Goods and Services Tax: Impact on Indian Manufacturing Industry

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ABSTRACT

On 1 July2017, India ushered in the biggest post-independence tax reform. It is one of the biggest tax reforms that are founded in order to make one nation one tax. With the help of GST system, India is projected to play a significant role in the world economy. As there is the economic crisis is running across the globe, in that situation India has posed a great tax reform of the GST policy with the ultimate hope of ambitious economic growth. GST which is more expected to support the Indian economy effectively by just transforming the existing barriers base of indirect tax policy toward the free movement of goods and services. The Indian manufacturing industry has emerged as one of the high growth sectors in India, and the launch of 'Make in India' initiative further propelled and gave this sector the necessary boost. This paper evaluate the impact of GST on manufacturing industry in India and it is found that India is expected to set its global mark by becoming the fifth largest manufacturing country in the world by the end of the year 2020. In addition, the Government of India has set an ambitious target of increasing the GDP share of manufacturing industry from its current stagnant 16% to 25% by 2025. GST policy is one of the bench mark and best beneficial step taken by the government of India.

KEYWORDS: GST 2017, Impact of GST on Indian Industry, Indian manufacturing sector, Impact of GST on manufacturers.

Background

Undoubtedly, the Goods and Services Tax, popularly referred to as GST, is one of the most remarkable historic reforms in the effort to bring the entire nation under a single tax regime. The earlier taxation system was mainly divided into two major categories- Direct Taxes and Indirect Taxes (Excise Duty, Sales Tax, Local Body Tax, Customs Duty, and Service tax), depending on whether the tax burden is borne by the payer directly or shifted to others in the value chain. This taxation system ultimately led to the tax on tax cycle resulting in increased cost of all goods and services. Thus, GST is a move to merge the taxation system to make it simpler and more effective. So, basically with the notion of 'one nation, one tax, one market', GST will subsume the indirect taxes both at the central level and state level. These alterations have impacted every sector of the economy and have also ensured in bringing every business under the tax net.

So far, the complex tax structure has been one of the main reasons affecting the progress of the Indian manufacturing sector. But, the implementation of the unified tax system – GST, the manufacturing sector is set for an overall revival impacting factors such as production cost, operation cost, logistics cost, and time and compliance savings.

- **Reduced cost of production** - As GST subsumes various types of taxes, it will directly have its impact on reducing raw material cost and production cost. Additionally, easier tax credit system will drive better accounting and cash flow for the organization.
- **Reduced transportation time and cost** - The GST system will result in a smooth and hassle-free flow of goods within the country by removing multiple checkpoints and

permits at state border checkpoints. It is anticipated that by unifying the domestic market, almost 60% of logistics time and effort will be saved resulting in faster delivery of goods.

- **Restructuring of warehouse** - So far, manufacturers used to set up a local warehouse to save cost incurred due to the state based indirect tax system. But, with GST coming into play, manufacturers can relax themselves from setting up local warehouses and utilize that cost towards capacity building. Also, by consolidating warehouses or by building larger warehouse facilities, the organizations can save on IT costs incurred by deployed ERPs at many small warehouses. This will considerably reduce the cost of the overall supply chain.
- **Removal of area based exemptions** - The GST model will consider the entire nation as one market thereby absolving the area based incentives. This will attract businesses to all locations. With the above-mentioned alterations, the cost of manufacturing goods is expected to reduce while the consumption is expected to rise. It is also expected that India's GDP will see a growth by 1-2% with the proposed GST. This indicates that it is a good time to invest in a manufacturing business either by **taking a business loan** or a commercial loan or expanding the existing business. The business loan or commercial loan can be utilized for various purposes, such as expansion, infrastructure, working capital, and other business requirements. Finally, the GST structure has the potential and is anticipated to be the game changer for the Indian economy by providing the manufacturing sector the much-needed thrust to make its place in the global mark.

