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**The "One-Ness" of One Nation, One Tax: Travails of Legislating  
GST in India**

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## The "One-Ness" of One Nation, One Tax: Travails of Legislating GST in India.

### Abstract

A decade long passage of the GST Bill in India was an exercise in testing the strength of the Indian federation. It was seen to be a touchstone of cooperative fiscal federalism. The GST was propounded as a “One Market, One Nation, One Tax” reform. In a centralized federation like India, how was this process negotiated? What were some of the issues that proved to be most contentious in arriving at a consensus, not only among the disparate states of the Union of India, but also between the Centre and States? In this paper, we analyze this much-touted GST tax reform in India using a top-down lens that investigates the process of legislating the GST in a federation. Our endeavor is to understand the accommodations and the trade-offs that were made to strike a balance in making this tax reform a truly "one" nation, "one" tax reform.

All decisions pertaining to the legislation of the GST are taken by the GST council that comprises representatives from both the center and the state. Till February 2019, around 33 GST Council meetings were held, touching on several pertinent issues. All decisions have been brought in through consensus, and the provision of voting has not been used. GST was propounded as a revenue-neutral, price-neutral and efficient tax reform. Yet, a massive tax reform of such type would have gainers and losers. Based on the analysis of the GST council minutes, we have delineated the following topics that resulted in a lot of heated debate in the council meetings:

- Compensation to the states in lieu of loss of revenue
- Composition Levy Scheme
- Cross Empowerment
- GST and the Real Estate sector

It should not come as a surprise, that in the short span of the implementation of the GST Act in the country, these very issues continue to plague its implementation. We also postulate some policy changes that would be required to deal with these roadblocks.

**Keywords:** Goods and Services Tax (GST), India, fiscal decentralisation

## 1. INTRODUCTION

The passing of Goods and Services Tax (GST) bill in 2017 was the culmination of more than a decade long process of consensus towards a major indirect taxes reform in post independent India. Hailed as a game changer, it was touted as a tax reform that would reshape the economic landscape of the country. The official economic narrative on GST was around benefits in terms of uniformity of tax structure, removal of cascading effects, efficient tax administration, improvement in government finances and the expected role of GST in formalizing the informal sector of Indian economy (Comptroller and Auditor General of India, 2010).

The critics point to the facts that cascading has been re-introduced due the multiplicity of rates and exemptions, GST has impacted the informal sector adversely, due to which it will neither lower inflation nor result in higher employment and growth (Arun Kumar, 2018).

While is too soon to arrive a conclusion on the economic narrative, either ways, we can definitely examine the political process behind the passage of the various enactments that finally made into the GST bill. Understanding this political narrative is essential, not only because it is a test of cooperative fiscal federalism, but it gives important clues to issues that will continue to plague the implementation of GST. We feel that the stresses and strains of this decade long political process give several key insights into the road-blocs in the implementation of GST. Our task is to understand the accommodations and the trade-offs that were made to strike a balance in making GST a "one" nation, "one" tax reform.

Indirect tax reform in India was a part of the structural reforms package initiated in the country, post 1990s. With the setting up of a tax reforms committee in 1991, the idea of single taxation emerged and was proposed as "Goods and Services Tax (GST)". In 2000, under the chairmanship of the then Finance Minister of the state of West Bengal, Sri Asim Das Gupta an empowered committee was formed to design a GST model with a strong and robust IT back-end. Later a task force team was formed under Vijay Kelkar in 2002, known as Kelkar committee to recommend tax reforms. In 2005, the committee recommended GST and in the 2006 budget of the Government of India, it was proposed to introduce GST by April 1<sup>st</sup>, 2010. The first discussion paper (FDP) on GST was released in the year 2009 by the Empowered Committee of State Finance Ministers with the proposed GST features. The states and Centre carried out discussions on the FDP from 2006 to 2017.

**Table 1. Chronology of the enactment of the GST Act**

<b>Year</b>	<b>Details of events</b>
<b>1991</b>	Setting up of Reforms committee
<b>1999</b>	Meeting with advisory panel
<b>2000</b>	Empowered Committee to study Tax reforms formed
<b>2002</b>	Kelkar Committee formed to study Tax reforms
<b>2005</b>	Kelkar committee recommended for GST
<b>2006</b>	In the budget the then finance Minister proposed rolling of GST by 2010
<b>2009</b>	The Empowered Committee–released First Discussion Paper
<b>2011</b>	Discussions between States and Centre started on GST
<b>2014</b>	The 122 <sup>nd</sup> constitutional Amendment Bill introduced in Lok Sabha.
<b>2016</b>	The Constitution (One Hundred and First Amendment) Act was Enacted
<b>Sep 2016</b>	The Union Cabinet on 12th September 2016 approved setting-up of GST Council
<b>Mar2017</b>	First GST Council meeting- Council Recommends the Central GST (CGST), State GST (SGST), IntegratedGST (IGST), Union Territories GST (UTGST) and Compensation Cess Act
<b>April 2017</b>	CGST, IGST, UTGST and Compensation Cess Acts passed
<b>May 2017</b>	Council recommends rules for all the acts
<b>June 2017</b>	Except J&K all states pass SGST Act.
<b>1<sup>st</sup> July2017</b>	GST launched and rolled out through the country.
<b>8<sup>th</sup>July 2017</b>	GST extended to J&K by CGST and IGST ordinances. J&K passes SGST Act.
<b>2017 to Dec2018</b>	31 GST council meetings held on various features of the GST Act

## 2. FEATURES OF THE GST

Before the Goods and Service Tax System in country, a number of indirect taxes like the Value Added Tax (VAT), excise duties, customs duties, and service taxes were collected at different rates and different stages by both the Center and the States. The taxable event under Excise Duty was manufacturing; Customs Duty was on Import and Export of Goods; service tax was on rendering of services and sales tax/VAT on sale or transfer of ownership. Schedule-VII of Constitution of India provided the power to Central and State Governments to levy these taxes. Therefore, under this regime there used to be different rates for the same commodity, in different states, which lead to a disparity between trade and lead to trade diversions. For the enactment of the GST, the 101<sup>st</sup> constitutional amendment Act enabled all the States and Centre to levy and collect taxes under concurrent jurisdiction both by the Center and States.

