Issues for Consideration: The Goods and Services Tax Bills, 2017

The Central Goods and Services Tax Bill, 2017, the Integrated Goods and Services Tax Bill, 2017, the Union Territory Goods and Services Tax Bill, 2017, and the Goods and Services Tax (Compensation to States) Bill, 2017 were introduced in Lok Sabha on March 27, 2017.[1,2,3,4] This note provides the key features of the Bills and some issues for consideration.

Context

The Constitution (101st) Amendment Act, 2016 allows both the centre and states to levy the Goods and Services Tax (GST). Before the 2016 amendment, taxation powers were divided between the centre and states. For example, while the centre exclusively taxed services, the states exclusively taxed goods at the time of sale. The 2016 amendment replaces various central and state taxes such as excise duty, service tax, sales tax, entry tax and entertainment tax with GST. While most goods and services will be covered under GST, alcohol for human consumption will remain outside its purview. Petroleum products are initially outside its purview but may be brought under GST if the GST Council so decides.

Under the GST framework: (i) the centre will levy and collect the Central GST, (ii) the states will levy and collect the State GST, on supply of goods and services within a state. The centre will levy the Integrated GST (IGST) on inter-state supply of goods and services, and apportion the state's share of tax to the state where the good or service is consumed. The 2016 Act requires Parliament to compensate states for any revenue loss owing to the implementation of GST.

The 2016 Constitutional amendment creates a GST Council consisting of the Union Finance Minister and representatives from all states to implement GST. The Council decide upon subjects including: (i) GST rates, (ii) taxes to be subsumed under GST, (iii) goods and services to be covered under GST, (iv) model laws to be passed by Parliament and state assemblies, (v) apportionment of IGST, and (vi) special provisions for the North-Eastern or Himalayan states.

Goods and Services Tax Bills

The following are some key features of the (i) Central GST Bill, 2017, (ii) Union Territory GST Bill, (iii) Integrated GST Bill, 2017, and (iv) Goods and Services Tax (Compensation to States) Bill, 2017. The SGST Bills will be introduced in various state assemblies, and we have assumed that they would be similar to the Central GST Bill.

- **Levy of GST:** The centre will levy Central GST (CGST) and the states will levy State GST (SGST) on the supply of goods and services within a state. The centre will levy IGST in the case of (i) inter-state supply of goods and services, (ii) imports and exports, and (iii) supplies to and from special economic zones.
- **Tax rates**: The GST Council will recommend the tax rates with respect to CGST, SGST and IGST. The tax rates for each CGST and SGST will not exceed 20%. The tax rate of IGST will not exceed 40%. In addition, a cess will be levied on certain goods and services to compensate states for revenue loss (discussed later). The Central GST Bill allows certain taxpayers with turnover less than Rs 50 lakh to pay CGST at a flat rate on turnover (composition levy), instead of the value of supply of goods and services.
- **Date of liability**: The liability to pay GST in relation to supply of goods and services will arise on the date of: (i) issue of invoice, (ii) receipt of payment, whichever is earlier.
- **Exemptions from GST**: The centre may exempt certain goods and services from the purview of GST through a notification. This will be based on recommendations of the GST Council.
- **Taxable amount (value of supply):** The GST will be levied on the supply of goods and services, whose value will include: (i) price paid on the supply, (ii) taxes and duties levied under other tax laws, (iii) interest, late fee, penalties for delayed payments, among others.

Supply of goods and services

- **Place of supply of goods:** The Integrated GST Bill provides separate rules for goods and services to determine the place (state) of their supply. In cases where a good has been physically moved, the place of supply will be the final destination of the good. In other cases, the place of supply will be where the good is received by the recipient.
- **Place of supply of services:** Provisions with respect to determining the place of supply of services vary depending upon the nature of services. For example, place of supply for immovable property (such as

Aravind Gayam
aravind@prsindia.org

Vatsal Khullar
vatsal@prsindia.org

March 27, 2017

architects designing a building), will be the location of the immovable property. Specific provisions have also been made for supply of services such as catering, sporting events, transportation of goods, advertisement, telecommunications, among others.

