

# IMPACTS OF PROGRESSIVE TAX REFORM IN INDIA: GOODS AND SERVICES TAX (GST) - AN APPROACH

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## Abstract

*The present paper is a brief overview of the introduction of goods and services tax (GST), a progressive tax system and its impacts in India. GST is an indirect taxation that merged multiple taxes into a single tax system. It will eliminate cascading effects and generate revenue for both central and state government. Composition of GST as central goods and services tax (CGST), state goods and services tax (SGST), and integrated goods and services tax (IGST) projects scientific and transparent indirect tax system in India. GST is going to reduce tax leakage and prevent corruption in pricing of products. To implement and control such technology based taxation system since independence, IT industry acts as spinal cord. GST emerged as service based consumption oriented tax in India. Concept of GST, formation of GST council, positive and negative impacts on economy especially on Indian business, foreign investment of the GST are addressed in this study. To present the study, descriptive type of research design on the basis of secondary data is applied. This is a modest attempt to forecast the after effect of GST in India.*

**Keywords:** Goods and Services Tax, Cascading Effect, Tax Leakage, Impacts on Economy

## INTRODUCTION

More than 1 billion customers, 29 states, 22 official languages, 9 million businesses - all had been operating under a spider's web of taxes and creating complications in the Indian economy in a large manner. These complications are the reasons behind introduction of goods and services tax (GST) in India. In 1954, GST was first introduced in France and since then more than 150 countries adopted this unique tax system. Most of the countries followed unified GST, while some other countries like Brazil and Canada adopted dual GST system where tax is levied by both central and state governments; the same is also followed in India as central goods and services tax (CGST), state goods and services tax (SGST) respectively (Kumar, 2016). GST acts as an indirect tax for the whole nation with an objective to remove the cascading effect of multiple tax system currently operated in India. In recent times, central government imposed tax on manufacture (central excise duty), services (services tax), interstate sale of goods (levied by centre but collected by the states), state levy of tax on retail sale (VAT), entry of goods in the state (entry tax), luxury tax, purchase tax etc. levied and collected by different authorities. As a result, economy witnessed cascading effect of tax i.e. tax on tax. Tax payers were forced to pay high cost arising with several tariff and non-tariff barriers such as octroi, entry tax on check posts etc. which disturb free flow trade in India. Tax laws sometimes

turned business decisions based on tax considerations and not on logical economic factors. To overcome such barriers, GST will be applied at the final point of consumption that will lead in reduction of cascading effect of tax on tax, allow producers to claim credits, and minimise the opportunity of corruption and revenue leakage. One of the major sectors going to be benefitted after the introduction of GST is the information technology (IT) sector. The services like software development, website design, development of mobile applications, online financial transaction facilities, and many more are exclusively provided IT sector. Some of the IT firms like Kentico, Dynamics CRM, Dynamics NAV and Sitefinity will be implementing GST in their software. GST will help the economy to grow in more efficiently by improving tax collection system, disrupt tax barriers between states, and integrate whole country via single tax rate system (Prajapati, 2016) etc. Being a destination-based tax imposed on final consumption, supply is considered as a keyword to levy GST either at the time of sale or a service is rendered. GST has been launched all over India since July 2017.

## REVIEW OF LITERATURE

Prajapati (2016) examines the challenges faced at the time of implementation of GST, the crucial tax reforms in India with some practical examples and also examined the tax credit mechanism applied under GST, the tax on value added

goods and services. Siddiqui (2016) opines GST would replace the multipurpose tax system applied in manufacture, sale and consumption of goods and services in India. The study also highlights on the merits and demerits at the time of application and its impact on overall economy. Tanwar (2014) investigates the significance of Arthashastra in present scenario. With the help of Arthashastra, the study focused on the importance of levy of tax under moderate tax rate otherwise people would decide for tax evasion and which would decrease the revenue income of the government. The study proves that the strategy of Kautilya applies in modern world too. Prahraj (2017) analyse the GST on the basis on one nation, one tax and one market in India. Exemptions under GST for start-up and small businesses and easy registration clearly aligned with the study. Challenges faced by general businessmen after introduction of GST are also a part of this study. Garg (2014) analyses the details of characteristics, background and impact of new tax system to be introduced in India. Benefits of GST model, opportunities and justification of GST are the key areas of the study. Mujalde and Vani (2017) in their paper make an attempt to present the GST over the current taxation system in India. Advantages of input tax credit and results of GST implications are the main objectives of the study. Kumar (2016) in his paper examines GST as the biggest tax reform in India since independence. Effects of GST bill on pricing of products and services, supply chain optimisation, IT accounting, and tax compliance system are the main issues of the study.

