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Impacts, Challenges and Pitfalls of GST after Implementation in India

Manjur Alam
Assistant Teacher (Commerce Department) Masunda (N.B) Boys High School, New Barrack pore Kolkata, West Bengal, India

ABSTRACT

The Good and services tax (GST) is the biggest and substantial indirect tax reform since 1947. Goods and Services Tax (GST) is a comprehensive tax levy on manufacture, sale and consumption of goods and services at a national level. The GST regime holds an enormous opportunity for various sectors of the economy and is expected to herald a new era of indirect tax regime. By replacing various indirect taxes, GST is expected to be a key step in the field of indirect tax reform in India. The uniform tax reform under GST is expected to provide a uniform market for MSMEs. By cutting down multiple taxes, this reform will increase the flexibility in transfer of goods, hence reducing the total business cost. Also with GST enabling a centralized registration, starting a business would be much easier. With this act of standardizing the process under the new tax regime, many other activities like purchase of capital goods and products, reduction of tax burden on new businesses will help to boost this sector. While the lower Goods and Services Tax (GST) rates may lead to a decline in inflation, economic growth may not improve significantly in the short term even though it will benefit both India Inc and the government in the medium term. GST is unlikely to be a “positive” for economic growth in the short term, Crisil’s Joshi said the reform will improve the ease of doing business, bolster investor sentiment and lure more foreign investment in coming years. . It will also improve government's fiscal health as the tax collection system would become more transparent, making tax evasion difficult. An attempt is made in this paper to study the concept of goods and service tax and its impact on Indian economy. The study also aims to know the real benefits, present problems and challenges of GST after implementation and some issues which are yet to be considered in Indian scenario.

Keywords: Goods and service tax, Indirect tax, Implementation, Challenges, Tax regime, Economic growth.

I. INTRODUCTION

After several rounds of deadlock in the parliament, India rolled out the Goods and Services Tax (GST) on July 1, replacing a thicket of indirect central and state levies that critics argue have blunted economic competitiveness and hobbled efforts to lift more out of poverty [1,4]. Observers have described the reform as the most meaningful change to India's tax regime since the country became independent in 1947. The government is introduce GST for a variety of goods and services along four main rate bands: 5-, 12-, 18- and 28 percent irrespective of the location of purchase. Certain goods such as fresh meat, eggs, milk, among others, will not be taxed. The Goods and Services Tax (GST) framework operates on a handful of key principles [5]. The Centre will levy and collect the Central GST. 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 [6].

Literature Review

Indirect Taxes Committee of Institute of Chartered Accountants of India (ICAI) (2015) submitted a PPT naming Goods and Service Tax (GST) which stated in brief details of the GST and its positive impact on economy and various stakeholders [2,3].

The Institute of Companies Secretaries of India (ICSI) (2015) published a Reference on Goods and Service Tax to provide the information on the concept of GST in details [6].

Objectives of the Study

1. To study the concept of Goods and Services Tax (GST) and its impact on Indian Economy.
2. To identify the problems and prospects of GST in India.
3. To understand how GST will work in India.
4. To know the challenges of GST in Indian context.

II. Research Methodology

The paper is based on secondary sources of data, which have been obtained from various GST implementation discussion papers, published article in journals, web articles (internet sources), past studies and news paper etc. With the help of these secondary sources, attempt has been made to find the obstacles coming on the way of GST and looking for future opportunities of it in India.

Real Benefits of GST

The real benefits of GST to the consumer and businesses are long term and can be stated as following:-

1: Merger of Taxes

At present, there are a large number of taxes at central and state level. They shall all be merged and become one GST as shown in figure.

2: One Law One Country

At present, you have multiple central laws and state laws for taxations. If you are trading your goods at all India level, you must know and follow all the different laws of India. It is due to this reason that many people avoid trading goods in different states. As GST is implemented India would become one market and you can trade anywhere in India hassle-free.