‘Goods and Service Tax’ (GST) is a combination of these indirect taxes of central and states. All the previously levied and collected Central taxes Viz excise duty, additional excise duty, service tax) and state taxes viz. VAT, Central Sales Tax, Horse Racing and Betting Tax, Tax on Luxuries, Entertainment Tax, tax on entry of goods, entry of Motor vehicles, cesses levied on manufacturers, distributors and consumers of goods and services throughout the nation, were now subsumed in to one tax, named goods and services tax.

Since a major reform of this nature was to be carried out for the first time, requiring a major re-haul of tax and accounting systems of businesses, the Indirect tax administration had to proactively engage with the various stake holders through awareness programs, workshops, interactions, and trade and sector wise meetings. Changing the perceptions of the stake holders and overcoming the transitional issues were the major challenges. It is being hoped that through the widening the registration base, digitization and analysis of the data will help in sustaining the revenue growth. (RaviSankar K., 2018)

All decisions pertaining to the legislation of the GST are taken by the GST council that comprises representatives from both the centre and the state. Till December 2018, 33<sup>rd</sup> GST Council meetings were held, and several contentious issues were discussed. All issues were resolved through consensus, and the provision of voting has not been used in the GST council meetings. By doing a content-analysis of the GST Council Meeting Minutes, we arrive at some issues that were repeatedly being discussed in more than three meetings. Several points of view

and differing perspectives regarding means and ends before the states (or the center and states) meant that they eluded consensus in one meeting. We have delineated the following issues:

- Compensation in lieu of loss of revenue under GST
- Composition Levy Scheme
- Cross Empowerment
- GST and the Real Estate sector

We will analyse these issues from the perspective of the Council meeting debates and discussions. Precisely because each of these issues eluded an easy consensus, we will go on to show how they are still plaguing the implementation of the GST Act.

### **3. COMPENSATION IN LIEU OF LOSS OF REVENUE UNDER GST**

The GST is a new tax with a complex structure. Its implementation too was not easy. States were rightly worried that they would lose revenue with the roll-out of GST. The centre assured the states that states that they would be compensated for any revenue loss. As per the Goods and Services Tax (Compensation to States) Bill, introduced in Lok Sabha on March 27, 2017, compensation “means an amount, in the form of goods and services tax compensation, as determined under section 7” (of the GST Act).<sup>1</sup> Compensation will be provided to a state for a period of five years from the date on which the state brings its State GST Act into force. In other words, the compensation under this Act shall be payable to any State during the transition period.

How did the GST council arrive at this consensus? One of the worries of the states was that GST was a new tax with a complex structure. Its implementation would not be easy; they would fall short of revenue in the interim period. There was also a difference of opinion between the industrialized producer states versus the less industrialised consumer states, since GST is ultimately a destination-based tax, and the tax revenues accrue to the destination states. We give below the issues raised by the various states, voicing their concerns in these meetings.

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<sup>1</sup><http://gstcouncil.gov.in/sites/default/files/GST-Compensation-to-States-Law./pdf/last/> last accessed 15<sup>th</sup> April, 2019.

**Table 2: GST Compensation – States’ Concerns.<sup>2</sup>**

States	Concerns Raised
Delhi	Requested why the year 2016-17 couldn't be taken as base year. It was over ruled saying that the figures of 2016-17 will be available much later and hence calculation will be difficult.
Jammu and Kashmir	Requested to define the term “Revenue” and expressed that base year should be the normal year as 2015-16, as floods in 2016-17 resulted in less revenue collection, and Comptroller and Auditor General (C&AG) figures may put the states in to difficulty.
Uttar Pradesh	Wanted to know the compensation formula.
Telangana	Stated that as the state is newly formed, only figures for 2016-17 will be available.
Kerala & Gujarat	Expressed that the base year should be the best three years of last ten years and requested for payment of compensation regularly.
West Bengal, Punjab, Rajasthan & Madhya Pradesh	Stated that in the lines of VAT, the compensation be given best three years out of five preceding years. West Bengal requested that the compensation be given monthly or quarterly so that the states ways and means will not be badly affected. The compensation be automatic, and IT based.
Haryana, Maharashtra, Tamil Nadu and Punjab	Concerned about the cesses which are not accounted for in the State Consolidated Fund. 11% of VAT funds transferred to local bodies, no octroi in GST, hence requested for all taxes subsumed be part of what constitute Revenue for compensation. Tamil Nadu requested for six preceding years for calculating base year revenue.
Bihar and Andhra Pradesh	Requested for the same methodology followed at the time of VAT compensation be followed for GST compensation.
Chhattisgarh, Arunachal Pradesh & Assam	Requested the current year i.e. 2016-17 as the base year as the revenue for that year was good.
Pondicherry	Requested to amend the Article 366(26B) to include union Territories in the clauses for compensation. The Council assured that

<sup>2</sup>Source: <http://www.gstcouncil.gov.in/> last accessed 15<sup>th</sup> April, 2019.

	they will get compensation directly from the centre and accepted to include in the definition.
Karnataka	Requested to create a fund as suggested by the Parliamentary committee and Finance Commission.
Mizoram	Requested to take care of North Eastern States prior to implementation of GST and expressed fear of future GDP growth as low, which will hamper them.
Tamil Nadu, Andhra Pradesh, Karnataka, Telangana & Maharashtra	Requested for immediate payment of pending Central Sales Tax (CST) compensation.

In all the discussions, the States were very vocal in stating that the existing VAT methodology should not be taken as the basis, as the compensation has to be more under GST. The final word on compensation had to consider these demands raised by the states, as seen below<sup>3</sup>:

- **Period of compensation:** The period of compensation will be five years from the date of implementation or introduction of GST in the state.
- **Projected growth rate and base year:** 2015-16 was taken as the base year for calculating the compensation, Common projected growth rate taken by assuming growth rate at 14%.
- **Base year revenue:** it was agreed that the Base year revenues consists of the revenues received by states from i.e. VAT, CST, Entry tax, local taxes, Luxuries Tax, Entertainment Tax etc, excluding the revenues received from Alcohol, petroleum products.
- **Calculation and release of compensation:** It was decided to give compensation on provisional basis at the end of every two months. The annual revenue received will be audited by C&AG and will be distributed.
- **GST compensation cess:** it was proposed to levy a cess on some goods on the recommendations of the council. The revenue from the cess will be deposited in a Fund and will be used for compensating states for the loss due to the implementation of GST.