Advantages – Impact of GST on Manufacturers

1. **Reduced Cost of Production** – Under the erstwhile tax regime, manufacturers had to pay an excess of 25-26% as production costs, quite clearly due to the effect of cascading taxes such as excise duty (at 12.5%) and VAT (at 14.5%), on the lines of taxing two different taxable events. Now under GST though, tax would be levied on single taxable event. This consequently means goods are expected to get cheaper, thus, driving more sales and lending the concerned stakeholders a strong hold in an increasingly competitive market.
2. **Simplification of taxes levied through removal of differential valuations**–Excise duty, which under the old tax structure was calculated on the basis of different methods such as – Specified duty, Tariff Value, Value based on Retail Sale price, Ad Valorem duty – will now be streamlined and easier to calculate as GST pushes for transaction-based valuations only.
3. **Subsumed taxes mean less costs and better quality of goods and services** – A key factor in driving down production costs is that most of the taxes on inter-state supplies that were earlier not creditable (central sales tax, OCTROI, entry tax, etc.) would now be available for set-offs, thus, reducing the burden on the manufacturing sector and setting up a steady flow of credit. With **most taxes getting subsumed under the GST structure**(except customs duty, Stamp Duty which will continue to be levied as before), other participants in the trading channel also stand to gain from this move i.e. retailers and distributors will now be able to avail credit on the taxes levied, and such accessibility of input tax credit at various stages of the commercial process would effectively lead to reduced prices, which can safely be considered a win-win scenario for both the manufacturing and other related sectors *and* the end consumer. Also, with the burden of indirect tax on the manufacturers substantially lessened, the industry shall now be able to focus more on the quality aspect of the production process rather than merely the commercials, thereby filling the quality gaps in a country severely in need of an up gradation in goods produced.

4. **Restructured and streamlined supply chain leading to improved business efficiency–** Most of the supply chain management earlier depended on taxes operating in different states. Now flagged under the 'one-nation-one tax' concept of GST, businesses are now required to re-engineer their supply chains, which in turn will encourage them to focus more on optimizing business efficiency and operability instead. For example, multiple warehouses in different states would no longer be needed, and with the extra layers of the supply chain done away with, manufacturing businesses can now solely focus on strategizing their supply chain with respect to economic, demographic and geographic targets. The resultant improved inventory management, when combined with input tax credit benefits (as described above) will lead to plummeting storage costs, less time wasted at various checkpoints, and ultimately, the emergence of a sturdy manufacturing sector, the immediate effect of which shall undoubtedly be felt in the logistics sector.
5. **Only registration as per the State to apply henceforth –**Earlier, if a single manufacturer had multiple factories in a single state, he was required to obtain a separate registration for each of the factories. However, under the current GST regime, a single taxable manufacturer would need to apply for a single registration only, irrespective of the number of factories that lie within the said state. This logically means less paperwork and less bureaucratic intervention to be dealt with at every stage, eventually resulting in better business management.
6. **Small manufacturing businesses can now opt for Composition Scheme –**Manufacturing businesses with a turnover of not more than 75 lacs are now eligible for availing the Composition Scheme under GST (at a rate of 2%), providing some measure of tax relief to the intended beneficiaries. Of course, exceptions apply as to which manufacturing businesses *can* and *cannot* opt for this scheme, along with documentary compliance and other conditions that must necessarily be fulfilled by the said consumption dealers who stand eligible to apply for the same.
7. **No assessment by multiple tax authorities –**Previously, separate tax assessment authorities were to take care of varied taxes those being –VAT, Service tax, Central Excise, sales tax, etc. This not only rendered the whole procedure chaotic but was extremely time-consuming as well; leaving manufacturers vulnerable to dealing with tax queries they did not quite know how to navigate, while negatively affecting their business. Henceforth though, instead of separate authorities assigned to take care of the assessment based on the type of tax, assessment will be carried out in defined three-fold system i.e. State authorities would take care of SGST assessments, while Central authorities would look into CGST and IGST assessments respectively. This would result in a more efficient tax assessment system, that would not only save a lot of time, but would also aid manufacturers in dealing with the procedure better without having to deal with multiplicity of tax-related queries as well as their implications.

Apart from aforementioned advantages being some of the striking results of the GST, a few others are also expected to make their impact felt. For example, compliance with **GST's anti-profiteering clause** (that mandates businesses pass on benefits derived from tax reduction/input tax credit availability to end consumers) would ensure manufacturers operate on the right side of law, while keeping customer interests in mind. This paves the way for the government as well as the manufacturing sector to work in harmony for a common good than functioning from a perspective of us-versus-them. With introduction of the electronic mode of filing forms, manual paperwork would be considerably reduced; going electronic shall also ensure bureaucratic laches at multiple filing stages is also done away with.

