

## Chapter I : Implementation of GST

This chapter gives an overview of the features of the Goods and Services Tax (GST) including GST returns mechanism and the status of implementation of GST.

### 1.1 Background of GST

A comprehensive GST based on the Value Added Tax (VAT) principle was first suggested by the Kelkar Task Force in December 2002. The introduction of GST in India was first announced in the Union Budget 2006-07. Since then the Empowered Committee of Ministers had worked on preparing the background material for GST and the draft GST Acts. Implementation of GST finally materialised with the Parliament passing the Constitutional Amendment Act in September 2016, followed by the State Legislatures and GST was rolled out with effect from 1 July 2017 (including Jammu and Kashmir with effect from 8 July 2017).

***As stated by the President of India Sri Pranab Mukherjee on the launch of GST from the Central Hall of Parliament on 30 June 2017, “GST is the result of a broad consensus arrived at between the Centre and the States and is a tribute to the maturity and wisdom of India’s democracy”.***

### 1.2 Concept of GST

#### 1.2.1 Definition of GST

GST is a tax on supply of goods or services or both and a single tax on entire value chain of supply, right from the manufacturer to the consumer. Credit of input taxes paid at each stage will be available in the subsequent stage of value addition, which makes GST essentially a tax only on value addition at each stage. The final consumer will thus bear only the GST charged by the last dealer in the supply chain, with set-off benefits at all the previous stages.

GST is a consumption based tax i.e. tax accrues to the State where goods and / or services are finally consumed.

### 1.2.2 Taxes subsumed

GST subsumed the following central and state taxes: -

Central Taxes subsumed	State Taxes subsumed
<ul style="list-style-type: none"> <li>• Central Excise Duty (except five Petroleum<sup>1</sup> and tobacco products)</li> <li>• Additional Excise Duty</li> <li>• Service Tax</li> <li>• Additional Customs Duty commonly known as Countervailing Duty</li> <li>• Special Additional Duty of Customs.</li> </ul>	<ul style="list-style-type: none"> <li>• State Value Added Tax (VAT)/Sales Tax (except five petroleum products and alcoholic liquor for human consumption)</li> <li>• Entertainment Tax (other than the tax levied by the local bodies)</li> <li>• Central Sales Tax (levied by the Centre and collected by the States)</li> <li>• Octroi and Entry tax</li> <li>• Purchase tax</li> <li>• Luxury tax</li> <li>• Taxes on lottery, betting and gambling</li> </ul>

Central / State Excise duty and VAT would be continued on five Petroleum products, which would be subject to the levy of GST whenever notified on the recommendation of the GST Council. Tobacco products could be subjected to both Central Excise duty and GST. Alcoholic liquor for human consumption had been kept outside the ambit of GST.

### 1.2.3 Components of GST

There are three components of GST as follows: -

- **Central Goods and Services Tax (CGST)** : payable to the Central Government on supply of goods and services within the State/Union Territory.
- **State/Union Territory Goods and Services Tax (SGST/UTGST)** : payable to the State/Union Territory Government on supply of goods and services within the State/Union Territory.
- **Integrated Goods and Services Tax (IGST)** : in case of inter-state supply of goods and services, IGST is levied by the Government of India. Equivalent

<sup>1</sup> petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel.

IGST is also levied on imports into India. IGST shall be apportioned between the Union and the States as per the provisions of IGST Act.

- **GST Compensation Cess:** In addition to GST, a cess named GST Compensation Cess can be levied on notified goods and services and currently such cess is levied on pan masala, tobacco, aerated drinks, cars and coal.

### **1.3 Key legislations**

The Constitution (One Hundred and Twenty Second Amendment) Bill, 2016, for introduction of Goods and Services Tax in the country was passed by Rajya Sabha on 3 August 2016 and by Lok Sabha on 8 August 2016. Consequent upon this, the President of India accorded assent on 8 September 2016, and the same was notified as the Constitution (One Hundred and First Amendment) Act, 2016.

The following Acts were passed for implementation of GST with effect from 1 July 2017: -

- The CGST Act, 2017;
- The UTGST Act, 2017,
- The IGST Act, 2017;
- The GST (Compensation to States) Act, 2017

The above Acts were assented by the President of India on 12 April 2017 and enacted with effect from<sup>2</sup> 1 July 2017. In addition to the above, each of the States have also passed the SGST Act.

All the above Acts were further amended vide the CGST Amendment Act, 2018 and the GST (Compensation to States) Amendment Act, 2018, the IGST (Amendment) Act, 2018 and the UTGST (Amendment) Act, 2018 notified on 29 August 2018 and made effective from 1 February 2019.

### **1.4 New factors in GST**

Some of the notable factors introduced in GST, which were not there in the pre-GST era, have been detailed below : -

#### **1.4.1 GST Council**

In terms of Article 279A (1) of the Constitution of India, as amended, the President of India constituted the GST Council with effect from 12 September 2016. The GST Council is a constitutional body for making recommendations to the Union and the State Governments on the issues related to GST. The

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<sup>2</sup> applicable to the State of Jammu and Kashmir with effect from 8 July 2017 after the State passed these Acts as Extension to Jammu and Kashmir Acts in view of Article 370.

GST Council, a joint forum of the Centre and the States, is chaired by the Union Finance Minister and members are the Union State Minister of Revenue or Finance and Ministers in-charge of Finance or Taxation or any other Minister nominated by each of the States.

As per Article 279A (4), the Council will make recommendations to the Union and the States on: -

- a) the taxes, cesses and surcharges levied by the Union, the States and the local bodies which may be subsumed in the GST;
- b) the goods and services that may be subjected to, or exempted from GST;
- c) the model GST Laws, principles of levy, apportionment of GST levied on inter-State trade supplies and the principles that govern the place of supply (POS);
- d) the threshold limit of turnover below which goods and services may be exempted from GST;
- e) the rates including floor rates with bands of GST;
- f) any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster;
- g) special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand; and
- h) any other matter relating to the GST, as the Council may decide.

While discharging the functions conferred by this article, the GST Council shall be guided by the need for a harmonised structure of goods and services and for the development of a harmonised national market for goods and services.

#### **1.4.2 Goods and Services Tax Network**

Goods and Services Tax Network (GSTN) was registered on 28 March 2013 under Section 8 of the Companies Act, 2013 as a Non-Government Company and a 'Not for Profit Organisation'. It was formed to provide common and shared Information Technology (IT) infrastructure and services to the Central and State Governments, taxpayers and other stakeholders for implementation of the GST.

