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## *Goods & Service Tax*

**An Unprecedented Reform in History of Indirect taxes**

## GST – Background

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- ☛ GST - Next generation of reforms in the area of Indian Indirect taxes
- ☛ Replacement of VAT at state level and excise and service taxes at the national level (besides a host of local levies)
- ☛ Central government has already released a Discussion paper
- ☛ Constitutional amendment is a prerequisite to introduction of GST
- ☛ Integration of efforts required not only between the Centre and all the States, but also between various departments of the Centre (i.e. department of Service tax, Excise and customs) and of the respective States (i.e. department of VAT, Octroi, Entry tax, etc)
- ☛ Mutual exclusivity of taxation of services by Centre and of sale of goods by State will no longer remain
- ☛ Government committed to implement the same effective April 1<sup>st</sup>, 2011



## GST – Expected Benefits

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- ☛ **GST rate** – Presently, the combined rate of indirect taxes on goods are close to 22% which shall be reduced to 12-18%, benefiting trade and industry
- ☛ **GDP gains** – Detailed study by Task force has estimated GST to provide gains to India's GDP from 0.9%-1.7%
- ☛ **Reduction in prices of goods** – Estimated to decline as cascading effect of taxes may be eliminated



- ☛ **Export-oriented industries** would become internationally more competitive as entire taxes in supply chain would be refunded (zero-rating)
- ☛ **Import-substituting industries** would also become competitive as prices of Indian commodities would reduce

## GST – Expected Benefits

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In a phased manner, we will be able to achieve a single CGST and SGST rate for both goods and services.  
The gain from GST will propel India from a \$1-trillion economy to a \$2-trillion economy in a short span of time.  
Therefore, the successful implementation of GST would create win-win-win situations for the Centre-State, industry and consumers.



**Pranab Mukerjee -  
Finance Minister, India**

## Content

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*Indirect Taxes – A Journey of Reforms*

*VAT & Central Excise – Present regime*

*How will GST work*

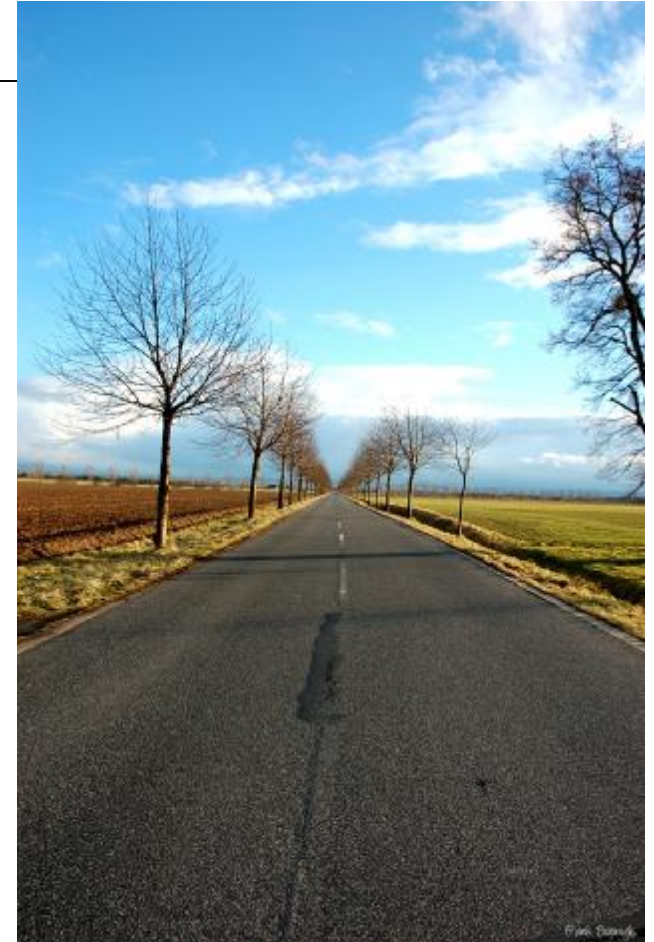
*Examples and Illustrations*

*GST – Key concerns, issues & Challenges*

## Indirect Taxes – a Journey of Reforms

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- ☛ **Erstwhile Sales tax and Central excise regime** – No credit available on Payment of taxes at each level resulting in cascading effect of taxes – price of commodity increased substantially
- ☛ **Central Excise** – Concept of VAT introduced (i.e. MODVAT wef March 1, 1986 which was later christened as CENVAT)
- ☛ **Service tax** – 1994 being first year when services also brought within ambit of Indirect taxes – No credit availability at time of introduction – Later concept of CENVAT extended to Service tax also – Input credit on Service tax and CENVAT can be utilized on payment of Output tax (i.e. discharge of liability of Service tax and Central excise)
- ☛ **VAT** – Nationwide roll-out of VAT in April 1st, 2005 – Availability of input tax credit against output tax liability – However, CST not yet integrated in current regime; Any CST paid not available as credit



## Indirect Taxes – a Journey of Reforms

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### ☉ **Goods & Service Tax** – Next generation of reforms in the area of Indian Indirect taxes

- Introduced for first time in 1954 in France – now prevalent in more than 150 countries
- Replacement of VAT at state level and excise and service taxes at the national level (besides a host of local levies)



- Discussion paper on GST released in 2009 laying down the roadmap for new regime
- Revised Target date now kept as April 1st, 2011

## Content

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*Indirect Taxes – A Journey of Reforms*

