Indirect Taxes : A Balance of Resources and Expenditure

Dr. Aarti Mundan
Ambala Road, Near Gurudwara, Town & PO Sarsawa, Saharanpur (UP)

Abstract

India has federal system of Government and the division of taxes among the Centre and State Governments is very complex. Though, the Indian constitution creates a dual polity based on divided Governmental powers and functions, this division is not watertight compartment. Exact correspondence between resources and functions at different levels of the Government is not possible to secure in any federal system. The emergence of imbalances between functional responsibilities and financial resources is a characteristic feature of all federations. GST is also an information Technology driven tax mechanism. It clearly, shows a upward change in government revenue. It is further expected to have a charge on unlawful tax-aviodance. GST will benefit both governments as well as the consumers. Further, after the implementation of GST, the business will have to get GST ready software's. Hence, it is clear here that just registration is not enough for entire business management, government is planning a portal for easy excess monitoring. Here, it is notable that the increase in revenue which is being expected by the Government is not targeted from consumer's pocket but from the tax-aviodance. The present paper gives a comparison and benefits between previous VAT and present GST.

Keywords : *Indirect Taxes, VAT, GST, Tax-Avoidance.*
JEL Classification : *H 21, H 22, H 26, H 27.*

1. INTRODUCTION

Taxes are the most important source of public revenue. In modern time, with the increase in various activities of the Government like welfare, administrative, development etc, the need of revenue has been constantly increasing. The Government tries to generate as much revenue as possible from different sources, however taxes both direct and indirect remain the most important source. Despite many limitations, the Government has widen its tax structure, both at the Centre and the State Government levels.

India has federal system of Government and the division of taxes among the Centre and State Governments is very complex. Though, the Indian constitution creates a dual polity based on divided Governmental powers and functions, this division is not watertight compartment. Exact correspondence between resources and functions at different levels of the Government is not possible to secure in any federal system.

Access This Research Paper Online
Paper Code : JCT-O17-AM-4
http://jctindia.org/october2017/v12i2-4.pdf
https://ideas.repec.org/a/jct/journl/v12y2017i2p27-33.html
http://EconPapers.repec.org/RePEc:jct:journl:v:12:y:2017:i:2:p:27-33
How to Cite This Research Paper
Mundan, Aarti. Indirect Taxes : A Balance of Resources and Expenditure. Journal of Commerce and Trade October 2017; 12 : 2; Pp. 27–33.

The emergence of imbalances between functional responsibilities and financial resources is a characteristic feature of all federations. The mismatch between functions and taxation powers occurs partly because of changing responsibilities of different Government and partly because of the dominant position of the national Government regarding taxation powers, which is often by design. Therefore, a kind of vertical imbalance of resources and expenditure responsibilities emerges between different levels of Government calling for transfer of resources from the centre to the states.

2. FINANCIAL RESOURCES

Recognising the fact that the financial resources of the states may prove inadequate for undertaking welfare, maintenance, and development activities, the framers of India's constitution did make elaborate, complex, arrangements relating to flow of funds from the Centre to the States. The disequilibrium between the proliferating functional responsibilities of the states and their own resources is corrected by Central affected through three main channels:

a. Statutory transfers through the Finance Commission.

b. Plan transfers through the Planning Commission, and

c. Discretionary transfers by Central Ministries for various purpose.

Although, taxation powers allocated to the Centre and the States are mutually exclusive yet, all the taxes and duties levied by the Centre are not meant entirely for the purpose of the Centre. In fact, revenues form certain taxes and duties leviable by the Centre are totally assigned to are shared with the States to supplement the revenues of the States in accordance with their needs. Excise duties are levied and collected by the Centre but their proceeds are shared permissively with the States. Articles 268 and 269 of the Constitution mention items of taxes and duties of proceeds of which are wholly assignable to the States. The Constitution provides for Central transfers, it neither indicates the share of the States in the divisible taxes nor prescribes any principles for the distribution of States share among the States themselves. The precise manner of sharing taxes is left to the deliberations of the Finance Commission which is appointed by the president every eqinquennium or earlier if necessary. The Finance Commission, consisting of a chairman and four members, recommends to the president, interalia, the principles of distribution between the Union and the States of proceeds of taxes which are to be, or may be divided between them and the allocation among States of the respective share of such proceeds. The president is required to place the recommendations of the Finance Commission, together with a statement of action taken thereon, before both the Houses of Parliament. The President is not bound the accept the recommendations of the Finance Commission, but they are generally accepted in view of the quasi-judicial nature of the Commission. By and large, Finance Commissions have worked independently and some of them, particularly the recent ones, have been quite assertive. The award of Finance Commission generates considerable interest in issues pertaining to the financial relations between the Centre and the States. Ten Finance Commissions have reported since the commencement of the Constitution.

