

The standard tax rate for states has come down sharply compared to the VAT regime. Merging the present multi-rate system into a single rated one would further reduce revenue

IT'S TIME TO REVISIT THE BASICS OF GST

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GST has failed to deliver the promise. Even after four years, the IT backbone for its full implementation is not in place. The tax buoyancy has been far below expectations and with Covid, the shortfall has ballooned. The compensation payments are delayed and in arrears. And now, as the compensation guarantee period is drawing to an end, most states are drifting to the precipice of sudden fall in revenue and inevitable fiscal crisis. There is a lack of dialogue on these issues—the GST Council failed to meet for more than six months at a stretch and when it finally did, some veterans of the Council openly complained of the undemocratic manner in which the business was transacted. The discussions have degenerated to party alignments. A former Union finance minister feared that the time might come to script an elegy for the GST.

It is time now to undertake a comprehensive review of the experience with the GST. I feel that minor tinkering will not do, some modifications will have to be brought in its structure itself so that the federal concerns are addressed, buoyancy of revenue assured, and the GST Council become truly an institution of federal cooperation.

Federal flexibility: Let me recall the initial discussions in the Em-

powered Committee of State Finance Ministers (EC) on the introduction of GST. The three left finance ministers in the committee shared concerns about the implication of the new tax regime for state rights. The introduction of the uniform state VAT, the overseeing of which was the mandate of the EC, had abridged individual autonomy but there continued to exist some leeway regarding the tax rates.

GST was seen as extension of the VAT principle to the national scale, with most of the other indirect taxes of the states and service and excise tax of the Centre subsumed in the new tax. Both Centre and states were to jointly administer the GST. In every invoice, both CGST and SGST had to be separately shown and the taxes so collected paid separately into the account of the Centre and states. The GST on inter-state trade (IGST) was to be separately collected. In this scheme of things, the SGST did not directly impact inter-state trade. Therefore, the basic architecture of the GST and its input credit chain is not affected by giving states the option to choose a particular SGST within a narrow band. Though the VAT had introduced uniform tax rates throughout India, in practice, there existed minor variations between states. It was the general under-

standing that this flexibility would be carried into the GST.

In the GST law adopted by Parliament, the only flexibility that was permitted was the right of the states to impose a special cess for a definite period in extraordinary circumstances like natural calamities, that too with the approval of the Council. On the basis of experience so far, the situation has to be revisited and some level of federal flexibility must be introduced.

The issue of rate split: Another key issue was the rate of apportionment of the GST rates between the Centre and states. Many states had adopted a consistent position during the discussions in the EC that the apportionment of rates of GST between the Centre and the states should be 60:40. The logic for this was recognised by the Government of India committee on Revenue Neutral Rates headed by

the then chief economic advisor.

Yet, the final decision went against the states with the equal apportionment of GST rates (on a 50:50 basis) between the Centre and the states. Now, for most of the commodities that were taxed at 14.5% under the VAT regime, the states receive only 9%, which is 50% of the 18% GST. This too on a base which is devoid of CST and Union excise duty.

Revenue neutral rate?: The GST rates were fixed after elaborate discussions in the Council and its committees. Unfortunately, with elections on the horizon, ad hoc decisions were made, reducing the rates so that the present structure is not revenue neutral anymore. The major rates are 5, 12, 18 and 28. Besides there are zero rated commodities, 3% for gold and 0.25% for precious metals. Initially, the standard rate in GST was 18%. Presently, the rate under which more than 80% of goods and services are taxed are at 18 and 12% respectively.

This implies, as we have just seen, that the standard rate for states has come down sharply compared to the VAT regime. The Centre still has many other buoyant direct taxes and customs duty, which is not the case for the states. The tax on petroleum products can be subsumed in GST, if the Council

decides to do so. So the states have been permanently handicapped by the reduction of the standard rate. The clamour for merging the present multi-rate GST into a single rated one, if attended to, would result in further deterioration of GST revenue collections.

Need for progressivity in the rates: If there is movement to a single rate, GST would lose even the semblance of progressivity in an otherwise regressive indirect tax. Rates on consumer durables and urban products are the ones that have seen the sharpest decline. It is these same products that would further gain if the demand for a maximum ceiling rate of 18% is accepted. The problem of the multiplicity of rates is exaggerated. One only needs to think of the rate structure that existed before GST to realise the extent to which the tax structure has been simplified. It is not multiple rates but the procedures and the frequent changes that is responsible for the complexity of the GST. Given the mass poverty and high level of income inequality in the country, it is preposterous to suggest a common rate of tax for grain flour and luxury vehicles. The ideal of equity should be considered at least as important as the ease of doing business.

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