

Goods and services tax

[Economics](#), [Tax](#)



K SYMBIOSIS INSTITUTE OF MANAGEMENT STUDIES Goods & Services Tax Report submitted to Dr. Dharendra Deshpande in partial fulfillment for the degree of Masters in Business Administration Symbiosis International University, Pune Abstract: This report is an attempt to understand the impact of GST on Indian economy. The report defines Sales Tax and Value-Added Tax (VAT). It then looks at the Goods and Services Tax (GST) design in India which has been adapted to suit the Indian taxation system.

The report ends with the probable impact of GST on Indian economy and the limitations of the implementation of GST. ? Contents Introduction3 Sales Tax3 Types of sales tax3 Sales tax in India4 Value- Added Tax (VAT)6 Importance of VAT in India6 Advantages Of VAT6 Disadvantages of VAT7 Items covered under VAT7 Tax implication under Value Added Tax Act8 VAT vs. Sales Tax8 Goods and Services Tax (GST)10 Introduction10 The Need for GST10 Benefits of GST11 How GST Will Work12 GST vs. VAT14 GST vs. SALES TAX15 Limitation of GST16 Introduction

This report is an attempt to understand the impact of GST on Indian economy. The report starts by defining Sales Tax and Value-Added Tax (VAT). It then looks at the Goods and Services Tax (GST) design in India which has been adapted to suit the Indian taxation system. The report ends with the probable impact of GST on Indian economy. Sales Tax A sales tax is a tax paid to a governing body by a seller for the sales of certain goods and services. Laws allow the seller to collect funds for the tax from the consumer at the point of purchase.

Laws may allow sellers to itemiz (state item by item) the tax separately from the price of the goods or services, or require it to be included in the price

<https://assignbuster.com/goods-and-services-tax/>

(tax-inclusive). The tax amount is usually calculated by applying a percentage rate to the taxable price of a sale. When a tax on goods or services is paid to a governing body directly by a consumer, it is usually called a use tax. Often laws provide for the exemption of certain goods or services from sales and use tax. Types of sales tax

Gross receipts taxes: This tax has been criticized for its "cascading" or "pyramiding" effect, in which an item is taxed more than once as it makes its way from production to final retail sale.

- Excise taxes:** Applied to a narrow range of products, such as gasoline or alcohol, usually imposed on the producer or wholesaler rather than the retail seller.
- Use tax:** Imposed directly on the consumer of goods purchased without sales tax, generally items purchased from a vendor who is not under the jurisdiction of the taxing authority (e. g. , a vendor in another state).

Use taxes are commonly imposed by states with a sales tax, but are usually only enforced for large items such as automobiles and boats.

- Securities turnover excise tax** on the trade of securities.
- Value added taxes:** In which tax is charged on all sales, thus avoiding the need for a system of resale certificates. Tax cascading is avoided by applying the tax only to the difference ("value added") between the price paid by the first purchaser and the price paid by each subsequent purchaser of the same item.
- Fair Tax:** A proposed federal sales tax, intended to replace the U. S. federal income tax.
- Turnover tax:** Similar to a sales tax, but applied to intermediate and possibly capital goods as an indirect tax.

Sales tax in India

Central Sales tax is generally payable on the sale of all goods by a dealer in the course of inter-state Trade or commerce or, outside a State or, in the course of import

into or, export from India. According to S3, a sale or purchase shall be deemed to take place in the course of interstate trade or commerce in the following cases: 1. When the sale or purchase occasions the movement of goods from one State to another; 2.

When the sale is affected by a transfer of documents of title to the goods during their movement from one State to another. Where the goods are delivered to a carrier or other bailee for transmission, the movement of the goods for the purpose of clause (b) above, is deemed to start at the time of such delivery and terminate at the time when delivery is taken from such carrier or bailee. Also, when the movement of goods starts and terminates in the same State, it shall not be deemed to be a movement of goods from one State to another.