3. THE TAX GDP

Level of taxation in a country is traditionally judged in terms of the ration which taxes bear to some measure of national income aggregate. Change in the ration is determined by variations in both the numerator and the denominator. Tax GDP ration is generally regarded as an index or relative tax burden in a country over a period of time of when countries are compared for the same period. However to describe tax burden in terms of tax, GDP ration can be misleading because taxes, though burden for individuals, are used to finance vital governmental activities and to make transfers to needy sections of society. Tax GDP ratio indicates the percentage of national income that is compulsorily transferred from private pockets to the public exchequer. It signifies the relative share of the Government in the disposition of national income. The GDP ratio is determined by such factors as the level of per capita income, composition of national income, size of the foreign trade sector, and the degree of monetisation in the economy.

In 1950-51, total tax collections in India were a mere 6.7 percent of GDP with the launching of the Five Year Plans in 1951, expansion in administrative and welfare activities for the Government at different levels, the need for revenue increased and it was met mainly by additional tax efforts. Consequently, tax GDP ratio started increasing from decade to decade, being 8.3 percent in 1960-61, 11.0 percent in 1971-71, 14.6 percent in 1980-81 and 16.6 percent in 1990-91. It declined to 15.8 percent in 1995-96 and again rise slighting to 17-18 percent in 2000-01 and declined 9.4 per cent in 2009-10. In 2015-16 it further increased to 16.6 percent. By and large, tax policy has fared reasonably well as an instrument of resource mobilisation.

4. VAT

The various weakness of sales tax despite it being the most important state tax, make it imperative at certain reforms are introduced in structure. In keeping with the present trend of globalization, the introduction of VAT in India is important because VAT will remove the disadvantages of sales tax to a large extent.

Theoretically, Value Added Tax (VAT), as prevalent in most West European countries, is the desirable method to combat adverse effects of input taxation. In its ideal form, VAT is a multi-stage tax levied on all stages of production of a commodity. It is collected installment on the basis of value added at each stage of production and distribution. Since an inputs is taxed only once, VAT avoids the cascading effect which is the chief demerit of a generalized system of excise or sales taxation. Value added tax discourages vertical integration of industries to the advantage of small-scale sector. Since the cumulative effect or input taxation is absent under the VAT, the impact of this tax on cost of production is limited to the amount of tax itself. By not allowing unnecessary cost escalation, VAT promotes competitiveness among domestic industries in the world market and thus generates favorable effects on exports.

The single point VAT at the central level deals with the cascading effects of both excise duties and sales tax. Since, sales tax is the most important source to tax revenue for the states, such a drastic suggestion, which will have left the states at the mercy of the centre, is difficult to implement. Replacement of existing system of excises, sales taxation and octroi by comprehensive VAT would require amendment of the Constitution by a two-thirds majority in Parliament and it's approval by more than half of the states, A comprehensive VAT at the national level has to be ruled out on economic as well as political considerations. Switch over to VAT has to be an independent excise by the Central Government and 28 State Government. In this connection, the Tax Reforms Committee, 1991, observed, "As regards sales tax, the Committee is of the view that this tax could be converted into a form of State VAT within the manufacturing sector. There may be no need for levying sales tax at more than two rates since the distributional and other non-revenue objectives could be left to be performed by the central taxes which apply uniformly throughout the country. Even this dual VAT system is difficult to achieve because it is highly unlikely that the 28 states will move in tandem to ensure smooth transition to a uniform system of VAT in place of their differing practices of sales tax. Thus, the problem of coordination is not only between the centre and the states but also among the states themselves."

The introduction and extension of

MODVAT scheme at the central level would step in the right direction to reform excise taxation. Unfortunately, similar reforms have not been introduced at the level of states. The State Finance Ministers' Conference held in New Delhi on May 27, 1994 failed to arrive at a consensus on the replacement of indirect tax at the state level by a value added tax. The matters to go into this and related question. MODVAT scheme provides for instant and complete reimbursement of excise duty and additional duty of customs (countervailing duty) paid on the components and raw material when used in the manufacture of the final products. Articles which are not used as inputs in the manufacturing process are not eligible for credit under this scheme. The Government had made it clear in its Long Term Fiscal Policy that the introduction of MODVAT which considerably reduced the cost of final products, the rates of duty of final products were suitable revised upwards by the Finance Act, 1986, to retain the collection of excise duties at the earlier level. This was justified on grounds or resource mobilisation for the plans.