<sup>3</sup>Source:[https://www.apct.gov.in/gstportal/gst\\_portal/pdf/GST%20ACTS/gst-compensation-to-states-act.pdf](https://www.apct.gov.in/gstportal/gst_portal/pdf/GST%20ACTS/gst-compensation-to-states-act.pdf) last accessed 14<sup>th</sup> April 2019.

- **Capping of Cess:** Cess to be levied on coal, Pan Masala, Tobacco and other other goods including motor cars and aerated water. There was a cap stipulated on the levy of cess on these items.
- **Unutilized money:** Any unutilised money in the Fund will be distributed at the end of the period. Out of the total 50% will be shared between states in proportion and the remaining will be distributed as part of the centre's divisible pool of Taxes.
- **Where no compensation is due:** Where ever no composition is due it is to be released in any financial year, and in case any excess amount has been released to a State in the previous year, this amount shall be refunded by the State to the Central Government and such amount shall be credited to the Fund in such manner as may be prescribed.<sup>4</sup>

### 3.1 Implementation Issues on the Distribution of Compensation to States:<sup>5</sup>

Originally as per the agreement, it was decided that the centre will distribute the loss for every two or three months and finally on the audited figures of the C&AG, but the centre started distributing the compensation out of the IGST to all the states without the proper apportionment ratio. So far, a sum of Rs. 48,178 Crores for the year 2017-18 and Rs 3,899 Crores up to May 2018 were disbursed as part of compensation to the states. This was not done on any coherent basis. Some states have gained and some have lost revenues. States have started opposing the distribution of this compensation. A key apprehension of the states is that the centre is not distributing the IGST amount based on agreed percentage of calculation and that it is doing this unilaterally. This issue was raised in the 31st GST council meeting by The Hon'ble Minister for Finance of Andhra Pradesh at length. The GST Collections up to March 31st, 2018 was one lakh Crores. The centre has deposited this amount in the Consolidated Fund of India. The centre going per the mandate of the Finance commission, distributed only 42% of this among states. But as this amount belonged both to the states and centre, only 50% is to be deposited and the remaining 50% was to be shared among the states. As per the ratio laid down by the council, Rs. 21,000crores are to be distributed among the states, treating the remaining 50% as directly being distributed to the states. In this instance, the states would have got Rs. 71,000 Crores instead of Rs. 42,000 Crores, which was distributed, resulting in a loss of Rs. 29,000 Crores to the states. All the states have called for immediate distribution of the

<sup>4</sup><http://gstcouncil.gov.in/sites/default/files/GST-Compensation-to-States-Law.pdf> last accessed on 15 april2019.

<sup>5</sup><http://gstcouncil.gov.in/sites/default/files/GST-Compensation-to-States-Law.pdf> last accessed on 15 april2019.

remaining amount. Therefore, in this case, we feel that the Centre should re-calculate the compensation as per the ratio laid down, especially with regard to IGST. All the revenue figures be audited by C&G for apportionment of final amount and any unutilized be dispersed among all the states.

#### 4. COMPOSITION LEVY SCHEME

The composition levy scheme was another issue that was deliberated heatedly in the Council meetings. By design, the economics of the GST regime favours (a) formalisation and (b) scale and vertical integration. Therefore, large companies in the organized sector are the ones most adept to benefit from it. The composition scheme was aimed at benefitting the small traders in the unorganized/informal sector from heavy tax burden and filing returns. Initially it was thought to fix the composition limit at 50 lakhs, but with increasing demand from states, Trade bodies, and associations it was raised to 1 crore and a proposal was made to extend or increase the threshold limit to 1.5 crore with certain exceptions to North Eastern states. Bifurcation of dealers based on their turnover and taxability was an issue from the beginning. The scheme of composition was not new to State administration unlike Centre, since under VAT the composition scheme was extended to small traders whose turnover was below 50 Lakhs per annum, with a flat rate of 1%. The debates and discussions in the GST Council meetings based on the numerous representations received from trade, commerce and Industry is given below:

**Table 4: GST council meetings - decisions on composition levy<sup>6</sup>**

GST council Meetings	Issues around composition levy
1 <sup>st</sup> council meeting	The threshold limit discussed at 25 lakhs other than special category states and finally suggested to be at 50 lakhs with manufacturers and service sector outside.
15 <sup>th</sup> council meeting	Notified provisions regarding composition levy and appointment of officers
17 <sup>th</sup> council meeting	The Council approved the following – For special category states – composition levy- 50 lakhs For Uttarakhand- proposal to levy at seventy-five lakhs.

<sup>6</sup><http://www.gstcouncil.gov.in/> last accessed 15<sup>th</sup> April, 2019.

	Jammu & Kashmir - it is proposed to discuss later.
22 <sup>nd</sup> council meeting	Proposal for increasing the threshold limit from seventy-five lakhs to one crore, and fifty lakhs to special category states except to J&K and Uttarakhand.
23 <sup>rd</sup> council meeting	Increase of composition limit from Rs. 1.00 crore to Rs. 1.5 crore and may also increase up to Rs. 2.00 Crores based on discussions. Composition levy tax payers are also allowed to make supply up to a limit of Rs 5 lakh for all services except for the Job Work services.

It was agreed that the dealers under composition will be given a unique identity number (GRN). After deliberations in the council it is decided to distribute dealers at 90:10 between State and centre. Section 10 of the SGST Act describes in detail about the composition levy, eligibility and its features.

#### **4.1 Implementation of the composition levy scheme and its unintended consequence on the informal sector**

The composition dealers can't make any sale of goods or services to other states, restricting their business activities to a small territory i.e within the state. It will still be a burden for them to maintain books of accounts and will cost them to maintain accountants and staff. This was seen as a problem to MSME's below a threshold limit of Rs 1.5 Crores. By the provisions in the Act, those who opt for composition will not be given Input Tax Credit and are liable to pay a tax rate @1%. They are restricted from supply of exempted goods and can't make business through e-Commerce platform as they are not eligible to deduct TCS (Tax Collected at Source). Thus, once bits and pieces of the economy start getting exempted, the seamless tax chain across the entire value addition chain envisioned by the GST falls through.