To make a sale as one in the course of interstate trade, there must be an obligation to transport the goods outside the state. The obligation may be of the seller or the buyer. It may arise by reason of statute or contract between the parties or from mutual understanding or agreement between them or, even from the nature of the transaction, which linked the sale to such transaction. There must be a contract between the seller and the buyer. According to the terms of the contract, the goods must be moved from one state to another.

If there is no contract, then there is no inter-state sale. There can be an interstate sale even if the buyer and the seller belong to the same state; even if the goods move from one state to another as a result of a contract of sale; or, the goods are sold while they are in transit by transfer of documents. Sales tax is payable to the sales tax authority in the state from

which the movement of goods commences. It is to be paid by every dealer on the sale of any goods effected by him in the course of inter-state trade or commerce, notwithstanding that no liability to tax on the sale of goods arises under the tax laws of the appropriate state. No state can levy sales tax on any sale or purchase where such sale or purchase takes place •outside the state and •in the course of import of goods into or export of goods outside India. Only the parliament can levy tax on inter-state sale or purchase of goods Not all despatches of goods from one state to another result in inter state sales rather the movement must be on account of a covenant or incident of the contract of sales.

There are some instances wherein the goods are moved out of the selling state and yet they are not considered inter state sales :- 1. Intra-state sales 2. Stock transfer from head office to branch & vice versa 3. Import and Export sales or purchases 4. Sale through commission agent / on account sales 5. Delivery of Goods for executing works contract Exceptions in the sales tax include: 1. Sales to resellers such as wholesalers and retailers that have a valid state resale certificate. 2.

Sales to tax-exempt institutions such as schools or charities Value- Added Tax (VAT) VAT is a multi point levy where the tax paid on local purchases from the registered dealer can be set off against the tax payable on the sale of goods, other than special goods. Example: Consider the manufacture and sale of any item, which in this case we will call a widget. In what follows, the term " gross margin" is used rather than " profit". Profit is only what is left after paying other costs, such as rent and personnel. Importance of VAT in India

India, particularly being a trading community, has always believed in accepting and adopting loopholes in any system administered by State or Centre. If a well-administered system comes in, it only closes options for traders and businessmen to evade paying their taxes, but also makes sure that they are compelled to keep proper records of sales and purchases. Under the VAT system, no exemptions are given and a tax is levied at every stage of manufacture of a product. At every stage of value-addition, the tax that is levied on the inputs can be claimed back from tax authorities.

At a macro level, two issues make the introduction of VAT critical for India. 1. Industry watchers believe that the VAT system, if enforced properly, will form part of the fiscal consolidation strategy for the country. It could, in fact, help address issues like fiscal deficit problem. Also the revenues estimated to be collected can actually mean lowering of fiscal deficit burden for the government. International Monetary Fund (IMF), in the semi-annual World Economic Outlook expressed its concern for India's large fiscal deficit - at 6 per cent of GDP. 2.

Moreover any globally accepted tax administrative system would only help India integrate better in the World Trade Organization regime Advantages Of VAT 1. Simplification - Under the CST Act, there are 8 types of tax rates- 1%, 2%, 4%, 8%, 10%, 12%, 20% and 25%. However, under the present VAT system, there are only 2 types of taxes 4% on declared goods and 10-12% on RNR. This will eliminate any disputes that relate to rates of tax and classification of goods as this is the most usual cause of litigation. It also helps to determine the relevant stage of the tax.

This is necessary as the CST Act stipulates that the tax levies at the first stage or the last stage differ. Consequently, the question of which stage of tax it falls under becomes another reason for litigation. Under the VAT system, tax is levied at each stage of the goods of sale or purchase.

2. Transparency - The tax that is levied at the first stage on the goods or sale or purchase is not transparent. This is because the amount of tax, which the goods have suffered, is not known at the subsequent stage. In the VAT system, the amount of tax is known at each and every stage of goods of sale or purchase.
3. Fair and Equitable - VAT introduces the uniform tax rates across the state so that unfair advantages cannot be taken while levying the tax.
4. Procedure of simplification - Procedures, relating to filing of returns, payment of tax, furnishing declaration and assessment are simplified under the VAT system so as to minimize any interface between the tax payer and the tax collector.
5. Minimize the Discretion - The VAT system proposes to minimize the discretion with the assessing officer so that every person is treated alike.

