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GST AND INDIAN FEDERALISM

Dr. Ashok Gaur
Assistant Professor,
B.J.Vanijya Mahavidyalaya, Vallabh Vidyanagar
Vallabh Vidyanagar

Abstract

Many economy of world have Federal systems in which there is a sharing of powers, including the power to tax, between a central government and lower-tier, provincial or state governments. The taxation system in the Republic of India is quite well structured. The Department of Revenue of the Finance Ministry of the Government of India is responsible for the computation; levy as well as collection of most the taxes in the country. However, some of the taxes are even levied solely by the Local State Bodies or the respective governments of the different states in the nation. – After the introduction of GST, indirect taxation system of India will be subsumed under GST because a line of different taxes will be covered in a single tax law which is GST (Goods and Service Tax). Before GST the main indirect taxation which is generally used are VAT, Service Tax, and Excise etc. For the successful operation of the federal form of government financial independence and adequacy is essential. For successful implementation of GST, all the confusion and grievances on GST must clear. This paper is about impact of GST on Indian Federalism system

Keywords : *Indian taxation system, Indian Federalism, Direct and Indirect Goods and Serves Tax*

Introduction

Introduction of GST would be a important step in the field of indirect tax reforms in India. By amalgamating a large number of Central and State taxes into a single tax and allowing set-off of prior-stage taxes, it would mitigate the ill effects of cascading and pave the way for a common national market. The consumer will be benefited in form reduction in the overall tax burden on goods, which is currently estimated at 25%-30%. Introduction of GST would also make our products competitive in the domestic and international markets. Studies show that this would instantly spur economic growth. There may also be revenue gain for the Centre and the States due to widening of tax base, increase in trade volumes and improved tax compliance. This will also help policy maker and administrator because of transparency and use if ITC in taxation. India is Federal nation and the main souse of revenue of government is Tax and Non tax revenue which is collected by both sate and central government according to Article 246 of the Indian Constitution which distributes legislative powers including taxation, between the Parliament of India and the State Legislature. Schedule VII enumerates these subject matters with the use of three lists: List - I entailing the areas on which only the parliament is competent to make laws, List - II entailing the areas on which only the state legislature can make laws, and List - III listing the areas on which both the Parliament and the State Legislature can make laws upon concurrently .Separate heads of taxation are no head of taxation in the Concurrent List (Union and the States have no concurrent power of taxation. Implementation of GST taxation policy between central states is going affect Indian federalism

The Federalism Dilemma

The spirit of cooperative federalism requires both the Union and the State governments to sacrifice their fiscal autonomy in favor of a collective decision-making process. The giving up of the fiscal autonomy is unprecedented and reflects that the modern economy of today calls for increasing cooperation among the economic players for the common good, instead of focusing on individual gains. The current taxation system in India provides truncated taxation powers to the central government (the Centre) and the States and is not in tune with the modern businesses and the complex supply chains. The patchwork of taxes has led to balkanization of the common market and fragmentation of the supply chains. The differential taxes in different States give rise to arbitrage opportunities. Taxes such as central sales tax (an origin-based tax) and entry tax being non-creditable further add to the costs of businesses. While the States will get the power to tax both goods and services, the Centre will be able to levy taxes beyond the manufacturing point, across the full supply chain. At the same time, the tax provisions that restricted inter-State movement of goods within the country will now be dispensed with. These provisions are absolutely fundamental to modernizing the tax system and making it simple and efficient. GST will be supply chain neutral and will obviate the need for bundling or unbundling of goods and services for taxation purposes.

Indian Taxation federalism

Indian constitution has divided the taxing powers as well as the spending powers (and responsibilities) between the Union and the state governments. The subjects on which Union or State or both can levy taxes are defined in the 7th schedule of the constitution. Further, limited financial powers have been given to the local governments also as per 73rd and 74th amendments of the constitution and enshrined in Part IX and IX-A of the constitution. The Union government is responsible for issues that usually concern the country as a whole, for example national defense, foreign policy, railways, national highways, shipping, airways, post and telegraphs, foreign trade and banking. The state governments are responsible for other items including, law and order, agriculture, fisheries, water supply and irrigation, and public health. Some items for which responsibility vests in both the Centre and the states include forests, economic and social planning, education, trade union~ and industrial disputes, price control and electricity. Then, there is devolution of some powers to local governments at the city, town and village levels. The taxing powers of the central government encompass taxes on income (except agricultural income), excise on goods produced (other than alcohol), customs duties, and inter-state sale of goods. The state governments are vested with the power to tax agricultural income, land and buildings, sale of goods (other than inter-state), and excise on alcohol. Local authorities such as Panchayat and Municipality also have power to levy some minor taxes. The authority to levy a tax is comes from the Constitution which allocates the power to levy various taxes between the Centre and the State. An important restriction on this power is Article 265 of the Constitution which states that "No tax shall be levied or collected except by the authority of law." This means that no tax can be levied if it is not backed by a legislation passed by either Parliament or the State Legislature.