Apart from pursuing a policy to allow interstate transactions to composition levy business firms by amending the law, the only other policy option before the government relates to the broader MSME (Micro, Small and Medium Enterprises) sector of credit access and other specific problems related to this sector. The assumption being made under this provision is that so long as firms are small and informal, they can take advantage of the composition levy scheme, but as they expand they get into the formal GST tax-rate structure. The problem is that with the

geographical curtailing of businesses of such firms, how far can this assumption of growth be upheld?

A major criticism of the GST Act is its differential impact vis-à-vis the big/medium firms and the small/micro firms (mainly in the informal/unorganised sector). The small units kept out of GST fall into two categories. Those that have a turnover of less than Rs. 20 lakhs, which do not have to pay GST and those, that with a turnover between Rs. 20 lakhs and 1.5 crores. These units are covered by the composition levy. These firms are not allowed to make inter-state sales thereby limiting their market. They would not benefit from warehouse consolidation like the large firms and would still have to incur costs on computerized accounts, making them less competitive vis-à-vis the larger firms. Their problem is similar to that of firms who have not registered under GST which, would neither get ITC nor be able to offer ITC to those who purchase from them. Firms buying from such firms could pay the tax the smaller firm was liable to pay and claim ITC, (Reverse Charges) but that would raise the working capital requirement of the larger firm, further skewing the bias against buying from such firms.

Around 90% of India's total labour force is employed in the informal sector. A contraction of this sector will have considerable impact on the country's employment and growth. The activity in the "formal" sector, after all, is sustained in part by demand from the "informal" sector itself and inextricably linked with it. Expansion of the formal, in many cases is accompanied by, and encourages expansion of the informal. Claims made that the current slowdown is only transitory, that the problems caused by the GST are only "teething troubles", will be unfounded, given these linkages. The setback to activity caused by the GST is not just because of the procedural complications of the current scheme which businesses would "soon get used to", or which could just be simplified at the next meeting of the GST Council. If the informal in India is hit, then the formal too cannot escape contraction. The entire economy consequently can get caught in a downturn spiral.

## **5. CROSS EMPOWERMENT UNDER GST**

The GST is conceived to a single tax across the nation, replacing a multi tax system where both centre and state used to levy, collect taxes and administrate. Since this was now a single tax, it was desirable to have a single interface for the tax payers. Cross empowerment for both these agencies was the major issue that underwent lengthy and prolonged discussions in GST council meetings. Some of the underlying issues were:

- whether there should be cross empowerment or not,
- how to handle the existing dealers between centre and state,
- how to distribute the powers between centre and state,
- how to distribute goods and services between the two,
- the methodology to be adopted on geographical areas and
- How to maintain parity between centre and state doing the same work?

The various council meeting minutes show that this issue faced tremendous hurdles in arriving at a consensus. Underlying this issue was the key question of centre-state relations of division of administrative and adjudication powers. In the very first council meeting, it was observed that in the Goods sector, as the Central and State tax administrations were administering the same law, it would be desirable to deploy the experienced staff of the Centre and States to add to the efficiency of the system and use the available personnel optimally on the basis of the proposed protocol without having a threshold limit. As an alternative, it was proposed that there could be a clean break where taxpayers below Rs. One and half Crores administered by the States and above Rs. One and half Crores by the Centre. However, this was not agreeable to the states on the ground that above Rs. One and half Crore, duality of control already existed as they were assessed to tax both under Central Excise and VAT. It was also observed that Service Tax was a new area for States and in order to maintain stability of tax administration, it would be better that for now, the Central tax administration should continue to administer all existing Service Tax registrants. The Centre shall give training to the officers of the State Governments on Service Tax and till such time, the present arrangement shall continue.

In this meeting, the council began with the following modalities for a single interface:

- Traders and manufacturers of goods with an annual turnover of less than Rs. One and half Crores shall be under the jurisdiction of the State administration, and above Rs one and half Crores shall be administered by both tax administrations on the basis of the cross-empowerment model presented in the meeting which can be suitably modified by a Committee of Central and State Government officials.
- All existing registered service providers irrespective of the value of turnover, for the present, shall continue to be administered by the Central tax administration.
- States will also get jurisdiction along with the Centre over those service providers who get registered under GST in future and a protocol in this regard could be devised.

Specific arrangements for the training of State Government officers in assessment of Service Tax assess be made.

- The percentage of audit in all cases would be restricted to 5% of total assesses.
- Information-based enforcement powers can be exercised by both in all cases irrespective of division.

In the 2<sup>nd</sup> Council meeting, as expected, most of the states differed with the council on exclusive administration of existing service tax dealers by the centre and requested for administration by both on bifurcation. Council agreed to appoint group of officers to study this issue.

The 3<sup>rd</sup> council meeting was a key one, where provision for Cross-Empowerment to ensure single interface under GST resulted in the five options being put forth before the council. They were:

**Option 1**-Pure turnover based division where taxpayers below Rs. One and half Crore turnover administered only by State and taxpayers above Rs. One and half Croreturnovers should be administered only by the Centre. However, this was not acceptable to States as bulk of revenue comes from taxpayers with turnover above Rs. 1.5 Crore.

**Option II**- Turnover-based decision with overlap where taxpayers below Rs. One and half crore turnovers should be administered only by States and taxpayers above Rs one and half Crore turnover should be administered both with cross-empowerment. This was not acceptable to Centre as ninety three percent of the tax payers of services and eighty five percent of Value Added Tax payers have turnover below Rs. 1.5 Crore and thus it led to highly skewed distribution.

**Option III** - tax payers shall be divided based on their annual turnover and the nature of business. It was proposed that tax payers dealing with goods below Rs. one and half crore – Administrated by States. Tax payers dealing with goods above Rs. one and half crore to be administrated by both centre and states. Tax payers dealing in services to be administered by centre till states were trained. However, it was later observed that it will create a divide between goods and services. This also creates jurisdictional problems with tax payers dealing with both the services and goods.

