

## ***Decoding the Model GST Law***

### **Key features of the draft Model GST Law**

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## ***India on the brink of GST***

The introduction of Goods and Services Tax (GST) has been one of the biggest tax reforms in recent history. While the process of amending the constitution to enable the introduction of GST has been slow, the other processes for introduction of GST have been proceeding at a reasonable pace. As a result, a few months back, the Government had released documents outlining four processes under GST regime, i.e. registration, payment of tax, returns and refunds, for giving industry an insight in the thinking of the Government towards GST. Taking a further step towards introduction of GST, the Government has released the draft model GST law for public comments.

The model law provides a common draft of Central GST (CGST) Act and State GST (SGST) Act. The model law also includes the draft of Integrated GST (IGST) Act as well as draft GST Valuation Rules.

The key features of the draft model GST law are as under:

### ***1 Coverage of the law***

The law covers entire India, including Jammu and Kashmir. In the present regime, service tax was not extended to Jammu and Kashmir.

### ***2 Important definitions***

The definition of **capital goods** is similar to present definition of capital goods under CENVAT Credit Rules, before amendments made in budget, 2016.

The definition of **consideration** includes payment made or to be made for the supply, and also the monetary value of any act or forbearance. This is aimed to include the non-monetary consideration in its ambit.

**Goods** are defined to mean every kind of movable property, and includes securities, but excludes actionable claim, money and any intangible property.

**Input** is defined to mean any goods, other than capital goods, used for making supply in the course of business.

**Input service** is defined to mean any services used for making supply in the course of business.

**Location of recipient of service** is defined to mean a place where the supply is received. In case of receipt of supply at multiple places, the location of recipient is the place which is most directly concerned with receipt of the supply. In the absence of any such place, the location is the usual place of residence of the recipient.

**Location of supplier of service** is defined to mean a place from where the supply is made. In case supply is made from multiple places, the location of supplier is the place which is most directly concerned with provision of the supply. In the absence of any such place, the location is the usual place of residence of the supplier.

**Usual place of residence** is defined as a place where an individual ordinarily resides and, in other cases, the place where the person is incorporated or legally constituted.

**Recipient** is defined to mean a person liable to pay consideration for the supply and, where no consideration is payable, the person who receives the supply. It also includes an agent acting as such on behalf of the recipient.

**Service** is defined to mean anything other than goods, and includes intangible property and actionable claims but does not include money.

**Supplier** is defined to mean the person supplying the goods and/ or services, and includes an agent acting as such on behalf of such supplier.

**Works contract** is defined to mean agreement for carrying out building, construction, fabrication, erection, installation, fitting out, improvement, modification, repair, renovation or commissioning of any movable or immovable property. This implies that any other contracts not specified here, which were hitherto treated as works contracts, would now be treated as supply of goods or services.

### 3 **Ambit of 'supply'**

The taxable event under GST is supply of goods and services. The term 'supply' includes all forms of supply, such as sale, transfer, barter, exchange, license, rental, lease or disposal made in the course of business, and importation of service. Transactions between principal and agents are deemed to be supplies.

'Supply' also includes specified transactions such as permanent transfer of business assets, temporary application of business assets to a non-business use, services put to non-business use, assets retained after deregistration, and supply by a taxable person to another taxable or non-taxable person in the course of business. However, supply of goods to a job worker would not be treated as supply.

It is specified that, *inter alia*, sale of under construction properties, temporary transfer of intellectual property rights, works contracts (including transfer of property in goods involved in execution of works contracts), transfer of right to use any goods and development, upgradation, customisation etc., of software would be supply of service.

#### PwC Comments

The term, 'supply' is widely defined to cover all forms of supplies, some of which were not under the tax net till now, such as barter. The scope and ambit of the clause 'supply by a taxable person to other person' and exact scope of taxability of transactions between principal and agent would need to be clarified, given the possibility of wide range of interpretation of such terms.

Since actionable claims are specifically treated as services, the tax treatment of transfer of actionable claims would need to be assessed as to whether the same would be treated as taxable supply.

It would be important for the industry to appropriately categorise the different types of the supplies made by them to assess the impact on taxability.

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#### **4 Time of supply**

Time of supply of goods is the earliest of:

- i date of removal/ making available goods by the supplier;
- ii date of issue of invoice;
- iii date of receipt of payment by the supplier; or
- iv date on which the recipient shows the receipt of goods in his books of accounts.

Time of supply of services is the earliest of:

- i date of issue of invoice or date of receipt of payment, if invoice is issued within prescribed period,
- ii date of completion of service or date of receipt of payment, if invoice not issued within the prescribed period,
- iii date on which recipient shows the receipt of services in his books of accounts, where (i) or (ii) above does not apply.

Time of supply under reverse charge is the earliest of:

- i date of receipt of supply;
- ii date of payment;
- iii date of receipt of invoice; or
- iv date of debit in the books of accounts.

In addition to the above, there are provisions to determine the date of supply in case of continuous supply of goods/ services.