*VAT & Central Excise – Present regime*

*GST – Justification & proposed regime*

*Discussion Paper on GST*

*GST – Key concerns, issues & Challenges*



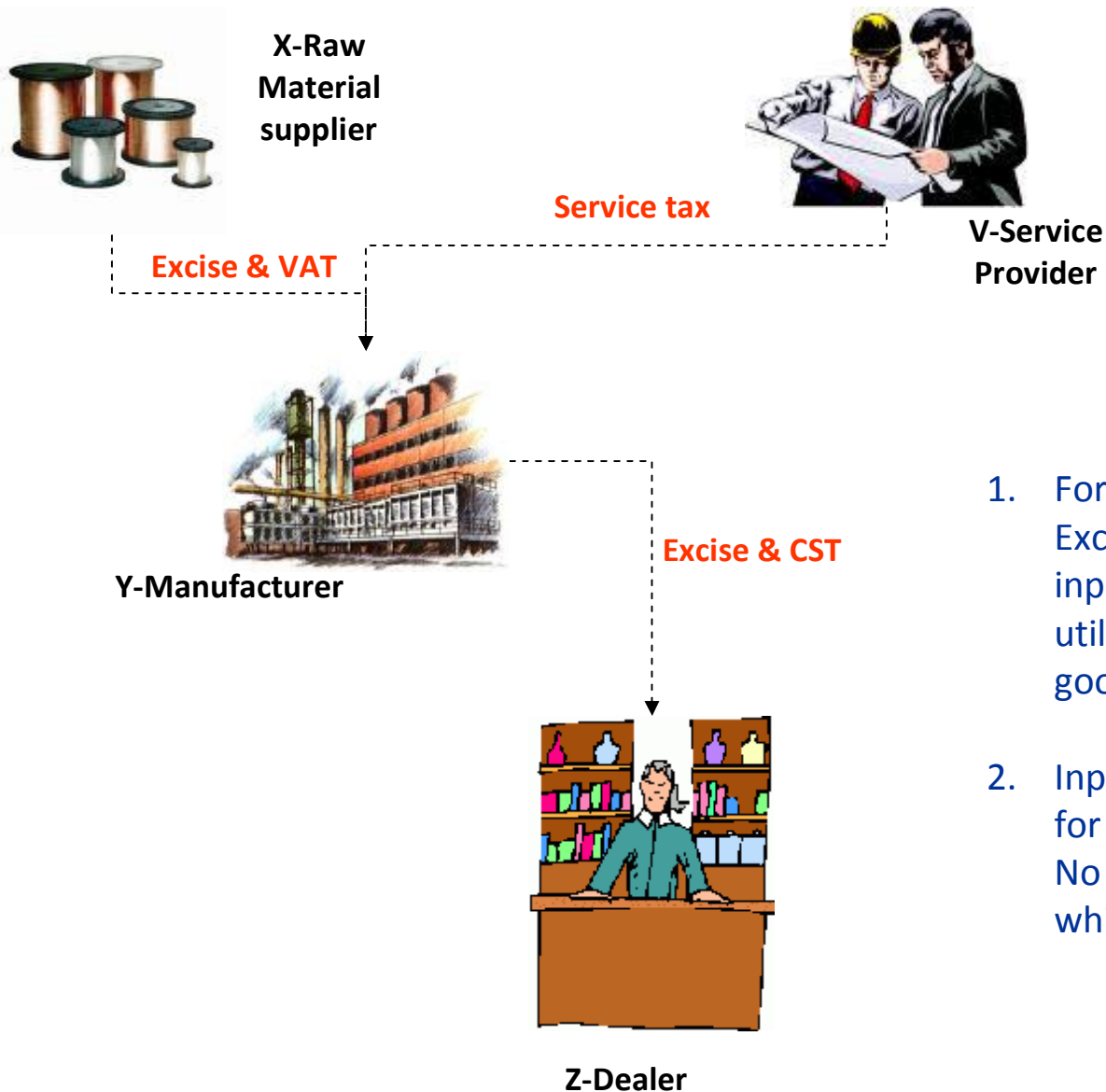
## Pitfalls in existing regime

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- ☛ No benefit of CENVAT (Excise paid on goods and service tax paid on services) in discharging Sales tax liability and **vice-versa, *so chain broken***
- ☛ No benefit of CST (i.e. no credit on inter-state sales) – ***Resulting in manufacturers to setup distribution depots in other states or make sales through consignment agents***
- ☛ Non-inclusion of several Central taxes in the overall framework of CENVAT, such as additional customs duty, surcharges, etc.
- ☛ In existing State-level VAT structure, several taxes which are in the nature of indirect taxes viz. luxury tax, entertainment tax, etc., and yet not subsumed in VAT



## VAT & Central Excise – Present regime (Example #1)

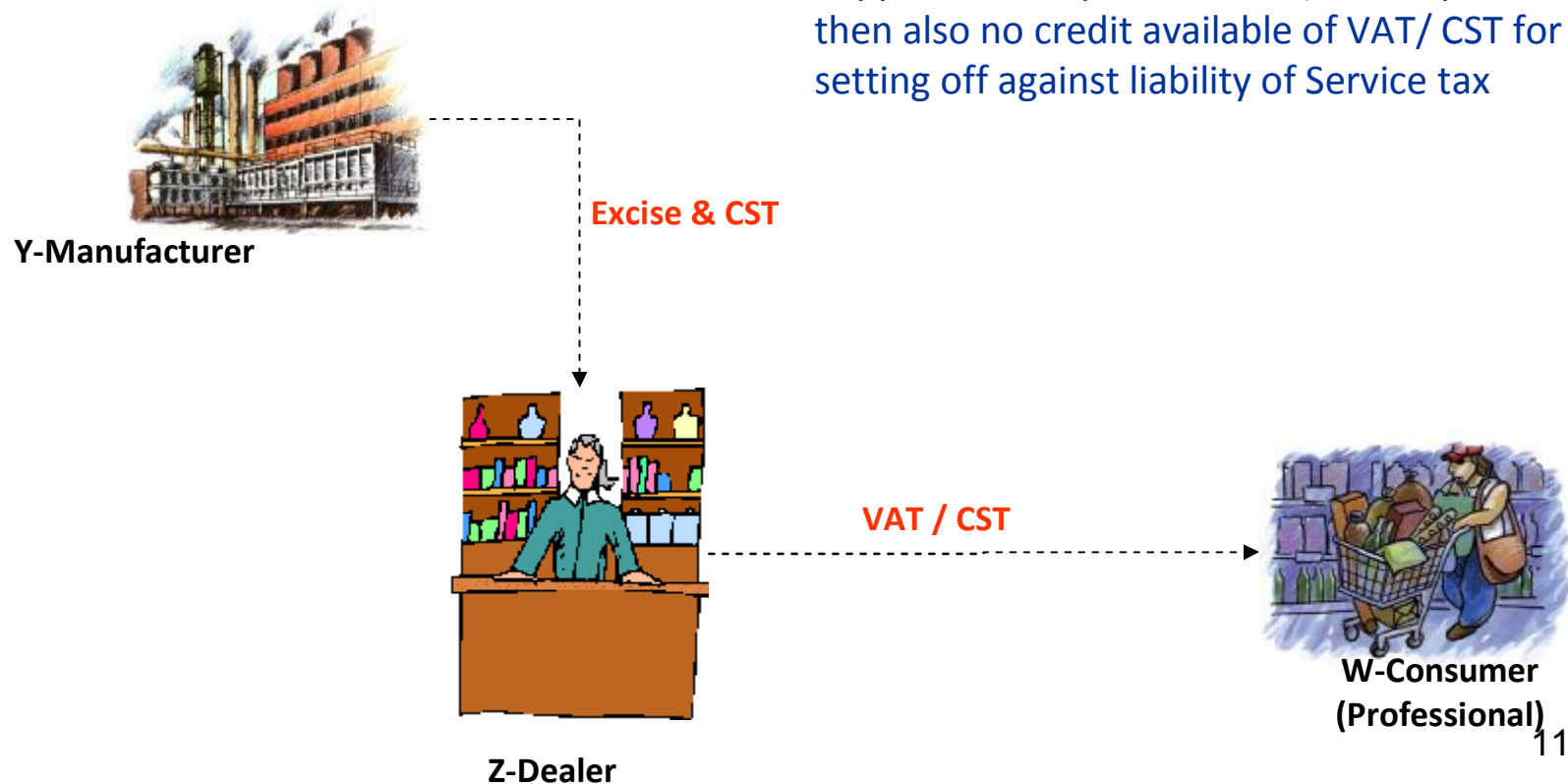


1. For Y, Cenvat credit on account of Excise and Service tax paid on inputs is available as credit for utilisation against Excise on sale of goods to Z.
2. Input credit of only VAT available for utilisation against CST liability; No credit if CST had been paid while making purchases

