorts decisions regarding choice of production methods, particularly decisions on vertical and horizontal integration and what inputs to produce or sell. Since the GST will be a tax on consumption, all stages of production and distribution will be mere pass-through. Therefore, there will be no tax incentive for vertical and horizontal integration. **Third**, the taxation of capital goods discourages savings and investment and retards productivity growth. The ‘flawless’ GST envisages full and immediate credit for GST on capital goods (both buildings and plant and machinery), thereby fully eliminating the incidence of any indirect tax on the capital goods. This enhances the productivity of capital and hence reduces the incremental capital-output ratio (ICOR). This is perhaps the most important gain through the introduction of the GST in India. **Fourth**, for a given constellation of exchange rates and price levels, violation of the destination principle places local producers at a competitive disadvantage, relative to producers in other jurisdictions. The GST envisages comprehensive taxation of imports on consideration of consumption in India and irrespective of whether the imported goods and services are produced in India or not, thereby, providing a level playing field to domestic producers particularly in the import-substitution industry. **Fifth**, differences in the tax structure of different States and the Central Government greatly increase the cost of doing business⁵³. The proposed GST, though dual in nature, envisages a uniform structure, design and compliance system at all levels of Government and across States.

⁵³ This is a league table in which we have long languished at the bottom.

Therefore, the cost of doing business in India will significantly reduce. The GST based tax reform provides a real policy opportunity to deal with this problem without waiting for prior and sweeping political economy changes. **Sixth**, GST, once introduced, will create a common market across the length and breadth of the country- something which has eluded us since long. The size of the market will cease to be limited by tax considerations. Further, it will restore the comparative advantage of resource rich states and enable them to emerge as production hubs. **Seventh**, at present, the combined statutory rate of VAT is close to 22 per cent⁵⁴. Further, this marginal rate is applied to a very narrow base on account of a plethora of exemptions. Since economic decisions and compliance behaviour are based on the marginal rate, the higher the rate the greater the distortion and evasion. This is further compounded by distortion in resource allocation on account of a plethora of exemptions. Since we have recommended a substantially lower, uniform, and combined single rate of 12 percent⁵⁵ on all goods and services, the economic distortion and the incentive to evade will be considerably reduced. We can also expect an upsurge in compliance and hence, revenue collections. This in turn will improve fiscal management and reduce the 'crowding-out' effect.

7.4 The overall macroeconomic effect of reduction in economic distortions due to GST would be to provide an impetus to economic growth. Using CGE Model, the NCAER study commissioned by the Thirteenth Finance Commission estimates the impact of the introduction of a GST which would eliminate all taxes on production and distribution and rest on final consumption only. The study is based on two important assumptions of full employment and that 50 percent of indirect taxes remain embedded and 'stick' on production and distribution. The study concludes that 'implementation of a comprehensive GST in India will lead to efficient allocation of factors of production thus leading to gain in GDP and exports. This would translate into enhanced economic welfare and returns to the factors of production, i.e. land, labour and capital. The gains in real returns to land range between 0.42 and 0.82 per cent. Wage rate gains

⁵⁴ Prior to the tax cut in December 2008 as part of the economic stimulus, the combined rate was 28 per cent approximately.

⁵⁵ However, there will be a special rate of 1 percent on high value items like gold and platinum and zero rate on exports.

vary between 0.68 and 1.33 per cent. The real returns to capital would gain in the range of 0.37 and 0.74 percent.’.

7.5 Further, the study also shows that ‘implementation of GST across goods and services is expected, *ceteris paribus*, to provide gains to India’s GDP somewhere within a range of 0.9 to 1.7 per cent. The corresponding change in absolute values of GDP over 2008-09 is expected to be between Rs. 42,789 crore and Rs. 83,899 crore, respectively.

7.6 These additional gains in GDP, originating from the GST reform, would be earned during all years in future over and above the growth in GDP which would have been achieved otherwise. The present value of the GST-reform induced gains in GDP may be computed as the present value of additional income stream based on some discount rate. We assume a discount rate as the long-term real rate of interest at about 3 per cent. The present value of total gain in GDP has been computed as between Rs. 1,469 thousand crores and 2,881 thousand crores. The corresponding dollar values are \$325 billion and \$637 billion or as much as one-third to one-half of the country’s GDP for the year 2009-10.

7.7 The manufacturing sectors would benefit from economies of scale. Output of sectors including textiles and readymade garments; minerals other than coal, petroleum, gas and iron ore; organic heavy chemicals; industrial machinery for food and textiles; beverages; and miscellaneous manufacturing is expected to increase. The sectors in which output is expected to decline include natural gas and crude petroleum; iron ore; coal tar products; and nonferrous metal industries.”. The results of the NCAER Study are also suggested of the GSTs positive environmental impact on the economy.

7.8 Further, the changeover to GST will be neutral to vertical and horizontal integration. This will therefore, encourage industries to be located in states which enjoy a comparative advantage. This has far reaching implication for resource rich backward states; it will serve as an attraction to natural resources based industries to locate in these states regardless of the

fact that the consumer is located elsewhere. Another dynamic implication of the GST would be to generate greater employment as GST helps to increase labour intensive sectors.

b. GST and International Trade

7.9 There are also benefits to foreign trade that can be reasonably expected. At present export of taxes to other countries is sought to be eliminated through the mechanism of duty draw back on the basis of estimated incidence of embedded taxes. This scheme is far from satisfactory.

7.10 Destination based taxation is a fundamental principle of a sound GST. It requires that exports from the taxing jurisdiction would be tax free by zero rating and imports into the jurisdiction would be taxed at the same rate as products produced and consumed within the jurisdiction. The 'flawless' GST embodies this principle. Consequently, both export-oriented industries and import-substituting industries would become internationally more competitive. As a result, while exports can be expected to register an increase, imports are likely to decrease. These outcomes are supported by the NCAER study.

7.11 Gains in exports are expected to vary between 3.2 and 6.3 per cent with corresponding absolute value range as Rs. 24,669 crore and Rs. 48,661 crore. Imports are expected to gain somewhere between 2.4 and 4.7 per cent with corresponding absolute values ranging between Rs. 31,173 crore and Rs. 61,501 crore.

7.12 The sectors with relatively high proportional increase in exports include textiles and readymade garments; beverages; industrial machinery for food and textiles; transport equipment other than railway equipment; electrical and electronic machinery; and chemical products: organic and inorganic. The moderate gainers are agricultural machinery; metal products; other machinery; and railway transport equipment. Exports are expected to decline in agricultural sectors; iron and steel; wood and wood products except furniture; and cement. There are minor gains and losses in exports of other sectors.

7.13 The major import gaining sectors include leather and leather products; furniture and fixtures; agricultural sectors; coal and lignite; agricultural machinery; industrial machinery; other machinery; iron and steel; railway transport equipment; printing and publishing; and tobacco products. The moderate gainers include metal products; non-ferrous metals; and transport equipment other than railways. Imports are expected to decline in textiles and readymade garments; minerals other than coal, crude petroleum, gas and iron ore; and beverages.

7.14 In general, our imports are sourced from countries which effectively zero rate their exports. Further, India has also entered into a large number of free trade agreements under which it will, in general, not be possible for India to use customs duty as a means to providing protection/level playing field. Therefore, it is necessary to ensure that the imports into the country are subject to the same level of taxation as domestically produced goods. The ‘flawless’ GST will ensure this by subjecting the imports to both CGST and SGST. This will provide a level playing field to the domestic industry and, in particular, the manufacturing sector vis-a-vis imports.

c. GST: Equity and Poverty reduction

7.15 Poverty reduction will continue to remain the central objective of economic policy making in India. Any policy for poverty reduction must enable the provision of, at least, food, clothing, shelter, education and health.

7.16 At present, primary food articles like rice and wheat are liable to tax by many states either by way of purchase tax or sales tax at a lower rate. As a result, the incidence of tax on primary food articles comprises of two elements: tax on inputs and tax on the output (primary food articles). However, under the ‘flawless’ GST, all food items covered under the public distribution system are proposed to be exempt from GST. As a result primary food articles like rice and wheat would be exempt from GST (i.e. there will be no output tax). Hence, the tax incidence on such items of mass consumption will be limited to tax on inputs. Since expenditure

on food constitutes a large proportion of the total consumption expenditure of the poor, the GST is designed as a pro-poor policy initiative. In any case, the poor will continue to have accessibility to these items at subsidised prices through the public distribution system. Therefore, the poor will not suffer any additional burden on their consumption of food items due to the implementation of GST.

7.17 Like food, basic health and education services are also intended to be fully exempt. As a result consumption of these services will bear a relatively lower burden. Since these services are necessary to meet the basic human needs, the tax exemption for these services will enable the poor to have cheaper accessibility. In any case, as at present, these services will continue to be exempt from tax and therefore no additional burden will arise on account of the switchover to GST.

7.18 Housing is yet another important item of basic needs of the poor. The GST provides for including within its scope the transactions in real estate. Therefore, for a registered real estate builder, all taxes on inputs (including on land) will be off-set against the tax payable on the constructed property.⁵⁶ This will effectively reduce cost of housing to the extent of embedded taxes and hence, benefit the poor.

7.19 Another necessary item of consumption by the poor is clothing. The NCAER study shows that the implementation of the GST will result in a sharp decline in the prices of cotton textiles (by 6.44 percent), wool, silk & synthetic fibre textiles (by 11.4 percent), and textile products including wearing apparel (by 17.45 percent). To the extent, the share of expenditure on clothing in the total expenditure on consumption is relatively higher than in the case of the rich, the poor will gain relatively more from large drop in prices.

7.20 The rural poor comprise essentially of small and marginal farmers and landless labourers. Similarly, the urban poor comprises of the unemployed. The implementation of GST

⁵⁶ At present, the value of a constructed property includes stamp duty on land and other indirect taxes on inputs. Hence, these taxes form part of the cost of the property. On registration of the constructed property, stamp duty is payable on the entire cost including the embedded taxes. There is no mechanism for complete off-set of these taxes. This results in an increase in the overall cost of the property

will witness an increase in the real returns to land, labour and capital (as shown in the NCAER study). Therefore, the rural poor will also enjoy an increase in their income. Similarly, on account of increase in economic activity resulting in higher growth, there will be new opportunities for employment which will directly benefit the urban poor.

7.21 Further, in terms of the theory of optimal taxation, tax rates should **not** be uniform. They should, rather vary inversely with the elasticity of demand for particular goods and services, and tax rates should be higher on products that are complementary with leisure that cannot be taxed directly. (as opposed to work which generates income that can be taxed). This holds well in a world where it is possible to implement optimal tax reforms without any residual distortions caused by successful attempts at incidence shifting. However, in practice, shifting of tax incidence is well documented. Further, the representative consumer assumption that operates an optimal tax model is not just invalid, but actively dangerous in a policy context where poverty reduction and inclusive growth are key policy objectives. For instance, if, as intuition would lead us to expect, the demand for the basket of goods consumed by the poor is less elastic than that consumed by the rich, then the regressive policy implications of implementing optimal tax reform would be horrific i.e impose a higher tax on goods of consumption by the poor. Hence, the principle remains valid that all consumption should be taxed uniformly without regard to source and use. Even in this context, the GST reform is potentially far pro poor than theoretically elegant competing alternatives.

7.22 The benefit to the poor from the implementation of GST will therefore, flow from two sources: first through increase in the income levels and second through reduction in prices of goods consumed by them. The proposed switchover to the 'flawless' GST should, therefore, be viewed as pro-poor and not regressive. Hence, the switchover will improve the vertical equity of the indirect tax system.

7.23 The switchover to GST also entails the taxation of all goods and services in the formal sector. To the extent purchases are made from the informal sector by producers in the formal sector, no input tax credit would be available. Consequently, the value addition in the informal

sector on such inputs would be recaptured when used in the formal sector. Similarly, to the extent purchases are made from the formal sector by the informal sector, they will be GST borne and since no output tax will be payable in the informal sector, the tax will stick on the producer. Therefore, comprehensive consumption type destination based GST will also result in a higher tax burden on the informal economy than the present level. Hence, the switch over to the 'flawless' GST will also improve horizontal equity.

d. GST and Prices

7.24 Prices of agricultural commodities and services are expected to rise. Most of the manufactured goods would be available at relatively low prices especially textiles and readymade garments.

7.25 There are two opposing forces which determine the changes in price levels. First, increased payments to the primary factors of production, viz. land, labour and capital, increase the cost of production and hence tend to have upward pull on prices. Second, sectors under imperfect competition (manufacturing sectors) get benefits of cost reduction through increasing returns to scale which are not reaped by sectors assumed to be in perfect competition. The relative impact of the force determines the overall price change. It may also be noted that the share of primary inputs (land, labour and capital) in total output is relatively high in agricultural and services sectors.

7.26 Another factor that impacts the price levels refers to the quantum of intermediate input purchases from sectors under perfect competition versus imperfect competition. Relatively low proportions of intermediate inputs purchased by agriculture and service sectors (i.e. sectors under perfect competition) are sourced from manufacturing sectors and hence these sectors do not reap the benefit of relatively low cost inputs from manufacturing sectors.

7.27 Further, the terms of trade can also be expected to improve in favour of agriculture vis-a-vis manufactured goods. The prices of agricultural goods would increase between 0.61 and 1.18 percent whereas the overall prices of all manufacturing sector would decline between 1.22

and 2.53 percent. Consequently, the terms of trade will move in favour of agriculture between 1.9 to 3.8 percent.

7.28 The increase in agricultural prices would benefit millions of farmers in India. Similarly, the urban poor will also benefit from new employment opportunities. With regard to the food crops the poor would continue to remain secured through the public distribution system. The prices of many other consumer goods are expected to decline. These include sugar; beverages; cotton textiles; wool, silk and synthetic fibre textiles; and textile products and wearing apparel.

e. GST and informal sector

7.29 Another challenge to the consensus on GST based indirect tax reform in developing countries like India has been the argument that given the existence of an informal sector, a comprehensive GST can be welfare reducing, when revenue neutral. The argument rests on the premise that when the choice of a commodity set for VAT increase is restricted by the existence of a large informal sector, then there are negative welfare effects in transition to a revenue neutral VAT. If this holds true then there are serious policy implications if such negative welfare incidence impacts the consumption basket of the poor. However this argument rests on the foundation that the relative size of the formal and informal economies is exogenous to the tax structure in place. In India, the implementation of VAT is in fact expected to reduce the size of the informal economy relative to the formal economy by moving producers who choose to remain in the informal sector for *tax avoidance* reasons, incentivized by the size biased nature of indirect tax exemptions in the historic regime of taxation of domestic goods and services. When this is taken into account the welfare effects of GST can, in fact, be expected to be positive.

7.30 This highlights the fact that a GST based reform of the present indirect tax system can be expected to have significant positive welfare effects even while maintaining revenue neutrality.

f. GST and Fiscal management

7.31 The changeover to GST is designed to be revenue neutral at existing levels of compliance. Given the design of the 'flawless' GST, the producers and distributors will only be pass through for the GST. Further, given the single and low rate of tax the benefit from evasion will significantly reduce. Therefore, there will be little incentive for the producers and distributors to evade their turnover. Accordingly, this policy initiative should witness a higher compliance and an upsurge in revenue collections. This will also have an indirect positive impact on direct tax collections. Further, given the fact that GST will trigger an increase in the GDP, this in turn would yield higher revenues even at existing levels of compliance. Another important source of gain for the Government would be the savings on account of reduction in the price levels of a large number of goods and services consumed by the Government.

7.32 However, to the extent, the Central Government will be required to incentivise the states to adopt the GST, there will be an increase in the budgetary outgo. Given the smallness of the size of the compensation, it is expected that there would be a net gain in the tax revenues. This should enable the Central Government to better manage its finances.

7.33 As regards the State Governments, the design and the road map of the GST recommended by us would lead to substantial gain in revenues. While the revenue neutral rate for the States is estimated to be 6 percent, we have recommended that the states should be allowed to impose GST at the rate of 7 percent. An increase in the RNR of the States by 1 percent implies a revenue gain of Rs. 31381 crores per annum in the base year 2007-08 (i.e. 16.67 percent increase in the revenues from the 'TF- taxes'). If the States decide to phase out the stamp duty over a period of three years, the revenues from stamp duty will be additionality for the States. Therefore, in the first year of implementation of GST and phasing out of the Stamp duty, the States should expect additional revenues to the extent of Rs 70,000 crores (excluding the incentive amount). However, in the subsequent years this gain would diminish on account of the phasing out of stamp duty but will be more than adequately compensated as compliance starts improving.

7.34 Therefore, overall the implementation of GST should enable the Government at both levels to better meet the challenges of fiscal correction.

g. GST and vertical balance of power

7.35 The GST envisages a mechanism whereby both the Centre and the States will cease to have any independent power to make changes in the design and structure once agreed upon. Since both levels of Government would be similarly placed, this has no impact on the balance of power.

7.36 Under the proposed GST, both the Centre and the States will have concurrent power to tax all goods and services. Therefore, the taxing powers of the states would now also extend to services which comprises 54 percent of the GDP and also constitutes the fastest growing sector in the economy. Similarly, the taxing powers of the Centre will also extend to the retail stage and to this extent there will be an expansion in its taxing powers. This increase will be limited to about 12 percent of the GDP (assuming a retail margin of 25 percent on manufacturing value). In addition, the Centre will also acquire the power to tax land /real estate transaction which would account for an estimated 10 percent of GDP. Since the expansion in the power of the States is significantly larger than the Centre, the proposed GST will alter the balance of power in favour of the states thereby reducing the vertical imbalance.

7.37 To conclude, the implications of a switch over to the ‘flawless’ GST recommended by us are indeed far-reaching. Every stakeholder stands to gain. This has the potential to transform not only the tax system in the country but also the way we organise and do business.

CHAPTER - VIII

“Flawless” Goods and Services Tax and the autonomy of States

8.1 The design of the GST based on a common base and a uniform rate across states without the power to make any unilateral changes, is viewed by some states as undermining the fiscal autonomy of the States. Therefore, it is argued that the states should agree to a floor rate of tax and should have the flexibility to increase their rates to meet any revenue crisis.

8.2 Full autonomy in the exercise of taxation powers would mean that the Centre or the States, as the case may be,-

- a. Retain the power to enact the tax;
- b. Enjoy the risks and rewards of ‘ownership’ of the tax (i.e. not be insulated from fluctuations in revenue collections),
- c. Be accountable to their constituents; and
- d. Be able to use the tax as an instrument of social or economic policy.⁵⁷

8.3 Tax autonomy to any level of Government is necessary to enable it to design the base and set the tax rates according to its revenue needs. However, it is equally important to ensure that the exercise of these powers do not result in inter-jurisdictional differences in policies and procedures so as to generate additional economic distortions, create negative externalities, or impose higher compliance and enforcement burden.

8.4 In general, the States would like to have some degree of control to design the base and set the rates as an instrument to promote various social and economic policy objectives. However, cross-country experience shows that there is complete disillusionment with the use of the tax system as a tool to promote various social and economic objectives by allowing exemptions and incentives. Therefore, tax reforms undertaken across countries since the mid-1980 have focussed on re-designing the tax system so as to restrict its role to revenue collection. There is almost unanimity amongst fiscal experts on assigning a limited role of revenue collection to the tax system and using the direct transfer mechanism for achieving the

⁵⁷ See Poddar, Satya and Ehtisham Ahmad (2009)

various social and economic objectives. Given this new strand of economic thinking, the ability to use the tax system as a tool for achieving various social and economic objectives should cease to be a measure of tax autonomy.

8.5 In the past under the sales tax regime in the states, the flexibility to use the tax system as a tool for achieving various social and economic objectives has generated economic distortions and also triggered a race to the bottom. Further, if the States are allowed the autonomy to increase the rates by setting the SGST rates as the floor rates, they would have a tendency to opt for this lazy option rather than improve their enforcement mechanism. Such increase in rates would mean a greater incentive to evade which, in turn, would make industries in competing states uncompetitive. It would also trigger tax-induced migration. Consequently, the decision to increase the rate would generate negative externalities which must necessarily be curbed.

8.6 Hence, it is only appropriate that in a federal structure with overlapping powers to tax goods and services, Governments across levels cease to enjoy the autonomy to design the base, set the rates and the flexibility to use the tax system as a tool for achieving various social and economic objectives. In the context of the federal structure of India, what is relevant is overall fiscal autonomy rather than tax autonomy per se. Since States would continue to have the full freedom to promote various social and economic objectives through direct transfers, effectively, there would be no loss of fiscal autonomy of the States.

8.7 The design of the 'flawless' GST, as recommended by us in the preceding Chapters, is essentially an attempt at **absolute harmonization** of the tax base, tax rates and tax infrastructure(i.e. the administration and compliance system) across Centre and all States. As discussed above, harmonization of the tax base and the tax rates will eliminate the distortionary impact on economic efficiency and equity arising from inter-jurisdictional differences. Further, such harmonization will enable consequent harmonization of the tax laws and the administration and compliance systems.

8.8 Harmonization of tax laws is critical. Variation in the wording and structure of tax provisions can be an unnecessary source of confusion and complexity, which can be avoided if the Centre and all the States adopt a common GST law as in the case of the Central Sales Tax or agree to separately legislate an identical GST law. In either situation, there would be harmonization in respect of critical elements like common time and place of supply rules, common rules for recovery of input tax, valuation of supplies, invoicing requirements, tax interpretations and rulings regarding classification of goods and services, determination of what constitutes taxable consideration and definition of export and import.

8.9 Administration and compliance is an area where the need for harmonization is the greatest, and where Centre-State or inter-state variations are unlikely to serve any social or economic policy objective. This includes items such as the taxpayer registration system, taxpayer identification numbers, tax forms, tax reporting periods and procedures, invoice requirements, cross-border trade information systems and IT systems. Harmonization of these elements would result in significant savings in costs of implementing the GST (by avoiding duplication of effort in each government), as well as recurring savings in compliance costs. Harmonization would also permit exchange of information between different levels of Government so as to enable effective monitoring of cross-border transactions. A common tax identifier number across states and the Central government is a key element in the efficient exchange of information.

8.10 Harmonization of the GST tax base, tax rate and administrative and compliance systems should be viewed as an imperative for optimizing the efficiency and productivity of GST across jurisdictions in a federal structure. All jurisdictions will be worse off without harmonization. Therefore, it should not be perceived as eroding the fiscal autonomy of the Centre or the States.

8.11 If harmonization across Centre and all states is envisaged, what should be the institutional mechanism to usher and maintain such harmonization? At present, the responsibility for designing the initial structure of the GST has essentially been left to the

Empowered Committee of State Finance Ministers and official level representatives of the Central Government. This body is now internationally recognised as an important institutional arrangement which has rendered yeoman service in substantially furthering the cause of indirect tax reform in the country. However, there is also a need to maintain stability and integrity in the structure of the GST to ensure that no distortions creep into the indirect tax system. Therefore, the existing mechanism for arriving at a collective decision on the structure of the GST should be permanently institutionalised so that changes in the initial design of the GST are collectively agreed and implemented by both the Centre and the States.

8.12 In view of the above, we recommend that the Empowered Committee of State Finance Ministers may, upon the introduction of the GST, be transformed into a permanent constitutional body known as the **Council of Finance Ministers**. This Council shall comprise of the Union Finance Minister and all State Finance Ministers. The Union Finance Minister would be the Chairman of this Council.

8.13 The Council should be responsible for any modification in the initial design of the dual GST and regulating the indirect tax system in the country. The initial design of the dual GST should be approved by the Chairman and three-fourth of the State Finance Ministers. Thereafter, any change in the structure of the GST (both base and the rates) should be allowed to be carried out only if the Chairman **and** two-thirds of the State Finance Ministers agree to do so. Consequently, neither the Centre nor any State will have the authority to unilaterally make any change in the agreed design of the GST. However, in the event of a crisis, the Member State or the Centre may take immediate steps to impose a surcharge subject to ex-post facto approval by the Council within one month. Further, such surcharge should not be allowed to remain in force beyond a period of one year.

8.14 This Council should, in due course, have a permanent secretariat of its own in New Delhi.

8.15 The proposed mechanism will also ensure that all changes are thoroughly analysed and debated before being implemented. More importantly, since both the Centre and the States

would surrender their individual autonomy to change the structure of the GST to the proposed constitutional body, the existing balance of federal fiscal powers will continue to be maintained.

8.16 Further, with a view to compensating for the **perceived** erosion in the tax autonomy of the States, we also recommend that there should be an increase in the formula-based devolution to the states.

CHAPTER - IX

Incentivising States to adopt GST

9.1 The movement from sales tax to VAT at the state level entailed the adoption of uniform RNR rate by all states. The RNR rate is the weighted average of rates across states. Since there was no significant expansion in the base, it implied that states with average weighted rate higher than the RNR would lose revenue while those below it would gain revenue. Hence, the States demanded compensation for adopting VAT. The States have now also demanded compensation for any loss which might be incurred as a result of the shift from the existing indirect tax system at the state level to the GST level.

9.2 States have expressed concern that the RNR for State GST may be revenue neutral at the aggregate level but not necessarily for all individual States. It has, therefore, been suggested that if the States were to be denied the flexibility of upward adjustment to the tax rates, they should be compensated for the revenue loss estimated on a transparent basis.

9.3 The RNR calculated by us in the preceding paragraph is estimated to be 6 percent if all the taxes listed in paragraph are subsumed. Our calculations of revenue estimates, based on estimated C-efficiencies of the existing state level indirect tax structure and of the proposed State GST, for each state indicates that there would be no revenue loss for any state on account of the switch over to GST at the estimated RNR rate of 6 percent and existing level of compliance. This is primarily due to the fact that the change entails significant increase in the tax base for the States. In fact, we estimate that there would be significant revenue gain at 7 percent RNR as recommended by us.⁵⁸

9.4 The Group recognises that the adoption of the GST would create significant positive externalities to impact GDP and various other macroeconomic variables. This would result in reduced cost of economic management to the Central Government. Hence it is logical that the Central Government shares with the States such positive externalities.

⁵⁸ Our detail calculations can be made available on request.

9.5 Some States have expressed their lack of confidence in the existing compensation arrangement for revenue loss to the States. It has been suggested that the compensation mechanism, to be credible, must be administered by a body independent of the Finance Ministry in which the State Governments have a say in governance. The suggestion merits consideration.

9.6 Therefore, we recommend the following:-

- i) A GST Compensation Fund should be created under the administrative control of the **Council of Finance Ministers**.
- ii) The Central Government shall transfer to the GST Compensation Fund a minimum sum of Rs 6000 crores per annum over the next five years (i.e. a total amount of Rs 30,000 crores) if, and only if, the States-
 - a. introduce the 'flawless' GST as recommended by us; and
 - b. follow the road map, as suggested by us, for its introduction;
- iii) The amounts in the Fund should be used only for the following purposes:-
 - a. To compensate the states for any revenue loss on account of the adoption of the 'flawless' GST;
 - b. The balance, if any in the Fund, to be carried forward to the subsequent year;
 - c. The balance, if any remaining at the end of the fifth year, to be distributed amongst the states on the basis of the same formula used for distributing resources in the divisible pool.
- iv) The amount will be transferred in quarterly instalments.
- v) The amounts shall be disbursed by the Council on the basis of the recommendations by a three member Compensation Committee comprising of the Secretary, Department of Revenue, Government of India, Secretary to the Council and any fiscal expert appointed by the Central Government for this purpose.
- vi) No contribution to the Fund shall be made by the Central Government in any year in which the States fail to adhere to the roadmap for implementation of the GST.

vii) The methodology to be used for estimating the revenue loss and the compensation shall be decided by the Council.

9.7 These recommendations will serve as an incentive for the states to adopt the flawless GST and also ensure that the payment for compensation, if any, is legitimate and transparent.

9.8 One of the lessons drawn from the implementation of VAT at the State-level is the frequent tendency by the States to deviate from the collectively agreed position relating to the base and the rates. This creates significant tax induced distortions in economic behaviour across states. Further, as stated earlier, it also creates negative externalities. Therefore, it is imperative to establish a mechanism whereby the defaulting state is made liable to pay for the negative externalities. Accordingly, we recommend the following:

- i. Any state which deviates from the GST base or rates, collectively agreed upon, without the authority of the Council, should be liable to such penalty for the year, as may be recommended by the Thirteenth Finance Commission.
- ii. If the deviation is for a period less than a year, the state will be liable for a proportionate amount of penalty attributable to the period of deviation. Similarly, if the deviation is for a period more than a year, the state will be liable for the completed years and the proportionate amount relating to the remainder period.
- iii. The amounts collected in penalty shall be deposited in the GST Compensation Fund for formula based devolution to the States.

9.9 This mechanism will provide symmetric treatment of positive and negative externalities whereby creation of positive externalities will be rewarded and negative externalities will be penalised.

CHAPTER - X

Goods and Services Tax - The way forward

10.1 The introduction of the Value Added Tax at the state level was discussed over a prolonged period of more than a decade before implementation. Given the fact that the reform of the indirect tax system is critical to any effort to increase efficiency and economic growth, such prolonged period of discussion on issues in respect of which there is adequate well documented international experience is costly and should, therefore, be avoided. In spite of such prolonged period of discussion, the state VAT regime in the last four years has witnessed many States deviating from the classification and the rates agreed upon in the White Paper of the Empowered Committee, released in January, 2005.

10.2 Similarly, the discussions on the introduction of a comprehensive dual GST, both at the Centre and State level, have been in progress since early 2006. It is unfortunate that no agreement on the GST has yet been reached even though the target date for its introduction i.e., 1st April, 2010, is less than six months.

10.3 The Central Government has entered into a number of free trade agreements. As these agreements are operationalized, it is necessary to optimise the efficiency and competitiveness of Indian industry. There is no headroom for pursuing distortionary policies. To the extent, the distortions are induced by the indirect tax system, there is an urgent need to reform the same by adopting a flawless Goods and Services Tax along the lines recommended in this Report. The adoption of a flawless Goods and Services Tax is critical to the survival of the Indian industry in the face of increasing international competition consequent to a number of free trade agreements entered into by India.

10.4 Hitherto, the approach of the Central Government has been to act as a catalyst in the process of the design of the GST. This responsibility has essentially been left to the Empowered Committee of State Finance Ministers and official level representatives of the Central

Government. Since the design of the GST will also impact the indirect tax system of the Central Government, it is necessary for the Central Government to play a more proactive role in this effort. Towards this, the leadership of the Union Finance Minister would be vital. This will provide the necessary impetus to the process of 'grand bargaining' for the GST.

