Need for a GST Version 2.0

What is the issue?

- After four years, the promises of the Goods and Services Tax (GST) remain substantially unrealised.
- A GST version 2.0 may have to be designed soon given the flaws in the existing structure.

What is the overall outcome?

- The goal of avoidance of cascading of various taxes is not met.
- The tax system continues to be a not very transparent multi-rate system.
- There are also associated difficulties in computing and assessing tax liability, tax burden and tax incidence.
- States have less headroom in handling GST collection shortfall after surrendering their fiscal autonomy.

- The tax base of GST does not appear to be expanding as the recent uptick has reversed in July 2021.
- Revenue collection of the GST is dependent on the nominal growth rate of Gross Value Added (GVA) in the economy.
- The Tax to Gross value addition is only about 5% to 6.5% though GVA growth was much higher.
- This indicates that a very large segment is covered by exemption, composition schemes, evasion and lower tax rate.

What are the key challenges in the current GST structure?

- **Disputes** - The fundamental weakness of the GST is its political architecture as it is asymmetrically loaded in favour of the Centre.
- No particular body is tasked to adjudicate disputes, between States and between the Centre and the States, that are inevitable in a tax arrangement as the GST.
- This is despite the fact that the original Constitution (115th Amendment) Bill 2011 (GST Bill) had a provision for such an institution.

- **Compensation scheme** - GST Compensation Cess was introduced to compensate the losses of states for the first 5 years under the GST regime.
- Severe fiscal strain is expected when this 14% compensation comes to an endin 2022.
- The contraction of GST revenue across the country means that the compensation amount will be higher.
- So, the demand for a continuance of compensation scheme is inevitable.

What are the other issues to be resolved?

- **Design flaws**-Nearly 45% to 50% of commodity value is outside the purview of the GST, such as petrol and petroleum products.
- In addition, States which export or have inter-State transfers or mineral and fossil fuel extractions are not getting revenue as the origin States.

- They require a compensation mechanismto get this.
- Most trading and retail establishments, (however small) are out of the fold of the GST.
- At the retail level, irrespective of whether Input Tax Credit (ITC) is required or not, the burden can be passed on to the consumer.
- As a result, the loss could be as high as one third.
- **Exemptions** - Exemptions from registration and taxation of the GST have further eroded the GST tax base compared to the tax base of the pre-existing VAT.
- Exemptions are purely distortionary and directly increase evasion or misclassification, and reduce tax realisation.
- **Exclusion**- Petroleum products remaining outside the purview of GST has helped the Centre to increase cesses and decrease central excise.
- This would have otherwise been shareable with the States.
- In April 2017, cess and surcharge formed 56% and 35% of the excise duty on petrol and diesel, respectively.
- Now, their share has increased to 91% and 85%, respectively.
- But the shareable central excise (with the states) has reduced by ₹6.5 a litre together (both petrol and diesel).
- **GSTR** - Compliance with GST return (GSTR-1) filing stipulation and the resultant tax information is not up to date.
- Also, fraudulent claims of Input Tax Credit (ITC) because of a lack of timely reconciliation are quite high though it has come down by two thirds.
- Tax evasionis at least 5% in minor States and plus 3% in the major States.

What do these call for?

- Instead of the four rates/slabs, a single uniform tax rate for all commodities and services at all stages, inputs and outputs alike, would work better.
- Over all, policy gaps along with compliance gaps need to be addressed.
- Without proper tax information, infrastructure and base, the States would go in for selective tax enforcement.
- In the long run, voluntary compliance will suffer and equity in taxation will be violated.
- Given all these problems, a version 2.0 of GST may have to be designed sooner rather than later.

Source: The Hindu