3: Increased Input Credit

At present, input credit is not available for inter-state sales of goods. This would now be available under GST regime. Thus the next tax liability to businesses would come down.

4: More Export Incentive

An exporter presently gets the refund/drawback on mostly the central taxes. Now they shall be able to get the refund/drawback of State taxes as well. This will boost export.

5: GST Network

Since all registration and return filing shall be done online, the scope of evasion shall be reduced considerably. This will boost the tax revenue and cause more development of the country.

III. Impacts of GST After Implementation

1. Shaking up corporate operations

The new tax regime will force many companies to restructure their operations. Companies will now insist vendors and suppliers to furnish invoices as GST will make it impossible for firms to evade taxes. Big companies stand to benefit as they have a supply chain in order and can offset taxes paid on inputs. Smaller firms may end up spending more as compliance cost will rise."While the impact on companies varies following existence of production units in the excise exempted zones, implementation of GST should result in cost savings in the supply chain network and expedite a shift from unorganized to organized trade.

2.Passing on the benefit of lower tax

While the GST Council, headed by finance minister Arun Jaitley, will keep a close vigil on whether companies are passing on the benefit of lower taxes to consumers, experts expressed doubt on the implementation of anti-profiteering norm. I believe that while corporate would pass on the direct benefits of GST (like a lower tax rate), they would aim to retain partly (if not fully) the indirect benefits from the saving in logistics costs, streamlining of business processes and the seamless flow of input credits.

While GST laws include anti-profiteering measures—the benefits of the reduction in the tax rate and input credit shall be passed on by a commensurate reduction in prices—such measures are difficult to implement and would be a retrograde step, similar to price controls, if implemented in haste. Companies may use the savings from tax outgo under the GST regime to improve profit margin to some extent and invest the rest in building new capacities.

3. Inflation may remain low

Analysts have no doubt that inflation will remain low as GST rates on essential goods such as food grain, household consumer items and essential services have been either exempt or kept lower. However, assuming that GST does have the intended effect of increasing tax compliance, the tax burden would increase, Morgan Stanley said in a note. This could lead companies to pass the costs of higher tax compliance on to the consumer at a later stage, it said. Most of the services are not accounted in the consumer price CPI inflation basket and hence the higher GST rates may not get reflected on the retail price movement as measured by the government data.

There are services like health, education, miscellaneous segment, transportation are outside the ambit of GST. “Hence, GST implementation on CPI impact will be minimal. We estimate that GST will have neutral impact on headline CPI,” he said forecasting the average inflation at 4-4.5% during 2017-18.

4. RBI may not cut rates in June

While inflation is expected to ease further with GST rollout from a record low of 3% in April, analysts expect RBI may not immediately lower policy interest rates.“RBI will watch out for the monsoon progress as also how the GST pans out, “In the last policy review, RBI had flagged concerns that the “one-off” impact GST may be inflationary. The central left policy rates unchanged in April. SBI’s Ghosh says the RBI will most probably pause on June policy review.

5. Economic growth may not jump immediately

Economists are not sure of the immediate impact of GST and some even say it may impeded growth in the short term as big companies reorganise their businesses and as small firms lose revenue.

“The GST implementation will be disruptive as there will be a major change in the supply chain,” but added the tax reform will be beneficial to the economy in the medium to long term.

Some issues that are yet to be considered

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 potential problems which are discussed below.

No Parliamentary approval needed for CGST rates

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 and state legislatures. 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. 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. 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.

IV. AGAINST THE IDEA OF THE 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.

In December 2015, the Expert Committee on the Revenue Neutral Rate for GST had suggested a three rate structure for GST. 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.

GST on services 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.

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.

V. SHARING OF UN-UTILISED MONEY

The rationale behind sharing un-utilised 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. 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.

