Decoding GST - Dual GST framework, rates & impact on Indian economy

Introduction

The spread of value added tax *('VAT')* and goods and services tax *('GST')* has shown an increasing trend over the last two decades. Most of the current experts and international authorities agree that out of 194 countries in existence over 160 countries have implemented VAT/GST. Most of these countries have a unified GST system barring countries like Brazil and Canada which follow a dual system wherein GST is levied by both federal and state or provincial governments. The latest is GST implemented in Malaysia in April 2015.

VAT was the first step in India's indirect tax reform process in the year 2005. Now, GST is a comprehensive tax likely to mark a landmark reform in the country's indirect tax system as it proposed to transition from existing, origin-based tax policy to destination-based tax policy.

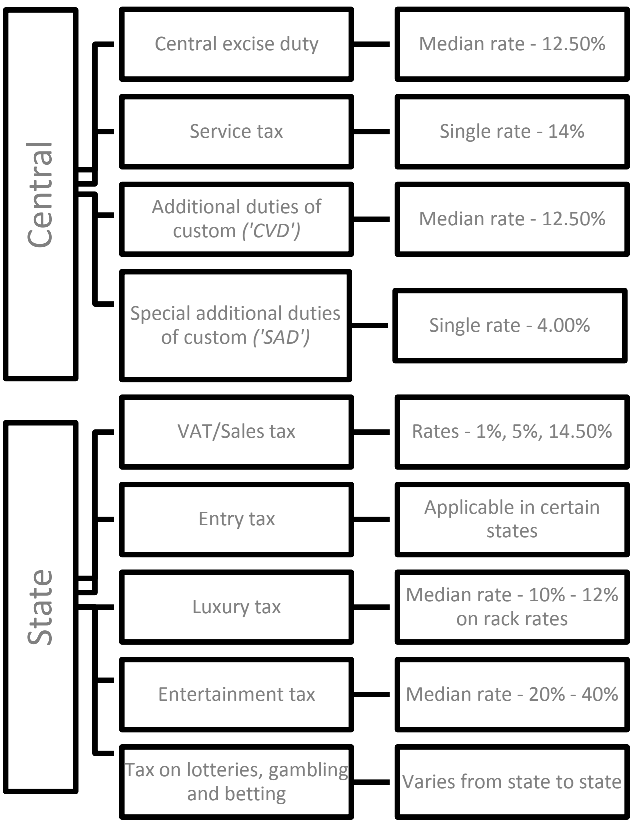
GST is based on the fundamental indirect tax principle of destination based consumption tax - France was the first country to introduce the concept of value-added tax in 1954 - At present, 160 out 194 countries have implemented VAT/GST - Brazil and Canada have implemented dual GST.

GST framework

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. India is planning to implement a dual GST system where central GST *('CGST')* and state GST *('SGST')* would be applicable. Under new laws, there will be no distinction between goods and services. By amalgamating a large number of central and state taxes, the new tax law will mitigate cascading or double taxation in a major way and pave way for a common national market.

The CGST and the SGST would be levied simultaneously on every transaction of supply of goods and services except, goods which are outside the purview of GST, the exempted goods and services 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 excise duty.

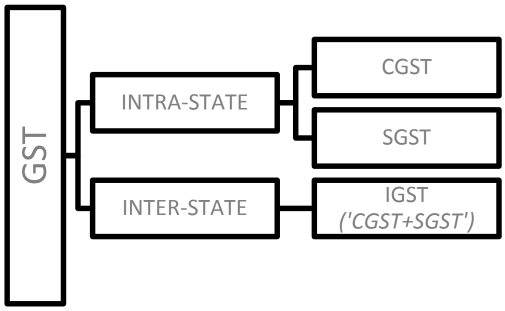
Further, it should also be noted that integrated GST *('IGST')* will not be a tax in addition to the CGST and SGST so one should not presume that IGST is a third tax but it is only a mechanism to monitor the inter-state trade of goods and services and further to ensure that the ultimate SGST which is collected by the centre as IGST is gone to the consumer state since the GST is a destination based tax.



Taxes to be subsumed

However, GST does not subsume/cover the following -

- Petroleum products;
- Entertainment and amusement tax levied and collected by panchayat/municipality/district council;
- Tax on alcohol/liquor consumption;
- Stamp duty, customs duty; &
- Tax on consumption and sale of electricity.



Proposed taxes under GST

World-wide VAT/GST rates

They say only death and taxes are certain in this world. Taxes amount to a large percentage of country's total available funds. Some countries have higher tax rates than others, thus procuring more funds for various government services and projects, but higher taxes don't necessarily have to yield better results. Lower taxes can and usually do attract various potent economic partners.

With the noted exception of Scandinavian countries, where the standard rate is 25%, only few countries have been successful in levying a high rate of GST. Successful models of GST suggest a rate of tax in the region of 10% or less.

Rates of GST - Indian scenario

There is some degree of divergence around the general contours of rates. Originally, it was thought it is better to specify the GST rate in the constitution amendment bill itself so that the mutually decided rate will remain unaltered for a reasonable period of time. However, the same was excluded from the amendment bill and will now be decided upon recommendation of GST council.

The panel under chief economic advisor *('CEA')* Arvind Subramanian, constituted by the government to decide GST rates, has recommended a revenue-neutral rate *('RNR')* of 15-15.5%. RNR is a single rate at which there will be no revenue loss to the centre and states in the GST regime. It has recommended a three-tier rate structure wherein some essential goods will be taxed at a lower rate of 12%; so-called demerit goods such as luxury cars, aerated beverages, pan masala and tobacco products at a higher rate of 40%; and all remaining goods at a standard rate of 17-18%.

Luxury items - 40%
Standard rate - 17% - 18%
Essential goods - 12%

The rates proposed by the Subramanian panel are much lower than the 27% rate initially arrived at by the national institute of public finance and policy *('NIPFP'),* the rate was too high. Subsequently, last year, NIPFP submitted its revised calculations. The report said that the standard rate could be in the range of 23-25% if goods are taxed at three different rates - special rate for precious metals, a lower merit rate for some important goods as well as a standard rate that will be applicable to most goods.

Impact of GST on Indian economy

By replacing a confusing mass of central, state, inter-state and local taxes - among the most common complaints of businesses - the GST is widely expected to transform India into a common market, bringing with it increased efficiency and productivity - simpler and transparent taxation regime.

The implementation of GST is going to help in widening of the tax base and increasing the taxes collections and streamlining the credits.

What experts have to say -

World Bank chief economist Kaushik Basu, who is believed to be in race for Reserve Bank of India governor's post, hails India's effort to implement GST saying that the single tax structure would provide further boost to Indian economy which has recently overtaken China in growth rate.

Outgoing RBI Governor Raghuram Rajan said that - "The Reserve Bank of India will have to watch for any impact on inflation from the new GST, which will harmonize 11 state and central levies into a national sales tax." Dr Rajan left key policy rates unchanged, as inflation hit a nearly two-year high, and he cautioned that price adjustment from GST could add to generalized inflation in the economy.

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