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What is GST in India? Goods & Services Tax Law Explained

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In this article, we take a closer look at what is GST (<https://cleartax.in/gst>) and the reason why it is making business and taxes simpler and easier.

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Feedback

1. What is GST?

GST is an Indirect Tax which has replaced many Indirect Taxes in India. The Goods and Service Tax Act was passed in the Parliament on 29th March 2017. The Act came into effect on 1st July 2017; Goods & Services Tax Law in India is a **comprehensive, multi-stage, destination-based tax** that is levied on every **value addition**.

In simple words, Goods and Service Tax (<https://cleartax.in/s/gst-full-form-meaning>) (GST) is an indirect tax levied on the supply of goods and services. This law has replaced many indirect tax laws that previously existed in India.

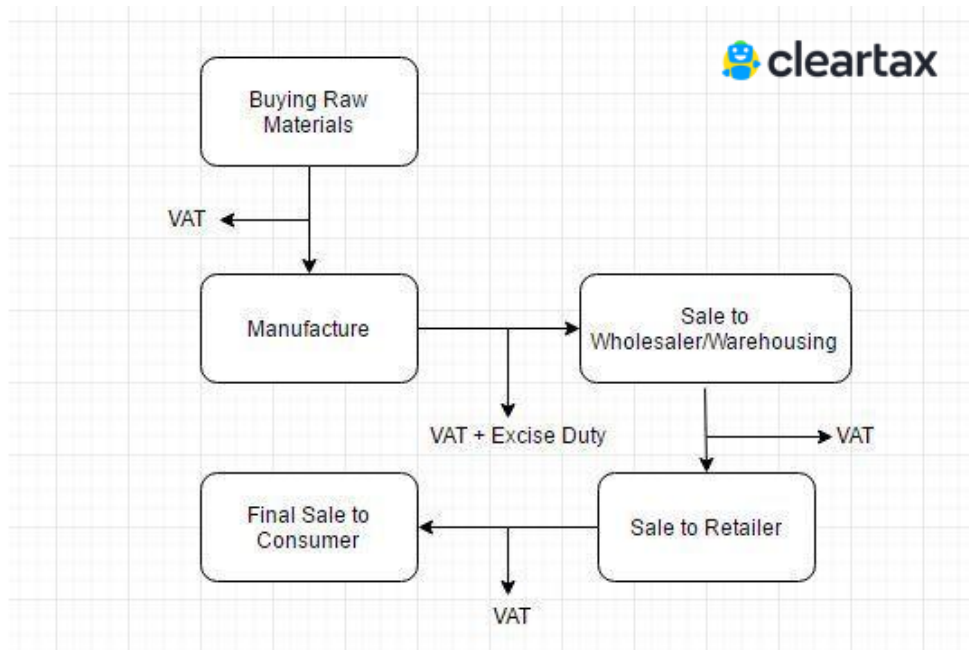
GST is **one indirect tax** for the **entire country**.

So, before Goods and Service Tax, the pattern of tax levy was as follows:

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File GST Returns



Under the GST regime, the tax will be levied at every point of sale. In case of intra-state sales, Central GST and State GST will be charged. Inter-state sales will be chargeable to Integrated GST.

Now let us try to understand the definition of Goods and Service Tax – “GST is a comprehensive, **multi-stage, destination-based tax** that will be levied on every **value addition**.”

Multi-stage

There are multiple change-of-hands an item goes through along its supply chain: from manufacture to final sale to the consumer.

Let us consider the following case:

- Purchase of raw materials
- Production or manufacture
- Warehousing of finished goods
- Sale to wholesaler
- Sale of the product to the retailer
- Sale to the end consumer



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Goods and Services Tax will be levied on each of these stages which makes it a multi-stage tax.

Value Addition



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Feedback

The manufacturer who makes biscuits buys flour, sugar and other material. The value of the inputs increases when the sugar and flour are mixed and baked into biscuits.

The manufacturer then sells the biscuits to the warehousing agent who packs large quantities of biscuits and labels it. That is another addition of value after which the warehouse sells it to the retailer.

The retailer packages the biscuits in smaller quantities and invests in the marketing of the biscuits thus increasing its value.

GST will be levied on these value additions i.e. the monetary worth added at each stage to achieve the final sale to the end customer.

