

# GS FOUNDATION FOR CSE 2024

## ECONOMY-15

### FISCAL POLICY-5

### TAXATION-3 – INDIRECT TAXES (GST)

#### 1. TABLE OF CONTENTS

2.	<i>Basics – Understanding Cascading Effect.....</i>	2
3.	<i>Problems That Existed Before GST System was enforced .....</i>	2
4.	<i>GST .....</i>	2
5.	<i>Advantages of GST.....</i>	4
6.	<i>Some other important features.....</i>	5
1)	<b>Threshold turnover for Applicability of GST .....</b>	5
2)	<b>Composition Scheme / Compounding Scheme.....</b>	5
3)	<i>GST Compensation Cess on Sin Goods – done separately in details .....</i>	6
7.	<i>Current GST Rates on Various items (As of Jan 2023).....</i>	6
1)	<i>50<sup>th</sup> Meeting of GST Council (July 2023) .....</i>	7
8.	<i>Other Important Aspects.....</i>	7
1)	<i>GST Network (GSTN) .....</i>	7
9.	<i>6 Years of GST – An analysis .....</i>	8
10.	<i>GST on Gaming Sector.....</i>	10

## 2. BASICS – UNDERSTANDING CASCADING EFFECT

## 3. PROBLEMS THAT EXISTED BEFORE GST SYSTEM WAS ENFORCED

- India had perennially marked the presence of one of the **most complicated indirect tax regimes**. This had been due to:
  - » **Cascading Effect:** Tax over tax led to very high effective tax rates.
  - » Divided powers between center and state to levy different taxes
  - » Distinction between goods and services
  - » Multiple tax rates and arbitrage on rates across the country (For e.g., different states had different sales tax rates) -> this led to different prices of same goods and services in different states -> fragmentation of India's market -> made doing business difficult
  - » Multiplicity of assessments
- **The GST regime** has fixed the above issues and ensure reform aims at simplifying the indirect tax regimes.

## 4. GST

- **Introduction**
  - » The GST is the most important indirect tax reform in recent years and it carried VAT to its logical conclusion. It was passed by Parliament in Aug 2016 through the 101st Constitutional Amendment Act and was rolled out from 1st July 2017.
- **Key Features:**
  - » It has subsumed several indirect taxes at central and state level and acts as one indirect tax for the whole nation on the supply of goods and services.
    - **Central taxes that GST has replaced**
      - **Excise Duties:** Central Excise Duty (except few fossil fuels and tobacco), Duties of Excise (medicinal and toilet preparation) and **Additional duties of excise** (goods of special importance)

- **Custom Duties:** **Additional duties of custom** (commonly known as Countervailing duty) and **Special additional duty** of custom (SAD)
- **Service Tax**
- **Cesses and surcharges** in so far as they relate to supply of goods and services.

▫ **State Taxes that GST has subsumed.**

- State VAT (except few fossil fuels and tobacco), Central Sales Tax, Purchase Tax, Luxury Tax, Entry tax (all forms), Entertainment Tax (other than those levied by local bodies), Tax on advertisement, Tax on lotteries, betting and gambling, State Cesses and surcharges.

» **Avoids Cascading** of taxes through **input tax credit (ITC)** mechanism.

▫ **Understanding the concept of Input Tax Credit** and how it removes cascading effect:

<b>Business:1</b> <ul style="list-style-type: none"> <li>• Input Cost = 0</li> <li>• Value Added = 100</li> <li>• Sale Price = Rs 100</li> <li>• GST (18% = 9% CGST, 9% SGST) = Rs 18</li> <li>• Invoice = Rs 18</li> </ul>	<b>Net Tax to Government =</b> Rs 18
<b>Business:2</b> <ul style="list-style-type: none"> <li>• Cost of Input = Rs 118</li> <li>• Value Added = Rs 500</li> <li>• <b>Input Tax Credit (GST Refund)</b> = Rs 18</li> <li>• <b>Sale Price</b> = Rs 600</li> <li>• <b>GST (18%)</b> = Rs 108</li> <li>• <b>Invoice</b> = Rs 708</li> </ul>	<b>Net Tax to Government =</b> 108 - 18 = 90 Rs 90

- Total tax that went to government = Rs 18 + Rs 90 (i.e. 18% of total value added (Rs 100 + Rs 500))
- Thus no cascading effect.
- Credits of input taxes paid at each stage is available in the subsequent stage of value addition. The final consumer thus bears only GST charged by the last dealer in the supply chain, with set-off benefits at all previous stages.

