

## THE GOODS AND SERVICES TAX REGIME IN INDIA: A CONFLUENCE OF LEGAL PRINCIPLES AND PUBLIC POLICY

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### Abstract

The paper attempts to delineate the concept of goods and service tax ["GST"] and its applicability in India especially in terms of public policy. The paper discusses the history of taxation laws in India with focus on indirect taxes and the various committees formed for this purpose and the subsequent recommendations made by them. The research also compares the bills introduced in the legislature on GST and the subsequent act passed to gauge the legislative intent and their consequences. The following section discusses the role of federalism within GST and how this has channeled the centre-state relations. The researcher has analyzed the role of GST council in the light of the judgment of the Union of India v. M/s Mohit Minerals Pvt. Ltd. to assess how the role of GST council within GST affects the relations between centre and state. The impact GST has had on the various stakeholders has also been made part of the article including the government, the individuals, and across the nation as well. The reasons of alcohol, petroleum not being included within GST have also been explained. The researcher has included the statistical data and its subsequent representations through charts wherever required to substantiate the arguments made. The entire research has been summed up with a suitable conclusion at the end.

**Key Words-** Goods and Service, Public Policy, Indirect Tax, Federalism, Government

### Introduction

The entire mechanism of taxation can be traced back to the Vedic period and the pre-historic period. Initially, tax was used to pay an individual (the king) for the services rendered by him to the society.<sup>1</sup> Subsequently, this notion expanded with revenue being used for the welfare of the society. From this very period, there was a clarity in the difference between the direct taxes and indirect taxes where the former was imposed on the income of the individual while the latter was imposed on availing goods and services. This includes the custom duty (*Shulka*), import duty (*Praveshya*), countervailing duties (*Vaidharana*) etc.<sup>2</sup> The modern taxation post-independence took the shape on the recommendations of various commissions such as that of Dr. John Matthai, LK Jha, Prof. Raja J Chelliah etc.<sup>3</sup> The recommendations of these led to imposition of taxes such as central excise, manufacturing level Value Added Tax (MANVAT), modified Value Added Tax (MODVAT), central Value Added Tax (CENVAT) etc.<sup>4</sup> Though the systemic implementation of the taxes significantly improved the taxation ecosystem nevertheless the problem of cascading effect remained there. Here, cascading effect means imposing tax on tax causing the increase in the prices of the goods where the ultimate burden is to be borne by the ultimate consumer of goods and services. This artificial increase in the price created a depression in the demand of the goods and services which is not considered suitable for a healthy economy. As per a study, out of the total revenue from indirect taxes, a significant share of 35-40 percent comes from merely the cascading effect of these taxes.<sup>5</sup> Although, the Value Added Tax ["VAT"] was rolled out to eliminate this ripple effect; it had a very limited effect with the reason that along with VAT there were several taxes. When there is change in taxes due to their very nature; the cascading effect is bound to be there. The period of 1990 witnessed a landmark shift in the economic policies of the nation where the government adopted the policy of liberalization, privatization and globalization.<sup>6</sup> The economy was opened for the foreign entities in India where the old laws were repealed and new legislations were introduced keeping in line with the standards adopted globally. This includes the laws governing indirect taxes as well which at that point of time were of 'origin' based in nature opposed to the practice of keeping the indirect taxes 'destination' based as followed in most of the foreign countries. This created a need for the first time to implement the Goods and Service Tax ["GST"] in India.

### Goods and Service Tax: An Introduction

GST can be defined as a tax levied on consumption of goods and services implemented based on the invoice; where the tax is accrued to the state where the final consumption is taking place rather than the earlier position where the states where manufacturing of the goods or services are being originated had the right to impose the tax.<sup>7</sup> GST was implemented in India

<sup>1</sup> Dr. Bageshree p. Bangera Bandekar, The Evolution of Taxation in India: From Ancient Civilizations to Modern Systems, Vol. 9(4), International Journal of Research Publication and Reviews (2023).

<sup>2</sup> Varun Kumar, Evolution of Tax System in India, Vol. 8(9) International Journal of Novel Research and Development, 2023.

<sup>3</sup> Goods and Service Tax (Concept and Status), Central Board of Indirect Taxes and Customs (April 1, 2019), [https://cbic-gst.gov.in/pdf/01042019\\_GST-Concept-Status.pdf](https://cbic-gst.gov.in/pdf/01042019_GST-Concept-Status.pdf).