The Government of India holds 24.5 per cent equity in GSTN and all the States of the Indian Union, including NCT of Delhi and Puducherry and the Council, together hold another 24.5 per cent. The balance 51 per cent equity is with Non-Government financial institutions. It was decided (May 2018) to

convert GSTN into a fully owned Government Company. Further action on this decision was yet to be taken by the Government.

The objectives and organizational structure have been further detailed in Chapter III of this report.

### **1.4.3 Cross empowerment and distribution of taxpayers**

Under GST, the taxpayers have to obtain separate registration in each State where they operate. A single challan is generated for paying all taxes of GST (viz. CGST, IGST, SGST and UTGST) under each registration and one single return is filed for both the central and state taxes.

In view of this dual control, the GST Acts provide for cross empowerment of the Central and State tax officers to administer all the components of GST viz. CGST, SGST, UTGST and IGST. The tax officers carry out administration of all components of GST in respect of the taxpayers or specific areas allocated to them. While the State Commercial tax departments are responsible for administering functions assigned to the States, the Central Board of Indirect Taxes and Customs (CBIC) and its field formations carry out functions assigned to the Centre.

As per circular of the GST Council dated 20 September 2017, the following criteria should be followed for the division of taxpayer base registered in a State between the Centre and the State to ensure single interface :-

- a) Of the total number of taxpayers with turnover below ₹ 1.5 crore, all the administrative control over 90 per cent of the taxpayers shall vest with the State<sup>3</sup> tax administration and 10 per cent with the Central tax administration;
- b) In respect of the taxpayers with turnover above ₹ 1.5 crore, all the administrative control shall be divided equally in the ratio of 50 per cent each for the Central and the State tax administration;
- c) The division of taxpayers in each State shall be done by computer at the State level based on stratified random sampling and could also take into account the geographical location and type of the taxpayers, as may be mutually agreed.

The State tax officers have been empowered<sup>4</sup> (October 2017) to grant refund of IGST and CGST and similar instructions on the State side were also issued empowering the Central tax officers to grant refund of SGST. The GST Council in its 9th meeting (16 January 2017) recommended that both the Central and

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<sup>3</sup> Except for the State of Jammu and Kashmir where all the taxpayers below ₹ 1.5 crore were allocated to the State.

<sup>4</sup> Vide notifications No.11/2017–Integrated Tax and No.39/2017-Central Tax, both dated 13 October 2017.

State tax administrations shall have the power to take intelligence-based enforcement action in respect of the entire value chain and CBIC gave effect to this decision through a DO letter<sup>5</sup> issued (October 2018) to its field formations.

#### **1.4.4 Compensation to the States for loss due to implementation of GST**

The Constitution Amendment Act, effective from 16 September 2016, has provided that Parliament should, on recommendation of GST Council, provide for compensation to the States for loss of revenue arising on account of implementation of GST for a period up to five years. The GST (Compensation to the States) Act, 2017 was passed to give effect to these provisions. This Act also provided for levy of a cess for the purpose of GST Compensation.

The States should be compensated for any shortfall in getting a revenue of 14 per cent over the base year (2015-16) revenue relating to taxes / duties subsumed into GST. The shortfall in revenue was to be arrived at after taking into account the SGST collection (collected as SGST as well as IGST settled as SGST) and collection of arrears of state taxes subsumed into GST. The GST compensation is payable bi-monthly and should be calculated finally for every financial year after the receipt of final revenue figures, as audited by the CAG.

#### **1.4.5 Anti-profiteering**

Section 171 of CGST Act, 2017 stipulated that any reduction in rate of GST on any supply of goods or services as compared to pre-GST tax rates, or the benefit of ITC, should have been passed on to the recipient by way of commensurate reduction in the prices. The wilful action of not changing the final price of the good or service by various means, despite the reduction in the rate of the tax for that particular goods or services, would amount to “profiteering”. The CGST Act, 2017 provided for a 3-tier structure for investigation and adjudication of the complaints regarding profiteering.

- National Anti-profiteering Authority
- Directorate General of Anti-profiteering
- State-level screening committees and standing committee

Any consumer or organisation experiencing the non-reduction in the price of the goods or services despite reduction in the rate of GST could file the complaint with proper evidences.

Any supplier, trader, wholesaler or retailer, who could not get benefit of ITC on account of reduction in the rate of GST, can also file the complaint with proper evidence. The Authority might inquire into any alleged contravention of the provisions of section 171 of the CGST Act, 2017 on its own motion or on receipt of information from any interested party as defined in the Rule 137 (c) of CGST Rules, 2017, person, body, association or on a reference having been made to it by the Central Government or the State Government.

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<sup>5</sup> D.O. F.No. CBEC/20/43/01/2017-GST (Pt.) dated 5 October 2018.

The Authority shall cease to exist after the expiry of two years from the date on which the Chairman enters upon his office unless the Council recommends otherwise.

#### **1.4.6 Pan-India roll out of E way bill**

After introduction of GST, for quick and easy movement of goods across India without any hindrance, all the check posts across the country have been abolished. The E-way (electronic way) bill has envisaged one electronic way bill, to be carried by the person in charge of conveyance, providing for a hassle free movement of goods throughout the country. The e-way bill system, a web based solution designed and developed by National Informatics Centre (NIC), has been introduced nation-wide for all inter-State supplies with effect from 1 April 2018 and has been made compulsory for movement of goods of consignment value exceeding ₹ 50,000. As regards intra-State supplies, option was given to the States to choose any date on or before 3 June 2018. All the States have notified e-way bill rules for intra-State supplies, the last being NCT of Delhi where it was introduced with effect from 16 June 2018. Different threshold limits have been fixed by different States for generation of e-way bills for intra-state supplies.

#### **1.5 Central Administrative Structure**

The Department of Revenue (DoR) of Ministry of Finance (MoF) functions under the overall direction and control of the Secretary (Revenue) and coordinates matters relating to all the Direct and Indirect Union Taxes through two statutory Boards namely, the Central Board of Indirect Taxes and Customs (CBIC<sup>6</sup>), and the Central Board of Direct Taxes (CBDT) constituted under the Central Board of Revenue Act, 1963. Matters relating to the levy and collection of GST are looked after by the CBIC.