#### **5 Value of supply**

The value of supply of goods/ services for levy of GST is the transaction value. To determine transaction value, specific additions are prescribed to be made to the price charged. Such additions include value of goods/ services supplied free/ at concessional rates by the recipient to the supplier, subsidies linked to the supply, reimbursable expenditure, etc. In addition, royalties or licence fees related to the supply of goods and/ or services are to be added to the value of taxable supplies.

The valuation provisions retain current provisions relating to pure agent in case of services. The discounts, including the post-sale discounts known at the time of supply (and linked to specific invoices), are allowed as deduction from transaction value, which is quite similar to the provisions prevalent presently.

When the supply consists of both, taxable as well as non-taxable supply, the taxable supply is to be deemed to be for such part of monetary consideration as is attributable thereto.

The concept of justification of transaction value in case of related party transactions continues in the valuation provisions.

The draft law also provides for rejection of value of supply if accuracy of valuation is doubted.

There is no provision to levy GST on the basis of maximum retail price, where the transaction value is below maximum retail price.

### PwC comments

There are many potential complications due to the various provisions covering value of taxable supply. One is double taxation. The goods and services provided free by the customer would typically have suffered GST, for which the customer would have taken credit. If the value of these supplies are to be included in the taxable supplies by the service provider, an amount that is already taxed would once again suffer taxation. In addition, if the customer is entitled to take credit for this amount, there would be no additional revenue due to this step. A similar position applies with respect to charges such as royalties, etc. related to a supply of goods and/ or services.

On the other hand, if the nature of the transaction is such that the customer cannot take credit (such as for construction of an immovable property), taxing the transactions twice would result in the amount being added to cost twice (since it is not creditable).

A much more troubling provision relates to valuation. In related party transactions or in case of the officer having reason to doubt the value as reported in the transaction, the officer can apply various valuation methodologies and arrive at the correct value. There are many problems with this provision. However, the chief among these is that for 29 states and 1 central jurisdiction to separately assess transactions and act reasonably and judiciously in every case of rejection of value does not seem feasible. For any taxpayer to potentially defend the declared value in 30 jurisdictions (for different transactions) across country seems quite a large burden.

Overall, industry should represent strongly for deletion of these provisions.

## **6 *Place of supply***

One of the most important aspects of GST is determination of place of supply. Detailed provisions to determine the place of supply, separately for goods and services, are laid down in the IGST Act.

The place of supply of goods is the place where the goods are delivered, except in few cases.

The place of supply of services to a registered person, is the location of such registered person. For services provided to an unregistered person, it is the address of recipient, and if it is not available, the location of the supplier of services. There are various exceptions provided to these principles, such as services pertaining to immovable property, training and appraisal, admission to the events and organisation of events, transportation, telecom, financial services etc.

### PwC comments

The industry would need to assess all the activities carried out by them for determination of appropriate place of supply, and to revisit contractual arrangements, where required. Another important task would be to assess the place of supply of their suppliers and to revisit the contractual arrangements, so that the credits are not lost or accumulated at a location. The default place of supply for services is the location of the client. It is not going to be in one state in most cases, as clients would be registered in more than one state. These provisions would therefore require extensive rework. Additionally, there are many transactions such as Annual Maintenance Contracts that are not adequately dealt with by the provisions. Industry would need to review whether the place of supply rules adequately address transactions in their industry. If there are gaps or ambiguities, these need to be brought to the notice of the government so that the rules can be appropriately redrafted.

## 7 Input tax credit

The GST law provides for credit of GST paid on all the inputs, barring some exceptions. The exceptions include the services received and used by employees and also vehicles (except when they are used for specified purposes), supplies received for execution of works contract for construction of immovable property, etc. Supplies used for personal consumption are also ineligible for credit.

The following procedural conditions also need to be fulfilled for claiming credit:

- possession of tax invoice;
- receipt of the underlying supply of goods/ service;
- payment of tax charged in invoice by supplier;
- filing of GST return

In addition, the credits claimed need to be matched with the tax liability of the supplier, and in case of any discrepancies, the amount of excess credit claimed will be added in the tax liability of the recipient.

The time limit for claim of credit is one year from the date of the invoice. However, no credit pertaining to a financial year is allowed to be claimed post filing of the return for September of the next financial year, or the filing of the annual return for the year to which the credit pertains, whichever is earlier. Effectively, for the purchases made post September month in a financial year, the time period for claiming credit is curtailed.

The concept of input service distributor is continued in the GST regime. However, credits of GST paid on inputs or capital goods cannot be distributed. The provisions of distribution of credit to outsourced manufacturing unit are also not available.

### PwC comments

The restriction on claim of credit of specific supplies is against the basic premise of GST, and it is hoped that there would be re-thinking on this aspect. Another area of concern is the availability of credit linked to compliance by the supplier and matching of records for credit.

Industry should represent to the Government for a simpler credit regime, to allow credit of all the taxes paid on the procurements, and to relax the requirements of compliance by vendor and matching of the credits.

On the operational side, the industry would also need to reassess the procurement strategies, to minimise the loss of tax credits.

