ELP

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IMPACT OF GST ON FTP SCHEMES

Introduction

While a lot is being deliberated on the manner in which the current Indirect taxes would be subsumed into the Goods and Services Tax ('GST') regime, it is imperative to simultaneously examine the potential impact of the new GST regime on various Government policies in respect of foreign trade. The Foreign Trade Policy ('FTP') is formulated with the objective to increase India's share of global merchandize trade and to use trade expansion as an effective instrument of economic growth and employment generation. Government of India has introduced various export-linked concessional import schemes under the FTP along with relevant notifications under the Customs Act, 1962 ('Customs Act') and Central Excise Act, 1944 ('Central Excise Act') to give effect to such concessions with a view to completely neutralize the incidence of taxes on exports, thereby encouraging the export of goods and services from India, by rendering them more competitive in the international market and as a result, maximizing the foreign exchange earnings of the country. Likewise, the constant endeavour, even under the proposed regime would also be to rebate the impact of GST on supply chain entailing exports of goods and services.

GST on import and impact on FTP

Presently, the strategies devised for achieving the objectives under FTP *inter alia* involve prevention of export of taxes and levies, reduction in transaction costs, simplification of documents and procedural requirements for cross border transactions, introduction of special focus area, sector specific incentives, etc. The export-linked tax incentives extended under the FTP *inter alia* include the Schemes namely; Served from India Scheme ('SFIS'), Focus Product Scheme ('FPS'), Focus Market Scheme ('FMS'), Export Promotion Capital Goods Scheme ('EPCG'), Establishment of Export Oriented Units ('EOU'), Special Economic Zones (SEZ'), Foreign Trade & Warehouses Zones ('FTWZ'), etc. The tax incentives extended under the FTP principally consist of exemption from Central levies such as Central Excise duty, Customs duty, Central Sales tax, etc. Going forward, we are likely to adopt a dual GST structure under which the Centre and States will separately legislate, levy and administer a Central GST ('CGST') and State GST ('SGST'), respectively. The CGST will almost certainly subsume Central Excise duty, Service tax and the Additional Customs duties. The SGST will almost certainly subsume VAT and perhaps also Entry tax (at the State level) and other taxes.

The Constitution (One Hundred and Twenty Second Amendment) Bill, 2014 ('Amendment Bill') proposes to treat supply of goods and services, in the course of import into the territory of India as though these are supplies in the course of inter-state trade or commerce. Thus, import transactions will be subjected to IGST under the GST model of taxation. The switchover to GST regime would principally not affect the Customs provisions, as import of goods, as against Basic Customs duty ('BCD') and Additional Customs duties, is likely to attract BCD and IGST. Similarly, import of services, as against Service tax at present, is likely to attract IGST in the GST regime. The IGST rate is likely to be an aggregate of CGST and SGST rates, to enable apportionment of IGST proceeds among the Centre and the States, basis the recommendation of the GST Council. The duties and taxes on imports are expected to rise from those applied today.

Keeping the likely GST structure in mind, the various benefits / incentives granted under FTP would require amendments:

- The Foreign Trade Policy and Customs notifications will have to be modified to align them with the CGST provisions.

- On the switchover to GST, it will have to be seen whether the option of procurement without payment of Central levies continues and whether such concessions would also be extended to the impost of SGST. Considering the primary intention being prevention of export of taxes and levies, the exports would either be granted outright exemption from levies under GST regime or alternatively, the benefit of refund of applicable levies would be made available. Thus, whatever the mechanism for achieving its objective, it is important that exports must be zero rated and also the tax impact on Inputs and Capital goods used in manufacturing exported goods be neutralized.

- Most of the export-linked incentives grant exemption from payment of Customs duties on imported Inputs and Capital goods used in manufacture of goods or rendering of services exported outside India. The Additional Customs duties would be replaced by IGST. It is therefore pertinent to examine whether similar incentives would be extended to that portion of IGST which would be towards SGST element.

- In respect of domestic procurements, it will have to be examined whether similar concessions, as available under current Excise laws, will be legislated by the States under the GST regime wherein the taxing events at the Central and State levels are synchronised.

- It would be advisable in the context of GST that FTP be made a self-contained document with all relevant procedures currently prescribed under different laws, including Excise and other laws.

- Since most of the incentives under FTP are linked with Customs and Excise duty, therefore, there exists a need to revisit and evaluate the schemes for their continued subsistence and relevance during the GST regime. To illustrate, in the current tax regime, for a particular industry/business, the Advance Authorization scheme may be more beneficial when compared to the Duty Drawback scheme (both schemes having the objective to eliminate the Input tax cost). However, GST regime may set out different equations with the change in the duty rates and structure and accordingly require a renewed comparison of alternative schemes under FTP.

- FTP grants the benefit of drawback of duties (particularly Customs duty and Excise duty) on procurement of raw materials used for the manufacture of export products. Given the likely structure of GST, the duty drawback rates are likely to undergo change and accordingly, the impact would need to be evaluated.

- The Bonds and Bank Guarantees that are required to be executed under the existing schemes such as EPCG and EOU are directly linked to the estimated amount of duty saved during a particular period of time. Due to the envisaged change in the duty structure, there may arise a need for revising the Bonds and Bank Guarantees already executed.

- The export obligation under the EPCG Scheme is linked with the quantum of duty saved. The suggested rate change and duty structure is likely to impact the cash flows and the ability to fulfil the export obligation under EPCG Scheme over the stipulated period of time.

- It would be imperative to ascertain whether coverage of duty credit scrip obtained under various schemes would be extended for payment of SGST and IGST (to the extent of SGST element).

Various export oriented industries such as metals, electronic goods, heavy machinery, automobiles, pharmaceuticals, chemical industries, etc. will have significant impact as discussed above. Therefore the Central Government must ensure that effective measures are devised not only to rationalise the tax incidence but also to facilitate procedural requirement, ease of compliance and reduction in transaction cost.

Further, intensive service sector such as information technology and information technology enabled services, BPOs, KPOs, telecom, media and entertainment, banking and other financial services are likely to be most affected. Presently, these service sectors claim refund of Service tax paid on Input services (being the major cost element) from the Central Government under one Central registration. However, it is probable that they would be required to file multiple refund claims for SGST element in every State, leading to increase in compliance cost and hardships. Moreover, increase in rates would lead to higher accumulation of credits and consequent impact on Company's cash flows.

Most significantly, once the Central Excise provisions are replaced by the CGST legislation and the CENVAT provisions are recast into the credit provisions under CGST and SGST, trade and industry will have to re-evaluate the relative schemes that provide for the recovery or exemption of taxes on inputs and opt for the most beneficial option. The Government must use the opportunity to integrate proposed FTP with the 'Make in India' programme. The Government should attempt and rationalise the inverted duty structure presently prevailing in various sectors and provide various incentives to augment domestic value addition to dovetail strongly in the 'Create in India' initiative. The integration of FTP with the said initiatives would help in efficient realisation of greater objective of making India a low cost global manufacturing hub.