VI. Some of the challenges are highlighted after implementation of GST

We have a system today across a majority of small units where an accountant comes (in) once a month makes vouchers and inputs details for taxes, that will have to end now because we are moving to an online, almost real-time system that will need a lot of manpower.

Industry, services not yet there

India’s industry and its banking system will have to change systems, train personnel and accept the extra workload for the new taxation system. The banking system has clearly said it is not yet ready. Industry is ambivalent.“Nearly 50% of Indian businesses are not aware of the changes that GST will usher in,” Bharat Goenka, managing director, Tally Solutions, was quoted as saying in the Economic Times on June 5, 2017.Tally accounting software is widely used by Indian companies. The company is waiting for the GST rules to be finalised, so that it can roll out its GST software for Indian companies, the Economic Times reported.

A senior official of Federation of the Indian Chambers of Commerce and Industry (FICCI), requesting anonymity because the launch date was close, said GST was “now a fact”, and industry was trying to adapt. FICCI has been conducting awareness sessions among industry verticals to help understand the new structure, he added the industrial sector, especially the services sector, is waiting for more clarity on tax rates, processes and the time frame for the systems to settle down. “While it is good that the taxation system will be streamlined and we will not have to deal with multiple tax payments like excise, service tax and value added tax, we still don’t know how much time it will take for everybody to be on board.”

- Swift boost in Assesses and supply channel rehabilitation:

The GST model extends the tax band by taxing each economic supply within the distribution network, which results to fast augment in, assesses. Here, businesses need to reshuffle their distribution network, in order to reduce additional tax burden on the consumer, while thinking in price competitive terms. Regardless of the bigger picture to generate revenue in a neutral and transparent way, the Government will require ensuring that this doesn’t take place on the cost of consumers paying more than the worth. Also, one needs to keep an eye out for the reinvention of supply channel. For the current tax regime, place of supply formed a minor issue as service is taxed by the Centre and revenue receipts remained at ease from place of levy. Post GST; inter-state transactions would be in an unprecedented situation as places of taxation need to be clearly demarcated.

- Challenges to legislation:

Implementation of GST comes at the behest of significant Constitutional re-shaping, making the reform tread on a stickier path. Constitution of India, in past, has allayed powers to the Union and the States to levy and collect taxes as per Union, State and Concurrent List. This has turned out to be a self- inflicted bugbear, restricting the Government from bringing about any change in this structure. In order to enable the Centre and the State Governments to levy GST, the Constitution of India requires modification to provide for powers to levy and collect GST both by the Union and the States.

- IT Infrastructure:

Rapid need for implementation necessitates IT infrastructure for the Goods and Services to upgrade itself. This requires development of comprehensive solutions to facilitate the adoption in the required timeframe. The IT systems on ERP and API side would be largely affected from the inculcation, as existing ERP vendors require to build patches that meet complete needs of GST execution on a techno-enable scale. This would then facilitate integration of API’s; with GSTN released API needs to be tweaked.

New formats of Invoice, Vendor master, Revenue master, Stock transfer, PO & SO master, Customer master, Expense GL, Goods & Service master need to be integrated into the system , taking the whole number of API’s to 80, where every API need 2 weeks of all-inclusive testing, prior to being released as a stable version. The need of the hour is for GSP’s to start working together to develop API jointly, sharing the workload. GST is set to become a welcome change for the economy, simplifying the indirect tax structure in India. Yet, the above challenges need to be assessed fully, with immediate changes to facilitate growth. Aided by a more comprehensive framework of constitution and other factors, GST can embolden the frame of a reformed economic system, empowering India to reach greater heights.

VII. Keeping infrastructure on standby

The all-new Goods and Services Tax (GST) has created chaos and a sense of panic among existing and prospective taxpayers. But in spite of it all, the new era will throw open huge opportunities for information technology (IT) companies enterprise resource planning (ERP) solution providers, tax consultants and the legal fraternity. GST is a complete overhaul of the old indirect tax system, and what makes it even more disruptive is the fact that all transactions under GST - right from registration and raising invoices to filing returns and paying taxes - have to be done online. There would be no manual filing of returns, no paper invoices and no physical payment of taxes. It also means all existing assessees and those who are likely to come under the tax net after its formal launch on July 1, have to adopt a digital interface to interact with the tax authorities and move their internal operations to the digital space.