<sup>4</sup> Ram Krishna Mandal, Value Added Tax in North-East India, 1<sup>st</sup> Ed., 2009.

<sup>5</sup> Michael Kleen, Targeting, Cascading and Indirect Tax Design, Raja Chelliah Memorial Lecture Series at National Institute of Public Finance and Policy New Delhi (February 9, 2012), <https://nipfp.org.in/media/medialibrary/2013/09/Michael.pdf>.

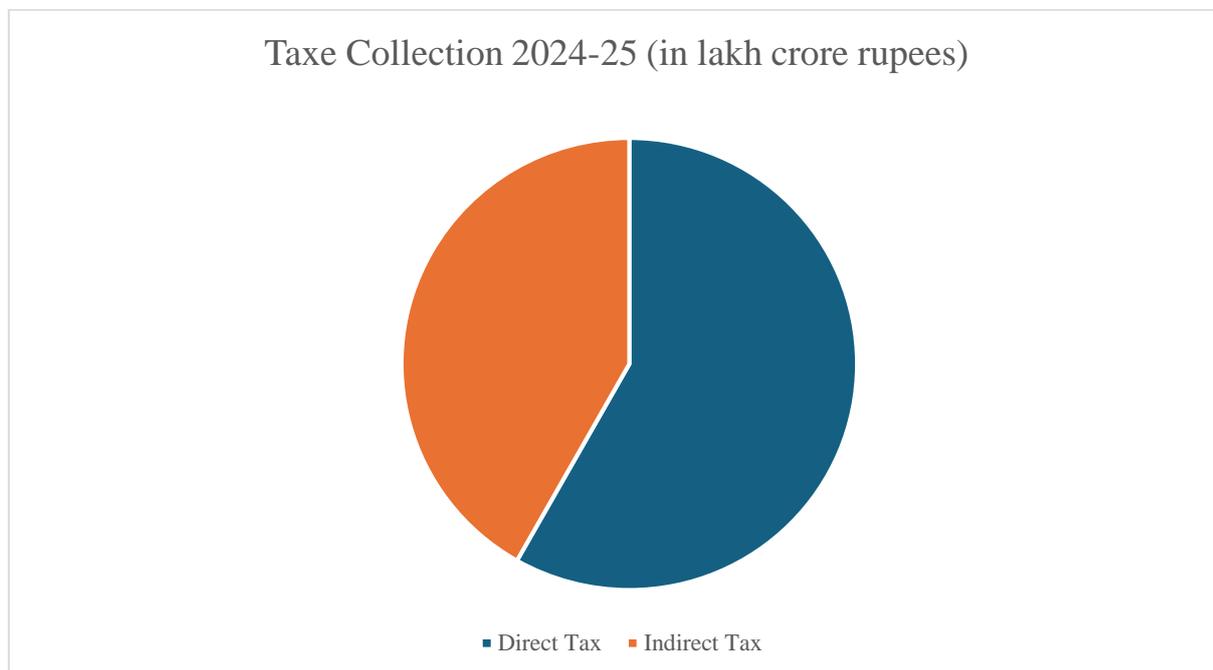
<sup>6</sup> Dr. Anju Garg, LPG Policy and Growth of Indian Economy, Vol. 8(4) International Journal of Creative Research and Thoughts (2020).

<sup>7</sup> M. Govinda Rao, Goods and Service Tax in India: Progress, Performance & Prospects, Working Paper No. 2019-02, <https://indianeconomy.columbia.edu/sites/indianeconomy.columbia.edu/files/content/201902-Govinda%20Rao%20-%20GST.pdf>.

after much deliberations and discussions. This includes the Vijay Kelkar committee, the Joint Working Group of 2007 etc.<sup>8</sup> These bodies analyzed the GST implementation in foreign countries and made certain recommendations considering the requirements in India:<sup>9</sup>

- the tax shall be levied on the ultimate consumer of the goods/ services while the intermediate shall act as a mere tax pass through.
- The dual model of GST to be adopted in India where both the centre and the state shall have the power to impose the tax where the proceeds collected shall be credited to the accounts of the respective governments.
- Both the central goods and service tax [“CGST”] and states goods and service tax [“SGST”] shall be levied on the identical base value.
- The negative list approach to be followed where the tax shall be applicable universally on all the goods and services with certain exceptions such as education, healthcare services, public service provided by the government etc.
- Exemption from GST registration where the aggregate turnover is less than 10 lakhs. Moreover, special provisions can be created for the north-eastern states. At the same time, if the individual intends to voluntarily register for the GST, then he/ she may be allowed for the same.
- Taxes such as sales tax, service tax, additional customs, entry tax etc. forming part of the earlier indirect taxes should be subsumed in the GST.

