*International Journal of
Emerging Research in Management &Technology
ISSN: 2278-9359 (Volume-6, Issue-6)*

Research Article | **June 2017**

Impact of GST on Automobile Sector in India

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Abstract:

The Automobile industry in India is one of the most successful manufacturing space from past liberalization. The industry has potential to grow to become a major economic contributor. The Government of India has also recognized the importance of Automobile industry holds in the Indian economy and hence is currently working on Automotive Mission Plan 2026 to set targets for the industry for the year 2026. The Government of India has planned to implement of GST to the manufacturing sector in India. The objective of this study is the impact of GST on Automobile sector in India.

Keywords: GST, Automobile Sector, Economic Development,

I. INTRODUCTION

Automobile sector in India is growing fast and the growth pattern seems to have a clear correlation with the reforms related policies those influenced both domestic demand pattern as well as trade. India is global major in the two wheeler industry producing motor cycles, scooters and mopeds principally of engine capacities below 200cc. The two wheeler industry in India has grown at a compounded annual growth rate of more than 15% during the last five years and Indian two wheelers comply with some of the most stringent emission and fuel efficiency standards maintained world wide. In India two wheelers is the second largest producer in the world and the world's number one producer is located in India. India is the largest tractor manufacturer, the fifth largest commercial vehicle manufacturer and the thirteenth largest producer of passenger cars in the world.

The Auto industry currently employs more than 30 million people both directly and indirectly. The auto industry is a key employment generator in the OEM factory that manufacturers the vehicles, in the inbound auto component and logistics industry that makes and delivers components & systems and the out bound logistics and dealer network that sells, maintains and distributes the cars. Every vehicle produced, generates secondary and tertiary employment. The industry generates employment of 13 persons for each truck, 6 persons for each car and four persons for each three wheeler and one person for two wheelers. It is important to appreciate the sector's multiplier effect on economic activity. If the industry produces as per its potential, it could generate employment of over 35 million people by 2020.

II. ABOUT THE GST

The GST as the biggest taxation reform and is basically a proposed tax reform at the moment. This is indirect tax much like the VAT, Service tax, entertainment tax, etc. and this would be levied by the state and center in the form of State GST and Centre GST on the manufacture, sale and consumption of almost all goods and services all across India. The auto industry is likely to gain from the implementation of the GST since it is expected to reduce logistics costs by removing trade hurdles, paving way for more competitive manufacturing. The execution of GST will remove the effect of multiplicity of taxes on the cost of goods and services. Currently, most of car manufacturers are located in few of the states in India and by some estimates, 80% of these cars are sold to dealers in states outside the state in which they are manufactured. Moreover, with the effective tax rate dropping to around 18% from up 27% fro some segments currently, it will result in lower prices and consecutively, boost the demand for automobiles with respect of taxation and duties, cars have been classified into four categories (i) Small cars with petrol engine capacity below 1200cc and under four meters in length, (ii) Mid size cars with petrol engine below 1200cc , (iii) Diesel engine below 1500cc , (iv) Luxury cars with engine capacity of 1500cc and above, (v) SUVs with engine capacity above 1500cc, 170 mm of ground clearance and longer than four meters. On small cars, a total tax of around 28% is levied currently which includes VAT and excise duty while for Mid size cars, it's around 39% once GST gets implemented, the total taxes levied on cars is likely to be reduced.

The industry requires the Government to support by providing it an atmosphere that facilitates growth. While the auto industry is focused on generating volumes in the different segments to garner growth, it is in the interest of the Government to continue with the lower excise rates as this will help increase volumes and garner additional tax revenue. High tax rates and consequent high prices of vehicles have a harmful effect of lowering volumes, lowering gross tax collections and ultimately lowering growth in the auto sector.

