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Tax Alert India

India Paves the Way to GST Rollout

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Summary and Analysis

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On **3 August 2016**, the Indian Parliament approved the introduction of the long awaited **Goods and Services Tax**, GST. It is perhaps the biggest tax reform in the modern history of India. Until today, the country's indirect tax system is split into a great number of tax regimes, covering Central Sales Tax, state based Value Added Taxes, municipal Octroi taxes, taxes on the manufacture of goods (Excise Duty) and on rendering of services (Service Tax). Plus many more. The GST is bound to replace most of these regimes and to create a uniform country-wide indirect tax system. The rollout of GST will ease the business in India to a great extent.

It is expected to boost India's GDP growth rate by upto 2% according to recent comments and a study published by India's National Council of Applied Economic Research.

GST Bill being Passed

The Indian political system witnessed a historical moment on 3rd August 2016, when the Constitutional (122nd Amendment) Bill 2014 ("**Constitutional Amendment Bill**"), which is the enabling law for implementation of Goods and Services Tax ("GST") was unanimous passed by the Upper House of the Indian Parliament. With the passage of the Constitutional Amendment Bill, the stage is now set for rolling out of GST in India with a challenging deadline of 1 April 2017. After discussions with all stakeholders, the Government dropped the provision proposing the contentious 1% additional non-creditable GST on inter-state supply of goods and services. Yet, other proposals on capping of GST rate in the Constitution and modalities of dispute resolution between the Central and State Governments have been left to the proposed GST Council.

Taxes to be Replaced by GST

GST will replace the following tax regimes:

Central Level Taxes	*State Level Taxes*
Central Excise Duty on manufacturing in India	**Value Added Tax/ Central Sales Tax** on sale of goods in India
Service Tax on provision of services	**Entry Taxes** on specified goods
Additional Customs Duty ("CVD") on imports	**Octroi/ Local Body Tax**
Special Additional Customs Duty ("SAD") on imports	**Luxury Tax** on hotels
Various Cesses such as Swachh Bharat Cess, Education Cess etc. on goods and services	**Entertainment Tax** on events etc.
Additional Excise Duty on specified goods	**Purchase Tax** on goods

Customs duty in the form of **Basic Customs Duty** ("BCD") on import of goods into India and **Research & Development Cess** on import of technology into India will continue to apply. Also **Stamp Duty** on immovable property and legal instruments will stand unchanged. GST will further not replace taxes on electricity, petroleum, alcoholic liquor for human consumption and tobacco products.

Structure of the GST

The final structure of GST is not yet set. However, a model Goods and Services Tax Act ("**Draft GST law**") was released on 14 June 2016 for public comments.

The Draft GST law prescribes that both the Central and State Governments would levy GST in parallel on supply of goods and/or services where such **supply is made within the state**.

- The tax to be levied by the Central Government would be referred to as **Central Goods and Services Tax** ("CGST").

- The tax to be levied by Sate Government would be known as **State Goods and Services Tax** ("SGST").

In case of Inter-State supply, an **Integrated Goods and Services Tax** ("IGST") will be levied, which would be collected and administered by the Central Government.

Imports into India would be subject to **IGST** and **Basic Customs Duty**.

The **rate of GST** is not fully settled, yet. It may range between 16-20% of the value of supply, which is still being debated by the political parties.

Threshold Limit and Registration

It is proposed that every person engaged in supply of goods/ services with an **aggregate turnover exceeding INR 0.9 million** per Financial Year (INR 0.4 million for north-eastern states) shall be required to obtain registration in the respective State. However, GST would apply on the supplies once the turnover crosses INR 1 million (INR 0.5 million for north-eastern states). Exemptions exist. The turnover limits would not be applicable for persons undertaking inter-state supply, persons liable to pay tax under reverse charge mechanism, casual dealers (persons undertaking business in states where they do not have any place of business), E-Commerce operators/ aggregators and non-resident taxable person (foreign companies not having a fixed establishment in India), in whose case, registration would be mandatory.