**Option IV** - Cross-empowerment with division for specific functions in which it was envisaged to divide taxpayers only where human interface was required like audit, return scrutiny etc. as most of the other functions would be automated. It envisaged capping audit to 5% of the total number of taxpayers. Under this option, every year, both the Central and the state officials in each State shall prepare a data of taxpayers on the basis of risk parameters for audit and distribute between them either through a Protocol or on random basis. It also proposed stability in division for the purposes of audit for three years. It also envisaged that if required for other administrative purposes, the tax payers could be allocated between Central and State administrations through State level Committees.

**Option V** - Complete vertical division where the entire taxpayer base to be divided between Central and State tax administrations in a particular ratio for a period of 3 years for all purposes, including audit. The possible ratios for distribution of taxpayers between Centre and State above and below Rs. 1.5 Crore turnover could be 50%:50% or 40%:60%. It was proposed that if percentage distribution was asymmetric, then a mirror image approach shall be adopted in favour of the Centre for turnover above Rs. One and half Crore.

On the issue of administration of Integrated Goods and Services Tax (IGST) and information based enforcement action, it was pointed out that it was a Central levy and that Article 269A of the Constitution provided that IGST be levied and collected by centre.

In order to achieve single interface for audit and assessment, it was proposed that States should conduct audit or enforcement action for interstate supplies but subsequent legal action like issue of show cause notice/adjudication/appeal, etc. shall remain with the officers of the Centre.

On the subject of information based enforcement action, it was proposed that officers of the Centre and States shall act independently on the basis of intelligence. Initiation of action by one authority shall be intimated to the other and the other would not normally initiate any enforcement action for a given period of time except in cases where concrete information was available and action was authorized by an officer at a higher level.

It was emphasized that for smooth implementation of GST, co-operation between Central and State tax departments was extremely essential, especially at the field level and it would be better if strengths of each department complement the other rather than compete. It was also

pointed out that the suggestion for vertical division overlooked the fact that the human interface in GST would be minimal as most processes would be automated and there would hardly be any need to obtain any permission from the tax department for any procedural requirements.

With regard to these five options, the varying views of the States given below, points out to the interesting dynamics of fiscal federalism.

**Table 6: Cross-empowerment – States’ Concerns <sup>7</sup>**

States	Concerns Raised
Uttar Pradesh	The Council should go back to the Original decision of the Empowered exclusively handle all taxpayers whose turnover was below Rs.1.5 crore, including the audit and enforcement functions. He suggested that for taxpayers above the threshold of Rs.1.5 crore cross - empowerment model could be applied with an audit cap of 5%.
Tamil Nadu and west Bengal	Suggested a relook at the Service Tax threshold if the data presented was correct. Finally, it was decided to discuss this issue in the next meeting with actual data.
Andhra Pradesh, Tamilnadu, West Bengal and Delhi	Supported Option II.
Tamil Nadu	Stated that the State officers must be empowered to carry out administration of IGST and in its absence, GST would not function. It stated that IGST was a combination of CGST and SGST and there could be instances like false invoicing showing inter-State supply which State officials would require to verify. The representation from Tamil Nadu added that there was no bar for State administration to administer a Central law and if any clarification was required in course of its administration, the issue could be referred to any one of the Government. It was observed that the best method of apportionment of work between the two administrations

<sup>7</sup><http://www.gstcouncil.gov.in/> last accessed 15<sup>th</sup> April, 2019.

	needed to be worked out. Article 269A of the Constitution provided the levy and collection of IGST by the centre.
Punjab	The power of the Central Government under Article 269A of the Constitution could be delegated to the State Governments as was done for Article 269.
Andhra Pradesh	Stated that the traders wanted a single interface and a legal solution to this issue was possible as was done in respect of CST.
Tamil Nadu	Stated that it was a mistake to make GST a three dimensional tax. He stated that there should be only one tax and sharing its proceeds between the Centre and the States should be an internal matter.

The Hon'ble Chairperson of the council summing up the position observed that broadly two suggestions had emerged: one was to have a horizontal division with taxpayers below Rs.1.5Crore turnover to be with the States and those above to be administered on cross-empowerment model and the second was to divide the taxpayers vertically between the Centre and the State administrations. He observed that these two options or a mix of the two needed to be further discussed informally to find a political solution. The states' position was that GST was a single tax, so it was desirable to have a single interface. However, the States were of the view that small shopkeepers and traders should remain in the domain of the States; IGST was to be levied, collected and apportioned by the Union of India, and going by the language of the Constitution, single interface would not be possible. Conventionally, CBEC had been administering service tax and the crucial question was how to optimally use the machinery of the Central and State Governments.

IGST conflated this issue further. One proposal was that the present Value Added Tax (VAT) dealers could report to the State tax administration and the service tax registrants could report to the Central tax administration and that the tax payers who were registered with both the administrations, could be given a choice as to which administration to report to. Two options emerged, one proposed by Gujarat and the other by Tamil Nadu.

**Gujarat's proposal:** There should be a vertical division of taxpayers where two-third share should go to the States and one -third share should go to the Centre.

**Tamil Nadu's proposal:** For tax payers below Rs. 1.5crore, the administrative control should vest with the States and only 10% of units to be audited by the Central tax administration.

The GST Council in its 9<sup>th</sup> Meeting approved to the following decisions on cross empowerment.

- Both the Central and State tax administration shall have the power to take intelligence based enforcement action in respect of the entire value chain.
- Powers under IGST Act shall be cross empowered to the State tax administration on the same basis as under the CGST and SGST Acts either under law or under Article 258 of the Constitution but with the exception that the Central tax administration shall alone have the power to adjudicate a case where the disputed issue relates to place of supply, or when an affected State requests that the case be adjudicated by the CGST authority and for such issues of export and import as may be discussed in the Law Committee of officers and brought back to the Council for decision

Statutory provisions, i.e section 6 of SGST / CGST and Sec 4 of IGST, clearly authorizes the respective authorities to exercise powers , under the Acts, as mutually permitted.