Indirect Tax laws are administered by the CBIC through its field offices, the Commissionerates. In view of implementation of GST, CBIC restructured its field offices into 21 Zones of GST headed by the Principal Chief Commissioner/Chief Commissioner vide circular dated 16 June 2017. Under these 21 Zones of GST, there are 107 GST Taxpayers Services Commissionerates that deal with GST and Central Excise, headed by the Principal Commissioner/Commissioner. Divisions and Ranges are the subsequent formations, headed by Deputy/Assistant Commissioner and Superintendents respectively. Apart from these Commissionerates, there are 49 GST Appeal Commissionerates, 48 GST Audit Commissionerates and 22 Directorates dealing with specific functions such as DG (Systems) for management of Information Technology projects and DG, NACEN for training needs.

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<sup>6</sup> formerly Central Board of Excise and Customs (CBEC).

## 1.6 The objectives of GST

It was envisaged that GST would subsume a number of indirect taxes presently being levied by Central and State Governments into a single tax, thereby reducing the cascading of taxes and providing a common national market for Goods and Services. GST was also expected to simplify the tax regime and result in better tax compliance and a non-intrusive E tax system due to a robust IT Infrastructure. Due to the seamless transfer of input tax credit from one stage to another in the chain of value addition, GST was to have an in-built mechanism in its design that would incentivise tax compliance by trader.

### 1.6.1 Mechanisms to achieve these objectives:

The key mechanisms to achieve the objectives of GST were: -

- Unifying multiple central and state taxes;
- Simplified tax structure by eliminating multiple tax rates and introducing simplified forms and procedures;
- IT enabled compliance, with system verified seamless flow of ITC credit forming the core of IT system, providing for a single IT interface for taxpayer and IT based tax administration.

### 1.6.2 Implementation status of envisaged mechanisms

By the end of first month of roll out of GST (i.e. by 31 July 2017), 63.9 lakh taxpayers from Central Excise, Service Tax and VAT were migrated into the GST portal and 10.9 lakh taxpayers applied for new registrations. The tax payment functionality was available on the GST portal from the date of roll out of GST i.e. 1 July 2017. GST revenue amounting to ₹ 92,283 crore was collected in the first month i.e. July 2017 which included ₹ 14,894 crore of CGST, ₹ 22,722 crore of SGST, ₹ 47,469 crore of IGST and GST Compensation Cess of ₹ 7,198 crore.

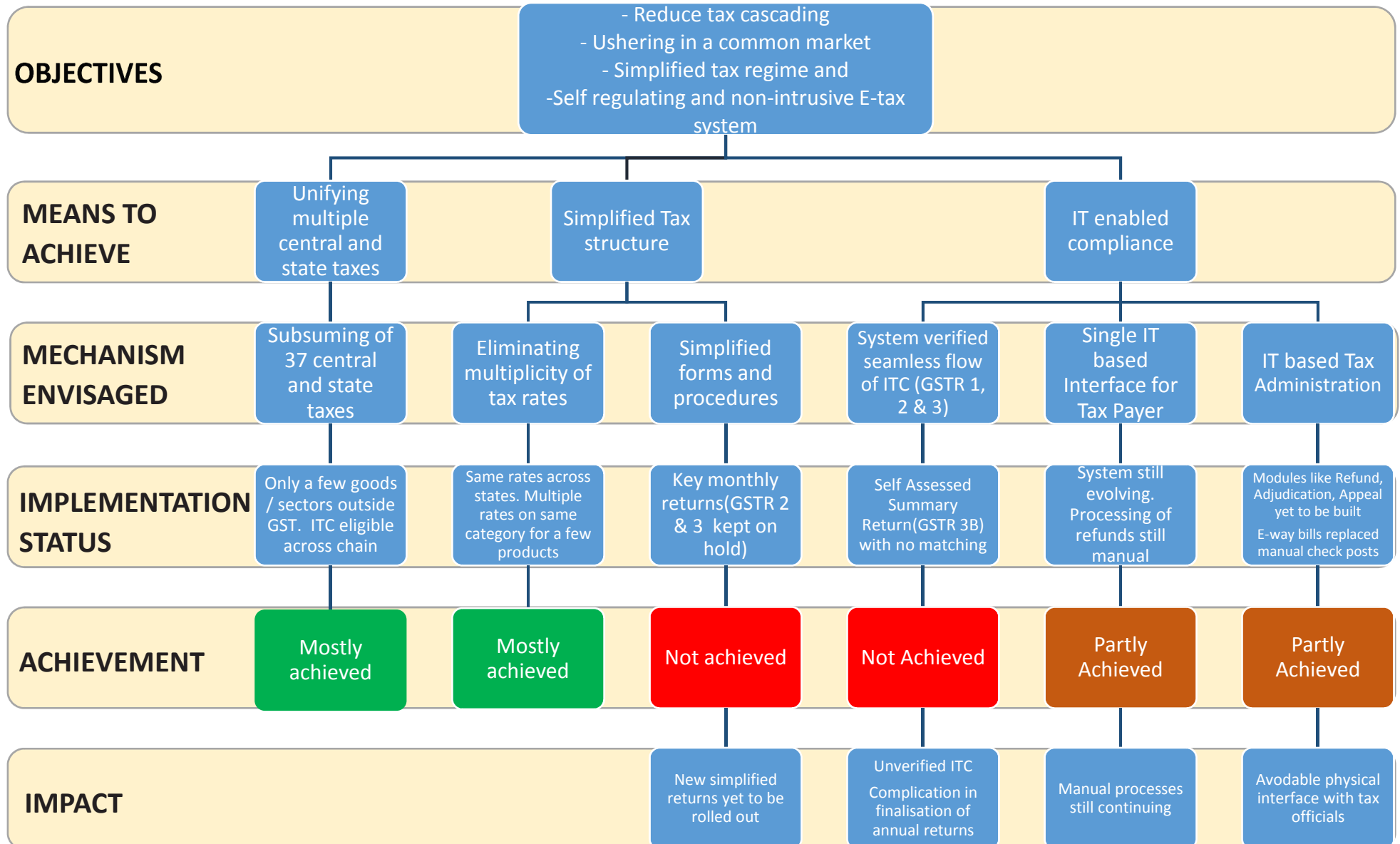
51.4 per cent of the taxpayers filed GSTR-3B return for July 2017 by due date (28 August 2017). The monthly returns GSTR-1 and 2 were released on the portal by 1 September 2017.

