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GOODS AND SERVICES TAX

'Robust IT set up, info dissemination key to successful implementation'

GST is likely to strengthen cooperative federalism and have far-reaching implications for growth, inflation, public finances, says the RBI report

ENS ECONOMIC BUREAU
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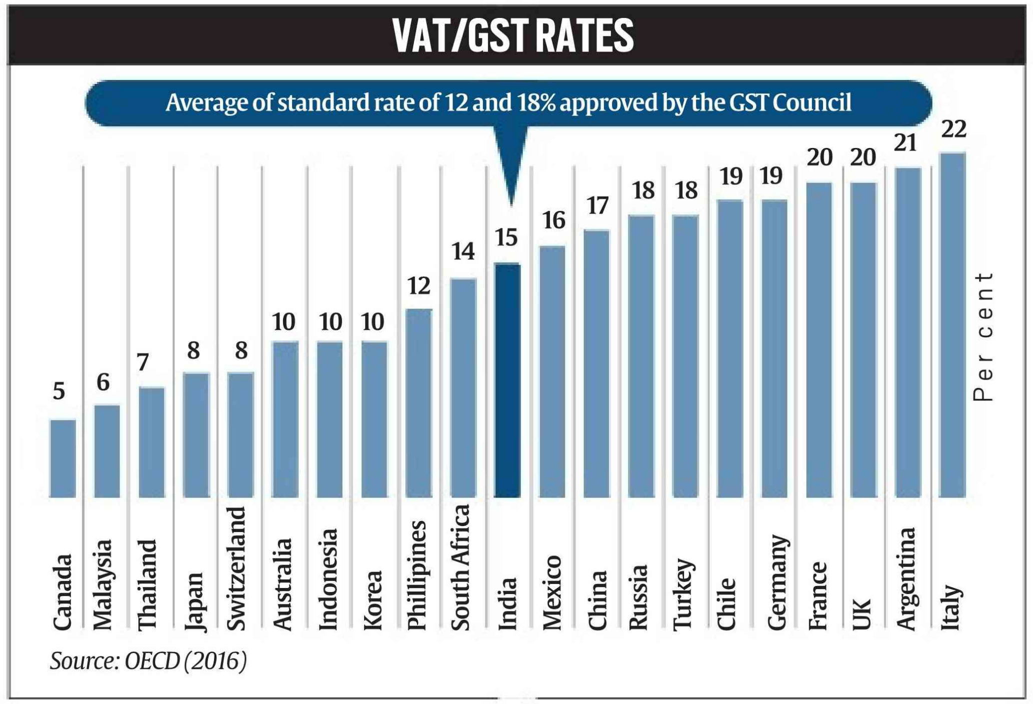
AS INDIA prepares to roll out Goods and Services Tax in July 2017, a report released by RBI 'State Finances: A Study of Budgets' has said that while there are several merits of implementing the proposed indirect tax regime, it isn't completely devoid of risks related to tax evasion and avoidance.

The report pointed out that the international experience of GST implementation shows that tax authorities and government may need to be careful about issues around tax evasion such as small businesses not registering; under-reporting of actual sales by traders; traders reducing their liability by exaggerating the proportion in the lower tax slabs; traders collecting tax but not remitting to the government; and traders making false claims for refunds.

The report prepared by the Fiscal Analysis Division of the Department of Economic and Policy Research (DEPR) at RBI, however, also highlighted several merits of GST implementation. While on the one hand, it is likely to strengthen cooperative federalism and have far-reaching implications for growth, inflation, public finances and external competitiveness in the Indian economy, it is may also bolster states' revenue and anchor fiscal consolidation without compromising on expenditure quality.

The report said that while India has proposed an initial rate of 15 per cent (average of standard rates – 12 and 18 per cent approved by GST Council), the average VAT/GST rate in major OECD countries is higher than the rate proposed for India and those prevailing among other emerging market economies (EMEs) in 2016. It also stated that India's plan to have central GST (CGST) and state GST (SGST) has some resemblance to the structure of the system existing in the Canadian province of Quebec where independent federal (GST) and provincial (QST) VATs are operative simultaneously.



The RBI report suggested that a robust and fail-proof information technology (IT) framework is an essential prerequisite for the success of the GST, given the large volume of transactions involved.

It is also important to sensitise the industry and public through information dissemination such as release of legislative documents and conducting outreach programmes/media interactions with the tax authorities. The tax laws need to be simplified to avoid definitional issues and defray administrative costs, the report added.

Referring to lessons from implementation of GST from other countries, it said that a well-designed goods and services tax should ensure that, "A single rate is levied on a comprehensive base (goods and services); no exemptions are given beyond standard ones; GST refunds are processed expeditiously; an adequate threshold is delineated to exclude small and micro business; and initial rates are suitably calibrated to avoid disruptions to economic activity and macroeconomic stability."

It has been a matter of debate for couple of years now as to what kind of impact GST may have on the average growth, the report states that the average growth in some advanced economies increased by about 0.7 percentage point following fiscal (including tax) reforms. "As it promotes competitiveness, efficiency gains from GST is considered to be higher vis-a-vis other taxes, the benefits of which accrues to growth over the medium-term," said the report.

Even from a fiscal perspective the international evidence suggests that implementation of VAT/ GST have resulted in a higher government revenue-GDP ratio over time. "An earlier study concluded that the tax-GDP ratio increased significantly after VAT implementation in twelve European countries (Aaron, 1981). Moreover, OECD data on member countries from Europe suggest an increase of 37 per cent in the VAT revenues-GDP ratio between 1975 and 2006 (OECD, 2008)," it said.