



International Journal of Financial Management and Economics

P-ISSN: 2617-9210
E-ISSN: 2617-9229
IJFME 2020; 3(2): 103-106
Received: 25-10-2020
Accepted: 21-11-2020

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GST: A catalyst for sustained economic growth

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DOI: <https://www.doi.org/10.33545/26179210.2020.v3.i2.502>

Abstract

To make India as a financial super power, the introduction of GST is must. There are much apprehension relating to proposed GST regime regarding the growth in Indian Economy and its effects thereof. As we know in India economy, destination-based taxation requires high compliance cost and efficient administration. Taxation both direct and indirect plays an important role in promoting economic growth as well as equitable distribution. As we are facing the cascading system of indirect taxes in India and with the introduction of GST, all the cascading effects of Cenvat (Central Value Added Tax) and service tax will be more comprehensively removed with a continuous chain set off from the producer's point to the retailer's point. Moreover, certain major Central and State taxes also subsumed in GST. We have also experienced the benefits from the VAT reform which include the growth in economics of States and business community.

Keywords: Cenvat, employment, Tax, GST, VAT

Introduction

In July 2017, India embarked on a landmark tax reform journey with the introduction of the Goods and Services Tax (GST). This comprehensive indirect tax system replaced multiple taxes levied by the central and state governments, creating a single, unified tax framework. In this article, we delve into the key features, benefits, challenges, and impact of GST on various stakeholders.

Direct and indirect taxation play an important role in promoting economic growth as well as equitable distribution. As we are facing the cascading system of indirect taxes in India and with the introduction of GST, all the cascading effects of Cenvat and service tax will be more comprehensively removed with a continuous chain set off from the producer's point to the retailer's point. Moreover, certain major Central and State taxes will also be subsumed in GST. The greatest impact of the implementation of the GST would create a common market across the country and reduce compliance costs and thus, creates an equitable distribution. In the absence of significant fiscal options, incentivized policy to attract investors to states would shift to greater emphasis on structural reforms. The over macroeconomic effect of reduction in economic distortions due to GST would be to provide an impetus to economic growth. Finance commission estimates the impact of the introduction of a GST which eliminate all taxes on production and distribution and rest on final consumption only. It is also expected that the opportunities of employment will be enhanced. The implementation of a comprehensive GST led to efficient allocation of factors of production and will lead to gain in GDP and exports. It enhance economic welfare and returns to the factors of production, i.e. land, labour and capital.

Features of GST

GST will subsume central indirect taxes like excise duty, services tax etc and also state levies like VAT, Octroi, entry tax, luxury tax etc.

GST is a multi-tier tax with several components to address the various types of transactions within and across states. The four primary components of GST are:

- **Central Goods and Services Tax (CGST):** Levied by the Central Government on intra-state supplies of goods and services.
- **State Goods and Services Tax (SGST):** Levied by the State Government on intra-state supplies of goods and services.

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- **Union Territory Goods and Services Tax (UTGST):** Levied by the Union Territory Government on intra-UT supplies of goods and services.
- **Integrated Goods and Services Tax (IGST):** Levied by the Central Government on inter-state supplies of goods and services, as well as on imports into India.

Intra-State and Inter-State Transactions

- **Intra-State Transactions:** For transactions within a state, both CGST and SGST (or UTGST) are applied. The tax revenue is shared equally between the central and the state governments.
- **Inter-State Transactions:** For transactions between states, IGST is applied. The tax is collected by the central government and then shared with the destination state where the goods or services are consumed.

GST Compensation Cess

In addition to the primary components, the GST Compensation Cess is levied on certain goods to compensate states for any revenue loss due to the implementation of GST. This ensures that states are not adversely affected by the shift to the new tax regime.

The GST Framework

GST is a dual tax system, with both the central government (CGST) and state governments (SGST) levying taxes. The tax structure comprises three slabs: 5%, 12%, and 18%, with some goods and services exempt or taxed at 0%. The input tax credit mechanism eliminates tax cascading, while the destination-based tax system ensures taxes are collected where goods and services are consumed.

Simplification of Tax Structure

GST has simplified India's tax structure, reducing complexity and compliance costs. By subsuming multiple taxes, such as excise duty, service tax, and value-added tax (VAT), GST has eliminated the cascading effect of taxes, making goods and services cheaper. This has led to increased competitiveness, benefiting consumers and businesses alike.

The Pre-GST Tax Regime: Challenges and Inefficiencies

Before GST, India's indirect tax system was complex and fragmented, characterized by multiple taxes at different levels of government. The central government levied taxes such as Central Excise Duty, Service Tax, and Customs Duty, while states-imposed taxes like Value Added Tax (VAT), Sales Tax, Entry Tax, and Octroi. This multiplicity of taxes created several issues:

Cascading Effect of Taxes: The tax-on-tax phenomenon increased the overall tax burden on businesses and consumers.