As per the GST Network (GSTN), the company that has created and maintains the IT framework for GST, there are eight million excise, VAT (value-added tax) and service tax assessees under the existing system, out of which 6.5 million have registered with the GSTN. But the number of micro, small and medium enterprises (MSMEs), according to government data, stands at 36 million and many will now come under GST's purview. These are the businesses which must get GST-ready and there lies the opportunity for most businesses mentioned above.

The Compliance Trigger

In spite of all the talk about simplification, the final shape that the five-tax-slab, dual authority (the Centre and the states) GST has taken is exceedingly complex and may result in huge confusion among taxpayers. Therefore, a lot of action is bound to be seen in the compliance space and almost everyone could be making hay. ERP solution providers will continue to gain business as GST requires companies to change their internal systems and realign with the new tax regime. In fact, two different categories of entities have come up ever since the GST contour started emerging. These are the GST service providers (GSPs) and the application service providers (ASPs).

The primary role of GSPs is to act as facilitators for uploading invoices and returns. On the other hand, ASPs will provide more value-added services such as processing raw business data and entering the same into a GST-compliant format to be uploaded on the GST Network. As GSPs will directly interact with the GSTN system, they have to be approved by the latter. So far, the GSTN has selected 34 entities while 160 more have shown interest. In contrast, anyone can operate as an ASP. The government or the GSTN has no role in their selection.

The Strategy Boost

In the current system, the tax is applied only after sales happen, but post-GST, the tax will be levied when the goods move. Given this paradigm change, companies will have to realign their business strategies and rethink their inventories, pricing and warehousing. All these will require restructuring and consolidation, opening up opportunities for ERP solution providers like SAP, Tally and Oracle, as well as financial and legal professionals. Finally, the new tax regime will unleash a data deluge, which will be of immense value. The data gathered will throw up many trends and patterns, ushering in better business intelligence that can benefit both businesses and the government. This can also be a big income generator for data analytics and software firms. The only catch: Wherever data is involved, its misuse is also a concern.

Lack of information on GST provision

India's Goods and Services Tax (GST), is being called a 'game changer' for its far-sweeping impact on business. Manufacturers, traders, and service providers across India have been placed under one unified tax umbrella, and no longer need to work with a tedious array of 17 distinct types of taxes they currently need to comply with. The industry, at present, is struggling to get on with the destination-based tax from an origin based tax.

GST preparedness among clients is missing

Clients' understanding of GST provisions and its impact on their business is still at a nascent stage, and many are still identifying the locations and places they need to be registered in. These businesses are also assessing the mandated GST-compliance their relevant functional departments need to adhere to, including their Supply Chain, IT Systems, and Legal. This is necessary for identifying their new Working Capital, Cash Flow, and Fund Flow needs. To be on the right side of the GST anti-profiteering clause, businesses are also assessing their cost sheets while performing Comparable Analysis of the Lack of Clarity on GST Provisions (Rules and Regulation) Various provisions of GST are still ambiguous. Categorisation of goods and services in various cases is still unclear. Provisions for anti-profiteering, as well as the now-deferred e-way bill, which tracks consignments across states, are unclear. The new tax regime requires transporters to generate e-way bills on the GST portals which include incurring substantial costs to install radio frequency identification devices (RFIDs). Currently there is no clarity on who will bear the bill for GST.

Increased compliance, with increase in the number of returns to be filed annually

Businesses will need to file multiple returns, a minimum of 37 in most cases for assesses, and this can increase multifold in accordance with business models. Clients will need to ensure timely compliance by registered suppliers to ensure there is no loss of input credit. This will necessitate correct data and reports to fill accurate GST returns.