As mentioned above, GST was supposed to be a destination-based tax. This was done with a sound rationale to ensure the all-inclusive growth of the economy. When it comes to the indirect taxes, there are two approaches to levy tax i.e. origin based (originating state shall get the tax) or destination based (consuming state shall get the tax). India is divided into different states and union territories. Although, the goods and services are consumed in these different states while the manufacturing/production of these services was largely skewed towards few big states where there were majority of the factories and companies. Earlier, when the origin-based taxes were imposed, the manufacturing states were getting dual benefits in the form of not only the tax revenue but also the employment opportunities created from the manufacturing of goods/services. This also meant that there was a flow of revenue from the smaller states to the larger and more capable states. However, post the implementation of GST, this gap between the bigger and smaller states has narrowed down.<sup>10</sup> Since, the GST is destination based where the revenue share in the taxes is allocated to the states where the final consumption is taking place. This has ensured equity in the revenue allocation between the states thus ensuring the overall growth of the country. The importance of GST for the Indian economy is clear from the following diagrams:<sup>11</sup>



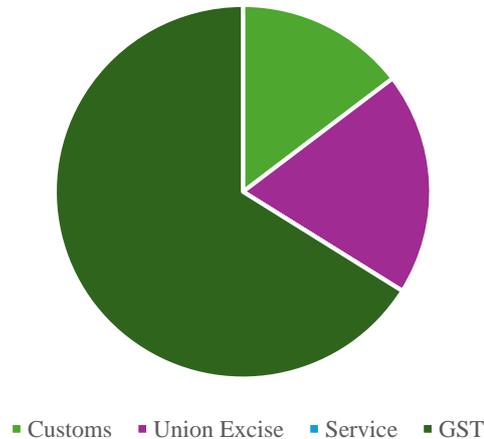
<sup>8</sup> <https://dor.gov.in/goods-and-services-tax>.

<sup>9</sup> Report of the Task Force on Goods & Service Tax, Thirteenth Finance Commission, [https://prsindia.org/files/bills\\_acts/bills\\_parliament/2014/Report\\_of\\_Task\\_Force\\_GST.pdf](https://prsindia.org/files/bills_acts/bills_parliament/2014/Report_of_Task_Force_GST.pdf) (December 15, 2009).

<sup>10</sup> Sachidananda Mukherjee, Revenue Assessment of Goods and Services Tax (GST) in India, NIPFP Working paper series, No. 385 (July 6, 2022).

<sup>11</sup> Abstract of Receipts, Receipt Budget (2025-2026), <https://www.indiabudget.gov.in/doc/rec/ar.pdf>.

## Composition of Indirect Taxes in India in lakh crore rupees (2024-25)



### GST and Federalism

In India, both the centre and the state are interdependent on each other with independence granted to each of these entities in a limited sphere under federalism. Federalism can be defined as the system of government in which the territory is governed by two different levels of government and the powers to make the laws is shared by both these governments.<sup>12</sup> Federalism has been an essential feature of the Indian constitution.<sup>13</sup> The federalism allows the necessary liberty to both the levels of government and ensures not only a participative decision making but acts as a safety valve.<sup>14</sup> The history is marred with the instances of sections advocating schism for they felt secluded in the governance and hence, federalism appears as a sort of compromise between the unionists and the separatists.<sup>15</sup> The power to impose taxes especially the indirect ones have been an inherent aspect of federalism. Before the GST, both the central government and state government had considerable autonomy in terms of the levy of the tax, the principles governing it, the rates, the procedure etc. However, GST had the capability to completely overhaul this system. In the GST, the power had to be shared between the two levels of government and had to be exercised co-jointly. Prima facie, it seems that the essence of federalism has been adhered to in GST however, on a closer scrutiny there were apprehensions from the side of states.