5. GST

At the moment, we have GST. It is a common and simplified tax system. While previously, VAT and Service tax which were taken separately as VAT was for goods and Service Tax was clearly for what was mentioned.

The previous tax system gave rise to a high tax rate as it had several indirect taxes and that increased the tax rate respectively along with every state having their own tax rate which increased the amount of tax rate as the goods were being transported from state to state which is no longer be a problem since GST is implemented. It will have no separate tax based on good or services and state borders which will make it easier and less expensive for importers and exporters.

VAT used to be calculated on the value of sales of good or services which but with the tax rate that is already levied on the goods. But it changed to only paying tax on value addition and separately for the service. With GST coming into the picture the tax will be collected together without separate tax for goods and services.

In India, GST has replaced almost all the indirect taxes and bring a common market for easy tax structure and simple tax payment. The cost of tax on all the commodities will lower as the result of GST implementation. The excise is removed, as the tax on tax, is one of the major reasons that the rate of tax goes up once it is traded. But with GST this becomes several times less and easier.

The business that have an income lower than 20 lakhs requires no registration in GST and also it will remove several taxes that the payers pay without realizing as it is a tax on tax and GST also provide a clear view of what tax you are paying.

To learn the difference between the previous taxation and the new GST Regime in India one will have to know exactly what is GST tax. GST is basically a tax policy that will bring uniform market all around the country. This system will reduce the complicated structure of taxation as it will create a common market. This will also reduce the burden of a tax payer as it will reduce the indirect tax and will also reduce the import and export taxes.

6. BENEFITS OF GST

The benefits that GST implementation provides

Business to Industry:

a) Taxation will be available on real time web like registration, returns, payments, etc. GST is not complex for tax payers and provides enhanced transparency to all tax related activities.

b) GST removes differences and anomalies in the tax-structure and brings on the concept of common market.

c) GST has removed all hidden and hard cost of doing businesses. It made the requirement easy for doing business.

d) Transparency and commonness in tax-net will automatically bring fair competition in business, hence, the reduction in price.

e) The central, state and indirect taxes are now replaced by one GST making it all simplified to manage and to pay.

f) GST supports better tax compilation with the real-time transfer of input tax credit from one stage to another where of value addition is made.

g) No doubt, GST may bring burden on the pocket of consumer. But, there will be more clear view of tax-payment, reduced confusion and more effective tax-input to government.

h) In the long run, the fair policies of tax-system will bring the price reduction which will result in check on leakages and decreased burden of tax.

7. TYPES OF TAXES

The taxes that are being charged by central and state are:

Central

- ❖ Central excise duty
- ❖ Service tax
- ❖ Additional excise duty
- ❖ Additional custom duty
- ❖ Special additional duty of customs

State

- ❖ Taxes levied by local bodies known as entertainment tax
- ❖ Central sales tax
- ❖ State value added tax or sales tax
- ❖ Entry tax and Octroi tax
- ❖ Purchase tax
- ❖ Luxury tax
- ❖ Taxes on lottery and betting and gambling

8. IMPACT OF GST TAX IN INDIA

GST will impact every sector of Indian Economy as well as Indian society. Some of the impacts may be short in life but same may have catalytic effect. But, it is dead sure that the economy as well as Indian Society will receive high impact of tax as the change in Tax-System is unexpected and sudden. Following are some sectors where in the impact will be high :

a) Automobiles : There is 18 percent tax slab for automobiles, it is expected that it will force decrease 10-17 percent fall in sale. Major hit area will be tractor market which was not expecting this much tax as it is a supporting automobile to Agriculture. And, agriculture is exempted from tax.

But, it will bring check on the factory to dealer unhealthy practices.

b) Textiles : Previously, the textile industry was experiencing a variety of tax. It also depended upon the size of business. Moreover, the type and quality of fibre being used also determines the tax-rate. Mill and Powerlooms were also used to be a category of tax-determination. But, now, GST has a common tax rate. It will decrease tax-confusion and complication which is expected to contribute to boost production and exports.

c) Engineering and Related Equipments : This sector was into extreme puzzle since there was high and varied tax rates. Somewhere on some points, tax was double. GST due to its commonness has broken down this complex structure in simplified tax-net. In this way, the reduction in complications will bring more business and export income.

d) Pharmaceuticals : This industry will definite be transformed. As new changes come daily in this sector. There are companies which were charging high price in the marketing and incidencing the tax in different manner.

e) **FMCG :** The FMCG market will also undergo a drastic change after GST. As, there will be more tax-scope and paper work. However, the cigarette and jewelry market will receive negative effect.

