INTRODUCTION OF GST INTO THE INDIAN TAX SYSTEM

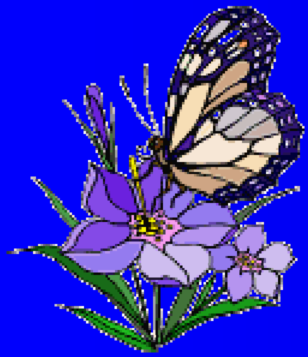
INTRODUCTION

GST stands for Goods and Services Tax. It is a domestic trade tax that will be levied in the form of a value added tax on all goods and services - in practice with some exemptions.

A value added tax exempts all inputs including capital goods. Hence, it becomes a general tax on domestic consumption.

It is a convenient and economically efficient way of taxing consumption.

If it is levied at a single rate and there are only very few exemptions, it becomes a proportional tax on consumption.



In order to ensure that the tax burden is distributed according to the consumption of different individuals, it must be levied on the basis of the principle of destination, that is to say that the tax on a good should go to the state in which the concerned consumer lives. This automatically takes place if the tax is levied at only the central level, or if the state is a unitary one with only one level of taxation.

In a federation, there are special problems to be solved if GST is to be levied at the level of the states as well as the federal government.

There are two angles from which to look at the question:

a) economic

b) federal

Economic: ensuring the application of the principle of destination.

As far as goods are concerned, this can be done by granting zero-rating privilege for all inter-state sales. The precise location of the delivery of services is more difficult in the case of services rendered across different states.

For example,

A railway traveler buys a ticket to travel from a station in State A. The Railways should pass on the amount to the State A, but the Railways might have paid taxes to State A on inputs bought there. These taxes must be deducted from what is collected on tickets bought from within State A. An elaborate system of accounting will be needed.

It would be of great benefit to the taxmen and the Railways, if GST on Railway Services were made a purely Central tax whose proceeds could be shared with the states. The same could be true of telecom services.

Federal angle

In order that there is state autonomy, the states must have enough resources of their own. That is why the Constitution makers assigned to the central government only excises i.e. the central government could levy domestic trade tax only at the manufacturing stage.

The states are authorized to levy sales tax on goods at all stages. Income tax on non-agricultural income can be levied only by the central government.

Thus, the distribution of taxing powers between the Central government and the states is evenly balanced, by providing the central government with some money to be transferred to the states.

The introduction of a single GST at the Central level, absorbing the state VATs into it would destroy state autonomy.

A single GST along the lines suggested by the Vijay Joshi Task Force is not advisable.

In tax matters, where inter-governmental relations are concerned, we should not look for perfect solutions. Practicability is a criterion that needs to be kept in mind.

There is one other aspect: The states have been given the power to levy taxes only on a few services such as the passengers and goods tax. As part of the introduction of GST, they wish to be given the power to levy tax on all services along with the Central government.

We have argued earlier that the Central government may be empowered to levy goods tax only at the manufacturing stage. Similarly, we argue here that the states may be allowed to levy tax only on services sold generally internally – i.e. within the states, not inter-state services like railways, airways and transport. Taxes on these services may be levied by the central government and a part of it may be given to the states.

By limiting the reforms to these changes only :

We will

a) prevent the Central Government from raising a very high proportion of GST, cutting into tax autonomy of the states and their power to experiment

b) Avoid having to add substantially to the strength of tax collectors in order to collect tax at wholesale and retail stages, and

c) Avoid making the system of taxing services very complicated.

Two final points:

1) The current average rate of Cenvat is 16 per cent. The states are trying to have an average rate of 12.5 per cent for State VAT.

Now, of course, Cenvat is applied only to the manufacturing stage, there are many exemptions and the states are not taxing most services.

For a comprehensive GST, an average rate of 28.5 per cent would be too high.

Simultaneously, with the settling of the GST format, an attempt should be made to put the taxation of petroleum products on a national footing. Taxation of petroleum products must be made part of GST. The states could be allowed to levy this part. An additional non-rebatable levy should be levied by the central government as a regulatory measure.

My suggestions on GST format for India

a) Dual GST

1. On goods, GST will be levied by the central government as now at the manufacturing stage.
2. At subsequent stages, GST will be levied by the states on their own behalf and also on behalf of the central government.

b) Split of Service Tax

1. The central government will levy GST on services except for small local services. Their proceeds will be shared with the states.