
FIEO'S ANALYSIS OF NEW DRAFT MODEL GST LAW

The roll out of GST is expected to be game changer for the Indian economy. GST has the potential to transform the economic, business and fiscal landscape of India, and increase GDP growth by about 1 -1.5% per annum. The idea is to impart efficiencies into the Indian economy by subsuming various indirect taxes like excise, service tax, VAT, and entry tax into a single unified tax and creating a unified national market. Implementation of GST is also expected to give a boost to the exports of the country by rebating some of the un-rebated State taxes . However, to achieve this much awaited boost to the exports, there are several issues that need to be addressed which, FIEO feels, have not been paid due attention to in the Model GST Law released by the Government. Some of these issues are -

1. **Definition of India in Customs Act needs to be aligned with GST Act and manner of taxation of supplies originating/terminating in territorial waters and in CS &EEZ beyond 12 Nautical Miles (NM)**

The definition of India for the purpose of IGST is 200 NM and whereas for the purpose of Customs Act is 12 NM plus specified structures up to 200 NM. This can create aberrations. For example High Sea sales between 12 NM and 200 NM may be taxed twice to IGST – once as a supply and later at the time of import. There is also lack of clarity in Model GST law on manner of taxation of supplies terminating/originating in territorial waters and in Continental Shelf (CS) & Exclusive Economic Zone(EEZ) beyond 12 NM. As per definition of interstate and intra state sales given in IGST Act, these would fall in neither of the two categories.

Suggestions –

- a. Definition of India as given in Section 2(27) and (28) of Customs Act needs to be aligned with GST Act to ensure there are no aberrations.
- b. Manner of taxation of supplies originating/terminating in territorial waters and in CS &EEZ beyond 12 NM need to be specifically dealt with in IGST Act. Possibly a deeming clause can be added by which such transactions are treated as interstate transactions chargeable to IGST.
- c. Supplies within CS/EEZ between the same taxable person should not be taxed, while such supplies between two taxable persons would be chargeable to IGST.
- d. The issue of tax jurisdiction over territorial waters and in CS &EEZ beyond 12 NM would also need to be addressed – jurisdiction can be given to the Central GST authority having jurisdiction over the principle place of business of the person carrying out activity in this area.

2. Export of goods under Bond/LUT

Currently the facility of export under bond/Letter of Undertaking is available to the exporters which is preferred choice of export procedure for a large number of exporters. This facility is also available to supporting manufacturers / suppliers. It is understood that in the GST scenario this facility is being done away with and exporters will be expected to export on payment of GST taxes and claim refund. This would have a huge impact on exporters. Not only would the procedure be onerous, it would add to the working capital requirements of exporters. This will impact the liquidity particularly of MSME exporters.

Suggestion –

The facility of export under bond/letter of undertaking should continue in the GST regime.

3. Zero Rating of export of Non -GST Products

In normal course, credit of GST would not be allowed on inputs, input services and Capital Goods used for manufacture of non-GST products and would, therefore, be embedded in the cost of such non-GST goods. In case such non GST products are exported ,the GST paid on such inputs, input services and Capital Goods would also be exported and make the exports un-competitive.

Suggestions –

There has to be a mechanism under GST law for complete zero rating of export non-GST goods (Petroleum products, alcohol etc) including the GST embedded in the cost of such goods. An easy mechanism for this would be-

- a. In case a manufacturer/supplier is engaged in manufacture/supply/export of both GST and non-GST goods, he should be allowed credit of GST paid on inputs/input services/CGs used in manufacture/supply/export of non-GST goods and use the same for payment of GST on GST goods. In-case, he is unable to utilize this credit then refund should be permitted after a specified period say 3 months.
- b. In case a manufacturer/supplier is engaged in manufacture/supply/export of only non-GST goods, he should be allowed refund of GST paid on inputs/input services/CGs used in manufacture/supply of non-GST goods that are exported.
- c. Fixing drawback rates for non-GST products

4. **Treatment of composite supplies in the course of import/export**

Whether the supplies of services along with the goods are to be treated a part of the value of the goods or as an independent service is a moot question . If they are treated as part of the goods, they will be liable to be assessed at the lower rate in respect of merit rate goods or else at a higher rate in respect of services. This will also impact the place of supply as well as time of taxation.

Suggestions -

Valuation should be done for both purposes as per Customs Act; but no dual levy on service portion again (as at present e.g. freight). Rule of ‘dominant nature test’ propounded by the Supreme Court in BSNL case needs to be adopted.

5. **Exemption of GST on goods or services imported into/exported out of SEZs**

In terms of Chapter- II & Section 7 of the SEZ Act 2005, any goods or services exported out of, or imported into, or procured from the Domestic Tariff Area by, i) a Unit in a Special Economic Zone; or ii). a Developer; are exempt from the payment of taxes, duties or cess under all enactments specified in the First Schedule.