» It is applicable on **supply of goods and services** instead of earlier concept of tax on the manufacture or sale of goods or on provision of services. It is a **destination-based tax (Consumption based tax)**. Earlier indirect taxes were origin based.

- Note: At times GST is payable by the recipient of supply of goods and services or both instead of supplier of such goods and services. It is called "**reverse charge**".

» GST is a **dual tax** and centre and states are simultaneously levying it on a common base.

» An **integrated GST (IGST)** is levied on inter-state supply of goods and services.

- This is levied and collected by the centre so that the credit chain is not disrupted. Centre will then distribute IGST proceeds among the states.
  - » The IGST would roughly be equal to CGST plus SGST.

- » **Imports of goods or services** are deemed as supply of goods or services or both, in the course of inter-state trade or commerce and thus attract IGST.
  - Note: Basic custom duties which were levied on import of goods, continue to be levied in addition to IGST on imported goods.
  - **Earlier**, import of goods attracted Basic Customs Duty (BCD), Additional Customs Duty (ACD) and Special Additional Customs Duty (SAD).
    - Services attracted Service Tax or Research and Development cess in some instances.
  - **After GST Regime**
    - **Import of goods or services** are deemed as supply of goods or services or both, in the course of inter-state trade or commerce thus attracting IGST.
    - **Thus,**
      - **Import of Goods** attract BCD and IGST
      - **Import of Services** attract IGST
- » **Exports** are zero-rated.
  - The GST paid in the entire value chain and the IGST paid at the border is refunded/credited back to the suppliers. So, effectively there is not tax on exports and hence we can say that exports are "zero rated" supplies.
  - Supplies to SEZs are also zero rated.
- **GST Council** is a federal Constitutional authority created to give recommendations on the rates of taxes on different goods and services. It is chaired by Union Finance Minister.
  - **Some exceptions:**
    - GST is applicable on all goods and services except alcohol for human consumption.
      - This is the only item mentioned as an exception, all other sectors/goods will be included under GST.
    - GST on petroleum products would be applicable from a date to be recommended by GST Council.
    - **Tobacco and Tobacco** products are subjected to GST. **In Addition**, the centre would continue to levy central excise duty.
    - **Electricity:** As per the notification dated 28th June 2017 - '**Transmission or distribution of electricity** by an electricity transmission or distribution utility' are taxable under GST@ '**NIL**'.
- **Cross Utilization of Credit**
  - i. **Between CGST and SGST :** Credit of CGST paid on inputs may be used only for paying CGST on the output and the credit of SGST paid on inputs may be used only for paying SGST. In other words, the **two streams of input tax credit (ITC) cannot be cross utilized**, except in specified circumstances of inter-state supplies, for payment of IGST.
  - ii. **Cross Utilization Between Goods and Services** would be **allowed.**

## 5. ADVANTAGES OF GST

- i. **For Business and Industry->**

- » **Easy compliance** (online filing, single tax, less chance of harassment);
- » **Uniform tax rate** (common national market, easy expansion);
- » **Removal of cascading** (reduction of total tax payment); Increase competitiveness;
- » **gain for manufacturers and exporters.**

ii. **Advantages of Government (Center and State) ->**

- i. **Easy administration** (Single Tax, end to end IT system);
- ii. **Better control over leakage** (robust IT infra, simple tax structure -> easy compliance);
- iii. **Improved tax base.**
- iv. A more transparent basis for apply WTO's National Treatment Principle;
- v. **Higher revenue efficiency** (less cost of administration);
- vi. **Spur economic growth**;
- vii. **Reduced corruption**;
- viii. **Promote cooperative federalism** (In GST system center and states work together for the nation's benefit).

iii. **For Consumers/citizens ->**

- **Cheaper goods and services.**
- Higher revenue efficiency-More money with government -> More social initiatives;
- **Increased resource for resource consuming states** (as this is a destination-based tax).

