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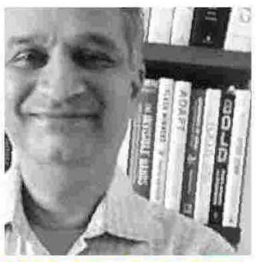
THEIR VIEW

What four years of GST have taught us about this tax regime

There's a long way to go for it to fulfil its promise even as many of its myths have been demolished



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When the Goods and Services Tax (GST) was launched on 1 July 2017, it was an achievement. There had been a lot of political bickering and getting it off the mark was a daunting task. The idea was for India to adopt this new taxation regime and fine-tune it along the way. Four years on, how does it look?

When GST talks were on, there were two divergent views. The establishment-supported view spoke of how gross domestic product (GDP) growth will increase by 1-2 percentage points, inflation would come down, and government revenue would increase. However, it rarely happens that everyone is better off and no one worse off. At the other end, sceptics argued that a GST system with five rates was hardly a worthwhile regime. Besides, Micro, Small and Medium Enterprises (MSMEs) would face serious problems on taxes, refunds, set-offs and fines. Therefore, it hardly made sense. There were political noises on the compensation part for states in case of shortfalls, and there was an assurance that there would be payments made from the cess buffer created for this purpose in case state revenues did not rise 14% annually.

Let us see how things have progressed. Two adjustments made by the government were the introduction of a 'composition scheme' for MSMEs and the altering of GST rates for various commodities after representations were made. Clocking ₹1 trillion every month in GST revenue emerged as a thumb rule for its success. As GST is a consumption-based tax, the economy has to keep ticking along and people have to spend for it to work.

The twist in tale began with 2017-18, when GDP growth slowed down. From 8.3% in 2016-17, it declined to 4% in 2019-20 before it turned negative in 2020-21 with an 8% output contraction. Hence, India's GST collection base has narrowed in relative terms, creating a conundrum. As a proportion of GDP, GST collections were 6.9% in 2018-19 which came down to 6.6% in 2019-20 and 5.8% in 2020-21. Clearly, this part of the story has not worked out.

The biggest challenge for the GST regime concerns compensation to states. This is something the states would like reviewed, as the 14% growth-determined compensation was to last five years, and with just a year of it left, appears to be on slippery ground. Due to lockdowns in 2020 and again in 2021, people have not been able to spend much. This has affected revenue intake. When GST compensation was initially discussed, it was not expected that all states would have to be paid for shortfalls at the same time. It may be recollected that neither the states nor the Centre wanted to borrow to fill this gap in FY21, and finally the latter had to relent and go to the market. This issue has to be addressed, as such a situation could arise again and the provision may have to be extended by five more years.

The second challenge relates to exclusions. The government had kept fuel and 'sin goods' out of GST's ambit so that it could retain control of this lever to raise rates and garner revenue. This has to change, as an unintended consequence has been higher inflation, as witnessed today. It is quite absurd that out of petrol's retail price of ₹100-105 per litre, a little over ₹60 goes as taxes. The problem is that its price is influenced by the global crude oil price, which is now testing $75 per barrel. Add to this taxes in the form of excise (₹33 per litre) and value-added tax (30% in Delhi), and the consumer confronts high pump prices. Lockdowns result in less fuel consumed and lower revenue for the government. The solution has been to raise these taxes so as to protect revenue. Post-GST excise collections had come down to ₹2.3 trillion, but rose to ₹3.7 trillion in 2020-21.

The secondary effects of higher fuel costs are through the transport route, as prices of all commodities increase once transport costs get worked in. Petrol and diesel have a combined weight of 2.3% in the consumer price index. This may seem small. But the knock-on effect is sharp, as it leads to higher prices of foodgrains and manufactured goods alike. This is why retail inflation has been higher than it should be and the role of fuel not being under GST is very significant.

The third challenge is fulfilling our need to apply a single rate to all goods. Otherwise, GST resembles the complex earlier regime, except for its subsuming of state taxes. The last four years have given us an understanding of how goods should be taxed and the revenue that will accrue to the government. There is now a pressing need to reduce multiple rates into a single slab.

Our four-year experience has also demolished a few myths about the tax. GDP growth increases only in case there is more income that gets spent, which is best accomplished by creating more jobs. GST itself cannot increase GDP, though it can statistically include the unorganized sector to an extent, and should not be mistaken for a growth enhancer. Second, with deep contradictions in our tax structure, inflation will remain beyond the grasp of GST. Third, for government revenue to rise, the economy needs buoyancy. Under our present low-growth syndrome, we cannot expect miracles. These are the revealed facts of GST.

These are the author's personal views.

10 YEARS AGO

JUST A THOUGHT

Tolerance implies no lack of commitment to one's own beliefs. Rather, it condemns the oppression or persecution of others.

JOHN F. KENNEDY