Suggestion -

Exemption from Goods and Services Tax on any goods or services exported out of, or imported into, or procured from the Domestic Tariff Area by, i) a Unit in a Special Economic Zone; or ii). a Developer should be incorporated by amending SEZ Act First Schedule by a Notification in terms of SEZ Act Section 54.

6. **Alignment of GST Act with SEZ Act.**

- a. Definition of Import and Export in the GST law is aligned with Customs Act but not with SEZ Act. Thus, a number of transactions, in particular to and from SEZs with DTA will become subject to CGST and SGST in case of intra-state transactions and subject to IGST in case of inter-state transactions. This will create many issues on domestic procurement of goods by SEZ Units / Developers. Particularly, if supplies to SEZ is not taken as exports, domestic producers will be at disadvantage vis-à-vis imports.
- b. Duties of Customs for Imports from SEZs are charged under Section 30 of the SEZ and not in terms of the Customs Act.
- c. Exemptions from Central Excise is provided presently in Section 3 of the Central Excise Act. Thus, there is no such mention in the SEZ Act. This provision under Central Excise Act is the base on which the whole edifice of SEZ concept stands.
- d. Whether the supplies to and from SEZ to another State be treated as inter-state or as imports / exports. Clarity necessary to protect special status of SEZ and also for providing level playing field to domestic producers.
- e. IGST Act for inter-state sale is at considerable variance from Customs Act e.g. valuation, point of taxation, etc. Divergence of law would lead to uncertainty and compliance risk for producers.

Suggestions -

- a. Since SEZ overrides all other legislations. It is advisable to match the two definitions of 'import' and 'export' as well as treatments.

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- b. SEZ Act needs to be amended to provide exemption from both CGST and SGST. Similar exemptions may be extended to SEZ Act to non-GST products also.
 - c. Supplies to SEZ need to be treated as exports and supplies from SEZ need to be treated as imports.
 - d. IGST Act and Customs Act should be preferably aligned in terms of concepts like valuation, PoS etc for a level playing field. Variance would also lead to a compliance nightmare.
 - e. IGST on imports should be levied as a countervailing duty through amendment of section 3 of the Customs Tariff Act and not under the IGST Act.

7. **Introduction of concept of ‘supply in the course of exports’ similar to Section 5(1) of CST Act.**

Currently, Section 5(1) of CST Act explains the concept of **sale** in the course of exports of the goods out of the territory of India

Suggestion

In terms of proposed Article 286, Parliament will need to either amend the said Section 5(1) or frame a new legislation to explain the concept of supply in the course of exports of the goods or services or both out of the territory of India. While doing so, under Article 286(2), the following supplies need to be treated as exports:

- a) Supplies from Indian territory to SEZ and any export oriented unit as prescribed under FTP
- b) Supplies to Notified Deemed Export Project, including to Authorisation holder
- c) Supplies by Supporting Supplier

Note - Currently, sales to SEZ are governed by the State specific VAT Laws, where different practices are adopted by

States while granting exemption / refund. Further, no VAT exemption is currently extended by the State Government on sales to Projects Notified by Central Government, including sales by Supporting Manufacturers. GST will give a unique opportunity to bring uniformity in practise and ensure effective zero rating of supplies to his critical export related sector of the economy.

8. Special Fiscal provisions for SEZ under GST regime

In terms of Chapter VI, Section 26 of SEZ Act 2005, Special Fiscal Provisions have been provided for Special Economic Zones including –

- a) Exemptions, drawbacks and concessions to every Developer towards import or DTA procurement;
- b) Exemption from any duty of customs, on goods imported into, or service provided in, a SEZ or a Unit, to carry on the authorized operations;
- c) Exemption from any duty of customs, on goods exported from, or services provided, from a SEZ or from a Unit;
- d) Exemption from any duty of excise, on goods brought from Domestic Tariff Area to a SEZ or Unit, to carry on the authorized operations;
- e) Drawback or such other benefits as may be admissible from time to time on goods brought or services provided from the DTA into SEZ or Unit or services provided in SEZ or Unit by the service providers located outside India to carry on the authorized operations;
- f) Exemption from service tax on taxable services provided to a Developer or Unit to carry on the authorized operations;
- g) Exemption from CST on goods meant to carry on the authorized operations.

Suggestion -

- a) Exemption from GST should be incorporated by amending SEZ Act by a Notification in terms of SEZ Act Section 26 .
- b) Section 26 should also include Zero rating of supply of services by an SEZ Unit to a DTA Unit within the same legal entity.
- c) Exemption similar to Service Tax exemption/refund Notification No. 12 / 2013-Service Tax 01.07.2013 be issued for exemption /refund of GST.
- d) Zero rated purchases on Intra-State Transactions and for Inter-State transaction (Form –I purchases) should be continued.