9. OVERALL IMPACT OF GST IN INDIA

According to the prediction, the economic growth at 2 per cent is expected to grow after GST implementation. The overall impact of GST in India will be as given below :

a) It will diversify the tax regime by expending the coverage on goods and services and will bring in transparency in tax-net.

b) It will bifurcate the indirect taxes between the center and the state level taxes.

c) It will make the manufacturing sector free from cascading effects of taxes and will improve the cost competitiveness of goods and services.

d) The prices of goods and services will go down thus increasing the tax GDP ratio.

e) Ease of Doing business in India will be more comfortable as the tax rules and structure has become much simpler.

f) There will be a dual control on the GST where state and central authorities will all the invoices will be captured online by GSTN.

g) Simplification in tax-maintenance will be experienced through CGST, SGST, IGST.

h) GST will benefit both economy and corporations as it will reduce heavy burdens on production cost and making exporters more competitive.

i) It will reduce corruption as it will build a transparent and corruption free tax administration. There will be less red tapism and beauracrtic system.

j) Suppliers, manufacturers, wholesalers, retailers will be able to recover GST incured more input costs as tax credits. This will reduce the cost of doing business, thus enabling fairer prices for consumers. Companies which are under organized sector will come under tax regime. More business entities will come under the tax system hence, widening the tax base. This will lead to more revenue collections.

k) The simplified and balanced division of GST will bring development to backward states.

l) It will remove the layered tax from some goods and hence the prices are likely to come down for such products.

10. CONCLUSION

GST is also an information Technology driven tax mechanism. It clearly, shows a upward change in government revenue. It is further expected to have a charge on unlawful tax-aviodance. GST will benefit both governments as well as the consumers. Further, after the implementation of GST, the business will have to get GST ready software's. Hence, it is clear here that just registration is not enough for entire business management, government is planning a portal for easy excess monitoring. Here, it is notable that the increase in revenue which is being expected by the Government is not targeted from consumer’s pocket but from the tax-aviodance.

REFERENCES

1. Murali, D. “Into the VAT of Unknown. Business Line 1 Apr. 2003: 4.
2. National Council of Applied Economic Research. Moving to Goods and Service Tax in India: Impact on India's Growth and International Trade. New Delhi: NCAER, 2009.
3. Nazarudeen, T. “Govt. will Consider Our.” Kerala Calling 26. 5 (2005): 26.
4. Nimbur, Basawaraj N. Introduction to Value Added Tax: Feasibility, Problems and Prospects. New Delhi: Criterion, 1984.
5. Padmanabhan, V. “Finances of State Governments and VAT Reforms.” Southern Economist. 48. 10 (2009): 5-7.
6. Pandey, I. M. Financial Management. 7 th Rev. ed. New Delhi: Vikas, 1995.
7. Patel, Chirag. “VAT Audit.” The Chartered Accountant Student. 12. 10 (2009): 15-18.
8. Pattabhi Ram, V., and S. D. Bala. Management Accounting and Financial Analysis. 2 nd ed. Mumbai: Snow White, 2007.
9. Paul, M. L., and Jenny Thekkekkara. “VAT in Kerala: Rationale, Features and Transitional Issues.” Kerala Calling 26. 5 (2005): 14-19.
10. Pillai, G. K. VAT: A Way Out of the Indian Tax Muddle. 3 rd ed. Mumbai: Jaico, 2003.
11. Prabhakara Menon, B. “A Transparent and Legitimate method of Tax collection.” Kerala Calling 26. 5 (2005): 27.
12. Navjot (2010), “Structure and Implementation of VAT in Punjab: an Evaluation”, A U.G.C. Research Project, Post-Graduate Department of Economics, Khalsa College, Amritsar.
13. Nour, Abdul Naser I.; and Pramanik, Alok Kumar (2005), “Value Added Tax: A Suggested Method”, in Pramanik, Alok Kumar (Ed.), Value Added Accounting and Reporting VAT, Kanishka Publishers, New Delhi.
14. Poddar, Satya; and Ehtisham, Ahmad (2009), “GST Reforms and Intergovernmental Considerations in India”, Working Paper No. 1/2009-DEA, Department of Economic Affairs, Ministry of Finance, Government of India.