10.5 While the Council is engaged in the process of designing the GST, the Council should approve the draft of the amendment to the Constitution to the effect that the Centre and the States shall exercise concurrent jurisdiction to subject all goods and services (other than SIN-goods) to a consumption type value added tax based on destination principle where exports will be zero rated and all imports will be subject to the levy like any other goods and services domestically produced and consumed. Further, it should also provide that the base for the levy should be common for both the Centre and the States and there would be a legislated agreement amongst the States and the Centre to (a) adopt uniform classification, (b) adopt uniform rates, (c) not modify the classification or the rates except with the agreement of all the States and the Centre and (d) provide for other essential common features like zero-rating of (or credit by importing State for) inter-State sale of goods. This could be on the lines of the GST legislation in Australia, under which all the States and the Commonwealth (the Centre) have to agree before any change in the rate or the base of GST can be implemented.

10.6 The implementation of the GST is scheduled for 1st April, 2010. However, given the fact that the discussion paper on GST has not yet been released for public debate, it is unlikely that the Centre and the States would be able to complete all legislative and administrative processes before the 1st April, 2010. Therefore, it would be appropriate for the Council to postpone the implementation by six months to 1st October, 2010. However, the Council should release a timeline of various activities for introduction of GST simultaneously with the announcement for postponement. This will enable all stakeholders to monitor the progress and ensure that the new implementation date is not missed out. The new timeline starting 1st January, 2010 is contained in Annexures.

10.7 The SGST is being designed by the Empowered Committee to subsume the ‘EC-taxes’⁵⁹ only. One of the main elements of the ‘flawless’ GST recommended by us is that all taxes on goods and services, levied by the Centre or the States, should be subsumed in the GST. Therefore, we have recommended that the following other taxes levied by the States on goods and services should also be subsumed:

- a. Stamp duty;
- b. Taxes on Vehicles;
- c. Taxes on Goods and Passengers; and
- d. Taxes and duties on electricity.

10.8 There is also a view amongst States that while they agree that these taxes should eventually be subsumed, they would like to gradually move in that direction rather than adopt a ‘big bang’ approach.

10.9 The introduction of the GST should be viewed as the last mile in the reform of the indirect tax system of this country initiated in 1986 with the introduction of the MODVAT. The present system of taxes on goods and services is an outcome of a gradual approach to tax reform over the last 23 years. Consequent to this approach, the country has undoubtedly lost out on potentially higher economic growth, higher real wage rates, fiscal consolidation and consumer welfare. All stakeholders other than the oligarchs, both within and outside the system, stand to gain from a swift comprehensive changeover to the GST. The multitude of the poor will gain from this reform measure more than any other stakeholder. To the extent the switchover is staggered, the potential gains from the comprehensive GST would remain unrealised thereby adversely impacting the poor. We therefore, recommend that all taxes on goods and services, whether levied by the Centre or the States, should be subsumed in the GST in the very first year of its introduction.

10.10 However, if for some political economy reasons it is considered expedient to introduce the GST in a phased way, we recommend the phasing in the following manner:-

⁵⁹ See para 2.11

- a) In the year 2010-11, all elements of the Flawless GST recommended by us whereby
- i. the single CGST rate should be 5 percent and the corresponding SGST rate should be 7 percent; and
 - ii. Transactions in immoveable property (i.e real estate and housing services) should be brought within the fold of GST; and
 - iii. Stamp duty may not be subsumed but the rate of stamp duty in all states should be calibrated so as not to exceed 4 percent. As a result, transactions in real estate will be subject to a dual levy like in the case of SIN-goods;
- b) In the year 2011-12, same as (a) above, with the modification that the rate of stamp duty should be reduced to 2 percent; and
- c) In the year 2012-13, same as (a) above, with the modification that-
- i. Stamp duty should be eliminated and replaced by a Registration Fee at a specific rate;
 - ii. the revenues attributable to 2 percentage point out of the 7 percentage point of SGST should be set apart for devolution to the third-tier of Government and the revenues from the balance 5 percentage points will remain with the State Government so that the third-tier of Government have a interest in the efficient functioning of the GST and do not have to impose any cascading taxes like cess, entry tax or Octroi.⁶⁰

10.11 Further, we also recommend that the phased program for introduction of the GST as outlined above should be incorporated in the GST legislation so that there is no uncertainty on the evolution of the GST which will enable trade and industry to appropriately structure their business.

⁶⁰ We are aware that this aspect will also require to be included in the proposed amendment to the Constitution for introduction of GST.

10.12 We do not envisage any loss of revenue at the rates of CGST and SGST recommended by us. However, the rates being sufficiently low, we expect more than normal growth in revenues through better compliance and ease of administration. These low rates will also provide sufficient fiscal space to the Government to meet any contingency which may arise in the future by raising the rates as was done in Japan, Singapore and New Zealand⁶¹.

10.13 The Central Government and State Governments must come together in national interest to build a consensus on the GST and adhere to the new deadline of 1st October, 2010 for rolling out GST. Given the strategic importance of this game-changing reforms, the country can little afford any delay.

⁶¹ Japan increased the VAT rate from 3 percent to 5 percent, Singapore from 3 percent to 7 percent and New Zealand from 10 percent to 12.5 percent.

Chapter-XI

Conclusion

11.1 The taxation of goods and services in India has, hitherto, been characterised as a cascading and distortionary tax on production resulting in mis-allocation of resources and lower productivity and economic growth. It also inhibits voluntary compliance. It is well recognised that this problem can be effectively addressed by shifting the tax burden from production and trade to final consumption. A well designed destination-based value added tax on all goods and services is the most elegant method of eliminating distortions and taxing consumption. Under this structure, all different stages of production and distribution can be interpreted as a mere tax pass-through, and the tax essentially ‘sticks’ on final consumption within the taxing jurisdiction.

11.2 The efficiency of the VAT enhances with increase in the purity of the GST Model. The most important ten elements of a pure GST are the following:-

- a. The base should extend to all goods and services including immovable property;
- b. There should be a single low rate;
- c. The tax should be destination based;
- d. The tax should be designed on invoice-credit method;
- e. Full and immediate input tax credit in respect of capital goods;
- f. The GST must replace all transaction based taxes on goods and services and factors of production.
- g. There should be seamless flow of the tax through all stages of production and distribution so as to stick on “final” consumption;
- h. The exports should be zero rated and imports should be fully taxed;
- i. There should be a threshold exemption for small dealers;
- j. Full computerisation of the compliance and administrative systems.

11.3 In the light of the above, we have recommended a ‘flawless’ GST in the context of the federal structure which would optimise efficiency, equity and effectiveness. The ‘flawless’ GST is designed as a consumption type destination VAT based on invoice-credit method. It provides for a comprehensive base including financial services and immovable property. To the extent there are exemptions, albeit limited to items covered for distribution through the public distribution system, and health and education services, the purity of the GST is diluted. A threshold exemption of Rs. 10 lakh has also been provided for small businesses. Imports into the country are proposed to be taxed in the same manner as domestically produced goods. Like intermediate inputs, full and immediate credit for tax paid on capital goods will also be provided. Further, it also provides for a single rate of tax of 12 percent for all general goods and services across all states, comprising of 5 percent by the Centre and 7 percent by the States⁶². However, products of high value like gold and platinum will be subject to tax at the rate of 1 percent each by the Centre and the States and exports will be zero rated.

11.4 There is empirical evidence to suggest that the switchover from the present distortionary taxation of goods and services to a ‘flawless’ GST will, amongst others, increase productivity of all factors of production and hence enhance GDP. The switchover has also been analysed to be pro-poor and therefore, further the cause of poverty reduction. Further in the Indian context, a dual VAT type tax concurrently levied by both the Centre and the States would enable the creation of a common market.

11.5 Given the benefits of the changeover to the flawless GST, it would be economically rational for all levels of Government to introduce and successfully implement the flawless GST and for the Central Government to invest in incentivising the State Government to adopt the flawless GST. We have, therefore, recommended that the Central Government should provide a sum of Rs 30,000 crores over the next five years which will be used to compensate the States

⁶² However, products of high value like gold and platinum will be subject to tax at the rate of 1 percent each by the Centre and the States and exports will be zero rated.

for revenue loss, if any, and the balance for distribution between the States on the basis of the same formula applicable for tax devolution to the States.

11.6 The implications for fiscal management are far-reaching. It will significantly improve fiscal management through higher tax buoyancy. While the RNR for State level ‘TF- taxes’ (including Stamp duty) is only 6 percent, we have allowed them a higher rate of 7 percent along with the flexibility to phase out the stamp duty over a period of next three years. This has the potential to increase the combined tax revenues of States by an estimated amount of Rs 70,000 crores. In addition, we have also recommended that the States should be provided with an additional Rs 30,000 crores as incentive to adopt a ‘flawless’ GST. Therefore, the switch over to the flawless GST will augment the combined resource base of the States by an aggregate sum of Rs 100,000 crores⁶³.

11.7 We recognise that the levy will be imposed and enforced by a large number of Governments. Therefore, there would be constant pressure on States to deviate from the pure VAT model and trigger harmful tax competition. This would jeopardise the sustainability of the benefits from the implementation of the ‘flawless’ GST. Therefore, it is also necessary to establish an institutional mechanism which would be responsible for making any change in the design and structure of the VAT. Our recommendation to establish a Council of Finance Ministers is intended to subsume the independent powers of the both the Central and State Governments to levy tax on goods and services in favour of collective exercise of the powers. Therefore, there is no exacerbation in the vertical imbalance in the fiscal powers.

11.8 The First Discussion Paper released by the Empowered Committee of Finance Ministers on 10th November, 2009 envisages an extremely diluted form of GST under which, inter alia, (i) a number of cascading taxes including purchase tax will continue to be levied by the States; and (ii) the base is considerably eroded on account of the proposed continuation of the exemptions. We are also given to understand that the Empowered Committee is considering a two rate structure for general goods and services (other than high value goods). The design of the GST as

⁶³ This is equivalent to 2 percent of GDP.

envisaged by the Empowered Committee is, therefore, a significant dilution of the ‘flawless’ GST. Consequently, the potential economic benefits from a switch over to the flawless GST, which we have discussed in the foregoing chapter, would not be realised.

11.9 We have recommended that the implementation of the GST should be postponed to 1st October, 2010. We believe that it should be possible to adhere to this timeline. The benefits from the switch over to the GST are contingent upon the purity of the GST design. In the context of VAT, international experience shows that any design-related ‘VAT mistakes are very hard to rectify’. Therefore, it must be ensured that there are no design related mistakes at birth. However, if there is a trade-off between the timeline and the design of the GST, the dilemma must be resolved in favour of design.

11.10 Further, in order to implement the ‘flawless’ GST it would be necessary to undertake constitutional amendments to enable both the Centre and the States to exercise concurrent jurisdiction over the taxation of all goods and services, creation of the proposed Council of Finance Ministers and assignment of part of the GST proceeds to the third-tier of government. These amendments must, inter alia, provide that the taxation of goods and services by both the Centre and the States should be a consumption-type, destination based GST.

11.11 The introduction of the ‘flawless’ GST is one of the most important reform agenda which can provide a new impetus to Indian industry and inclusive growth. It is an economic game changer. All stakeholders must unite and develop the necessary will to cooperate in introducing the flawless GST. It would be worthwhile to make greater political investment in this endeavour.

Annexures

Treatment of immovable properties under Goods and Services Tax

The **case for** including the real estate sector in the tax base for the GST rests on a number of competing reasons. **Firstly**, the construction and exploitation of real estate comprises one of the larger sources of gross domestic product. Therefore, any exclusion of the real estate sector would lead to significant reduction in the tax base. This would lead to an increase in the GST rate for other sectors thereby distorting economic efficiency and incentive for compliance.

Secondly, expenditure on housing also constitutes a significantly large proportion of total personal consumption expenditure. Therefore, the exemption of the housing sector from the GST base would distort the consumption pattern. Further, it would also undermine vertical equity in as much as consumption of housing services is relatively high in the case of the rich.

Thirdly, real estate is subject to multiple taxation at both levels of Government. At the Central Government level, there has been an attempt to introduce service tax on housing services and allow credit for inputs used for the supply of such services. However, at the State level input tax credit is not available for all taxes, thereby leading to significant cascading effect. Further, there is no incentive to the purchaser to obtain an invoice. Consequently, the audit trail of such transactions is lost and producers of inputs are also encouraged to suppress such transactions. The cumulative effect is to incentivise transactions in black money.

At the State level, the taxes on the real estate sector include 'sales tax' on works contract, state level VAT on various inputs used in the construction of real estate, stamp duty and registration fee. Registration and stamp duties exhibit the same distortionary cumulative and cascading effects as excises. The problem is further compounded by the fact that in most states, the statutory rates of stamp duty on immovable property transaction are high. Therefore, the effective rate on value addition is exorbitant, thereby encouraging under-

reporting of transactional value and evasion of stamp duty. Since stamp duties are directly or indirectly related to other taxes, any stamp duty evasion triggers a similar adverse response to compliance with other taxes. As with other transaction taxes, it generates a bias in favour of not selling, and inhibits the development of a liquid secondary market. In the context of a distortionary tax regime governing the real estate industry in India, there is a strong tendency for this industry to remain outside the organised sector and consequently the regulatory framework. Therefore, it serves as a breeding ground for tax evasion and criminal activities.

Fourthly, rationalisation of the tax regime governing the real estate industry could yield numerous benefits : improve tax compliance in the property tax which is critical for the revenue base of local government, a reduced role for black money, and a reduced role for the criminal element in the real estate sector and significantly lowering of costs by mass housing.

At a conceptual level, under a VAT, sales, rentals, and rental values of immovable property would be taxable and credit would be available for the VAT embedded in purchases. Immovable property that generates housing services should be treated in the same manner. The theoretically most attractive solution would be to register all legal persons, who own or buy residential real estate, for VAT purposes. By purchasing a dwelling, these persons would become producers of housing services. In their role as producers, they would subsequently sell the housing services to consumers. These consumers could be lessees who buy the services for consideration, i.e., a rental charge. It is also possible that producers would put the dwelling at their own disposal. In other words, as owner-producer they would "sell" the housing services to themselves in their role as occupier consumers. Therefore, the purchaser of an immovable property could use the housing services produced from ownership either for self-consumption or for 'sale' by renting out the property.

The VAT consequences of these events are as follows. On purchase of a bundle of housing services in the form of dwelling, the registered taxpayer pays tax on the purchase price,

but at the same time, he is entitled to a tax credit (and refund, if due) for the same amount. If he sells the housing services to lessee, he would have to charge VAT on the amount of the rental. The lessee, being an unregistered consumer, would not be able to pass the tax on; he would be stuck with it just like consumers of other services. Similarly, in his role as owner-occupier, the producer of housing services would "charge" VAT on these services, whose value equals the rental value of the dwelling rendered to himself as consumer. And like the lessor, he would have to remit that tax (net of any tax on inputs, such as repair and maintenance services) to the government.

In practice, the registration of all owner occupiers and the computation of all imputed rental values present formidable administrative problems and are, therefore, not feasible. If imputed rental values cannot be taxed, the taxation of rental charges would appear to favour owner-occupiers over lessees. Further, the practical difficulties of taxing small landlords might be severe. Therefore, as a second-best approach, it would be appropriate to provide a threshold exemption for GST which would ensure that the large majority of small landlords are outside the scope of GST. Since the imputed rental values in the case of self owners would predominantly be below the threshold exemption limit, it would be desirable from an administrative aspect to exclude imputed rental values in the case of self owners from the scope of GST.

The treatment of housing under a VAT like GST regime can be designed following either the comprehensive taxation method or one of the two variants of the exemption method. The treatment of transactions in immovable property and real estate/housing services under the three methods is summarised in the Table below.

Table
VAT treatment of immovable property under two approaches

Nature of transaction	Comprehensive taxation	Exemption method	
		(variant-A)	(variant-B)
A. Existing residential property stock			
i. Sale	T	T	E
ii. Rental charges	T	E	E
iii. Imputed rental values	E	E	E
iv. Alteration and maintenance	T	T	T
B. New residential property			
i. Construction/ First Sale	T	T	T
ii. Resale	T	T	E
iii. Rental charges	T	E	E
iv. Imputed rental values	E	E	E
v. Alteration and maintenance	T	T	T
C. Existing commercial property stock			
i. Sale	T	T	T
ii. Rental charges	T	E	T
iii. Imputed rental values	E	E	E
iv. Alteration and maintenance	T	T	T
D. New commercial property			
i. Construction/First Sale	T	T	T
ii Resale	T	T	T
iii. Rental charges	T	E	T
iv. Imputed rental values	E	E	E
v. Alteration and maintenance	T	T	T
E. Inputs (both goods and services) used for construction	T	T	T

Under the **comprehensive taxation method**, all new properties (both residential and commercial) constructed after the introduction of the VAT are liable to tax on construction/first sale of the building on the reasoning that the cost of construction or the price of first sale represent the present discounted value of the flow of imputed rental services over the life of the property. Thereafter, the rental charges for leasing of such properties is also liable to VAT

with the landlord being entitled to input credit on the tax paid on construction/purchase of the building. However, if the property is owner occupied, no VAT is applicable on imputed rental value of the house. Correspondingly, the owner is also not entitled to input tax credit. Upon resale of the property, VAT is realised on the full resale value and input credit to the extent not utilised against rental income is allowed as a deduction. If the input credit is greater than the VAT on resale value, the excess is ignored and no refund for such excess is allowed. As a result, VAT is payable on the margin earned on sale of the property i.e., the difference between the sale price and the cost of procurement and improvements thereto. It applies only to enhancement in the value of the property. The treatment in respect of resale of properties built prior to the introduction of VAT would be the same with the modification that no input tax credit is allowed in respect of VAT which is paid at the time of its purchase. Further, VAT is also levied on the value of the supply of all goods and services for construction, alteration and maintenance of an immovable property.

The comprehensive method, as its name suggests, is extremely wide in its scope. **Firstly**, it extends to the consumption of existing stock of properties, as well as to any unanticipated future increases in the rental value of the new properties. **Secondly**, this method also effectively entails full taxation of imputed rental value of owner-occupied properties. New properties attract tax on their full capital value (i.e., the purchase price) at the time of purchase, for which no deduction is allowed to the owner during the period of self-occupation of the property. **Thirdly**, the existing properties also attract tax on their full capital value at the time of resale. Further, this method simplifies legislation in as much as no distinction is required to be made between residential or commercial properties.

The case against the comprehensive method is essentially built on the following considerations. **Firstly**, under the method landlords would tend to register themselves to avail of credit in respect of input tax paid on construction/purchase of the property thereby increasing the administrative burden of dealing with a large number of small registrants. However, this problem is highly exaggerated in the context of a reasonably moderate threshold

exemption for small businesses whereby most small landlords would remain exempt. **Secondly**, application of tax on resale of dwellings would require the owners to keep track of input taxes paid on the acquisition of the dwellings, on improvements undertaken over the period of their ownership and input credit availed against VAT payable on rental value. Further, in many cases, there are frequent changes in the use of the dwelling as owner-occupied residence or rental dwelling. Since input tax credits are allowed only for houses used for rental purposes, these changes in the usage of the dwelling would require special rules for appointment of the input tax credits resulting in increased administration burden for the tax office. However, these problems are surmountable by not allowing any credit for input tax paid on construction/purchase of the property or improvement thereto against VAT payable on rental value. The credit for such input tax can be allowed only at the time of resale, after adjusting the same for inflation. **Thirdly**, in the case of existing stock of properties, the tax applies on the full resale value. This may be appropriate only where the existing properties did not previously bear the taxes that were being replaced by the VAT. If indeed substitute taxes (though of the cascading variety) are applied to some or all components of the existing properties, subjecting them to full taxation again under VAT would amount to double taxation. This can be resolved by allowing credit for the taxes already paid or levying the VAT only to enhancement in the value of the property.

Under the Variant – A of the exemption method, like in the comprehensive taxation method, all new properties (both residential and commercial) constructed after the introduction of the VAT are liable to tax on construction/first sale of the building. However, both the rental charges for leasing of such properties and the imputed rental value are exempt with no benefit for input tax credit whatsoever. Upon resale of the property VAT is realised on the full resale value and input credit for tax paid on construction/purchase of the property is allowed as a set off. If the input credit is greater than the VAT on resale value, the excess is ignored and no refund for such excess is allowed. As a result, like in the comprehensive taxation method, the VAT on resale is payable only on the margin earned on sale of the property. The treatment in respect of resale of properties built prior to introduction of VAT is

the same with the modification that no input tax credit is allowed in respect of VAT which is paid at the time of its purchase. Further, VAT is also levied on the value of the supply of all goods and services for construction, alteration and maintenance of an immovable property.

The Variant-A is economical neutral between rented properties and owner occupied properties in as much as both the actual rent and imputed rent is exempt. Similarly, this method is also neutral across properties constructed before and properties constructed after the introduction of VAT since resale of the property is liable to VAT. The administrative and compliance difficulties are similar to those faced under the comprehensive taxation method with the modification that the number of landlords seeking registration would be relatively small since actual rent is exempt. However, administrative complexity would increase in case of mixed use of properties i.e. where the building is partly used for residential and partly for commercial rentals or where the use of the unit changes between commercial and residential use since this would required special rules of apportionment of the input tax credits. Further, in many cases, along with the renting of the unit, various related services such as utilities, furnishings, meals and maid services are also provided. Special rules would need to be framed to segregate residential rentals from the related supplies.

Under Variant –B of the exemption method, a distinction is made between residential and commercial properties. The commercial properties are treated in the same manner as under the comprehensive taxation method. In the case of residential properties, VAT is levied at the time of construction/first sale of such properties which are constructed after the introduction of VAT. All resale of properties, whether constructed before or after the introduction of the VAT is exempt. As a result, the scope of VAT does not extend to existing properties. Further, VAT is also levied on the value of the supply of all goods and services for construction, alteration and maintenance of an immovable property.

Variant-B is extremely narrow in its scope since sale and resale of both existing and new residential properties, rental value and imputed rent are exempt. This can be highly

distortionary since the benefit from such exemption would depend on the mix of taxable and non-taxable inputs used in construction. Further, a distinction would also need to be made between residential and non-residential properties to allow for the exemption and input tax credit. This would add to the complexity in the tax administration.

The real estate sector should be integrated into the GST framework keeping in view the implications of the different methods.

**Report of the Task Force on Goods and Services Tax
Thirteenth Finance Commission**

FORM	GST 1	Goods and Services Tax [This form is to be used for reporting of transactions and payment of both CGST and SGST]	Financial Year					

Business Identification Number (BIN)	Date of deposit(DD/MM/YYYY)	Month to which transactions relate

Form Identification Number (FIN)	BSR Code	Date (DD/MM/YYYY)	Serial Number
Transaction Reference Number			

Full Name	
Complete Address with City & State	
Email Address	PIN
Phone Number (with STD Code)	
Mobile No.	

Details of payment											
Total amount of CGST and SGST payable (in figures)											
Total Amount of CGST and SGST payable (in words)	Crores	Lakhs	Thousands	Hundreds	Tens	Units					
Paid by debit to account (Account No. of the deductor)					Date of debit						
Name of the Bank in which payment is made											

Computation of tax liability				
Sale transactions		Value of transaction	CGST	SGST
a.	Registered dealers (intra-state)			
b.	Unregistered dealers (all transactions)			
c.	Exports out of India			
d.	Inter-state sales (registered, dealers)			
e.	Inter-state branch transfer			
f.	Total			
Purchase transactions				
a.	Registered dealers (intra-state)			
b.	Unregistered dealers (all transactions)			
c.	Exports out of India			
d.	Inter-state sales (registered dealers)			
e.	Inter-state branch transfer			
f.	Total			
Total GST payable (CGST plus SGST)				
Interest				
Penalty				
Others				
Total amount				

**Report of the Task Force on Goods and Services Tax
Thirteenth Finance Commission**

Details of Transactions of sale or purchase undertaken during the month (if the number of records exceeds 10 for registered dealers, upload transaction file)					Upload transaction file	
Unique Transaction Number	BIN of the person with whom the transaction of sale or purchase is undertaken		Name of seller/purchaser	Value	Amount of CGST	Amount of SGST
a. Purchase transactions						
b. Sale transactions						

VERIFICATION

I..... son/daughter of holding Permanent Account Number solemnly declare that to the best of my knowledge and belief, the information given in the return and the schedules thereto is correct and complete and that the particulars shown therein are truly stated and are in accordance with the provisions of the Central Goods and Services Tax Act, 2010 and the provisions of the State Goods and Services Tax Act, 2010 in respect of the Central Goods and Services Tax and State Goods and Services Tax chargeable for the month of..... I further declare that I am making this return in my capacity as and I am also competent to make this return and verify it.

Place :

Date :

Sign here

Note: Please do not furnish transaction wise details of unregistered purchases and sales.

Report of the Task Force on Goods and Services Tax Thirteenth Finance Commission

Table-13: States' Own Tax Revenues on goods and services -2007-08

(All figures in Rs in crores)

S. No.	States	State Excise	Sales Tax, VAT and Purchase Tax	Central Sales Tax	Other Receipts	Total Sales Tax	Sales tax and CST on POL	Sales Tax on alcohol	Total Non-POL Non-Alch'l Sales Tax	Ent't Tax	Entry tax in lieu of Octroi	Taxes on Vehicles	Taxes on Goods and Passengers	Taxes and Duties on Electricity	Stamps and Regn Fees	Other Taxes and Duties	Total EC-taxes*	Total TF-taxes*
		Col. 1	Col. 2	Col. 3	Col. 4	Col.5 (2+3+4)	Col.6	Col.7	Col.8 (5+6-7)	Col.9	Col.10	Col.11	Col.12	Col.13	Col.14	Col.15	Col.16	Col. 17
	General Category State																	
1	Andhra Pradesh	4041	17538	1433	56	19026	5301	3248	10478	0	78	1604	80	195	3086	171	10727	15692
2	Bihar	525	2491	44	-1	2535	1133	147	1255	14	979	273	938	64	654	0	2249	4178
3	Chhattisgarh	843	2448	521	54	3024	939	0	2085	5	0	277	511	395	463	2	2092	3737
4	Goa	76	3	60	817	879	370	0	509	11	127	82	113	0		191	838	1032
5	Gujarat	47	189	1905	13010	15105	5332	12	9760	0	240	1310	152	2047	2018	263	10263	15790
6	Haryana	1379	6364	1357	0	7721	2040	11	5670	17	0	234	379	107	1763	7	5695	8179
7	Jharkhand	157	2215	636	-6	2846	730	45	2070	5	151	136	71	76	156	0	2227	2666
8	Karnataka	4767	3507	1262	9125	13894	3896	0	9998	353	0	1650	837	449	3409	37	10388	16734
9	Kerala	1169	3335	1016	5021	9372	2336	1998	5038	1	0	853	0	39	2028	78	5117	8037
10	Madhya Pradesh	1854	5488	557	0	6045	2512	0	3533	12	0	703	916	626	1532	16	3562	7338
11	Maharashtra	3963	24362	2385	6	26753	10076	1080	15596	410	0	2143	388	2688	8550	634	16640	30409
12	Orissa	525	3567	551	0	4118	1077	132	2910	2	0	459	627	327	405	29	2941	4760
13	Punjab	1862	4920	328	94	5342	1482	29	3832	5	587	499	0	604	1568	2	4427	7098
14	Rajasthan	1805	7126	405	219	7751	2819	1	4931	16	0	1164	161	584	1544	43	4990	8443
15	Tamil Nadu	4764	16434	1722	0	18156	5081	3889	9186	9	1097	1483	1097	37	3805	173	10465	16888
16	Uttar Pradesh	3948	12464	1385	1174	15023	4653	28	10342	94	553	1146	110	207	3977	63	11052	16491
17	West Bengal	935	7249	798	14	8060	2465	342	5253	30	0	532	1	507	1417	311	5595	8052
	Total	32660	119701	16365	29585	165651	52242	10961	102448	986	3812	14549	6381	8953	36374	2020	109266	175524
	Special Category States																	
1	Arunachal Pradesh	12	0	0	77	77	16	0	61	0	0	6	0	0	1	0	61	68
2	Assam	189	1310	0	1382	2691	1154	0	1537	3	0	139	12	5	110	4	1544	1809
3	Himachal Pradesh	390	979	113	0	1092	239	32	821	0	0	114	55	82	87	137	958	1295
4	Jammu & Kashmir	244	1802	0	3	1805	341	80	1384	0	97	73	265	93	66	3	1484	1981
5	Manipur	4	0	0	115	115	27	1	87	0	0	4	1	0	3	0	88	96
6	Meghalaya	42	52	21	8	81	68	26	0	1	0	5	2	0	3	1	2	12
7	Mizoram	2	51	0	11	62	21	0	41	0	0	5	1	0	0	0	41	48
8	Nagaland	3	10	9	75	95	28	0	66	0	0	12	2	0	1	0	66	82
9	Sikkim	29	25	4	27	56	21	0	35	1	0	4	0	0	2	4	40	46
10	Tripura	38	263	2	0	265	59	14	192	0	0	23	0	0	15	2	194	232
11	Uttaranchal	442	1627	0	0	1627	404	38	1185	6	5	155	0	55	424	5	1201	1836
	Total	1393	6119	150	1698	7967	2378	192	5397	11	102	541	338	235	713	156	5666	7492
	Union Territories																	
1	Chandigarh	128	429	124	0	553	114	0	439	5	0					0	444	444
2	Delhi	1295	5285	1723	0	7009	1695	293	5021	60	0	425	0	0	1350	378	5459	7234
3	Daman and Diu	0	120	50	0	170	8	0	162	0	0					0	162	162
4	Pondicherry	224	189	181	0	369	5	4	360	0	0	35	0	0	37	0	360	432
5	Port Blair	0	0	0	0	0	0	0	0	0	0					0	0	0
	Total	1647	6023	2078	0	8100	1822	297	5981	65	0	460	0	0	1387	378	6424	8271
	Grand Total	35701	131843	18593	31282	181718	56442	11450	113826	1062	3914	15549	6719	9188	38473	2554	121356	191287

* This includes an estimated amount of Rs 3000 crores as Sales Tax on Tobacco products for which we do not have State-wise breakup. Therefore, the amount of EC-taxes and TF-taxes for the purposes will be lower by Rs 3000 crores each.