**But changes were made to the formats of the reports. Due dates for various key activities were postponed and GSTR-2 and 3 kept in abeyance. These changes were due to various factors like complexity of the formats or technical glitches on GST portal or the claimed lack of preparedness of stake holders and further changes triggered by these changes. As a result, GST System has remained a system still in the making even after nearly two years of roll out with the entire return mechanism undergoing major changes.**

The chart No.1 maps the objectives of the GST with the mechanisms envisaged and their current status of implementation



**Chart 1: Objectives of GST. extent of achievement and fall out**



The following is the status of implementation of mechanisms envisaged under GST, as depicted in Chart No.1.

**(a) Multiple taxes**

The objective of subsuming multiple taxes has been mostly achieved with GST subsuming 37 different central and state taxes with ITC eligible across the value chain. Only a few goods / sectors have been kept outside GST, with a provision in constitutional amendment to subsume the major product viz. petroleum products as and when decided by the GST Council.

**(b) Tax structure**

GST ushered in a tax structure in which the same good or service has been subjected to same tax rate across the States. There are four major tax slabs right now (5 per cent, 12 per cent, 18 per cent and 28 per cent tax rates) with some luxury and sin goods in the 28 per cent slab such as cars, tobacco products, pan masala and aerated drinks, being further subject to GST Compensation cess. An indicative list of GST rates on goods and services has been given in **Appendix-I**.

There are a few products where the goods or services of same nature (i.e. same HSN / SAC code) attract multiple tax rates depending on the nature of the product or the unit value of the product as illustrated in table No.1 below:

**Table No.1 : Multiple tax rates on same category of goods / services**

Foot wear	Up to ₹1000 ₹ 1000 and above	5 per cent 12 per cent
Fiber	Silk and Jute Cotton and natural Manmade	Nil 5 per cent 18 per cent
Readymade apparel	priced below ₹1000 ₹ 1000 and above	5 per cent 12 per cent
Hotels and Lodges	Tariff Below ₹ 1000 ₹ 1000 - ₹ 2500 ₹ 2500 - ₹ 7500 ₹ 7500 and above	Nil 12 per cent 18 per cent 28 per cent

From the above table, it could be seen that goods or services of same nature have been subjected to multiple tax rates.

The GST Council, through its various meetings, reviewed the slab and rate structure from time to time. Since the inception of GST, CBIC issued 47, 30 and 9 notifications relating to changing of CGST rates in 2017, 2018 and 2019 (up to 31 March 2019) respectively. Similarly, 50, 31 and 8 notifications were issued changing IGST rates in 2017, 2018 and 2019 (up to 31 March 2019) respectively.

Thus, though the tax rate structure has been simplified as compared to pre-GST tax era, there is scope for further simplification.

**(c) Returns prescribed**

In GST, the taxpayers have to file a single return for all GST taxes viz CGST, SGST, IGST and GST Compensation Cess. The basic features of the return mechanism in GST envisaged electronic filing of returns, uploading of invoice level information, auto-population of information relating to ITC from returns of supplier to that of recipient, invoice level information matching and auto-reversal of input tax credit in case of mismatch. The returns mechanism was designed to assist the taxpayer to file returns and avail ITC. The various returns prescribed in GST have been detailed in **Appendix-II**.

The GST Council announced (July 2018) that a new simplified return mechanism would be implemented with effect from 1 January 2019. These new simplified forms were yet to be rolled out (June 2019). The very need for simplifying the returns indicates that the initially designed forms and the supporting IT features were not in line with the objective of a simplified tax regime.

**(d) System verified seamless flow of ITC**

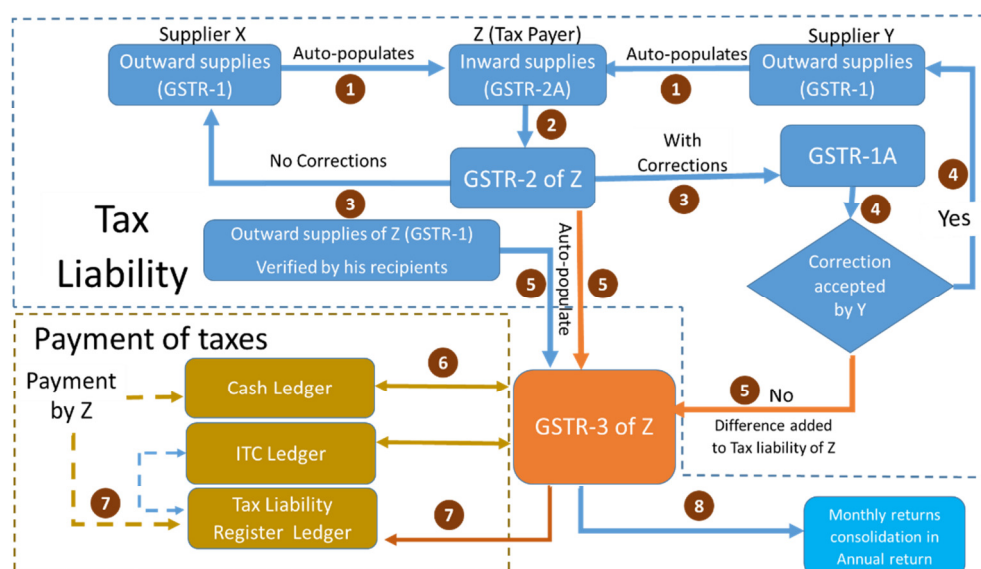
The system verified seamless flow of ITC was envisaged to be achieved through the returns GSTR 1, 2 & 3. It was originally envisaged that suppliers would file invoice-wise details of outward supplies made by them during the month through GSTR-1. The details of outward supplies so furnished by the supplier in GSTR-1 were to be made available electronically to the registered recipients through form GSTR-2A. Similarly, details of supplies relating to composition taxpayers, Input Service Distributors and Non-Resident taxpayers as well as Tax Deducted at Source (TDS) by Government departments / agencies and E-commerce operators also were to be made available electronically to the recipients. Thereafter, based on details available in form GSTR-2A, the taxpayer was supposed to furnish form GSTR-2 after including details of other inward supplies.

The details of inward supplies added, corrected or deleted by the recipient in his form GSTR-2 were to be made available to the supplier electronically in form GSTR-1A through the common portal. The supplier may either accept

or reject the modifications made by the recipient and Form GSTR-1 furnished earlier by the supplier should stand amended to the extent of modifications accepted by him.

