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IMPACT OF GST ON REAL ESTATE AND AUTOMOBILES SECTOR

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ABSTRACT

One of the crucial reforms, changing the landscape of indirect taxation in India is the introduction of Goods and Services Tax (GST), to be implemented from 1st July, 2017. It is after a lot of amendments and deliberations that this act has seen the light of the day. The proposed idea is to have a single tax rate for all goods and services, charged by states and central governments, in tune with the developed nations. This paper aims to analyze the impact of GST on the real estate and automobile sector in India. The findings suggest that the sectors can benefit from GST if they are well prepared for the changes in the business environment.

KEYWORDS: Goods and Service Tax, Taxation System, Automobile, Real Estate

INTRODUCTION

Goods and Services Tax (GST) or the One Hundred and Twenty Second Amendment Bill, 2014 is soon to become a reality, with implementation in effect from July 1, 2017. It is the most awaited tax reform in India. The idea was initially proposed by the NDA government in the year 2000, when an empowered committee to design GST model was formed. Beginning that time, a number of debates have arisen relating to various aspects of GST implementation. In the budget of 2006 – 07, the then Finance Minister, P. Chidambaram, made an announcement of 1st April 2010 to be the target date for GST implementation, that was not met. Consequently, in the year 2014 The Constitution (122nd Amendment) Bill was finally passed in the Lok Sabha on 8th August 2016 and in the Rajya Sabha on 3rd August 2016. President Pranab Mukherjee gave his concurrence on 8th September 2016, post the ratification by the States and finally will be put into practice on July 1, 2017.

GST is already enforced in more than 160 countries. France was the first nation to introduce GST in 1954. Several models of GST are prevalent in different countries. For instance, National GST model exists in Australia and China, where the center levies tax and shares revenue with the states. In contrast, the USA has a state GST model where the states levy GST. India has opted for a Concurrent Dual GST model, where both the Centre and the state levy taxes. This model is followed in Brazil and Canada.

India had a complex structure of indirect taxes, including VAT, Excise duty, Service tax, Sales tax, custom duty, and local taxes, which GST intends to dismantle. Currently, there is no uniform rate of taxation of goods and services across states, which give rise to corruption and tax evasion. In the current model of GST, there will still be a number of taxes which will be outside the purview of GST, like taxes on petroleum & alcoholic products, levy on lottery and betting, stamp duties on immovable properties, Taxes on vehicles, Entertainment and Luxury taxes levied by the local bodies etc. Though GST initially proposed a single tax rate but the final version has two components - the central GST (CGST), subsuming central indirect taxes which are levied and collected by the centre, and states GST (SGST) or Interstate GST

(IGST), incorporating sales tax (or VAT), Entertainment Tax, Octroi and Luxury Tax, Entry Tax, Tax on lottery and gambling, which is levied and collected by respective states,

The basic rationale for the introduction of GST lies in the fact that it is not desirable for goods and services to be taxed separately. Experts are of the opinion that GST would boost the economic growth of the country, by about 0.9% to 1.7%, by creating a single market. This is believed to ease out the burden on the corporate sector for tax compliance and eliminate the cascading effect of taxes by providing for setting off of tax credit. However, it is important to note that these benefits of GST will only be reaped if the companies and tax collectors are well prepared to make changes in the way business is carried out.

Although it's a long road for the effect of GST to translate in terms of higher growth and employment, it is essential to see the specific impact of GST on different sectors. The present study highlights the impact of GST on two major sectors of the economy, real estate and automobiles.

