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CHAPTER

INTRODUCTION TO GST

LEARNING OBJECTIVES

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1.1 CONSTITUTIONAL FRAMEWORK OF TAXES BEFORE GST

India is a union of diverse languages, cultures, religions and beliefs. Unity is "enshrined in" and "ensured by" Constitution of India. In administrative terms India is a federation of many states strengthened by centre at the axis. The architects of constitution recognized the importance of dependence as well as independence of states and centre and accordingly distributed taxation powers amongst them in the Seventh Schedule of the Constitution. List I of Seventh Schedule listed the taxation power of centre (Union) Government *via* entries 82 to 92, whereas List II mentioned the taxation powers of State Governments through entries 45 to 63. List III does not contain any entry which means that Union and States had no concurrent Powers of taxation. This was to avoid duplication in tax administration and also to minimize tax rivalry between Centre and States and among the States themselves. The residual powers of taxation belonged to Union *vide* entry 97 of List I. Service tax was imposed by Union Government using such powers.

The constitution does not provide any taxation powers to Local Government, however the states on their own many assign any of taxes in State list (List II) to the local bodies. The taxes generally assigned to local government were Property Taxes, octroi and taxes on vehicles.

Constitutional Framework of Taxes

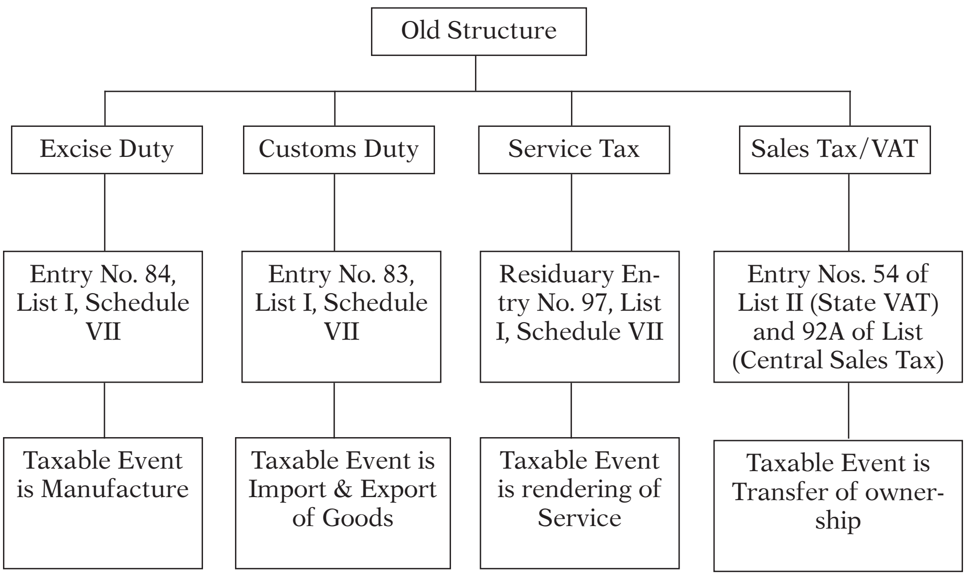
Taxes Within Union Jurisdiction as Enumerated in List I in the Seventh Schedule of the Constitution of India	Taxes Within Union Jurisdiction as Enumerated in List II in the Seventh Schedule of the Constitution of India
Entry No. 82 - Taxes on income other than agricultural income.	Entry No. 45 - Land revenue.
Entry No. 83 - Duties of customs including export duties.	Entry No. 46 - Taxes on agricultural income.
Entry No. 84 - Duties of excise except on alcoholic liquors and narcotics but including medicinal and preparation containing alcohol.	Entry No. 47 - Duties in respect of succession to agricultural land.
Entry No. 85 - Corporation tax.	Entry No. 48 - Estate duty in respect of agricultural land.
Entry No. 86 - Taxes on the capital value of assets, exclusive of agricultural land, of individuals and companies; taxes on the capital of companies.	Entry No. 49 - Taxes on lands and buildings.
Entry No. 87 - Estate duty in respect of property other than agricultural land.	Entry No. 50 - Taxes on mineral rights subject to any limitations imposed by Parliament by law relating to mineral development.
Entry No. 88 - Duties in respect of succession to property other than agricultural land.	Entry No. 51 - Duties of excise on alcoholic liquors and narcotics manufactured or produced in the State but not including medicinal and toilet preparations containing alcohol.
Entry No. 89 - Terminal taxes on goods and passengers carried by railway, sea or air; taxes on railway fares and fares and freights.	Entry No. 52 - Taxes on the entry of goods into a local area for consumption, use or sale therein.
Entry No. 90 - Taxes other than stamp duties on transactions in stock exchanges and future markets.	Entry No. 53 - Taxes on the consumption or sale of electricity.
Entry No. 91 - Rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies, and receipts.	Entry No. 54* - Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of Entry 92A of List I.
Entry No. 92 - Taxes on the sale or purchase of newspapers and on advertisements published therein.	Entry No. 55** - Taxes on advertisements other than advertisements published in the newspapers (and advertisements broadcast by radio or television)
Entry No. 92A* - Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase taken place in the course of inter-State trade or commerce.	Entry No. 56 - Taxes on goods and passengers carried by road or on inland waterways.
Entry No. 92B** - Taxes on the consignment of goods (whether the consignment is to the person making it or to any other person, where such consignment takes place in the course of inter-State trade or commerce.	Entry No. 57 - Taxes on vehicles, whether mechanically propelled or not, suitable for use on roads, including tramcars subject of the provisions of Entry 35 of List III.
Entry No. 92C - Tax on services [w.e.f. 15/1/04 Parliament but yet Not Notified]	Entry No. 58 - Taxes on animals and boats.
Entry No. 97 - Any other matter-not included in List II [Residual Powers].	Entry No. 59 - Tolls.
	Entry No. 60*** - Taxes on professions, trades, callings and employment.
Entry No. 97 - Any tax not enumerated in List II or List III of the Seventh Schedule.	Entry No. 61 - Capitation taxes.