Sources of Revenue of Central and State government as per Federalism

The sources of Revenue of the Union Government: Income (except tax on agricultural income), Corporation Tax & Service Tax Currency, Coinage, legal tender, Foreign Exchange Custom duties (except export duties) Excise on tobacco and other goods. Estate Duty (except on agricultural goods) (Kindly note that its mentioned in the constitution but Estate duty was abolished in India in 1985 by Rajiv Gandhi Government) Fees related to any matter in Union list except Court Fee Foreign Loans Lotteries by Union as well as State Governments. Post Office Savings bank, Posts, Telegraphs, Telephones, Wireless Broadcasting, other forms of communication Property of the Union Public Debt of the Union Railways Stamp duty on negotiable instruments such as Bills of Exchange, Cheques, Promissory notes etc. Reserve Bank of India Capital gains taxes, Taxes on capital value of assets except farm land Taxes other than stamp duties on transactions in stock exchanges and future markets Taxes on the sale and purchase of newspapers and advertisements published therein. Terminal Taxes on Goods and passengers, carried by Railways and sea or air. Sources of revenue for State Governments

Sources of revenue for State Governments: Taxes and duties related to agricultural lands Capitation Taxes Excise on liquors, opium etc. Fees on matters related to state list except court fee Land Revenue, Land and buildings related taxes Rates of Stamp duties in respect of documents other than those specified in the Union List Taxes on mineral rights subject to limitations imposed by the parliament related to mineral development Taxes on the consumption or sale of electricity Sales tax on goods (other than newspapers) for consumption and use within state. Taxes on advertisements except newspaper ads. Taxes on goods and passengers carried by road or on inland waterways Taxes on vehicles, animals and boats, professions, trades, callings, employments, luxuries, including the taxes on entertainments, amusements, betting and gambling. Toll Taxes.

Certain Taxes levied as Concurrent Powers Please note that the Union and the State Governments have the concurrent powers to fix the principles on which taxes on motor vehicles shall be levied and to impose stamp duties on non-judicial stamps. The property of the Union is exempted from State Taxation; and the property of the states is exempted from the Union Taxation. But the parliament of India can pass legislation for taxation by Union Government of any business activities / trade of the state which are not the ordinary functions of the state. Residuary Power of Taxation Union Government has exclusive powers to impose taxes which are not specifically mentioned in the state or concurrent lists. Some taxes imposed using these powers include Gift tax, wealth tax and expenditure tax.

The sales tax on consumer goods such as toothpastes, soaps, daily use items, electronic items etc. are imposed, collected and appropriated by state governments. However, newspapers and newspaper ads are exception to this. Further, there are four restrictions to this power of the state. These include: A state cannot impose sales tax if a good is produced there but is sold outside the state. A state cannot impose sales tax if the sale and purchase is taking place for items due for export. A state cannot impose tax on interstate trade and commerce of goods. State cannot impose a tax on a good that has been declared of special importance by parliament. Other facts about levying and appropriation of Taxes Sales tax is imposed, levied, collected, appropriated by states as mentioned above Income tax, Corporation Tax, Service tax are levied and collected by Centre but are appropriated by both states and centers as per distribution formula recommended by Finance Commission. This formula is no binding upon the parliament. However states have no share in surcharges, cesses on these taxes. Stamp duties on negotiable instruments and excise duties on medicinal and toilet preparations that have use of alcohol and narcotics are levied by Centre. But these taxes don't make a part of consolidated fund of India. They are assigned to respective states only, which appropriate these taxes. Sales tax in case of Inter-state trade of goods (except newspapers) is levied and collected by the centre but such proceeds are assigned to states. (This is known as Central Sales Tax)