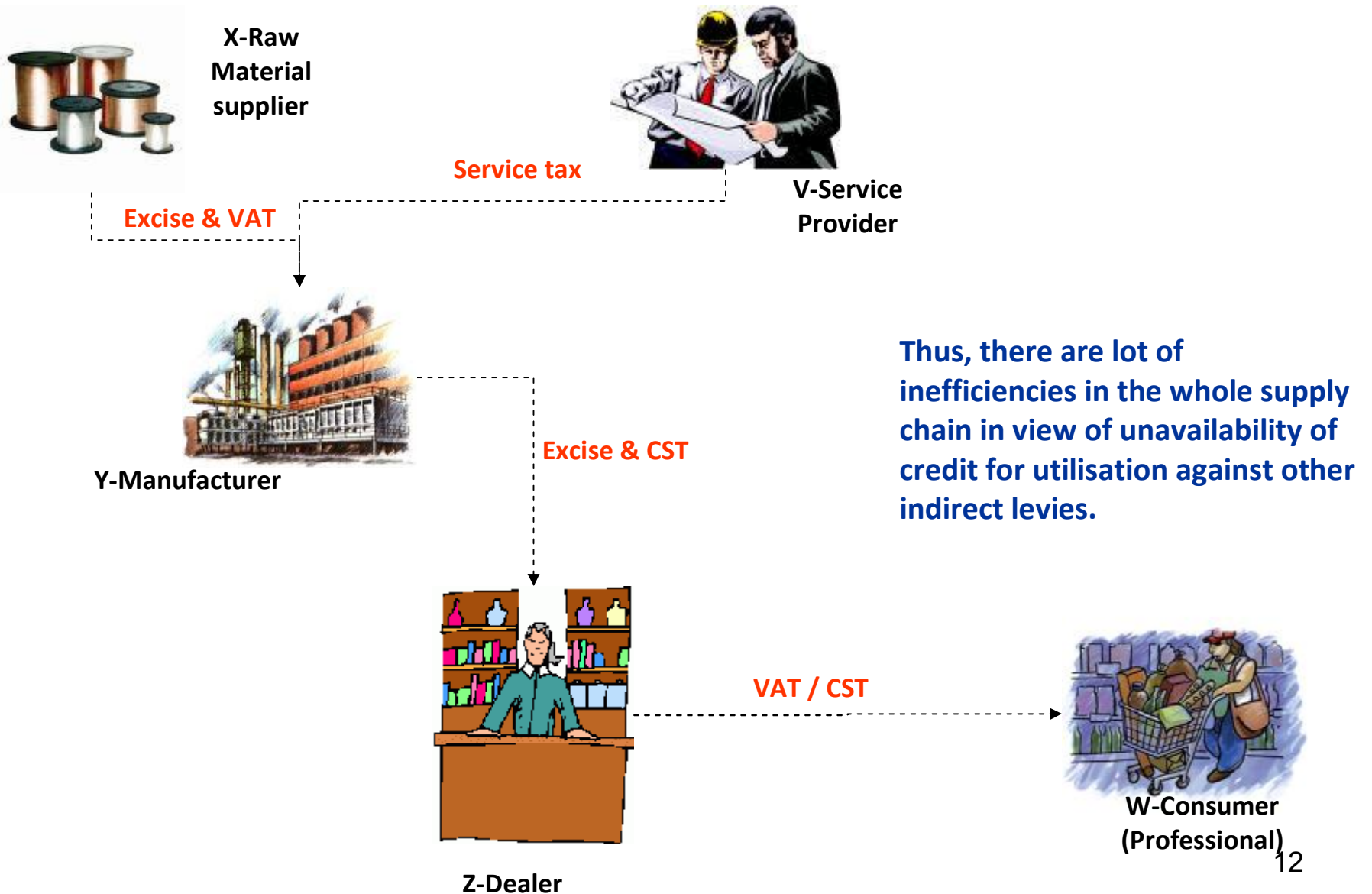
## VAT & Central Excise – Present regime (Example #1)

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1. For Z, while discharge of VAT / CST liability, no credit available for CST (only VAT paid locally is available as credit)
2. Cenvat credit not available to Z for utilisation
3. Suppose W is a professional (service provider), then also no credit available of VAT/ CST for setting off against liability of Service tax



## VAT & Central Excise – Present regime (Example #1)



## Pitfalls in existing regime

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- ☛ As services outside the ambit of State Taxation, governments resorting to tax through right to use, etc.
  - Advancement in digitization and Information technology blurring the distinction (like taxation of software) **and**
  - increase cost of products in case of composite contracts (involving both goods and services)

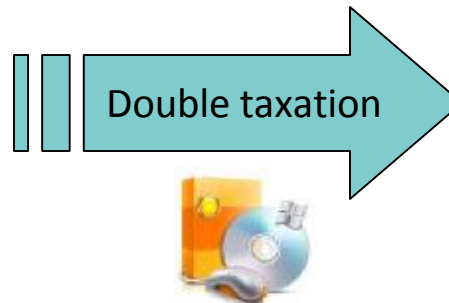
*State governments unable to generate sufficient revenue from services, so exclusion they tend to increase tax rates on goods and increase compliance*

## VAT & Central Excise – **Double taxation of software (Example #2)**

Service tax applicable under category of 'Information technology Software services' – Supply of customised software and acquisition of 'right to use' software



**A-Company**



**B-Consumer**

Many states are levying VAT on the transfer of both packaged and customised software.

## VAT & Central Excise – **Works contract (Example #3)**

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- ☛ Levy of tax on Works contract is complex subject
- ☛ As a principle, VAT is payable on the value of goods involved in a works contract and service tax is payable on the value of services provided.
- ☛ Problem arises in Composite contract where contractors can have certain options under both laws
  - Payment of tax at composition rates on the entire value
  - Abatement of value at prescribed percentage and payment of tax on the abated value
- ☛ Composite contracts may result in excess levy, then what it would have been in case of one single levy on the entire value



## Content

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*VAT & Central Excise – Present regime*