#### Position of Federalism in GST Council

The Indian constitution though adjusts both the central government and the state government in terms of power sharing; this power nonetheless is generally inclined in favour of the centre. This is evident from the principle of repugnancy<sup>16</sup>, the emergency provisions<sup>17</sup>, the subject matters as enshrined in article 246<sup>18</sup>, the power to admit or establish new states<sup>19</sup> etc. Under GST, the power to make the laws vest with the parliament and the state legislature on the recommendation of the GST council. The composition of GST council ensures the participation of the representatives of both central government and the state government with the position of the Chairman designated for the Union Finance Minister (of the Cabinet rank).<sup>20</sup> Further, the decisions of the GST council are required to be taken on the basis of voting where the central government holds one-third voting power while the state governments collectively hold two-third voting power.<sup>21</sup> Interestingly, the threshold to pass any agenda within the council requires a minimum of three-fourth votes.<sup>22</sup> This essentially means that for any decisions to be taken, the affirmative action on the part of the central government is a must. Taking into consideration these facts, it means that superficially there is an element of federalism within the GST regime but deep down there is an imbalance in the power factor. It is pertinent to discuss the case of Mohit Minerals<sup>23</sup> here which is essential to be discussed here. In this case, the court dealt with the role of the GST council in formulating the laws on GST. Whether the

<sup>12</sup> Dr. Rahul Tripathi, Federalism: Concept and its Importance in Democratic System, Vol. 6(5), International Journal of Management and Social Sciences Research (2017).

<sup>13</sup> M. Asas Malik, Changing Dimensions of Federalism in India: An Appraisal, Vol. 2 ILI Law Review (2019).

<sup>14</sup> Sara Chatfield, Philip Rocco, Is Federalism a Political Safety Valve? Evidence from Congressional Decision Making, 1960–2005, *The Journal of Federalism*, Volume 44, Issue 1, 2014.

<sup>15</sup> David Melding, Federalism, Union and Secession, The Federal Trust for Education and Research (2023).

<sup>16</sup> Article 254, The Constitution of India, 1950.

<sup>17</sup> Article 352, The Constitution of India, 1950.

<sup>18</sup> Article 246, The Constitution of India, 1950.

<sup>19</sup> Article 2, The Constitution of India, 1950.

<sup>20</sup> Article 279A(2), The Constitution of India, 1950.

<sup>21</sup> Article 279A(9), The Constitution of India, 1950.

<sup>22</sup> Article 279A(9), The Constitution of India, 1950.

<sup>23</sup> Union of India v. M/s Mohit Minerals Pvt. Ltd., Civil Appeal No. 1390 of 2022.

recommendations made by the GST council as outlined under article 279A is merely advisory or it has a binding effect? The hon'ble Supreme Court in this case clearly stated that the recommendations of GST council are merely advisory in nature and there are only few exceptional areas where the recommendations have a binding effect especially where the legislation itself expressly provides for the same. The court was of the opinion that the source of the power of the GST council is article 279A while for the legislature (both centre and state) it is article 246A<sup>24</sup>. Under the constitutional scheme of the country, the legislature holds the power to make laws on different subjects. On a comparison of these two provisions, the court analyzed that the non-obstante clause which gives an overriding effect to a provision is present in article 246A and not in article 279A. Had the parliament intended to give the ultimate rule making power in GST to the GST council- the 'notwithstanding' provision would have been retained. Further, the GST council makes the recommendations to the 'union' and the 'state' and not to the 'President' and 'Governor'. A necessary question which arose here was if the intention was to give the binding effect to the recommendations of the GST council; the recommendations would have been made directly to the latter. Moreover, the court also compared the 2011 bill of GST and the amendment of 2017 in the constitution. In contrast to the 2017 amendment where decisions are to be taken through voting, 2011 bill mentioned that all the decisions of the GST council shall be taken by 'consensus' of all the stakeholders of the council.<sup>25</sup>

