



India's new GST

The countdown is on

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After 10 years of effort, India's new goods and services tax (GST) seems set to take effect on 1 July 2017, ushering in one of the most significant reforms in the country's history. But even though the tax has been at least a decade in the making, detailed rules have only started being published recently. Many businesses in India have been left with little time to understand their new obligations and get ready to comply.

GST implementation is likely to have an impact across a company's operations, from cash flow to supply chain to people, systems and processes. Planning for the transition offers an excellent opportunity for organizations to take a transformative approach, assessing and realigning business models to drive efficiencies, gain competitive edge and boost profits.

In this article, you'll find out how the tax is likely to apply and what businesses with operations in India should be doing in the short timeframe to get ready.



How will the new GST operate?

With its new GST, India joins some 160 countries globally in imposing a form of value added tax (VAT). These taxes are widely acknowledged as progressive, with inbuilt efficiencies to broaden the tax base, decrease the cascading effect of multiple indirect taxes and contain revenue leakage.

India's GST will replace a complex web of existing taxes, bringing uniform tax rates and rules and simplifying compliance for businesses. The list of taxes subsumed by the proposed GST is expected to spell the end for most existing central and state taxes on supplies of goods and services, including central excise and service tax, central sales tax, state VATs and other local levies on goods.

India will operate a dual GST. The central and state governments will levy the GST on supplies of both goods and services on a common taxable value and receive the revenues from their component of the tax. Imports and interstate supplies will attract an Integrated GST (IGST) levied by central government. Businesses can claim input tax credits (ITC) to recover the tax they pay on the incremental value they add to a product or service, so the tax is ultimately borne by the final consumer.

The GST will apply at five basic rates:

- a 0 percent rate will apply to essential food items, exports and supplies to Special Economic Zones
- a 5 percent rate will apply to some mass consumption items (e.g. spices, tea)
- a 12 percent rate will apply to other commonly used items (e.g. soap, cell phones, processed foods)
- an 18 percent standard rate that will apply to most products and services
- a 28 percent rate will apply to durable consumer goods (e.g. televisions, cars).

A surcharge on top of the 28 percent high rate will apply to luxury items, such as high-end cars, and 'sin tax' items, such as tobacco.

Exactly which goods and services will be included in each bracket is not yet known.

Businesses will have to register for the tax if they have an annual turnover of 2 million Indian rupees (INR) (INR1 million for businesses in special category states). The threshold includes all taxable and exempt supplies of goods and services, exports and interstate supplies, and it is computed on an India-wide basis.

A special registration procedure is prescribed for:

- businesses required to deduct or collect tax at source
- taxable non-residents
- businesses supplying online information and database access or retrieval services from a place outside India to a non-taxable online recipient.

Existing registrants will migrate into GST as of 1 July 2017 on a provisional basis (with the option to cancel later), and they will be registered state-wide under a single Permanent Account Number (PAN). The transitional rules allow for the transfer of unutilized ITCs from the current regime to the new GST system. Businesses can register voluntarily if they want to be part of the input tax credit chain.



Missing details, short timeframe

While the new GST's reduced complexity and easier compliance promises benefits down the road, businesses have been given little warning of the tax's detailed operation, with wide-ranging effects. For example:

- **Tax software:** The delayed release of detailed rules has hampered the ability of tax software providers to produce reliable compliance assistance products in advance of the deadline.
- **Extensive new obligations:** Banks and other financial services companies that were previously only subject to taxation centrally will now need to marshal the resources to deal with new state tax obligations in each state they operate in.
- **Valuation and pricing:** Uncertainty over tax rates for not-yet-classified goods and services may be complicating pricing decisions and negotiations with suppliers.
- **Tax incentives:** State tax incentives in the form of exemptions in the current indirect tax regime are expected to be converted in to post tax cash refunds. This will lead to probable significant effects on financing, cash flow and working capital. These include tax holidays for businesses in special category states and exemptions for export oriented units and supplies to merchant exporters.
- **Inter-state inter-branch transfers:** The IGST will be imposed on previously non-taxable inter-state transfers of goods and services between branches of the same company. It will be difficult to set values for these transactions, and new systems will be required to track and report them.
- **Advance payments:** The GST will apply to advance payments for goods, requiring tax payments to be made before goods are received. This could significantly affect commercial arrangements for large projects in India's construction industry, where such payments are common.
- **Online matching:** One-to-one invoice matching for business-to-business transactions will match buyers' ITC claims against supplier GST liabilities, and ITC credits will be denied to suppliers with unmatched credits.