## 6. SOME OTHER IMPORTANT FEATURES

### 1) **THRESHOLD TURNOVER FOR APPLICABILITY OF GST**

- **Initially**, threshold turnover for applicability of GST was Rs 20 lakh. For the special category states, it was Rs 10 lakh.
- **From 1st April 2019 for goods** the limit has been increased to Rs 40 lakhs for normal category states and Rs 20 lakh for Special category states.
  - » **For services**, there has been no change in limit (i.e. Rs 20 lakh and Rs 10 lack respectively)
  - » **However, the states were given choice** to opt for either the existing limits or the new limits. Some special category states also opted for the higher limit of Rs 40 lakhs for goods instead of Rs 20 lakhs.

### 2) **COMPOSITION SCHEME / COMPOUNDING SCHEME**

- **What is composition scheme?**
  - » It is an alternative method of tax levy under GST designed to simplify compliance and reduce costs for small taxpayers.
  - » The main feature of the scheme is that business or person who have decided to come under composition scheme can pay tax at a **flat percentage of turnover** every quarter, instead of paying tax at normal rate every month.
  - »
- **Who may opt for composition scheme?**

- » **Small manufacturers or traders** whose taxable business turnover is upto Rs 1.5 crore (Rs 75 lakh in case of NE-States),
- » A **service provider** whose taxable turnover is upto Rs 50 lakh.
- » **Exceptions:**
  - » Businesses with inter-state supply, manufacturers of ice cream, pan masala, and tobacco, and e-commerce players can't opt for composition scheme.
- **Rates:** 1% for manufacturers (0.5% CGST and 0.5% SGST), 5% for restaurants not serving alcohol and 6% for other service providers.
- **Note:** The tax is to be paid from taxpayers' own pocket without charging the customer. The words, "composition taxable person, not eligible to collect tax on supplies" should be mentioned at the top of every bill issued by the business.

### 3) GST COMPENSATION CESS ON SIN GOODS – DONE SEPARATELY IN DETAILS

## 7. CURRENT GST RATES ON VARIOUS ITEMS (AS OF JAN 2023)

A four-tier tax structure has been decided by GST council (5, 12, 18 and 28%) (Nov 3, 2016)

### 1. 0% (items of basic needs)



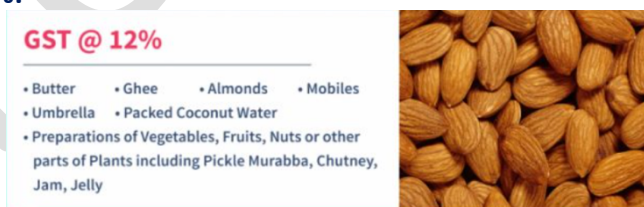
Unpacked food grains, unbranded atta, unbranded maida, besan, Prasad, Kajal, Education services and health services.

### 2. 5% - items of mass consumption which are used particularly by common people, green technologies (like Electric Vehicles)



Life saving drugs, Roasted Coffee Beans, Coffee (except instant) Mishti/Mithai (Indian sweets) etc.

### 3. 12%:



Computers, mobiles, Processed food, umbrella etc.

### 4. 18%: Pegged as standard rate - products for "lower middle class" and other products.



Soap, Corn flakes, Soup, Capital goods, Industrial intermediaries Toiletries etc.

5. **28%** - white goods, like non-luxury cars etc.

- **28% + Cess : Luxury car, aerated drinks, pan masala and tobacco products.**

28%	Small cars (+1% or 3% cess)	High-end motorcycles (+15% cess)
28%	Consumer durables such as AC and fridge	Beedis are NOT included here
28%		Luxury & sin items like BMWs, cigarettes and aerated drinks (+15% cess)

6. **Note:** There are few lesser used GST Rates like 3% and 0.25%

- Lowest rates for essential items and highest for luxury and de-merit goods that would also attract an additional cess was decided.
- With a view to keeping inflation under check, essential items including food, which presently constitute roughly half of consumer inflation basket, will be taxed at zero rate.