GSTR-3 is a monthly return with the details of sales and purchases during the month along with the amount of GST liability. Most of GSTR-3 was supposed to be auto-generated from GSTR-1 and GSTR-2 while the taxpayer had to include the details of discharge of liability of tax, interest, penalty, refund claimed from electronic cash ledger and debit entries in electronic cash/credit ledger while filing GSTR-3. The flow of data and auto population of details in GST monthly returns as originally envisaged, has been shown pictorially in chart No.2 given below:

**Chart No.2: GST Returns as originally envisaged**



NB: Similarly details from GSTRs-4, 5, 6, 7 and 8 representing supplies from composition taxpayers, Non-Resident taxpayers, Input Service Distributors, Tax Deducted at Source (TDS) by Government departments / agencies and TDS by E-commerce operators respectively were also to auto-populate GSTR-2A of recipient. Only GSTR-1 has been shown in the above flow chart for illustrative purposes.

While this was the system originally envisaged and designed, the due dates of these key returns were postponed, a fortnight before launch of GST quoting lack of familiarity of the trade and apprehensions expressed with regard to the system readiness, as informed to the 17<sup>th</sup> GST Council meeting held on 18<sup>th</sup> June 2017. It was also informed to the Council in the same meeting that though the systems were ready for roll out of GST from 1<sup>st</sup> July 2017, trade and industry, specifically from the banking, civil aviation and telecom sector had requested for some more time to test the systems, get themselves familiarised and get assurance about the stability and robustness of the

system. It was further stated that though GSTN was ready, big businesses and their Enterprise Resource Planning (ERP) software were not ready and that GST Savidha Providers (GSPs) needed time to test the software.

***However, this contention is not fully justified. GSTN was formed in March 2013, the constitutional amendment to bring in GST was passed in September 2016 and it was announced in January 2017 that GST would be implemented from 1<sup>st</sup> July 2017. Even before the constitutional amendment was passed, the Empowered Committee of Ministers (ECM) had started working on the model GST Acts and business processes and the first model GST Act was placed in public domain in June 2016. The Business Process Documents on Registration, Payment, Registration and Refund were also placed in public domain during April 2015 to October 2015.*** The GST model laws were prepared by Nov 2016 and Acts passed by Parliament in April 2017. The Draft Rules on Returns, Registration, Payments, Refunds, Invoice initially prepared in Sep 2016 and the next version of draft rules duly adding ITC, Transition, Valuation and, Composition were finalised in March 2017 and approved by Council in May 2017. The draft forms (Invoice, Payments, Registration, Refund, Return and Mismatch) were finalised in Sep 2016 and further set of draft forms covering Composition, ITC, Payment, Refund and Registration were finalised in May 2017. Final rules and forms were notified on 19 June 2017.

GST is a major tax reform and Government had made its intent very clear that GST would be rolled out from 1<sup>st</sup> July 2017. Under the circumstances, it was expected that the system design would be firmed up well in advance and that the system would be robust enough to take care of changes. Even though the rules and formats were finalised very close to the roll out date, it is equally true that enough preparation could have been done on the basis of draft rules, and fine-tuned on the basis of finally approved rules.

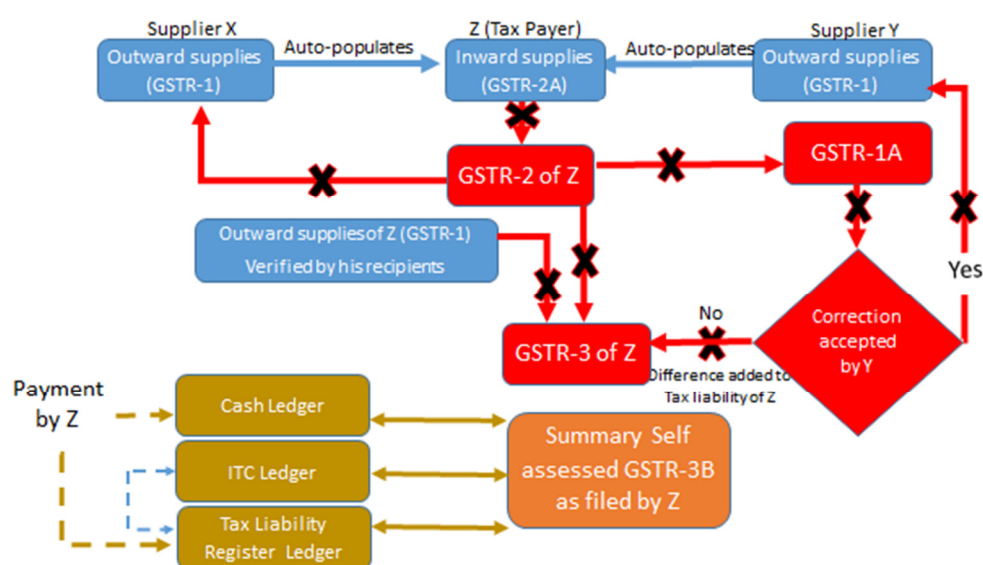
The GST Council approved (June 2017) GSTR-3B, a simpler temporary measure for two months citing lack of preparedness of industry and GSPs. GSTR-3B was designed as a self-assessed summary return which captured summary of outward supplies and inward supplies liable to reverse charge. ITC was being settled based on these self-assessed summary returns filed by taxpayers. This temporary return, initially introduced for two months, has been continued till date and GSTRs-2 and 3 have been kept in abeyance. As a result the key mechanism of system verified ITC and invoice matching was not achieved. As on date ITC as reported by the taxpayer in the summary return is used for further transactions.

In July 2018, i.e. one year after introduction of GSTR-3B putting GSTRs-2 and 3 on hold, the GST Council announced that a new simplified return

mechanism would be implemented from 1 January 2019. The new return mechanism is yet to be finally rolled out (June 2019), which is two years after introduction of GSTR-3B as a temporary measure. With the delay in framing a revised return mechanism, the summary return GSTR-3B, which is more of a self-declaration continued since the roll out of GST instead of the system-generated return based on verified invoices.

The processes and returns kept in abeyance have been shown in red colour in the flow chart No.3 depicting current status of returns.

**Chart No.3: Current status of Key GST Returns**



Currently, the IT system only captures the outward supplies as filed by supplier in GSTR-1, which can be viewed by recipient in GSTR-2A. The further processes of verification and correction of supplies by the recipient through GSTR-1A and 2 and the monthly return GSTR-3, based on matched invoice details, have been kept in abeyance.

*The sequence of events clearly points to the complexity of the format and the design of the original returns.*

**(e) Impact of keeping GSTRs-2 and 3 in abeyance**

- **Unverified ITC**

ITC claimed by the taxpayers was not system verified and ITC ledger was getting auto populated based on un-verified ITC flowing from self-assessed summary monthly return (GSTR-3B) filed by the taxpayers.