For example, there would be no discretion involved in the imposition of penalty, late filing of returns, non-filing of returns, late payment of tax or non-payment of tax or in case of tax evasion. Such system would be free from all these harassment

6. Computerization - The VAT proposes computerization which would focus on the tax evaders by generating Exception Report. In a large number of cases, no processing or scrutiny of returns would be required as it would free the tax compliant dealers from all the harassment which is so much a part of assessment.

The management information system, which would form a part of integral computerization, would make the tax department more efficient and responsive. Disadvantages of VAT

1. VAT is regressive
2. VAT is difficult to operate from position of both administration and business
3. VAT is inflationary
4. VAT favors capital intensive firms

Items covered under VAT

1. All business transactions that are carried on within a State by individuals/partnerships/ companies etc. are covered under VAT.
2. More than 550 items are covered under the new Indian VAT regime out of which 46 natural ; unprocessed local products will be exempt from VAT
- 3.

Nearly 270 items including drugs and medicines, all industrial and agricultural inputs, capital goods as well as declared goods attract 4 % VAT in India.

4. The remaining items attract 12. 5 % VAT. Precious metals such as gold and bullion will be taxed at 1%.
5. Petrol and diesel are kept out of the VAT regime in India.

Tax implication under Value Added Tax Act

Seller	Buyer	Selling Price (Excluding Tax)	Tax Rate	Invoice value (InclTax)	Tax Payable	Tax Credit	Net Tax	Outflow
AB	100	4%	104	4	0	0	4	4
BC	114	12.5%	128.25	14.25	14.25	0	14.25	14.25
CD	124	12.5%	139.50	15.50	15.50	14.25	1.25	1.25
D	Consumer	134	12.5%	150.75	16.75	15.50	1.25	1.25
Total to Govt. VAT CST								
16.75								

4. 00 VAT vs. Sales Tax

- VAT is a form of indirect tax which is imposed on products or services at different stages of manufacturing, where as Sales Tax is levied at the time of the purchase of the products or services.
- VAT is levied on both the producer and consumer while a sales tax is levied on only the end consumer.
- VAT involves tricky accounting while sales tax involves simpler accounting.
- VAT is applied at the various stages of production while sales tax is applied on the total value of the purchase. VAT efficiently avoids

evasion of taxes while a sales tax is unable to deal with this. •In VAT the method adopted is Input Tax Credit while Sales tax, liability of a dealer for a particular period is determined using the multiplication method. Goods and Services Tax (GST) Introduction Goods and Service Tax is a tax on goods and services, which is leviable at each point of sale or provision of service, in which at the time of sale of goods or providing the services the seller or service provider can claim the input credit of tax which he has paid while purchasing the goods or procuring the service. GST is the rate of tax remains the same but as per the necessity of the nation some goods or services can be declared as “ exempted” or “ Zero rated”. •A system Exports are zero rated and all the taxes paid while purchasing and manufacturing the goods including the taxes paid on raw material and services are returned to the exporter to make the exports competitive. •The sellers or service providers collect the tax from their customer, who may or may not be the ultimate customer, and before depositing the same to the exchequer, they deduct the tax they have already paid.

The Need for GST •Avoid cascading effect of taxation: A main reason of the introduction of GST is to avoid cascading effect of taxes in India. For example manufacturing of a product attract CENVAT (Central Value Added Tax) is a component of the tax structure employed by many countries in the western section of Europe. CENVAT is derived from a tax system that is generally referred to as VAT. The manufacturer pays CENVAT on goods produced. According VAT rules, the sales tax is payable on the aggregate selling price which include CENVAT. Here there is no set off benefits available. Shortfall of Existing VAT: Indirect taxes like luxury tax, entertainment tax, are yet to be

included in the VAT. These taxes are still existing and payable. •Shortfall of Existing CENVAT: Several taxes like additional customs duty, surcharges not included under CENVAT. Input tax and service tax set off is out of reach to the manufacturer and dealers. Benefits of GST •GST provide comprehensive and wider coverage of input credit setoff, you can use service tax credit for the payment of tax on sales of goods. •CST will be removed and need not pay.