*How will GST work*

*Examples and Illustrations*

*GST – Key concerns, issues & Challenges*



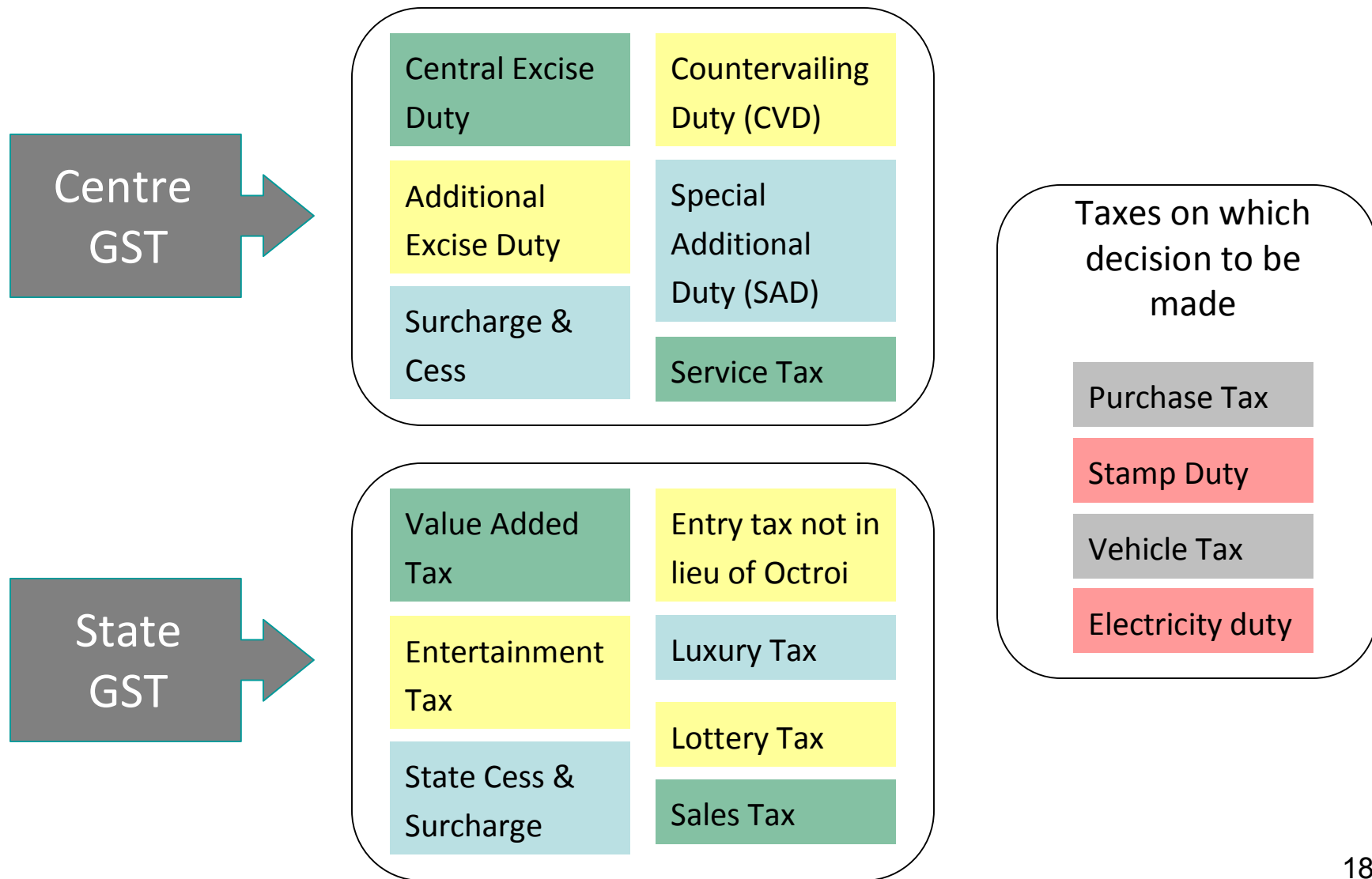
## GST key points – **Concept**

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- ☛ **Concept** – Taxable event is ‘supply of goods’ and ‘supply of services’ as against ‘manufacture of goods’, ‘sale of goods’ and ‘rendition of services’.
- ☛ **Multiple statutes:** one for centre and one each for each of the states.
- ☛ **Rate structure** : Three rates on the rest of the transactions – two rates for goods – a lower rate for “necessary items and goods of basic importance” and a standard rate for the rest, and a third rate for services
- ☛ **Uniform state GST threshold** – proposed at Rs 10 lakh [Threshold for central GST for goods could be kept at Rs 1.5 crore and for central GST on services may also be appropriately high]



## Subsuming of Taxes – Centre & State GST



## GST key points – **Concept**

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- ☛ **Dual GST:** a central GST (CGST) and state GST (SGST) to apply on the same base – on Inter-state transactions, IGST proposed which covers both CGST & SGST - Exports to be zero-rated and all imports subject to GST
- ☛ **Area based exemption** - Exemptions will be modified - goods exempt so far will be charged to tax - Benefit of exemption promised to such units could be retained as post tax cash refunds to be effected by the Centre / State
- ☛ **Administration** - Timely refund where credit accumulation takes place - PAN-linked taxpayer identification number, to allow for easy sharing of information across the different tax administrations, including income tax - functions such as assessment, enforcement, scrutiny and audit to be undertaken by the authority which is collecting the tax, with information sharing between the centre and the states.
- ☛ **Alcoholic products and tobacco** – Status quo maintained



## Content

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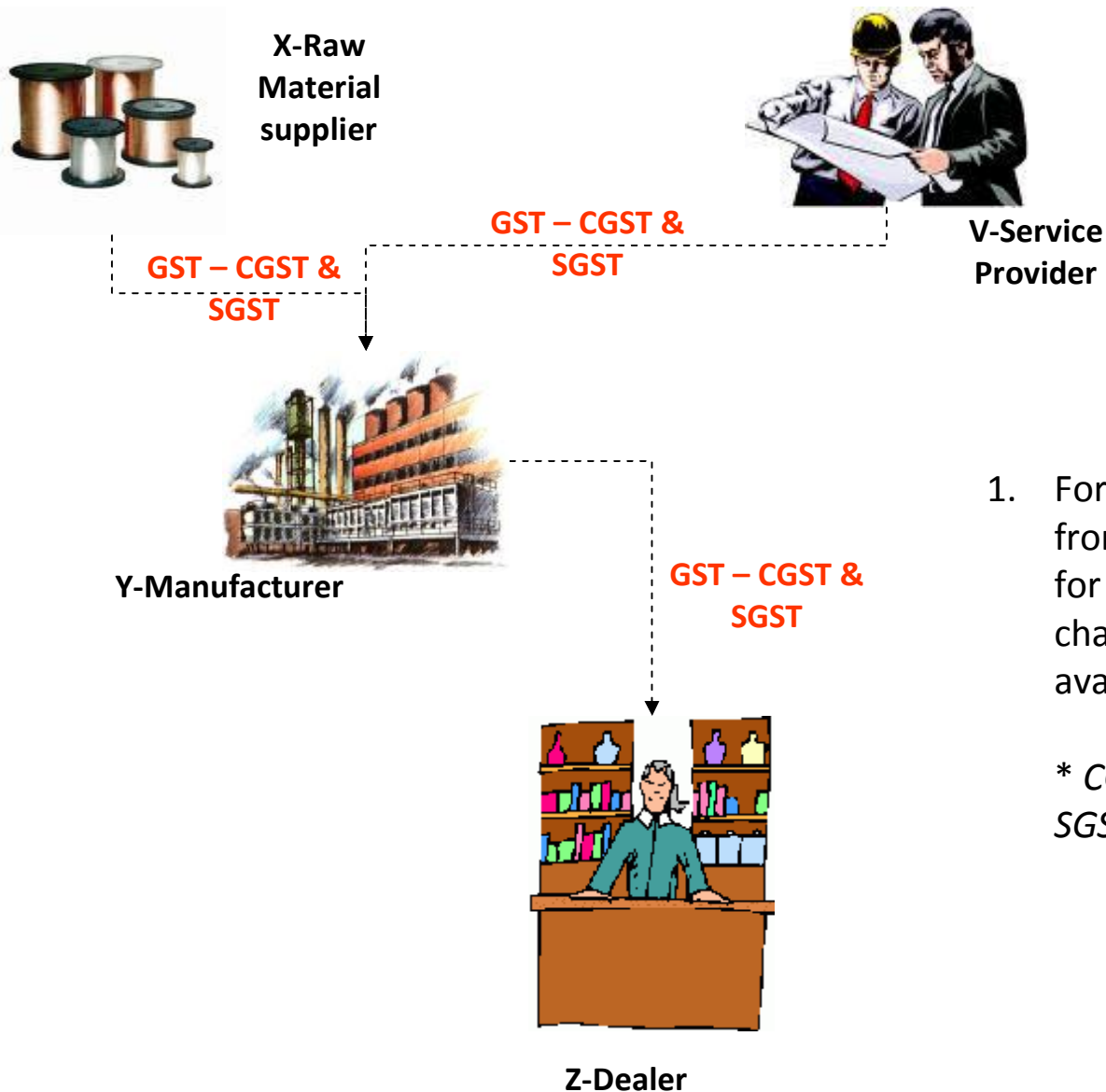
*VAT & Central Excise – Present regime*