The Government should facilitate a conducive environment for growth of the auto industry by defining favorable long-term policy for investment. Due to the unfavorable policy environment in the country where tax rates on vehicles are getting changed every year and Government is negotiating FTAs where custom duties are likely to come down, many international companies that had planned to enter the market have stalled the plan and are now considering other emerging markets, such as China and Brazil.

The industry has potential to grow to become a major economic contributor. The Government also recognizes the importance the automobile industry holds in the Indian economy and hence is currently working on Automotive Mission Plan 2026 to set targets for the industry for the year 2026 and to suggest interventions that would be critical for growth of the industry. The industries identified by the Prime Minister for “Make in India” also include the automobile and auto component industry. The Ministry of Finance has laid down the roadmap for implementing Goods & Services Tax (GST) from April 1, 2010 and the Empowered Group of State Finance Ministers on Value-Added Tax (VAT) has accepted the report of the Joint Working Group which suggests a dual GST structure (a central GST and a state GST).

Impact of the GST on Automobile Sector

The Goods and Service Tax is a single rate tax levied on the manufacture, sale and consumption of goods as well as services at a national level. In this system the GST is implemented only on the value added at every stage of production. This will ensure there is no cascading effect of taxes (tax on tax paid) on inputs that are used in manufacturing goods. With the GST in place, the prices of goods are expected to fall, and in the long term we can expect the dealers to pass on these benefits to the end consumer as well. The Automobile industry has seen significant disputes under central excise valuation like, sale below the cost for market penetration, inclusion of State Industrial Promotion subsidies retained by the manufacture, deductibility of past sale discounts from value under excise, valuation of demo cars treatment of PDI charges and other dealer reimbursement advertisement charges recovered from dealers etc., and sales though marketing companies and mutuality of interest. The model GST law continues with the concept of transaction value which is a welcome measure, however the powers for rejection of the transaction value are very wide, and could lead to significant valuation disputes.

The GST is working towards a more viable approach when it comes to tax, which is applicable in the manufacturing process. The tax under the new regime which the manufacturer has already levied in the manufacturing process in deducted when the final product created by the manufacturer is produced in the market. Hence, the tax on products in overall reduced as the tax otherwise charges on the final product does not include the pre charged one. The same process is followed on the level of the wholesaler who sets off the tax when he purchases the good from the manufacturer and releases them in the market. The product passes from the wholesaler to the retailer the retailer after adding value to the product again sets off the tax when releasing the goods finally in the market. In this chain of passing the goods from one to another, the tax sets off at every level, releasing a bit of pressure on all the people on the respective stages. Hence, when the final product is released the overall value of the good when taxed has a marginal variation in favor of the consumer as to re-existing rate of taxes. The double tax burden is being eliminated from this region as taxes that may have been charged and again charged on the tax that was already paid has been done away with the section, though has variations as per type of vehicle depending on the size and emissions by the same. Moreover the overall compliance burden is expected to decrease and bring lots more efficiency in operations of the indirect tax prospective the whole country will be treated as one market and will add to operational efficiencies.

The GST will be positive for the automotive sector,primarily because of the efficiency and the removal of cascading that is expected with GST, example a car is manufactured in a particular state and generally 80 percent of these cars are sold to states outside the state of manufactures to dealers outside the state. So today, to straight away give you an example, the two percent central sales tax (CST) that they pay will not be there tomorrow because hopefully origin tax is not there. Even the two percent CST will be an integrated GST (IGST) which will be fully creditable by the dealer when he sells the car in the other state, and even from a procurement point of the view, if there is interstate procurement we suffer today at two percent CST which is a cost to the manufacturer, that also will not happen because those interstate procurements will have an IGST in it which is again available as a full credit to the manufacturer if the credit rules are simple and easy. The second efficiency could be also on the input side, a bigger, more easy credit mechanism so that all the taxes on the input side, whether it is input services, whether it is capital goods, whether it is manufactured products are set off against the output liability of GST.