### **GST, Federalism and States**

As stated before, the states had the power to impose indirect taxes independently prior to the advent of GST while the GST very much limited this power where the taxes had to be 'collectively' and in a 'coordinated' manner by both the centre and the states. This could have rather serious implications. Firstly, while making a comparison between the multiple indirect taxes and GST in terms of revenue generated, the earlier taxation system was largely beneficial to the governments although not suitable for the economy and the Indian markets. The compound annual growth rate ['CAGR'] in pre-GST taxes was 11.53% as compared to the 10.09% in the post GST regime for a specified period of time.<sup>26</sup> It means that for states GST would have meant not only the limited corpus but the limited freedom to impose the taxes as well. To address this and assuage the concerns of the states, the alcohol and petrol were kept out of the purview of GST. In the overall tax collection by the states through indirect taxes, petroleum<sup>27</sup> and alcohol<sup>28</sup> are the significant contributors. This ensured that states can impose taxes on these two products by themselves and adjust the tax rates according to their needs. Additionally, it is worthwhile to note that some states like Gujarat are dry states where the alcohol is no business within the state.<sup>29</sup> Therefore, keeping the alcohol within the GST would have induced states like these to modify their policies which is largely within the state list. Economists believe that petroleum and alcohol fall within the category of 'sin goods',<sup>30</sup> the consumption of which is harmful and should be controlled as much as possible which can be done by imposing higher tax rates. The governments by resorting to the old taxation mechanism have essentially complied with the same.

### **Conclusion**

The paper attempts to dissect the intersection of Goods and Service Tax and the public policy in India. The success of the mechanism of GST has largely been accepted across the globe. Today, GST is present in more than 160 countries with all the major economies following the GST model as per the domestic structure of their countries. In India, we follow the dual GST model. The move to implement GST in India is considered a historic move which replaced the indirect taxation system of the era of independence. Although, this period faced multiple amendments in laws as and when the need arose, they were still lagging when compared to the indirect taxation laws of other countries which have over the period of time shifted to the advanced GST. The domestic economy was finding it difficult to match the GST which has been accepted universally with the non-GST taxes. The reasons for this were plenty. Firstly, the implementation of different taxes with diverse application in terms of levy and procedure made it difficult to comply especially in inter-state trade. Secondly, the decision to invest in a country by the foreign companies and its investors is majorly taken on the factor of 'ease of doing business'. The earlier taxation system was peculiar as there were certain taxes exclusively for 'goods' and other taxes solely dealing with 'services'. Moreover, since each state had its own laws governing indirect taxes- it was especially inconvenient for the companies/ firms involved in inter-state supply of goods/services. This was evident from India's massive jump in Ease of Doing Business Index from 130<sup>th</sup> position to 100<sup>th</sup> position. Although, GST is considered to be a historic measure in the reformation of indirect tax structure in India; it has its own share of challenges. This includes the fake invoices being generated for the bogus input tax credit (ITC) claims, lack of beneficial initiatives for small businesses etc. In the next two years, the GST will complete a decade and the things have run rather smoothly. The GST has covered a long distance and still it has a long way to go and will be a major factor in realizing the dream for India to be a 'five-trillion economy'.

<sup>24</sup> Article 246A, The Constitution of India, 1950.

<sup>25</sup> Section 12(8), The Constitution (One Hundred and Fifteenth Amendment) Bill, 2011.

<sup>26</sup> Fiscal Developments: Revenue Relish, Economic Survey 2022-23, <https://www.indiabudget.gov.in/budget2023-24/economicsurvey/doc/eschapter/echap03.pdf>.

<sup>27</sup> Centre of Excellence in Fiscal Policy and Taxation (CEFT), Projection of Tax Revenue on Petroleum Products and Sales Tax and State's Own Tax Revenue (SOTR) Effort Analysis of States in India (2019), Xavier University, Bhubaneswar, (March 2019).

<sup>28</sup> Sacchidananda Mukherjee et al., Revenue Mobilisation from Taxes on Alcoholic Beverages, NIPFP Working Paper Series No. 415 (July 9, 2024).

<sup>29</sup> Asha Jadeja, Gujarat is anything but a dry state. Decriminalise liquor, use tax revenue for development, The Print, <https://theprint.in/opinion/gujarat-a-dry-state-decriminalise-liquor-use-tax-revenue-for-development/1310697/> (January 13, 2023).

<sup>30</sup> Richard M. Bird, Tobacco and Alcohol Excise Taxes for Improving Public Health and Revenue Outcomes (Marrying Sin and Virtue?), Policy Research Working Paper 7500, World Bank Group (November 2015).