- **No self-regulating system**

As ITC and monthly returns were not based on system-verified details, the self-regulating system was not in place. Further, in the originally envisaged

returns mechanism, it could be verified if the suppliers have paid their overall tax liability as emanating in GSTR-3 from the matched outward and inward supplies, as taxpayer had to furnish payment details while filing GSTR-3. No such check could be in-built into the summary self-assessed GSTR-3B.

- **Manual check of details in returns**

In the absence of a self-regulating system, data analytics and Business Intelligence tools were being used by the tax departments to cross check data available in GSTRs 1 and 3B as well as E-way bill data. Information or clarifications had to be sought from the taxpayers in the manual form. This is disadvantageous to the taxpayers also as they have been denied a chance to get details in GSTRs-1 filed by their suppliers modified or rectified while such information was being used for verification.

- ***Roll out without key safeguards made the system vulnerable***

There were several reports of detection of fraudulent ITC claims made by certain taxpayers including use of fake invoices to claim ITC. Thus, partial roll out of GST IT system withdrawing key control mechanisms originally envisaged, without any other safeguards or impact assessment, made the system vulnerable.

- **Impact on annual returns**

The Annual return was to contain crucial information like the details of outward and inward supplies, ITC declared in returns and details of tax paid. It also has other information like demands and refunds, supplies received from composition taxpayers and HSN wise summary of outward and inward supplies.

The discontinuation of GSTR-2 and 3 has complicated the process of filing annual returns as very limited data from GSTR-2A and 3B would auto populate the annual return. The taxpayers are required to tally the data available in GSTR-1 being filed with their GSTR-3B before finalising the annual return.

It was originally envisaged in the GST Acts that the annual return pertaining to a financial year would be filed by the following 31 December. The due date for annual return of 2017-18 has been extended from time to time and the date has been finally extended to 31<sup>st</sup> August 2019.

It was envisaged in the GST law that any unmatched credit in the monthly returns should be rectified only up to the filing of annual return or filing of return for the month of September of the financial year whichever is earlier. The last date for claiming ITC on invoices relating to Financial Year 2017-18 originally was September of the financial year or submission of annual

returns whichever is earlier. Thus with the extensions, the utilisation of ITC as well as finalisation of returns of 2017-18 continue to remain open-ended.

- **Incomplete IGST settlement**

All the details required for IGST settlement or apportionment could not be captured in GSTR-3B, being a summary return introduced as a stop-gap arrangement initially. This has been detailed in the findings of IT audit of GSTN (**Paragraph 3.22 of Chapter III refers**).

When we pointed out the absence of key aspects in GST Return mechanism, resulting in the system being still a system still in the making (March 2019), the Ministry stated (April 2019) that the GST Council recommended to do away with the steps like invoice matching as a concessionary measure to give more time to the trade and industry to adjust to the new regime. They also informed that parallelly, the Government introduced alternative mechanisms to plug revenue leakages through data analytics and Business Intelligence (BI) tools. Though envisaged as a self-correcting system, the Ministry has held that due to difficulties to trade and industry, the system was being fine-tuned.

**Thus, the self-correcting system, as originally envisaged, was not in place and this led to continuation of avoidable assessee-tax officer physical interface instead of IT based interface. This goes against the objective of reducing the avoidable physical interface to minimum, if not eliminated completely.**

**(f) Other envisaged self-policing mechanisms**

- ***Non-implementation of reverse charge mechanism for supplies by unregistered person***

Generally, the supplier of goods or services is liable to pay GST. However, in specified cases, the liability to pay tax is on the recipient of supply of goods or services instead of the supplier, which is called the reverse charge. The GST Acts provide that wherever a registered person procures supplies from an unregistered supplier, the registered person needs to pay GST on reverse charge basis.

Initially<sup>7</sup> (June 2017) the supplies received by a registered person from any or all the unregistered suppliers up to five thousand rupees in a day have been exempted from reverse charge. However, all categories of registered persons were exempted<sup>8</sup> (October 2017) from the provisions of reverse charge on supplies by unregistered persons till 31 March 2018 initially. Such exemption

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<sup>7</sup> Notification No.8/2017-Central Tax(Rate) dated 28 June 2017.

<sup>8</sup> vide notification no.38/2017-Central Tax (Rate) dated 13 October 2017, (corresponding IGST notification no.32/2017-Integrated Tax (Rate) dated 13 October 2017).



was extended<sup>9</sup> from time to time up to 30 June 2018, 30 September 2018 and finally up to 30 September 2019.

The rationale for introduction of RCM and the impact of its subsequent deferral needs to be examined before further changes in this mechanism are made.

- **Tax Deduction at Source**

Section 51 of the CGST Act, 2017, provided for Tax Deduction at Source (TDS) by the Government departments, Local authority and the Governmental agencies. TDS is applicable for payments above ₹ 2.5 lakh.

TDS provisions were postponed from time to time. The reasons for this postponement, as mentioned in the 18<sup>th</sup> GST Council meeting minutes, were lack of preparedness of the Government agencies to deduct TDS and the need for TDS to be linked to fund settlement mechanism of respective States. It was also pointed out that since GSTR-2 was not getting filed, the TDS benefit could not be passed on to the taxpayer.

TDS provisions were finally made operational from 1 October 2018. Tax deductors were supposed to file a return by 10<sup>th</sup> of the succeeding month. However, the due date for this return for the months of October 2018 to December 2018 was extended<sup>10</sup> to 31 January 2019 stating that certain operators were unable to obtain registration because of technical issues being faced by them on GST Portal.

TDS data could be used to arrive at the turnover of suppliers, at least where supplies were made to the Government and thereby, identify non-registrants and tax evaders. Given the glitches being faced and the fact that tax collection is a function of tax department and not all the government departments, it is recommended that Government may review implementation of TDS and consider alternative ways of achieving what is sought to be achieved through TDS. For instance, having a Service Tax registration was made compulsory for a bidder providing consultancy and other services to government. Similarly, by making GST registration compulsory for providing goods or services above a certain threshold to Government, real time analysis of the other data of payments made by Government departments to its suppliers and similar methods that Government may identify might serve the same purpose as this whole process of TDS.

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<sup>9</sup> Notifications No. 10/2018–Central Tax (Rate) dated 23 March 2018, No. 12/2018–Central Tax (Rate) dated 29 June 2018 and No.22/2018–Central Tax (Rate) dated 6 August 2018.