## 1) 50<sup>TH</sup> MEETING OF GST COUNCIL (JULY 2023)

- **Marking the 50th Meeting:**
  - » The Chairperson released a short video film titled 'GST Council-50 Steps towards a journey'. The film depicts the journey of the GST council and has been made in Hindi, English and 11 other regional languages.
  - » To mark the 50th meeting, the first set of a Special Cover and Customized 'My Stamp' were also presented to Chairperson and Members of the Council by the Chief Postmaster General, Delhi.
- **Key recommendation:**
  - » Reduction in the rate of uncooked/unfried snack pallets, by whatever name called, to **5%**.
  - » **GST rates on Services:**
    - GST exemption on satellite launch services supplied by ISRO, Antrix Corporation Limited and New Space India Limited (NSIL) may be extended to such services supplied by organizations in private sector also to encourage startups.
    - **Casino, Horse Racing and Online Gaming** to be taxed at the uniform rate of **28%**.

## 8. OTHER IMPORTANT ASPECTS

### 1) GST NETWORK (GSTN)

- **About GSTN**
  - GSTN is a not-for-profit company created under Section 8 of the Companies Act 2013. It provides the IT backbone of the GST system.



- ~~It is a private, not-for-profit company in which the central government and states and UTs together hold 49% (24.5% centre and 24.5% state. The rest 51% is owned by non-government financial institutions.~~
  - It provides shared IT infrastructure and services to central and state governments, tax payers and other stakeholders.
    - It is a portal on which all tax assesses have to register.
  - The **key objectives** of the GSTN are.
    - To provide a **standard and uniform interface to taxpayers**
    - Shared infrastructure and services to central and state/UT governments.
  - GSTN has developed a state-of-art comprehensive IT infrastructure including the common GST portal providing frontend services of registration, returns and payments to all taxpayers, as well as the backend IT modules for certain state that include processing or returns, registrations, audits, assessments, appeals etc.
  - There would be **no manual filing of returns**. All taxes can also be paid online. All miss-matched return will be autogenerated, and there would be no need for manual interventions.
- **Bringing 100% government ownership of GSTN**
- » Union Cabinet has approved increasing the government ownership in GSTN and change in the existing structure with transition plan (Sep 2018)
    - **51% equity of non-government institutions** in GSTN will be acquired equally by centre and states.
    - Now, Centre and State will have **50-50** ownership of GSTN.
    - **Board of the company** will also be restructured having 11 directors as follows:
      - a. Three directors will be center's nominee.
      - b. Three directors will be states' nominee
      - c. Three independent directors who shall be nominated by the Board of directors.
      - d. One chairman
      - e. One chief executive officer.
  - » **Why?**
    - GSTN has faced a number of issues (including crashes initially) which led to delays and difficulties in filing returns.

## 9. 6 YEARS OF GST – AN ANALYSIS

- **Positives:**
  - » **Tax base has increased** (Update)
    - Average monthly GST collections has increased to **1.55 lakh crore** in 2022-23.
    - **Number of GST taxpayers** have increased from 70 lakh in FY18 to **1.4 crore** in FY23.
    - **Small businesses and informal sectors** initially faced some issues, but many of them jumped to the tax net to take advantage of ITC.
    - **GSTN**, as a common technology platform has simplified tax compliance. It provides a one stop solution where key business process registration, payment of duties and filing of returns are done online in a transparent manner.
    - **Action taken against tax evaders, including steps being taken by tax authorities**, has resulted in better compliance and helped push the growth in GST collection.



- » **Facilitated free movement of goods and services and Increased efficiency of logistic supply chain:**
  - Earlier, check posts served as bottlenecks that not only involved a lot of waiting time but were also breeding spot for corruption - as tax varied from state to state, city to city and even local bodies.
- » **Reduced Tax Burden:** Overall tax on many essential use items have come down. Further, with input tax credit the cascading has been reduced.
  - For e.g. reduction in food inflation is one of the key features of GST regime.
- » **Push for Cooperative federalism:** GST Council has played a crucial role in forging a national consensus on key issues related to tax regime - rates, exemptions, business, processes, and movement of ITC.
- » **System has evolved to simplify tax compliance for MSME sector:** Recently, threshold exemption limit was increased from 20 lakh to 40 lakh for goods and Quarterly Returns and Monthly Payments (QRMP) system was introduced.
- » **Tax Evasion has reduced:**
  - E-Invoicing has become an integral part of doing business in India.
  - The GST number that can track every supply chain transaction has helped to address fraudulent claim.
  - **Coordination between CBIC and CBDT** has increased to ensure easy compliance.