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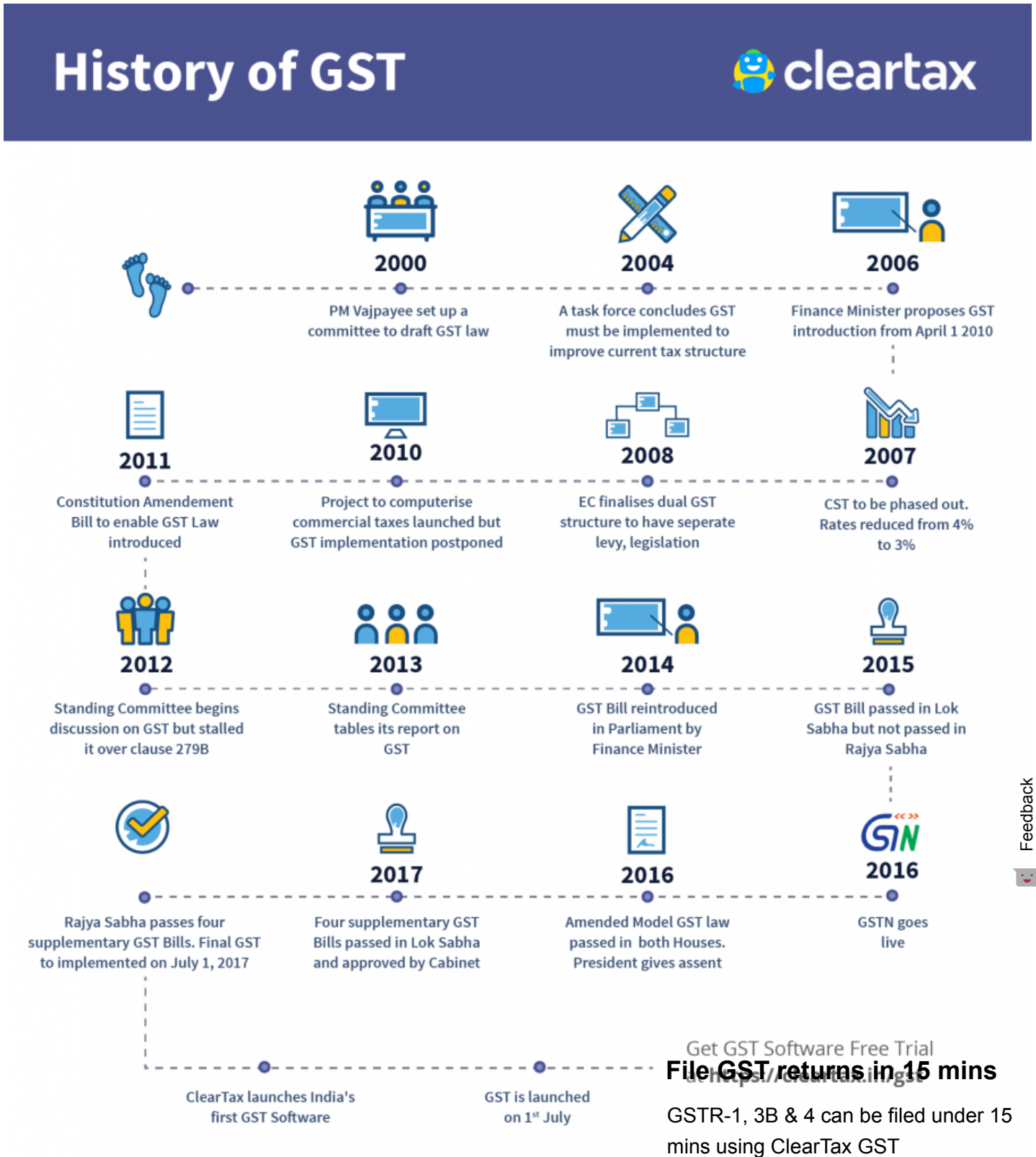
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Destination-Based

Consider goods manufactured in Maharashtra and are sold to the final consumer in Karnataka. Since Goods & Service Tax is levied at the point of consumption, in this case, Karnataka, the entire tax revenue will go to Karnataka and not Maharashtra.