## 8 ***Procedural aspects***

### ***Registration***

Any person having aggregate turnover of INR 0.9 million (INR 0.4 million for person carrying out business in the north-east) across all locations in India will need to obtain registration in the States from where they make a supply. In addition, the following persons would be required to obtain GST registration irrespective of turnover:

- person making inter-state supply
- casual taxable persons and non-resident taxable persons
- person required to pay tax under reverse charge
- persons making supply on behalf of other registered taxable persons, whether as agent or otherwise
- input service distributors
- persons making supply (except of branded services) through an e-commerce operator
- e-commerce operator
- aggregator supplying services under his brand name

It is envisaged that in each State, one registration would be obtained, unless the taxpayer chooses to obtain separate registrations for its different business verticals in the State.

### ***Returns***

For each month, a person who has not opted for composition is required to file the returns, separately for outward supplies made, inward supplies received, and monthly return. In addition to these returns, separate returns are required to be filed by input service distributors and by a person deducting tax at source. An annual return is also required to be filed.

The taxpayers having turnover exceeding the prescribed limit will also be required to get their accounts audited by a Chartered Accountant or a Cost Accountant, and submit a copy of the audited annual accounts with the annual return. In addition, they would also be required to submit a reconciliation statement, reconciling the value of supplies declared in the return furnished for the year with the audited annual financial statement, and any other documents as may be prescribed.

#### ***PwC comments***

Such enhanced compliance requirements would increase the compliance burden on industry, especially service industry. Industry would need to gear up their IT systems and strengthen the compliance team to meet these compliance requirements.

## 9 Special provisions

### *Job work transactions*

The principal has the option to send taxable goods without payment of GST to a job worker and bring it back, after processing, to any of his own place of business, for supplying such goods on payment of GST or export it.

The principal also has the option to directly supply final products to end customers on payment of GST or export from the premises of job worker itself, subject to fulfilment of applicable conditions.

GST credit is allowed in case of direct receipt of inputs or capital goods by the job worker, subject to receipt of goods back by the principal within specified period.

#### PwC Comments

While such relaxation is welcome, it may create a practical problem. While the principal manufacturer would claim the credit of GST paid on inputs in the State from where such inputs are dispatched, the transfer of such inputs to the job worker would not be subject to GST. In case of direct dispatch of finished goods from the job worker's location, GST would be payable in the State from where the goods are dispatched. In case of lack of GST liability for the principal in the dispatching state, GST credit would be accumulated in dispatching State. Industry would need to assess this aspect while planning for migration to GST regime.

### *E-commerce*

In a unique provision, in case of supplies made by using an e-commerce platform, it is proposed that the company operating the e-commerce platform would collect tax at source from the payment made to the actual supplier. This provision is not applicable when the e-commerce operator is making supplies himself, and not just facilitating the supply by another person. The operator would need to make payment of such tax collected at source to Government and file periodical returns for the same.

#### PwC Comments

This would result in additional compliance burden for the e-commerce operators. This can also lead to potential credit accumulation issues for the persons making supplies using the e-commerce platforms. In particular, in cases where the supplier is operating with thin margins, (for example 1%-2%), the GST payable would be 18% of 1%-2% of the price payable. If the tax collection at source is higher than this amount, it would result in such a business becoming unviable. Industry should make representation for doing away with this requirement.

## 10 Transitional provisions

Specific transitional provisions are incorporated to provide for the following:

- All the taxpayers registered under existing indirect taxes would automatically get temporary GST registration numbers, which would be issued on a final basis on the submission of prescribed information.



- Carry forward of existing credit balance as well as claim of credits on goods available with the taxpayer, subject to such credit being admissible under existing indirect taxes as well as under GST law.
- Treatment of return of goods removed under existing indirect tax regime.

#### PwC Comments

Some of the unaddressed issues in the transitional provisions are availability of credits on goods in transit on cut-off date, availability of credit of excise duty paid by traders and VAT paid by the service providers on goods in stock, etc.

Industry would need to ensure that all credits which would be available to them as part of the transitional provisions are captured in returns/ records so that the claim of credit is supported by adequate records. Industry will also need to represent for allowing credit of VAT/ excise duty on goods in stock to service providers/ traders.

## **In conclusion**

While considerable amount of work has been done for release of the draft law, it is evident that some more work needs to be done to remove ambiguity from some of the provisions. The release of the draft law provides significant visibility to the industry on GST structure. However, Industry would be in a position to better assess the impact on their operations once there is more clarity on the rate of GST, exemption list, fate of area based exemptions/ incentive schemes and release of various rules, such as credit rules etc.

The Government has already stated its intent that if the Constitutional Amendment bill is passed in monsoon session of the Parliament, a roll out date of 1 April, 2017 is targeted. If this stringent time limit has to be met, the Government needs to provide clarity on the open areas mentioned above fairly soon. It would enable Industry to assess the impact on a timely basis and raise the concerns on law, if any, to the Government so that there is time available for redressal of such concerns. The Government, on its part, should also institute a mechanism to understand and address the concerns of Industry.

For Industry, this is the time to kick start the various activities such as assessing the impact of GST and planning the transition. Industry would also need to effectively represent to the Government about any changes that are needed in the law to address their genuine concerns.

## ***Let's talk***

For a deeper discussion of how this issue might affect your business, please contact:

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