

Who 'pays for' the Compensation? Goods and Services Tax (Compensation to States) Bill, 2017



GST is expected to give fillip to the economy and create a surplus in the States' budget. But the economics behind the politics is insurmountable even for a Government that has been growing from strength to strength in its presence and aura. The GST (Compensation to States) Bill, 2017 is the compromise of sorts to show the source from where the Union will compensate the States for any loss of revenue. With the assurance that the money will come from this law to meet the compensation commitments, the States can now rest assured that as long as they are able to demonstrate loss of revenue on account of implementation of GST, they will get compensated. But who is to 'pay for' this Compensation. This article briefly surveys where the journey of compromise between the Centre and the States has reached and how it will impact the industries involved. Read on to know more.....



CA. A. Jatin Christopher

(The author is a member of the Institute who may be contacted at jatin.christopher@gmail.com.)

The preamble of the GST (Compensation to States) Bill, 2017 presupposes that loss of revenue will arise on account of implementation of GST pursuant to the 101st Amendment to the Constitution. Experience suggests that every tax reform has invariably brought windfall gains to the exchequer directly from the increased compliance and indirectly from the

decreased cost of administration. Consensus building in order to proceed with implementation of GST demanded not merely assurance of compensation in the event of any loss but the clear roadmap to generate revenue and a formula for distribution of the compensation.

GST (Compensation to States) Bill:

Effect of consolidation under GST

With the reduction in the multiplicity of taxes imposed in the entire supply chain, inefficiencies due to cascading of taxes are eliminated. This produces a 'cost reduction effect' and an increase in overall revenues due to improved compliance. Any working capital pressure experienced is short lived due to the immediate offset that is enjoyed by the taxpayer. Admittedly, this efficiency will only come to those who are vigilant about reporting and compliance and bears down heavily on those lax in reporting and only partially report their transactions.

Computation of loss

Tax revenues of the financial year ending March 2016 are compared with the tax revenue of each year in order to determine the loss and claim compensation with a growth rate of 14% projected over the previous year. Revenues of the base year will exclude revenues coming from taxes not subsumed into GST and tax on commodities not included within GST. The difference between such revenue and revenue from the following would constitute loss on account of GST:

- SGST
- Share of IGST and
- such other subsumed taxes

Payment of Compensation

Compensation towards loss will be provisionally calculated and released on a bimonthly basis. It will be finalised based on revenue figures duly audited by CAG of India. Any shortfall in the provisional release will be made in the provisional release occurring next. Any excess in the provisional release will have to be returned back and credited to the Fund.

Levy of Cess

This cess is levied under Section 8, on:

- intra-State supplies in Section 9 of CGST Act
 - inter-State supplies in Section 5 of IGST Act
- So, this levy will be imposed on all supplies attracting Section 9 and Section 5, respectively.

In other words, if a supply escapes levy under the respective Principal Act, cess under this Act will also not apply.

Once intra-State supplies attract the levy of cess, reference to SGST Act / UTGST Act is not warranted given that GST in India will be a dual tax.

Exclusion from levy

Composition taxable person is excluded from levy of cess. There is no power to grant exemption from cess nor is any such power derived from the respective Principal Acts.

Any exemption from CGST or IGST will not automatically exempt the levy of the cess.

Levy on imports

Cess will be imposed in accordance with Section 3 of the Customs Tariff Act, 1975.

Rates of Cess

Central Government to notify the effective rate of cess not exceeding the given rates on articles specified in the schedule, namely:

Description	Rate
Pan Masala	135% ad valorem
Tobacco	➤ ₹4,170/1000 or ➤ 290% ad valorem or ➤ Combination of above
Coal briquettes	₹400/ton
Aerated waters	15% ad valorem
Passenger cars (<10 pax.)	15% ad valorem
Any other supplies	15% ad valorem

Cess on services

From the residual entry 'any other supplies', it is possible that cess may be imposed on notified services. It would merit studying the implications of the 8(2) notification with great caution.

Input tax credit

The provisions of the Principal Acts have been borrowed for the purposes of allowing input tax credit in respect of the cess by Section 11. Credit of cess is permitted to be exclusively utilised for payment of cess.

Valuation

The taxable value will continue to remain the value determined for the purposes of imposing CGST/IGST and Customs Valuation Rules in the case of import of goods.

Issues for Consideration

Entries in schedule

After overcoming any alarm about the rate of cess prescribed in respect of certain articles such as masala and tobacco products, definition given to motor cars and motor vehicles may be a matter of concern. Those closely following announcements about the imposition of cess on luxury cars will eagerly await clarity about the definition of luxury cars. However, the schedule allowing room to levy cess on the entire entry 8703 heightens the concern until 8(2) notification is issued.

One need not be amazed that so few are the articles in India that seem to meet the ostensible reasons given to justify imposition of this cess. The residual entry is jaw-dropping due to the lack of any fetters of tariff entry that the description—‘any other supply’—covers. Except being rescued by an 8(2) notification, all inter-State and intra-State supplies are exposed to levy of cess.