**Report of the Task Force on Goods and Services Tax
Thirteenth Finance Commission**

Nature of business for income tax purposes

Sector	Sub-Sector	Code	Sector	Sub-Sector	Code
1. Manufacturing Industry			5. Contractors	Civil Contractors	0501
	Agro-based industries	0101		Excise Contractors	0502
	Automobile and Auto parts	0102		Forest Contractors	0503
	Cement	0103		Mining Contractors	0504
	Diamond Cutting	0104		Others	0505
	Drugs and Pharmaceuticals	0105	6. Professionals	Chartered Accountants, Company Secretaries.	0601
	Electronics including Computer Hardware	0106		Fashion designers	0602
	engineering goods	0107		Legal professionals	0603
	Fertilizers, Chemicals, Paints	0108		Medical professionals	0604
	Flour & Rice Mills	0109		Nursing Homes	0605
	Food Processing units	0110		Speciality hospitals	0606
	Marble & Granite	0111		Others	0607
	Paper	0112	7. Service sector	Advertisement agencies	0701
	Petroleum and Petrochemicals	0113		Beauty Parlours	0702
	Power and energy	0114		Consultancy services	0703
	Printing & Publishing	0115		Courier Agencies	0704
	Rubber	0116		Computer/training/educational and coaching i	0705
	Steel	0117		Forex Dealers	0706
	Sugar	0118		Hospitality services	0707
	Tea, Coffee	0119		Hotels	0708
	Textiles, handloom, Power looms	0120		I.T. Enabled services, BPO service providers	0709
	Tobacco	0121		Security agencies	0710
	Tyre	0122		Software development agencies	0711
	Vanaspati & Edible Oils	0123		Transporters	0712
	Others	0124		Travel agents, tour operators	0713
				Others	0714
2. Trading	Chain Stores	0201	8. Financial Service	Banking Companies	0801
	Retailers	0202		Chit Funds	0802
	Wholesalers	0203		Financial Institution	0803
	Others	0204		Financial service providers	0804
3. Commission Agents	General Commission Agents	0301		Leasing Companies	0805
				Money Lenders	0806
4. Builders	Builders	0401		Non-Banking Finance Companies	0807
	Estate Agents	0402		Share Brokers, Sub-brokers etc.	0808
	Property Developers	0403		Others	0809
	Others	0404	9. Entertainment	Cable T.V. productions	0901
				Film distribution	0902
				Film laboratories	0903
				Motion Picture Producers	0904
				Television Channels	0905
				Others	0906

Report of the Task Force on Goods and Services Tax
Thirteenth Finance Commission

VALUE OF OUTPUT

TABLE-12 : CROSS CLASSIFICATION OF OUTPUT/VALUE ADDED BY KIND OF ECONOMIC ACTIVITY					
Sl.No	Industry		Gross Output	Intermediate Consumption	Gross Domestic Product
			2007-08	2007-08	2007-08
1	Agriculture, forestry & fishing				
	a	Agriculture	918846	192105	726742
	b	Forestry & Logging	32299	3039	29260
	c	Fishing	42178	6499	35679
	d	Total	993323	201643	791681
2	Mining & Quarrying		155075	36777	118298
3	Manufacturing				
	a	Registered			504253
	b	Unregistered			225875
	c	Total	3404517	2674389	730128
4	Electricity, Gas & Water supply		189288	107868	81420
5	Construction		1070400	692732	377668
6	Trade, Hotels & Restaurants				
	a	Trade	NA	NA	650663
	b	Hotes & Restrurants	NA	NA	71350
	c	Total	993621	271608	722013
7	Transport, Storage & Communication				
	a	Railways	72838	27294	45545
	b	Transport by other means	584385	348728	235657
	c	Storage	6587	3907	2681
	d	Communication	118937	22843	96094
	e	Total	782747	402772	379977
8	Financing, Insurance, Real Estate & Business services				
	a	Banking & Insurance	274316	31912	242404
	b	Real estate, Ownership of dwellings & business services	423493	57105	366388
	c	Total	697809	89017	608792
9	Community, Social & Personal services				
	a	Public administration & defence	333098	91131	241967
	b	Other services	569906	222397	347509
	c	Total	903004	313528	589476
10	Total (Allsectors)		9189784	4790333	4399451
11	GST Comparable Sectors [10-1d-(0.5*9b)]		7578410	4386362	3192050.5
Source: CSO					

Report of the Task Force on Goods and Services Tax Thirteenth Finance Commission

TIMELINE FOR IMPLEMENTATION

Timeline for Implementation of GST													
Sl. No	Activities	Jan	Feb	Mar	Apr	May	Jun	July	Aug	Sept	Oct	Nov	Dec
1	Adoption of the GST Model by Centre and States												
2	Amendments to the Constitution												
a	To be carried out by the Centre												
b	To be approved by the States												
3	Other Legislation & Rules												
a	Finalise draft tax law												
b	Auxiliary law												
c	Draft rules												
d	Ministry of Law review												
e	Obtain approval of the Union/State Cabinet												
f	Obtain Legislative Approval/ Issue Ordinance												
g	Obtain President's/Governor's Assent												
4	Publicity & Outreach												
a	Private sector discussion on Model and draft Law/Rules												
b	Private sector consultation on operation												
c	Copies for trade/professions												
d	Seminar for trade/professions												
e	Finalise GST guide for trade and Industry												
f	Finalise dealers' registration leaflet												
5	Advertising												
a	Registration advertising												
b	Implementation advertising												
c	Payment advertising												
6	Organisational												
a	Finalize Organizational Structure												
b	Finalize estimation of no. of taxpayers												
c	Finalize on no. of Officers and Staff for the Organization												
d	Appoint Officers and staff to administer												
e	Appoint Managerial and Supervisory Staff and Officers												
f	Appoint Auditors & Processors												
g	Appoint Date entry staff												
h	Appoint Recovery Officers and Staff												
7	Operational												
a	Design audit system												
b	Design registration system												
c	Design returns/payment/processing system												
8	Forms												
a	Finalise registration application form												
b	Finalise registration certificate												
c	Finalise payment and return form												
9	IT Infrastructure												
a	Appoint official-level Team for building IT Infrastructure												
b	Appoint Professional Consultant												
c	Finalise IT Architecture and RFP documents												
d	Appoint Vendor												
e	Complete user specifications of all business processes												
f	Develop registration system												
g	Test and load registration system												
h	Develop Payments and Tax Accounting system												
i	Test and load payments and Tax Accounting Systems												
j	Develop, test and load other business process modules												
10	Manuals												
a	Prepare Staff manual												
b	Prepare supplementry manual												
c	Prepare audit and compliance manual												
11	Training Delivery												
a	Preliminary training												
b	General training												
c	Audit traning delivery												
12	Registration and implementation												
a	Issue registration application forms												
b	Issue registration certificates												
c	Conduct advisory visits												
d	Issue first return forms												
e	Receive first payments												
f	Identify defaulters												
g	Pursue defaulters												
13	Monitoring cell												
a	Follow price movements												
b	Inform traders												
c	Action taken												

Report of the Task Force on Goods and Services Tax Thirteenth Finance Commission

Responsibility and Accountability for various Activities relating to Implementation of GST				
Sl. No	Activities	Centre	States	Empowered Committee
1	Adoption of the GST Model by Centre and States			
2	Amendments to the Constitution			
a	To be carried out by the Centre			
b	To be approved by the States			
3	Other Legislation & Rules			
a	Finalise draft tax law			
b	Auxiliary law			
c	Draft rules			
d	Ministry of Law review			
e	Obtain approval of the Union/State Cabinet			
f	Obtain Legislative Approval/ Issue Ordinance			
g	Obtain President's/Governor's Assent			
4	Publicity & Outreach			
a	Private sector discussion on Model and draft Law/Rules			
b	Private sector consultation on operation			
c	Copies for trade/professions			
d	Seminar for trade/professions			
e	Finalise GST guide for trade and Industry			
f	Finalise dealers' registration leaflet			
5	Advertising			
a	Registration advertising			
b	Implementation advertising			
c	Payment advertising			
6	Organisational			
a	Finalize Organizational Structure			
b	Finalize estimation of no. of taxpayers			
c	Finalize on no. of Officers and Staff for the Organization			
d	Appoint Officers and staff to administer			
e	Appoint Managerial and Supervisory Staff and Officers			
f	Appoint Auditors & Processors			
g	Appoint Date entry staff			
h	Appoint Recovery Officers and Staff			
7	Operational			
a	Design audit system			
b	Design registration system			
c	Design returns/payment/processing system			
8	Forms			
a	Finalise registration application form			
b	Finalise registration certificate			
c	Finalise payment and return form			
9	IT Infrastructure			
a	Appoint official-level Team for building IT infrastructure			
b	Appoint Professional Consultant			
c	Finalise IT Architecture and RFP documents			
d	Appoint Vendor			
b	Complete user specifications of all business processes			
c	Develop registration system			
d	Test and load registration system			
f	Develop Payments and Tax Accounting system			
g	Test and load payments and Tax Accounting Systems			
h	Develop, test and load other business process modules			
10	Manuals			
a	Prepare Staff manual			
b	Prepare supplementary manual			
c	Prepare audit and compliance manual			
11	Training Delivery			
a	Preliminary training			
b	General training			
c	Audit training delivery			
12	Registration and implementation			
a	Issue registration application forms			
b	Issue registration certificates			
c	Conduct advisory visits			
d	Issue first return forms			
e	Receive first payments			
f	Identify defaulters			
g	Pursue defaulters			
13	Monitoring cell			
a	Follow price movements			
b	Inform traders			
c	Action taken			

Terms of Reference of the Task Force

The Task Force shall examine the impact of the proposed implementation of the Goods and Services Tax (GST) with effect from 01.04.2010. For this purpose, it shall examine, inter alia, -

- (a) the GST model best suited for the country;
- (b) the modalities of the implementation of GST including threshold limits, composition limits, treatment of inter-state transactions, place of supply rules;
- (c) the potential tax base of the GST as exhaustively as possible and determine an appropriate revenue neutral rate for the Centre and the states;
- (d) suggest ways to incentivize states to adopt a model GST; and
- (e) recommend a framework for administering the GST including payment of compensation, monitoring of compliance and institutional mechanism for making any change in the initial design of the GST.

References

Ahmad, Ehtisham (2008): **“Tax Reforms and the Sequencing of Intergovernmental Reforms in China: Preconditions for a Xiaokang Society”** in Louo Jiwei and Wang Shuilin (eds), *Fiscal Reforms in China*, The World Bank.

Ahmad, Ehtisham, Satya Poddar A.M. Abdel-Rahman, Rick Matthews, and Christopher Waerzeggers (2008): **“Indirect Taxes for the Common Market”**, Report to the GCC Secretariat.

Ahmad, E and Nicholas Stern (1984): **“The theory of tax reform and Indian indirect taxes”**, *Journal of Public Economics*, 25, 259-98.

---and Nicholas Stern (1991): **“The Theory and Practice of Tax Reform in Developing Countries”**, Cambridge University Press.

Aujean, Michel, Peter Jenkins and Satya Poddar (1999): **“A New Approach to Public Sector Bodies”**, 10 *International VAT Monitor* 144 (1999).

Bagchi, Amresh et al (1994): **“Reform of Domestic Trade Taxes in India: Issues and Options”**, National Institute of Public Finance and Policy, New Delhi.

Barrand, Peter (1991): **“The treatment Non-Profit Bodies and Government Entities under the New Zeland GST”**, *International VAT Monitor*, January 1991.

Bird, Richard M. (1994): **“Where Do We Go From Here? Alternatives to the GST”**, KPMG, Toronto, April.

---(1996): **“Harmonized Sales Tax”**, Technical Paper, Department of Finance, Ottawa.

---(1998): **“Dual VAT and Cross-Border Trade: Two Problems, One solution”**, *International Tax and Public Finance*, 5(3) July, pp.429-442.

---(2000): **“CVAT, VIVAT and Dual VAT: Vertical Sharing and Inter-State Trade”** mimeo, (Revised).

---(2001): **“VATs in Federal Countries : International Experience and Emerging Possibilities”**, *International Bureau of Fiscal Documentation*, July, pp.293-309.

Bird, Richard M. and P.P. Gendron (1998): **“Dual VATs and Cross-Border Trade: Two Problems One Solution?”** *International Tax and Public Finance*, Vol. 5, No.3, Kluwer Academic Publishers, Boston, July, pp.429-442.

---and P.P. Gendron (2006): **“Is VAT the Best Way to Impost a General Consumption Tax in Developing Countries?”** *ITP Paper 0602, International Tax Program*, Institute for International Business, University of Toronto.

--- and Pierre-Pascal Gendron (2007): **“The VAT in Developing and Transition Countries”**, Cambridge University Press, Cambridge.

--- and Michael Smart (2008): **“Impact on Investment of Replacing a Retail Sales Tax by a Value-Added Tax: Evidence from Canadian Experience”**, *Working Paper No. 15*, the Institute of International Business, University of Toronto.

Boesters et al: **“Economic Effects of VAT Reform in Germany”**, Discussion paper No. 06030, ZEW, Centre for European Economic Research.

Buckett, Alan (1992): **“VAT in the European Community”**, Butterworths, London.

Burgess, Robin, Stephen Howes and Nicholas Stern(1993): **“Tax Reforms of Indirect Taxes in India”**, Discussion Paper No. EF No.7 of the Suntory-Toyota International Centre for Economic Research and Related Disciplines, London School of Economics, London.

Canada Department of Finance (1987): **“Federal Sales Tax Reform”**, Government of Canada, 1987.

Canada (1996): **“Harmonized Sales Tax”**, Technical Paper, Department of Finance, Ottawa.

Cnossen, Sijbren (2001) **“Tax Policy in the European Union: A Review of Issues and Options”** Erasmus University, Rotterdam.

---(1993): **“VAT Treatment of Immovable Property”**, *The Value Added Tax: Coming to America?*

Desai, Mihir A. and James R. hines (2002): **“Value-Added Taxes and International Trade: The Evidence”**.

Devarajan et al (1991): **“A Value-Added Tax (VAT) in Thailand: Who Wins and Who Loses?”**, *TDRI Quarterly Review*, 6(1).

Ebrill, Liam P, Keen, Michael J. Bodin, Jean-Paul and Summers, Victoria P. (2001): **“The Modern VAT”**, International Monetary Fund, Washington D.C.

Empowered Committee of State Finance Ministers (2008): **“A Model Roadmap for Goods and Services Tax in India”**, New Delhi.

---(2009): **“Model for Monitoring Interstate Transactions of Goods under proposed Goods and Services Tax”**, Report of Sub-Working Group-III, New Delhi.

Emran, M. Shahe and Joseph E. Stiglitz (2005): **“On selective indirect tax reform in developing countries”**, *Journal of Public Economics* 89 (2005) 599-623,

Ernst & Young (1998): **“Value Added Tax: A Study on the application of VAT to the non-profit sector and Public Bodies”**.

Evans, Michael (2009): **“The Value-Added Tax Treatment of Financial Services and Real Property”**, International Seminar on GST Architecture in a Federal System.

European Community (1987): **“Completing the Internal Market – The Introduction of VAT Clearing Mechanism for Intra-Community Sales”**, pp.7

Government of India (1953-54): **“Report of the Taxation Enquiry Commission”**, Ministry of Finance (Department of Economic Affairs), New Delhi.

--- (1978): **“Report of the Indirect Taxation Enquiry Committee”**, Ministry of Finance, New Delhi.

---(1990): **“Report of the Working Group for Review of the Modvat Scheme”**, Ministry of Finance, New Delhi.

---(1991-92): **“Tax Reforms Committee, Interim and Final Reports”**, Ministry of Finance, New Delhi.

---(1998): **“Report of the Finance Ministers Committee to Chart a Time Path for the Introduction of VAT”**, Ministry of Finance, New Delhi.

---(1999): **“Report of the Committee of Finance Secretaries for Identification of Backward Areas”**, Ministry of Finance New Delhi.

---(2001): **“Report of the Advisory Group on Tax Policy and Tax Administration for the Tenth Plan”**, Planning Commission, New Delhi.

---(2002): **“Report of the Task Force on Indirect Taxes”**, Ministry of Finance, New Delhi.

---(2004): **“Report of the Task Force on Implementation of the Fiscal Responsibility and Budget Management Act, 2003”** Ministry of Finance, New Delhi.

--- (2007): Input flow matrix 2006-07, at factor cost from IOTT 2006-07 – Central Statistical Organization (CSO), Ministry of Statistics & Programme Implementation, Government of India.

(2007): **“Report of the Joint Working Group on Goods and Services Tax, submitted to the Empowered Committee of State Finance Ministers”**, New Delhi.

---(2008): **“A Model and Road Map for Goods and Services Tax in India”**, New Delhi.

---(2008): **“Input-Output Transactions Table 2003-04”** , Central Statistical Organisation, Ministry of Statistics & Programme Implementation, New Delhi.

---(2008): **“National Accounts Statistics”**, Central Statistical Organisation, Ministry of Statistics & Programme Implementation, New Delhi.

---(2009): **“Input-Output Transactions Table 2006-07”** , Central Statistical Organisation, Ministry of Statistics & Programme Implementation, New Delhi.

---(2009): Statement No. (76.3), share of unorganized segment in net domestic product- National Accounts Statistics (NAS).

---(2009): IOTT, 2003-04- National Accounts Statistics (NAS).

---(2009): Statement No.(36) Government Final Consumption Expenditure by purpose- National Accounts Statistics (NAS)

---(2009): Statement No. (19), capital formation by type of asset and by type of institutions-National Accounts Statistics (NAS).

---(2009): Statement No. .(36) Government Final Consumption Expenditure by purpose- National Accounts Statistics (NAS).

Government of Karnataka (2001): **“Final Report of the Tax Reforms Commission”**, Finance Department, Bangalore.

Hamilton, Bob and Chun-Yan Kuo (1991): **“The Goods and Services Tax: A General Equilibrium Analysis”**, Canadian Tax Journal, 39(1).

Keen, Michael (2009) : **“What makes a successful VAT?”**, Presentation at the Workshop, National Institute of Public Finance and Policy, New Delhi.

Keen, Michael and Stephen Smith (2000): **“Viva VIVAT!”**, *International Tax and Public Finance*, Vol. 7, 741-751

--- and Stephen Smith (2000): **“VIVAT, CVAT and All That: New Forms of Value Added Tax for Federal Systems”**, *Canadian Tax Journal*, 48, pp.409-424.

--- and Ben Lockwood (2007): **“The value-Added Tax: its Causes and Consequences”**, Economics Working Papers EC)2007/09, European University Institute.

Kelkar, Vijay et al (2004): **“Report on Implementation of the Fiscal Responsibility and Budget Management Act, 2003”**, Ministry of Finance, Government of India, New Delhi.

---(2009a): **“Convocation Address at the Indira Gandhi Institute of Development Research”**, IGIDR, Mumbai, 6 February.

--- (2009b): **“GST for Accelerated Economic growth and Competitiveness”**, Special Address at 3rd National Conference of ASSOCHAM, New Delhi, 29 June.

Kuo, C.Y., Tom McGirr, Satya Poddar (1988): **“Measuring the Non-neutralities of Sales and Excise Taxes in Canada”**, *Canadian Tax Journal*, 38, 1988.

Longo, C.A. (1992): **“Federal problems with VAT in Brazil”**, paper presented at the *International Conference on Tax Reforms*, NIPFP, New Delhi.

McLure, Charles (1993): **“The Brazilian Tax Assignment: Ends, Means and Constraints”**, in *A Reforma Fiscal No Brasil*, proceedings of the International Symposium on Fiscal Reform, Sao Paulo.

---(1998): **“Electronic Commerce and the Tax Assignment Problem: Preserving State Sovereignty in a Digital World”**, *State tax Notes*, 14(15), pp 1169-81.

---(2000a): **“Implementing Sub-national Value Added Taxes on Internal Trade : The Compensating VAT (CVAT)”** *International Tax and Public Finance*, 7(6), pp.732-740

---(2000b): **“Implementing sub-national VATs on internal trade: The compensating VAT (CVAT)”**, *International Trade and Public Finance*, Vol 7.

---(2003): **“Harmonizing the RSTs and GST: Lessons from Canada from Canadian Experience”**, Hoover Institution, Stanford University.

Millar, Rebecca (2007): **“Cross-border Services – A Survey of the Issues”**, in Krever, Richard and David While (ed): *GST in Retrospect and Prospect*, Brookers Ltd., New Zealand 2007.

Mintz, Jack M. (1994): **“Canada’s GST: Sales Tax Harmonization is the Key to Simplification”**, *Tax Notes International*, Tax Analysts.

Musgrave, Richard A. (1999): **“Fiscal Federalism”**, pp.155-175 in John M. Buchanan and Richard A. Musgrave, *Public Finance and Public Choice : Two Contrasting Visions of the States*, MIT Press, Mass.USA.

National Institute of Public Finance and Policy (1994): **“Reforms of Domestic Trade Taxes in India – Issues and Options”**, New Delhi.

NCAER (2009): **“Moving to Goods and Services Tax in India: Impact on India’s Growth and International Trade”**, Thirteenth Finance Commission, Government of India.

OECD (2004): **“Report on the Application of Consumption Taxes to the Trade in International Services and Intangibles”**, Centre for Tax policy and Administration, OECD.

--- (2008): **“Revenue Statistics – Special Feature: Taxing Power of Sub-Central Governments (1965-2007)”**, OECD

--- (2008): **“Consumption Tax Trends”**, VAT/GST and Excise Rates, Trends and Administration Issues, OECD.

Poddar, Satya (1990): **“Options for VAT at the State Level”** in Gills, M.C. Shoup and P. Sicat (ed.), *Value Added Taxation in Developing Countries*, The World Bank, Washington D.C.

--- (2001): **“Zero-Rating of Inter-State Sales under a Sub-National VAT: A New Approach”**, paper presented at the 94th Annual Conference of NTA on November 8-10, Baltimore.

--- (2003): **“Consumption Taxes, The Role of the Value Added Tax”**, in Patrick Honohan (ed.) *Taxation of Financial Intermediation: theory and practice in emerging economies*, (World Bank and the Oxford University Press).

---(2007): **“VAT on Financial Services-Searching for a Workable Compromise”**, in Krever Richard and David While (ed): *GST in Retrospect and Prospect*, Brookers Ltd, New Zealand.

- (2009): **“Treatment of Housing under VAT”**, mimeograph, presented at the conference on VAT organized by the American Tax Policy Institute, Washington, Feb.18-19, 2009
- and Nancy Harley (1989): **“Problems in Moving from a Flawed to a Neutral and Broad-Based Consumption Tax”**, *Australian Tax Forum*, Volume 6, Number 3, 1989.
- and M. English (1997): **“Taxation of financial services under a value-added tax: Applying the cash-flow method,”** *National Tax Journal*, pp.89-111.
- and Eric Hutton, (2001): **“Zero-Rating of Inter-State Sales Under a Sub-national VAT: A New Approach”**, Paper presented at the National Tax Association, 94th Annual Conference on Taxation, Baltimore, November 8-10, 200.
- and Amresh Bagchi (2007): **“Revenue-neutral rate for GST”**, *The Economic Times*, November 15, 2007.
- and Ehtisham Ahmad (2009): **“GST Reforms and Intergovernmental Considerations in India”**, Department of Economic Affairs, Ministry of Finance, Government of India.
- Purohit, Mahesh C. and Vishnu Kanta Purohit (2009): **“Goods and Services Tax in India: Estimating Revenue Implications of the Proposed GST”**, Thirteenth Finance Commission, Government of India.
- Rao, M. Govinda (1998): **“Model Statute for Value Added Sales Tax in India”**, New Delhi.
- (2001): **“Report of the Expert Group on Taxation of Services”**, Government of India, March, 2001.
- (2008): **“Unfinished Reform Agendum: Fiscal Consolidation and Reforms - A comment”** in Jagdish Bhagwati and Charles W. Colomiris, *Sustaining India’s Growth Miracle* Columbia Business School, 2008 pp.104-114
- Rao, M. Govinda and R. Kavita Rao (2006): **“Trends and Issues in Tax Policy and Reform in India”** *India Policy Forum – 2005-06, NCAER-Brookings Institution*.
- Shankar (2005): **“Thirty Years of Tax Reform in India”**, *Economic and Political Weekly*.
- Shome Parthasarathi (1992): **“Trends and Future Directions in Tax Policy Reforms: A Latin American Perspective”**, Bulletin for International Fiscal Documentation (DIFD), Amsterdam.
- (2002): **“India’s Fiscal Matters”**, Oxford University Press, New Delhi.

---(2003): **“Tax Policy and Development of a Single Tax System”**, Bulletin for International Fiscal Documentation (DIFD), Amsterdam.

Singh, Nirmal (2009): **“Rationalizing Taxation of Petroleum Products”**, National Institute of Public Finance and Policy, New Delhi.

Smart and Bird (2006): **“The GST Cut and Fiscal Imbalance”**, ITP Paper 0604, International Tax Programme, Institute for International Business, University of Toronto.

Spiro, Peter S. (1993): **“Evidence of a Post-GST Increase in the Underground Economy”**, Canadian Tax Journal, Vol.41, No.2, pp.247-58

Tait, Alan A. (1988): **“Value Added Tax: International Practice and Problems”**, International Monetary Fund, Washington D.C.

Varsano, Richardo (2000): **“Sub-national Taxation and the Treatment of Interstate Trade in Brazil: Problems and Proposed Solutions”** pp.339-56 I S.J. Burki et al.(eds.) *Decentralization and Accountability of Public Sector*, proceedings of the Annual Bank Conference on Development in Latin America and the Caribbean, World Bank, Washington D.C.

Comments of the Department of Revenue (DoR) on the First Discussion Paper on GST

<u>Sr. No.</u>	<u>Para No. of the Discussion Paper</u>	<u>Issues</u>	<u>Comments of the DoR</u>
1	3.1	It is important to take note of the significant administrative issues involved in designing an effective GST model in a federal system with the objective of having an overall harmonious structure of rates. Together with this, there is a need for upholding the powers of Central and State Governments in their taxation matters. Further, there is also the need to propose a model that would be easily implementable, while being generally acceptable to stakeholders.	Agreed.
2	3.2	Keeping in view the report of the Joint Working Group on Goods and Services Tax, the views received from the States and Government of India, a dual GST with defined functions and responsibilities of the Centre and the States is recommended. An appropriate mechanism that will be binding on both the Centre and the States should be worked out whereby the harmonious rate structure along with the need for further modification could be upheld, if necessary with a collectively agreed Constitutional Amendment.	Dual GST model with appropriate binding mechanism to harmonise the various important aspects of the GST like rate structure, taxation base, exemption etc. between Centre and States is agreed.
3	3.2 (i)	The GST shall have two components: one levied by the Centre (hereinafter referred to as Central GST), and the other levied by the States [hereinafter referred to as State GST]. Rates for Central GST and State GST should be prescribed appropriately, reflecting revenue considerations and acceptability. This dual GST model would be implemented through multiple statutes (one for CGST and a 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. should be uniform across these statutes as far as practicable.	Agreed. In addition, IGST on inter-State transactions should be levied by the Centre. SGST on imports should also be levied and collected by the Centre. Centre should pass on SGST collection on imports to concerned States on the destination principle.

4	3.2 (ii)	The Central GST and the State GST should be applicable to all transactions of goods and services made for a consideration except the exempted goods and services, goods are outside the purview of GST and the transactions which are below the prescribed threshold limits.	Agreed. There should be a common base for taxation between Centre and States.
5	3.2 (iii)	The Central GST and State GST are to be paid to the accounts of the Centre and the States separately. It would have to be ensured that account-heads for all services and goods would have indication whether it relates to Central GST or State GST (with identification of the State to whom the tax is to be credited).	Agreed. In addition, IGST should be paid to the accounts of the Centre.
6	3.2 (iv)	Since the Central GST and State GST are to be treated separately, taxes paid against the Central GST shall be allowed to be taken as input tax credit (ITC) for the Central GST and could be utilized only against the payment of Central GST. The same principle will be applicable for the State GST. 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 Central GST and the State GST would be aligned.	Agreed.
7	3.2 (v)	Cross utilization of ITC between the Central GST and the State GST should not be allowed except in the case of inter-State supply of goods and services under the IGST model which is explained later.	Agreed.
8	3.2 (vi)	Ideally, the problem related to credit accumulation on account of refund of GST should be avoided both by the Centre and the States except in the cases such as of exports, purchase of capital goods, input tax at higher rate than output tax etc. where, again refund/adjustment should be completed in a time bound manner.	Agreed.
9	3.2 (vii)	To the extent feasible, uniform procedure for collection of both Central GST and State GST may be prescribed in the respective legislation for Central GST and State GST.	Agreed.
10	3.2 (viii)	The administration of the Central GST to the Centre and for State GST to the States would be given. This would imply that the Centre and the States would have concurrent jurisdiction for the entire value chain and for all taxpayers on the basis of thresholds for goods and services prescribed for the States and the Centre.	Agreed. The threshold for goods and services should be common between Centre and State on one hand and between goods and services on the other.

11	3.2 (ix)	The present thresholds prescribed in different State VAT Acts below which VAT is not applicable varies from State to State. A uniform State GST threshold across States is desirable and, therefore, it is recommended that a threshold of gross annual turnover of Rs.10 lakh both for goods and services for all the States and Union Territories may be adopted with adequate compensation for the States (particularly, the States in North-Eastern Region and Special Category States) where lower threshold had prevailed in the VAT regime. Keeping in view the interest of small traders and small scale industries and to avoid dual control, the States also considered that the threshold for Central GST for goods may be kept Rs.1.5 Crore and the threshold for Central GST for services may also be appropriately high. It may be mentioned that even now there is a separate threshold of services (Rs. 10 lakh) and goods (Rs. 1.5 crore) in the Service Tax and CENVAT.	There should be a uniform threshold for goods and services for both SGST and CGST. This annual turnover threshold could be Rs.10 lakh or even more than that. The threshold exemption should not apply to dealers and service providers who undertake inter-State supplies. The problem of dual control is better addressed through a compounding scheme as well as administrative simplification for small dealers through measures such as: • Registration by single agency for both SGST and CGST without manual interface • No physical verification of premises and no pre-deposit of security • Simplified return format • Longer frequency for return filing • Electronic Return filing through certified service centres / CAs etc. • Audit in 1-2% cases based on risk parameters • Lenient penal provisions There may not be any need to have direct link between compensation package, if decided for, and the threshold for registration for North-Eastern and special category States.
12	3.2 (x)	The States are also of the view that Composition / Compounding Scheme for the purpose of GST should have an upper ceiling on gross annual turnover and a floor tax rate with respect to gross annual turnover. In particular there will 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 should also allow option for GST registration for dealers with turnover below the compounding cut-off.	Agreed. Centre may also have a Composition Scheme up to gross turnover limit of Rs. 50 lakh, if threshold for registration is kept as Rs.10 lakh. The floor rate of 0.5% will be for SGST alone, in case Centre also brings a Composition Scheme for small assesses. The Centre may consider leaving the administration of Compounding Scheme, both for CGST and SGST to the States.