Salient Features of GST

The salient features of GST are as under:

1. The GST would be applicable on the supply of goods or services as against the present concept of tax on the manufacture and sale of goods or provision of services. It would be a destination based consumption tax.
2. It would be a dual GST with the Centre and States simultaneously levying it on a common tax base. The GST to be levied by the Centre on intra-State supply of goods and / or services would be called Central GST (CGST) and that to be levied by the States would be called State GST (SGST).
3. The GST would apply to all goods other than alcoholic liquor for human consumption and five petroleum products, viz. petroleum crude, motor spirit (petrol), high speed diesel, natural gas and aviation turbine fuel. It would apply to all services barring a few to be specified.
4. Tobacco and tobacco products would be subject to GST. In addition, the Centre could levy Central Excise duty on these products.
5. The GST would replace the following taxes currently levied and collected by the Centre:
   a) Central Excise duty
   b) Duties of Excise (Medicinal and Toilet Preparations)
   c) Additional Duties of Excise (Goods of Special Importance)
   d) Additional Duties of Excise (Textiles and Textile Products)
   e) Additional Duties of Customs (commonly known as CVD)
   f) Special Additional Duty of Customs (SAD)
   g) Service Tax
6. State taxes that would be subsumed under the GST are:
   a) State VAT
   b) Central Sales Tax
   c) Luxury Tax
   d) Entry Tax in lieu of octroi
   e) Entertainment Tax (not levied by the local bodies)
   f) Taxes on advertisements
   g) Purchase Tax
   h) Taxes on lotteries, betting and gambling
   i) State cesses and surcharges insofar as they relate to supply of goods and services
7. An Integrated GST (IGST) would be levied and collected by the Centre on inter-State supply of goods and services. Accounts would be settled periodically between the Centre and the States to ensure that the SGST portion of IGST is transferred to the destination State where the goods or services are eventually consumed.
8. Tax payers shall be allowed to take credit of taxes paid on inputs (input tax credit) and utilize the same for payment of output tax.However, no input tax credit on account of CGST shall be utilized towards payment of SGST and vice versa. The credit of IGST would be permitted to be utilized for payment of IGST, CGST and SGST in that order.
9. HSN (Harmonised System of Nomenclature) code shall be used for classifying the goods under the GST regime. Taxpayers whose turnover is above Rs. 1.5 croresbut below Rs. 5 crores shall use 2 digit code and the taxpayers whose turnover isRs. 5 croresand above shall use 4 digit code.
10. Exports shall be treated as zero-rated supply. No tax is payable on export goods but credit of the input tax related to the supply shall be admissible to exporters.
11. Import of goods and services would be treated as inter-State supplies and would be subject to IGST in addition to the applicable customs duties.

12. The laws, regulations and procedures for levy and collection of CGST and SGST would be harmonized to the extent possible.

GST and Centre-State Financial Relations

Currently, the fiscal powers between the Centre and the States are clearly demarcated in the Constitution with almost no overlap between the respective domains. The Centre has the powers to levy tax on the manufacture of goods (except alcoholic liquor for human consumption, opium, narcotics etc.) while the States have the powers to levy tax on the sale of goods. In the case of inter-State sales, the Centre has the power to levy a tax (the Central Sales Tax) but, the tax is collected and retained entirely by the States. As for services, it is the Centre alone that is empowered to levy service tax.

Introduction of the GST would require amendments in the Constitution so as to simultaneously empower the Centre and the States to levy and collect this tax. The assignment of simultaneous jurisdiction to the Centre and the States for the levy of GST would require a unique institutional mechanism that would ensure that decisions about the structure, design and operation of GST are taken jointly by the two. For it to be effective, such a mechanism also needs to have Constitutional force.