Input Tax Credit

The credit of input CGST can be taken against output CGST and IGST. Vice versa, credit of input SGST can be taken against output SGST and IGST. **Cross-utilization of credit between CGST and SGST is not allowed.** However, credit of input IGST can be taken against all three types of GST, i.e. CGST, SGST and IGST.

Transitional Provisions for Existing Companies

It is proposed that existing taxpayers would be **automatically migrated to the new GST regime** without having to make a separate application for registration. The Draft GST law however provides for transition provisions connected with pending litigations and other matters. Further, it is also proposed to allow the existing taxpayers to carry forward the unutilized Input Tax Credits under the CENVAT and VAT schemes to the new GST regime.

Our Comment

The new GST will **simplify Indian indirect taxes** to a great extent. Unclear and heavily debated qualifications such as "manufacture", "sale" and "provision of service" will lose their relevance. This will also reduce the issues of double taxation under sectors like Information Technology Software and Construction Services. The highly complicated customs duty structure with several duties such as BCD, CVD and SAD being levied and calculated on each other would get cleared out. Under the GST regime, import of goods would attract BCD and IGST making the structure simpler. The availability of Input Tax Credit of IGST to importing resellers would significantly improve the tax cost in the supply chain.

On the **downside**, the GST regime would require companies to maintain **separate input tax records** for each state they are operating in (selling from) in order to correctly utilize the tax credit. The draft GST law also provides for electronic cross verification of input tax credit between information submitted by the supplier and recipient for entitlement. This will significantly increase the compliance burden due to the requirement of maintenance of itemwise details for supplies along with costs associated with robust IT infrastructure. Further, apart from certain exclusions, GST would be applicable on all commodities and articles. With a broad definition of the term "Service" which includes anything other than goods, **the coverage of GST will be very vide**. This would enable the Government to tax items such as the transfer of actionable claims which were outside the present tax structure. GST will further not replace taxes on electricity, petroleum, alcoholic liquor for human consumption and tobacco products. Exclusion of electricity and petroleum from the GST regime would continue to impair implementation of a unified tax regime and the said sectors may face inflationary situations on account of blockage of input tax credits.

Road Ahead

The Government is looking at a challenging deadline of **1 April 2017** for implementation of GST. In order to achieve this, the Constitution Amendment Bill needs to be again approved by the Lower House, ratified by a minimum of 51% of the State assemblies and assented by the President. Thereafter, the GST Council would be notified which shall be entrusted to recommend on various key matters such as approving of GST Bills, rate of GST, list of exemptions, dispute resolution mechanism, etc. The CGST Bill and IGST Bill would then have to be passed by the Central Government while the SGST Bill would have to be passed by all the State Governments to make GST a reality.

While the Government seems to be ready with the IT infrastructure which is expected to be tested in October 2016 and subsequently launched in February 2017, it has to finalize the most contentious issues such as the GST rate as well as dual administration/ control.

The industry now needs to get "**GST ready**" with the essential infrastructural and strategical arrangements beforehand such as IT infrastructure, pricing strategy, supply chain structure and effective transitioning to avoid any last minute issues.

Way Forward

- Assess the situation of your enterprise in India.
- Evaluate the impact of GST of all transactions (input and output) undertaken in India.
- Revisit the pricing policy for your products and legal agreements executed with customers/ vendors.
- Assess the need for change in the supply chain including additional tax registration.
- Review the existing IT infrastructure and training needs for your employees to make your Indian Enterprise "GST Ready".

Rödl & Partner:

In 2007 Rödl & Partner established its own presence in India with offices located today in Pune, Mumbai and Delhi. Rödl & Partner has recently set up its 4th of presence in India, as a working point in the city of Chennai, Tamil Nadu to meet the growing demand of quality services in the southern region of the country. Chennai is strategically located with good access to the Shri City area. The Rödl & Partner working point in Chennai, together with further specialists in the Pune office, is available to provide all required services from planning the suitable form of set up right up to the day-to-day compliances for the operations of the unit in Shri City.

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