## OBJECTIVES OF THE STUDY

The study is based on past literature from respective journals, reports, newspapers and magazines covering wide collection of academic literature on GST. Available secondary data were used for the study. The objectives of the study are as follows.

- To analyse the concept and probable impacts of GST as progressive tax regime in India.
- To suggest measures to minimise the loopholes after implementation of GST.

## RESEARCH METHODOLOGY

The research is an attempt based on available secondary data collected from journals, articles, newspapers, magazines, and Internet. According to the requirements of the objectives of the study, descriptive type of research design is adopted to impart more accuracy and analysis of research study.

## ANALYSIS

The GST law is applicable to whole of India including Jammu & Kashmir (earlier services tax was not extended to Jammu & Kashmir). Given the passage of the Constitution (101st) Amendment Bill, 2016 in the parliament on 8th August, 2016, ratification of the said bill in the Lok Sabha on 29th March, 2017 and in the Rajya Sabha on 6th April, 2017, with no clear roadmap being prescribed by Finance Ministry, the Government of India has implemented GST from 1st July, 2017. GST is not a new concept to the rest of the world and they followed product wise several GST rate structure as per nature of the product. Table 1 shows the GST rates applicable in different countries.

**Table 1: GST Rates Applicable in Different Countries**

Country	GST Rate
Australia	10%
Canada	5%
France	19.6%
Germany	19%
Japan	5%
New Zealand	15%
Singapore	7%
United Kingdom	17.50%

Source: [www.gstindia.com](http://www.gstindia.com)

In case of GST rate in India, a four tier GST structure has been passed on 3rd November, 2016. The final slab rate being agreed upon are 0%, 5%, 12%, 18%, and 28%. The products covered under these rates are shown in Table 2. The rates for different products are subject to revision.

**Table 2: Product Wise Rate of GST in India**

Rate of GST	Name of the Products
0%	Milk, eggs, crud, lassi, unpacked food grains, unpacked paneer, gur, unbranded natural, honey, fresh vegetable, salt, kajal, education services, health services, children drawing and coloring books, unbranded atta, unbranded maida, besan, prasad, palmyra jaggery, phool bhari, jhaado.
5%	Sugar, tea, edible oils, domestic LPG, PDS kerosene, cashew nuts, milk food for babies, fabric, spices, coal, lifesaving drugs, packed paneer, raisin, roasted coffee, beans, skimmed milk powder, footwear (<Rs. 500), apparels (<Rs. 1000), coir mats, matting and floor covering, agarbatti, mishti, mithai (Indian sweets), coffee (except instant).
12%	Butter, ghee, almonds, fruit juice, packed coconut water, processed food, mobiles, preparation of vegetables, fruits, nuts or other parts of plants including pickle, murabba, chutney, jam, jelly, umbrella.
18%	Hair oil, toothpaste, soap, pasta, corn flakes, soups, capital goods, industrial intermediaries, ice-cream, toiletries, computers, printers.
28%	Small cars (+1% or 3% cess) consumer durables such as air-condition, TV, fridge, high-end motorcycle (+15% cess), beedis are not included here, luxury & sin items like BMWs, cigarettes and aerated drinks (+15% cess).

Source: [www.cleartax.in](http://www.cleartax.in)

Several taxes are replaced after the introduction of GST in India. Table 3 shows the taxes replaced by central and state governments separately.