Taxes Within Union Jurisdiction as Enumerated in List I in the Seventh Schedule of the Constitution of India	Taxes Within Union Jurisdiction as Enumerated in List II in the Seventh Schedule of the Constitution of India
* Inserted by the Constitution (Sixth Amendment) Act, 1956. ** Inserted by the Constitution (Forty-sixth Amendment) Act, 1982. *Source*: Government of India, Ministry of Law, Justice and Company Affairs, The Constitution of India, Seventh Schedule, List I.	Entry No. 62 - Taxes on luxuries, including taxes on entertainment, amusements, betting and gambling.
	Entry No. 63 - Rates of stamp duty in respect of documents other than those specified in the provisions of List I with regard to rates of stamp duty.
	* Substituted by the Constitution (Sixth Amendment) Act, 1956. ** The words 'and advertisements broadcast by radio or television' inserted by the Constitution (Forty-second Amendment) Act, 1976. *** The scope of these taxes is spelt out in Article 276, the clause (2) of which fixes the amount payable by a person on account of these taxes. *Source*: Government of India, Ministry of Law, Justice and Company Affairs. *The Constitution of India*, Seventh Schedule, List II.

In case of Union Territories, Union Government can make laws in respect of all the entries in all the lists.

1.1.1 Major Indirect Taxes

Out of the many Indirect Taxes provided by the constitution, major source of income for the government were excise duty levied on manufactured goods, customs duties levied on import of Goods, service tax levied on rendering of service and VAT levied on Sale of Goods. These major sources of income are summarized in the following manner.



1.2 DEFECTS IN STRUCTURE OF INDIRECT TAXES BEFORE GST

Over the period of almost six decades the prevailing indirect tax regime created complexities and showed several shortcomings forcing Government to overhaul the existing system. These short comings are summarised below:

1. **Cascading Effect:** Both central and state Government levy tax on the same goods. Former levy tax on manufacture of goods and the later levy VAT on sale of very same goods. State Government does not permit credit of excise duty paid by the manufacture to the dealer on sale of goods. Thus VAT is also payable on excise duty component of the price resulting in cascading effect. Similarly service tax is payable on rendering of service. No credit of service tax paid on input service used in selling of goods is provided by the state government. So tax is levied on tax. It boosted inflation.

2. **Multiplicity of Tax/Cess:** Multiple taxes were levied in pre GST regime like Excise duty, VAT, Entry tax, luxury tax, Entertainment tax, Service tax, Octroi etc. These taxes were in additions to various cesses imposed by State and Central Government like Krishi Kalyan Cess, clean energy cess etc. All this made the tax structure very cumbersome.

3. **Overlapping of Jurisdiction:** Over the years, distinction between goods and services has become hazy, due to which there is overlapping of state VAT and Central Service tax on transactions like works contract, food related services of restaurants, caterers, computer software, SIM cards, renting of movable property etc. In these cases it was difficult to judge whether the transaction was sale of goods or rendering of service. Therefore both the central and state Government would impose tax.

