
GST - Department of Revenue vis a vis Empowered committee report

In January 2010, Department of revenue replied to various points stated by empowered committee of state finance ministers in their report.

I will discuss the comments by Department of revenue in three parts:

Part 1: DOR seconded the views of Empowered committee.

Part 2: DOR rejected the views of Empowered committee.

Part 3: DOR made additions to views of Empowered committee.

Part 1: Department of Revenue agreed to following views:-

- a) Twofold GST: A dual GST with defined functions and responsibilities of the Centre and the States is recommended. An appropriate mechanism that will be binding on both the Centre and the States should be worked out whereby the harmonious rate structure along with the need for further modification could be upheld, if necessary with a collectively agreed Constitutional Amendment.
- b) Applicability: The CGST and the SGST should be applicable to all transactions of goods and services made for a consideration.
- c) General: It is important to take note of the significant administrative issues involved in designing an effective GST model in a federal system with the objective of having an overall harmonious rate structure. Together with this, there is a need for upholding the powers of Central and State Governments in their taxation matters. Further, there is also the need to propose a model that would easily be implemented,, while being generally accepted by the stakeholders.
- d) Input tax credit: Since the CGST and SGST are to be treated separately, taxes paid against the Central GST shall be allowed to be taken as input tax credit (ITC) for the CGST and could be utilized only against the payment of CGST. The same principle will be applicable for the State GST. A taxpayer or exporter would have to maintain separate details in books of account for utilization or refund of credit. Further, the rules for taking and utilization of Credit for the CGST and the SGST would be aligned. Cross utilization of ITC between the CGST and the SGST

- should not be allowed except in the case of inter-State supply of goods and services under the IGST model which is explained later.
- e) Refund: Ideally, the problem related to credit accumulation on account of refund of GST should be avoided both by the Centre and the States except in the cases such as exports, purchase of capital goods, input tax at higher rate than output tax etc. where, again refund/adjustment should be completed in a time bound manner.
 - f) Uniform procedure: To the extent feasible, uniform procedure for collection of both CGST and SGST may be prescribed in the respective legislation for Central GST and State GST.
 - g) Taxpayer identification number: Each taxpayer would be allotted a PAN-linked taxpayer identification number with a total of 13/15 digits. This would bring the GST PAN-linked system in line with the prevailing PAN-based system for Income tax facilitating data exchange and taxpayer compliance.
 - h) Tax on Tobacco products: Tobacco products should be subjected to GST with ITC. Centre may be allowed to levy excise duty on tobacco products over and above GST without ITC.
 - i) Zero Rating of Exports: Exports should be zero- rated. Similar benefits may be given to SEZ's.
 - j) Special Industrial Area Scheme: After the introduction of GST, the tax exemptions, remissions etc. related to industrial incentives and special industrial area schemes should be converted into cash refund schemes.
 - k) Information Technology Infrastructure: After acceptance of IGST model for Inter-State transactions, the major responsibilities of Information Technology infrastructural requirement will be shared by the Central Government through the use of its own IT infrastructure facility. The issues of tying up the State Infrastructure facilities with the Central facilities as well as further improvement of the States' own IT infrastructure, including TINXSYS, is now to be addressed expeditiously and in a time bound manner.
 - l) Dispute Resolution & Advance Rulings: Specific provisions will also be made to the issues of dispute resolution and advance ruling.

Part 2: Department of Revenue disagreed to following views:-**1. Imports**

State view: GST is proposed to be levied on imports with necessary Constitutional Amendments. Both CGST and SGST will be levied on import of goods and services into the country. The incidence of tax will follow the destination principle and SGST amount will accrue to the State where the imported goods and services are consumed. Full and complete set-off will be available on GST paid on import of goods and services.

DOR remarks: Levy of GST on imports may be handled by Centre through a Central legislation either as a customs duty (as is being done now) or along the lines of IGST. SGST collected by Centre may be passed on to the concerned State following the destination principle. Taxation of import of services may be on the basis of reverse charge model, as is being done at present.

2. Thresholds

State View: A threshold of gross annual turnover of Rs.10 lakh both for goods and services for all the States and Union Territories may be adopted with adequate compensation for the States (particularly, the States in North-Eastern Region and Special Category States) where lower threshold had prevailed in the VAT regime. Keeping in view the interest of small traders and small scale industries and to avoid dual control, the States also considered that the threshold for CGST for goods may be kept at Rs.1.5 Crore and the threshold for CGST for services may also be appropriately high. It may be mentioned that even now there is a separate threshold for services (Rs. 10 lakh) and for goods (Rs. 1.5 crore) in the Service Tax and CENVAT.