*How will GST work*

*Examples and Illustrations*

*GST – Key concerns, issues & Challenges*

## GST – Proposed regime



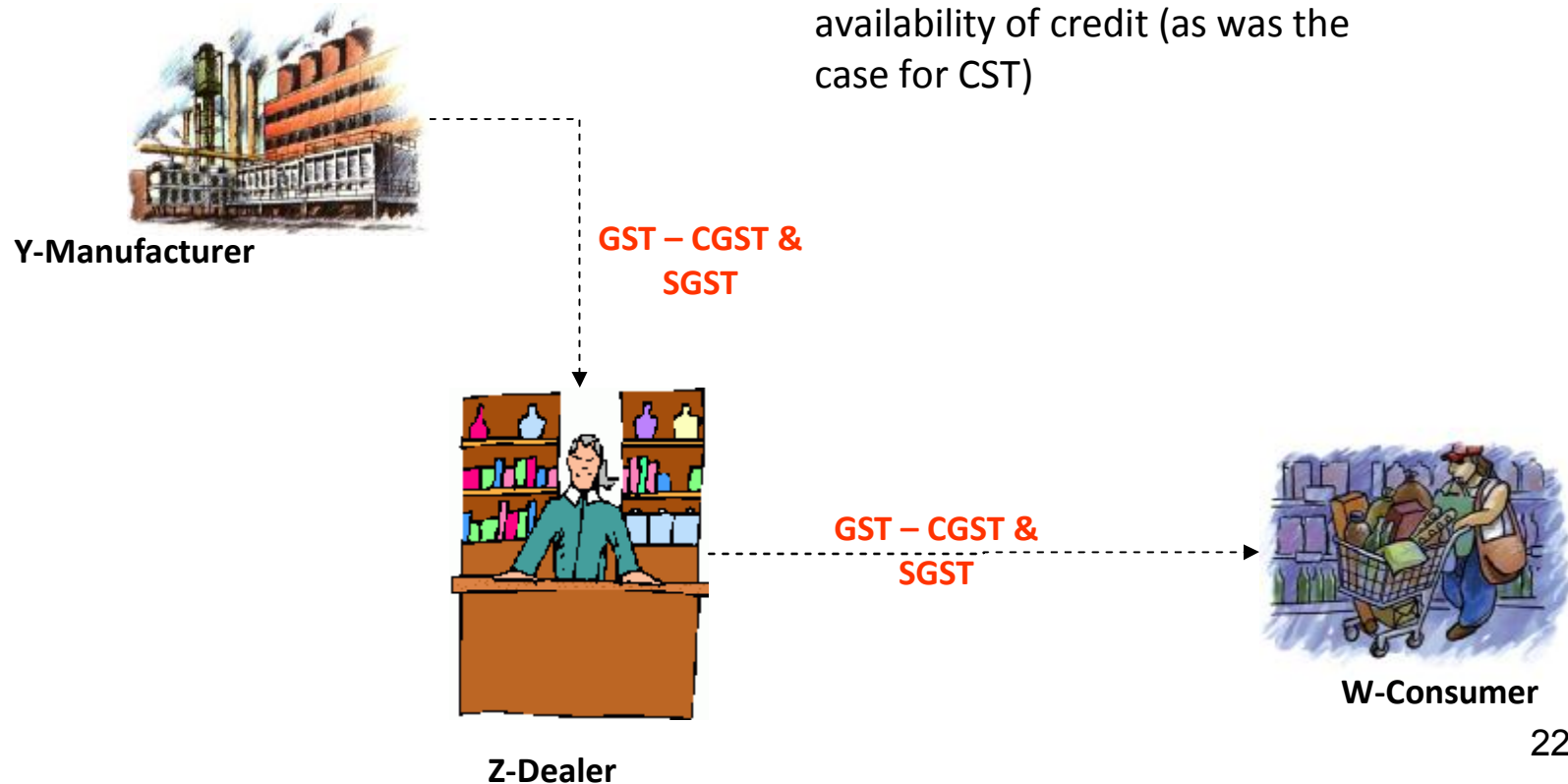
1. For Y, CGST on sale to Z discharged from CGST paid to X & V (similarly for SGST) – Efficiency in supply chain as all taxes paid now available as credit