**Table 3: List of Taxes Replaced by Central and State Governments**

Central Taxes	State Taxes
Central excise duty (including additional excise duties, duties of excise (medicine and toilet preparations).	Value added tax
Services tax	Octroi and entry tax
Additional customs duty (CVD)	Purchase tax
Special additional duty of customs (SAD)	Luxury tax
Central sales tax (levied by the Centre and collected by states)	Taxes on lottery, betting and gambling.
Central surcharge and cess (relating to supply of goods and services).	State cess and surcharges.
	Entertainment tax (other than the tax levied by the local bodies)
	Central sales tax (levied by the Centre and collected by states).

Almost all the goods and services are covered under GST except the following:

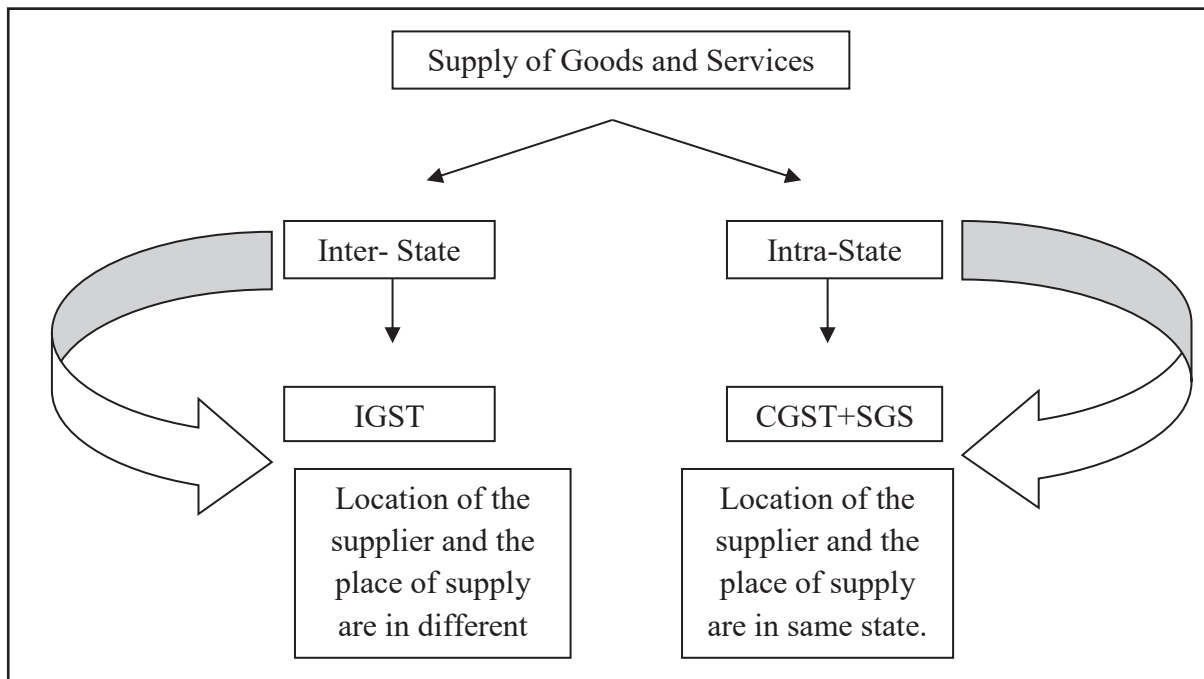
- Petroleum products: Petroleum crude, high speed diesel, motor spirit (petrol), natural gas and aviation turbine fuel are under central sales tax.
- Real estate: Stamp duty plus property taxes will be payable.
- Electricity: Electricity duty.
- Tobacco products: Under GST and central excise.
- Alcohol for human consumption: State excise (Praharan, 2017).