13	3.2 (xi)	The taxpayer would need to submit periodical returns, in common format as far as possible, to both the Central GST authority and to the concerned State GST authorities.	In addition, taxpayers having inter-State transactions will require submission of returns to related Central IGST authority.
14	3.2 (xii)	Each taxpayer would 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.	There should be a uniform registration system through-out the country and this registration system should enable easy linkage with Income Tax database through use of PAN number.
15	3.2 (xiii)	Keeping in mind the need of taxpayers convenience, 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.	Since the tax base is to be identical for the two components, viz., CGST and SGST, it is desirable that any dispute between a taxpayer and either of the tax administrations is settled in a uniform manner. The possibility of setting up a harmonised system for scrutiny, audit and dispute settlement may be developed.
16	3.4	On application of the principle, it is recommended that the following Central Taxes should be, to begin with, subsumed under the Goods and Services Tax: (i) Central Excise Duty (ii) Additional Excise Duties (iii) The Excise Duty levied under the Medicinal and Toiletries Preparation Act (iv) Service Tax (v) Additional customs duty, commonly known as countervailing duty (CVD) (vi) Special Additional Duty of Customs - 4% (SAD) (vii) Surcharges, and (viii) Cesses.	Agreed.

		Following State taxes and levies should be, to begin with, subsumed under GST: (i) VAT / Sales tax (ii) Entertainment tax (unless it is levied by the local bodies). (iii) Luxury tax (iv) Taxes on lottery, betting and gambling. (v) State Cesses and Surcharges in so far as they relate to supply of goods and services. (vi) Entry tax not in lieu of octroi.	Electricity duty, Octroi, purchase tax and taxes levied by local bodies should also be subsumed under GST.
		Purchase tax: Some of the States felt that they are getting substantial revenue from Purchase Tax and, therefore, it should not be subsumed under GST while majority of the States were of the view that no such exemptions should be given. The difficulties of the food grain producing States and certain other states were appreciated as substantial revenue is being earned by them from Purchase Tax and it was, therefore, felt that in case Purchase Tax has to be subsumed then adequate and continuing compensation has to be provided to such States. This issue is being discussed in consultation with the Government of India.	Purchase tax is nothing but sales tax where the responsibility for collection of tax is with the purchaser (and not with the seller as in the case of sales tax). Keeping 'purchase tax' outside will give the loophole to the States to impose 'purchase tax' on any commodity (food-grains, agricultural / forest produce, minerals, industrial inputs etc.) over and above GST. Hence, purchase tax must be subsumed. The compensation package, if agreed, need not have any link to any particular tax being subsumed.
		Tax on items containing Alcohol: Alcoholic beverages may be kept out of the purview of GST. Sales Tax/VAT can be continued to be levied on alcoholic beverages as per the existing practice. In case it has been made Vatable by some States, there is no objection to that. Excise Duty, which is presently being levied by the States may not be also affected.	Alcoholic beverages should be brought under the purview of GST in order to remove the cascading effect on GST paid on inputs such as raw material and packaging material. Sales tax / VAT and State excise duty can be charged over and above GST. Similar dispensation should apply to opium, Indian hemp and other narcotic drugs and narcotics but medicines or toilet preparations containing these substances should attract only GST.
		Tax on Tobacco products: Tobacco products should be subjected to GST with ITC. Centre may be allowed to levy excise duty on tobacco products over and above GST without ITC.	Agreed.

		Tax on Petroleum Products: As far as petroleum products are concerned, it was decided that the basket of petroleum products, i.e. crude, motor spirit (including ATF) and HSD should be kept outside GST as is the prevailing practice in India. Sales Tax could continue to be levied by the States on these products with prevailing floor rate. Similarly, Centre could also continue its levies. A final view whether Natural Gas should be kept outside the GST will be taken after further deliberations.	Keeping crude petroleum and natural gas out of the GST net would imply that the credit on capital goods and input services going into exploration and extraction would not be available resulting in cascading. Diesel, ATF and motor spirit are derived from a common input, viz., crude petroleum along with other refined products such as naphtha, lubricating oil base stock, etc. Leaving diesel, ATF and motor spirit out of the purview of GST would make it extremely difficult for refineries to apportion the credit on capital goods, input services and inputs. These products are principal inputs for many services such as aviation, road transport, railways, cab operators etc. As such, these may be levied to GST and in select cases credit of GST paid on these items may be disallowed in order to minimize the possibility of misuse.
		Taxation of Services: As indicated earlier, both the Centre and the States will have concurrent power to levy tax on all goods and services. In the case of States, the principle for taxation of intra-State and inter-State has already been formulated by the Working Group of Principal Secretaries/Secretaries of Finance / Taxation and Commissioners of Trade Taxes with senior representatives of Department of Revenue, Government of India. For inter-State transactions an innovative model of Integrated GST will be adopted by appropriately aligning and integrating CGST and SGST.	The sub-working group of the Empowered Committee in its report has suggested two options each for B to B and B to C transactions. A decision is required to be taken by the Empowered Committee with respect to the option to be adopted. Such a decision may be taken and communicated to DoR.
17	3.5	Inter-State Transactions of goods & services: The Empowered Committee has accepted the recommendations of the Working Group of concerned officials of Central and State Governments for adoption of IGST model for taxation of inter-State transaction of Goods and Services The scope of IGST Model is that Centre 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.	Agreed. It may however be noted that IGST model will work smoothly only when there is a common threshold for goods and services and for Centre and States. Having more than one rate either for CGST or SGST will complicate the working of IGST model.

		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 is also 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. The major advantages of IGST Model are: - Maintenance of uninterrupted ITC chain on inter-state transactions. - No upfront payment of tax or substantial blockage of funds for the inter-state seller or buyer. - No refund claim in exporting State, as ITC is used up while paying the tax. - Self monitoring model. - Level of computerization is limited to inter-state dealers and Central and State Governments should be able to computerize their processes expeditiously. - As all inter-state dealers will be e-registered and correspondence with them will be by e-mail, the compliance level will improve substantially. - Model can take 'Business to Business' as well as 'Business to Consumer' transactions into account.	

18	3.6	GST Rate Structure: The Empowered Committee has decided to adopt a two-rate structure – a 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. For upholding of special needs of each State as well as a balanced approach to federal flexibility, and also for facilitating the introduction of GST, it is being discussed whether 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. It is also being discussed whether the Government of India may adopt, to begin with, a similar approach towards exempted list under the CGST.	There should be a single rate of SGST both for goods and services. A two rate structure for goods would pose the following problems: a) Likelihood of inversions in duty structure with raw materials and intermediates being at a higher rate and finished goods being at a lower rate, especially as the intention is to apply the lower rate to necessities. b) Inversions would result in input credit accumulation and demand for refunding the same from time to time. c) The general rate (RNR) would have to be higher than under a single rate structure. d) Currently, services are chargeable to tax at a single rate. Adopting a dual rate for goods would generate a similar demand for services too. e) Having different rates for goods and services would imply that the distinction between goods and services should continue. Around 99 items presently exempted under VAT may continue to remain exempted in GST regime. There should be no scope, with individual States, for expansion of this list even for goods of local importance. Efforts will be made by Centre to substantially reduce the number of items presently exempted under CENVAT regime. At the end, there must be a common list of exemptions for CGST and SGST.

		The States are of the view that for CGST relating to goods, the Government of India may also 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.	There should be one CGST rate both for goods as well as services.
		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.	SGST and CGST rates are required to be put in public domain much before initiation of legislative action.
19	3.7	Zero Rating of Exports: Exports should be zero-rated. Similar benefits may be given to Special Economic Zones (SEZs). However, such benefits should only be allowed to the processing zones of the SEZs. No benefit to the sales from an SEZ to Domestic Tariff Area (DTA) will be allowed.	Agreed.
20	3.8	GST on Imports: The GST is proposed to be levied on imports with necessary Constitutional Amendments. Both CGST and SGST will be levied on import of goods and services into the country. The incidence of tax will follow the destination principle and the SGST amount will accrue to the State where the imported goods and services are consumed. Full and complete set-off will be available on the GST paid on import on goods and services.	Levy of GST on imports may be handled by Centre through a Central legislation either as a customs duty (as is being done now) or along the lines of IGST. SGST collected by Centre may be passed on to concerned State following the destination principle. Taxation of import of services may be on the basis of reverse charge model, as is being done at present.
21	3.9	Special Industrial Area Scheme: After the introduction of GST, the tax exemptions, remissions etc. related to industrial incentives and special industrial area schemes should be converted, if at all needed, into cash refund or subsidy schemes after collection of tax, so that the GST scheme on the basis of a continuous chain of set-offs is not disturbed. Regarding Special Industrial Area Schemes, it is clarified that the benefits of such exemptions, remissions etc. would continue up to legitimate expiry time both for the Centre and the States. Any new exemption, remission etc. or continuation of earlier exemption, remission etc. would not be allowed. In such cases, the Central and the State Governments could provide reimbursement after collecting GST.	Agreed.
22	3.10	IT Infrastructure: After acceptance of IGST Model for Inter-State transactions, the major responsibilities of IT infrastructural	Agreed.

		requirement will be shared by the Central Government through the use of its own IT infrastructure facility. The issues of tying up the State Infrastructure facilities with the Central facilities as well as further improvement of the States' own IT infrastructure, including TINXSYS, is now to be addressed expeditiously and in a time bound manner.	
23	3.11	Constitutional amendments, legislations and rules for administration of CGST and SGST: It is essential to have Constitutional Amendments for empowering the States for levy of service tax, GST on imports and consequential issues as well as corresponding Central and State legislations with associated rules and procedures. With these specific tasks in view, a Joint Working Group has recently been constituted (September 30, 2009) comprising of the officials of the Central and State Governments to prepare, in a time bound manner a draft legislation for Constitutional Amendment, draft legislation for CGST, a suitable Model Legislation for SGST and rules and procedures for CGST and SGST. Simultaneous steps have also been initiated for drafting of a legislation for IGST and rules and procedures. As a part of this exercise, the Working Group may also address the issues of dispute resolution and advance ruling.	The Joint Working Group (JWG) has held several meetings by now. Department of Revenue is closely working with Ministry of Law, Government of India, for finalisation of draft Constitutional amendment. The issue of empowering States to levy GST on imports has been deliberated by the JWG and the view which has emerged out of discussion is that the Centre shall collect GST on imports and pass on the SGST component of it to concerned State on destination principle.
24	3.12	Harmonious structure of GST and the States' autonomy in federal framework: As a part of the exercise on Constitutional Amendment, there would be, as mentioned earlier, in para 3.2, a special attention to the formulation of a mechanism for upholding the need for a harmonious structure for GST along with the concern for the States' autonomy in a federal structure.	Agreed in principle.
25	3.13	Dispute Resolution & Advance Rulings: As a part of the exercise on drafting of legislation, rules and procedures for the administration of CGST and SGST, specific provisions will also be made to the issues of dispute resolution and advance ruling.	The provisions related to dispute resolution, advance rulings and other business processes need to be harmonised between Centre and States.
26	3.14	Need for compensation during implementation of GST: Despite the sincere attempts being made by the Empowered Committee on the determination of GST rate structure, revenue neutral rates, it is difficult to estimate accurately as to how much the States will gain from service taxes and how much they will lose on account of	Empowered Committee has already referred the issue to the Thirteenth Finance Commission (TFC). TFC is likely to submit its report shortly. A view on the subject will be taken after more clarity on the subject is

		removal of cascading effect, payment of input tax credit and phasing out of CST. In view of this, it would be essential to provide adequately for compensation for loss that may emerge during the process of implementation of GST for the next five years. This issue may be comprehensively taken care of in the recommendations of the Thirteenth Finance Commission. The payment of this compensation will need to be ensured in terms of special grants to be released to the States duly in every month on the basis of neutrally monitored mechanism.	available.
27	3.15	With this First Discussion Paper and the Annexure on frequently asked Questions and Answers on GST, interaction with the representatives of industry, trade and agriculture would begin immediately at the national level, and then also simultaneously at the State levels. Similarly awareness campaign for common consumers would also be initiated at the same time. As a part of the discussion and campaign the views of the industry, trade and agriculture as well as consumer may be sought to be obtained in a structured and time bound manner.	Empowered Committee may prepare a plan with clear timelines for orientation of stakeholders so that required steps may be taken by all the States in time.

**First Discussion Paper
On
Goods and Services Tax
In India**



**The Empowered Committee
Of
State Finance Ministers**

**New Delhi
November 10 , 2009**

Foreword

If the Value Added Tax (VAT) is considered to be a major improvement over the pre-existing Central excise duty at the national level and the sales tax system at the State level, then the Goods and Services Tax (GST) will be a further significant breakthrough - the next logical step - towards a comprehensive indirect tax reform in the country.

Keeping this overall objective in view, an announcement was made by Shri P. Chidambaram, the then Union Finance Minister in the Central Budget (2007-2008) to the effect that GST would be introduced from April 1, 2010 and that the Empowered Committee of State Finance Ministers, on his request, would work with the Central Government to prepare a road map for introduction of GST in India. After this announcement, the Empowered Committee of State Finance Ministers decided to set up a Joint Working Group (May 10, 2007), with the then Adviser to the Union Finance Minister and the Member-Secretary of Empowered Committee as Co-convenors and the concerned Joint Secretaries of the Department of Revenue of Union Finance Ministry and all Finance Secretaries of the States as its members. This Joint Working Group, after intensive internal discussions as

well as interaction with experts and representatives of Chambers of Commerce and Industry, submitted its report to the Empowered Committee (November 19, 2007).

This report was then discussed in detail in the meeting of Empowered Committee (November 28, 2007). On the basis of this discussion and written observations of the States, certain modifications were made and a final version of the views of Empowered Committee at that stage was prepared and was sent to the Government of India (April 30, 2008). The comments of the Government of India were received on December 12, 2008 and were duly considered by the Empowered Committee (December 16, 2008). It was decided that a Committee of Principal Secretaries/ Secretaries of Finance/Taxation and Commissioners of Trade Taxes of the States would be set up to consider these comments, and submit their views. These views were submitted and were accepted in principle by the Empowered Committee (January 21, 2009). Consequent upon this in-principle acceptance, a Working Group, consisting of the concerned officials of the State Governments was formed who, in close association with senior representatives of the Government of India, submitted their recommendations in detail on the structure of GST. An important interaction has also recently taken place between Shri Pranab Mukherjee, the Union Finance

Minister and the Empowered Committee (October 19, 2009) on the related issue of compensation for loss of the States on account of phasing out of CST. The Empowered Committee has now taken a detailed view on the recommendations of the Working Group of officials and other related matters. This detailed view of the Empowered Committee on the structure of GST is now presented in terms of the First Discussion Paper, along with an Annexure on Frequently Asked Questions and Answers on GST, for discussions with industry, trade, agriculture and people at large.

The Discussion Paper is divided into four sections. Since GST would be further improvement over the VAT, Section 1 begins with a brief reference to the process of introduction of VAT at the Centre and the States and also indicates the precise points where there is a need for further improvement. This section also shows how the GST can bring about this improvement. With this as the background for justification of GST, Section 2 then describes the process of preparation for GST. Thereafter, Section 3 presents in detail the comprehensive structure of the GST model. For illustrating this GST model further, there is in the end an Annexure on Frequently Asked Questions and Answers.

This Discussion Paper has been the result of truly collective efforts on the basis of hardwork of all the

concerned officials of the States, the officials of Empowered Committee Secretariat and the Adviser and officials of the Union Finance Ministry, the counsel and active participation of Finance Ministers and concerned Senior Ministers of the States at each stage, and the encouragement and advice of the Union Finance Minister.

With the release of this First Discussion Paper and the Annexure on Frequently Asked Questions and Answers, we now sincerely invite interaction with the representatives of industry, trade, agriculture and common people. This interaction and campaign will immediately start at the national level and at the State levels. As a part of this interaction, we look forward to receiving the views of industry, trade, agriculture as well as consumers in a time-bound manner.

Asim Kumar Dasgupta
Chairman,
Empowered Committee of
State Finance Ministers
&
Minister of Finance & Excise,
Government of West Bengal

New Delhi,
November 10, 2009

1. Introduction

1.1 Introduction of the Value Added Tax (VAT) at the Central and the State level has been considered to be a major step – an important breakthrough – in the sphere of indirect tax reforms in India. If the VAT is a major improvement over the pre-existing Central excise duty at the national level and the sales tax system at the State level, then the Goods and Services Tax (GST) will indeed be a further significant improvement – the next logical step – towards a comprehensive indirect tax reforms in the country.

1.2 Keeping this objective in view, an announcement was made by the then Union Finance Minister in the Central Budget (2007-08) to the effect that GST would be introduced with effect from April 1, 2010 and that the Empowered Committee of State Finance Ministers, on his request, would work with the Central Government to prepare a road map for introduction of GST in India. After this announcement, the Empowered Committee of State Finance Ministers decided to set up a Joint Working Group (May 10, 2007), with the then Adviser to the Union Finance Minister and Member-Secretary of the Empowered Committee as its Co-convenors and concerned four Joint Secretaries of the Department of Revenue of Union Finance Ministry and all

Finance Secretaries of the States as its members. This Joint Working Group got itself divided into three Sub-Groups and had several rounds of internal discussions as well as interaction with experts and representatives of Chambers of Commerce & Industry. On the basis of these discussions and interaction, the Sub-Groups submitted their reports which were then integrated and consolidated into the report of Joint Working Group (November 19, 2007).

1.3 This report was discussed in detail in the meeting of the Empowered Committee on November 28, 2007, and the States were also requested to communicate their observations on the report in writing. On the basis of these discussions in the Empowered Committee and the written observations, certain modifications were considered necessary and were discussed with the Co-convenors and the representatives of the Department of Revenue of Union Finance Ministry. With the modifications duly made, a final version of the views of Empowered Committee on the model and road map for the GST was prepared (April 30, 2008). These views of Empowered Committee were then sent to the Government of India, and the comments of Government of India were received on December 12, 2008. These comments were duly considered by the Empowered Committee (December 16, 2008), and it was decided that a Committee of Principal Secretaries/ Secretaries of Finance/Taxation

and Commissioners of Trade Taxes of the States would be set up to consider these comments, and submit their views. These views were submitted and were accepted in principle by the Empowered Committee (January 21, 2009). As a follow-up of this in-principle acceptance, a Working Group consisting of the concerned officials of the State Governments was formed who, in association with senior representatives of Government of India, submitted their recommendations in detail on the structure of GST. An important interaction has also recently taken place between Shri Pranab Mukherjee, the Union Finance Minister and the Empowered Committee (October 19, 2009) on the related issue of compensation for loss of the States on account of phasing out of CST. The Empowered Committee has now taken a detailed view on the recommendations of the Working Group of officials and other related matters. This detailed view is now presented in terms of the First Discussion Paper, along with an Annexure on Frequently Asked Questions and Answers on GST, for discussion with industry, trade, agriculture and people at large. Since the GST at the Centre and States would be a further improvement over the VAT, a brief recalling of the process of introduction of VAT in India is worthwhile.

Value Added Tax at the Central and the State level

1.4 Prior to the introduction of VAT in the Centre and in the States, there was a burden of multiple

taxation in the pre-existing Central excise duty and the State sales tax systems. Before any commodity was produced, inputs were first taxed, and then after the commodity got produced with input tax load, output was taxed again. This was causing a burden of multiple taxation (i.e. “tax on tax”) with a cascading effect. Moreover, in the sales tax structure, when there was also a system of multi-point sales taxation at subsequent levels of distributive trade, then along with input tax load, burden of sales tax paid on purchase at each level was also added, thus aggravating the cascading effect further.

1.5 When VAT is introduced in place of Central excise duty, a set-off is given, i.e., a deduction is made from the overall tax burden for input tax. In the case of VAT in place of sales tax system, a set-off is given from tax burden not only for input tax paid but also for tax paid on previous purchases. With VAT, the problem of “tax on tax” and related burden of cascading effect is thus removed. Furthermore, since the benefit of set-off can be obtained only if tax is duly paid on inputs (in the case of Central VAT), and on both inputs and on previous purchases (in the case of State VAT), there is a built-in check in the VAT structure on tax compliance in the Centre as well as in the States, with expected results in terms of improvement in transparency and reduction in tax evasion. For these beneficial effects, VAT has now been introduced in more than 150 countries, including several federal

countries. In Asia, it has now been introduced in almost all the countries.

1.6 In India, VAT was introduced at the Central level for a selected number of commodities in terms of MODVAT with effect from March 1, 1986, and in a step-by-step manner for all commodities in terms of CENVAT in 2002-03. Subsequently, after Constitutional Amendment empowering the Centre to levy taxes on services, these service taxes were also added to CENVAT in 2004-05. Although the growth of tax revenue from the Central excise has not always been specially high, the revenue growth of combined CENVAT and service taxes has been significant.

1.7 Introduction of VAT in the States has been a more challenging exercise in a federal country like India, where each State, in terms of Constitutional provision, is sovereign in levying and collecting State taxes. Before introduction of VAT, in the sales tax regime, apart from the problem of multiple taxation and burden of adverse cascading effect of taxes as already mentioned, there was also no harmony in the rates of sales tax on different commodities among the States. Not only were the rates of sales tax numerous (often more than ten in several States), and different from one another for the same commodity in different States, but there was also an unhealthy competition among the States in terms of sales tax rates – so-called

“rate war” – often resulting in, revenue-wise, a counter-productive situation.

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

Standing Committee of State Finance Ministers was formed which was then made an Empowered Committee of State Finance Ministers.

1.9 Thereafter, the Empowered Committee has met regularly. All the decisions were taken on the basis of consensus. On the strength of these repeated discussions and collective efforts, involving the Ministers and the concerned officials, it was possible within a period of about a year and a half to achieve nearly 98 per cent success in the first objective, namely, harmonisation of sales tax structure through implementation of uniform floor rates of sales tax.

1.10 After reaching this stage, steps were initiated for systematic preparation for introduction of State-level VAT. In order again to avoid any unhealthy competition among the States which may lead to distortions in manufacturing and trade, attempts have been made from the very beginning to harmonise the VAT design in the States, keeping also in view the distinctive features of each State and the need for federal flexibility. This has been done by the States collectively agreeing, through discussions in the Empowered Committee, to certain common points of convergence regarding VAT, and allowing at the same time certain flexibility to accommodate the local

characteristics of the States. In the course of these discussions, references to the Tenth Five Year Plan Report of the Advisory Group on Tax Policies & Tax Administration (2001) and the report of Kelkar (Chairman) Task Force were helpful.

1.11 Along with these measures, steps were taken for necessary training, computerization and interaction with trade and industry. While these preparatory steps were taken, the Empowered Committee got a significant support from Shri P. Chidambaram, the then Union Finance Minister, when he responded positively in providing Central financial support to the States in the event of loss of revenue in transitional years of implementation of VAT.

1.12 As a consequence of all these steps, the States started implementing VAT beginning April 1, 2005. After overcoming the initial difficulties, all the States and Union Territories have now implemented VAT. The Empowered Committee has been monitoring closely the process of implementation of State-level VAT, and deviations from the agreed VAT rates has been contained to less than 3 per cent of the total list of commodities. Responses of industry and also of trade have been indeed encouraging. The rate of growth of tax revenue has nearly doubled from the average

annual rate of growth in the pre-VAT five year period after the introduction of VAT.

Justification of GST

1.13 Despite this success with VAT, there are still certain shortcomings in the structure of VAT both at the Central and at the State level. The shortcoming in CENVAT of the Government of India lies in non-inclusion of several Central taxes in the overall framework of CENVAT, such as additional customs duty, surcharges, etc., and thus keeping the benefits of comprehensive input tax and service tax set-off out of reach for manufacturers/dealers. Moreover, no step has yet been taken to capture the value-added chain in the distribution trade below the manufacturing level in the existing scheme of CENVAT. The introduction of GST at the Central level will not only include comprehensively more indirect Central taxes and integrate goods and service taxes for the purpose of set-off relief, but may also lead to revenue gain for the Centre through widening of the dealer base by capturing value addition in the distributive trade and increased compliance.

1.14 In the existing State-level VAT structure there are also certain shortcomings as follows. There are, for instance, even now, several taxes which are in the nature of indirect tax on goods and services, such as luxury tax, entertainment tax, etc., and yet not

subsumed in the VAT. Moreover, in the present State-level VAT scheme, CENVAT load on the goods remains included in the value of goods to be taxed under State VAT, and contributing to that extent a cascading effect on account of CENVAT element. This CENVAT load needs to be removed. Furthermore, any commodity, in general, is produced on the basis of physical inputs as well as services, and there should be integration of VAT on goods with tax on services at the State level as well, and at the same time there should also be removal of cascading effect of service tax. In the GST, both the cascading effects of CENVAT and service tax are removed with set-off, and a continuous chain of set-off from the original producer's point and service provider's point upto the retailer's level is established which reduces the burden of all cascading effects. This is the essence of GST, and this is why GST is not simply VAT plus service tax but an improvement over the previous system of VAT and disjointed service tax. However, for this GST to be introduced at the State-level, it is essential that the States should be given the power of levy of taxation of all services. This power of levy of service taxes has so long been only with the Centre.

A Constitutional Amendment will be made for giving this power also to the States. Moreover, with the introduction of GST, burden of Central Sales Tax (CST) will also be removed. The GST at the State-level is, therefore, justified for (a) additional power of levy of taxation of services for the States, (b) system of

comprehensive set-off relief, including set-off for cascading burden of CENVAT and service taxes, (c) subsuming of several taxes in the GST and (d) removal of burden of CST. Because of the removal of cascading effect, the burden of tax under GST on goods will, in general, fall.

1.15 The GST at the Central and at the State level will thus give more relief to industry, trade, agriculture and consumers through a more comprehensive and wider coverage of input tax set-off and service tax set-off, subsuming of several taxes in the GST and phasing out of CST. With the GST being properly formulated by appropriate calibration of rates and adequate compensation where necessary, there may also be revenue/ resource gain for both the Centre and the States, primarily through widening of tax base and possibility of a significant improvement in tax compliance. In other words, the GST may usher in the possibility of a collective gain for industry, trade, agriculture and common consumers as well as for the Central Government and the State Governments. The GST may, indeed, lead to the possibility of collectively positive-sum game.

2. Preparation for GST

2.1 Keeping this significance of GST in view, an announcement was made by the then Union Finance Minister in the Union Budget, as mentioned before, to

the effect that GST would be introduced from April 1, 2010, and that the Empowered Committee of State Finance Ministers would work with the Central Government to prepare a road map for introduction of the GST. After this announcement, the Empowered Committee, as stated earlier, had set up a Joint Working Group which submitted a report on a model and road map for GST. After accommodating the views of the States appropriately on this report, the views of the Empowered Committee on the model and road map were sent to the Government of India on 30th April, 2008. The comments of the Government of India were received on 12th December, 2008. These comments were duly considered by the Empowered Committee in its meeting held on 16th December, 2008 and it was decided that a Committee of Principal Secretaries/Secretaries (Finance/Taxation) and Commissioners of Trade Taxes should consider the comments received from the Government of India and submit its views and also work out the Central GST and State GST rates. The Committee held detailed deliberations on 5th and 6th January, 2009, and submitted its recommendations to the Empowered Committee. The Empowered Committee considered these recommendations in its meeting held on 21st January, 2009 and accepted them in principle. The Empowered Committee also decided to constitute a Working Group consisting of Principal Secretaries/Secretaries (Finance/Taxation) and Commissioners of Trade Taxes of all States/UTs to

give their recommendations on (a) the commodities and services that should be kept in the exempted list, (b) the rules and principles of taxing the transactions of services including the transactions in inter-State services, and (c) finalization of the model suggested for inter-state transaction/movement of goods including stock transfers in consultation with the State Bank of India and some other nationalized banks. It was also decided that the senior representatives from the Government of India may also be associated. The Working Group deliberated on the issues on 10th February, 2009 and decided to form three Sub Working Groups to deliberate each item in depth. The Reports of the Working Group on the three issues have already been received, and the Empowered Committee has taken a view on these recommendations for concluding the details of GST structure.

2.2 While making this preparation of GST, it was also necessary, as mentioned earlier, to phase out the CST, because it did not carry any set-off relief and there was a distortion in the VAT regime due to export of tax from one State to other State. The Empowered Committee accordingly took a decision to phase out CST on the understanding with the Centre that, since phasing out of CST would result in a loss of revenue to the States on a permanent basis, an appropriate mechanism to compensate the States for such loss would be worked out. The rate of CST has already been reduced to 2% and will be phased out with effect from the date of introduction of GST on the basis of such

GST structure which, with necessary financial support to the States, should adequately compensate for the loss of the States on a permanent basis. With these steps at preparation in mind, it is important now to turn to the proposed model of GST.

3. Goods & Services Tax Model For India

3.1 It is important to take note of the significant administrative issues involved in designing an effective GST model in a federal system with the objective of having an overall harmonious structure of rates. Together with this, there is a need for upholding the powers of Central and State Governments in their taxation matters. Further, there is also the need to propose a model that would be easily implementable, while being generally acceptable to stakeholders.

Salient features of the GST model

3.2 Keeping in view the report of the Joint Working Group on Goods and Services Tax, the views received

from the States and Government of India, a dual GST structure with defined functions and responsibilities of the Centre and the States is recommended. An appropriate mechanism that will be binding on both the Centre and the States would be worked out whereby the harmonious rate structure along with the need for further modification could be upheld, if necessary with a collectively agreed Constitutional

Amendment. Salient features of the proposed model are as follows:

(i) The GST shall have two components: one levied by the Centre (hereinafter referred to as Central GST), and the other levied by the States (hereinafter referred to as State GST). Rates for Central GST and State GST would be prescribed appropriately, reflecting revenue considerations and acceptability. This dual GST model would be implemented through multiple statutes (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.

(ii) The Central GST and the State GST would be applicable to all transactions of goods and services 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.

(iii) The Central GST and State GST are to be paid to the accounts of the Centre and the States separately. It would have to be ensured that account-heads for all services and goods would have indication whether it relates to Central GST or State GST (with

identification of the State to whom the tax is to be credited).

(iv) Since the Central GST and State GST are to be treated separately, taxes paid against the Central GST shall be allowed to be taken as input tax credit (ITC) for the Central GST and could be utilized only against the payment of Central GST. The same principle will be applicable for the State GST. 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 Central GST and the State GST would be aligned.

(v) Cross utilization of ITC between the Central GST and the State GST would not be allowed except in the case of inter-State supply of goods and services under the IGST model which is explained later.

(vi) Ideally, the problem related to credit accumulation on account of refund of GST should be avoided by both the Centre and the States except in the cases such as exports, purchase of capital goods, input tax at higher rate than output tax etc. where, again refund/adjustment should be completed in a time bound manner.

(vii) To the extent feasible, uniform procedure for collection of both Central GST and State GST would be

prescribed in the respective legislation for Central GST and State GST.

(viii) The administration of the Central GST to the Centre and for State GST to the States would be given. This would imply that the Centre and the States would have concurrent jurisdiction for the entire value chain and for all taxpayers on the basis of thresholds for goods and services prescribed for the States and the Centre.

