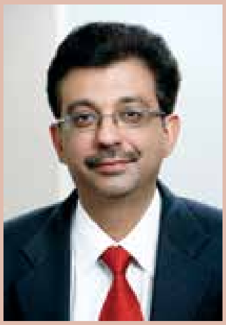
GST: A Game Changer



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After more than a decade of tribulations and travails, the GST – independent India's most awaited tax reform – has finally gone live. The scale of this transformation is enormous, and touches practically every citizen, directly or indirectly. It took stakeholders time and effort to gear up for the transition. While the overall structure of the legislation might not be ideal, credit must be given to the GST Council and other government officials who have invested significant efforts in framing the law, rules and regulations. Substantive thinking and planning behind the scenes to reduce business disruption is quite evident.

Smooth transition

Defying expectations, the transition itself has been smooth, and the disruption reasonably limited. Most manufacturers shut down their businesses for only a few days in July to revalue their stocks and determine tax credits that could be carried over to the new regime. Registration migration also took place in a systematic manner with few hiccups. Government officials have been agile in supporting the transition with proactive communication and engagement. Neutrality of the tax impact has been ensured, by and large. However, the transition is not over yet, and all the back-end transactional compliance and input-tax credit matching exercise would be the next big milestone in this journey. Some challenges would surely unfold as we continue to move forward.

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Looking below the surface

On the surface, GST replaces a bunch of Central and state level tax legislations and is intended to simplify tax compliance and administration. Its implications, however, run much deeper, impacting the business environment and the economy more broadly. In particular, it will significantly impact business models and strategy, making it a game-changer indeed.

Logistics and warehousing strategies will see major changes. In the pre-GST world, supply-chain design was based on the need for tax efficiencies. Most involved moving goods from manufacturing plants to multiple warehouses as stock transfers, before eventually being moved to end-markets. This resulted in the setting-up of a large number of smaller warehouses, and impacted logistics and transportation costs. Post GST, the supply chain architecture can be redesigned to optimise the number of warehouses required, reduce the number of shipments, and thereby achieve greater cost efficiencies.

Larger consignment sizes will change the transportation game, making it more viable for transporters to operate trucks and lorries with higher tonnage

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and container-carrying capacity. The elimination of check-posts has already reduced transportation time, in some cases by as much as 30 per cent, which further adds to supply-chain efficiencies. Eventually, this redesign will help manufacturers to plan and optimise their production, procurement and supply levels, resulting in inventory and working capital optimisation.

Input costs will rationalise and reduce with the elimination of the cascading tax effect. Also, input costs will no longer be pushed up by the non-availability of inter-state VAT set-off and the CST impact on inter-state purchases. Further, countervailing and additional import duties have been replaced by IGST, and importers can claim input set-offs, which earlier would add to cost for non-manufacturing businesses.

Procurement strategies can now be based on strategic, economy-of-scale calculations rather than on the need for proximity to suppliers arising from tax efficiencies. The consolidation of supplier bases will also become more meaningful, and help manufacturers improve their quality parameters on account of bigger production volumes. The reduction of input costs will eventually benefit consumers, with competitive forces ensuring fairer pricing.

The organised sector will benefit and the unorganised segment will be under pressure to align with the mainstream. Transactional inter-linkages between suppliers and recipients will force the entire ecosystem to report purchases and sales seamlessly to claim input-tax set-off benefits. Organised sellers will prefer to work with GST-registered suppliers, a push down the chain to get registered and ensure compliance. The recent surge in registrations – about 2 million within just a few days of GST's launch – is a clear indication that the taxpayer base is expanding. Once suppliers get registered with the GST network, their ability to evade tax will be checked. This will help level out the

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playing field in terms of pricing ability between compliant suppliers and the erstwhile non-compliant unorganised sector.

An expansion of the taxpayer base should result in higher tax revenues for the exchequer, gradually allowing a move towards fewer and lower bands of GST rates. Once the network captures purchase and sales transactions, the incentive to settle transactions in cash will reduce, thereby driving the move towards a 'less-cash' economy. The linkage of GST registration numbers with the income tax PAN will enable direct-tax authorities to validate the level of revenue and realistic profits declared in income tax returns. This will also boost direct-tax collections. Although ingenious people will keep looking for new ways and means to evade taxes, the disincentives will rise, and it will become increasingly difficult for individuals and businesses to avoid taxes.

Operating efficiencies will go up. In the erstwhile regime, an army of operating and commercial teams would be perpetually engaged in the maze of C, F, H, I forms, and a substantial amount of time was lost in collecting these forms and reconciling them at the time of assessment. The availability of input-tax credit for both goods and services means that the significant VAT and service tax 'burn' of the past will disappear, thus reducing costs and improving both profitability and business viability. More uniform business models will make the bidding and tendering process less tedious and more easily comparable on merit, and execution more operationally efficient. Input-tax credit set-off on capital goods will encourage businesses to enhance capacity, thereby supporting investment.

An emphasis on digitisation and automation will improve the transparency of commercial transactions between suppliers and customers. The accounts payable and receivable processes are likely to get automated, digitised and streamlined. Transactional confirmations will happen monthly, and the likelihood of future disputes will come down, reducing avoidable litigation. This will be a step-change from the current environment, where there are often lags in communication between suppliers and customers in terms of the acceptance and confirmation of business transactions. Since payments to suppliers need to be made within 180 days of the invoice date for input-tax credits to be valid, the discipline of releasing payments against supplies will improve, helping the working capital cycle become more efficient.

Transaction velocity should also go up once the GST systems settle down. This will, over time, enable scale and business volumes to increase across sectors, and positively impact employment generation.

In conclusion

The transition has just started, and it will take time before the dust settles. The challenges will be humongous, and business paradigms will be challenged. However, in a country of India's scale and size, it is indeed commendable that a transformation of this magnitude has been attempted. This indicates both resilience and the ability to embrace change. For India, the next few years will be very exciting, offering opportunities for growth across sectors. GST will certainly act as a catalyst to propel the economy along this trajectory. ■