2. Journey of GST in India

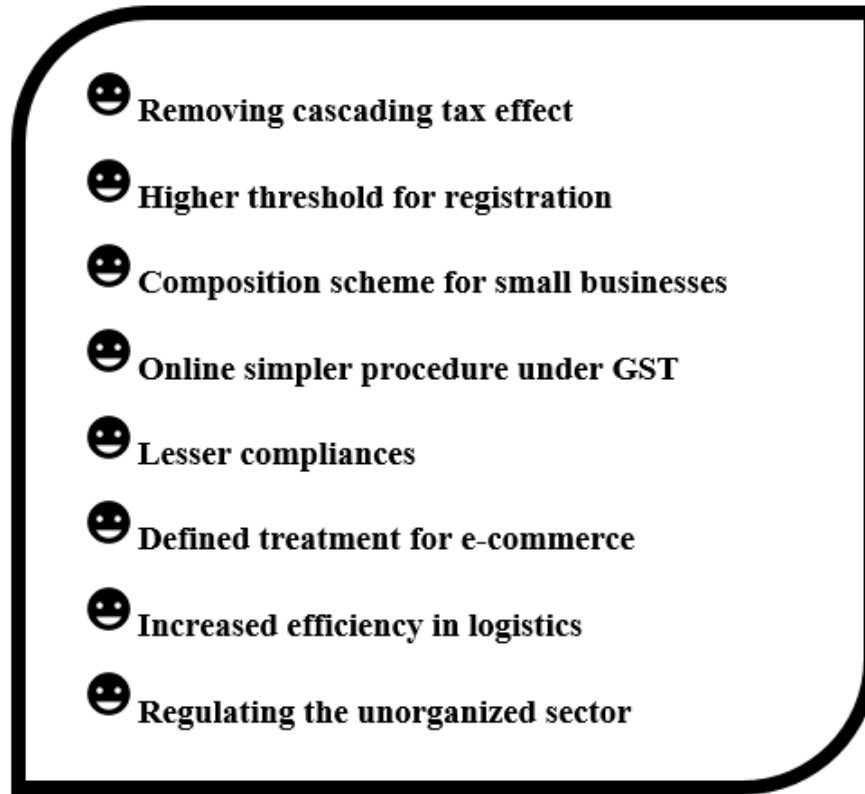
The GST journey began in the year 2000 when a committee was set up to draft law. It took 17 years from then for the Law to evolve. In 2017 the GST Bill was passed in the Lok Sabha and Rajya Sabha. On 1st July 2017 the GST Law came into force.



3. Advantages Of GST

GST will mainly remove the Cascading effect on the sale of goods and services. Removal of cascading effect will directly impact the cost of goods. Since tax on tax is eliminated in this regime, the cost of goods decreases.

GST is also mainly technologically driven. All activities like registration, return filing, application for refund and response to notice needs to be done online on the GST Portal. This will speed up the processes.



4. What are the components of GST?

There are 3 taxes applicable under this system: CGST, SGST & IGST (<https://cleartax.in/s/what-is-sgst-cgst-igst>).

- **CGST:** Collected by the Central Government on an intra-state sale (Eg: transaction happening within Maharashtra)
- **SGST:** Collected by the State Government on an intra-state sale (Eg: transaction happening within Maharashtra)
- **IGST:** Collected by the Central Government for inter-state sale (Eg: Maharashtra to Tamil Nadu)

In most cases, the tax structure under the new regime will be as follows:

Transaction	New Regime	Old Regime	
Sale within the State	CGST + SGST	VAT + Central Excise/Service tax	Revenue will be shared equally between the Centre and the State
Sale to another State	IGST	Central Sales Tax + Excise/Service Tax	There will only be one type of tax (central) in case of inter-state sales. The Center will then share the IGST revenue based on the destination of goods.

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Illustration:

- Let us assume that a dealer in Gujarat had sold the goods to a dealer in Punjab worth Rs. 50,000. The tax rate is 18% comprising of only IGST.

In such case, the dealer has to charge Rs. 9,000 as IGST. This revenue will go to the Central Government.

- The same dealer sells goods to a consumer in Gujarat worth Rs. 50,000. The GST rate on the good is 12%. This rate comprises of CGST at 6% and SGST at 6%.

The dealer has to collect Rs. 6,000 as Goods and Service Tax. Rs. 3,000 will go to the Central Government and Rs. 3,000 will go to the Gujarat government as the sale is within the state.

5. Tax Laws before GST

In the earlier indirect tax regime, there were many indirect taxes levied by both state and center. States mainly collected taxes in the form of Value Added Tax (VAT). Every state had a different set of rules and regulations.

Interstate sale of goods was taxed by the Center. CST (Central State Tax) was applicable in case of interstate sale of goods. Other than above there were many indirect taxes like entertainment tax, octroi and local tax that was levied by state and center.

This lead to a lot of overlapping of taxes levied by both state and center.

For example, when goods were manufactured and sold Excise Duty charged by the center was charged by the center. Over and above Excise Duty, VAT was also charged by the State. This lead to a tax on tax also known as cascading effect of taxes.