4. **Rivalry amongst states:** Pre-GST regime of indirect tax was not destination based tax but origin based tax. In that regime taxes are collected and utilized by the state administration where goods/services are transacted/manufactured or supplied. This would encourage state to provide sales tax/VAT relief to attract industries and at the same time discourage supply of goods from other state by imposing entry tax, octroi, luxury tax etc. on goods coming from other states.

5. **Hindrance to Integrated market system:** India despite being one nation could not develop into a national market due to invisible barriers of Central State tax, VAT, entry tax etc. as mentioned in last point. These invisible barriers were visible in the form of check posts on the boundaries of states.

6. **Loss of Man and Truck hours:** Due to check posts mounted by states on entry point million of man hours and Truck hours were lost Besides that huge corruption was involved which made logistics management a costly affairs.

7. **Difficulty in Compliance for Taxpayers:** As mentioned already pre GST regime had multiplicity of Tax and consequently tax laws. Moreover each tax had a different taxable event like manufacture for Excise, VAT for sales etc. Also there were multiple of Tax authorities. Compliance required voluminous efforts on the part taxpayers. It also promoted Inspector raj.

8. **Difficulty in Cross Verification of Credit availed by Assessee:** Earlier it was difficult for the tax department to get the verification report from supplier of goods to know whether the supplier has issued particular invoice on the basis of which input tax credit has been taken by the purchaser. Due to lack of online data the verification was done off line. Often the report of supplier was not received or received after considerable lapse of time. Many scrupulous dealer exploited this and availed fraudulent credit.

9. **Tax Evasion:** Burden of compliance, multiplicity of tax laws increased the propensity to evade taxes. Fudging of records, concealment of transaction, bribing the tax officials were the tools adopted to remain out of tax net.

10. **Huge Amount of litigation:** With multiple tax laws each having different taxable events result was lot of disputes regarding availment of credit, determining manufacture of goods, value of goods, classification of goods etc. Dispute settlement mechanism is almost choked with such disputes resulting in pendency of tax demands.

1.3 RATIONALE FOR GST

As mentioned in the preceding sections the six decade old indirect tax regime had become too cumbersome and obstructive for the growth of our Nation, a major overhaul was required. This came in the form of GST which was made effective from 1-7-2017. GST will subsume almost 17 central and state taxes and 21 cesses and bring nation under united, common market with simplified tax structure, with emphasis on greater self compliance environment. It shall ignite the growth of economy through a comprehensive but simple indirect tax regime which, aims at enlarging tax base not by coercion but compliance, ensures vertical equity of taxes yet lowers overall tax rates.

GST in based on the concept of Value Added Tax (VAT) whereby the cascading effect is extinguished completely.

Also GST is a consumption and **"destination based"** tax system, unlike the earlier System which was based on origin of sale or manufacture. This feature reduces the regressive impact of indirect taxes. So GST brings benefits to all the stakeholders namely industry, Government and consumer.

Benefits of GST

1. **Integrated National Market:** GST aims to make India a common market with common tax rates and procedures and remove the economic barriers thus paving the way for an integrated economy at the national level. This will ensure seam less and smooth movement of goods and service across the nation.

2. **Elimination of Cascading Effect:** Cascading of tax occurs when each successive transfer is being taxed inclusive of previous tax levied. At certain occasions, a particular activity is taxed by both Center and State Government which leads to duality of taxes. This results in cascading effects of Taxes. GST will overcome the problem of tax cascading through Input Tax Credit Mechanisms and ultimate burden of taxes to be paid would be on the consumer of Goods and Services.

3. **Removal of Multiplicity of Taxes:** GST will remove all the multiple taxes which are levied in the present regime. Duties & Taxes like Excise Duty. Value Added Tax, Entry Tax, Luxury Tax, Entertainment Tax, Octroi, and Services Tax shall subsume under GST. There shall remain only one tax called GST. It will bring transparency and ease of doing business in India.

4. **Increase in GDP:** GST will certainly bring ease of doing business in India. It is expected that the Ease of Doing Business Index of India which remains around 140 shall fall to double figures. It will certainly bring trust and faith in the taxation regime, leading to huge capital inflow from Foreign Investors. There shall be boom in the manufacturing as well as service sector leading to GDP Growth.

5. **Efficient Administration by Government:** GST is a fully automated tax regime. From filing of returns to refunds to assessment proceedings everything shall be online. There shall be least physical interaction between the taxpayer and the revenue authorities. Online System is set to bring transparency, lower corruption and better administration by the Government.