The way forward on GST

On the 1st of July, India transitioned to a Goods and Services Tax (GST) regime where a multitude of indirect taxes were replaced by a single levy. So far, it is still a policy in the making with new rules emerging on a frequent basis, necessitating repeated changes to ERP systems and accounting protocols. Clearly, everybody is learning on the job. The GST seeks not only to simplify the tax chain but, more significantly, to widen the tax net. India's large 'informal sector' has historically enjoyed a tax arbitrage which the GST seeks to eliminate. It is possible that the Government, aware that GST was bound to happen, demonetised 86 per cent of currency in circulation as a means also to induce small businesses to transcend into the formal economy. The GST will now compel them to do so.

In an ideal world, there should have been one tax at one rate instead of the current structure with six slabs and several exclusions. However, when a decision needs consensus from 28 states and 7 Union Territories, arriving at a common denominator is a demanding task and compromises are inevitable. A second reason for multiple tax slabs was the desire to maintain tax neutrality to keep inflation in check. Nothing can be more damaging politically than price instability. Optimists suggest that in the fullness of time, a Government of the future may choose to move in a more ideal direction.

One consideration that is worrying businesses is the anti-profiteering clause wherein a complaint from almost anyone can trigger pricing investigations. Under the new regime, if a product benefits by way of lower tax incidence the seller would be required to reduce its price. A multi-product company that wants to maintain a higher price to cross subsidise another might then need to formally justify its pricing decisions. The same would apply to companies that follow psychological pricing where it is not always feasible to pass on marginal changes in cost. There isn't clarity yet on how to make these decisions compliant but some believe the Government will take a lenient view for now. In the meantime, the consensus seems to be that businesses will avoid price hikes for at least six months.

A second challenge is in the domain of supplier relations. Input tax credit can only be accounted for when suppliers comply and upload their tax returns properly. If suppliers don't file returns, customers cannot get the benefit. In some ways, the Government has outsourced tax compliance. There have also been complaints that dealers have refused to carry stock to avoid transition-related losses. To address this some companies are providing guarantees for compensation. Then there are misgivings about grandfathering clauses with respect to tax exemptions. States such as Uttarakhand, Himachal Pradesh and those in the North East have provided fiscal sops to industry and no one knows if these would now be honoured. It is believed that the central Government will cough up its 58 per cent share but state Governments, with their stretched balance sheets, are perhaps unlikely to follow.

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The Government intends to set up an authority to offer advance rulings to provide greater certainty. Although this is yet to happen, it is a game changer if the administration can create a well-staffed, fair and efficient institution. Such a mechanism could go a long way in smoothening the transition and assuring tax payers that they would not be unduly harassed later. ■

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