<sup>10</sup> Order No.4/2018–Central Tax dated 31 December 2018.

**(g) Partially rolled out GST Portal**

For implementing the project, GSTN prepared Project Management Plan in which various use-cases<sup>11</sup> and functionalities of different modules were planned with timelines for implementation. The implementation of GST portal was conceived to be implemented in three phases as discussed below.

***Phase-I***

Phase-I consisted of taxpayer registration, taxpayer registration approval, Invoice upload, Payments, Return, Input Credit reconciliation, IGST Settlement, MIS Reports, System Administration, Security Management and Help Desk.

The functionalities for this phase of the project, as envisaged in the Software Requirement Specifications (SRS), were initially categorised into 184 use cases targeted to be completed over a period from January 2017 to August 2017. However, only 35 functionalities of Phase-I were in production environment at the time of GST roll out as on 1 July 2017. Out of the 184 use cases, 25 use cases were not in production as of January 2019. GSTN informed (January 2019) that 12 of these 25 use cases were de-scoped, 11 were moved to Phase-II and two cases pertaining to Annual Returns (forms notified in September 2018) were work-in-progress. The de-scoped use cases were primarily those related to GSTR-3 returns (held in abeyance) and those which had become redundant due to changes in law/rules.

***Phase-II***

Phase-II consisted of Assessment, Refund, Adjudication and Appeal, Audit and investigation, Recovery and Write-off (for 27 States / UTs).

Total 122 use cases covering various functionalities of this Phase were planned to be taken into User Acceptance Testing<sup>12</sup> (UAT) environment over a period starting from January 2017 to March 2019. SRS for most of these modules, however, were signed off between January and September 2018 and SRS of two modules (MIS and Audit) was yet to be signed off. 103 use cases of this Phase were to be taken into UAT environment by October 2018. However, we noticed that only 87 use cases were implemented as of January 2019.

These delays had an impact on implementation of GST which could be clearly seen in case of the refund module as detailed below: -

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<sup>11</sup> A use case is a list of actions or event steps typically defining the interactions between a role and a system to achieve a goal.

<sup>12</sup> UAT is the last phase of the software testing process. During UAT, virtual software users test the software to make sure it can handle required tasks in real-world scenarios, according to specifications.

The module for processing the refund of **IGST paid on export of goods outside India**, with linkage between Customs IT system and GST portal was provided during September- October 2017. But **for the other categories of refunds**, it was originally envisaged that taxpayer would file Refund application on GST Portal, the application filed would be made available to tax officers online and the entire processing of refund would be automated. However, **as refund module was not provided on GST portal, it was decided (October 2017) that the application pertaining to refund claim should be filed and processed manually**. Hence, a workaround was created by developing a functionality RFD-01A to facilitate taxpayers to file refund applications on GST Portal and give a print out to the jurisdictional tax officer for manual processing, **necessitating avoidable interface with tax officer instead of a faceless IT interface, which defeated the original purpose of having non-intrusive E-Tax system**.

The refund application that could be transferred online to the tax officer, as originally envisaged, was made available on the GST portal for one category of refunds (viz. Exports of services- With payment of Tax) in October 2017 and for the remaining seven categories<sup>13</sup> during August to October 2018. **The back office module relating to online processing of refunds was not ready (May 2018)**.

As per the phase wise implementation plan of GSTN, the crucial module of refund was originally planned for phase II. On the recommendation of the GST Council and the instructions of the GoI, the work on Refund functionality was commenced along with Phase I. As the module was not ready, however, manual processing of refunds continued.

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*The automated refund application which would be made available online to tax officer, was introduced in most of the cases more than one year after the roll out of GST, while the processing of refunds was still being done manually except refund of IGST paid on export of goods. This pointed towards the faulty planning of Refund module.*

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<sup>13</sup> (i) Excess balance in Electronic Cash ledger, (ii) Exports of goods / services- Without payment of Tax, i.e., ITC accumulated, (iii) On account of assessment/provisional assessment/ appeal/ any other order, (iv) ITC accumulated due to inverted tax structure, (v) On account of supplies made to SEZ unit/ SEZ Developer (with payment of tax), (vi) On account of supplies made to SEZ unit/ SEZ developer (without payment of tax) and (vii) Tax paid on an intra-State supply which is subsequently held to be inter-State supply and vice versa (change of POS).

### **Phase III**

Phase-III consisted of BI, Management Dashboards and Dynamic Reporting.

M/s. Infosys, the Managed Service Provider of GSTN, was to deliver 50 BI reports based on statistical analysis which were to be made available to 500 users from the States/UTs and CBIC. The reports were to be based on analysis of return, registration, payment and e-way bill data to identify anomalies in database and comparison of data like GSTR-1, GSTR-3B, e-way bill data to find out ITC mismatch and other anomalies. As per Request for Proposal (RFP), the execution plan of BI was to be finalised based on the requirement for reports. GSTN was in the process of identifying the required BI reports as of October 2018 and hence, the execution plan was under preparation stage only, with no timelines finalised for implementation.

### **Response of GSTN to partial roll out of GST portal and our comments**

*When we pointed out (November 2018) the status of phase-wise implementation of GST portal, GSTN stated (January 2019) that GST was to be rolled out from July 2017 and there were changes subsequent to signing-off of SRS in December 2016. Therefore, implementation of the functionalities of Phase-I was re-prioritised. For both Phases I and II, in view of the frequent changes in rules, notifications and decisions of the GST Council, Change Requests (CR) were planned and implemented in the GST portal on a continuous basis.*

The reply of the GSTN should be seen in light of the following facts :-

- i. There had been no inadequacy as far as funding and hired human resource capacity was concerned.
- ii. Scope for fast and recurring changes in the rules / forms and consequent changes in enabling IT system was expected and should have been factored into the project governance system to ensure smooth transitioning of the current indirect tax regime to the GST regime.
- iii. Deficiencies were noticed in the implemented systems and also in the changes made thereafter as could be seen from the findings of the 'IT audit of GSTN' reported in Chapter II of this report. Deficiencies pointed by this audit remained unaddressed in some cases even after corrective action was reported by GSTN.
- iv. GSTN management was given independence to fix its own timelines for implementation of functionalities within the broad timelines for the activities given by the GST Council / the Government.