To implement and control GST in India, Goods & Services Tax Council (GST Council) has been constituted as the apex body in September, 2016. Under Article 279A of the Constitution of India, the GST Council is a federal forum with both centre and states in India on board. The Union Finance Minister acts as the chairman, while the Union Minister of State in charge of Revenue and Finance and the Minister in charge of Finance or Taxation, or any other minister nominated by each state government constitute the council. The aforesaid council has the right to take decisions on the following matters:

- Taxes, cesses, and surcharges to be subsumed under the GST.
- Goods and services that may exempt from GST.
- The threshold limit of turnover for applications of GST.
- Rates of GST.
- Frame model GST Laws, principles of levy, appointment of IGST and issues related to place of supply.
- Special provisions with respect to the eight northern states, Himachal Pradesh, Jammu & Kashmir and Uttarakhand; and other related issues.

GST is single consumption based tax/ levy applied for both central and state governments. As GST is a destination-based tax system, it will be computed at the time final/ actual

consumption (Garg & Gupta, 2017). Under a federal country both centre and state have assigned the power to levy and collect taxes on intrastate supply of goods and services. GST is to be levied as CGST (for central government) and SGST (for state government), while on interstate supply of goods and services and on imports, integrated goods and services tax (IGST) will be levied and collected by the centre with an objective of one nation, one tax and dual tax system both for centre and state to collect revenue. GST is collected on value added goods and services at each stage of sale or purchase in the supply chain. All the registered manufacturers, wholesalers or retailers will pay the requisite amount as per applicable GST rate but will claim back through tax credit mechanism. The end user of the product has to bear the tax burden as collected by consequent supplier of goods and services. The mechanism of application of GST is shown in Fig. 1.



**Fig. 1: Mechanism of Application of GST**

Application of GST in different states of India is an important issue for every indirect taxpayer. All the goods and services will be levied under both CGST and IGST. To simplify the fact, a GST model with hypothetical figures is applied to show the generation of tax invoice and input tax credit receivable at every point of supply in a particular business. Taking an example of car trading business, there are three steps involved to reach the car from manufacturer to final consumer of the car. Tax invoices of GST such as

tax invoice X (from manufacturer of car component to car manufacturer), tax invoice Y (from car manufacturer to car dealer), and tax invoice Z (from car dealer to car buyer) are generated by the respective supplier. Input tax credit is calculated as the difference between taxes generated among each stage separately for SGST and CGST. The difference of amount of tax is realised due to value added in each stage of sale value of the car. The aforesaid transactions are analysed as per Fig. 2.