References to Provisions

Legislation by reference is not uncommon in taxation and Section 11 borrows the following provisions:

- assessment
- input tax credit
- non-levy
- short levy
- interest
- appeals
- offences and
- penalties

On a comparison with Section 21 of IGST Act, the brevity of Section 11 is apparent. Provisions such as scope of supply and time and value of supply are included by attaching the levy of cess with the levy under the Principal Acts. However, non-inclusion of any essential chapter from the Principal Acts will deny the authority to the Central Government to avail the benefit of that chapter(s) in

One need not be amazed that so few are the articles in India that seem to meet the ostensible reasons given to justify imposition of this cess. The residual entry is jaw-dropping due to the lack of any fetters of tariff entry that the description—‘any other supply’—covers. Except being rescued by an 8(2) notification, all inter-State and intra-State supplies are exposed to the levy of cess.

Omission to include cess in the terms of a contract for supply may render the duty to pay cess to behave like a direct tax even though it is well understood that this is an indirect tax. This is a liability that the taxable person is required to discharge whether he has made provision to reimburse himself the incidence from his customer or elected to bear the burden himself.

relation to cess. The decision in *Pioneer Silk Mills Pvt. Ltd. vs. UoI 1995 (80) ELT 507 (Del.)* may be referred.

Undistributed Cess

Any balance lying in the Fund undistributed at the end of the transition period will be applied as follows:

- 50% to the Consolidated Fund of India
- 50% to the States in proportion to revenues in the last transition year.

Cess—after five years

The five-year limit for imposition of this cess is not indelible because Section 8 provides for levy of this cess “...for a period of five years or for such period as may be prescribed.....” It is hoped that no circumstances will prevail at the end of five years to necessitate the continuation of cess even if we have become accustomed to pay it and hardly resist if it continues. Power of the Government to levy GST upto 40% rate, however, indicates that with the phasing out of cess, possibility of enhanced tax rates may remain open.

Levy under Constitution

This levy also derives power from the same Article 246A and 269A of the Constitution. The authority to collect this cess from the taxable person is ensured by the Government but the remedy to recoup this levy still remains contractual.

Omission to include cess in the terms of a contract for supply may render the duty to pay cess to behave like a direct tax even though it is well understood that this is an indirect tax. Reference may be made to the decision in *Chhotabhai Jethabhai Patel & Co vs. UoI & Anr., 1962 AIR 1006 (SC)*. This is a liability that the taxable person is required to discharge whether he has made provision to reimburse himself the incidence from his customer or elected to bear the burden himself.

Incidence of Cess

With the power to impose cess commonly exercised with the power to impose tax under the Principal Acts, the presumption remains that the incidence is transferred to the recipient of the supply. Considering that this levy is to compensate the loss of revenue to the States, the equity in picking-out the supplies that would eventually bear this incidence requires some thought. Consideration is also owed to whether the 'sinfulness' of these articles of supply will diminish at the end of five years.

Raising these questions only draws unwanted attention of tax administration and the ire of socially conscious taxpayer. It would be remarkable to see the movement in the retail price of these articles in the quarters leading up to the introduction of GST. All other things but the burden of tax leads these industries into the red, what then is one more tax?

The remarkable investment in technology does not seem to facilitate restoration of the recovery in the event of surplus in the Fund. Perhaps the concern about unjust enrichment is the motivation for a 50:50 sharing of undistributed cess, but wouldn't this be another role befitting the anti-profiteering authority?

Retaining undistributed balance in the Fund causes distortion in the class of consumers who shouldered burden imposed due to overestimation of loss of revenue and the classes of consumers who eventually enjoy indirect benefits from efficient use of the share. Any measure that minimises this distortion may go down in history that no class of consumers 'paid for' any more than what was merited.

Conclusion

Cess levied under the GST (Compensation to States) Bill, 2017 is no less a tax requiring the urgent attention of members, tax administration and industry at large. Attention is needed to examine the levy of this cess does not fail the basics of taxation in its imposition because of the fetters unmistakably present in its preamble—to provide for compensation to States for the loss of revenue arising on account of implementation of—GST. Motivated by the uniformity in law and the removal of interface with tax administration will bring great revenues to the exchequer by improving voluntary compliance. It would be fitting to see this cess not last even the five years proposed. ■



Non-Receipt of *The Chartered Accountant* Journal

This is for the information of Members/subscribers who fail to receive *The Chartered Accountant* journal despatched to them either due to un-intimated change of address or postal problems.

Members and Students are requested to inform the respective regions immediately after you change the address to ensure regular and timely delivery of journals to you as the mailing list is drawn from ICAI's centralised database updated till 15th of every month. Subscribers are requested to mail their changed address to eb@icai.in.

Members can also update their address online in the 'Members' section placed on the top bar of ICAI website. The required link in the 'Members' section is titled 'Members: Update Your Residential and Professional Addresses' (<http://www.icai.org/addupdate/>). Fill the Membership No and Date of Birth to open the Form. Fill the Form to update your changed address.

After updating the address online, the member is also required to download the updated Form and submit the same at their respective regions with their signature. Please note that once updated in the respective regional head offices' records, the new address gets automatically updated in the centralised data base of the Institute, from where the journal mailing list is prepared.

While updating the address members can opt for their 'Residential Address' to receive the copy of the journal by clicking the option "Do you want to get your journal on Residential Address" at the bottom of the Form. Thereafter you will get your copy of the Journal at your residential address.

Any queries or complaints in this regard can also be sent by email at journal@icai.in (for members) and eb@icai.in (for students and Subscribers) or contact at 0120-3045921.