DOR remarks: There should be a uniform threshold for goods and services for both SGST and CGST. This annual turnover threshold could be Rs.10 lakh or even more than that. The threshold exemption should not apply to dealers and service providers who undertake inter-State supplies. The problem of dual control

is better addressed through a compounding scheme as well as administrative simplification for small dealers through measures such as:

- a) Registration by single agency for both SGST and CGST without manual interface
- b) No physical verification of premises and no pre-deposit of security
- c) Simplified return format
- d) Longer frequency for return filing
- e) Electronic Return filing through certified service centres / CAs etc.
- f) Audit in 1-2% cases based on risk parameters
- g) Lenient penal provisions

There may not be any need to have direct link between compensation package, if decided for, and the threshold for registration for North-Eastern and special category States.

3. Purchase tax:

State View: Some of the States felt that they are getting substantial revenue from Purchase Tax and, therefore, it should not be subsumed under GST while majority of the States were of the view that no such exemptions should be given. The difficulties of the food grain producing States and certain other states were appreciated as substantial revenue is being earned by them from Purchase Tax and it was, therefore, felt that in case Purchase Tax has to be subsumed then adequate and continuing compensation has to be provided to such States. This issue is being discussed in consultation with the Government of India.

DOR remarks: Purchase tax is nothing but sales tax where the responsibility for collection of tax is with the purchaser (and not with the seller as in the case of sales tax). Keeping 'purchase tax' outside will give the loophole to the States to impose 'purchase tax' on any commodity (food-grains, agricultural / forest produce, minerals, industrial inputs etc.) over and above GST. Hence, purchase tax must be subsumed. The compensation package, if agreed, need not have any link to any particular tax being subsumed.

4. Tax on items containing Alcohol:

State View: Alcoholic beverages may be kept out of the purview of GST. Sales Tax/VAT can be continued to be levied on alcoholic beverages as per the existing practice. In case it has been made Vatable by some States, there is no objection to that. Excise Duty, which is presently being levied by the States, may also not be affected.

DOR remarks: Alcoholic beverages should be brought under the purview of GST in order to remove the cascading effect on GST paid on inputs such as raw material and packaging material. Sales tax / VAT and State excise duty can be charged over and above GST. Similar dispensation should apply to opium, Indian hemp and other narcotic drugs but medicines or toilet preparations containing these substances should attract only GST.

5. Tax on Petroleum Products:

State View: As far as petroleum products are concerned, it was decided that the basket of petroleum products, i.e. crude, motor spirit (including ATF) and HSD should be kept outside GST as is the prevailing practice in India. Sales Tax could continue to be levied by the States on these products with prevailing floor rate. Similarly, Centre could also continue its levies. A final view, whether Natural Gas should be kept outside the GST will be taken after further deliberations.

DOR remarks: Keeping crude petroleum and natural gas out of the GST net, this implies that the credit on capital goods and input services going into exploration and extraction would not be available resulting in cascading. Diesel, ATF and motor spirit are derived from a common input, viz., crude petroleum along with other refined products such as naphtha, lubricating oil base stock, etc. Leaving diesel, ATF and motor spirit out of the purview of GST would make it extremely difficult for refineries to apportion the credit on capital goods, input services and inputs. These products are principal inputs for many services such as aviation, road transport, railways, cab operators etc. As such, these may be levied to GST

and in selected cases credit of GST paid on these items may be disallowed in order to minimize the possibility of misuse.

7. Rate Composition:

State View: The Empowered Committee has decided to adopt a two-rate structure – a lower rate for necessary items and goods of basic importance and a standard rate for goods in general. There will also be a special rate for precious metals and a list of exempted items. For upholding of special needs of each State as well as a balanced approach to federal flexibility, and also for facilitating the introduction of GST, it is being discussed whether the exempted list under VAT regime including Goods of Local Importance may be retained in the exempted list under SGST in the initial years. It is also being discussed whether the Government of India may adopt, to begin with, a similar approach towards exempted list under the CGST.

- a) DOR remarks: There should be a single rate of GST both for goods and services.¹

Around 99 items presently exempted under VAT may continue to remain exempted in GST regime. There should be no scope with individual States, for expansion of this list even for goods of local importance. Efforts will be made by Centre to substantially reduce the number of items presently exempted under CENVAT regime. At the end, there must be a common list of exemptions for CGST and SGST.

¹ A two rate structure for goods would pose the following problems:

- a) Likelihood of inversions in duty structure with raw materials and intermediate goods being at a higher rate and finished goods being at a lower rate, especially with the intention to apply the lower rate to necessities.
- b) Inversions would result in input credit accumulation and demand for refunding the same from time to time.
- c) The general rate (RNR) would have to be higher under a single rate structure.
- d) Currently, services are chargeable to tax at a single rate. Adopting a dual rate for goods would generate a similar demand for services too.

Having different rates for goods and services would imply that the distinction between goods and services should continue.

8. CGST for goods as well as services

State View: The States are of the view to have a two-rate structure relating to goods for CGST, with conformity in the levels of rate under the SGST. For taxation of services, there may be a single rate for both CGST and SGST.

DOR remarks: There should be one CGST rate both for goods as well as services.