*\* CGST shall be paid to Centre and SGST to State*

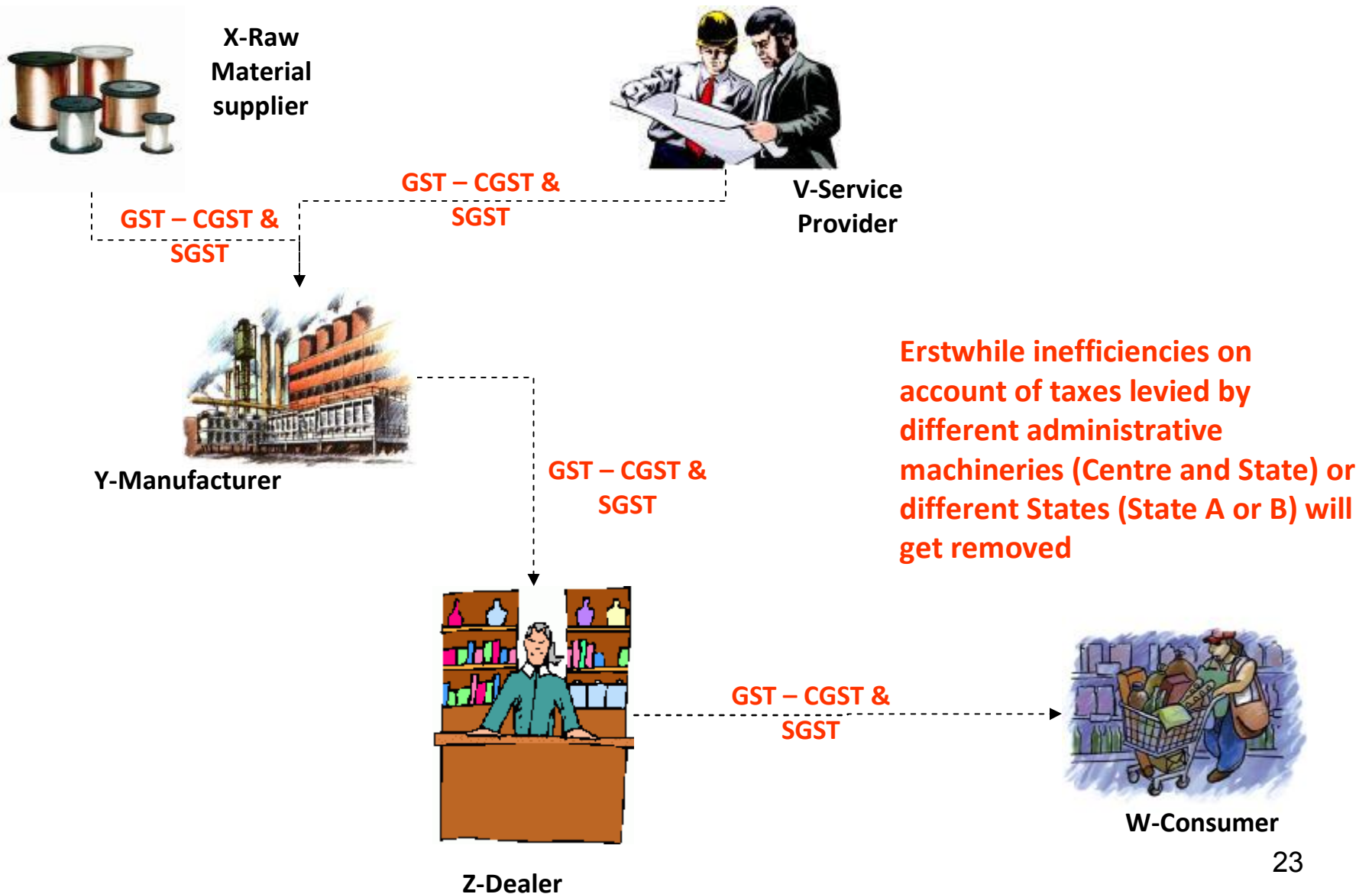
## GST – Proposed regime

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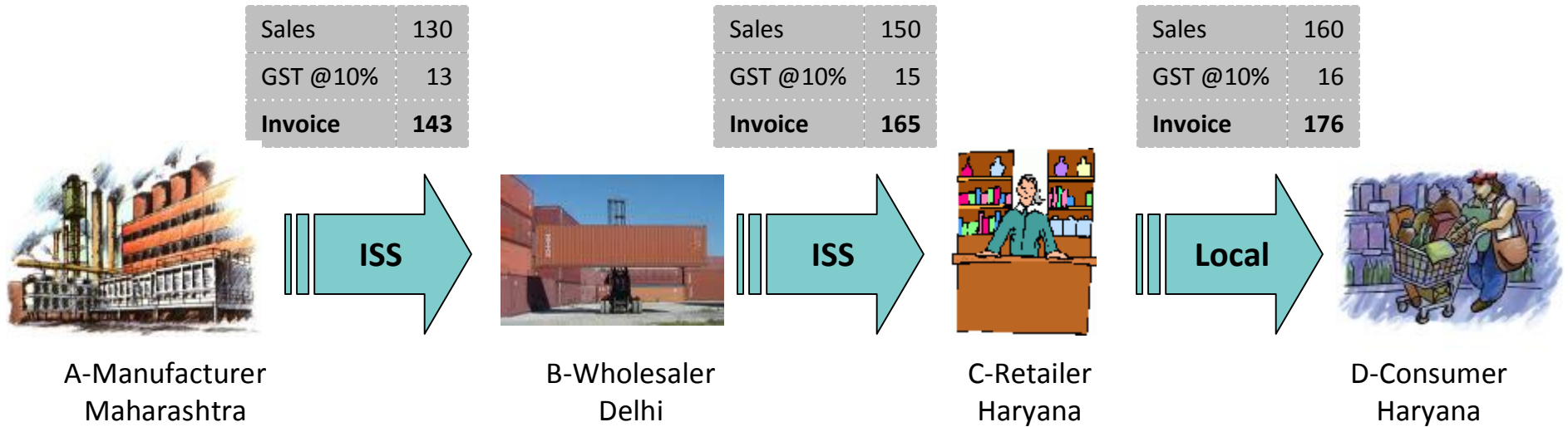
1. For Z, CGST on sale to W discharged from CGST paid to Y (similarly for SGST) – No consideration that supply in inter-state trade would not entitle for availability of credit (as was the case for CST)