Apex decision making body GST Council had persistent differences on cross empowerment issue, especially with respect to Place of supply rules issue under IGST. Under these circumstances, the council decided to defer the approval and issue of notifications cross empowering both the CGST AND SGST officers. And as such the officers of both Central Tax and State Tax are NOT authorized to initiate intelligence based enforcement action on the entire taxpayers' base irrespective of the administrative assignment of the taxpayer to any authority.

It is pertinent to note that the Centre proposed that SGTS / UTGST Officers shall exercise their powers except in respect of the following purposes, namely:-

- a) Any disputed issues requiring determination of place of supply under Chapter V of the IGST Act;
- b) Where one of the states involved in an Inter-State transaction requests that the case be adjudicated by the officer appointed under section 3 of the IGST Act;

The cross-empowerment issue reached some kind of a consensus in the 9<sup>th</sup> GST Council Meeting held on 16 January 2017:

- There shall be a division of taxpayers between the Central and the State tax administrations for all administrative purposes;
- Out of the tax payers below Rs. one and half Crore 90% with the State and 10% with the centre;
- In respect of the taxpayers above Rs. one and half crore, will be divided equally in the ratio of 50% between centre and state.
- With mutual consent the taxpayers shall be divided through IT help, taking the geographical location.
- The new registrants shall be initially divided one each between the both administrations. At the end of the year, out of the tax payers below Rs. one and half Crore 90% with the State and 10% with the centre and in respect of the taxpayers above Rs. one and half crore, they shall be divided equally in the ratio of 50% between centre and state.
- The division of the taxpayers may be switched between the both as may be decided by the Council;
- It shall be reviewed by the Council from time to time; both the tax administrations shall have the power to take intelligence-based enforcement action.
- Cross empowerment under IGST, to the State shall be on the same basis ( as under the CGST and the SGST Acts either under law or under Article 258 of the Constitution ), but with the exception that the Central tax administration shall alone have the power to adjudicate a case where the disputed issue relates to place of supply, or when an affected State requests that the case be adjudicated by the CGST authority and for such issues of export and import as maybe discussed in the Law Committee of officers and brought back to the Council for decision;

During the 22<sup>nd</sup> council meeting, it was proposed to issue the government notification on cross-empowerment prepared in accordance with the decisions of the Council taken during its 9<sup>th</sup> and 21<sup>st</sup> meeting. The issue of tax refunds still remained. Since a lot of ground work was still required to be done and data such as turnover details of migrated tax payers, removing from it the data of turnover of taxpayers with centralised registration, etc.<sup>8</sup>

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<sup>8</sup>Notification No. 39/2017 – Central Tax. New Delhi, the 13th October 2017.

The states opined that this could take time and for such period, a taxpayer should be given the freedom to approach any tax administration for claiming refund. The Secretary of the Council stated that this could be permitted subject to a declaration being given by the applicant that the same refund claim has not been claimed.

### **5.1 Implementation Issues regarding cross-empowerment**

Cross empowerment issues continue to plague implementation. As per an internal note circulated by the Central Board of Indirect Taxes and Customs (CBIC)<sup>9</sup> instructing the central authorities to conduct intelligence-based enforcement action i.e. inspections, investigations and audits on the dealers of both central and state has sparked off a heated debate. It states that “The authority which initiates such action is empowered to complete the entire process of investigation, adjudication, recovery, filing of appeal, etc, arising out of such action.” It relied on the minutes of the 9<sup>th</sup> GST council meeting and further stated “In other words if an officer of Central Tax Authority, initiates intelligent based enforcement action against the taxpayer, administratively assigned to State Tax Authority, the officer of the Central Tax Authority would not transfer the said case to its State Tax counterpart and would themselves take the case to its logical conclusion. Similarly, the position would remain in case of the intelligence based enforcement action initiated by the State Authorities against a taxpayer administratively assigned to the Central Tax Authority.”

In the 22<sup>nd</sup> council meeting the secretary stated that “due to persistent differences on cross empowerment for Place of supply rules issue under IGST, notifications regarding cross empowerment in respect of other matters (other than refund) could be deferred”. This shows that there is no uniformity of decision arrived on cross empowerment especially with respect to place of supply under IGST Act.<sup>10</sup> After the 22<sup>nd</sup> council meeting, till today this issue was not discussed in council meetings and no circular or notification has been issued in this regard.

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<sup>9</sup> In an official communication to the central administrative authorities, dated 5<sup>th</sup> October 2018.

<sup>10</sup>Source: <http://www.gstcouncil.gov.in/22nd-gst-council-meeting/> last accessed on 15<sup>th</sup> april 2019.

## 5.2 Action by State GST Authorities

State officers in many states have also taken a similar stand on intelligence-based enforcement. The officers of the Department have been conducting audit of tax payers allotted to state authorities and whenever any tax evasion issue has been unearthed, the audits are confined to State allotted taxpayers, leaving the tax payers allotted to central tax authorities unattended. This is resulting in non-realization of the SGST dues to the State from the taxpayers allotted to Central Tax Authorities. Powers under IGST Act cross empower the State tax administration as per the powers vested under the Central GST and State GST Acts either under law or under Article 258 of the Constitution. The exception here is that the Central tax administration shall alone have the power to adjudicate a case where the disputed issue relates to place of supply, or when an affected State requests that the case be adjudicated by the CGST authority and for such issues of export and import as may be discussed in the Law Committee of officers and brought back to the Council for decision. This dual action by the state and central authorities could create legal problems.

Section-6 of SGST Act, 2017 authorizes the officers of State tax or Union territory tax as proper officer in certain circumstances. Similarly, in the State GST Act, the words Central Goods and Service Tax replaced the State Goods and Services Act. From the above it can be understood that “.... Under intimation to the jurisdictional officers of state tax.....” mentioned in Section 6(2)(a) indicate that GST law does envisage dual control on assessee by both Central and State tax officers in all aspects. The only issue is that there should be a notification/order under SGST Act declaring central tax officers as proper officers for different sections of SGST act and vice versa. Presently enforcement actions like search/inspection and recording of statements are being done by officers of Central tax or State Tax are under powers derived from their acts read with proper orders issued there under. But real problem comes when central tax officers require giving notice demanding both Central tax and state tax and state tax officer to demand both State tax and central tax or integrated tax.