Part 3: DOR agreed subject to additions:**1. Levy of GST & basic provisions**

State Views: The GST shall have two components: one levied by the Centre (hereinafter referred to as Central GST), and the other levied by the States (hereinafter referred to as State GST). Rates for CGST and SGST should be prescribed appropriately, reflecting revenue considerations and acceptability. This dual GST model would be implemented through multiple statutes (one for CGST and a SGST statute for every state). However, the basic features of law such as chargeability, definition of taxable event and taxable person, measure of levy including valuation provisions, basis of classification etc. should be uniform across these statutes as far as practicable.

DOR additions: Agreed. In addition, IGST on inter-State transactions should be levied by the Centre. SGST on imports should also be levied and collected by the Centre. Centre should pass on SGST collection on imports to concerned States on the destination principle.

2. Central/State taxes to be subsumed

State Views: On application of the principle, it is recommended that the following Central Taxes should be subsumed under the GST:

- (i) Central Excise Duty
- (ii) Additional Excise Duties
- (iii) The Excise Duty levied under the Medicinal and Toiletries Preparation Act

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- (iv) Service Tax
 - (v) Additional customs duty, commonly known as countervailing duty
 - (vi) Special Additional Duty of Customs - 4% (SAD)
 - (vii) Surcharges, and
 - (viii) Cesses.

Following State taxes and levies should be subsumed under GST:

- (i) VAT / Sales tax
- (ii) Entertainment tax (unless it is levied by the local bodies).
- (iii) Luxury tax
- (iv) Taxes on lottery, betting and gambling.
- (v) State Cesses and Surcharges in so far as they relate to supply of goods and services.
- (vi) Entry tax not in lieu of octroi.

DOR additions: Electricity duty, Octroi, purchase tax and taxes levied by local bodies should also be subsumed under GST.

3. Payment of net output tax

State Views: The CGST and SGST are to be paid to the accounts of the Centre and the States separately. It would have to be ensured that account-heads for all goods and services would have indication whether it relates to CGST or SGST (with identification of the State to whom the tax is to be credited).

DOR additions: Agreed. In addition, IGST should be paid to the accounts of the Centre.

4. Composition Scheme

State Views: The States are also of the view that Composition / Compounding Scheme for the purpose of GST should have an upper ceiling on gross annual turnover and a floor tax rate with respect to gross annual turnover. In particular

there will be a compounding cut-off at Rs.50 lakh of gross annual turnover and a floor rate of 0.5% across the States. The scheme should also allow option for GST registration for dealers with turnover below the compounding cut-off.

DOR additions: Agreed. Centre may also have a Composition Scheme up to gross turnover limit of Rs. 50 lakh, if threshold for registration is kept as Rs.10 lakh. The floor rate of 0.5% will be for SGST alone, in case Centre also brings a Composition Scheme for small assesses. The Centre may leave the administration of Compounding Scheme, both for CGST and SGST to the States.

5. IGST:

State Views: The Empowered Committee has accepted the recommendations of the Working Group of concerned officials of Central and State Governments for adoption of IGST model for taxation of Inter-State transaction of Goods and Services. The scope of IGST model is that, Centre would levy IGST which would be CGST plus SGST on all Inter-State transactions of taxable goods and services with appropriate provision for consignment or stock transfer of goods and services. The inter-State seller will pay IGST on value addition after adjusting available credit of IGST, CGST, and SGST on his purchases. The Exporting State will transfer to the Centre the credit of SGST used in payment of IGST. The Importing dealer will claim credit of IGST while discharging his output tax liability in his own State. The Centre will transfer to the importing State the credit of IGST used in payment of SGST. The relevant information is also submitted to the Central Agency which will act as a clearing house mechanism, verify the claims and inform the respective governments to transfer the funds.

The major advantages of IGST Model are:

- (i) Maintenance of uninterrupted ITC chain on inter-state transactions.
- (ii) No upfront payment of tax or substantial blockage of funds for the inter-state seller or buyer.
- (iii) No refund claim in exporting State, as ITC is used up while paying the tax.

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- (iv) Self monitoring model.
 - (v) Level of computerization is limited to inter-state dealers and Central and State Governments should be able to computerize their processes expeditiously.
 - (vi) As all inter-state dealers will be e-registered and correspondence with them will be done by e-mail, the compliance level will improve substantially.
 - (vii) Model can take 'Business to Business' as well as 'Business to Consumer' transactions into account.

DOR additions: Agreed. It may however be noted that IGST model will work smoothly only when there is a common threshold for goods and services both for the Centre and the States. Having more than one rate either for CGST or SGST will complicate the working of IGST Model.

6. Miscellaneous

State Views: Keeping in mind the need of taxpayer's convenience, functions such as assessment, enforcement, scrutiny and audit would be undertaken by the authority which is collecting the tax, with information sharing between the Centre and the States.

DOR additions: Since the tax base is to be identical for the two components, viz., CGST and SGST, it is desirable that any dispute between a taxpayer and between the tax administrations is settled in a uniform manner. The possibility of setting up of a harmonized system for scrutiny, audit and dispute settlement may be developed.