- **Input tax credit**: Every taxpayer while paying taxes on outputs may take credit for taxes paid earlier by the supplier on inputs. However, this will not be applicable on supplies related to: (i) motor vehicles when used for personal consumption, (ii) supply of food, health services, etc. unless they are further used to make a supply.
- **Apportionment of IGST revenue**: The IGST collected will be apportioned between the centre and the state where the goods or services are consumed. The revenue will be apportioned to the centre at the CGST rate, and the remaining amount will be apportioned to the consuming state.
- **Registration of taxpayers**: Every person with a turnover exceeding Rs 20 lakh will have to register in every state in which he conducts business. This threshold will be Rs 10 lakh for special category states (i.e. Himalayan and North-Eastern states). A person may have multiple registrations for different business verticals in a state.
- **Returns:** Every taxpayer should self-assess and file tax returns on a monthly basis by submitting: (i) details of supplies provided, (ii) details of supplies received, and (iii) payment of tax. In addition to the monthly returns, an annual return will have to be filed by each taxpayer.
- **Refunds and welfare fund:** Any taxpayer may apply for refund of taxes in cases including: (i) payment of excess taxes, or (ii) unutilised input tax credit. The refund may be credited to the taxpayer, or to a Consumer Welfare Fund under certain circumstances.

Compensation to states for revenue loss

- **Compensation to states on loss of revenue**: States will be compensated by the centre for loss of revenue, due to the implementation of GST. Compensation will be provided for a period of five years from when the State GST Act comes into force. The compensation will be calculated and provided in the following way:
  - **Projected growth rate and base year**: The compensation amount will be calculated using revenue collections in 2015-16 as the base year. A growth rate of 14% per annum over the base year will be assumed. The base year tax revenue will consist of the states' tax revenues from: (i) Value Added Tax (VAT), (ii) central sales tax, (iii) entry tax, octroi, local body tax, (iv) taxes on luxuries, and (v) taxes on advertisements, among others. Revenue arising in relation to supply of alcohol for human consumption and certain petroleum products, will not be accounted in the base year revenue.
  - **Calculation and release of compensation**: The compensation payable to a state will be provisionally calculated and released at the end of every two months. An annual calculation of the total revenue will be undertaken, which will be audited by the Comptroller and Auditor General of India.
  - **Levy and compensation of GST compensation cess**: A GST Compensation Cess may be levied on the supply of certain goods and services, as recommended by the GST Council. The receipts from the cess will be deposited in a GST Compensation Fund. The receipts from the cess will be used for providing compensation to states for loss of revenue due to the implementation of GST. The cess will be capped at: (i) 135% for pan masala, (ii) Rs 400 per tonne for coal, (iii) Rs 4,170 + 290% per 1,000 sticks of tobacco, and (iv) 15% for all other goods and services including motor cars and aerated water.
  - Any unutilised money in the Compensation Fund at the end of the compensation period will be shared between the centre and states in the following manner: (i) 50% of the fund to be shared between the states in proportion of their SGST revenues, and (ii) the remaining 50% will be part of the centre's divisible pool of taxes.
- **Prosecution and appeal**: For offences such as mis-reporting of: (i) goods and services supplied, (ii) details furnished in invoices, a person may be fined, imprisoned, or both by the CGST Commissioner. Such orders can be appealed before the Goods and Services Tax Appellate Tribunal, and further before the High Court.
- **Transition to the new regime**: Taxpayers with unutilised input tax credit obtained under the current central excise and state VAT laws may utilise it under GST. In addition, businesses may also avail input tax credit on stock purchased before the implementation of GST.

Other provisions in the Bills

- **Anti-profiteering measure**: The central government may by law set up an authority to examine if reduction in tax rate has resulted in commensurate reduction in prices of goods and services. The powers of the authority will be prescribed by the government.

- **Compliance rating**: Every taxpayer shall be assigned a GST compliance rating score based on his record of compliance with the provisions of this Bill. The compliance rating score will be updated at periodic intervals and be placed in the public domain.

Issues for consideration

A. Multiple GST Tax Rate Structure *[Clauses 9 and 10, Central GST Bill, 2017]*

The Central GST Bill, 2017 allows the central government to notify rates at which CGST will be levied, subject to a cap of 20%. Further, businesses with turnover less than Rs 50 lakhs may choose to pay tax at a flat rate notified by the government (known as composition levy), which will be capped at 2.5%. This may lead to a few issues, which are discussed below.