At present there is no input tax credit available for CST. •Many indirect taxes in state and central level submit by GST, you need to pay single GST instead of all. •Uniformity of tax rates across the states. •Ensure better compliance due to aggregate tax rate reduces. •By reducing the tax burden the competitiveness of Indian products in international market is expected to increase and there by development of the nation. •Price of goods is expected to be reduced in the long run as the benefit of less tax burden would be passed on to the customer. Overall tax compliance cost will reduce for government and can concentrate on GST. How GST Will Work The dealers registered under GST (Manufacturers, Wholesalers and retailers and service providers) charge GST on the price of goods and services from their customers and claim credits for the GST included in the price of their own purchases of goods and services used by them. While GST is paid at each step in the supply chain of goods and services, the paying dealers don't actually bear the burden of the tax because GST is an indirect tax and ultimate burden of the GST has to be taken by the last customer.

This is because they include GST in the price of the goods and services they sell and can claim credits for the most GST included in the price of goods and

services they buy. The cost of GST is borne by the final consumer, who can't claim GST credits, i. e. input credit of the tax paid. How GST Will Work The dealers registered under GST (Manufacturers, Wholesalers and retailers and service providers) charge GST on the price of goods and services from their customers and claim credits for the GST included in the price of their own purchases of goods and services used by them.

While GST is paid at each step in the supply chain of goods and services, the paying dealers don't actually bear the burden of the tax because GST is an indirect tax and ultimate burden of the GST has to be taken by the last customer. This is because they include GST in the price of the goods and services they sell and can claim credits for the most GST included in the price of goods and services they buy. The cost of GST is borne by the final consumer, who can't claim GST credits, i. e. input credit of the tax paid.

Working

The illustration shown below indicates, in terms of a hypothetical example with a manufacturer, one wholesaler and one retailer, how GST will work. Let us suppose that GST rate is 10%, with the manufacturer making value addition of Rs. 30 on his purchases worth Rs. 100 of input of goods and services used in the manufacturing process. The manufacturer will then pay net GST of Rs. 3 after setting-off Rs. 10 as GST paid on his inputs (i. e. Input Tax Credit) from gross GST of Rs. 13. The manufacturer sells the goods to the wholesaler. When the wholesaler sells the same goods after making value addition of (say), Rs. 0, he pays net GST of only Rs. 2, after setting-off of Input Tax Credit of Rs. 13 from the gross GST of Rs. 15 to the manufacturer. Similarly, when a retailer sells the same goods after a value

addition of (say) Rs. 10, he pays net GST of only Re. 1, after setting-off Rs. 15 from his gross GST of Rs. 16 paid to wholesaler. Thus, the manufacturer, wholesaler and retailer have to pay only Rs. 6 (= Rs. 3+Rs. 2+Re. 1) as GST on the value addition along the entire value chain from the producer to the retailer, after setting-off GST paid at the earlier stages.

The overall burden of GST on the goods is thus much less. This is shown in the table below. The same illustration will hold in the case of final service provider as well.

Stage of supply chain	Purchase value	Input Value addition	Value at which supply of goods and services made to next stage	Rate of GST	GST on output	Input Tax credit	Net GST= GST on output + Input tax credit
Manufacturer	100	30	130	10%	13	10	13-10 = 3
Wholesaler	130	20	150	10%	15	13	15-13 = 2
Retailer	150	10	160	10%	16	15	16-15 = 1

The GST can be divided into following sections to understand it better: 1.

Charging Tax: The dealers registered under GST (Manufacturers, Wholesalers and Retailers and Service Providers) are required to charge GST at the specified rate of tax on goods and services that they supply to customers. The GST payable is included in the price paid by the recipient of the goods and services. The supplier must deposit this amount of GST with the Government.