GSTN in its response endorsed by DoR (June 2019) stated that the preparation of IT Business Processes of Registration, Payment and Return had started on the basis of draft Business Process Document and Model GST Acts, which were provided during April to October 2015 and June 2016. Thereafter, GST Rules were placed in the public domain in December 2016 and January 2017. These were not complete rules and the same were published for comments of the public. After receiving feedback from the taxpayers and tax consultants, and other stakeholders, these rules had undergone changes. Therefore, significant changes in the processes that were provided in 2015 and June 2016 were inevitable. Though GSTN had done proper planning and monitoring mechanism were in place, however, due to evolving nature of Law and rules there has been revision in the plan.

It was also stated that they had successfully implemented IT processes of a complex GST system and had integrated with different systems of tax departments, banks, accounting authorities and other stakeholders.

Audit holds that delays and changes are not entirely unexpected for a system as complex as GST. An organisation of GSTN has been created exclusively for the purpose of providing IT backbone for GST in March 2013 and has been in existence for four years before actual roll out of GST. Hence it would be assumed that they were preparing for this mammoth tax reform. *GSTN attributing delays in system development to frequent changes in Act / Rule provisions indicated that the evolving nature of GST was not factored into the project management.* Taxpayers, especially exporters suffered due to GST refunds being held up, which was due to faulty planning of Refunds module.

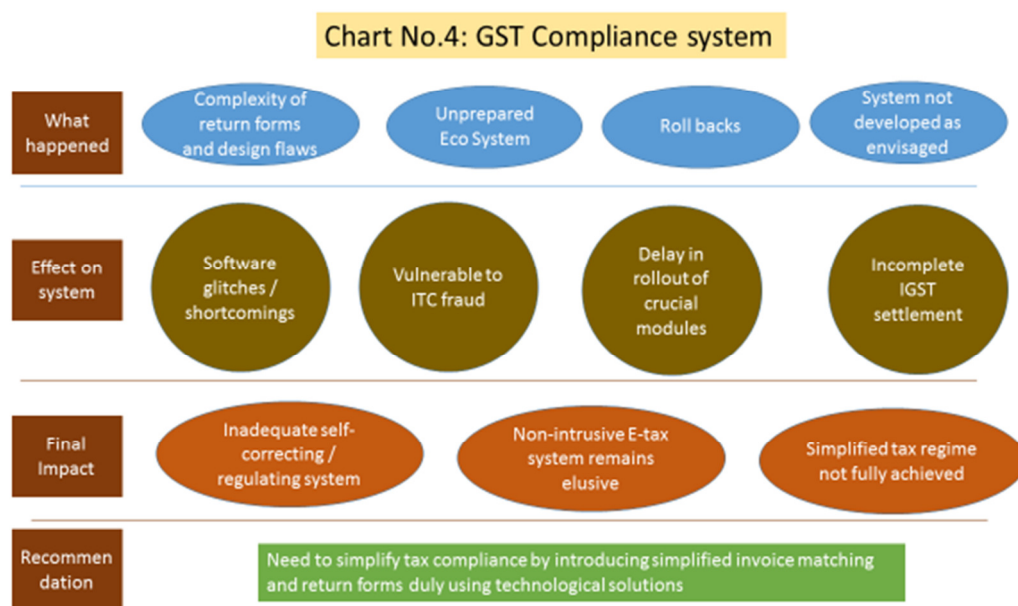
The efficiency of the system is the combined responsibility of all stake holders involved in its development. The implementation and progress of GST was also being regularly monitored by DoR, which was aware of the timelines for GST roll out. Inadequacies in the system show that there was a failure in not just system design but its testing by GSTN and acceptance by the tax departments before a pan-India roll out. As such, the executive who have endorsed the system as developed is equally accountable for the problems being faced.

### **1.6.3 Conclusion and Recommendations:**

The implementation of GST in India is perhaps the biggest tax reform in the world and the effort made by all the stake holders, including the Central Government, the State Governments, DoR, CBIC, GSTN, MSP and those of businesses which were ready, that made it possible is commendable. The advent of GST has provided a common national market for goods and services and paved the way to reduce tax cascading by providing ITC across the value chain of supply of all goods and services barring a few goods /

sectors kept outside the ambit of GST. GST ushered in uniformity in tax rates as well as formats of registration forms, returns and challans across the country. E-way bills have by and large replaced the manual check posts.

One significant area where the full potential of GST has not been achieved is roll out of the simplified tax compliance regime. The chart No.4 below explains what happened on GST front and how it impacted the GST Compliance system:



The complexity of return mechanism and the technical glitches resulted in roll back of the originally envisaged system-verified ITC based on invoice matching, using GST returns (GSTRs-1, 2 and 3). The summary self-assessed GSTR-3B return, introduced as a stop-gap measure has continued. Thus the system as in vogue today is an unverified return, without an IT based checking of invoices and is prone to ITC frauds. The self-correcting system, as originally envisaged, is not in place and this has led to continuation of avoidable assessee-tax officer physical interface instead of IT based interface. Without invoice matching and auto generation of refunds, assessments etc. on the whole, the envisaged GST tax compliance system is non-functional.

The settlement of IGST to the States also is impacted as the IGST settlement reports were linked to data flowing from returns and also from modules such as appeals and refunds.

Overall, when a major system change was on the anvil and was being thought about for quite some time, it was expected that all involved would be geared up enough to make this change possible. It is understood that a major transformation in the tax administration with Pan-India impact may have a few initial problems. The adherence to the business rules and the system design are the responsibility of DoR, CBIC, State Tax authorities and GSTN.

The extent of changes, having to be now undertaken, as well as the suspension of the key aspects of the system, however, points to inadequate co-ordination among the stake holders such as DoR, CBIC and GSTN as well as failure to try out the system adequately before roll out. The GST portal, to the extent implemented, was not fully aligned to the provisions of GST Acts and Rules and was fraught with operational deficiencies and system design deficiencies in certain areas as brought out in our IT audit findings reported in Chapter III of this report.

The system of payment and settlement of tax that was envisaged for GST was based on one hundred per cent invoice-matching and availment of input tax credit, as well as settlement of IGST on the basis of invoice-matching. Neither is possible as of now, as an invoice-matching system has not kicked-in. Invoice-matching is the critical requirement that would yield the full benefits of this major tax reform. It would protect the tax revenues of both the Centre and the States, it would lead to proper settlement of IGST and would minimise, if not eliminate, the tax official-assessee interface. In fact, even “assessment” in the sense understood in the manual system may no longer be necessary (returns themselves can be generated by a system that matches invoices); and cases of evasion etc., can be traced by applying analytical tools and AI to the massive data that crores of invoices generate.