REVIEW OF LITERATURE

The structure and loopholes of the Goods and Services Tax in India was examined in the first discussion paper of the Empowered Committee of Finance Ministers (2009). Poddar & Ahmad (2009) discuss different aspects of GST implementation, relating to the principles, issues, and procedures. The paper cited the introduction of GST to be the most significant tax reform in India, increasing tax compliance and transparency. Vasanthagopal (2011) focussed on how GST would be a significant improvement over the prevalent complex indirect tax system in the context of different sectors in the economy. FICCI (April 2013) emphasized GST to be a necessary condition for achieving double digit growth in India, provided all the stakeholders are prepared for the change. Mawuli (2014) suggested GST to be less than 10% in low income countries to mitigate the adverse effect of GST. Kumar (2014) highlighted GST's role in eliminating economic distortions by enabling the developing a unified national market with a common tax rate. Pinki and Verma (2014) illustrated that GST would result in a number of benefits for all the stakeholders involved, consumers, government at the central and state level. The study also highlighted robust IT infrastructure to be imperative for GST to be implemented successfully. Sehrawat and Dhanda (2015) concluded GST to result in increased output, employment and economic growth, owing to greater transparency. Caruso et al. (2016) suggested GST to aid economic development of India and also lead to an increase in the GDP by more than 2%. Khurana & Sharma (2016) point to the role of set offs available, as an advantage to the producers and consumers in the Indian economy. Rizwana (2016) found GST to have a positive impact on the employment and economic stability, thus improving the growth prospects of India. Kumar (2016) compares GST and the present system of taxation and mentions tax credit set off to be an important distinguishing factor. Lourdunathan & Xavier (2017) discuss the challenges in implementation of GST and identify prospects of GST that would benefit the producers and consumers.

The prior literature discusses GST as a concept and illustrates its benefits theoretically. Empirically, the focus on the impact of GST on economic growth, employment exists. The present study attempts to fill this research gap by empirically examining the impact of GST on the two chosen sectors of the economy – Real Estate and Automobiles sector, with significant contribution to the economic growth. The study also provides a comprehensive view on the GST implementation in this context.

REAL ESTATE SECTOR

Real estate industry contributes about 7-8% of India's GDP and it is the second largest employment generator after IT industry. Implementation of the GST will have enormous impact on the real estate sector which is as follows:

- In the case of **under-construction projects**:
    - There are many taxes and duties that a developer pays on the procurement side, such as Customs duty, Central Sales Tax, excise duty, entry tax, etc. These are subsequently passed on to the final pricing of the units and, thereby, to the buyer.
    - Buyers have to pay value-added tax (VAT) and service tax. While VAT is a state levy and its rate differs from one state to another, service tax is a central tax charged at 15 per cent.

As GST proposes to roll multiple taxes into one, it would lead to:

- Decrease in cost of construction as tax credits would be available for set off at various stages.
- Reduction in number of the tax complexities as it will roll multiple taxes into one.
- More transparency in the taxation structure for the buyer.

But it is easier said than done. As under construction projects are at different stages of construction and development would have already paid service tax and VAT for procurement of goods and services for which they will not get input credit. Hence cost reduction will be lesser than anticipated for current under construction project.

- **Works Contract, including** transfer of property in goods (whether in goods or in some other form) involved in the execution of a works contract shall be treated as "service" and tax would be charged accordingly (not as goods or partly goods / partly services). No specific valuation provision (abatement or composition) has been prescribed for works contract service so far. In case no abatement/ composition is provided, it may lead to significant increase in tax burden.
- In case of **ready-to-move-in properties**, buyers are not liable to pay any indirect tax. So, the impact of GST on buyers of resale properties is likely to be very little.
- **Stamp duty** payable on property is not subsumed in the GST. So, it could be a dampener for the buyers.
- **SEZ benefits** to continue under GST regime – supplies to SEZ to be zero rated.
- Under the current policy, infrastructure projects enjoy concessional duty benefits under various indirect tax laws, thus bringing down the cost of infrastructure projects. However, there is no clarity on concessions/exemptions for infrastructure projects under the GST regime.

Effect of GST on real estate in terms of outflow for developer & consumer will depend on the final rate of GST. GST would provide an audit trail for better control and monitoring of the sector.

AUTOMIBILE SECTOR

India's automobile exports contracted 9.7% during the first quarter of this fiscal year with a growth of approximately 1.91% over the previous fiscal year, with commercial vehicle segment leading the export growth. The automobile industry seems to be thrilled with the notion of a simplified tax regime, which can be achieved through the introduction of GST.

The current tax structure on automobiles is riddled with complexities. Currently, automobile sales are subject to six different types of tax at various rates, which includes Excise Duty, Infrastructure Cess, Octroi, VAT, Motor Vehicle Tax/Road Tax and Tax Collected at Source (TCS). At present, the excise duties on vehicles are divided into four slabs, in which the smallest tax rate is applicable to small cars. The current indirect tax provision comprises of:

- Small cars (less than 1200 cc) attract 27.6% tax (Excise Duty 12.50% + sees 1.1 % + VAT 14%)
- Medium cars (1200 cc - 1500 cc) attract 39.1% tax (Excise Duty 24% + sees 1.1 % + VAT 14%).
- Luxury cars (beyond 1500 cc) attract 42.1% tax (Excise 27% + sees 1.1 % + VAT 14%).
- SUVs (beyond 1500 cc) attract 45.1% tax (Excise Duty 30% + sees 1.1 % + VAT 14%).