This should be resolved by way of an order or notification to that effect retrospectively. Else, it is possible to take a stand that the evidence gathered under the provisions of CGST Act alone are not valid for actions under SGST Act and leading to avoidable litigation.

The 9<sup>th</sup> GST Council decision, with respect to administrative division, between the centre and state, and permitting the authorities to exercise powers even it is allocated to the other counterpart specifying the ‘intelligence based enforcement activity’ requires some analysis in the light of administrative set up of various state, and the centre while discharging their functions as ‘enforcement authorities’. Some states are having functional administrative set up i.e the enforcement authority for audit, inspection etc is different and the adjudicating authority is different. In some states, both the functions are being discharged by the same authority. Centre’s administrative set up functional administration and, specific enforcement agencies like have All India jurisdiction. In such scenario, it is very important to define the intelligence based enforcement activity which looks to be practical also. Mere administrative division of tax payers should not lead to evade and to make other stake holder as silent spectator and to lose legitimate tax to the exchequer. The scope of cross empowerment shall be expanded to the non filers of return and bogus taxpayers. The other important aspect, of limitation of Power of supply issue to Central Authorities also may lead state subordination which is not out to be. A redressal forum between the states shall be in national tribunal which is like Central Sales Tax Tribunal, chaired by Hon’ble High court judge.

## **6. GST AND REAL ESTATE**

Real estate industry is one of the most important revenue generating sectors of the Indian economy. It contributes between 6-8% to India’s Gross Domestic Product (GDP) and is the second largest employment generating industry after Information Technology sector. From the beginning the issue of taxing real estate was under litigation with enormous complexity in valuation and distinction. GST made the real estate sector simplified by subsuming services and Goods.

The comparison between the Pre-GST (VAT) and the Post GST scenario for buyers and developers is given in the table below:

**Table 7: Taxing Real Estate**

<b>STAKE HOLDER</b>	<b>PRE GST-POSITION</b>	<b>GST REGIME</b>
Buyer	Have to pay VAT+ Service Tax + Registration Charges +	12% on semi finished flats and no GST on completed properties.
Developers/ builders/works contractor.	Developers have to bear VAT + Excise duty + Customs duty+ Entry tax etc beside CST on interstate purchases. Due to this the burden is transferred to buyers. Multiple calculations to arrive at Input Tax Credit (ITC) were a problem.	Due to GST, all taxes are subsumed. Availability of credit on inputs and accounting for of all the invoices can reduce under-recording of expenditure.

The debates carried out in the GST Council between the various states and the center, especially on the issue of contracts having a high labour component, are given below:

**Table 8: Taxing Real Estate – States’ Concerns <sup>11</sup>**

<b>States</b>	<b>Concerns Raised</b>
Telangana state	Argued that proposed that the rate of tax should be 5% for the following Works Contract services: <ul style="list-style-type: none"> <li>- Any work given to an agency prior to 1<sup>st</sup>July 2017 with a sun set clause of 2 years for such projects;</li> <li>- Drinking water projects;</li> <li>- Projects with low material and high labour component.</li> </ul>

<sup>11</sup><http://www.gstcouncil.gov.in/> last accessed 15<sup>th</sup>April, 2019.

	<ul style="list-style-type: none"> <li>- Added that Projects with high material component could be taxed at the rate of 12%.</li> </ul>
Center	<ul style="list-style-type: none"> <li>- Prior to GST, service tax of 6% was levied on normal Works Contract and the rate for the Government Works Contract was nil.</li> <li>- However, such Works Contract suffered due to VAT and Central Excise duty on construction material and no input tax credit was available for the same.</li> <li>- In view of this, the proposed tax rate of 12% with full input tax credit eligibility on input materials was a reasonable proposal.</li> <li>- As per the rough calculation done by the Fitment Committee, 12% tax rate could be recovered through the input tax credit available and keeping this in mind, it had proposed to bring the tax rate down from 18% to 12%.</li> <li>- If the rate of tax was further reduced to 5%, then the Works Contractors would be encouraged to use non-GST paid materials procured from grey market.</li> <li>- The gap could not be so high as in pre-GST period, there was 14.5% tax on cement and iron rods in all States.</li> </ul>
West Bengal	Tax rate of 12% was acceptable <b>except</b> for those Works Contract services where the material component was low, like irrigation and water supply works for which the tax rate should be 5%.
Center	If the rate of tax was kept at 5% and refund of accumulated input tax credit was blocked, there was a likelihood that, on this pretext, the contractor would charge extra from the Government and at the same time, use the so-called blocked input tax credit for payment of tax in the supply of non-Government Works Contract services.
Haryana	The subject of Works Contract services was discussed extensively and it was recognized that construction materials were evasion prone commodities, and therefore, Works Contract services should be brought under GST with full input tax credit.

Gujarat	Earlier the rate of service tax was 6% and now since the rate of tax on supply of services had become 18 %, it clearly reflected an increased burden of 12%. Therefore, it would need to be considered as to who would bear this additional burden of tax, the Government or the contractor. There was no logic in setting up a committee to look into the principles for fixing the rate of tax on Works Contract services supplied to the Government as the increase in rate of tax was clearly visible.
Center	<p>In the 22nd Council meeting, the Council proposed that</p> <ul style="list-style-type: none"> <li>- A rate of tax in case of works contract services involving predominantly earth works (that is, constituting more than 75% of the value of the works contract) supplied to the Central Government, the State Governments, local authority or a governmental authority may be reduced to 5%.</li> <li>- the rate of tax in case of works contract services involving predominantly earth works (that is, constituting more than 75% of the value of the works contract) supplied to the Central Government, State Governments, local authority or a governmental authority shall be reduced to 5%.</li> <li>- Rate of tax on Works Contract in offshore areas beyond twelve nautical miles and transportation of natural gas through pipeline shall be reduced from 18% to 12%.</li> </ul>

In the final analysis, the following changes were made with respect to taxing real estate:

- There was no GST on ready to move (completed properties) as they are treated neither a supply of service nor a supply of goods as per Schedule III of GST Act. As the transaction is not liable for GST there is no Input Tax Credit (ITC).
- For under-construction properties which are purchased under credit linked subsidy scheme GST is applicable at 8% with ITC.
- For the properties other than the credit linked ones the GST is applicable at 12% with ITC.
- There was no GST on resale of properties.
- On the purchase and sale of land there is NO GST.