2. Getting Credit of GST: If the recipient of goods or services is a registered dealer (Manufacturers, Wholesalers and Retailers and Service Providers), he will normally be able to claim a credit for the amount of GST he has paid, provided he holds a proper tax invoice.

This "input tax credit" is set off against any GST (Out Put), which the dealer charges on goods and services, which he supplies, to his customers.

3. Ultimate Burden of Tax on Last Customer: The net effect is that dealers

charge GST but do not keep it, and pay GST but get a credit for it. This means that they act essentially as collecting agents for the Government. The ultimate burden of the tax falls on the last and final consumer of the goods and services, as this person gets no credit for the GST paid by him to his sellers or service providers. 4. Registration: Dealers will have to register for GST.

These dealers will include the Suppliers, Manufacturers, Service Providers, Wholesalers and Retailers. If a dealer is not Registered, he normally cannot charge GST and cannot claim credit for the GST he pays and further cannot issue a tax invoice. 5. Tax Period: The tax period will have to be decided by the respective law and normally it is monthly and (or) quarterly. On a particular tax period, this is applicable to the dealer concerned; the dealer has to deposit the tax if his output credit is more. Than the input credit after considering the opening balance, if any, of the input credit. . Refunds: If for a tax period the input credit of a dealer is more than the output credit then he is eligible for refund subject to the provisions of law applicable in this respect. The excess may be carried forward to next period or may be refunded immediately depending upon the provision of law. 7. Exempted Goods and Services: Certain goods and services may be declared as exempted goods and services and in that case the input credit cannot be claimed on the GST paid for purchasing the raw material in this respect or GST paid on services used for providing such goods and services. 8.

Zero Rated Goods and Services: Generally, export of goods and services are zero-rated and in that case the GST paid by the exporters of these goods and services is refunded. This is the basic difference between Zero rated goods

and services and exempted goods and services. 9. Tax Invoice: Tax invoice is the basic and important document in the GST and a dealer registered under GST can issue a tax invoice and on the basis of this invoice the credit (Input) can be claimed. Normally a tax invoice must bear the name of supplying dealer, his tax identification nos. , address and tax invoice nos. coupled with the name and address of the purchasing dealer, his tax identification nos. , address and description of goods sold or service provided. Impact of GST on Economy - International Experiences: Most countries have adopted VAT system and GST is considered similar to a VAT system. It is possible that some economies that have adopted VAT system are actually a GST as well. So we really do not know the broad experiences of most economies and stick to countries which call their tax systems as GST based. GST system has been adopted in a few economies - Canada, Australia, New Zealand and Singapore.

Hong Kong proposed to introduce it but had to abandon it amidst stiff opposition. Over a long term there are improvements across the macroeconomic variables but there were short-term glitches. Inflation did seem to rise in the years of introduction but was mainly blamed on the administration for the same. The impact on revenue and current account has been very impressive with sharp gains seen in all the three economies. In Australia there was a more dramatic impact of GST on the economy. Before GST's implementation, consumers rushed to purchase goods that they perceived would be substantially more expensive post-GST.

After the tax, consumer consumption and economic growth declined sharply initially. In Q1 2000, Australian economy recorded negative economic growth

for the first time in more than 10 years. Consumption and growth soon returned to normal. There was some negative impact on price of real estate as well but the market rose and property prices and demand increased sharply in 2002-04. GST increased the real output of the Canadian economy by 1.4% of GDP, principally through an increase in the productivity of capital and total factor productivity. The sectors like transportation, utilities, services and agriculture experienced significant gains.