Allowing government to notify CGST rates would not require parliamentary approval

The Central GST Bill, 2017 allows the central government to notify CGST rates, subject to a cap. This implies that the government may change rates subject to a cap of 20%, without requiring the approval of Parliament. Under the Constitution, the power to levy taxes is vested in Parliament an state legislatures.[5] Though the proposal to set the rates through delegated legislation meets this requirement, the question is whether it is appropriate to do so without prior parliamentary scrutiny and approval.

The Constitution does not allow a tax to be levied or collected except by authority of law.[6] Currently, most laws which levy taxes such as income tax, and service tax specify tax rates in the principal law, and any changes in these rates requires the approval of Parliament.[7,8] While, laws such as the Central Excise Tariff Act, 1985 allow government to notify a change in tax rates only in case of an emergency, these changes are subject to the tax rate, and certain restrictions and caps specified in the 1985 Act.[9]

A multiple tax rate structure maybe against the idea of GST

The Central GST Bill, 2017 provides for the centre to notify CGST rates, allowing for a multiple tax rate structure. The goods and services to be taxed at different rates will also be notified by the government. It may be argued that such a structure may be against the idea of a levying GST at a single rate on all goods and services.

Table 1: Structure suggested by the Expert Committee on Revenue Neutral Rate

Rate	RNR Report
Lower Rate (Items consumed by poor)	12%
Standard Rate (Most goods and services)	18%
Demerit Rate (Luxury items)	40%

Sources: Report on the Revenue Neutral Rate and Structure of Rates for the Goods and Services Tax; PRS.

In December 2015, the Expert Committee on the Revenue Neutral Rate for GST had suggested a three rate structure for GST (see Table 1).[10] However, while making this recommendation, the Committee had noted that 90% of the countries which have adopted GST, have opted for a single rate structure, which allows for easier tax administration. The 13th Finance Commission (2009) had recommended that GST should be levied at a single rate of 12%. It had added that goods and services such as education, health, and public services should be exempt from this tax.[11]

While a multiple tax structure may allow for controlling the impact of GST on prices of essential items, classifying goods and services under different slabs may be a complex exercise.[12] Currently, goods and services may be taxed at different rates across states owing to geographic, economic and cultural reasons. For example, coconut oil is taxed in Kerala at 5%, while in Uttar Pradesh, it is taxed at 12.5%.[13,14] Therefore, taxing each good and service at a particular rate will be a complex exercise as they cannot simply be moved to the nearest slab rate. A second disadvantage of a multiple rate structure is that it could lead to disputes on classification of goods and services.[15] .

B. GST levied on services delivered in a state may be consumed across multiple states *[Sections 2(14), 2(15), 12, Integrated GST Bill, 2017]*

Currently, services are taxed by the centre, and therefore the state where they are finally supplied and consumed does not matter for levying service tax. Under GST, states will also have the power to tax services, along with the centre. This means that states will levy SGST in case of intra-state supply of services, while the centre will levy IGST in case of inter-state supply of services and apportion a share of the revenue to the state which is the recipient of the service.

The general rule to determine the location of the recipient is his location or address on record; there are specific rules for various services such as telecom, property, transportation, etc. This means that while a service may be consumed across multiple states, the tax revenue would be attributed to the state where the recipient is registered or his office is located. This could lead to higher tax attributed to states that have more registered offices.

For example, a company A located in Mumbai advertises its products in the Patna edition of a newspaper, which has its registered office in Delhi. In this case, one may argue that the service is being finally consumed in Bihar. However, as the recipient of services is in Mumbai, the tax would accrue to Maharashtra.

C. Anti-profiteering authority *[Section 171, Central GST Bill, 2017]*

The Central GST Bill allows the central government to set up an anti-profiteering authority by law, or designate an existing authority to carry out the functions. The authority will be responsible for ensuring that the reduction of tax rates on account of implementation of GST results in a commensurate reduction in prices. It may be argued that this may allow the government to monitor and control prices of all goods and services, which may interfere with the idea of these prices being determined based on their demand and supply in the market.