(ix) The present threshold prescribed in different State VAT Acts below which VAT is not applicable varies from State to State. A uniform State GST threshold across States is desirable and, therefore, it is considered that a threshold of gross annual turnover of Rs.10 lakh both for goods and services for all the States and Union Territories may be adopted with adequate compensation for the States (particularly, the States in North-Eastern Region and Special Category States) where lower threshold had prevailed in the VAT regime. Keeping in view the interest of small traders and small scale industries and to avoid dual control, the States also considered that the threshold for Central GST for goods may be kept at Rs.1.5 crore and the threshold for Central GST for services may also be appropriately high. It may be mentioned that even now there is a separate threshold of services (Rs. 10 lakh) and goods (Rs. 1.5 crore) in the Service Tax and CENVAT.

(x) The States are also of the view that Composition/Compounding Scheme for the purpose of GST should 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 turn over 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.

(xi) The taxpayer would need to submit periodical returns, in common format as far as possible, to both the Central GST authority and to the concerned State GST authorities.

(xii) Each taxpayer would 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.

(xiii) Keeping in mind the need of tax payer's convenience, 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.

Central and State Taxes to be subsumed under GST

3.3 The various Central, State and Local levies were examined to identify their possibility of being subsumed under GST. While identifying, the following principles were kept in mind:

(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.

3.4 On application of the above principles, it is recommended that the following Central Taxes should

be, to begin with, subsumed under the Goods and Services Tax:

- (i) Central Excise Duty
- (ii) Additional Excise Duties
- (iii) The Excise Duty levied under the Medicinal and Toiletries Preparation Act
- (iv) Service Tax
- (v) Additional Customs Duty, commonly known as Countervailing Duty (CVD)
- (vi) Special Additional Duty of Customs - 4% (SAD)
- (vii) Surcharges, and
- (viii) Cesses.

Following State taxes and levies would be, to begin with, subsumed under GST:

- (i) VAT / Sales tax
- (ii) Entertainment tax (unless it is levied by the local bodies).
- (iii) Luxury tax
- (iv) Taxes on lottery, betting and gambling.
- (v) State Cesses and Surcharges in so far as they relate to supply of goods and services.
- (vi) Entry tax not in lieu of Octroi.

Purchase tax: Some of the States felt that they are getting substantial revenue from Purchase Tax and,

therefore, it should not be subsumed under GST while majority of the States were of the view that no such exemptions should be given. The difficulties of the foodgrains producing States and certain other States were appreciated as substantial revenue is being earned by them from Purchase Tax and it was, therefore, felt that in case Purchase Tax has to be subsumed then adequate and continuing compensation has to be provided to such States. This issue is being discussed in consultation with the Government of India.

Tax on items containing Alcohol: Alcoholic beverages would be kept out of the purview of GST. Sales Tax/VAT can be continued to be levied on alcoholic beverages as per the existing practice. In case it has been made Vatable by some States, there is no objection to that. Excise Duty, which is presently being levied by the States may not be also affected.

Tax on Tobacco products: Tobacco products would be subjected to GST with ITC. Centre may be allowed to levy excise duty on tobacco products over and above GST without ITC.

Tax on Petroleum Products: As far as petroleum products are concerned, it was decided that the basket of petroleum products, i.e. crude, motor spirit (including ATF) and HSD would be kept outside GST

as is the prevailing practice in India. Sales Tax could continue to be levied by the States on these products with prevailing floor rate. Similarly, Centre could also continue its levies. A final view whether Natural Gas should be kept outside the GST will be taken after further deliberations.

Taxation of Services :As indicated earlier, both the Centre and the States will have concurrent power to levy tax on all goods and services. In the case of States, the principle for taxation of intra-State and inter-State has already been formulated by the Working Group of Principal Secretaries/Secretaries of Finance/Taxation

and Commissioners of Trade Taxes with senior representatives of Department of Revenue, Government of India. For inter-State transactions an innovative model of Integrated GST will be adopted by appropriately aligning and integrating CGST and SGST. The working of this model is elaborated below.

3.5 Inter-State Transactions of Goods and Services

The Empowered Committee has accepted the recommendations of the Working Group of concerned officials of Central and State Governments for adoption of IGST model for taxation of inter-State transaction of Goods and Services. The scope of IGST Model is that Centre 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.

The major advantages of IGST Model are:

- 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.

3.6 GST Rate Structure

The Empowered Committee has decided to adopt a two-rate structure –a 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. For upholding of special needs of each State as well as a balanced approach to federal flexibility, and also for facilitating the introduction of GST, it is being discussed whether 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. It is also being discussed whether the Government of India may adopt, to begin with, a similar approach towards exempted list under the CGST.

The States are of the view that for CGST relating to goods, the Government of India may also 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.

3.7 Zero Rating of Exports

Exports would be zero-rated. Similar benefits may be given to Special Economic Zones (SEZs). However, such benefits will only be allowed to the processing zones of the SEZs. No benefit to the sales from an SEZ to Domestic Tariff Area (DTA) will be allowed.

3.8 GST on Imports: The GST will be levied on imports with necessary Constitutional Amendments. Both CGST and SGST will be levied on import of goods and services into the country. The incidence of tax will follow the destination principle and the tax revenue in case of SGST will accrue to the State where the imported goods and services are consumed. Full and complete set-off will be available on the GST paid on import on goods and services.

3.9 Special Industrial Area Scheme

After the introduction of GST, the tax exemptions, remissions etc. related to industrial incentives should be converted, if at all needed, into cash refund schemes after collection of tax, so that

the GST scheme on the basis of a continuous chain of set-offs is not disturbed. Regarding Special Industrial Area Schemes, it is clarified that such exemptions, remissions etc. would continue up to legitimate expiry time both for the Centre and the States. Any new exemption, remission etc. or continuation of earlier exemption, remission etc. would not be allowed. In such cases, the Central and the State Governments could provide reimbursement after collecting GST.

3.10 IT Infrastructure

After acceptance of IGST Model for Inter-State transactions, the major responsibilities of IT infrastructural requirement will be shared by the Central Government through the use of its own IT infrastructure facility. The issues of tying up the State Infrastructure facilities with the Central facilities as well as further improvement of the States' own IT infrastructure, including TINXSYS, is now to be addressed expeditiously and in a time bound manner.

3.11 Constitutional Amendments, Legislations and Rules for administration of CGST and SGST

It is essential to have Constitutional Amendments for empowering the States for levy of service tax, GST on imports and consequential

issues as well as corresponding Central and State legislations with associated rules and procedures. With these specific tasks in view, a Joint Working Group has recently been constituted (September 30, 2009) comprising of the officials of the Central and State Governments to prepare, in a time bound manner a draft legislation for Constitutional Amendment, draft legislation for CGST, a suitable Model Legislation for SGST and rules and procedures for CGST and SGST. Simultaneous steps have also been initiated for drafting of a legislation for IGST and rules and procedures. As a part of this exercise, the Working Group will also address the issues of dispute resolution and advance ruling.

3.12 Harmonious structure of GST and the States' autonomy in a Federal Framework

As a part of the exercise on Constitutional Amendment, a special attention would be given, as mentioned earlier in para 3.2, to the formulation of a mechanism for upholding the need for a harmonious structure for GST along with the concern for the States' autonomy in a federal structure.

3.13 Dispute Resolution and Advance Ruling

As a part of the exercise on drafting of legislation, rules and procedures for the administration of CGST and SGST, specific provisions would also be made to the issues of dispute resolution and advance ruling.

3.14 Need for compensation during implementation of GST

Despite the sincere attempts being made by the Empowered Committee on the determination of GST rate structure, revenue neutral rates, it is difficult to estimate accurately as to how much the States will gain from service taxes and how much they will lose on account of removal of cascading effect, payment of input tax credit and phasing out of CST. In view of this, it would be essential to provide adequately for compensation for loss that might emerge during the process of implementation of GST for the next five years. This issue may be comprehensively taken care of in the recommendations of the Thirteenth Finance Commission. The payment of this compensation will need to be ensured in terms of special grants to be released to the States duly in every month on the basis of neutrally monitored mechanism.

3.15 With the release of this First Discussion Paper and the Annexure on Frequently Asked Questions and Answers on GST, interaction with the representatives of industry, trade and agriculture would begin immediately at the national level, and then also simultaneously at the State levels. Similarly awareness campaign for common consumers would also be initiated at the same time. As a part of the discussion and campaign, the views of the industry, trade and agriculture as well as consumers are being sought in a structured and time bound manner.

Annexure

Frequently Asked Questions and Answers on GST

Question 1 : What is the justification of GST ?

Answer : There was a burden of “tax on tax” in the pre-existing Central excise duty of the Government of India and sales tax system of the State Governments. The introduction of Central VAT (CENVAT) has removed the cascading burden of “tax on tax” to a good extent by providing a mechanism of “set off” for tax paid on inputs and services upto the stage of production, and has been an improvement over the pre-existing Central excise duty. Similarly, the introduction of VAT in the States has removed the cascading effect by giving set-off for tax paid on inputs as well as tax paid on previous purchases and has again been an improvement over the previous sales tax regime.

But both the CENVAT and the State VAT have certain incompleteness. The incompleteness in CENVAT is that it has yet not been extended to include chain of value addition in the distributive trade below the stage of production. It has also

not included several Central taxes, such as Additional Excise Duties, Additional Customs Duty, Surcharges etc. in the overall framework of CENVAT, and thus kept the benefits of comprehensive input tax and service tax set-off out of the reach of manufacturers/dealers. The introduction of GST will not only include comprehensively more indirect Central taxes and integrate goods and services taxes for set-off relief, but also capture certain value addition in the distributive trade.

Similarly, in the present State-level VAT scheme, CENVAT load on the goods has not yet been removed and the cascading effect of that part of tax burden has remained unrelieved. Moreover, there are several taxes in the States, such as, Luxury Tax, Entertainment Tax, etc. which have still not been subsumed in the VAT. Further, there has also not been any integration of VAT on goods with tax on services at the State level with removal of cascading effect of service tax. In addition, although the burden of Central Sales Tax (CST) on inter-State movement of goods has been lessened with reduction of CST rate from 4% to 2%, this burden has also not been fully phased out. With the introduction of GST at the State level, the additional burden of CENVAT and services tax would be comprehensively removed, and a continuous chain of set-off from the original

producer's point and service provider's point upto the retailer's level would be established which would eliminate the burden of all cascading effects, including the burden of CENVAT and service tax. This is the essence of GST. Also, major Central and State taxes will get subsumed into GST which will reduce the multiplicity of taxes, and thus bring down the compliance cost. With GST, the burden of CST will also be phased out.

Thus GST is not simply VAT plus service tax, but a major improvement over the previous system of VAT and disjointed services tax – a justified step forward.

Question 2. What is GST? How does it work ?

Answer : As already mentioned in answer to Question 1, GST is a tax on goods and services with comprehensive and continuous chain of set-off benefits from the producer's point and service provider's point upto the retailer's level. It is essentially a tax only on value addition at each stage, and a supplier at each stage is permitted to set-off, through a tax credit mechanism, the GST paid on the purchase of goods and services as available for set-off on the GST to be paid on the supply of goods and services. The final consumer will thus bear only the GST charged by the last

dealer in the supply chain, with set-off benefits at all the previous stages.

The illustration shown below indicates, in terms of a hypothetical example with a manufacturer, one wholeseller 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 wholeseller. When the wholeseller 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 wholeseller. Thus, the manufacturer, wholeseller 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.

Table

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	$13-10 = 3$
Whole seller	130	20	150	10%	15	13	$15-13 = 2$
Retailer	150	10	160	10%	16	15	$16-15 = 1$

Question 3 : How can the burden of tax, in general, fall under GST ?

Answer : As already mentioned in Answer to Question 1, 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.

Question 4 : How will GST benefit industry, trade and agriculture ?

Answer : As mentioned in Answer to Question 3, the GST will give more relief to industry, trade and agriculture through a more comprehensive and wider coverage of input tax set-off and service tax set-off, subsuming of several Central and State taxes in the GST and phasing out of CST. The transparent and complete chain of set-offs which will result in widening of tax base and better tax compliance may also lead to lowering of tax burden

on an average dealer in industry, trade and agriculture.

Question 5 : How will GST benefit the exporters?

Answer : The subsuming of major Central and State taxes in GST, complete and comprehensive set-off 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. The uniformity in tax rates and procedures across the country will also go a long way in reducing the compliance cost.

Question 6 : How will GST benefit the small entrepreneurs and small traders?

Answer : The present threshold prescribed in different State VAT Acts below which VAT is not applicable varies from State to State. The existing threshold of goods under State VAT is Rs. 5 lakhs for a majority of bigger States and a lower threshold for North Eastern States and Special Category States. A uniform State GST threshold across States is desirable and, therefore, the Empowered Committee has recommended that a threshold of gross annual turnover of Rs. 10 lakh

both for goods and services for all the States and Union Territories may be adopted with adequate compensation for the States (particularly, the States in North-Eastern Region and Special Category States) where lower threshold had prevailed in the VAT regime. Keeping in view the interest of small traders and small scale industries and to avoid dual control, the States considered that the threshold for Central GST for goods may be kept at Rs.1.5 crore and the threshold for services should also be appropriately high. This raising of threshold will protect the interest of small traders. A Composition scheme for small traders and businesses has also been envisaged under GST as will be detailed in Answer to Question 14. Both these features of GST will adequately protect the interests of small traders and small scale industries.

Question 7 : How will GST benefit the common consumers?

Answer : As already mentioned in Answer to Question 3, 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.

Question 8 : What are the salient features of the proposed GST model?

Answer : The salient features of the proposed model are as follows:

- (i) Consistent with the federal structure of the country, the GST will have two components: one levied by the Centre (hereinafter referred to as Central GST), and the other levied by the States (hereinafter referred to as State GST). This dual GST model would be implemented through multiple statutes (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.

- (ii) The Central GST and the State GST would be applicable to all transactions of goods and services except the exempted goods and services, goods which are outside the purview of GST and the transactions which are below the prescribed threshold limits.
- (iii) The Central GST and State GST are to be paid to the accounts of the Centre and the States separately.
- (iv) Since the Central GST and State GST are to be treated separately, in general, taxes paid against the Central GST shall be allowed to be taken as input tax credit (ITC) for the Central GST and could be utilized only against the payment of Central GST. The same principle will be applicable for the State GST.
- (v) Cross utilisation of ITC between the Central GST and the State GST would, in general, not be allowed.
- (vi) To the extent feasible, uniform procedure for collection of both Central GST and State GST would be prescribed in the respective legislation for Central GST and State GST.

- (vii) The administration of the Central GST would be with the Centre and for State GST with the States.
- (viii) The taxpayer would need to submit periodical returns to both the Central GST authority and to the concerned State GST authorities.
- (ix) Each taxpayer would 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.
- (x) Keeping in mind the need of tax payers convenience, 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.

Question 9 : Why is Dual GST required ?

Answer : 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.

Question 10 : How would a particular transaction of goods and services be taxed simultaneously under Central GST (CGST) and State GST (SGST)?

Answer : The Central GST and the State GST would be levied simultaneously on every transaction of supply of goods and services except the exempted goods and services, goods which are outside the purview of GST and the transactions which are below the prescribed threshold limits. Further, both would be levied on the same price or value unlike State VAT which is levied on the value of the goods inclusive of CENVAT. While the location of the supplier and the recipient within the country is immaterial for the purpose of CGST,

SGST would be chargeable only when the supplier and the recipient are both located within the State.

Illustration I : Suppose hypothetically that the rate of CGST is 10% and that of SGST is 10%. When a wholesale dealer of steel in Uttar Pradesh supplies steel bars and rods to a construction company which is also located within the same State for, say Rs. 100, the dealer would charge CGST of Rs. 10 and SGST of Rs. 10 in addition to the basic price of the goods. He would be required to deposit the CGST component into a Central Government account while the SGST portion into the account of the concerned State Government. Of course, he need not actually pay Rs. 20 (Rs. 10 + Rs. 10) in cash as he would be entitled to set-off this liability against the CGST or SGST paid on his purchases (say, inputs). But for paying CGST he would be allowed to use only the credit of CGST paid on his purchases while for SGST he can utilize the credit of SGST alone. In other words, CGST credit cannot, in general, be used for payment of SGST. Nor can SGST credit be used for payment of CGST.

Illustration II: Suppose, again hypothetically, that the rate of CGST is 10% and that of SGST is 10%. When an advertising company located in Mumbai supplies advertising services to a

company manufacturing soap also located within the State of Maharashtra for, let us say Rs. 100, the ad company would charge CGST of Rs. 10 as well as SGST of Rs. 10 to the basic value of the service. He would be required to deposit the CGST component into a Central Government account while the SGST portion into the account of the concerned State Government. Of course, he need not again actually pay Rs. 20 (Rs. 10+Rs. 10) in cash as it would be entitled to set-off this liability against the CGST or SGST paid on his purchase (say, of inputs such as stationery, office equipment, services of an artist etc). But for paying CGST he would be allowed to use only the credit of CGST paid on its purchase while for SGST he can utilise the credit of SGST alone. In other words, CGST credit cannot, in general, be used for payment of SGST. Nor can SGST credit be used for payment of CGST.

Question 11 : Which Central and State taxes are proposed to be subsumed under GST ?

Answer : The various Central, State and Local levies were examined to identify their possibility of being subsumed under GST. While identifying, the following principles were kept in mind:

- (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.

On application of the above principles, the Empowered Committee has recommended that the following Central Taxes should be, to begin with, subsumed under the Goods and Services Tax:

- (i) Central Excise Duty

- (ii) Additional Excise Duties
- (iii) The Excise Duty levied under the Medicinal and Toiletries Preparation Act
- (iv) Service Tax
- (v) Additional Customs Duty, commonly known as Countervailing Duty (CVD)
- (vi) Special Additional Duty of Customs - 4% (SAD)
- (vii) Surcharges, and
- (viii) Cesses.

The following State taxes and levies would be, to begin with, subsumed under GST:

- (i) VAT / Sales tax
- (ii) Entertainment tax (unless it is levied by the local bodies).
- (iii) Luxury tax
- (iv) Taxes on lottery, betting and gambling.
- (v) State Cesses and Surcharges in so far as they relate to supply of goods and services.

(vi) Entry tax not in lieu of Octroi.

Purchase tax: Some of the States felt that they are getting substantial revenue from Purchase Tax and, therefore, it should not be subsumed under GST while majority of the States were of the view that no such exemptions should be given. The difficulties of the foodgrain producing States was appreciated as substantial revenue is being earned by them from Purchase Tax and it was, therefore, felt that in case Purchase Tax has to be subsumed then adequate and continuing compensation has to be provided to such States. This issue is being discussed in consultation with the Government of India.

Tax on items containing Alcohol: Alcoholic beverages would be kept out of the purview of GST. Sales Tax/VAT could be continued to be levied on alcoholic beverages as per the existing practice. In case it has been made Vatable by some States, there is no objection to that. Excise Duty, which is presently levied by the States may not also be affected.

Tax on Tobacco products: Tobacco products would be subjected to GST with ITC. Centre may

be allowed to levy excise duty on tobacco products over and above GST with ITC.

Tax on Petroleum Products: As far as petroleum products are concerned, it was decided that the basket of petroleum products, i.e. crude, motor spirit (including ATF) and HSD would be kept outside GST as is the prevailing practice in India. Sales Tax could continue to be levied by the States on these products with prevailing floor rate. Similarly, Centre could also continue its levies. A final view whether Natural Gas should be kept outside the GST will be taken after further deliberations.

Taxation of Services : As indicated earlier, both the Centre and the States will have concurrent power to levy tax on goods and services. In the case of States, the principle for taxation of intra-State and inter-State has already been formulated by the Working Group of Principal Secretaries/Secretaries of Finance/Taxation and Commissioners of Trade Taxes with senior representatives of Department of Revenue, Government of India. For inter-State transactions an innovative model of Integrated GST will be adopted by appropriately aligning and integrating CGST and IGST.

Question 12 : What is the rate structure proposed under GST ?

Answer : The Empowered Committee has decided to adopt a two-rate structure –a lower rate for necessary items and items 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. For upholding of special needs of each State as well as a balanced approach to federal flexibility, it is being discussed whether 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. It is also being discussed whether the Government of India may adopt, to begin with, a similar approach towards exempted list under the CGST.

For CGST relating to goods, the States considered that the Government of India might also have a two-rate structure, with conformity in the levels of rate with 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.

Question 13: What is the concept of providing threshold exemption for GST?

Answer : Threshold exemption is built into a tax regime to keep small traders out of tax net. This has three-fold objectives:

- a) It is difficult to administer small traders and cost of administering of such traders is very high in comparison to the tax paid by them.
- b) The compliance cost and compliance effort would be saved for such small traders.
- c) Small traders get relative advantage over large enterprises on account of lower tax incidence.

The present thresholds prescribed in different State VAT Acts below which VAT is not applicable varies from State to State. A uniform State GST threshold across States is desirable and, therefore, as already mentioned in Answer to Question 6, it has been considered that a threshold of gross annual turnover of Rs. 10 lakh both for goods and services for all the States and Union Territories might be adopted with adequate compensation for the States (particularly, the States in North-

Eastern Region and Special Category States) where lower threshold had prevailed in the VAT regime. Keeping in view the interest of small traders and small scale industries and to avoid dual control, the States also considered that the threshold for Central GST for goods may be kept Rs.1.5 Crore and the threshold for services should also be appropriately high.

Question 14 : What is the scope of composition and compounding scheme under GST?

Answer : As already mentioned in Answer to Question 6, a Composition/Compounding Scheme will be an important feature of GST to protect the interests of small traders and small scale industries. The Composition/Compounding scheme for the purpose of GST should have an upper ceiling on gross annual turnover and a floor tax rate with respect to gross annual turnover. In particular there will be a compounding cut-off at Rs. 50 lakhs of the gross annual turnover and the floor rate of 0.5% across the States. The scheme would allow option for GST registration for dealers with turnover below the compounding cut-off.

Question 15 : How will imports be taxed under GST ?

Answer : With Constitutional Amendments, both CGST and SGST will be levied on import of goods and services into the country. The incidence of tax will follow the destination principle and the tax revenue in case of SGST will accrue to the State where the imported goods and services are consumed. Full and complete set-off will be available on the GST paid on import on goods and services.

Question 16 : Will cross utilization of credits between goods and services be allowed under GST regime?

Answer : 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 which is explained in answer to the next question.

Question 17 : How will be Inter-State Transactions of Goods and Services

be taxed under GST in terms of IGST method ?

Answer : The Empowered Committee has accepted the recommendation for adoption of IGST model for taxation of inter-State transaction of Goods and Services. The scope of IGST Model is that Centre would levy IGST which would be CGST plus SGST on all inter-State transactions of taxable 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 is also 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.

The major advantages of IGST Model are:

- 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 computerisation is limited to inter-State dealers and Central and State Governments should be able to computerise 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.

Question 18 : Why does introduction of GST require a Constitutional Amendment?

Answer : The Constitution provides for delineation of power to tax between the Centre and States. While the Centre is empowered to tax

services and goods upto the production stage, the States have the power to tax sale of goods. The States do not have the powers to levy a tax on supply of services while the Centre does not have power to levy tax on the sale of goods. Thus, the Constitution does not vest express power either in the Central or State Government to levy a tax on the 'supply of goods and services'. Moreover, the Constitution also does not empower the States to impose tax on imports. Therefore, it is essential to have Constitutional Amendments for empowering the Centre to levy tax on sale of goods and States for levy of service tax and tax on imports and other consequential issues.

As part of the exercise on Constitutional Amendment, there would be a special attention to the formulation of a mechanism for upholding the need for a harmonious structure for GST along with the concern for the powers of the Centre and the States in a federal structure.

Question 19: How are the legislative steps being taken for CGST and SGST ?

Answer : A Joint Working Group has recently been constituted (September 30, 2009) comprising of the officials of the Central and State Governments to prepare, in a time-bound manner a draft legislation for Constitutional Amendment.

Question 20: How will the rules for administration of CGST and SGST be framed?

Answer : The Joint Working Group, as mentioned above, has also been entrusted the task of preparing draft legislation for CGST, a suitable Model Legislation for SGST and rules and procedures for CGST and SGST. Simultaneous steps have also been initiated for drafting of legislation for IGST and rules and procedures. As a part of this exercise, the Working Group will also address to the issues of dispute resolution and advance ruling.

GST Reforms and Intergovernmental Considerations in India

Satya Poddar
Ehtisham Ahmad



March 2009
Department of Economic Affairs
Ministry of Finance
Government of India

Foreword

The Economic Division in the Department of Economic Affairs has initiated a Working Paper series with the objective of improving economic analysis and promoting evidence based policy formulation in its mandated areas of work. The themes to be covered in the series include macro-economic and sectoral issues of relevance for national policy, strategy for addressing emerging global and national development concerns and the agenda for economic policy reforms. While the issues identified for the Working Papers have relevance as inputs for the flagship publications of the Department, namely Economic Survey and the Mid-Year Review, issues that are related to the larger work responsibility of the Department of Economic Affairs, including the economic aspects of financial services, revenues and expenditure are also the subject matter of this initiative. Papers prepared by the staff or commissioned by the Economic Division as well as other Divisions in the DEA will be included in the Working Paper series on suitable peer review.

The paper by Mr. Satya Poddar and Mr. Ehtisham Ahmad on *GST Reforms and Intergovernmental Considerations in India* is the first Working Paper for 2009 and the third since the initiation of the series. This paper discusses the contractual issue of carrying forward the sub-national tax reform agenda and throws light on the principles, issues and procedures related to the objective of achieving a common goods and services market.

The introduction of the State level VAT in 2005 was the first sub-national tax reform that provided for greater competitiveness of Indian industry and trade. The goods and service tax first proposed in the Budget speech of 2006-07 and now under active discussions of the Empowered Committee of State Finance Ministers is the next logical step in this quest for a common market. The Paper by the authors raises certain key issues in the objective of the tax, its design with tradeoffs in the available choices, administrative infrastructure and the tax base and rates. The paper has references to international best practices and may prove useful in the context of evolving the broad design of the tax.



(Arvind Virmani)

Chief Economic Adviser

GST Reforms and Intergovernmental Considerations in India
Satya Poddar and Ehtisham Ahmad*

Content

1. Introduction.....	3
2. The Current Taxes and Their Shortcomings.....	4
A. Taxation at Manufacturing Level.....	5
B. Exclusion of Services.....	5
C. Tax Cascading.....	6
D. Complexity.....	7
3. Objectives of Tax Reform.....	9
A. Basic Objectives.....	9
B. Fiscal Autonomy and Harmonization.....	10
C. Centre and State Taxation Powers	13
4. Options for the Centre and State GSTs	14
A. Concurrent Dual GST	15
B. National GST	16
C. State GSTs	18
D. Non-concurrent Dual VATs.....	19
5. Tax Base and Rates.....	20
A. Tax Rates.....	20
B. Food	23
C. Land and Real Property.....	25
D. Non-profit Sector and Public Bodies	27
E. Financial Services	30
6. Treatment of Inter-State and International Trade	32
A. Place of Taxation, International Transactions	32
B. Place of Taxation, Inter-State Transactions	37
C. Taxation of Imports by the States	38
D. Monitoring of Inter-State Supplies	39
7. Harmonization of Laws and Administration.....	40
8. Conclusion	42

*Ernst & Young (India) and London School of Economics respectively. The authors are thankful to Peter Jenkins, Rebecca Millar, Dr. Govinda Rao, and office of the Chief Economist, Government of India, for helpful comments and suggestions on an earlier draft of the paper. The views are personal.

1. Introduction

The replacement of the state sales taxes by the Value Added Tax in 2005 marked a significant step forward in the reform of domestic trade taxes in India. Implemented under the leadership of Dr. Asim Dasgupta, Chairman, Empowered Committee of State Finance Ministers, it addressed the distortions and complexities associated with the levy of tax at the first point of sale under the erstwhile system and resulted in a major simplification of the rate structure and broadening of the tax base. The state VAT design is based largely on the blueprint recommended in a 1994 report of the National Institute of Public Finance and Policy, prepared by a team led by late Dr. Amaresh Bagchi (hereinafter, the “Bagchi Report”).¹ In recommending a state VAT, the Bagchi Report clearly recognized that it would not be the perfect or first best solution to the problems of the domestic trade tax regime in a multi-government framework. However, the team felt that this was the only feasible option within the existing framework of the Constitution and would lay the foundation for an even more rational regime in the future.

Buoyed by the success of the State VAT, the Centre and the States are now embarked on the design and implementation of the perfect solution alluded to in the Bagchi Report. As announced by the Empowered Committee of State Finance Ministers in November 2007, the solution is to take the form of a ‘Dual’ Goods and Services Tax (GST), to be levied concurrently by both levels of government.

The essential details of the dual GST are still not known. Will it necessitate a change in the constitutional division of taxation powers between the Centre and the States? Will the taxes imposed by the Centre and the States be harmonized, and, if so, how? What will be treatment of food, housing, and inter-state services such as transportation and telecommunication? Which of the existing Centre and State taxes would be subsumed into the new tax? What will be the administrative infrastructure for the collection and enforcement of the tax? These are issues which ultimately define the political, social, and economic character of the tax and its impact on different sectors of the economy, and households in different social and economic strata.

It is some of these aspects of the proposed GST that are the subject matter of this paper. We focus on the essential questions relating to the Dual GST design, and first discuss the need for, and the objectives of GST reform. We then describes alternatives to the Dual GST already endorsed by the Empowered Committee, not because they are superior in any way to the Dual GST, but to allow a fuller discussion of the trade-offs involved in the choice among them. Subsequent sections consider the question of tax base and rate, and proper treatment of various components of the tax base (e.g., food, housing, and financial services) in light of international best practices. The last section provides a discussion of the issues that arise in the taxation of cross-border transactions, both inter-state and international. An important question in this regard is the feasibility of, and the rules for, taxation of inter-state supplies of services.

¹ Bagchi, Amaresh et al (1994)..

2. The Current Taxes and Their Shortcomings

The principal broad-based consumption taxes that the GST would replace are the CENVAT and the Service Tax levied by the Centre and the VAT levied by the states. All these are multi-stage value-added taxes. The structure of these taxes today is much better than the system that prevailed a few years ago, which was described in the Bagchi Report as “archaic, irrational, and complex – according to knowledgeable experts, the most complex in the world”. Over the past several years, significant progress has been made to improve their structure, broaden the base and rationalize the rates. Notable among the improvements made are:

- the replacement of the single-point state sales taxes by the VAT in all of the states and union territories,
- reduction in the Central Sales Tax rate to 2%, from 4%, as part of a complete phase out of the tax,
- the introduction of the Service Tax by the Centre, and a substantial expansion of its base over the years, and
- rationalization of the CENVAT rates by reducing their multiplicity and replacing many of the specific rates by ad valorem rates based on the maximum retail price (MRP) of the products.

These changes have yielded significant dividends in economic efficiency of the tax system, ease of compliance, and growth in revenues.

The State VAT eliminated all of the complexities associated with the application of sales taxes at the first point of sale. The consensus reached among the States for uniformity in the VAT rates has brought an end to the harmful tax competition among them. It has also lessened the cascading of tax.

