Remaking GST

Finance ministers from the Centre and states, on Friday, approved the pruning of the number of goods attracting the 28 per cent rate under the Goods and Services Tax (GST) from 224 to just 50, while similarly moving down several 18 per cent-rated items to the 12 per cent or even 5 per cent slabs. The motivation for the unprecedented rollback within four-and-a-half months of the roll-out of the new nationwide indirect tax regime appeared to be political (read Gujarat elections), rather than economic. There was no economic rationale, to begin with, for clamping a 28 per cent rate on almost a fifth of the goods under the GST schedule. Even now, it makes little sense for a commodity like cement to be subjected to a 28 per cent tax. How does this synchronise with the Centre's own plans of boosting job-generating construction activity through affordable housing and highway development schemes such as Bharatmala?

Normally, good economics makes for goods politics. In this case, the logic has worked in the reverse: Fear of political backlash seems to have drilled good economic sense into the GST council members and bureaucrats. The GST, it should be emphasised, was intrinsically a great reform, with the potential to transform business by creating a unified national market through taxing goods and services on a uniform value-added basis. Unfortunately, its flawed design (multiple rates, opening up the floodgates to classification disputes and lobbying by businessmen to seek concessions for their own industries) and execution (an IT backbone network prone to glitches and increased compliance burden for micro, small and medium enterprises) led to the GST's discrediting and being clubbed with the evident failures of demonetisation. There is no doubt that the back-to-back disruptions from demonetisation and a badly-desiged GST have inflicted huge collateral damage to the economy, forcing mass layoffs and shutdown of businesses. Friday's developments should hopefully be the start of making a fundamentally sound idea good in theory as well as practice.

The Centre and the GST Council should now work towards completing the rationalisation exercise by moving to a structure where 90 per cent or more items would fall under a single revenue neutral rate. That rate could be in the range of 15-15.5 per cent which was originally proposed by a committee headed by the chief economic advisor, Arvind Subramanian. There could be a small list of luxury or demerit goods (certainly not cement) attracting the top 28 per cent rate. It is fine, likewise, to charge primary produce or handicraft items at zero to five per cent. Finally, it is necessary to bring petroleum products, electricity and real estate under GST. A single revenue-neutral rate imposed on 90 per cent-plus items, minimal exemptions and ease of compliance — these would result in what is, in Prime Minister Narendra Modi's words, a Good and Simple Tax.

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