And last, but not the least, with the unification of taxes brought about under the GST, classification of disputes under excessive calculation heads of the erstwhile tax regime is expected to be significantly minimized, thus, clamping down on the volume of tax litigation currently plaguing the tax administration as well as the courts.

Disadvantages – Impact of GST on Manufacturers

Not all is hunky-dory though; there are a few concerns surrounding this newly developed tax mechanism, some of them being:-

- Manufacturers would now be faced with an increase in working capital requirements – owing to receipt of advance, stock transfers (other than own depot and warehouse in same state due to same GSTIN) as well as branch transfers now made taxable under GST.
- Petroleum products being kept out of the purview of GST, tax paid on the same would not be available as credit, thus bringing about no respite in related industries – such as power and logistics industries that will continue to feel the burden of balancing a cost-benefit scenario in such a context.
- Reverse charge that was earlier confined to specified services only, shall now be applicable to goods as well. And as a burden borne by recipients of goods/services instead of the supplier of the same, the manufacturing sector will find itself considerably strained under these increased costs.
- As regards CENVAT credit, the same shall be available only on goods purchased from registered dealers (in case of unregistered dealer first tax payment by debiting Cash ledger is required then can claim ITC on it) so this too, is a limitation in the sense that small businesses may not always find it feasible to purchase goods from registered vendors only.
- With GST aiming for better tax compliance, comes the inevitable requirement of businesses overhauling and streamlining their existing transactions, which, eventually calls for more resources and money to be pumped into these compliance measures. From hiring skilled personnel for taking care of the technical know-how, to ensuring legal checks and balances at every step, becoming GST-compliant itself will incur heavy costs for businesses that have till date not really followed the book.
- Operational and structural confusion is expected to last a while since most businesses do not still understand certain aspects of new rules brought under GST- one of them being area-based exemptions (that allowed exemptions for in select states like the North-East in case of threshold i.e. 10 lakhs while in other state it is 20 Lacs);. This means a considerable shift in financial position of manufacturing companies who would now have to take stock of the situation and reassess their business strategy.

The disadvantages, though not too many, are crucial when perceived in the larger scheme of things and can go a long way in providing a boost to manufacturers, if worked on/rectified. The inevitable consequences of GST cannot be wished away, as manufacturers realize they will have to put up with some inconvenience for a while now.

However, the government may re-consider lifting the limitation as regards availing of CENVAT credit – on goods purchased from registered dealers alone (while in case of unregistered first payment of Tax is mandatory). This will act in significantly reducing the burden on manufacturing units. However, purchase of worth Rs. 5000/- per day from unregistered person is still allowed without any tax compliance but still it's too less for big companies. More deliberation is required on bringing power and electricity under GST, which, if eventually sanctioned, would aid in bringing down operational costs for businesses in a dramatic way. As of now though, manufacturers have a lot to be relieved about, as they see less hassle and more structure in the management of their businesses.

Finding:

- India too has, emerged as one of the high growth sectors in the manufacturing space, a fact evidenced in an increase of no less than 7.9 percent in Gross Value Added (GVA) at basic constant prices year-on-year as of 2016-17.
- Make in India project helmed by the Government of India under the leadership of Prime Minister Narendra Modi, is all set to maximize the country's demographic and geographic advantages to build India into a manufacturing and technological hub (particularly in the electronics sector), marking its commercial territory on the world map by the end of 2020.
- On a statistical level, the GDP share of the manufacturing sector is expected to surge to 25 percent by 2022, up from the current 16 percent, **along with** 100 million jobs by 2022.

Conclusion:

The manufacturing sector in any country can rightly be deemed as the backbone of its economy, leveraging its resources for maximum economic boost, which then makes way for competitive trade and business to take place – locally, nationally as well as globally. India already figures as one of the powerhouses listed under the "Mighty Five" as per the Global Manufacturing Competitiveness Index published by Deloitte Touch and the Council on Global Competitiveness. With factors like cheap labour, a burgeoning demographic profile and economic expansion, the country is all set to take on rival neighbour China that continues to spell an aggressive boom in the manufacturing space. If GST indeed delivers the results expected of it, undeniably, India will soon get on the road to becoming an unstoppable force in this arena and many others.

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