Following are the impacts of GST on Australia, New Zealand and Canada :

AUSTRALIA	NEW ZEALAND	CANADA	Price Changes	Short run	one off effect
				Short run spike in prices, no longer run increase	Short run spike in prices, no longer run increase, price regulatory body Criticize Economic Growth
				Introduced during sustained economic growth period	Introduced at the end of recession, subsequent upswing
				Introduced in midst of major recession, criticized as Compounding problems	Revenue Growth
				Revenue exceeded expectations	Revenue exceeded Expectations
				Revenue exceeded Expectations	Current Account
				Slight improvement	ince introduction
				Rapid immediate improvement, longer term stabilization	Dramatic Improvement
				since introduction of GST, NAFTA	GST vs. VAT

- Limitations in Centre VAT system: There is CENVAT but several taxes are still out of the ambit like surcharges, additional customs duties etc. In some goods we get input tax and not in others, making the tax filing system complex and cumbersome.
 - Limitations in State VAT system: The States also have VAT but again story is the same. Many taxes like luxury taxes, entertainment tax etc, are not included. There is no input tax credit in case of CENVAT paid on certain items.
- Interstate Sales Tax (CST): Though it is an

important source of revenue for states it is seen as very burdensome by businesses. The companies make goods in one state but on distribution inside the country, end up paying taxes in each state. They are supplying goods within the country and should just be taxed at one place.

- Inclusion of Services in VAT system: Production of goods is because of both physical production and services. But Services are taxed only by Centre and that too is done selectively. The Services need to be taxed at State level and integrated with the Goods VAT system as shown in the example above.

International Standard: GST is becoming an international standard and it is important India also has one. There are many factors before international companies while choosing a country for its business and taxation system is one very important factor. With other countries having GST and India not having one, the companies are likely to opt for former ahead of India for locating their businesses. Likewise Indian companies may also prefer to increasingly set their bases in other countries where tax system is more efficient.

GST vs. Sales Tax

- Single versus multiple stage

Unlike the existing sales tax, GST is generally charged on the consumption of goods and services at every stage of the supply chain, with the tax burden ultimately borne by the end consumer. This multiple tax levels feature of GST is the fundamental change from the present single-stage sales tax levied at only one stage of the supply chain.

- Goods and services subject to tax

GST operates on a negative concept - all goods and services are subject to GST unless specifically exempted. For sales tax, the same concept applies where all goods are taxable unless specifically exempted.

It is anticipated that the number of exemptions under the present sales tax regime would be significantly reduced. •Tax payment and accounting periods Time of supply is an important feature under the GST regime (method or system of government) as it determines when one should account for GST in the GST returns. The approach used by many countries when adopting GST is that a supply is considered to have taken place at the earliest by three events that the time is invoice issue, the time any payment is received by the supplier and the time a taxable supply is made.

The GST rules differ from the existing sales tax structure where sales tax becomes due and payable when there is a sale or disposal otherwise than by sale. •Group registration Group registration is included as a facility that allows companies to file consolidated GST returns. The objective is to reduce their GST administration costs where supplies made within a group would be disregarded for GST purposes. The facility could potentially result in better cash flow management for the group if goods and services are regularly supplied between group companies.

The existing sales tax and service tax structures do not allow consolidated tax filings. Limitation of GST There are two main limitations of GST •Inflation: Most of the international case studies show an inflation spurt in initial months of GST implementation. In Australia's case we saw spurt in prices of goods which Australian consumers Thought would become expensive after the GST. Much of blame for inflation is accorded to the various regulatory bodies and uncertainty over the new tax regime.

The inflation situation stabilizes as implementation gains pace and is understood by consumers and producers. In India's case inflation could be

critical as unlike developed countries profiled above, India has far more inefficiencies in supply chain in local markets. The Indian GST reform is far larger in scale compared to above economies. Indian economy is already plagued with persistent high inflation and this new reform could further test inflation further. •Tax Revenue Shortfall: RBI in the State Finances Report (2010-11) said the revenue implications of GST are likely to vary across states.

The Centre and the States are still discussing various aspects of GST like taxation rates, revenue sharing model between Centre and States etc. As there is still uncertainty over the final blueprint of GST, it is difficult to estimate the impact of GST on state finances. Other issues are enhancing the administrative capacity of states and building IT (Information technology) infrastructure to capture the full benefits of GST. The report points that VAT led to improvement in tax revenue for most states.