

# Regulatory Hotline

August 29, 2016

## NO GHOST IN THE GST MACHINE

### A POST-GST REGIME MUST ENSURE THERE ARE NO REMNANTS OF A LEGACY TAX REGIME

Assignificant as the Constitution Bill (Amendment Bill) 2014 being passed in Parliament is, the passage of a single goods and services tax (GST) law would be even more unprecedented. Given India's complicated division of legislative powers, political landscape and the disparate needs of states, a GST law would be a remarkable achievement with few comparable precedents in the world.

Introducing levies beyond the proposed GST law, or raising these beyond reasonable limits, would defeat the economic benefit of an integrated value-added tax (VAT) regime. The fine print of the model GST law shows that credit is not allowed in respect of all taxes paid under the model GST law. So, increasing such taxes would only raise the cost of goods or services available to consumers.

Chief economic adviser Arvind Subramanian's views were echoed in Parliament when various MPs agreed that a high GST would effectively negate any benefit of the GST. This, in turn, would adversely affect startups that may not be able to absorb the burden of a high tax. For instance, the equalisation levy that is purportedly a tax on services received is enforced through the Finance Act and effectively denies the benefit of any credit under the model GST law or the existing Central VAT (Cenvat) Credit Rules.

High consumption taxes incurred by startups and e-commerce entities will create a cascading effect and may deter consumers. India's goods and services market is price-sensitive and quite elastic, and without taking these factors into consideration, levy of high taxes can have an adverse impact on India's startup and e-commerce entities.

## NO SPACE FOR SURPRISES

It is important that in an effort to raise revenue from a growing economy, taxes to be levied by the central and state governments are rationalised and all consumption taxes are subsumed in GST. Few things can be a dampener as finding in a post-GST regime remnants of a legacy tax regime that includes levies such as octroi, local cess and other local taxes. The government should also avoid taxing through the Finance Act. Such measures would defeat the economic and commercial objective behind GST.

India's taxation powers are shared between the Union government and state governments, and the Amendment Bill makes changes to these legislative powers. The Bill has deleted certain important legislative entries such as Entry 52 of List 2 (entry tax) and Entry 92C of List 1 (service tax), and amended others such as Entry 54 of List 2 (taxes on sale of petroleum, diesel, alcohol, etc). While the taxation powers of the state have been streamlined, it is imperative that for a GST to be successful, the central government will have to resist levying taxes through its residuary legislative powers in Entry 97 of List 1.

The Amendment Bill and GST may help reduce litigation in traditional dispute areas such as legislative powers of the central and state governments, since substantial taxation powers now vest with the former. However, if these powers are not efficiently exercised, GST may well lead to multiple taxes and more litigation on taxation powers.

For instance, while Entry 52 of List 2, which provides for the levy of entry tax, is deleted, the powers of the state government to impose taxes on goods under Entry 56 remains unaffected. The Amendment Bill has also omitted Entry 92 (taxes on advertisements in newspapers) and Entry 92C (service tax) of List 1.

This is disconcerting as it points to the central government resorting to residuary legislative powers in Entry 97 with more frequency. Entry 97 of List 1 provides for the residuary legislative powers (and plenary at that) of the Union government.

These changes to the legislative powers are crucial and integral to the Amendment Bill. It is important that Union and state legislatures respect these changes and the intent of the changes for the GST law to succeed. As every superhero knows, with great power comes great responsibility. And with great legislative power comes even greater responsibility.

Continuing with taxes -such as an equalisation levy or a service tax administered via the Finance Act would defeat the purpose of a centralised VAT. Although there is no morality in taxation, such taxes would be constitutionally dishonest.

## NO SELF-SAME TAX

The hard part of a GST law -political consensus and constitutional amendments -is done. What is required now is the practical and commercial administration to ensure that the government doesn't score an own goal in raising revenues from GST. It is important that the Union and state governments cooperate. Having a high GST rate would

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make GST and existing taxes mathematically similar and defeat the purpose of GST.

Keeping the GST simple will also help in cost-effective administration. Ultimately , all of these will help in the government achieving its objective of maximising revenues through indirect taxes.

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This article was published in The Economic Times dated August 27, 2016. The same can be accessed from the [link](#).  
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– **M.S. Ananth & Pratibha Jain**

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