Owing to different types of indirect taxes collected by the Centre and State separately, taxes paid on some of the inputs were not set-off against the final tax.

With the GST implementation, the automobile industry will be benefited in the following ways:

- Taxes levied by the Central government, such as Excise Duty and by state governments as Sales Tax would be subsumed into one tax uniform tax.
- If the proposed tax rate of 18-20% are approved, the prices of vehicle are expected to decrease by almost 8-18%, which will then lead to increase in demand for automobiles in the domestic market but will also make India-made vehicles more cost-competitive in export markets.
- All input taxes paid will be offset against the output liability of GST.
- Since CST will be subsumed in GST, manufacturers will no longer be required to have warehouses at multiple locations across states.
- The overall compliance burden is expected to decrease and bring lots more efficiency in operations.
- Due to complexities in the current tax structure Foreign investors were reluctant to invest in India, primarily because of the country's regulatory and bureaucratic complexities. A successful enactment of the new indirect tax regime would have a transformative effect on FDI in India.
- Since GST will also lessen overall production cost and hassles, thereby encouraging domestic as well as international car manufacturers to expand their businesses and make Indian products more qualitative and competitive across the world.

While the automobile industry is betting big on the new indirect tax regime, it still has some apprehensions of the same:

- How will the new rates be decided? Will there be a uniform rate for all sizes of cars? Will they all fall under the same 18-20% tax rate bracket?
- The Automobile industry has seen significant disputes under central excise valuation. The GST law continues with the concept of 'transaction value' which is a welcome measure, however the powers for rejection of the transaction value are very wide, and could lead to significant valuation disputes.
- The job work process is the backbone for automobile industry operations. The GST law treats 'job work' as a service and seeks to maintain existing excise procedures. However, some more clarity is needed in the conceptual framework for job work as it will pose as a challenge.
- Lack of clarity on subsuming of various cases applicable in the automobile industry.
- In the proposed GST system, it is not known whether the stock transfer would remain exempt from tax (at present, sales tax is not levied on Stock Transfer) or would be made taxable in the importing state; the industry needs to understand the treatment of stock transfers for input tax credit.
- Dealer incentive Schemes and MOU with the states.

Overall economic activity is expected to increase and we could expect a better GDP growth that should push demand for vehicle across categories. Impact of Tax cascading will also go away that will reduce overall cost of vehicle manufacturing as all taxes on input paid will be offset with the output liability of GST. The industry should be given sufficient lead time for adaptation before the introduction of GST.

CONCLUSIONS

One hundred and twenty second amendment, or popularly known as the GST is a landmark reform, changing the Indian economy for good. There are lots of speculations and apprehensions relating to GST, how will tax credit set off availed, who will levy, which tax and also how the actual impact of GST will differ on different sectors. This study aims to study the impact of GST specifically for the real estate and automobile sector in India.

In case of real estate, effect of GST on real estate in terms of outflow for developer & consumer will depend on the final rate of GST. GST would provide an audit trail for better control and monitoring of the sector. And in the case of Automobiles sector, it will benefit from the increase in the economic growth translating into higher consumer spending for vehicle across categories. Impact of Tax cascading will also go away that will reduce overall cost of vehicle manufacturing as all taxes on input paid will be offset with the output liability of GST. However, the industry would be able to translate all these benefits, given sufficient lead time for adaptation before the introduction of GST.

The findings of the study are pertinent to industry practitioners, academicians and policy makers. The study provides a comprehensive view on the impact of GST on the real estate and automobile sector, making it easier for adaptation. For the academicians, it is of interest a change as significant as GST which has economy wide ramifications are understood properly. Also a clear understanding of GST would help policy makers gain greater public acceptance and thus easier to migrate from the old taxation system.

In the future, studies can help understand the impact of GST on other sectors as well along with ex post impact analysis of GST on the economy.

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