- On works contract GST is 18% with ITC.
- On composite supply of contracts GST is 18% with ITC.
- On government contracts, for contracts of public utility and for affordable housing GST applicable is 12%.

## 6.1 Implementation issues regarding taxing Real Estate

The reason for lowering the GST on affordable housing was to give this sector a boost. The key implementation issue in relation to real estate is with regard to the classification of affordable and non-affordable housing (definition of affordable housing differs with regard to metro and non-metro cities) and recalculating, reversing and claiming of ITC. The following problems have cropped up:<sup>12</sup>

- No ITC on purchases from unregistered dealers increasing complexity.
- For unsold stocks of houses where ITC has been claimed, reversal of credit is a problem. For example, in a case where 10 flats are constructed and 7 are sold and three are not sold for claiming of ITC, reversal is a problem.
- In a scenario where construction is linked to the payment on construction of the property phase wise, and where ITC is to be reversed, will lead to additional cost on the project.
- The capital goods are ineligible for ITC and also increases expenditures. The proportionate reduction of ITC was another problem. The stock of capital goods as on 1-4-2019 needs complex calculations.

These reasons could lead to a temporary hike in prices of housing to consumers. This also leaves open several other issues: projects having residential cum commercial units and projects that are still work-in-progress.

Real estate and construction fall largely under the informal sector of the economy. It will persistently face issues of inputs bought from a buyer without GST or inputs available from registered suppliers who have not deposited tax.

Some alternatives that could be suggested are reducing the overall GST rate from 18 % to 12% and for approved affordable housing projects from 12% to 6%. In order to discourage tax

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<sup>12</sup>Source: <https://epaper.ntnews.com> dated 2 march 2019

avoidance practices, if 80% of purchases are to be made from registered dealers, the shortage will be liable for GST on reverse charge basis @18%. This will be checked on yearly basis. Deficiency to be paid within two months of year end, else it could be subject to interest. Any cancellation of booking after 31-3-2019 may be subject to audit to checks. All supplies made before 1-4-2019 shall be subject to section 14 of CGST, Act 2017 for determining affective rate of tax.

These recommendations might ameliorate the problems of a sector that is undergoing recession and burdened with unsold inventory. They would also benefit the consumer, and more importantly, since the real estate sector has several linkages with the other sectors of the economy (steel, cement for example), a boost to this sector could have a multiplier effect. And most crucially, the council has to clarify from whose account GST has to be paid in case of a sale of property.<sup>13</sup>

## 7. CONCLUSION

GST in India is a reform that is still a work-in-progress. There have been several claims made with regard to its revenue buoyancy, transparency in administration and accountability, minimum interference by the bureaucracy, leading to a decrease in the corruption at the administrative levels. Undoubtedly, with the abandoning of check posts between states, the efficiency in the logistics for big businesses has improved. The transparent procedure of refunds gives impetus to the formal industry in restructuring their finances. However, question mark on increased accounting hurdles for small businesses and the overall multiplicity of rates and exemptions leading to complexity of the tax persist.

In this paper, our aim was to look at the process of legislating this complex law, through the minutes of the GST council meetings. We were keen to delineate some of the niggling issues that were resolved only after several contentious debates among states, and between the centre and states. The questions raised during these debates, to us, were not only a key to understanding the political economy of a federation, but also markers for expected glitches during the implementation of this law.

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<sup>13</sup>Source: <https://epaper.andhrajyothy.com/c> dated 8th April 2019.

Distribution of compensation as per the compensation act and also methodology followed has become a pressing problem. States are under unrest due to this process. The compensation issue has to be discussed at length in the Council meetings in such a way that states facing a loss in receiving the IGST component should be compensated for their loss. This is imperative for the states to develop trust and confidence towards the centre.

The composition scheme took care of some problems of the small traders, but disallowing ITC, interstate transactions and restricting the services is seen by them as a major hurdle. It goes against the intended promise of the GST in formalising the economy; not to speak of the unintended consequences in terms of growth and employment; since India still relies heavily on this sector. In case of composition dealers, the government has to go beyond giving incentives to MSME's and small-scale sectors whose threshold is below 1.5 Crores. Another important legal hurdle was with respect to cross empowerment. Though there was no necessity for any circulars and notifications required on this as per decision of 9<sup>th</sup> and 22<sup>nd</sup> Council Meetings, but it will be good if the council takes a decision and issues clarifications. Cross-empowerment is an understanding between the centre and states by mutual agreement. The real estate sector continues to be bogged down with questions of claim-reversals and reclaiming of ITC. Some clarity in understanding of the ground realities of this sector would ameliorate the problems it is facing.

To be fair to the GST Council, it is working on a real-time basis and has made a number of changes. However, such a major tax reform can only be stabilised through an ear to the ground approach and a continuous coordination between Government (both centre and state) and the various stake holders.

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**ABBREVIATIONS:**

C& AG: COMTROLLER AND AUDITOR GENERAL

CBEC: CENTRAL BOARD OF EXCISE AND CUSTOMS

CBIC: CENTRAL BOARD OF INDIRECT TAXES AND CUSTOMS

CGST: CENTRAL GOODS AND SERVICES TAX

CST: CENTRAL SALES TAX

DGGI: DIRECTOR GENERAL OF GST INTELLIGENCE

EC: EMPOWERED COMMITTEE

FDP: FIRST DISCUSSION PAPER

GDP: GROSS DOMESTIC PRODUCT

GST: GOODS AND SERVICES TAX

IGST: INTEGRATED GOODS AND SERVICES TAX.

ITC: INPUT TAX CREDIT

MSME: MICRO SAMLL AND MEDIUM ENTERPRISES

RCM: REVERSE CHARGE MECHANISM

SGST: STATE GOODS AND SERVICES TAX

TCS: TAX COLLECTED AT SOURCE

TDS: TAX DEDUCTED AT SOURCE

UGST: UNION GOODS AND SERVICES TAX

VAT: VALUE ADDED TAX