## GST – Proposed regime



## GST concept with examples – Calculation

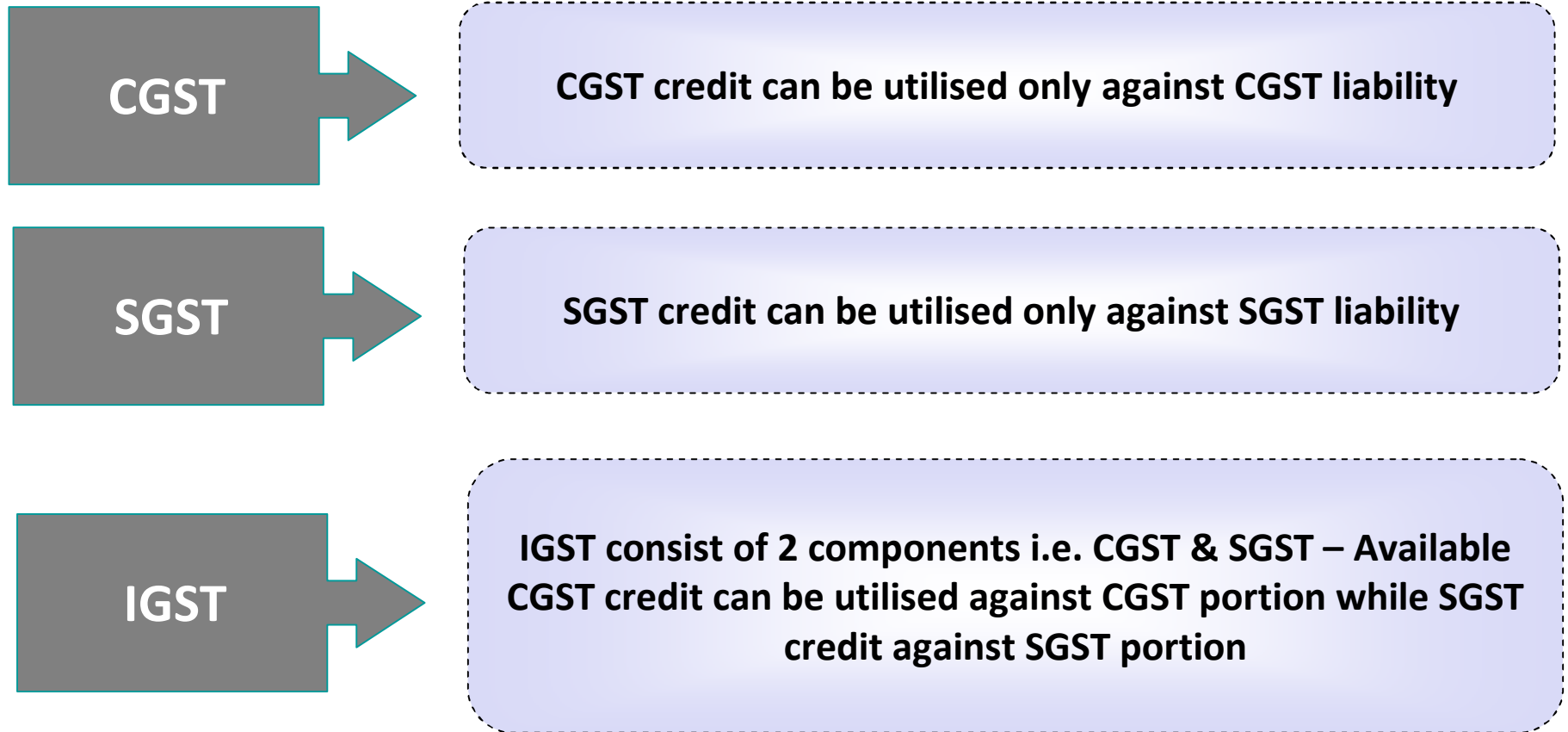


Stages of Supply chain	Purchase value	Value Addition	Value of Supply	GST rate	GST on output	ITC	Net GST
Manufacturer	100	30	130	10%	13	10	13-10=3
Wholesaler	130	20	150	10%	15	13	15-13=2
Retailer	150	10	160	10%	16	15	16-15=1



## GST concept with examples – **Credit utilisation**

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## GST concept with examples – **Local Sale**

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A-Manufacturer  
Delhi



B-Consumer  
**Delhi**

Particulars	Amount-Rs
Sales	150,000
CGST @5% of Sales	7,500
SGST @7% of Sales	10,500
<b>Sales Price</b>	<b>168,000</b>

Under the GST model of taxation, both CGST and SGST would be charged – CGST to be deposited with Centre and SGST with Delhi

## GST concept with examples – Local Sale



A-Manufacturer  
Delhi



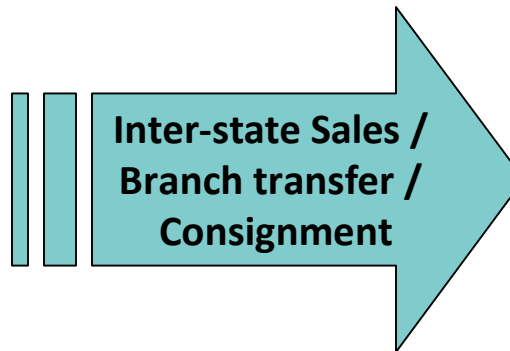
B-Consumer  
Delhi

Particulars	CGST	SGST
Output tax	7,500	10,500
Less: Input tax credit		
- CGST	4,000	-
- SGST	-	5,000
<b>Net tax payable in cash</b>	<b>3,500</b>	<b>5,500</b>
	Deposit with Centre	Deposit with Delhi

## GST concept with examples – **Inter-state Sale & Stock transfer**



A-Manufacturer  
Delhi



B-Consumer  
**Haryana**

Particulars	Amount-Rs
Sales	150,000
CGST @5% of Sales	7,500
SGST @7% of Sales	10,500
<b>Sales Price</b>	<b>168,000</b>

IGST

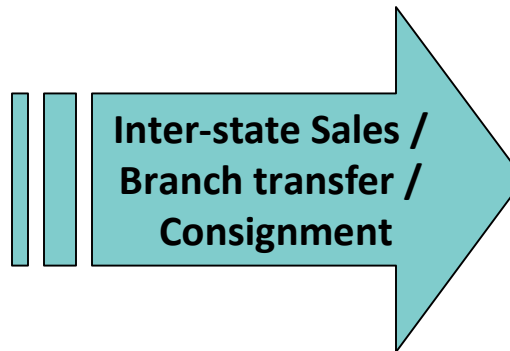


Under IGST model of taxation  
– Both CGST & SGST to be deposited with Centre (SGST portion to be transferred by Centre to Haryana)

## GST concept with examples – **Inter-state Sale & Stock transfer**



A-Manufacturer  
Delhi



B-Consumer  
**Haryana**

Particulars	CGST	SGST
Output tax	7,500	10,500
Less: Input tax credit		
- CGST	4,000	
- SGST	-	5,000
<b>Net tax payable in cash</b>	<b>3,500</b>	<b>5,500</b>
	Deposit with Centre	Deposit with Centre

For onward transfer  
to Haryana by Centre

## GST concept with examples – **Export**



A-Manufacturer  
India



B-Importer  
**USA**

Particulars	CGST	SGST
Output tax	-	-
Less: Input tax credit		
- CGST	4,000	-
- SGST	-	5,000
<b>Net tax payable in cash</b>	<b>(4,000)</b>	<b>(5,000)</b>

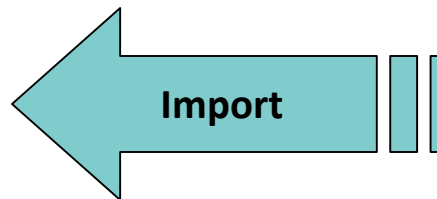
Under GST model of taxation – Exports are zero-rated i.e. no tax on goods, but credit available (can be refunded or utilised against local sales)

## GST concept with examples – **Import**

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A-Manufacturer  
**Delhi, India**



B-Exporter  
**USA**

Particulars	Amount-Rs
Import	150,000
CGST @5% of import	7,500
SGST @7% of import	10,500
<b>Purchase Price</b>	<b>168,000</b>

Under GST model of  
taxation – even imports  
would be subjected to  
CGST & SGST

## GST concept with examples – Credit Utilisation Illustration

Description	Quantity sold	Value of goods sold	CGST @5%	SGST @7%	IGST @12%
Sale within State	8,000	80,000	4,000	5,600	-
Export Sales	3,500	35,000	-	-	-
Inter-state sales	6,500	65,000	-	-	7,800
<b>Total</b>	<b>18,000</b>	<b>180,000</b>	<b>4,000</b>	<b>5,600-</b>	<b>7,800</b>

Particulars	CGST	SGST	IGST
Output tax	4,000	5,600	7,800
Less: Input tax credit			
- CGST (Rs 10,000)	4,000	-	3,250
- SGST (Rs 14,000)	-	5,600	4,550
<b>Net tax payable in cash</b>	<b>-</b>	<b>-</b>	<b>-</b>

Total IGST liability was Rs 7,800 (which consisted of CGST – 3,250 (5% of 65,000) & SGST – 4,550 (7% of 65,000))



## Content

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*Indirect Taxes – A Journey of Reforms*

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*How will GST work*

*Examples and Illustrations*

*GST – Key concerns, issues & Challenges*

## GST Key Concerns – **Constitutional amendments**

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- **Constitutional amendments** for levy of GST by both the Centre and States – Centre already in advanced stages of discussion.
  - Presently Constitution empowers Centre to levy and collect income tax (Entry No 82 of List I in 7<sup>th</sup> schedule to Constitution), Custom duties (83), Excise (84), Central Sales tax (92B), Service tax (92C);
  - States list includes octroi (Entry No 52 of List II in 7<sup>th</sup> schedule to Constitution), tax on sale or purchase of goods (54)
  - Now as both Centre and States would get power to levy tax on goods and services, a constitutional amendment is required.
  - Law Ministry likely to finalise the Constitutional amendment Bill which it proposes to introduce in Parliament soon – Ratification by 8 states required before assent by the President of India



## GST Key Concerns – **Agreement on GST rates**

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- ☛ Final rate with allocation between CGST & SGST not yet finalised
- ☛ Finance Minister Pranab Mukherjee recently proposed a 3-rate structure for GST which will simplify the indirect tax regime – under which
  - goods will attract 20% levy,
  - services 16%
  - essential items a concessional 12%.

wherein both Centre and State would have an equal share



- ☛ After initial protest, States are filing in line as Centre have agreed to compensate States for revenue losses consequent to the shift.
- ☛ However, a number of industries currently outside the indirect tax net could come within the purview of the GST
- ☛ Single GST rate is desirable as multiple rates become source of complexity and disputes adding to the cost of tax administration and compliance.