Compliance Burden: Businesses, especially SMEs, faced a significant compliance burden due to the need to adhere to multiple tax laws and filing requirements.

Interstate Barriers: State-level taxes created barriers to the free movement of goods across state borders, leading to logistical inefficiencies and increased costs.

Tax Evasion: The complexity of the tax system and the

lack of transparency facilitated tax evasion and corruption.

GST: Objectives and Structure

The GST was introduced with key objectives:

- **Simplification of Tax Structure:** Replace multiple indirect taxes with a single tax, simplifying the tax regime.
- **Elimination of Cascading Effect:** Ensure tax is levied only on the value added at each stage of the supply chain.
- **Creation of a Unified Market:** Facilitate the free movement of goods and services across state borders.
- **Enhancement of Compliance and Transparency:** Use technology to improve tax compliance, reduce tax evasion, and increase transparency.

Impact of GST on the Economy

Streamlining Taxation and Reducing Compliance Burden

The unification of multiple taxes into a single GST has significantly streamlined the tax structure. This has reduced the compliance burden on businesses, especially SMEs, which previously had to navigate a labyrinth of state and central taxes. The introduction of the GST Network (GSTN), an online platform for GST registration, return filing, and payment, has further simplified compliance.

Elimination of the Cascading Effect

GST has successfully eliminated the cascading effect of taxes by allowing businesses to claim input tax credits for the taxes paid on inputs. This has reduced the overall tax burden and made goods and services more affordable for consumers. For example, under the pre-GST regime, a manufacturer paying VAT on raw materials and excise duty on finished goods faced a higher tax burden due to the non-availability of cross-credit. GST has addressed this issue by enabling seamless input tax credit across the supply chain.

Creating a Unified Market

GST has transformed India into a single unified market, facilitating the free movement of goods and services across state borders. The removal of check posts and border taxes has reduced transit times and logistics costs. This has particularly benefited sectors such as e-commerce and manufacturing, which rely on efficient supply chains. According to a report by the World Bank, the implementation of GST has reduced the average travel time for interstate freight by approximately 20%.

Boosting Revenue Collection

The GST regime has led to a significant increase in revenue collection for both the central and state governments. The use of technology, such as e-invoicing and real-time transaction reporting, has enhanced compliance and reduced tax evasion. The increased transparency in the tax system has also contributed to higher revenue collection. In the fiscal year 2023-2024, GST revenue collection witnessed a growth of 15% compared to the previous year, reflecting the positive impact of the reform.

Encouraging Formalization of the Economy

GST has encouraged the formalization of the economy by bringing more businesses into the tax net. The requirement for businesses with an annual turnover exceeding ₹40 lakhs

to register under GST and the benefits of input tax credits have incentivized many informal businesses to formalize their operations. This formalization has multiple benefits, including better access to credit, improved business practices, and increased tax revenues. According to a report by the Confederation of Indian Industry (CII), the number of GST-registered businesses increased by 50% in the first three years of GST implementation.

Sectoral Impact of GST

Manufacturing Sector

The manufacturing sector has been one of the biggest beneficiaries of GST. The seamless flow of input tax credits and the removal of interstate barriers have increased efficiency and reduced costs. For instance, the automotive industry, which previously faced multiple taxes on different components, has seen a reduction in the overall tax burden. The elimination of border check posts has also reduced transit times for the movement of raw materials and finished goods, leading to cost savings and increased competitiveness.

Services Sector

The services sector, which previously faced multiple service taxes at different rates, now enjoys a simplified tax structure under GST. This has made compliance easier and reduced the tax burden. For example, the IT and IT-enabled services (ITES) sector, which often dealt with different service tax rates for various services, now benefits from a uniform GST rate. This has streamlined billing and accounting processes, allowing companies to focus more on innovation and growth.

E-commerce Sector

GST has been particularly beneficial for the e-commerce sector. The uniform tax structure and simplified compliance requirements have enabled e-commerce companies to expand their reach and operate more efficiently across states. The introduction of the concept of Tax Collection at Source (TCS) under GST has also provided a level playing field for online and offline retailers. This has encouraged more businesses to explore e-commerce as a viable sales channel, contributing to the sector's growth.

Real Estate Sector

The real estate sector has seen a mixed impact from GST. While the reduction in tax rates on under-construction properties has made housing more affordable, the input tax credit mechanism has created some challenges. Developers can no longer claim input tax credits for construction materials, leading to increased costs. However, the overall transparency and simplification of tax processes have benefited homebuyers and developers alike.

Challenges and Solutions

Compliance Complexity for Small Businesses

Despite the simplification brought about by GST, small businesses continue to face challenges in complying with the new tax regime. The need to file multiple returns and maintain detailed records has created a compliance burden for SMEs. To address this, the government has introduced several measures, such as the Composition Scheme, which allows small businesses with a turnover of up to ₹1.5 crore to pay a fixed tax rate and file quarterly returns.