Note that the price a good or service is dependent on a combination of factors, which include: (i) cost of inputs, (ii) technology used for production, (iii) tax rate, (iv) demand and supply of product, (v) consumer preferences and seasonal variations, (vi) competition in the market, and (vii) distribution channels. Since costs associated with these factors keep fluctuating, it may be difficult to determine if a reduction in tax rates has reflected in a commensurate decrease in price of goods or services. One concern could be that a company or a group of companies could collude together to rig prices; however, the Competition Commission of India has the jurisdiction to examine such cases and impose penalties.

D. Rationale behind sharing unutilised money in the GST Compensation Fund with the centre and among states being different from Finance Commission formula is unclear *[Section 10, GST (Compensation to States) Bill, 2017]*

The Constitution (101st) Amendment Act, 2016 requires the centre to compensate states for any revenue loss due to implementation of GST for a five-year period. To compensate states, an additional cess on certain goods and services will be levied under GST. However, at the end of the five-year period, the unutilised funds received by levying the cess will be shared equally between by centre and states; the share of states will be apportioned in the ratio of their SGST collections in the last year of transition.

This tax is collected from consumers by the central government and the question is how to apportion it among the centre and each state. In case of direct taxes (and other central taxes such as customs duty), the formula is based on the recommendations of the Finance Commission.[16] Such formula is used for dividing the funds collected through CGST and the centre's share of IGST too. The apportionment of excess funds collected through the compensation cess differs from such formula.

---

[1] The Central Goods and Services Tax Bill, 2017, http://www.prsindia.org/uploads/media/GST,%202017/Central%20GST%20Bill,%202017.pdf.
[2] The Integrated Goods and Services Tax Bill, 2017, http://www.prsindia.org/uploads/media/GST,%202017/Integrated%20GST%20Bill,%202017.pdf.
[3] The Union Territory Goods and Services Tax Bill, 2017, http://www.prsindia.org/uploads/media/GST,%202017/Union%20Territory%20GST%20Bill,%202017.pdf.
[4] The Goods and Services Tax (Compensation to States) Bill, 2017, http://www.prsindia.org/uploads/media/GST,%202017/GST%20(Compensation%20to%20States)%20Bill,%202017.pdf.
[5] Article 110, 117, 199, and 207, Constitution of India.
[6] Article 265, Constitution of India.
[7] Income Tax Act, 1961, http://www.incometaxindia.gov.in/pages/acts/income-tax-act.aspx.
[8] Chapter V of Finance Act, 1994 (Service Tax), http://www.cbec.gov.in/resources//htdocs-servicetax/st-act-ason24oct2013.pdf;jsessionid=563C94DA45C14F08F031341EB59CE67A.
[9] Section 3, The Central Excise Tariff Act, 1985.
[10] Report on the Revenue Neutral Rate and Structure of Rates for the Goods and Services Tax, Ministry of Finance, December 2015, http://www.prsindia.org/uploads/media/Constitution%20122nd/Report_Revenue_Neutral_Rate.pdf.
[11] Report of the 13th Finance Commission, December 2009, http://fincomindia.nic.in/ShowContentOne.aspx?id=28&Section=1.
[12] Report of the Taskforce on Goods and Services Tax, Thirteenth Finance Commission, December 2009, http://www.prsindia.org/uploads/media/Constitution%20122nd/Report%20of%20Task%20Force-%20GST.pdf.
[13] Kerala Commercial Taxes, http://keralataxes.gov.in/taxrate.aspx.
[14] Uttar Pradesh Value Added Tax Act, 2008, http://comtax.up.nic.in/Vat_Act/UPVAT%20SCHEDULE%20Updated%20upto%20dt%2012-03-2015.pdf.
[15] Poddar S and Ahmad E, "GST Reforms and Intergovernmental Considerations in India", Working paper No. 1/2009-DEA, Ministry of Finance, Government of India, http://finmin.nic.in/WorkingPaper/GST%20Reforms%20and%20Intergovernmental%20Considerations%20in%20India.pdf
[16] Report of the Fourteenth Finance Commission, February 2015, http://finmin.nic.in/14fincomm/14fcreng.pdf.