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GST accruals: Tax can lead to a formalisation of the workforce

The new indirect tax regime is all set to take over from July 1, 2017

GST is simplification of the existing indirect taxes by subsuming them into four bands of 5%, 12%, 18% and 28%. (Reuters)

Finally, GST is a reality. It took 17 years after inputs from four central governments, over 100 state governments, various committees, numerous discussions and a marathon seven hours debate in the Lok Sabha last week. The new indirect tax regime is all set to take over from July 1, 2017. GST is simplification of the existing indirect taxes by subsuming them into four bands of 5%, 12%, 18% and 28%. This apart, another category of tax between 40 and 65% will be imposed on luxury goods and socially 'bad' goods. Across the board, experts are hailing this as the second most important milestone in the history of Indian economy post-liberalisation of 1991. It is, therefore, imperative to ask how goods and services tax (GST) will change things? To assess the benefits, we must look at both the direct and indirect benefits of GST. Estimating the direct benefits imply assessing the three major stakeholders who will get affected by the new tax code—the consumers, the enterprise and the government. The indirect benefit is that it will bring a structural change in the way businesses are conducted across the country.

It is, now, estimated that the overall impact on the consumer price index (CPI) will be deflationary, to the tune of - 0.6%. This will be largely owing to the zero-tax regime on essential food items that forms a large part of the wholesale price index (WPI) basket. However, these estimates are static in nature. It compares indirect taxes to the end consumer, based on their current consumption patterns. Surely, such patterns are bound to change with the new effective prices they face, especially as more and more services make way into the consumption basket. Therefore, it may be too early to estimate how this will affect the inflationary forces. What then will be the effect on overall indirect tax collection? In the Union Budget 2017-18, the government estimates to collect nearly `19.27 lakh crore from indirect taxes next fiscal, up 9% over 2016-17. Undoubtedly, this is a positive step especially coming in the backdrop of an 11% increase in tax collection from services. Finally, what does it mean for the business? Initial estimates have already identified gainers and losers. What remains of primary concern to us is how will the benefits translate into employment, given India has witnessed jobless growth in the last decade? The curious case of jobless growth we have seen over the years puts all such exercises irrelevant. The true success of the GST will not be measured in terms of its impact on inflation or indirect tax collection, but on creating jobs! Does GST have anything there? This is where the indirect benefits of GST will perhaps be more visible than direct effects. Goods and services tax has the potential to change things by making tax compliance simple. This will be an incentive for small and medium enterprises (SMEs) to be part of the formal tax structure. In fact, it would be almost mandatory now because the entire supply chain would now have to be accounted for in the tax chain. The reason is plain to see. Firms up the value chain would only contract with those below whose taxes they can write-off. This would encourage more from the informal sector to join the formal sector. Various estimates peg the share of workforce in the informal sector at about 86% of total workforce. For one, any move from informal to formal sector would benefit the workforce who will be retained. However, there will be few job losses. But this is where the enabling systems need to work well for the indirect tax to be a success. While most experts view the main advantage of GST as making it easier for existing businesses, the government needs to understand the impact it will have on new start-ups and tweak incentives, if necessary. For example, the tax offsets would require maintaining higher working capital now. Thus, an accompanying thrust that makes working capital easily available would be a natural response. Goods and services tax would change the way we do business, but it is also expected to change the political economy. The usual 'populist' tax breaks in every subsequent budgets may be history now. This is investing for economies infrastructure. The issue is do we have the will and the architecture to go the distance?

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