Frequent Changes in Tax Rates and Rules

The frequent changes in tax rates and rules have created uncertainty for businesses. This has made it difficult for companies to plan their finances and operations. To address this, the GST Council, the apex decision-making body for GST, has been working towards stabilizing the tax rates and reducing the frequency of changes. The introduction of an annual return filing system and the rationalization of tax rates are steps in this direction.

Technological Challenges

The GSTN, the technology backbone of GST, faced several challenges in the initial years, including server downtime and technical glitches. This impacted the timely filing of returns and processing of refunds. To overcome these challenges, the GSTN has undergone significant upgrades, including increasing server capacity, improving the user interface, and introducing automated tools for reconciliation. These measures have improved the overall user experience and reduced technical issues.

Addressing Tax Evasion

While GST has improved compliance, tax evasion remains a concern. Some businesses still engage in practices such as underreporting sales or creating fake invoices to evade taxes. To combat this, the government has introduced measures such as e-invoicing, which mandates the generation of electronic invoices for B2B transactions, and the use of data analytics to detect discrepancies. These initiatives have enhanced the ability of tax authorities to track and monitor compliance.

The Road Ahead

Integration of Advanced Technologies

The future of GST in India lies in the integration of advanced technologies such as artificial intelligence (AI), machine learning (ML), and blockchain. AI and ML can be used to detect patterns of tax evasion and predict trends, allowing tax authorities to take proactive measures. Blockchain technology can provide a secure and immutable ledger for transactions, reducing the chances of fraud and ensuring greater transparency in the tax system.

Simplification of Compliance

Further simplification of compliance processes is essential to make GST more business-friendly. This includes reducing the number of returns required, simplifying the input tax credit mechanism, and providing more clarity on tax rates and rules. The government is already working on a new return filing system, which aims to further simplify the process for taxpayers. This system will streamline the filing process by integrating multiple returns into a single form, reducing the administrative burden on businesses.

Enhancing Data Analytics Capabilities

The use of data analytics and big data will play a crucial role in the future of GST. Advanced data analytics can help in identifying patterns of tax evasion, predicting revenue trends, and optimizing tax policies. The GSTN can leverage these capabilities to enhance compliance and improve the efficiency of the tax system. By analysing transaction data, the GSTN can identify discrepancies and potential fraud, allowing tax authorities to take timely corrective actions.

Strengthening the GST Council

The GST Council has been instrumental in the successful implementation of GST. Strengthening the Council's role and decision-making capabilities will be crucial for the future of GST. This includes ensuring a more collaborative approach between the central and state governments, improving the decision-making process, and addressing the concerns of various stakeholders. A stronger GST Council can drive further reforms and ensure the continued success of the GST regime.

Expansion

Expanding the GST base by including more goods and services under its ambit will increase revenue collection and simplify the tax structure. Items such as petroleum products, real estate, and electricity are currently outside the purview of GST. Bringing these sectors under GST can help in creating a more comprehensive and uniform tax system. The inclusion of these sectors will not only increase revenue but also reduce the complexity and fragmentation of the current tax structure.

International Best Practices

India can learn from the experiences of other countries that have implemented GST or similar value-added tax systems. By adopting international best practices, India can further refine its GST system to make it more efficient and effective. This includes studying the GST models of countries such as Australia, Canada, and Malaysia, and incorporating elements that have proven successful in these jurisdictions.

Recapitulation

The introduction of GST in India has been a transformative reform with far-reaching implications for the economy. By simplifying the tax structure, eliminating the cascading effect of taxes, and creating a unified market, GST has significantly contributed to the country's economic growth. The impact of GST has been felt across various sectors, with manufacturing, services, e-commerce, and real estate witnessing significant benefits. While challenges remain, such as compliance complexity for small businesses, frequent changes in tax rates and rules, technological issues, and tax evasion, the government has been proactive in addressing these concerns. The future prospects of GST look promising, with continued efforts to integrate advanced technologies, simplify compliance, enhance data analytics capabilities, strengthen the GST Council, expand the GST base, and adopt international best practices.

GST has not only improved the efficiency of the tax system but also contributed to the formalization of the economy, increased revenue collection, and boosted the overall business environment. As India continues to refine and optimize its GST system, it is poised to achieve sustained economic growth and become a more attractive destination for investment and business. By focusing on continuous improvement and addressing the challenges, GST can truly become a catalyst for sustained economic growth in India, driving the country towards greater prosperity and development.

Conclusion

The introduction of the Goods and Services Tax (GST) in India has streamlined the tax structure by consolidating

multiple indirect taxes into a unified system. This reform has eliminated the cascading effect of taxes, enhanced compliance, and increased transparency. By creating a unified national market, GST has reduced logistics costs and improved the ease of doing business. Despite initial challenges, GST has positively impacted revenue collection and economic growth, positioning India as a more attractive destination for investment. Ongoing refinements aim to further simplify compliance and broaden the tax base, ensuring sustained economic benefits.

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