The application of CENVAT at fewer rates and the new system of CENVAT credits has likewise resulted in fewer classification disputes, reduced tax cascading, and greater neutrality of the tax. The introduction of the Service Tax has been a mixed blessing. While it has broadened the tax base, its structure is complex. The tax is levied on specified services, classified into one hundred different categories. This approach has spawned many disputes about the scope of each category. Unlike goods, services are malleable, and can and are often packaged into composite bundles that include taxable as well as non-taxable elements. Also, there is no standardized nomenclature for services, such as the HSN for goods.

The design of the CENVAT and state VATs was dictated by the constraints imposed by the Constitution, which allows neither the Centre nor the States to levy taxes on a comprehensive base of all goods and services and at all points in their supply chain. The Centre is constrained from levying the tax on goods beyond the point of manufacturing, and the States in extending the tax to services. This division of tax powers makes both the CENVAT and the state VATs partial in nature and contributes to their inefficiency and

complexity. The principal deficiencies of the current system, which need to be the primary focus of the next level of reforms, are discussed below.

A. Taxation at Manufacturing Level

The CENVAT is levied on goods manufactured or produced in India. This gives rise to definitional issues as to what constitutes manufacturing, and valuation issues for determining the value on which the tax is to be levied.² While these concepts have evolved through judicial rulings, it is recognized that limiting the tax to the point of manufacturing is a severe impediment to an efficient and neutral application of tax. Manufacturing itself forms a narrow base.

Moreover, the effective burden of tax becomes dependent on the supply chain, i.e., the taxable value at the point of manufacturing relative to the value added beyond this point.³ It is for this reason that virtually all countries have abandoned this form of taxation and replaced it by multi-point taxation system extending to the retail level.⁴

Australia is the most recent example of an industrialized country replacing a tax at the manufacturing or wholesale level by the GST extending to the retail level. The previous tax was found to be unworkable, in spite of the high degree of sophistication in administration in Australia. It simply could not deal with the variety of supply chain arrangements in a satisfactory manner.

B. Exclusion of Services

The States are precluded from taxing services. This arrangement has posed difficulties in taxation of goods supplied as part of a composite works contract involving a supply of both goods and services, and under leasing contracts, which entail a transfer of the right to use goods without any transfer of their ownership. While these problems have been addressed by amending the Constitution to bring such transactions within the ambit of the State taxation⁵ (by deeming a tax on them to be a tax on the sale or purchase of goods), services per se remain outside the scope of state taxation powers. This limitation is unsatisfactory from two perspectives.

² A detailed discussion of the problems can be found in the Bagchi Report.

³ See Ahmad and Stern (1984) for the definition of effective taxes and applications to India. Bagchi (1994) provides estimates of effective excise tax rates, which are shown to vary from less than one percent to more than 22%.

⁴ For example, these were precisely the reasons for the replacement of the federal manufacturers' sales tax by the Goods and Services Tax in 1991. See Canada Department of Finance (1987), and Poddar, Satya and Nancy Harley (1989).

⁵ The Constitution (46th Amendment) Bill 1982 amended Article 366 (29A) of the Constitution to deem a tax on six items to be a tax on the sale or purchase of goods.

First, the advancements in information technology and digitization have blurred the distinction between goods and services. Under Indian jurisprudence, goods are defined to include intangibles, e.g., copyright, and software, bringing them within the purview of state taxation. However, intangibles are often supplied under arrangements which have the appearance of a service contract. For example, software upgrades (which are goods) can be supplied as part of a contract for software repair and maintenance services. Software development contracts could take the character of contracts for manufacturing and sale of software goods or for rendering software development services, depending on the roles and responsibilities of the parties. The so-called 'value-added services (VAS) provided as part of telecommunication services include supplies (e.g., wallpaper for mobile phones, ring tones, jokes, cricket scores and weather reports), some of which could be considered goods. An on-line subscription to newspapers could be viewed as a service, but online purchase and download of a magazine or a book could constitute a purchase of goods. This blurring also clouds the application of tax to transactions relating to tangible property. For example, disputes have arisen whether leasing of equipment without transfer of possession and control to the lessee would be taxable as a service or as a deemed sale of goods.

The traditional distinctions between goods and services (and for other items such as land and property, entertainment, and luxuries) found in the Indian Constitution have become archaic. In markets today, goods, services, and other types of supplies are being packaged as composite bundles and offered for sale to consumers under a variety of supply-chain arrangements. Under the current division of taxation powers, neither the Centre nor the States can apply the tax to such bundles in a seamless manner. Each can tax only parts of the bundle, creating the possibility of gaps or overlaps in taxation.

The second major concern with the exclusion of services from the state taxation powers is its negative impact on the buoyancy of State tax revenues. With the growth in per capita incomes, services account for a growing fraction of the total consumer basket, which the states cannot tax. With no powers to levy tax on incomes or the fastest growing components of consumer expenditures, the States have to rely almost exclusively on compliance improvements or rate increases for any buoyancy in their own-source revenues. Alternatives to assigning the taxation of services to the states include assigning to the states a share of the central VAT (including the tax from services), as under the Australian model.

C. Tax Cascading

Tax cascading occurs under both Centre and State taxes. The most significant contributing factor to tax cascading is the partial coverage Central and State taxes. Oil and gas production and mining, agriculture, wholesale and retail trade, real estate construction, and range of services remain outside the ambit of the CENVAT and the service tax levied by the Centre. The exempt sectors are not allowed to claim any credit for the CENVAT or the service tax paid on their inputs.

Similarly, under the State VAT, no credits are allowed for the inputs of the exempt sectors, which include the entire service sector, real property sector, agriculture, oil and gas production and mining. Another major contributing factor to tax cascading is the Central Sales Tax (CST) on inter-state sales, collected by the origin state and for which no credit is allowed by any level of government.

While no recent estimates are available for the extent of tax cascading under the Indian tax system (although see Ahmad and Stern 1984 and 1991, and Bagchi for earlier work), it is likely to be significant, judging by the experience of other countries which had a similar tax structure. For example, under the Canadian manufacturers' sales tax, which was similar to the CENVAT, the non-creditable tax on business inputs and machinery and equipment accounted for approximately one-third of total revenues from the tax. The extent of cascading under the provincial retail sales taxes in Canada, which are similar to the State VAT, is estimated to be 35-40% of total revenue collections. A priori, one would expect the magnitude of cascading under the CENVAT, service tax, and the State VAT to be even higher, given the more restricted input credits and wider exemptions under these taxes.⁶ The Service Tax falls predominantly on business to business (B2B) services and is thus highly cascading in nature.

Tax cascading remains the most serious flaw of the current system. It increases the cost of production and puts Indian suppliers at a competitive disadvantage in the international markets. It creates a bias in favor of imports, which do not bear the hidden burden of taxes on production inputs. It also detracts from a neutral application of tax to competing products. Even if the statutory rate is uniform, the effective tax rate (which consists of the statutory rate on finished products and the implicit or hidden tax on production inputs) can vary from product to product depending on the magnitude of the hidden tax on inputs used in their production and distribution. The intended impact of government policy towards sectors or households may be negated by the indirect or hidden taxation in a cascading system of taxes.

D. Complexity

In spite of the improvements made in the tax design and administration over the past few years, the systems at both central and state levels remain complex. Their administration leaves a lot to be desired. They are subject to disputes and court challenges, and the process for resolution of disputes is slow and expensive. At the same time, the systems suffer from substantial compliance gaps, except in the highly organized sectors of the economy. There are several factors contributing to this unsatisfactory state of affairs.

The most significant cause of complexity is, of course, policy related and is due to the existence of exemptions and multiple rates, and the irrational structure of the levies. These deficiencies are the most glaring in the case of the CENVAT and the Service Tax.

⁶ Kuo, C.Y., Tom McGirr, Saya Poddar (1988), "Measuring the Non-neutralities of Sales and Excise Taxes in Canada", Canadian Tax Journal, 38, 1988, provide estimates of tax cascading under the Canadian federal manufacturers' sales tax and the provincial retail sales taxes.

The starting base for the CENVAT is narrow, and is being further eroded by a variety of area-specific, and conditional and unconditional exemptions. A few years ago the Government attempted to rationalize the CENVAT rates by reducing their multiplicity but has not adhered to this policy and has reintroduced concessions for several sectors/products.

The key problem with the service tax is the basic approach of levying it on specified services, each of which generates an extensive debate as to what is included in the base. Ideally, the tax base should be defined to include all services, with a limited list of exclusions (the so-called “negative list”).⁷ The Government has been reluctant to adopt this approach for the fear that it could bring into the tax net many services that are politically sensitive.

The complexities under the State VAT relate primarily to classification of goods to different tax rate schedules. Theoretically, one might expect that the lower tax rates would be applied to basic necessities that are consumed largely by the poor. This is not the case under the State VAT. The lowest rate of 1% applies to precious metals and jewellery, and related products—hardly likely to be ranked highly from the distributional perspective. The middle rate of 4% applies to selected basic necessities and also a range of industrial inputs and IT products. In fact, basic necessities fall into three categories – exempted from tax, taxable at 4%, and taxable at the standard rate of 12.5%. The classification would appear to be arbitrary, with no well accepted theoretical underpinning. Whatever the political merits of this approach, it is not conducive to lower compliance costs. Most retailers find it difficult to determine the tax rate applicable to a given item without referring to the legislative schedules. Consumers are even less aware of the tax applicable to various items. This gives rise to leakages and rent seeking.

Another source of complexity under the State VAT is determining whether a particular transaction constitutes a sale of goods. This problem is most acute in the case of software products and intangibles such as the right to distribute/exhibit movies or time slots for broadcasting advertisements.

Compounding the structural or design deficiencies of each of the taxes is the poor or archaic infrastructure for their administration. Taxpayer services, which are a lynchpin of a successful self-assessment system, are virtually nonexistent or grossly inadequate under both central and state administrations. Many of the administrative processes are still manual, not benefiting from the efficiencies of automation. All this not only increase the costs of compliance, but also undermines revenue collection.

⁷ For a detailed discussion of the flaws of the current approach to taxation of services, see Rao (2001), which recommended replacement of taxation of selected services by a general tax on all services (other than excluded services).

3. Objectives of Tax Reform

A. Basic Objectives

The basic objective of tax reform would be to address the problems of the current system discussed above. It should establish a tax system that is economically efficient and neutral in its application, distributionally attractive, and simple to administer.

As argued in Ahmad and Stern (1991), distributional or sectoral concerns have been at the heart of the excessive differentiation of the Indian tax system—but that the objectives are negated by the cascading effects of the taxes. While an optimal design of the consumption tax system, taking into account both production efficiency and distributional concerns, would not imply uniformity of the overall tax structure, the desired structure can be achieved by a combination of taxes and transfers.

Ahmad and Stern (1991) analyze the optimal pattern of tax rates implied by a given degree of aversion to poverty and concern for the poor. At high levels of concern for the poor, one would reduce the tax on cereals (but not dairy products) and increase the taxes on non-food items (durables). Thus, a differentiated overall structure appears desirable for a country in which the government has consistently expressed a concern for the poor. However, individual taxes should not be highly differentiated, as that complicates administration and makes it difficult to evaluate the overall effects of the tax design. This applies particularly to value-added type of taxes. In principle, a single rate (or at the most two-rate) VAT, together with excises and spending measures could achieve the desired distributional effects, for reasonable degrees of inequality aversion of policy makers.

In particular, it is important from an administrative perspective that close substitutes should not be taxed at very different rates—to avoid leakages and distortions. Revenue considerations suggest that the tax base should be broad, and comprise all items in the consumer basket, including goods, services, as well as real property.

The neutrality principle would suggest that:

- the tax be a uniform percentage of the final retail price of a product, regardless of the supply-chain arrangements for its manufacturing and distribution;
- the tax on inputs be fully creditable to avoid tax cascading; and
- the tax be levied on the basis of the destination principle, with all of the tax on a given product/service accruing in the jurisdiction of its final consumption.

Multiple VAT rates become a source of complexity, and disputes, for example, over borderlines, adding to the costs of tax administration and compliance. It is for this reason that countries like New Zealand, Singapore, and Japan have chosen to apply the tax at a

low and uniform rate, and address any concerns about vertical equity through other fiscal instruments, including spending programs targeted to lower-income households.⁸

Another important objective of tax reform is simplification of tax administration and compliance, which is dependent on three factors. The first determining factor for simplicity is the tax design itself. Generally, the more rational and neutral the tax design, the simpler it would be to administer and encourage compliance. If the tax is levied on a broad base at a single rate, there would be few classification disputes and the tax-specific record keeping requirements for vendors would be minimal. The tax return for such a system can be as short as the size of a postcard. It would simplify enforcement, and encourage voluntary compliance.

The second factor is the infrastructure for tax administration, including the design of tax forms, data requirements, system of tax rulings and interpretations, and the procedures for registration, filing and processing of tax returns, tax payments and refunds, audits, and appeals. A modern tax administration focuses on providing services to taxpayers to facilitate compliance. It harnesses information technology to enhance the quality of services, and to ensure greater transparency in administration and enforcement.

The third factor in a federation such as India is the degree of harmonization among the taxes levied by the Centre and the States. The Empowered Committee has already indicated a preference for a dual GST, consisting of a Centre GST and a State GST. Under this model, harmonization of the Centre and State GSTs would be critical to keep the overall compliance burden low. Equally important is harmonization of GSTs across the states.

B. Fiscal Autonomy and Harmonization

An important consideration in the design of reform options is the degree of fiscal autonomy of the Centre and the States. It goes without saying that the power to govern and to raise revenues go together. The Constitution of India lays down a clear division of powers between the Centre and the States, including the power to levy taxes. Should the Centre and the States then have complete autonomy in levying and collecting the taxes within the parameters specified in the Constitution, or should they voluntarily or otherwise conform to certain common principles or constraints? Should they collectively agree to have their individual taxes consolidated into a single national tax, the revenues from which get shared in some agreed manner among the constituent units? Such a system would have much to commend itself from the perspectives of economic efficiency and the establishment of a common market within India. Indeed, such political-economy compromises have been adopted by China and Australia. China moved to a centralized VAT with revenue sharing with the provinces — ensuring that provinces got as much revenues as under the prior arrangements, plus a share of the increment. In Australia, the

⁸ Canada provides a refundable tax credit, GST Credit, lower-income households through the personal income tax system. The credit is paid in quarterly installments and income-tested for higher-income households.

GST is a single national levy and all the GST revenues collected by the center are returned to the states. However, such a compromise is unlikely to find much favor with the States in India, as is already revealed in their preference for the Dual GST.

To give political substance to the federal structure in India, the States (as well as the Centre) are likely to insist that they have certain autonomy in exercise of their taxation powers. Full autonomy would mean that:

- retain the power to enact the tax,
- enjoy the risks and rewards of ‘ownership’ of the tax (i.e., not be insulated from fluctuations in revenue collections),
- be accountable to their constituents, and
- be able to use the tax as an instrument of social or economic policy.

Notwithstanding the above, there is a clear recognition of the need for harmonization of the Centre and State Taxes. Fiscal autonomy is important to allow the Centre and the States to set the tax rates according to their revenue needs. Harmonization of tax laws and administrative procedures is needed to simplify compliance and enforcement. It is also necessary to ensure that inter-state differences in policies and procedures do not generate additional economic distortions. An important question then is the desired degree of harmonization and the mechanism for achieving it.

The elements of harmonization can be divided into three broad sets: tax rates, tax base and tax infrastructure, i.e., the administration and compliance system. The first two elements could be viewed as important levers on which States would want to have some degree of control to achieve their social, economic, and fiscal policy objectives. However, the experience of other countries as well as their sub-national governments suggests that changes to the GST base are not a suitable instrument for social and economic policy (as discussed in greater detail in a later section in considering the treatment of food). While the tax base is a subject of intense debates at the time the tax is introduced, changes in the base after its introduction have been infrequent. This has especially been the case where the tax was initially levied on a broad and comprehensive base. Where the tax was initially levied on a narrow base, subsequent changes in the base have then been felt necessary to minimize anomalies, distortions, and revenue leakages created by the narrow base. Achieving such changes once the tax has been brought in, however logical, is invariably politically contentious because of vested interests. It is thus important to get the structure right at the outset, as the base (and quite often the rate) cannot be easily changed, *ex post facto*.

The VAT in the European Union is an example reflecting these policy considerations. The base for the EU VAT is uniform, as codified in the EU Directive⁹, which is binding in all Member States. There are important variations in the base, but these are essentially in the form of derogations granted for the arrangements existing at the time of introduction of the tax, and were intended to be temporary (though this has not always

⁹ The Commission Directive on the Common System of Value Added Tax, which replaced the Sixth Directive.

been the case). The tax rates are specified as floor rates (with some provision for reduced rates and maximum rates), below which Member States cannot set their rates.

Administration and compliance is an area where the need for harmonization is the greatest, and where Centre-State or inter-state variations are unlikely to serve any social or economic policy objective. This includes items such as the taxpayer registration system, taxpayer identification numbers, tax forms, tax reporting periods and procedures, invoice requirements, cross-border trade information systems and IT systems. Harmonization of these elements would result in significant savings in costs of implementing the GST (by avoiding duplication of effort in each government), as well as recurring savings in compliance costs. Harmonization would also permit sharing of information among governments, which is essential for effective monitoring of cross-border transactions. A common set of tax identifier numbers across states and the central government is a key element in the efficient exchange of information.

Harmonization of tax laws is also critical. Variation in the wording and structure of tax provisions can be an unnecessary source of confusion and complexity, which can be avoided by having the Centre and the States adopt a common GST law. An alternative is to agree on the key common elements if separate laws are chosen. Some of the critical elements for harmonization include common time and place of supply rules, as well as common rules for recovery of input tax, valuation of supplies and invoicing requirements. There would then be merit in harmonizing the system of tax interpretations and rulings as well (e.g., about classification of goods and services, determination of what constitutes taxable consideration, and definition of export and import).

These considerations suggest that harmonization of virtually all major areas of GST law and administration would be desirable. There is merit in keeping even the GST rate(s) uniform, at least during the initial years until the infrastructure for the new system is fully developed (see Ahmad, Poddar et al, 2008 for the GCC proposals). Harmonized laws would mean lower compliance costs for taxpayers and may also improve the efficiency of fiscal controls.

The Central Sales Tax (CST) in India provides a very useful for model for such harmonization. The CST is a state-level tax, applied to inter-state sales of goods, based on the origin principle. The tax law (including the base, rates, and the procedures) is enacted by Parliament, but the States collect and keep the tax. It is a perfect example of absolute harmonization, with the States enjoying the risks and rewards of ownership of the tax.

It is worth emphasizing that harmonization should not be viewed as constraining the fiscal autonomy of the Centre or the States. Rather, this is a framework that facilitates more efficient exercise of taxation powers, and all jurisdictions would be worse off without harmonization. This was the case under the previous State sales tax system, under which inter-state tax rate wars became a race to the bottom. Even today, they all suffer because of lack of harmonization of information and technology architectures, as a

result of which they are unable to share information on inter-state trade. Harmonization should allow greater exploitation of the benefits of a common market.

C. Centre and State Taxation Powers

As noted earlier, the current division of taxation of powers under the Constitution is constraining for both the Centre and the States. Neither is able to design a comprehensive and neutral tax on goods and services of the type found in modern tax systems. The Constitution divides taxation powers between the Centre and the States by sector (e.g., agriculture, manufacturing, and land and property) or type of taxes (e.g., luxury tax, tax on the sale or purchase of goods, and excise duty). A notable feature of the current division is that the two levels of government have no area of concurrent jurisdiction, with the exception of stamp duties. This approach, while it may have served the country well in the past, is no longer optimal for modern economies where the traditional dividing lines between sectors are blurred, and new social, environmental, and economic issues emerge which require new forms of taxation instruments. The need for a substantial realignment of taxation powers is also emphasized by Rao (2008):

“Paradigm shift in tax policy is necessary to recognise that tax bases of central and state governments are interdependent. The principle of separation of tax bases followed in the Constitutional assignment does not recognise the interdependence. It is therefore desirable to provide concurrent tax powers to Centre and States in respect of both income and domestic consumption taxes. In the case of personal income tax, separation of tax powers between the centre and states based on whether the income is from agricultural or non-agricultural sector has been a major source of tax evasion. As agriculture is transformed into a business it is important to levy the tax on incomes received from all the sources both for reasons of neutrality and to minimise tax evasion. At the same time, both centre and states could be allowed to levy the tax with the latter piggybacking the levy on the central tax subject to a ceiling rate. Similarly, it is important to unify multiple indirect taxes levied by the central and state governments into a single goods and services tax (GST) preferably with states piggybacking on the central levy with clearly defined tax rooms for the two levels of government. The transition to such a concurrent tax system requires integrating the existing CENVAT and service taxes and extending the tax to the retail level which would, inter alia, entail amendment of the Constitution. The states could piggyback on the levy.”

Thus, the current search for options for tax reform warrants a review of the existing Constitutional arrangements, which may well require a substantial realignment. For example, the dual GST would require giving the Centre and the States concurrent indirect

taxation powers, subject to prohibition on extra-territorial taxation, i.e., that the incidence of tax be restricted to consumption within the territory of the taxing jurisdiction.¹⁰

While such a review is beyond the scope of this paper, our discussion of alternative options in the next section proceeds with the assumption that suitable constitutional amendments would be made to enable the implementation of the chosen option.

4. Options for the Centre and State GSTs

In defining options for reform, the starting point is the basic structure of the tax. For purposes of this discussion, we start with the assumption that any replacement of the current taxes would be in the form of a classical VAT, which is consumption type (allowing full and immediate credit for both current and capital inputs attributable to taxable supplies) and destination based (i.e., the tax levied on the basis of the place of consumption of the goods and services, not the place of production). Under this system, credits for input taxes are allowed on the basis of invoices issued by the vendors registered for the tax. This is the most common type of structure adopted around the world. Its superiority over other forms of consumption taxes is well accepted in India as well as other countries.

The choices that remain then relate essentially to the assignment of powers to levy the tax to the Centre and the States, and the tax base and rates. In the remainder of this section we deal with the question of assignment, and then turn to the question of tax base and rates in the next section.

The main options for the VAT assignments include:

- Concurrent Dual GST,
- National GST, and
- State GSTs.

All these options require an amendment to the Constitution. For the sake of completeness of discussion, we also consider an additional option, Non-concurrent Dual VAT, that does not require an amendment to the Constitution. We now discuss each of these options in turn below.

¹⁰ The division of taxation powers between federal and provincial governments in Canada provides an interesting example of such concurrent powers. Under the Canadian Constitution, the federal government can levy any tax, and the provinces have the power to levy any direct tax within the province. A tax is considered to be a direct tax if its incidence falls on the person on whom it is levied. Thus, it includes all forms of income and wealth taxes. A sales tax or VAT is also viewed to be a direct if it is levied on the buyer/consumer, but not on the vendor. The tax can be collected and remitted by the vendor, acting as an agent of the government, but it has to be levied on the buyer. As a result, the two levels of concurrent powers for all types of taxes, subject to the condition that the provincial taxes can only be levied on persons within the geographical boundary of the provinces.

A. Concurrent Dual GST

Under this model, the tax is levied concurrently by the Centre as well as the States. Both the Central Government and the Empowered Committee appear to favor this model.

While full details of the model are still awaited, two variants have been identified in public discussions so far. The initial variant, discussed in November, 2007, entailed both the Centre and the States levying concurrently the GST on goods, but most of the services (except services of a local nature) remaining subject to the Centre GST only. The Central GST would thus apply to both goods and services, extending to the entire supply chain, including wholesale and retail trade. The State GSTs would largely be confined to goods only, with minor changes from the current State VATs.

Under the more recent variant,¹¹ both goods and services would be subject to concurrent taxation by the Centre and the States. This variant is closer to the model recommended by the Kelkar Committee in 2002.¹²

The main difference between the two variants is in the treatment of services, reflecting apprehensions about the feasibility of defining the place of supply (i.e., destination) of inter-state services. Even the more recent variant recognizes that there would be a set of inter-state services for which the place of destination would be difficult to determine. The State tax on these services would be collected by the Centre, and then apportioned among the States in some manner.

Other notable features of this variant are as follows:

- There would be a single registration or taxpayer identification number, based on the Permanent Account Number (PAN) for direct taxation. Three additional digits would be added to the current PAN to identify registration for the Centre and State GSTs.
- States would collect the State GST from all of the registered dealers. To minimize the need for additional administrative resources at the Centre, States would also assume the responsibility for administering the Central GST for dealers with gross turnover below the current registration threshold of Rs 1.5 crores under the central Excise (CENVAT). They would collect the Central GST from such dealers on behalf of the Centre and transfer the funds to the Centre.
- Procedures for collection of Central and State GSTs would be uniform. There would be one common tax return for both taxes, with one copy given to the Central authority and the other to the relevant State authority.
- Other indirect taxes levied by the Centre, States, or local authorities at any point in the supply chain would be subsumed under the Central or the State GST, as long as they are in the nature of taxes on consumption of goods and services.

¹¹ See Empowered Committee of State Finance Ministers (2008).

¹² Kelkar, Vijay, et al (2004).

At a broad conceptual level, this model has a lot to commend itself. It strikes a good balance between fiscal autonomy of the Centre and States, and the need for harmonization. It empowers both levels of government to apply the tax to a comprehensive base of goods and services, at all points in the supply chain. It also eliminates tax cascading, which occurs because of truncated or partial application of the Centre and State taxes.

The apprehension about feasibility of application of State GST to inter-state services is understandable, given the complete absence of any framework in India for determining their place of supply. However, the task of developing of such a framework is not insurmountable. In fact, such frameworks do already exist for application of national VAT to international cross-border services, which could be adapted for inter-state services. Canada has developed such a framework for application of provincial sales taxes or GST to services.

Another point to note is that inter-state services are provided predominantly by the organized sector (e.g., telecom and transportation services), which is generally tax compliant. Once the rules are framed, they would program their accounting and invoicing systems to collect and remit the tax accordingly.

Admittedly, there are inter-state services which have no unique place of supply. Take for example the supply of group health insurance to a corporation with employees throughout India, or auditing or business consulting services provided to a corporation or conglomerate with business establishments in several States. The determination of place of supply of such services is going to be somewhat arbitrary. However, such services are almost entirely B2B supplies, the tax on which is fully creditable to the recipient under a comprehensive taxation model. The arbitrariness in the rules would thus have no impact on the final tax collections of the Centre or the States.

The Empowered Committee proposal is silent on the treatment of land and real property transactions in the description of this option. Assuming this omission is deliberate, it is a major drawback of the option. As discussed further in the next section, modern VATs apply to all supplies, including supplies of land and real property. The Service Tax has already been extended to rentals of commercial property and construction services. There are no compelling social or economic policy reasons for excluding these services from the scope of the GST.

B. National GST

Under this option, the two levels of government would combine their levies in the form of a single national GST, with appropriate revenue sharing arrangements among them. The tax could be controlled and administered by the Centre, States, or a separate agency reporting to them. There are several models for such a tax. Australia is the most recent

example of a national GST, which is levied and collected by the Centre, but the proceeds of which are allocated entirely to the States.¹³

In China, the VAT law and administration is centralized, but the revenues are shared with the provinces. In going to this model, the Centre had assure the provinces that they would continue to get what they did under the previous arrangement and that changes in revenue shares would be phased in over an extended period of 15 years—see Ahmad 2008.

Under the Canadian model of the Harmonized Sales Tax (HST), the tax is levied at a combined federal and provincial rate of 13 percent (5% federal rate, 8% provincial rate) in the three participating provinces. Tax design and collection are controlled by the Centre, but the provinces have some flexibility to vary their tax rate. The revenues from the tax are shared among the participating provinces on the basis of consumer expenditure data for the participating provinces.

In Austria, and Germany, the tax design is controlled by the Centre, but states collect the taxes. This has led to incentive problems, as some of the Länder have begun to use tax administration measures to achieve tax policy goals. In Mexico, the establishment of a VAT at the center replaced state sales taxes, but had to be part of a political-economy compromise that assured the states an automatic share of the revenues generated from all federal taxes.

A single national VAT has great appeal from the perspective of establishment and promotion of a common market in India. However, the States may worry about the loss of control over the tax design and rates. Indeed, some control over tax rates is a critical issue in achieving accountable sub-national governance and hard budget constraints (Ambrosiano and Bordignon, 2006). The States may also be apprehensive that the revenue sharing arrangements would over time become subject to social and political considerations, deviating from the benchmark distribution based on the place of final consumption. The Bagchi Report also did not favor this option for the fear that it would lead to too much centralization of taxation powers.

¹³ The Australian constitutional situation is that both the States and the Commonwealth (the Federal Government) have power to tax supplies of goods and services. The constitution prevents laws interfering with interstate trade (including tax laws) and gives the power to collect Customs and excise taxes exclusively to the Federal Government. It is forbidden for the Commonwealth to tax State Property. To meet this requirement, the GST implementation laws, of which there are 6, simply state that they do not impose tax on State properties and the States accept that view, at least at the moment. The GST was introduced on the pretence that it was a State tax being collected by the Commonwealth in order to (a) secure the States' agreements to abolish some of their preexisting transaction taxes, in particular certain stamp duties, financial institutions duties, etc and (b) to ensure that the States wouldn't start a round of attempts to challenge the constitutional validity of the law (as was done, unsuccessfully, in the past with income tax, which both States and Commonwealth also have power to collect. The current Government has acknowledged that GST is in fact simply a Federal Tax that it uses to make grants to the States and as a result of this acknowledgement, the Auditor General has for the first time since 2000 agreed to approve the Commonwealth accounts.

These concerns can be addressed partially through suitable administrative arrangements and centre-state agreements. The tax design could be made subject to joint control of the Centre and the States. The States would necessarily lose the flexibility of inter-state variation in tax design, but that is also the perceived strength of this option. Given that the Centre does not have the machinery for the administration of such a tax, the States would presumably play a significant role in its administration. The revenue sharing formula could also be mandated to be based on the destination principle, as under the Canadian HST.

The key concerns about this option would thus be political. Notwithstanding the economic merits of a national GST, will it have a damaging impact on the vitality of Indian federalism? With no other major own-source revenues, will individual States become too dependent on collective choices and feel disempowered to act on their priorities? Will it be possible for the governments with such diverse political interests and philosophies to reach a consensus and adhere to it?

While one can have a healthy debate on each of these issues, international experience suggests that discretionary use of broad-based consumption taxes for social, political, or economic policy purposes tends to be limited. The dominant consideration in their design is their neutrality and efficiency in raising revenues. This is also reflected in the design of the State VATs in India. In spite of vast political and economic differences among them, States have been able to forge a consensus on a common VAT design. A national GST would extend this consensus to the Centre. But participation of the Centre could fundamentally alter the delicate balance of interests that currently prevails in the Empowered Committee and make the consensus harder to achieve.