- **Unregistered suppliers:** Where a registered business makes purchases from an unregistered supplier, the liability to pay GST shifts to the registered business.
- **Anti-profiteering rules:** An anti-profiteering provision is being introduced to ensure any tax reductions resulting from the GST are passed on to consumers, but its operation is unclear, making it difficult for companies to avoid running afoul of the new rule.
- **Electronic waybill:** Businesses will need to meet cumbersome requirements to generate e-waybills for all transfers of goods and consignments valuing INR50,000 or more, either within or outside the state.

The new system will employ a nation-wide electronic portal for uploading details of each outward supplies, submitting returns and generating ITC refunds. Businesses that do not have the systems and processes in place for electronic invoicing by 1 July 2017 would put their compliance at risk. Further, their customers would be unable to recover ITCs through the portal on their purchases and might take their business elsewhere.

Additional complications could arise from the division of administrative control over taxpayers. With India's state governments unwilling to cede control of their tax assessment rights, the state and central governments have agreed to an assessment system to ensure taxpayers are not subject to double enforcement scrutiny. Ninety percent of registrants with annual turnover of INR15 million will be under state jurisdiction, while the remaining 10 percent (chosen by software at random) will be under central jurisdiction. Jurisdiction for registrants with turnover exceeding INR15 million will be divided equally between the center and the state.

In theory, GST registrants should get equivalent treatment from state and central authorities. However, it seems likely that state tax authorities may differ in their interpretation and assessment practices, leading to inconsistency and uncertainty for taxpayers.



Taking a transformative approach

Based on the experience of KPMG member firms with the implementation of significant indirect tax reforms in other regions, it is crucial for businesses to start preparing for the GST now.

For businesses in India, the GST entails a marked shift from origin-based taxation to a destination-based tax structure, with significant potential impacts on cash flow, pricing, working capital, supply chain and IT systems. The GST is much more than a tax change but a business change that will affect most functional areas. For example:

- **Operating model:** The GST may trigger substantial redesign of the operating model, which may include reorganizing internal roles, redefining the responsibilities of the tax function, and deploying IT fixes. Opportunities may arise to streamline complex operating structures designed to maximize inter-state indirect tax recoveries under previous regimes by consolidating warehouses and branches.
- **Business processes:** The GST reforms will affect order-to-cash, procure-to-pay and record-to-report processes, requiring new forms (electronic invoices) and new reports to facilitate the completion of GST returns. GST processes need to be strong enough to support the mapping and matching of invoices under India's electronic filing system.
- **Accounting and IT systems:** Complying with GST may require reconfiguration of IT systems, changes to vendor and customer master data, tax condition logic updates, and new tax code/GL accounts.
- **Contracts:** Contracts may need to be reviewed to help ensure compatibility with the GST. Long-term contracts may need to include new clauses on, for example, tax, pricing and changes in law
- **Pricing:** The pricing of products and services may need to be reviewed. In cases where customers cannot recover the tax charged, suppliers may need to consider absorbing some of the tax cost.
- **Human resources:** GST may apply to amounts paid to employees, such as fringe benefits, gifts, allowances and expense claims.

An effective and seamless transition calls for a 'business transformation' approach, involving multiple stakeholders in affected functional areas, such as finance, IT, supply chain, human resources and marketing. A good first step is to form a group that includes representatives of these functions to map out what the GST would mean for your business. This should be followed by a detailed impact analysis in all these areas using all available numerical data.

With this analysis in hand, companies can then begin developing and implementing a GST implementation plan, setting out key tasks such as negotiating and communicating with suppliers, vendors and internal stakeholders, and putting in place IT and supply chain-related changes.

Companies will need to ensure they have sufficient resources (e.g. accountants and tax advisers) to manage their new obligations. Many companies have employed people with specialized knowledge of compliance with one specific tax that is being replaced with the GST, which requires quite different technical skills. These people may need to be trained and redeployed as part of GST implementation. Additionally, filing for some former taxes was done at the operating location level (e.g. factory), and companies with multiple locations in one state may need to relocate staff or hire new people to centralize their GST reporting resources.

A detailed implementation plan, supported by adequate resources and regular monitoring, can help ensure that your company maximizes GST recovery on your business inputs, ensures timely compliance with VAT obligations and reporting, and mitigates the risk of fines and penalties. By taking a transformative approach to evaluating your various tax and business triggers and responses, your GST implementation can go beyond compliance to propel improvements in taxability and rates, exemptions and concessions, cash flow and refunds, supply chain network and governance — revealing efficiencies and improvements that drive superior performance and results.



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