Amendment of the Constitution and Other Legislative Requirements

(a) Constitution (One Hundred and Twenty Second) Amendment Bill, 2014

To address all these and other issues, a Constitution Amendment Bill was introduced in the Lok Sabha and the Bill (122nd Amendment Bill) has since been passed by the Lok Sabha (May, 2015). The Bill is currently under consideration of the Rajya Sabha. The salient features of the Bill are as under:

1. The GST shall be levied on all goods and services except alcoholic liquor for human consumption.
2. The tax shall be levied as dual GST separately by the Union and the States.
3. Parliament will have power to make laws with respect to GST imposed by the Union (CGST) and the State Legislatures will have power to make laws with respect to GST imposed by the States (SGST).
4. Parliament will have exclusive power to make laws with respect to GST where the supply of goods and/or services takes place in the course of inter-State trade or commerce (IGST).
5. The Government of India (GoI) will have exclusive power to levy and collect GST on inter-State trade or commerce. This tax shall be apportioned between the Union and States on the recommendations of the GST Council by Parliament by law.
6. Petroleum& petroleum products would be subject to GST. [However, it has been decided that these products would be kept out of the purview of GST in the initial years of implementation]. In the case of tobacco and tobacco products, the Centre alone would have the power to levy excise duty in addition to the GST.
7. Taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council shall not be subsumed under GST.
8. Parliament may, by law, provide for compensation to States for revenue loss arising out of the implementation of the GST, based on the recommendations of the GST Council. Such compensation would be for a period of 5 years.
9. A GST Council would be constituted comprising the Union Finance Minister (who will be the Chairman of the Council), the Minister of State (Revenue) and the State Finance/Taxation Ministers to recommend on

a) The taxes, cesses and surcharges to be subsumed under GST;
b) the goods and services that may be subjected to or exempted from the GST;
c) the date from which the specified petroleum products would be subject to GST;
d) model GST laws, principles of levy, apportionment of IGST and the principles that govern the place of supply;
e) the threshold limit of turnover below which the goods and services may be exempted from GST;
f) the rates including floor rates with bands of GST;
g) any special rate or rates for a specified period to raise additional resources during any natural calamity or disaster; and
h) special provision with respect to the North-East States, J&K, Himachal Pradesh and Uttarkhand.

The mechanism of GST Council would ensure some degree of harmonization on different aspects of GST between the Centre and the States as well as among States. It is being specifically provided that the GST Council, in its discharge of various functions, shall be guided by the need for a harmonized structure of GST and for the development of a harmonized national market for goods and services.The GST Council may decide about the modalities to resolve disputes arising out of its recommendation. The Constitution Amendment Bill is expected to be passed by the RajyaSabha in the ensuing monsoonsession of Parliament. After ratification of the amendment bill by 50% of State legislatures and receipt of assent by the President, the process of enactment would be complete.

(b) Other Legislative Requirements

Suitable legislation for the levy of GST (Central GST Bill, Integrated GST Bill and State GST Bills) drawing powers from the Constitution can be introduced in Parliament or the State Legislatures only after the enactment of the Constitution Amendment Bill. Unlike the Constitutional Amendment which requires 2/3rd majority, the GST Bills would need to be passed by a simple majority. Obviously, the levy of the tax can commence only after the GST law has been enacted by the respective legislatures. Also, unlike the State VAT, the date of commencement of this levy would need to be synchronized across the Centre and the States. This is because the IGST model cannot function effectively unless the Centre and all the States participate simultaneously.

Conclusion

Actually there is not technical difference between VAT and GST. In European countries it is known as VAT and in other countries as GST. The basic objective of either of them is to avoid cascading of taxes, input credit being available and a single tax being administered by the federal government for goods and services as a single tax. In India even though we have VAT it is not full fledged as it is as at state level and still there is cascading of taxes. Central GST and a state GST-with the states free to have different rates for the state GST so that we can preserve the autonomy of states and enhance healthy inter-state fiscal competition – a race to the top. and not to the bottom. This proposal only needs an appropriate Information Technology (IT) infrastructure for inter-state tax credits (ITC). Nandan Nilekani of the "Aadhar" program (Unique ID authority) is helping prepare such an infrastructure for the non-varying GST proposal in any case. For example, the European Union has achieved a single, efficient market while still having different value-added tax (VAT) rates for its member states using the VAT Information Exchange System

The proposed GST is supposed to address the same but with a caveat that it will not be federal administered tax but dual mechanism due to our constitutional mechanism of tax being levied both by state and center. The essence of federal form of government is that the Centre and the State Governments should be independent of each other in their respective, constitutionally demarcated spheres of Action. For the successful operation of the federal form of government financial independence is needed. dealing with fiscal imbalances between the center and states, as well as among the states.

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