9. Job Work transactions between SEZ and DTA

For operational reasons SEZ units need to send intermediate goods to DTA for Job work. The goods manufactured by DTA are either exported directly from the premises of DTA factory under Notification No 42/2001-CE (NT) or returned back to SEZ as per the permission granted by the Specified Officer of SEZ in terms of Rule 41/42 of SEZ Rules, 2006. Job work necessary to utilize the surplus production capacities existing in DTA, avoid duplication of investments in SEZ.

Suggestions

Facility of to and fro movement of goods on job work basis without payment of taxes – GST, Central Excise, VAT,etc – should be retained for meeting this imperative business requirement of SEZs.. Necessary provision should be incorporated in section 43A of the Draft CGST Law as also in IGST/SGST Acts.

10. **Procedural Issues relating to SEZs**

Duty free procurements from DTA against ARE-1 in Central Excise and Form I in respect of CST.

Suggestion –

These procedures need to be continued in the context of GST levies. Duty free procurement from DTA is necessary to provide level playing field to domestic producers;

11. **Incentives to FTWZs under GST regime**

The objective of introducing FTWZs in India has been to make India a logistics hub, similar to the likes of Jabel Ali in Dubai and other countries like Singapore and Netherlands (Rotterdam). By design, an FTWZ is intended to be designated as a deemed foreign territory in the nature of an integrated zone which is to be used as an International Trading Hub. Under the present construct of the indirect tax laws, while the Customs Act and the Excise Act deem FTWZs as a foreign territory, a similar deeming fiction has not been adopted under the Service tax law. As a result, any service activity undertaken inside of an FTWZ is liable to service tax, unless the same satisfies conditions of 'export' defined under the Service tax law. The resultant impact is that taxes are being exported out of India which only vitiates the objective of developing India into an international logistics hub.

Suggestions –

Under the GST, it is critical that FTWZs are recognized as 'foreign territory' and as a consequence the following provisions need to be incorporated -

- a) Goods imported into FTWZ are not liable to Customs duty until cleared from the FTWZ for home consumption. Upon clearance for home consumption, Customs duty should apply.

- b) Activities undertaken inside the FTWZ (whether manufacture or services) should not be taxable, being an activity undertaken outside India; suitable provisions need to be incorporated
- c) Goods and services supplied to the FTWZ should be considered as 'export' i.e. zero rated

12. **Retention of concept of supporting manufacturer**

Supporting manufacturers play a key role in exports from the country for which several benefits/exemptions are given to them.

Suggestions –

Exemptions/benefits given to supporting manufacturers under Excise Act and CST Act as well as in some VAT legislations need to be retained. Current concept of Supporting Manufacturer should be replaced with the concept of Supporting Supplier of goods and services.

13. **Continuation of Export promotion Schemes**

- a. Export Promotion Schemes by way of Advance Authorisation , EPCG allow exemption from Customs duties subject to specified end use. No clarity in GST with regard to exemption from IGST on such instruments . Capital Goods, Raw material and inputs required for export production must be allowed to be procured / imported without any taxes. This is necessary to retain export competitiveness of domestic producers.
- b. Currently the post-import duty credit scrips are being allowed to be used for the purpose of paying Central taxes and duties. There is no mechanism by which such duty credit scrips can be used to pay State Taxes. These scrips are an important component of export benefit schemes that benefit both manufacturer and trader exporters.

- c. Tax credits are not required to be reversed in cases of deemed exports under the present Rule 6(6) of the CCR. There is no such provision at present as the definition of exports is narrow. This will place a huge burden in respect of such deemed exports and make domestic producers non-competitive, vis-à-vis imports. All deemed exports are supplies by domestic producers, where imports at Nil Customs duty is permitted.
- d. There is no clarity on treatment of 100% EOUs / STP. At present the Scheme operates under suitable Exemption Notification issued under Central Excise Act. EOUs constitute a significant portion of country's exports. In case the Scheme is not provided for under GST law, exports would suffer.

Suggestions –

- a. All the export promotion schemes- Advance License, EPCG, Advance Authorization, 100% EOUs etc – which have played a stellar role in promoting country's exports should be continued under GST regime.
- b. Under GST, as the payment of the taxes (Central and State) shall be routed through GSTN, there is a possibility to permit the exporter to also utilise the duty credit scrips to pay SGST in addition to CGST and IGST.
- c. Suitable mechanism needs to be incorporated in the GST Act providing for non-reversal of credits in case of deemed exports similar to the current provisions in rule 6(6) of CCR.

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