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GST Impact on various sectors

Committee headed by the Chief Economic Adviser Dr. Arvind Subramanian, submitted its report on the possible Tax rates under GST on 4th December 2015. The summary of recommended options is provided in the table below

Table 1: GST Rates (%)

	Rate on precious metals	Low rate (goods)		Standard rate (goods & services)	High/Demerit rate (goods)
Preferred	15	6	12	16.9	40
		4		17.3	
		2		17.7	
Alternate	15.5	6	12	18.0	40
		4		18.4	
		2		18.9	

Source: Ministry of Finance

- The Committee's view is that the range should between 15% and 15.5% (centre and states combined) but with a preference for the lower end of that range based on the analysis in this report.
- The Committee recommends a two-rate structure. In order to ensure that the standard rate is kept close to the revenue neutral rate, the maximum possible tax base should be taxed at the standard rate. The Committee would recommend that lower rates be kept around 12% (centre plus states) with standard rates varying between 17% and 18%

Impact of GST

Sectors Covered

- Textiles
- Auto
- Auto-Dealerships
- Engineering, Capital Goods & Power Equipment
- Roads
- Pharmaceuticals
- Real Estate
- Hotels

Textiles – Positive

Presently, the textile industry has been divided into 9 broad categories for the purpose of taxation. These include cotton textile, woolen textile, silk textile, artificial silk, synthetic fibre textile, khadi and handlooms, jute, hemp and mesta textiles, carpet weaving, ready-made garments and miscellaneous textile products. The current taxes vary from 4% to 12% based on these categories. Further, textile sector is dominated by unorganized players who are given tax exemptions on the basis of size of their operations. All these factors result in a number of key concerns for the textile sector which include:

- Dispute over fabric versus garment classification: E.g. Sarees
- Differential taxation for cotton and manmade fibre: Zero duty for cotton fibre as compared to high excise duty structure of nearly 12.5% on manmade fibre segment
- Composite mills are taxed at a higher rate than the power looms discouraging integration of production

Also, the current taxation is production based leading to blocked input taxes which results in higher cost of production.

With the implementation of GST, there will be a uniform rate of tax which will result in:

- Blocked input taxes will be eliminated as GST is a consumption tax
- Zero rating on exports under GST will boost exports further without the need for explicit subsidy schemes
- Level-playing field will be provided to all textile segments Integration of production will be encouraged resulting in increased efficiency
- Goods movement within the states will also be much easier as lot of local state taxes which are levied on the borders of states which inhibit free movement of goods will be removed. This will help in improving the productivity & efficiency of the textile industry as now more factories/manufacturing units can be set up in various textile hubs across India without worrying for various state taxes which were earlier levied indirectly

Auto – Positive

GST is expected to result in a reduction in the cost of conducting business by removing the cascading effect of taxes especially for automotive distributors, which attracts high rates of CENVAT duties as well as VAT at State level, in addition to other levies such as National Calamity Contingent Duty (NCCD), Auto cess, entry taxes, octroi, registration charges and road taxes. Automobile exports are also likely to benefit, as embedded taxes in India's export prices will be eliminated.

Under the GST regime, with no embedded tax costs on inter-state movement of goods (CST or entry taxes) and a shift in the point of taxation to the consumer ultimately, businesses shall have greater flexibility to re-design their supply chains and thus, optimize logistics costs. Since their vendors are also likely to benefit from the transition, companies could negotiate with their vendors to pass on those benefits in terms of input prices.

However, there are various aspects which need to be resolved in order for the auto industry to be geared for the GST regime. Some prime issues being treatment of ongoing area based exemption schemes (from Central Excise perspective) and the State level incentives in form of subsidy or deferment, continuation of end use based exemptions (e.g. for vehicles used as taxis or ambulances) and the continuation of export incentives linked to indirect taxes.

Auto Dealers – Positive

At present the automobile OEMs transfer vehicles from their manufacturing units to their dealer network spread across the country through one of the following modes:

a) Direct transfer of vehicles to the dealer (dealer liable to pay CST)
b) Stock transfers to own warehouses in the consumption state and further transfer from the warehouse to the dealer (no CST applicable on the transfer of vehicle from the manufacturing unit to the warehouse, hence no input credit available to the OEM. Also dealer not liable to pay CST.)