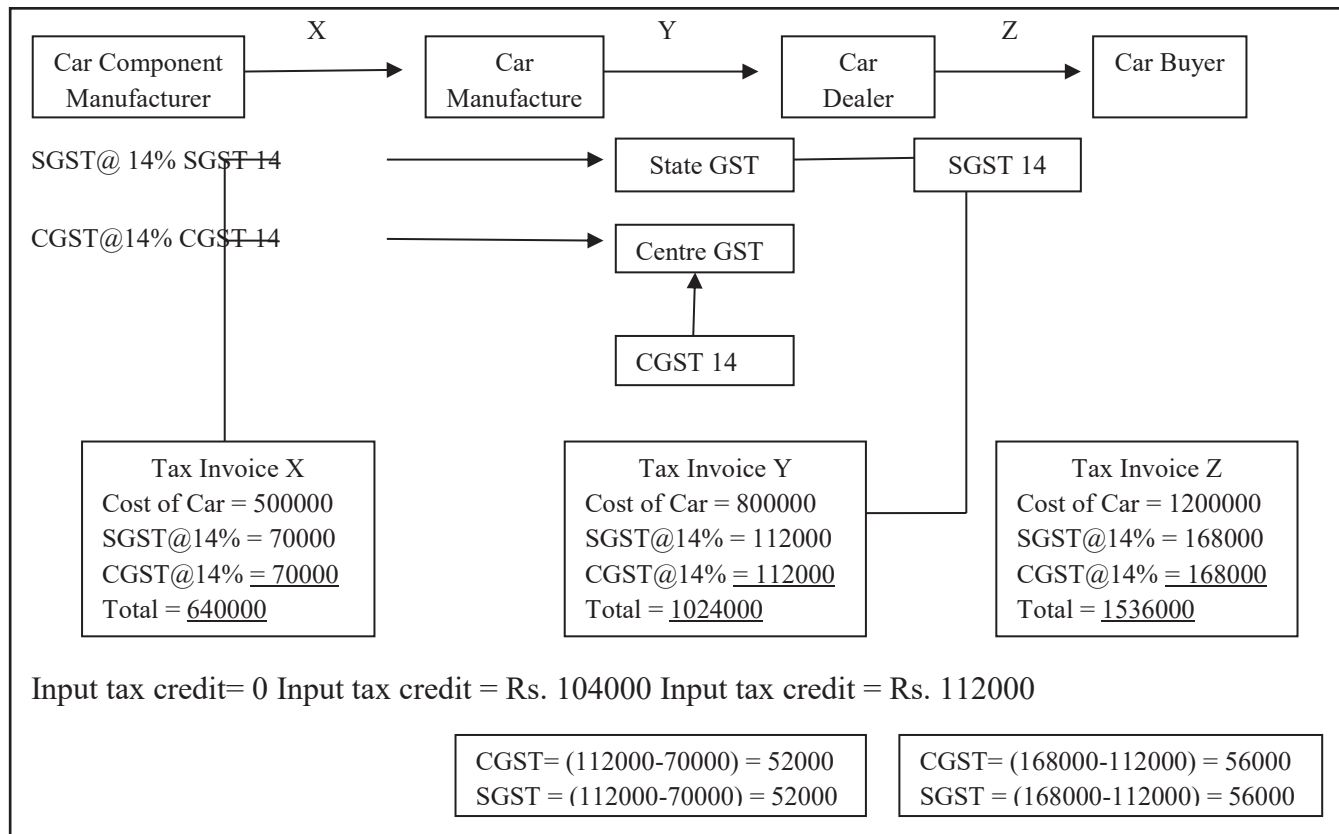


Fig. 2: GST Model (Applicable within State)