Preparedness of IT Systems

Various businesses are yet to map the accounting software and IT systems in line with the new tax provisions, to create GST invoices, and extract required reports. Tax and accounting professionals jointly need to ensure that their clients' current systems are compatible with their GST Service Provider (GSP). With GST demanding compliance, only days after guidelines were issued in their entirety, India Inc is rushed for time to modify the entire IT framework. Seamless implementation will require six million micro, small, and medium enterprises (MSMEs) to adapt their invoicing approaches for which they do not have adequate IT support and systems.

Lack of skilled resources and need for re-skilling

With GST rates and their complexities only recently becoming a part of our policy framework, skilled staff with updated GST subject knowledge and training is not easily available. This has placed an additional work load on personnel across industries, and created an urgent need for additional GST-skilled resources to ensure swift implementation. While GST aims to streamline business and protect consumer interests, the legislation should not allow a sense of apprehension to impact industrial interests. GST is both a challenge and an opportunity for tax and accounting professionals, and a knowledge of cloud, big data, analytics, and business.

VIII. The Pitfalls are Daunting

Technology

The GST Network will process as many as 3.5 billion invoices each month. Taxpayers may be required to file as many as 37 returns a year. Experts doubt the system will be able to seamlessly match billions of credits, facilitate tax collections, provide refunds and check evasions.

"Non-functioning of the GSTN portal, due to technical glitches is something which could give sleepless nights to the industry and thus can be a dark nightmare, "said Harpreet Singh, partner, indirect tax at KPMG in India.

Shortages

Some companies, particularly in the consumer goods sector, are selling off their inventories to avoid having to deal with two different prices for the same product. Some may also be delaying production so they can claim a credit against their costs for the first time under the new regime. Conversely, once July 1 rolls around there could be transportation bottlenecks as stores rush to restock.

Inflation

The fact that most commonly used items will be taxed at a lower rate than previously argues that the GST should in theory be disinflationary, according to the Nomura note. But Sonal Varma and Neha Saraf, authors of the note, said that while the consumer price inflation could drop by 33 basis points in the short term, core inflation could rise by 60 basis points because of increased taxes on services. They note it may be difficult for authorities to enforce anti-profiteering rules.

Law

GST laws have introduced multiple new concepts like "supply" and "location of supplier" which can throw up different interpretations. Lack of tax literature and judicial precedents may add to confusion as industry and lawyers begin to grapple with new concepts, said Singh of KPMG.

Small Business

Small businesses which haven't been in the tax net before may continue work in cash and have less than perfect books. Nevertheless, they'll be required to upload their tax details to the GSTN and compute their returns if they fall across the threshold for inclusion under GST which stands at 2 million rupees ($30,983) of annual sales. "Overall there will be some nagging problems to begin with on the implication and compliance sides," said Madan Sabnavis, chief economist at Credit Analysis

& Research Ltd. in Mumbai. "But this will be temporary for the first six to nine months."

IX. CONCLUSION

One of India's most ambitious economic reform plans in 70 years will ultimately boost tax receipts and provide simplicity for businesses, but the true impact may not be felt for at least a decade due to implementation challenges. It can also be used as an effective tool for fiscal policy management if implemented successfully due to nation-wide same tax rate. It execution will also results in lower cost of doing business that will make the domestic products more competitive in local and international market. No doubt that GST will give India a world class tax system by grabbing different treatment to manufacturing and service sector. But all this will be subject to its rational design and timely implementation. There are various challenges in way of GST implementation as discussed above in paper. Although implementation of GST requires concentrated efforts of all stake holders namely, Central and State Government, trade and industry. Thus, necessary steps should be taken. There will be a need for some regulation around data use because that [GST] data is extremely valuable. Although it should not be misused, the data should be utilised for the right reasons.

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