C. State GSTs

Under this option, the GST would be levied by the States only. The Centre would withdraw from the field of general consumption taxation. It would continue to levy income taxes, customs duties, and excise duties on selected products such as motor fuels to address specific environmental or other policy objectives. The loss to the Centre from vacating this tax field could be offset by a suitable compensating reduction in fiscal transfers to the States. This would significantly enhance the revenue capacity of the States and reduce their dependence on the Centre. The USA is the most notable example of these arrangements, where the general sales taxes are relegated to the states.

There would be significant hurdles in adopting this option in India. First, it would seriously impair the Centre's revenues. The reduction in fiscal transfers to the States would offset this loss, but still the Centre would want to have access to this revenue source for future needs. Second, the option may not be revenue neutral for individual States. The incremental revenues from the transfer of the Centre's tax room would benefit the higher-income states, while a reduction in fiscal transfers would impact disproportionately the lower-income states. Thus the reform would be inequality

enhancing—and against the traditions of successive governments in India (of all political shades). Third, a complete withdrawal of the Centre from the taxation of inter-state supplies of goods and services could undermine the States’ ability to levy their own taxes on such supplies in a harmonized manner. In particular, it would be impractical to bring inter-state services within the ambit of the State GST without a significant coordinating support from the Centre.

D. Non-concurrent Dual VATs

Under the concurrent dual GSTs, the Centre and State taxes apply concurrently to supplies of all goods and services. It poses two challenges. First, it requires a constitutional amendment. Second, a framework is needed for defining the place of supply of inter-state services and for the application of State GST to them. Both of these hurdles can be circumvented if the GST on goods were to be levied by the States only and on services by the Centre only. The States already have the power to levy the tax on the sale and purchase of goods (and also on immovable property), and the Centre for taxation of services. No special effort would be needed for levying a unified Centre tax on inter-state services.

This option would not address any of the deficiencies of the current system identified in Section 2 above, if the taxes on goods and services were to be levied in an uncoordinated manner as two separate partial taxes. It would perpetuate the difficulties in delineating supplies of goods and services, and compound tax cascading.

The main appeal of this option is as a variant of the State GST option discussed immediately above. In levying the VAT on services, the Centre would essentially play the coordinating role needed for the application and monitoring of tax on inter-state services. The Centre would withdraw from the taxation of goods. Even the revenues collected from the taxation of services could be transferred back to the States, partially or fully.

Within this framework, cascading could be completely eliminated by the States agreeing to allow an input credit for the tax on services levied by the Centre. Likewise, the Centre would allow an input credit for the tax on goods levied by the States.

The discussion above suggests that the design of a GST is going to be a challenge, regardless of the option chosen. All options require significant Centre-State coordination and harmonization, and there may be very little room for variance in rate setting by States at least in the near future. The best option would appear to be a national GST (either through the constitution or on a voluntary basis), with an appropriate Centre-State and inter-State revenue sharing arrangement. If a framework for taxation of inter-state services can be devised, then the concurrent dual VAT could be the most supportive of the objective of fiscal autonomy. To ensure harmonization of tax base, rules and procedures, it would be desirable to have a single common legislation enacted by Parliament, following the model for the CST. The law would delegate the collection of

tax to the Centre and States on their respective tax bases, i.e., the Centre to collect the central GST on supplies of goods and services any where in India, and the States to collect the state GST on supplies within their states (as per the place-of-supply rules specified in the legislation).

5. Tax Base and Rates

We turn now to the question of the tax base and rates, within the broad structure of a consumption-type, destination-based, credit-invoice GST. Ideally, the tax should be levied comprehensively on all goods and services at a single rate to achieve the objectives of simplicity and economic neutrality. However, governments often deviate from this ideal either because of concerns about distribution of tax burden (e.g., food), or because of administrative and conceptual difficulties in applying the tax to certain sectors of the economy (e.g., health care, education, and financial services). These concerns are likely to be paramount at both Centre and State levels and there will inevitably be calls to exempt, or tax at a reduced rate, items of importance to the poor or other particular groups.

As noted earlier, reduced rates or exemptions for basic necessities may not be an efficient way of helping the poor, because of a significant spillover of their benefits to the rich. Although the rich spend a smaller *proportion* of their income on such goods than do the poor, because their income is higher they are also likely to spend a larger *absolute* amount. As a result, the rich might gain most from applying a reduced tax rate to such goods. The needs of the poor could be more effectively addressed through spending and transfer programs. Distributional concerns should be seen as part of the overall balance of all fiscal instruments and not solely for the GST. Moreover, multiple rates and exemptions increase the costs of administration and compliance. They give rise to classification disputes, necessitate additional record keeping, and create opportunities for tax avoidance and evasion through misclassification of sales.

Notwithstanding the virtues of a single-rate and comprehensive base, debates about the proper treatment of food and a variety of other items are inevitable. In what follows, we discuss some of the most critical aspects this debate, starting with a discussion of the revenue neutral tax rates in the absence of any exemptions or other preferences.

A. Tax Rates

In discussions on the GST design for India, it has been suggested that the tax would need to be levied at a combined Centre-State tax rate of 20 percent, of which 12% would go to the Centre and 8% to the states (vide, for example, the Kelkar Task Force Report). While they fall below the present combined Centre and State statutory rate of 26.5% (Cenvat of 14%, and VAT of 12.5%), GST at these rates would encounter significant consumer resistance, especially at the retail level, and would give rise to pressures for exemptions and/or lower rates for items of daily consumption. With the notable exception of

Scandinavian countries, where the tax is levied at the standard rate of 25%, few countries have been successful in levying and sustaining a VAT/GST at such high rates.

Successful GST models adopted by other countries had a very broad base and a relatively modest tax rate, especially at the time of inception. For example, the New Zealand GST was introduced at the rate of 10%, with a base consisting of virtually all goods and services (with the exception of financial services). The Singapore GST was introduced at 3%, but the rate has now been raised to 7% as inefficient excises and customs duties have been progressively eliminated.

Table 1 provides a comparison of the tax base and rates in selected international jurisdictions with ‘modern’ VAT/GST. It provides data on C efficiency, which is a widely-used measure of the comprehensiveness of the tax base. It is calculated as the ratio of the share of GST revenues in consumption to the standard rate. Any deviation from a 100 percent C-efficiency indicates deviation from a single tax rate on all consumption. Zero-rating of some consumption items would lead to a C-efficiency of less than 100 percent while inclusion of investment or a break in the GST chain could lead to a C-efficiency higher than 100 percent. While a C-efficiency of 100 does not imply a perfect VAT, it can serve as a useful indicator of the productivity of GST revenue per percentage point of GST rate. The last column in the table shows revenue productivity of GST in these countries, measured as GST revenues per point of the standard rate divided by the GDP (i.e., (Aggregate Revenues/Standard Rate)/GDP).

Table 12

<u>Comparison of GST Base and Rates, Selected Jurisdictions</u>					
Country	Year	Standard Rate %	Consumption % of GDP	C Efficiency	Revenue Productivity
Canada	2005	7	74.8	0.46	0.34
Japan	2004	5	75.5	0.67	0.50
New Zealand	2005	12.5	76.0	0.94	0.73
Singapore	2004	5	54.2	0.70	0.40

Source: Various IMF reports and authors’ own estimates

As shown in Table 2, the New Zealand GST, which is levied at a single rate on virtually all goods and services, has the highest C efficiency. The Canadian GST, also levied at a single rate, has low C efficiency because of zero-rating of food and medicines, and rebates for housing and non-profit sector. Japan and Singapore levy tax at a single rate to a comprehensive base, including food. Yet, their C efficiency is lower than in New Zealand mainly on account of exemptions for supplies by non-profit organizations. The C efficiency of European VATs is generally much lower, in the range of 50%, as these taxes are levied at multiple rates, and with exemption for land and housing, financial services, and supplies by public bodies. In general, VATs that have been introduced around the world in the last few years have a higher C efficiency than the ‘old’ VATs.

A low C efficiency translates into lower revenue productivity of tax, as shown in the last column of the table.

With this background, we turn to an estimation of the size of the GST base in India and the GST rates that would be required to replace the current indirect tax revenues of the Centre and the States.

Poddar and Bagchi (2007) calculations show that if the GST were to be levied on a comprehensive base, the combined Centre-State revenue neutral rate (RNR) need not be more than 12%. This rate would apply to all goods and services, with the exception of motor fuels which would continue to attract a supplementary levy to maintain the total revenue yield at their current levels.

Here are some basic ingredients of the RNR calculations for 2005-06, the latest year for which the necessary data are available. The total excise/service tax/VAT/sales tax revenues of the Centre and the States in that year was Rs.134 thousand crore and Rs.139 thousand crore respectively. Assuming that approximately 40% of the central excise revenues and 20% of the state VAT/sales tax revenues are from motor fuels, the balance of the revenues from other goods and services that need to be replaced by the GST are Rs 89 thousand crore for the Centre and Rs 111 thousand crore for the states, making up a total of Rs 200 thousand crore.

In 2005-06, the total private consumer expenditure on all goods and services was Rs.2,072 thousand crore at current market prices. Making adjustments for sales and excise taxes included in these values and for the private consumption expenditure on motor fuels, the total tax base (at pre-tax prices) for all other goods and services is Rs 1763 thousand crore.

These values yield a revenue neutral GST rate of approx. 11% (200 as percent of 1763 is 11.3%). The RNR for the Centre is 5% and for the states 6.3%. Allowing for some leakages, the combined RNR could be in the range of 12%. The Centre excise duty rates have been reduced substantially (the standard rate reduced from 16% to 10%) since 2005. At the current duty rates, the Centre RNR is likely to be in the range of 3%, bringing the combined RNR to below 10%.

These estimates are by no means precise. Even so, they give a broad idea of the levels at which the rate of a national GST could be set to achieve revenue neutrality for both levels of government. An important question for policy makers is the costs and benefits of deviating from this benchmark of single rate GST. While there would be pressing calls for all kinds of exemptions and lower rates, the economic benefits of a single rate are enormous. The experience of countries like New Zealand, Japan and Singapore suggests that it is feasible to resist such calls by keeping the tax rate low. There is increasing political support for such an option. It would mark a clean break from the legacy structures and herald a new era of simple and transparent tax administration.

There is virtue in keeping the GST rate in the 10% range, especially at inception. Any revenue shortfall at this rate could be made up by the use of supplementary excises on select demerit goods (e.g., tobacco, and alcohol), besides motor fuels. Excises could also be used for select luxury items which do already attract tax at higher rates. This would help minimize undesirable shifts in the distribution of tax burden (see the discussion in Ahmad and Stern, 1984 and 1991). Clearly, such excises should be limited to a very small list of items which are discrete and not amenable to tax avoidance and evasion.

B. Food

The main issue in the application of GST to food is the impact it would have on those living at or below subsistence levels. In 2005, data, food accounted for one-third of total private final consumer expenditures. For those at the bottom of the income scale, it doubtless accounts for an even higher proportion of total expenditures and incomes. Taxing food could thus have a major impact on the poor. By the same token, a complete exemption for food would significantly shrink the tax base.

There are additional considerations that are pertinent to the treatment of food.

- Food includes a variety of items, including grains and cereals, meat, fish, and poultry, milk and dairy products, fruits and vegetables, candy and confectionary, snacks, prepared meals for home consumption, restaurant meals, and beverages. In most jurisdictions where reduced rates or exemptions are provided for food, their scope is restricted to basic food items for home consumption. However, the definition of such items is always a challenge and invariably gives rise to classification disputes. In India, basic food, however defined, would likely constitute the vast bulk of total expenditures on food.
- In India, while food is generally exempt from the CENVAT, many of the food items, including food grains and cereals, attract the state VAT at the rate of 4%. Exemption under the state VAT is restricted to unprocessed food, e.g., fresh fruits and vegetables, meat and eggs, and coarse grains. Beverages are generally taxable, with the exception of milk.
- In the rural sector, the predominant distribution channel for unprocessed food would be either a direct sale by the farmer to final consumers or through small distributors/retailers. Even where food is within the scope of the GST, such sales would largely remain exempt because of the small business registration threshold.
- Given the large size of farm community in India, which is mostly unorganized, consideration needs to be given to whether it is advisable to exempt (with no right of input tax deduction) all unprocessed farm produce sold by them at the farm gate. In the case of cash crops (produce for further manufacturing or processing, e.g., cotton, coffee beans, and oil seeds), it would not be in the interest of the farmers to be exempted from tax. They should thus be allowed the option of voluntary registration to pay the tax. It is recognized that an exemption for first sale at the farm gate would be difficult to administer and create inefficiencies in distribution and marketing of farm produce.

These considerations pose some difficult policy issues. Given that food is currently exempt from the CENVAT, the GST under a single-rate, comprehensive-base model would lead to at least a doubling of the tax burden on food (from 4% state VAT to a combined GST rate of 10-12%). It would call for some tangible measures to offset the impact on the lower-income households. One would be to limit the exemption only to cereals (see Table 1) as some of the other food items have lower distributional characteristics.

The alternative of exempting food altogether (or zero rating) would not be any better. First, the revenue neutral rate would jump from 10-12% to 18%. While the poor would pay less tax on food, they would pay more on other items in their consumption basket. Whether and to what extent they would be better off would depend on the composition of their consumption basket. The higher standard rate would, in turn, lead to pressures for exempting other items (e.g., medicines, books, LPG, and kerosene). Third, it could preclude unification of the tax rate on goods with that on services, which are currently taxable 12.36%. Imposition of tax rate at 18% on hitherto exempt services (e.g., passenger travel, health, and education) would encounter significant political resistance. Fourth, one cannot expect any improvement in taxpayer compliance at such high rates. To the contrary, greater visibility of the Centre tax at the retail level could have a negative impact on compliance. Thus, an exemption for food has the potential to totally unravel the simplicity and neutrality of GST.

One could consider a lower rate for food, instead of complete exemption. If the lower rate were to be 5%, the revenue neutral standard rate (based on 2005 rate structure) would be pushed up to 16%. This may be a reasonable compromise, provided all other goods and services are made taxable at the single standard rate of 16%. The risk is that the lower rate for food would become the thin edge of the wedge which would create irresistible demands for the opening the door wider.

An important question is the definition of food that would be eligible for the lower rate. To keep the base broad, and limit the preference to items of consumption by the lower-income households, the lower rate should be confined to 'unprocessed' food items (including vegetables, fruit, meat, fish, and poultry). Its scope can be further restricted by excluding from the preference food pre-packaged for retail sale. . This definition would not be without problems, especially where the processing value added is small. For example, if wheat were taxable at 5% as unprocessed food, but flour taxable at 16% as processed food, it would encourage consumers to buy wheat and then have it processed into flour.

Overall, the preferred option would appear to be a single-rate, comprehensive-base GST. While no option is perfect, it has the advantage of simplicity and neutrality. As noted earlier, sales of unprocessed food in rural India would largely remain exempt under this option because of the small business exemption. The poor can be further insulated from its impact through direct spending programs, and/or exempt from tax any sales under the Public Distribution System (PDS).

C. Land and Real Property

Under the ‘old’ VATs (such as those in Europe), land and real property supplies are excluded from the scope of the tax. To minimize the detrimental impact of an exemption under a VAT, business firms are given the option to elect to pay tax on land real property supplies.

Under a modern GST/VAT (e.g., in Australia, New Zealand, Canada, and South Africa), housing and construction services are treated like any other commodity. Thus, when a real estate developer builds and sells a home, it is subject to VAT on the full selling price, which would include the cost of land¹⁴, building materials, and construction services. Commercial buildings and factory sales are also taxable in the same way, as are rental charges for leasing of industrial and commercial buildings. There are only two exceptions: (1) resale of used homes and private dwellings, and (2) rental of dwellings:

- A sale of used homes and dwellings is exempted because the tax is already collected at the time of their first purchase, especially for homes acquired after the commencement of the tax. If the sale were to be made taxable, then credit would need to be given for the tax paid on the original purchase and on any renovations and additions after the purchase. Except where the prices have gone up, the net incremental tax on resale may not be significant. Theoretically, this system does create a windfall for the existing homes build and acquired prior to the commencement of the tax. In practice, the windfall is not significant as the home construction would have attracted other taxes on construction materials and services that prevailed at the time.
- Residential rentals are also exempted for the same reason. If rents were to be made taxable, then credit would need to be allowed on the purchase of the dwelling and on repairs and maintenance. Over the life of the dwelling, the present value of tax on the rents would be approximately the same as the tax paid on the purchase of the dwelling and on any renovation, repair, and maintenance costs. In effect (and as with other consumer durables), payment of VAT on the full purchase price at acquisition is a prepayment of all the VAT due on the consumption services that the house will yield over its full lifetime. A resale of a dwelling is exempted for the same reason: the tax was pre-paid when the dwelling was initially acquired.
- Many private individuals and families own residential dwellings (including their homes and summer residences) which they may rent to others. They are generally not in the VAT system, so do not get a credit for the VAT paid when they initially

¹⁴ Actually, in Australia and New Zealand, this is not always the case. In New Zealand, land (like any other “goods”) is the subject of a deemed input tax credit under the “second hand goods” scheme, which has the effect that the tax on a development of land acquired from an unregistered person is the margin of the supplier. This provision affects mainly the land held by individuals outside a business at the commencement of the GST. Such land is permanently sheltered from tax, even where it subsequently enters a commercial supply chain. In Australia, a margin scheme for land is used to work out the taxable value in similar circumstances: the margin scheme operates as a second hand scheme and as a transitional rule to prevent the value of most (but not all) of the value of land as at 1 July 2000 entering into the tax base.

acquire their new home. Nor do they claim any credit for any repairs or renovations they may have made to the existing homes. If the rental of such dwelling were subject to tax, owners should also be given a credit for the taxes paid on such costs—which would be complex, and difficult to monitor.

Thus, virtually all countries exempt long-term residential rents and resale of used residential dwelling. However, short-term residential accommodation (in hotels, for example) is normally subject to VAT. Any commissions charged by the agents and brokers for the sale or rental of a dwelling are treated as a service separate from the sale or rental of the dwelling and attract tax regardless of whether paid by the buyer or the seller.¹⁵

Sale or rental of vacant land (which includes rental of car parking spaces, fees for mooring of boats and camping sites) is also taxable under the ‘modern’ VAT system.

It would make sense to incorporate these concepts in the design of GST in India as well.

- Conceptually, it is appropriate to include land and real property in the GST base. To exclude them would, in fact, lead to economic distortions and invite unnecessary classification disputes as to what constitutes supply of real property.
- In the case of commercial and industrial land and buildings, their exclusion from the base would lead to tax cascading through blockage of input taxes on construction materials and services. It is for this reason that even under the European system an option is allowed to VAT registrants to elect to treat such supplies as taxable.
- Housing expenditures are distributed progressively in relation to income and their taxation would contribute to the fairness of the GST.
- The State VAT and the Service Tax already apply to construction materials and services respectively, but in a complex manner. For example, there is significant uncertainty whether a pre-construction agreement to sell a new residential dwelling is a works contract and subject to VAT. Where the VAT does apply, disputes arise about the allocation of the sale price to land, goods, and services. While land is the only major element that does not attract tax, the tax rates applicable to goods and services differ, necessitating a precise delineation of the two. Extending the GST to all real property supplies, including construction materials and services, would bring an end to such disputes, simplify the structure, and enhance the overall economic efficiency of the tax.

One potential argument against the levy of GST to land and real property would be that they already attract the stamp duty. This argument can be quickly discarded as the purpose and structure of the stamp duty is quite different from that of the GST. Stamp duty is a cascading tax on each conveyance of title to real property, whereas the GST is a tax on final consumer expenditures. The GST does not impinge on commercial property transactions, after taking into account the benefit of input tax credits. It does not result in tax cascading. Under the model described above, in the case of residential dwellings, the

¹⁵ Poddar(2009) provides a more detailed discussion of the options for taxation of housing under VAT/GST.

GST would apply to the first sale only. Thus, the two taxes cannot be viewed as substitutes. However, the application of GST to real property transactions does warrant a review of the structure and rates of stamp duties and registration fees. The rates should be lowered and the structure rationalized when the GST is introduced.

D. Non-profit Sector and Public Bodies

Historically, supplies made by governmental bodies and non-profit organizations (including religious institutions, social welfare agencies, and sports and cultural organizations) have been exempted from VAT on the grounds that such bodies are not engaged in a business and their activities are not commercial in nature. But this is often, and increasingly, not the case. Public enterprises are involved in a wide range of industrial and commercial activities. As deregulation proceeds, the dividing line between public administration and industrial/commercial activities becomes increasingly blurred. For example, postal and telecommunication services were historically viewed as public administration, but this is no longer the case. Government agencies/enterprises provide such services in competition with private firms. The same is true for other activities such as local and inter-city transit, operation of airports, radio and television broadcasting, and provision of water, sewer, and sanitation services. Moreover, the public sector in India, as in many other countries, is large and pervasive.

Under the EU VAT Directive, activities of the public sector are divided into three categories: non-taxable, taxable, and exempt. A public body is in principle eligible to claim input tax deductions only in respect of the VAT paid on inputs acquired for use in making taxable supplies (though a number of member states pay refunds of VAT by matching grant). While this approach may have provided the EU Member States with the needed flexibility in dealing with their domestic environment, it falls short of achieving the principal criteria of an efficient VAT system identified above. The exempt or non-taxable status of a wide range of supplies by public bodies violates the criterion of economic neutrality. Biases are created in favor of the self-supply of services within the public sector to minimize the amount of non-deductible VAT on inputs. Consumers may be influenced in their purchasing decisions by the fact that the VAT does not apply to certain public sector goods and services. The non-deductible input VAT embedded in the prices of public sector goods and services is passed along to persons in the production-distribution chain who are not final consumers.

The application of a value added tax requires identification of a supply and the consumer or buyer to whom the supply is made, and valuation of consideration for the supply. Determination of each of these elements gives rise to issues in the public sector due to the nature of the way services are delivered by governments and the manner in which the services are funded. For example, a public body may provide its services for no explicit charge (e.g., museum admissions, water, health, and education) and there may not be any identifiable buyer or consumer for certain services provided on a collective basis (e.g., sanitation, and police protection). In addition, the political sensitivity to the taxation of certain services, and the methods of inter-governmental funding may detract from a neutral application of tax to the public sector activities. As a result, the public sector is

subject to special rules in almost all VAT systems currently in place throughout the world.

This is a matter that cannot be dealt with satisfactorily without a systematic review of all of the activities of the governmental bodies and non-profit organizations. However, at this stage it is useful to describe the two broad approaches that other countries have followed.

First, the highly-regarded VAT system in New Zealand (and later Australia¹⁶) treats all activities of public sector and non-profit bodies as fully taxable.¹⁷ They thus collect the VAT on all of their revenues, with the sole exception of revenues from taxes, interest and dividends, and gifts and charitable donations. Under this broad and comprehensive approach, no distinction is made between public administration and commercial/industrial activities of the state or non-profit organizations. By the same token, these bodies are eligible to claim a full credit for their input VAT in the same manner as private enterprises. This system is conceptually simple, and consequently is in some respects easy to operate. And—by putting public and private sectors on an equal footing—it minimizes potential distortions of competition. In Australia, certain basic medical and educational supplies, and supplies by non-profit organizations below market value (i.e., subsidized supplies) are zero-rated.¹⁸ Other supplies are taxable under the standard GST rules, as in New Zealand.

¹⁶ The Australian system is structured quite different from the New Zealand one, even though the net outcome is similar. New Zealand's GST is designed to tax all flows of money through the Government, whereas Australia's is complicated by the Federal Structure. The Commonwealth does not in fact pay GST or claim ITCs -- it just does so notionally --, whereas the States actually do pay and claim. New Zealand taxes appropriations, whereas Australian says that they are not taxed. In addition, a range of Government provided services are GST-free or exempt.

¹⁷ See Peter Barrand (1991), for a description of the New Zealand system. Aujean, Michel, Peter Jenkins and Satya Poddar provide an analytical framework for such a system.

¹⁸ Zero-rated (called GST-free) supplies are defined as follows:

38-7 Medical services

(1) A supply of a medical service is GST-free.

(2) However, a supply of a medical service is not GST-free under subsection (1) if:

(a) it is a supply of a professional service rendered in prescribed circumstances within the meaning of regulation 14 of the Health Insurance Regulations made under the Health Insurance Act 1973 (other than the prescribed circumstances set out in regulations 14(2)(ea), (f) and (g)); or

(b) it is rendered for cosmetic reasons and is not a professional service for which medicare benefit is payable under Part II of the Health Insurance Act 1973.

[medical services are defined by cross-reference to services covered by a health and health insurance law]

38-85 Education courses

A supply is GST-free if it is a supply of:

(a) an education course; or

(b) administrative services directly related to the supply of such a course,

The second is the traditional approach followed in most other countries. Under this approach, the activities of public and non-profit bodies are divided into two lists: taxable and exempt. There are no simple or mechanical rules for this division, which in practice is based on a variety of economic, social, and practical considerations. For example, public enterprises engaged in industrial or commercial activities are generally taxable, especially if their revenues from their clients are expected to exceed their costs. Some countries exempt all other fees and charges, while others tax them on a selective basis (including postal charges, airport landing fees, port loading and unloading charges, sale of statistical and other publications, and fees for licenses and permits). Given that not all of the activities of an organization are considered taxable under this approach, an input tax credit is allowed for only those inputs that relate to the taxable activities of the organization.

This latter approach creates difficulties in determining what is taxable and what is exempt, and also in allocating the input taxes between the two (since credit would be given only in respect of taxable activities). It also creates a distortion in the form of a bias against the use of outside contractors by public bodies in their exempt activities. For example, if a municipality used a contractor for construction of a road or a bridge, it would pay the VAT on the contractor's fees, and not be eligible to claim a credit for the tax. However, it could avoid the tax if it hired its own employees to do the construction work. As noted above, some countries provide a full or partial rebate of the tax related to minimize this 'self-supply' bias.

There is little doubt that the New Zealand approach is conceptually superior. It does, however, lead to a larger number of taxpayers, many of which will be entitled to refunds. Since the management of refunds is an especially problematic aspect of the VAT, particularly in developing countries, the control issues may be a significant drawback.

If governments and public bodies are partially exempted, then one other issue that needs to be considered is the treatment of supplies to governments. This is especially important in a federation. Should one government apply its non-creditable tax to supplies to another government? Or should all governments be immune from taxation as sovereign bodies? In India, CENVAT and State VAT currently apply to government procurement.

but only if they are supplied by the supplier of the course.

[education course defined as a course leading to a diploma or degree from a primary, secondary or tertiary school with cross-references to recognition by the appropriate state education authority]

38-250 Nominal consideration etc.

(1) A supply is GST-free if:

(a) the supplier is a charitable institution, a trustee of a charitable fund, a gift-deductible entity or a government school; and

(b) the supply is for consideration that:

(i) if the supply is a supply of accommodation – is less than 75% of the GST inclusive market value of the supply; or

(ii) if the supply is not a supply of accommodation – is less than 50% of the GST inclusive market value of the supply.

Likewise, the GST could be made applicable to supplies to governments with no special rules. However, as noted earlier, this then would create a self-supply bias for public bodies where they buy inputs for an exempt activity.

E. Financial Services

Financial services are exempted from VAT in all countries. The principal reason is that the charge for the services provided by financial intermediaries (such as banks and insurance companies) is generally not explicit- a fee- but is taken as a margin, that is hidden in interest, dividends, annuity payments, or such other financial flows from the transactions. For example, banks provide the service of operating and maintaining deposit accounts for their depositors, for which they charge no explicit fee. The depositors do, however, pay an implicit fee, which is the difference between the pure interest rate (i.e., the interest rate which could otherwise be earned in the market without any banking services) and the interest actually received by them from the bank on the deposit balance. The fee is the interest foregone. Similarly, the charge for the services provided by banks to the borrowers is included in the interest charged on the loan. It is the excess of the interest rate on the loan over the pure rate of interest or cost of funds to the bank for that loan.

It would be straightforward to levy the tax on this implicit fee if the reference ‘pure rate’ were easily observable—but it is not. The spread between borrowing and lending rates, could be measured, and taken as measuring the *total* value added by the intermediary. But in order for the crediting mechanism to work properly, it is necessary to go further and *allocate* this value-added to borrower and lender (with a credit on the tax paid due only to registered taxpayers)—which again raises the problem of identifying a reference pure interest rate.¹⁹

Some financial services are, of course, charged for by a direct and explicit fee, examples being an account charge or foreign exchange commission. Services provided for an explicit charge could be subjected to VAT in the normal way with the taxable recipient having a right of deduction, and a growing number of countries do this. Nevertheless, some countries exempt them all, while others limit the exemption to banking and life insurance. The exemption avoids the need to measure the tax base for financial transactions, but gives rise to other distortions in the financial markets. The denial of credit to the exempt financial institutions for the VAT charged on their inputs creates disincentives for them to outsource their business process operations. Where they render services to business clients, the blockage of input tax credits results in tax cascading, adversely affecting their competitive position in the international markets.

Taxing explicit fees for financial services, but treating margin services as exempt, is a possible answer, but it is conceptually flawed (as the same service will be treated differently for VAT purposes depending on how the remuneration for it is taken) and runs

¹⁹ These concepts are discussed in greater detail in Poddar, S. and M. English (1997) and Poddar, Satya (2003).

the risk that there will be some arbitrage between the two methods of charging to lessen the VAT charge (particularly in the case of supplies to final consumers with no right of deduction).

In China, financial services are taxable under their business tax, which is a tax on turnover with no tax credits allowed on inputs. Because it is a turnover tax, it can be applied to the total spread for margin services, with no need to allocate the spread between borrowers and depositors. Israel, and Korea also apply tax in such alternative forms.

Under the Service Tax, India has followed the approach of bringing virtually all financial services within the ambit of tax where the consideration for them is in the form of an explicit fee. It has gone beyond this by bringing selected margin services (where the consideration is the spread between two financial inflows and outflows) within the Service Tax net. The following are principal examples of such taxable margin services:

- Merchant discounts on credit/debit card transactions are taxable as a consideration for credit card services, as are any explicit fees or late payment charges collected from the card member.
- In foreign currency conversion transactions without an explicit fee, tax applies to a deemed amount of consideration equal to 2% of the amount converted.
- The tax applies to that portion of life insurance premiums that represents a cover for risks.

As there are no compelling economic or social policy reasons for exempting financial services (other than the practical difficulties of defining the consideration for margin services), it would be appropriate to continue this approach under GST. There are, however, certain technical flaws in the measurement of consideration that need to be addressed when switching over to GST. For example, in the case of insurance, the tax applies to the gross amount of risk premium, while a proper measure would be the premiums net of any claims (whether the claim is settled in cash or in kind). This can be accomplished by allowing a credit in respect of any claims paid.