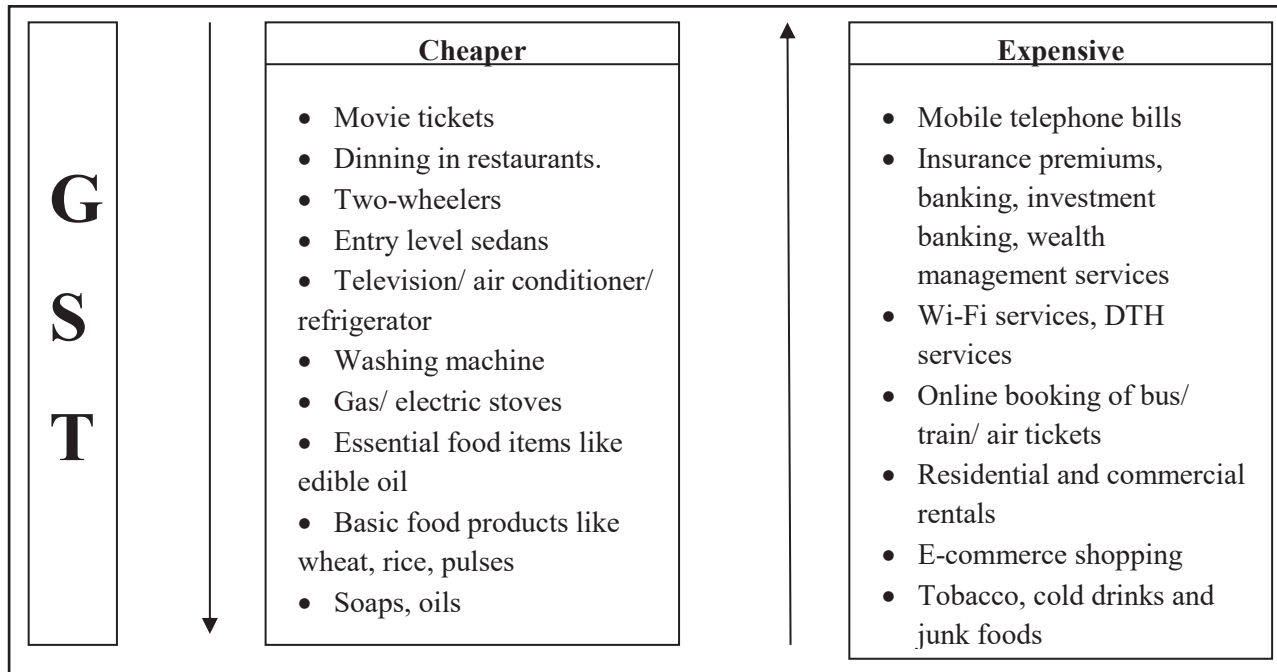
**POSITIVE IMPACTS**

Application of GST in India is going to witness several positive impacts in the economy. These are as follows:

- Reduction in number of indirect taxes with transparency in tax mechanism.
- GST will not be a cost to registered retailers; no hidden tax indicates cost of doing business is lower than earlier.
- Price will come down which in turn help consumers to satisfy their demand and consumption will increase.
- In modern society, cost of production and distribution of goods and services increased gradually because of several tax provisions under earlier tax system. Therefore, greater complications and administration including compliance cost stimulated the transaction values attributable to

value of goods and value of services for taxation purpose. Under GST system, it would be made possible to split the equity between manufacturing and services with an objective to reduce the production cost.

- It will help to construct a transparent and corruption free tax administration. Earlier tax structure provided a tax levied on manufacturer who paid the amount at the time when a finished product came out from factory; the same procedure may apply for the retailer at the time of sale. Therefore, cascading effect i.e. tax on tax stimulated high price of product that led to corruption. To overcome the issue, GST is introduced with provision of input tax credit and is expected to reduce tax burden issue on one hand and render transparent value added scientific levy of tax at each stage of consumption on the other. As per researchers, several goods are going to be expensive and cheaper after the implementation of GST in India. Some of the examples are shown in Fig. 3.



**Fig. 3: Effects of GST on Price of Product**

- Several researches predict that introduction of GST would help India to gain \$15 billion every year with the growth of exports, more employment opportunities, reduced burden of central and state government and overall growth of production that leads to higher gross domestic product (GDP) . The highest GST rate will definitely boost the tax to GDP ratio while giving financial muscle to the government for increasing the capital expenditure (Shaikh, Sameera, & Firoz, 2015).
- For Indian Business:
  - o Indirect benefit startups: Earlier VAT registration was mandatory for any business if their turnover exceeded Rs.5 lakh and in some states, it was Rs.10 lakh at the time of startup. But business with an annual turnover of over Rs.10 lakh (uniform across all states in India) is required to register for GST. Business with an annual turnover between Rs. 10-50 lakhs will be taxed at a lower rate additionally (Praharaj, 2017).
  - o Faster transportation of goods: Logistic sector will also be benefitted due to elimination of several indirect taxes that induce faster transportation by way of no hour-long waits at the sales tax check posts across borders.
  - o E-commerce will be benefitted a lot as GST will create a single unified market across India and allow free movement and supply of goods in every part of the country and reduce cascading effect.
  - o As per several research predictions, Indian domestic sector can achieve its targeted 3.5 percent share of world

exports by 2020 after the adoption of GST. Domestic goods will be produced and priced more competitively in international market and zero GST on export will turn exports cheaper than earlier.

- Increase in foreign investment: With reduction in cost after adopting GST, the goods manufactured within India will become more competitive in the world market, thus encouraging Indian export. Sectors like cement, building materials, automobiles, metal, consumer durables, entertainment, fast moving consumer goods will be apparently benefitted.
- Single tax will reduce both multiple tax burdens and commodity price in long run hence, consumer finally pays lesser amount at the final stage of consumption. Therefore, it will be termed as a development scheme for the economy with an aim of poverty elimination by generating more employment and work opportunity with more financial resources.

### NEGATIVE IMPACTS

Behind every light there is a dark waits. The statement is true in case of GST also. This new tax may have some negative impacts in Indian economy are as follows.