#### - **Negatives/Limitations**

##### » **Federal Issues:**

- **Fiscal Autonomy reduces for states and ULBs** - states now have limited scope to raise their own revenue. ULBs are also much weaker and more dependent on state grants.
- It **harms the producer state and reward the consumer state** in terms of revenues.
  - States like TN which have invested heavily in their manufacturing ecosystem are now facing revenue challenges. GST compensation period has also ended. **After the end of GST compensation,** fiscal strain is expected in state budget as the median growth rate of subsumed tax in many states are much lower than 14%.

- » **GST Council decides the increase or decrease of tax rates** . Earlier, these powers were only with Parliament/state legislatures.

#### - **Criticism of keeping some items out of GST Net.**

- This goes against the principle of 'One nation one tax'. It also allows continuance of cascading.
- Further, sectors like airline industry is not able to get credit for taxes paid of jet fuel.
- Major black money generating sector such as real estate are out of the GST regime

#### - **Multiple Rates and Cess -> not a simple tax**

#### - **Advanced Economies like USA have also not moved onto GST path yet:** It is mostly due to their federal structure and federal autonomy.

#### - **Large businesses/units are reluctant to purchase from MSME sector** as they don't get ITC.

#### - **Delay in establishment of Appellate tribunal** related to GST is increasing the burden on Judiciary. Trapped GST refunds and numerous court cases are alarming.

- **Update:** On Sep 15, 2023, Centre has notified setting up of 31 GST appellate tribunal benches across the country to ensure quick resolution of disputes related to GST.

▪ **Way Forward:**

- **GST structure needs to be further simplified and rationalized**: This was recommended both by 15th Finance Commission and the Revenue Neutral Rate Report.
  - New structure should have lesser number of rates (preferably 2, but at max 3).
  - National Institute of Public Finance and Policy has also recommended a three rate framework of 8%, 15% and 30%.
- **Petroleum products** should be brought under GST regime. This should be followed by inclusion of real estate and electricity sector.
- **To increase the attractiveness of MSME sector** by large enterprises, amend the law to provide that all units buying from unregistered GST suppliers would have to pay duty on a reverse charge basis.
- **Set up GST Appellate Tribunal** as soon as possible as dispute resolution remains a pain point.
- Finally, **GST Council's working needs tweaking**.
  - During Vajpayee regime, Yashwant Sinha established a culture of consensual decision making on indirect taxes. He did this by requiring the Empowered Committee of State Finance Ministers to be headed by a finance minister from an opposition-run-state government, such as Asim Das Gupta from WB and Sushil Modi from Bihar. **This spirit can be translated in GST Council's functioning as well**.

## 10. GST ON GAMING SECTOR

- **Why in news?**

- » GST Council, in its 50th meeting in July 2023 decided to **levy a uniform 28% tax on full face value for online gaming, casinos, and horse-racing**. (July 2023)

- **About Online Gaming Market:**

- » The revenue of the Indian Mobile Gaming industry is expected to exceed \$1.5 billion in 2022 and is estimated to reach \$5 billion in 2025.
  - It grew at a rate of **38% CAGR** between 2017-20.

- **Details of GST Council's decision:**

- » The GST council has recommended a uniform levy of 28% tax on the face value of chips purchased in the case of casinos, on the full value of bet placed with bookmaker/totalizer in the case of horse racing, and on the full value of the bets placed in case of online gaming.
- » Government has now expected to bring amendment to the GST-related laws to include online gaming and horse racing in Schedule III as taxable actionable claims.

- **Significance:**

- » Increase in tax base.
- » The taxation aligns with the regulation of the MeitY.
- » **Moral suasion** to stay away from betting and online gaming addiction.
- » **Simplification and transparency** in the gaming sector.

▪ **Criticism:**

- Online gaming companies have said that this will be catastrophic for online gaming industry which have to compete with several international players.
- They also complaint that it will benefit illegal gaming platforms.
- **Nowhere in the world** is tax levied on the entire money that is pooled in online game. The levy of tax is always on the amount charged for the provisions of service and this can only be on the platform fee or service charge levied by any gaming company.
- **Negative impact on employment** in a sector which already employs more than 100,000 employees.

Levelup IAS