Consideration could also be given to bringing interest margin on non-commercial loans and deposits within the next net on an aggregate basis, as opposed to for each transaction separately.²⁰ This could be done by computing the aggregate interest margin and apportioning it between the margin from B2B and B2C transactions. The B2B margin could then be zero-rated, and the tax applied to the B2C margin.

In some countries, transactions in gold, silver and other precious metals are also treated as part of the financial sector, given that these metals are often bought as investments, and not for consumption. They are exempted from tax. However, unlike the approach followed in India of applying a reduced rate of 1% to such metals and articles made of

²⁰ For a more complete discussion of the system in India and how it can be modified and extended, see Poddar, Satya (2007).

such metals, the exemption is confined to only metals of investment-grade purity levels. Jewellery and other articles made of such metals remain taxable at the standard rate.

6. Treatment of Inter-State and International Trade

Treatment of inter-state and international supplies of goods and services is one of the most crucial elements of the design of a Dual GST. A set of rules is needed to define the jurisdiction in which they would be taxable under the destination principle. Further a mechanism is needed for enforcing compliance to those rules.

The rules can be relatively straightforward for the application of the Central GST. However, there is a concern that, under a sub-national destination-based VAT, taxation of cross-border transactions could be a significant challenge in the absence of any inter-state fiscal border controls. Even if such border controls were to exist, they would be ineffective for taxation of services, which entail no physical inter-state movement. This concern has been a topic of increased discussion over the recent years due to the growth in internet sales and transactions. Cross-border VAT leakage is also a growing concern in the EU because of the removal of border controls between member countries.

In what follows, we first start with the basic framework for defining the place of supply, then look at the policy options for ensuring proper compliance. This discussion draws on Ahmad, Poddar et al (2008) for the GCC Secretariat.

A. Place of Taxation, International Transactions

In virtually all countries, VAT is levied on the basis of the destination principle. For this purpose, some countries follow the practice of prescribing a set of rules for defining the place of taxation or place of supply. A supply is taxable in a given jurisdiction only if the supply is considered to take place in that jurisdiction. An alternative approach followed by other countries is to first define what supplies are potentially within the scope of the tax, and then provide criteria for determining which of those supplies would be zero-rated as exports. The two approaches yield the same result, even though one excludes exports from the scope of the tax, while the other zero-rates them, having first included them in the scope. The Service Tax in India follows the second approach.

While the rules and approaches vary from country to country, the basic criteria for defining the place of taxation are as follows (approaches for taxation of services depicted in Chart 1):²¹

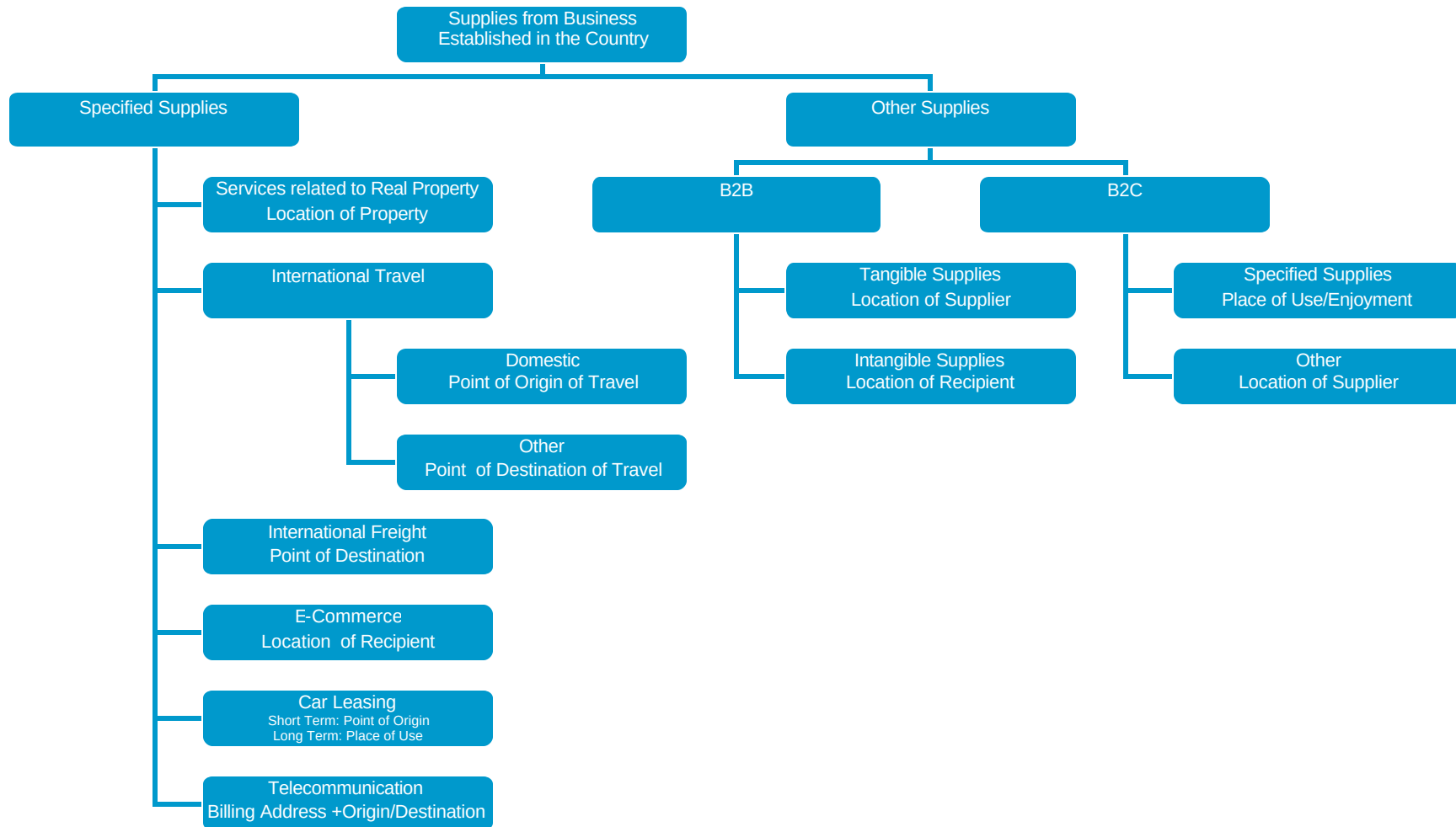
- A sale of goods is taxable if the goods are made available in or delivered/shipped to that jurisdiction (i.e., on the basis of place of delivery or shipment to the recipient)

²¹ What are discussed below are only the basic concepts. The actual rules can be complex, and highly varied from one jurisdiction to the next. For a more rigorous discussion of the approaches being followed in selected international jurisdictions, see Millar, Rebecca (2007).

- A sale of real property is taxable if the property is located in that jurisdiction (i.e., on the basis of place of location of the property). Services directly connected with real property are also taxable on this basis (e.g., services of estate agents or architects).
- A supply of other services or intangible property is taxable in that jurisdiction depending on one or more of the following factors:
 - Place of performance of the service
 - Place of use or enjoyment of the service or intangible property
 - Place of residence/location of the recipient
 - Place of residence/location of the supplier
- Special rules apply for certain supplies (also referred to as mobile services) for which there is no fixed place of performance or use/enjoyment, such as:
 - Passenger travel services
 - Freight transportation services
 - Telecommunication Services
 - Motor vehicle leases/rentals
 - E-commerce supplies

Chart 1

Place of Taxation (of supplies other than goods)



In defining the place of taxation of services and intangible property, a distinction is often made between supplies made to businesses (B2B) and final consumers (B2C). B2B supplies are generally defined to be made where the recipient is located or established, regardless of where the services are performed or used. This is particularly the case for the so-called intangible services (e.g., advisory or consulting services) for which the place of performance is not important. Thus, all such services rendered to nonresidents become zero-rated, and subject to a reverse charge in the country of the recipient, which charge is deductible as long as the recipient is fully taxable. This avoids tax cascading, which would otherwise occur.

By contrast, B2C services are deemed to be made in the jurisdiction where the supplier is located. Many B2C services tend to be tangible or physical in nature, e.g., haircuts, and admissions to place of amusement, which are used/consumed at the place of their performance. In some countries, B2C intangible services are treated in the same manner as B2B services, i.e., they are zero-rated when rendered to nonresident customers.

Special rules apply to the so-called mobile services. For transportation services, the place of supply is defined by reference to the point of origin or destination. In Europe, rail passenger transportation is taxed based on distance traveled in the taxing jurisdiction. For telecommunication, e-commerce and satellite broadcasting services, the origin rule (taxation in the country of the supplier) can lead to non-taxation, and various solutions have been followed to prevent this. For example, in the EU, e-commerce suppliers to EU final consumers are required to register and account for tax in the country of their customer, using a 'one stop shop' registration facility, if they wish. This rule is being extended to intra-EU supplies of telecommunications, e-commerce and satellite broadcasting from 1/1/2015 to prevent suppliers obtaining an arbitrage advantage by setting up their business in a low rate member state. In Canada, a two-out-of-three rule is followed, i.e., the supply is made in the jurisdiction if the points of origin and termination are in that jurisdiction, or if one of the points is in the jurisdiction and the supply is billed to an account in the jurisdiction. The rules for e-commerce are varied, but generally follow the rules for telecommunication services. Internet connectivity services are in fact telecommunication services. Goods and services bought and sold online are generally taxed on the same manner as those bought offline.

For short-term car rentals, in Europe the place of supply is where the car is first made available to the customer, regardless of the place of its subsequent use. For long-term leases, place of supply could depend on the place of use of the vehicle or the residence of the customer; the EU is adopting such a rule from 1/1/2010 to prevent 'rate shopping'. Often, similar rules are adopted for leases and rentals of other goods also.

In addition to the above, there are a variety of other complex cross-border transactions' for which supplementary rules are required. They relate to global transactions (or master service agreements) for individual supplies to legal entities of a corporate group around the world, triangular transactions, supplies among branches and between branches and head office, and cost reimbursement/ allocation arrangements. The complexity of the

rules for such transactions has been an issue under discussion by working groups at the OECD, with a view to developing a framework or guidance for uniformity and consistency in the treatment of international services and intangibles in different jurisdictions.²²

It is recognized that under these rules tax could be charged to nonresident business customers on supplies of an intermediate nature (i.e., not for final consumption) which would lead to cascading and create competitive distortions. To address this concern, many countries have provisions to provide a rebate of the tax charged to business customers.²³ Such rebates can also be extended to non-business customers, e.g., rebates to foreign tourist for the tax paid on goods bought locally for subsequent export when they return back.

Generally, these rules apply in a symmetrical manner to define exports and imports. Thus, where the supply of, say, consulting services by a domestic supplier is zero-rated because it is supplied to a business located outside the country, the supply of such services by a foreign supplier to a business located in the country would be taxable as an imported service. Imports generally attract tax at the customs border. For services and intangibles, the tax is self-assessed by the recipient under the reverse-charge mechanism.

The combined result of these rules (including the system of rebates for nonresident customers) is to define the place of destination of services and intangibles as follows:

- For B2B supplies, the place of destination is the place where the recipient is established or located.
- For B2C supplies of a tangible/physical nature (e.g., hair cuts, hotel accommodation, local transportation, and entertainment services), the place of destination is the place where the supplier is established or located, which is generally also the place where the service is performed. For highly mobile B2C supplies of an intangible nature (e.g., telecommunication, e-commerce and satellite broadcasting services, for which the place of performance is not linked to the rendering of the service), the place of supply could be the place of residence of the customer (as for B2B supplies), or the place where the services are used or enjoyed. But, because it is wholly impractical to subject final consumers to the reverse charge, in Europe the non-resident supplier is required to register and account for VAT to customers resident in the European Union.
- Special rules for specific supplies are generally designed to yield a result similar to that for other supplies. They serve the purpose of providing greater certainty and clarity in situations where the place of location or residence of the supplier or the recipient may not be well defined or easily ascertainable at the time of the supply.

²² For discussion of the issues and approaches, see OECD (2004).

²³ For example, such rebates are provided under Article XXX. of the EU VAT Directive.

B. Place of Taxation, Inter-State Transactions

An important question in the context of the Dual GST is whether these rules for international cross-border supplies can be adopted for domestic inter-state supplies also. Conceptually, there are no compelling reasons to deviate from them for defining the place of supply at the sub-national level. The only precedent available of a destination-based VAT at the sub-national level is that of Harmonized Sales Tax (HST) in Canada. (The precedent of the EU is different because it is a community of 27 sovereign member states rather than a single nation made up of a union of states in a federation. The EU solution of taxing intra-EU B2B supplies of goods and services by means of zero-rating and then reverse charge accounting in the member state of the taxable recipient may not be the right answer—and has led to the problem of carousel fraud). Surprisingly, Canada deviated from these rules in defining the place of supply in a province in one important respect. In defining the place of supply of services at the provincial level, the primary criterion used in Canada is the place of performance of the service. Thus, if all or substantially all of a service is performed in a province, then the place of supply of the service is considered to be that province, regardless of whether it is a B2B or B2C supply, and where it is used or enjoyed. There appear to be two reasons for it, which are also relevant for the design of the Dual GST in India.

First, it is recognized that the place where the supplier or the recipient is established cannot be defined uniquely at the sub-national level within a common market. A supplier may have establishments/offices in several States and one or more of them could be involved in rendering the service. At the national level, the country of residence of the counter parties to a transaction needs to be determined for direct tax as well as other regulatory purposes. However, at the sub-national level, such determination is not necessary, especially where there is no direct tax at that level. The basic rules outlined above for international supplies cannot be applied in the absence of supplementary rules for defining the place where the supplier and the recipient are located or established. Take, for example, an HR consulting firm with offices in several States providing recruitment services to a corporate entity with operations through India. In this case, the basic rule of defining the place of supply of the service to be where the recipient is established cannot be applied as the recipient is established in more than one State.

Second, under the Canadian HST, any input tax paid by a business can be claimed back as an input credit under the federal GST or the HST regardless of where it is established, as long as the inputs are used in a taxable activity. Thus, there is no adverse consequence of collecting the HST on services rendered to businesses located in other provinces. The HST is integrated with the GST to such an extent that it best fits the description of as a national GST, not a Dual GST.

Given these considerations, Canada defines the place of supply of services (other than those subject to special rules) to be the place where they are performed. If they are performed in more than one province, supplementary rules are employed to determine the place of supply. The main supplementary rule defines the place of supply/taxation to be the place to which the employee/officer of the supplier, who had responsibility for negotiating the service contract with the recipient, reports. In effect, under these rules the

sub-national tax on services is applied on the basis of the origin principle, i.e., where the services are performed.

The Canadian approach does not appear to be suitable for the Dual GST in India where the Centre and State GSTs would be harmonized, but not integrated. It would be desirable to tax B2B supplies of services (and intangibles) in the State of destination, and not of origin.

Given that any tax on B2B supplies would generally be fully creditable, excessive sophistication would not be warranted for defining the place of destination of such supplies. For multi-establishment business entities, the place of destination could be defined simply as the place of predominant use of the service. Where there is no unique place of predominant use, the place of destination could be simply the mailing address of the recipient on the invoice, which would normally be the business address of the contracting party. The risk of misuse of this provision would be minimal if it is limited to B2B supplies where the tax is fully creditable.

For B2C services, the tax should apply in the State where the supplier is established, which, in turn, could be defined as the place where the services are performed. Where there is no unique place of performance of the service, the place of taxation could be defined to be the State where the supplier's establishment most directly in negotiations with the recipient is located. This would be similar to the Canadian rule.

C. Taxation of Imports by the States

In most countries, imports attract the VAT/GST at the time of entry into the country. The tax is generally applied on the value of goods declared for customs purposes, including the amount of the customs duty. However, there are no well-established precedents for the application of sub-national taxes to imports. In India, the Centre levies an additional duty (called the special additional duty) on imports at the rate of 4%, which is meant to be in lieu of the state VAT. This duty is allowed as a credit against the central excise duty on manufacturing or refunded where the imports are resold and the State VAT is charged on them.

In Canada, the provincial HST is collected by the Customs authorities on non-commercial importations of goods. The tax is collected at the time of importation on the basis of place of residence of the person importing the goods, regardless of where the goods enter the country. Commercial importations do not attract the provincial HST because of difficulties in determining their destination within the country. For example, a large consolidated commercial shipment could contain goods that are initially destined to a central warehouse, for subsequent distribution to various parts of the country.

The Canadian system is conceptually appealing and could be considered for the application of State taxes under the Dual GST in India.

D. Monitoring of Inter-State Supplies

We turn now to the design of a suitable mechanism for payment and collection of tax on inter-state supplies. As noted earlier, there is a concern that a sub-national destination-based VAT could be subject to substantial leakages in the absence of effective inter-state border controls. Many policy prescriptions have been made to deal with the issue, but none implemented so far at the sub-national level.²⁴

In our view, these concerns are exaggerated, especially under a dual GST, harmonized between the Centre and the States and across the States. It is possible to design suitable mechanisms for proper application of tax on inter-state supplies, without resorting to border controls. The current border controls for goods, in the form of inter-state check posts have not been effective in the past. Border controls would not even be feasible for services and intangibles, which involve no physical inter-state movement.

As noted by Bird and Gendron²⁵, under a dual GST, the application of the Centre GST to all domestic supplies would automatically serve as an audit control for reporting of inter-State supplies for purposes of the State GST. The aggregate of the turnovers reported for the State GSTs must equal the total turnover reported for the Centre GST. Dealers can misclassify the turnover to different States, but would not be able suppress the turnover for State GST below the level reported for the Centre GST. Where the GST design, rate and the base is harmonized across the States, the dealers would have little incentive to misclassify the turnover. Under such a system, the focus of the authorities should be on proper reporting of the total turnover, not inter-State turnover.

Notwithstanding the above, a mechanism is needed for proper application of sub-national tax on inter-State supplies of goods as well as services. For reasons outlined elsewhere²⁶, zero-rating of inter-State supplies is not advisable. Instead, the preferred approach would be to require the vendors to collect the destination state GST on inter-State supplies (of goods and services) and remit the tax directly to the destination state. The tax would then be creditable in the destination state under the normal rules, i.e., if it relates to inputs for use in making taxable supplies.

This mechanism, referred to as Prepaid VAT (PVAT), is similar to the mechanism of the CST. Under the CST, the tax on inter-state sales is charged and remitted to the origin state. Under PVAT, the tax on inter-state supplies would be charged and remitted to the destination state.²⁷ It preserves the destination principle of VAT. Vendor in the origin state collect tax on all of their domestic supplies, whether intra-State or inter-State. The

²⁴ See, for example, McLure, Charles (2000); Keen, Michael and Stephen Smith (2000), and Poddar, Satya (1990).

²⁵ See Bird and Gendron (1998).

²⁶ See Poddar, Satya, Eric Hutton, (2001).

²⁷ The PVAT mechanism as originally developed by the authors entailed a prepayment of the destination state VAT before the goods are shipped. However, under a harmonized Dual GST, such prepayment may not be necessary. There would be enough safeguards in the system to enforce payment of tax on inter-state supplies at the same time as on intra-state supplies.

tax collected on inter-state supplies would be that of the destination state and remitted to that state by the vendor. On intra-state supplies, the tax collected would be that of the origin state and paid to that state.

Buyers who are GST registrants (in B2B transactions) would have a strong incentive to ensure that the vendor properly applies the destination tax, which would then be creditable against their output tax in the state of destination. Otherwise, the goods would be subject to the tax of the origin state, which would not be creditable in the state of destination.

Most supplies of services and intangibles to consumers and other exempt buyers (in B2C transactions) would be taxable in the state of origin, without the benefit of zero-rating. However, inter-state shipments of goods to consumers would be zero-rated in the state of origin and attract the tax of the destination state (including, for example, mail order supplies of goods). An inducement could be created for consumers also to ensure that the vendor charges the destination state tax on such shipments. This could be done by imposing a self-assessment requirement in the destination state on any inter-state purchases on which the vendor has not charged and remitted the destination state tax.

The PVAT mechanism establishes the output-tax-and-input-credit chain for inter-state transactions and, thereby, strengthens the audit trail property of the VAT system. Unlike the system of zero-rating, it creates strong incentives for both the origin and the destination states to monitor compliance independently of each other, as revenues of both are affected by the zero-rated sales declared by the vendor. This is a unique feature of PVAT, and perhaps it is most significant. Under the traditional system of zero-rating, the quantum of zero-rated sales reported by the vendor affects the revenues of the origin state, but not of the destination state. PVAT creates a simple and effective link between the two.

7. Harmonization of Laws and Administration

The need for Centre-State and inter-State harmonization is paramount under the Dual GST. The ultimate goal would be a unified base and one set of rules for the two taxes.

What should be the mechanism for achieving this harmonization? Different options have been adopted in other federations or trading blocks. At one extreme is the example of Australia where the GST is imposed and administered as a single unified tax levied by the national government. All the revenues from the tax are then distributed to the states. Another such example is that of Harmonized Sales Tax (HST) in Canada, which is levied in three of the ten provinces. The tax is levied and administered under a unified law by the national government, much like the Australian GST. The key difference is in the revenue allocation system. Under the Canadian system, provincial participation in the HST is elective, not mandatory. The tax is levied at the national rate of 7 percent (now reduced to 5%), which is increased by 8 percent in those provinces which have elected to participate in it. The revenues attributable to the supplementary rate of 8 percent are then distributed among the participating provinces on the basis of a statistical calculation

of the tax base in those provinces (which approximates the revenues they would have collected if they had levied a separate tax of their own). In Australia, there is no State “participation”. The tax is a federal tax that is distributed to the States under a political agreement. The revenues are distributed as grants to the States, taking into account factors such as fiscal capacity and need of individual States. In terms of the operation of the law, the enactment of the law, and the jurisdiction of law, it is exclusively a federal tax.

The system in the Province of Quebec in Canada offers another model of harmonization of the national and sub-national taxes. Quebec levies a goods and services tax, called Quebec Sales Tax (QST), the legislation for which follows very closely the model for the federal GST. The two taxes have the same base, definitions, and rules, but levied under two separate statutes. To ensure harmonization of administration, the two governments have entered into a tax collection agreement under which the collection, administration and enforcement of the federal GST is delegated to the provincial government. The agreement defines the role and responsibilities of the two governments and the policies and procedures to be followed in administering the tax. The federal government retains the power to make any changes in the legislation and to issue rulings, and interpretations, which are adhered to by the province in administering the federal GST. In practice, the province accepts the federal rulings and interpretations for both GST and QST, given the similarities in the two statutes.

The EU model is yet another example. This model is quite distinct from the Australian and Canadian models. The focus in the EU model is on minimization of distortions in trade and competition, and not on harmonization of administration. Thus, the VAT base (subject to continuing derogations) is harmonized, as are the basic rules governing the mechanism and application of VAT (time of supply, valuation, place of supply etc). The rates are harmonized only within broad bands (e.g., the standard rate may not be less than 15%) and administration is largely a matter for the member states to decide (but must respect basic principles such as neutrality).

As noted earlier, the CST in India also offers an interesting model of the harmonization mechanism. The CST law is central, but the tax is administered and collected by the States. Indeed, this appears to be most suitable model for India. The GST law for both the Centre and the States would be enacted by Parliament under this model. It would define the tax base, place of taxation, and the compliance and enforcement rules and procedures. The rates for the State GST could be specified in the same legislation, or delegated to the State legislatures. The legislation would empower the Centre and the States to collect their respective tax amounts, as under the CST.

If the governments fail to reach a political compromise on the CST model, the Quebec model would appear to be the next best alternative. It respects fiscal autonomy of the two levels of government, yet facilitates harmonization through the mechanism of binding tax collection agreements between the Centre and the States. These agreements would, in turn, encourage adoption of a common GST law.

The Centre can play an important role of providing a forum to discuss and develop the common architecture for the harmonized administration of the two taxes. It would have responsibility to develop policies and procedures for GST, in consultation with the Empowered Committee, e.g., on the place of supply rules, taxpayer registration and identification numbers, model GST law, design of tax forms and filing procedures, data requirements and computer systems, treatment of specific sectors (e.g., financial services, public bodies and governments, housing, and telecommunications), and procedures for collection of tax on cross-border trade, both inter-State and international. The proposal made by the Empowered Committee (for delegation of administration of the Centre GST for smaller dealers to the States) is very similar, even though the contractual framework for it is yet to be developed.

8. Conclusion

The Empowered Committee describes the GST as “a further significant improvement – the next logical step - towards a comprehensive indirect tax reforms in the country.” Indeed, it has the potential to be the single most important initiative in the fiscal history of India. It can pave the way for modernization of tax administration - make it simpler and more transparent – and significant enhancement in voluntary compliance. For example, when the GST was introduced in New Zealand in 1987, it yielded revenues that were 45% higher than anticipated, in large part due to improved compliance. Its more neutral and efficient structure could yield significant dividends to the economy in increased output and productivity. The Canadian experience is suggestive of the potential benefits to the Indian economy. The GST in Canada replaced the federal manufacturers’ sales tax which was then levied at the rate of 13% and was similar in design and structure as the CENVAT in India. It is estimated that this replacement resulted in an increase in potential GDP by 1.4%, consisting of 0.9% increase in national income from higher factor productivity and 0.5% increase from a larger capital stock (due to elimination of tax cascading)

However, these benefits are critically dependent on a neutral and rational design of the GST. The discussion of selected issues in this paper suggests that there are many challenges that lie ahead in such a design. The issues are not trivial or technical. They would require much research and analysis, deft balancing of conflicting interests of various stakeholders, and full political commitment for a fundamental reform of the system.

Opportunities for a fundamental reform present themselves only infrequently, and thus need to be pursued vigorously as and when they do become available. As the choices made today would not be reversible in the near future, one needs a longer-term perspective. Achieving the correct choice is then a political economy balancing act that takes into account the technical options and the differing needs and constraints of the main partners. Fortunately, there is a very substantial consensus among all stakeholders in the country for a genuine reform. In the circumstances, an incremental or timid response would be neither politically expedient, nor would it serve the needs of India of

the 21st century. Experience of countries with modern VATs, such as New Zealand, Singapore, and Japan suggests that a GST with single-rate and comprehensive base can be a win-win proposition for taxpayers and the fisc alike.

References

Ahmad, Ehtisham, Satya Poddar A.M. Abdel-Rahman, Rick Matthews, and Christophe Waerzeggers (2008), ***Indirect Taxes for the Common Market***; Report to the GCC Secretariat.

Ahmad, Ehtisham (2008), "Tax Reforms and the Sequencing of Intergovernmental Reforms in China: Preconditions for a *Xiaokang* Society," in Lou Jiwei and Wang Shuilin (eds), ***Fiscal Reforms in China***, The World Bank.

Ahmad, E. and N. Stern (1984), "The theory of tax reform and Indian indirect taxes," ***Journal of Public Economics***, 25, 259-98.

Ahmad, E and N. Stern (1991), ***The theory and practice of tax reforms in developing countries***, Cambridge University Press.

Aujean, Michel, Peter Jenkins and Satya Poddar (1999), "A New Approach to Public Sector Bodies", 10 ***International VAT Monitor*** 144 (1999).

Bagchi, Amaresh et al (1994), ***Reform of Domestic Trade Taxes in India: Issues and Options***", National Institute of Public Finance and Policy, New Delhi.

Barrand, Peter (1991), "The Treatment of Non-Profit Bodies and Government Entities under the New Zealand GST", ***International VAT Monitor***, January 1991.

Bird, Richard and Gendron (1998), "Dual VATs and Cross-border Trade, Two Problems and One Solution", ***International Tax and Public Finance*** 5(3), 1998

Canada Department of Finance (1987), ***Federal Sales Tax Reform***, Government of Canada, 1987.

Empowered Committee of State Finance Ministers (2008), ***A Model and Roadmap for Goods and Services Tax in India***, New Delhi.

Keen, Michael and Stephen Smith (2000), "Viva VIVAT!", ***International Tax and Public Finance***, Vol. 7, 741-751

Kelkar, Vijay, et al (2004), ***Report on Implementation of the Fiscal Responsibility and Budget Management Act, 2003*** ", Ministry of Finance, Government of India, New Delhi.

Kuo, C.Y., Tom McGirr, Satya Poddar (1988), “Measuring the Non-neutralities of Sales and Excise Taxes in Canada”, *Canadian Tax Journal*, 38, 1988.

McLure, Charles (2000): “Implementing subnational VATs on internal trade: The compensating VAT (CVAT).” *International Trade and Public Finance*, Vol. 7,

Millar, Rebecca (2007), “Cross-border Services – A Survey of the Issues”, in Krever, Richard and David White (ed): *GST in Retrospect and Prospect*, Brookers Ltd, New Zealand 2007.

OECD (2004), “Report on the Application of Consumption Taxes to the Trade in International Services and Intangibles”, Centre for Tax Policy and Administration, OECD.

Poddar, Satya and Nancy Harley (1989, “Problems in Moving from a Flawed to a Neutral and Broad-Based Consumption Tax”, *Australian Tax Forum*, Volume 6, Number 3, 1989.

Poddar, Satya (1990): “Options for s VAT at the State Level”, in M. Gillis, C.S. Shoup and G. Sicat, eds., *Value Added Taxation in Developing Countries* (Washington, World Bank).

Poddar, S. and M. English (1997), ‘Taxation of financial services under a value-added tax: Applying the cash-flow method,’ *National Tax Journal*, pp. 89–111.

Poddar, Satya, and Eric Hutton, (2001): "Zero-Rating of Inter-State Sales Under a Sub-national VAT: A New Approach", Paper presented at the National Tax Association, *94th Annual Conference on Taxation*, Baltimore, November 8-10, 2001.

Poddar, Satya (2003): “Consumption Taxes, The Role of the Value Added Tax”, in Patrick Honohan (ed.) *Taxation of Financial Intermediation: theory and practice in emerging economies*, (World Bank and the Oxford University Press).

Poddar, Satya (2007), “VAT on Financial Services – Searching for a Workable Compromise”, in Krever, Richard and David White (ed): *GST in Retrospect and Prospect*, Brookers Ltd, New Zealand.

Poddar, Satya and Amaresh Bagchi (2007), “Revenue-neutral rate for GST”, *The Economic Times*, November 15, 2007.

Poddar, Satya (2009), “Treatment of Housing under VAT”, mimeograph, presented at the conference on VAT organized by the American Tax Policy Institute, Washington, Feb. 18-19, 2009

Rao, M. Govinda (2001), *Report of the Expert Group on Taxation of Services*, Government of India, March 2001.

Rao, M. Govinda (2008), “Unfinished Reform Agendum: Fiscal Consolidation and Reforms – A Comment” in Jagdish Bhagwati and Charles W. Colomiris, ***Sustaining India’s Growth Miracle*** Columbia Business School, 2008 pp. 104-114