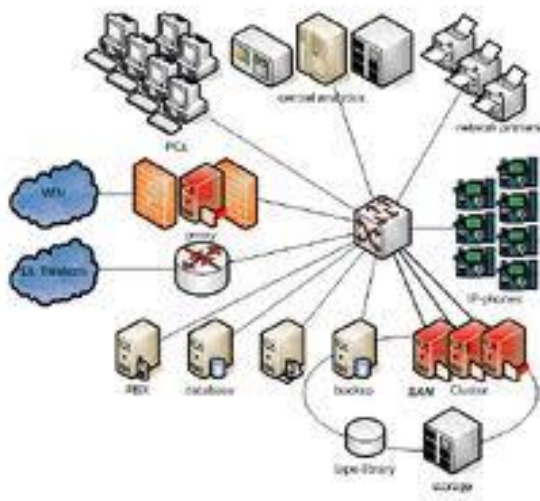
## GST Key Concerns – **Draft GST legislation**

- ☛ **Option I** - One centre legislation and each State to have its own legislation –
- ☛ **Option II** - Government can also go the way CST is being levied – legislation enacted by the Centre but administration and enjoyment of benefits by respective States
- ☛ However, with deadline round the corner, no draft of CGST & SGST laws out for discussion in public domain
- ☛ **Harmonization of Standards** - Legislations to elaborately include all definition rules defining the taxable consideration, input tax credit, timing of tax payments and adjustments in special circumstances, tax form design and audit, enforcement and appeal procedures, classification of goods and services, definition of export and import, etc
- ☛ **Simplification of legislation** is key factor for keeping disputes as low as possible – Design of tax forms and compliance procedures - The appeal forms, fees, pre-deposit requirement, stay procedures, time lines, etc, will also need to be standardised for a better GST system



## GST Key Concerns – IT infrastructure

- ☛ IT infrastructure is a key component for success of GST
- ☛ States as well as the Centre agreed to setup a clearing house to resolve tax collections and credits under the National Securities Depository Ltd (NSDL) as a SPV.
- ☛ The clearing house, a key part of the GST architecture, is expected to ease the creation of the common market, ensure that each state gets its share of revenue and also provide useful tax information to the authorities.
- ☛ The proposal envisages a standard electronic return, which each of the estimated 8 million establishments will be required to file every month.



- ☛ Centralized / integrated system integrating payments, refunds, returns and tracking of inter-state movement of goods and services – end to end tracking with proper re-conciliation and exception reports for enforcement agencies for assessment

## GST Key Concerns – Transition Rules

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- ☉ An area of concern – various questions in stakeholders' minds
- ☉ How the existing input tax credit under the excise and the VAT laws will be allowed to be transitioned into the GST system - can SGST arising in the post-GST period be paid out of input tax credit of state VAT (i.e. relating to pre-GST period) & CGST out of Cenvat credit balance as on date of transition?
- ☉ Transition issues to shift from the litigation under the existing tax litigation system to the litigation system under the GST regime?
- ☉ who would be the refund granting authority for any amount pre-deposited pending litigation under the pre-GST period but decision delivered in the post-GST regime?



## GST Key Concerns – **Taxation on services**

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- ☉ Two Options available for taxation of services
  - **Option I** – Maintaining positive list (as in current Service tax legislation)
  - **Option II** – Maintaining negative list (as practiced internationally)
  
- ☉ In inter-state trade, taxation of goods comparatively much easier than services
- ☉ Issue will arise in treatment of financial services, insurance, banking, telecommunication, passenger and freight transportation from one state to another, etc – which are rendered and consumed in different states –
  
- ☉ Place of supply rules for purpose of taxability (similar to the one pertaining to export and import of services under the current service tax legislation) need to be defined elaborately which are not yet in place



## GST Key Concerns – **Dispute resolution mechanism**

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- ☛ Challenges that will be faced for Tax litigation system
  - Unifying the tax litigation policies and processes under the GST regime
  - In a dispute over any transaction, will one have to file two appeals, i.e., one for state GST and the other for central GST? The answer may be even more complex in the case of inter-state transactions attracting integrated GST (IGST).
  - The other difficulty that may arise is due to destination-based tax principle. Will it mean that the goods or services provider will have to file an appeal in the destination state over dispute arising on goods or services supplied by him, especially in a B2C scenario





## GST Key Concerns – **Advance Ruling mechanism**

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- ☛ There is a procedure in some states to obtain an order on determination of disputed question; in some states additionally, there exists an advance ruling mechanism.
- ☛ Excise and Customs advance ruling authorities are different from the VAT advance ruling authorities.
- ☛ **Under the GST regime, whether these processes can be clubbed into a single, simple and standard appellate or advance ruling mechanism.**



## GST Key Concerns – Other issues

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- ☛ Subsuming of stamp duty and purchase tax in GST transactions
- ☛ GST applicability on Supplies by public bodies and non-profit organization (health and education services)
- ☛ Administration of such a complex legislation which will subsume lots of taxes would be an enormous task
- ☛ A study by the Comptroller and Auditor General of India (CAG) has brought out startling details of the manner in which several states are operating the value-added tax (VAT) system.



**Over half of the hundred thousand dealers covered under the CAG audit in 23 states were engaged in tax evasion. Tax evasion of Rs 873 crore was detected from the scrutiny of only 2,600 returns in 15 states.**

- ☛ It is important that the operational flaws detected by the CAG report should be understood and steps taken to prevent their recurrence when the state GST becomes operational from April 2011.

## GST Key Concerns – **Training and awareness among stakeholders**

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- ☛ Various stakeholders in the new regime (i.e. Department officials, professionals, manufacturers, service providers, trade associations, etc.) would need to be trained on various provisions of new legislation. The contours of new law would appear to be complicated at the outset creating apprehensions about the new regime.
- ☛ **Time required for shift** – For companies, entire systems have to be amended, such as purchase orders and invoices and sales orders and invoices and the accounting systems also which needs time. Department officials would need training for enforcing compliances.





*GST would be a landmark initiative which would kick start the next generation of reforms. All stakeholders would need to gear themselves for the regime.*

*Thank You!*



*You can send your comments  
and suggestions at  
[balwantraibansal@yahoo.co.in](mailto:balwantraibansal@yahoo.co.in)  
We would be happy to hear  
from you*