The following is the list of indirect taxes in the pre-GST regime:

- Central Excise Duty
- Duties of Excise
- Additional Duties of Excise
- Additional Duties of Customs
- Special Additional Duty of Customs
- Cess
- State VAT
- Central Sales Tax
- Purchase Tax
- Luxury Tax
- Entertainment Tax
- Entry Tax
- Taxes on advertisements
- Taxes on lotteries, betting, and gambling

CGST, SGST, and IGST has replaced all the above taxes.

However, the chargeability of CST for Inter-state purchase at a concessional rate of 2%, by issue and utilisation of c-Form is still prevalent for certain Non-GST goods such as:

- (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.

in respect of following transactions only:

- Resale
- Use in manufacturing or processing
- Use in the telecommunication network or in mining or in the generation or distribution of electricity or any other power

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6. What changes has GST brought in?

In the pre-GST regime, every purchaser including the final consumer paid tax on tax. This tax on tax is called Cascading Effect of Taxes.

GST avoids this cascading effect as the tax is calculated only on the value-add at each stage of transfer of ownership. Understand what the cascading effect is and how GST helps by watching this simple video:

GST Basics 02 - Cascading Effect Of The Current Tax Struc...



This indirect tax system under GST improve the collection of taxes as well as boost the development of Indian economy by removing the indirect tax barriers between states and integrating the country through a uniform tax rate.

Illustration:

Based on the above example of biscuit manufacturer along with some numbers, let's see what happens to the cost of goods and the taxes in the earlier and GST regimes.

Tax calculations in earlier regime:

Action	Cost	10% Tax	Total
Manufacturer	1,000	100	1,100
Warehouse adds label and repacks @ 300	1,400	140	1,540
Retailer advertises @ 500	2,040	204	2,244
Total	1,800	444	2,244

Along the way, the tax liability was passed on at every stage of the transaction and the final liability comes to rest with the customer. This is called the **Cascading Effect of Taxes** where a tax is paid on tax and the value of the item keeps increasing every time this happens.

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Tax calculations in current regime:

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Action	Cost	10% Tax	mins using ClearTax GST Actual Liability	Total
Manufacturer	1,000	100	100	1,100

Warehouse adds label and repacks @ 300	1,300	130	30	1,430
Retailer advertises @ 500	1,800	180	50	1,980
Total	1,800		180	1,980

In the case of Goods and Services Tax, there is a way to claim credit for tax paid in acquiring input. What happens in this case is, the individual who has paid a tax already can claim credit for this tax when he submits his taxes.

In the end, every time an individual is able to claim input tax credit (<https://cleartax.in/s/what-is-input-credit-and-how-to-claim-it>), the sale price is reduced and the cost price for the buyer is reduced because of a lower tax liability. The final value of the biscuits is therefore reduced from Rs. 2,244 to Rs. 1,980, thus reducing the tax burden on the final customer.

GST also brought with it a single nation-wide system of waybills by the introduction of “E-way bills”. This system started on 1st April 2018 for Inter-state movement of goods and 15th April 2018 for intra-state movement of goods in a staggered manner. By this system, manufacturers, traders & transporters are benefitted by a common portal where e-way bills can be generated and presence of its visibility to all stakeholders in the process of moving goods from the place of its origin to its destination. Tax authorities are also in vantage as this reduces the time at check -posts and help reduce tax evasion.

For further reading and understanding, check out our articles:

- Know about gst.gov.in (<https://cleartax.in/s/all-about-gst-gov-in-gst-portal>)
- GST Council (<https://cleartax.in/s/gst-council>)
- EWay Bill Guide for rules (<https://cleartax.in/s/eway-bill-gst-rules-compliance>)
- Guide on How to login to GSTN (<https://cleartax.in/s/cleartax-guide-on-gst-portal>)
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- View your Form 26AS (<https://cleartax.in/s/view-form-26as-tax-credit-statement>)
- What is Form 16 (<https://cleartax.in/s/what-is-form-16>)
- Salary Income (<https://cleartax.in/s/salary-income>)

File Income Tax Return (<https://cleartax.in/income-tax-efiling>)

- Guide to Income Tax (<https://cleartax.in/s/income-tax>)
- Guide to Efiling (<https://cleartax.in/s/efiling-income-tax-return>)
- Secion 80 Deductions (<https://cleartax.in/s/80c-80-deductions>)
- NRI (<https://cleartax.in/s/income-tax-for-nri>)
- Capital Gains Income (<https://cleartax.in/s/capital-gains-income>)
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