In the first scenario, though the dealer pays CST, it cannot set-off the same against its VAT liability (VAT is payable by the dealer in both the above scenarios).

The GST will enable the auto dealers to get input tax credit for the GST paid by them at the time of acquiring the vehicles from the OEMs. Similar benefit will accrue to them on the spare part/service businesses.

Engineering, Capital Goods & Power Equipment – Positive

Introduction of GST is expected to improve the prospects of engineering, capital goods and power equipment (ECPE) sector by simplifying the tax structure.

The complexity in this sector is that companies are involved simultaneously in manufacturing of goods and rendering of services. For example a company engaged in manufacturing of transmission towers also does EPC of entire transmission lines which not only involve manufacturing of transmission towers but supply of bought out items and rending of services. The EPC players pay service tax at present while the manufacturers pay excise duty.

However, in general, a comprehensive tax like GST which would combine the state and central taxes in a single structure and where tax credit would be available at each stage of production and final sale so that double taxation could be avoided. This would bring in more cost competitiveness to the domestic players.

In this sector indirect tax range is much wider as compared to the other sectors where the product range is limited. Hence, depending upon the products manufactured by the company and services rendered, basket of goods provided in the EPC contract, it goes upto around 30% and any GST below this could improve the cost competitiveness of players in this sector.

Roads – Neutral

There are no major implications of GST on toll and annuity based road projects. Further, road construction sector is currently exempt from the preview of excise and service tax. However, EPC contractors are currently paying indirect taxes (mainly on key inputs and service tax to be paid to transporters) at average rate of 9-11% net of credit availed. The same is expected to continue under GST. However, processes are expected to be streamlined with implementation of single point tax system which can result in lower cost for the compliance. Moreover, extent of liberalization in credit available under GST against various input used for the civil construction is crucial for the EPC contractors.

Pharmaceuticals – Positive

The biggest advantage to the industry would be that of reduction in transaction cost, with an immediate impact coming from the discontinuance of CST. The multistage taxation along with the inability to take full benefit of the CENVAT credit /refund has been an issue for the industry. With central GST expected to be a single rate for goods and services, going forward credit accumulation may not be an area of concern. Furthermore, if the legislation provides for carrying forward of the unutilised credit this would be an additional boost to the industry.

Furthermore, the pharmaceutical sector currently enjoys various location based tax holidays on its manufacturing activities. Under the proposed structure of GST, such area based exemption will be done away with. However, taking into account past precedents suitable work around/refund process would be constituted to ensure that any existing hubs do not get impacted and continue to get the agreed benefits.

GST would bring everything on a single and same platform for all. It would bring more transparency in the system. However, GST is not likely to impact financial or operational performance of the companies in a notable manner.

Real Estate – Positive

Implementation of GST will result in reduction in property prices. At present, the developers pay various non-creditable taxes like excise duty, customs duty, CST, entry tax, etc. on the procurement side, and the buyers pay service tax and VAT on purchase of residential units when booked prior to their completion. The proposed GST will replace these multiple taxes with a single tax and will also ensure smooth flow of credits through the chain. Hence, it is expected that GST will reduce the construction cost incurred by the developers and thereby help in reducing the current level of property prices. However, high GST rates will offset any possible gains on incremental credits. GST will also result in improved inflow of foreign funds in the real estate sector, as implementation of GST will improve the investor sentiments.

Hotels – Neutral

The GST, once implemented, is expected to rationalise indirect tax structure and usher in seamless tax credit. However, the impact for the hotel sector is more likely to be neutral depending on the final GST rate. Since hotels/restaurants are mainly subject to service tax, VAT (state subject), luxury tax (state subject), the impact of GST would depend on the tax levied by various states. If the GST rate gets capped at 18%, the impact is likely to be neutral as presently service tax payable by hotels is around 8.7% and luxury tax at around 8-12% (depending on the state and type of service). Restaurants have to pay service tax at around 5.6% and VAT at around 12%-14.5%.

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