- This is a service-based tax and earlier service tax rate was 15%. As per economists, all the services especially telecom, banking, airlines etc. become more expensive after implementation of GST.
- The new tax mechanism is welcomed by India as it is

consumption-based tax. Some complications regarding the place of services where actual service is provided need to be determined. If actual benefit is not passed to consumer and the seller increases his profit margin, it will increase the price of the product.

- There is a debate on the issue proposed at the time of constitutional amended bill placed at Lok Sabha that allowed states to levy an additional 1% non-VAT tax on inter-state supply of goods for the initial two years, with an objective to compensate the states for loss of revenue while moving to GST.
- Four critical state level taxes have been excluded from GST, i.e. tax on petroleum products, electricity duties, excise duty on alcohol, and stamp duty on immovable property. Therefore, the theory behind GST as a single tax would subsume all central and state level tax to eliminate cascading effect is actually partially exercised.
- Robust IT backup connecting all state governments, trade and industry, banks and all other stakeholders on a real time basis with a software called goods and services tax network (GSTN) has to develop a GST portal front end system for trade and industry and back end system for all government agencies. All sorts of procedures such as registration, return filing, tax payment, IGST settlement, and all other dashboard on GST port to all stakeholders will require adequate technology support under GSTN. But the actual performance and results are yet to achieve.
- Both central and state governments have to reschedule their budget to bear additional cost for the implementation of the biggest tax revolution since 1947.
- The tax neutrality will not differentiate luxury good and normal goods. The present tax structure imposed higher rate of tax on luxury goods but under GST implementation same amount of tax will lead to rich becoming richer and poor becoming poorer. In case of micro small medium enterprises (MSMEs), this is not an ideal situation to compete with large business.
- In order to taxation of stock transfer, the impact will vary depending on stock turnaround time at warehouse, credit cycle to customers, quantum of stock transfer etc. will require higher working capital that increases interest costs and finally increases the price of finished product.

## SUGGESTIONS TO MINIMISE THE LOOPHOLES OF GST

Even though GST is one of the major taxation reforms regarding revenue collection since independence of India, there are some issues which disturb the public interest and common predefined objectives of the federal government.

Every possible measure should be taken into consideration after implementation of any new tax mechanism with the aforesaid study including the following:

- There should be a clear indication about type of product and tax rates individually for the benefit of all stakeholders and for transparent taxation system.
- In order to provide every possible sphere of business such as registration, filing of return, tax payment, IGST settlement with software based online system, adequate professional training will require eliminating the conception and application barriers of GST.
- Local self-government should take care of revenue collection under GST to decrease the vertical imbalances of resources and responsibilities among governments. Finance Commission should adopt sufficient measures in near future.
- Clear definition is needed to define goods and services individually, otherwise conflict may arise at every stage of revenue generation.
- Union government needs to co-ordinate with 30 states for “input credit” as transfer of credit in SGST. State tax officials need proper training and development to meet the issues.

## CONCLUSIONS

GST is the biggest tax reforms in the history of India since independence. The goal of GST is to get life simpler by replacing 17 indirect tax levies, result in fall of compliance cost, boost the public revenue, create a common market within states, increase investment, and finally make the concept of Make in India a success. Although GST fuels inflation in short run, but in a long run stakeholders will be benefitted. GST has the potential to affect cash flow, pricing, working capital, supply chain and IT systems. It will facilitate an opportunity to transform the business as a whole. Globally GST is acknowledged as a progressive tax regime with inbuilt efficiencies to broaden the tax base, decrease cascading effect and reduce revenue leakage. GST will bring down the tax burden on final consumers. As a result, price will fall, consumption and demand will go up, ultimate investment will increase, and GDP will go up. GST as ‘one point single taxation system’ renders helping hand for businessman at the time of price modalities, supply chain etc. without thinking too much about tax at later stages. The concept of ‘reverse charge’ as well as its recording, submission of return and adjustment with input tax credit at the time of exchange of goods and services between a registered dealer and an unregistered dealer in the field of education is an open area for future research. The paper work of GST bill predicts beneficial to all in terms

of easy calculations and implementation. In a nut shell, this tax system will establish the opportunity of corruption free transparent Indian revenue services in near future.

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