Table showing the different types and rate of taxes levied on the passenger vehicles/ SUV

Segment	**Excise duty**	***Nccd +auto cess**	**VAT**	***Road Tax**	***Motor vehicle tax**	**Total**	**CGST**	**SGST**	**TOTAL**	**Difference**
Small Cars <1200cc	12.50%	1.1%	14%	State based	State based	28% (approx)	9%	9%	18%	10%
Mid-SizeCars from 1200cc to 1500cc	24%	1.1%	14%	State based	State based	39%	9%	9%	18%	21%

Luxury Cars>1500cc	27%	1.1%	14%	State based	State based	42%	14%	14%	28%	14%
SUV's >1500cc, >170mm ground clearance	30%	1.1%	14%	State based	State based	45%	14%	14%	28%	17%

The GST law treats job work as a service and seeks to maintain existing excise procedures for the job work transactions, i.e. non taxability of job work transaction and providing credits to the principal for supplies to job worker 180 days condition for bringing back goods after job work. The automobile industry for vendors to develop tools for the manufacture of parts of automobiles. The ownership of such tools is transferred to the OEMs, and the cost is also recovered from OEMs. However, the tools are physically located in the vendor's factory for manufacture of parts. As specified in model GST law the definition of capital goods covers only those goods which are used at the place of business of supply of goods. Thus, only goods which are used in the place of business of OEM seem to be eligible for GST credit in the OEM's hands. This could possibly result in increase in the cost of totaling and cost for manufacture. The automotive industry has witnessed several cesses including automobile cess, NCCD, tractor cess and infrastructure cess. In the discussions on GST, the Government has indicated its intention to subsume all Central and State cesses into GST.

The existing CENVAT credit rules the input tax credit will be allowed only of those goods falling within specified chapters to the model GST law. Further the definition of inputs and input services also provides for exclusions. Therefore, it appears that even under GST, restrictions on input tax credit will continue. Generally, states provide for various incentives including investment promotion subsidies (IPS). A majority of the automobile manufacturers enjoy special benefits from the State government in the form of State investment promotion subsidies (IPS). This is given in the form of refund of VAT/CST paid. The implementation of GST, taxes move from the origin state to the consumption state. This could result in significant reduction of flow back of IPS, since GST on inter state sales is not credited to the origin state unless on inter state sales is not credited to the origin state unless there is a compensation mechanism to the states or to the OEMs with regard to the impact on the IPS due to GST.

Existing Excise Duty rates

Vehicle Category	Excise Duty
Small cars	12.5%
Length >4m but engine capacity less than 1500cc	24%
Length >4m and engine capacity more than 1500cc	27%
SUVs/MUVs (length >4m, engine capacity >1500cc and Ground clearance >170mm)	30%
Hybrid cars	12.5%
Specified components of Hybrid vehicles	6%
Electric cars, Buses, 2W & 3W	6%
Specified components of Electric vehicles	6%
Buses	12.5%
Trucks	12.5%
Three wheelers	12.5%
Two wheelers	12.5%

Source: SIAM

Existing Import Duty rates

Criteria / Applicability	Import Duty in %
Used car import	125
Cars CBUs whose CIF value is more than $ 40,000 or Petrol Engine > 3000 CC or Diesel engine > 2500 CC	100
Cars CBUs whose CIF value is less than $ 40,000 and Petrol Engine < 3000 CC and Diesel engine < 2500 CC	60
Two-wheeler CBUs with engine capacity <800 cc	60
Two-wheeler CBUs with engine capacity >=800 cc	75
Commercial Vehicle CBUs (Trucks & Buses)	20
CKD containing engine or gearbox or transmission mechanism in pre-assembled form, but not mounted on a chassis or a body assembly	30
CKD containing engine, gearbox and transmission mechanism not in a pre-assembled condition	10

Source: SIAM

III. TAX RATE FOR THE INDUSTRY

The tax rate on inputs and output should be fixed considering the pattern of input purchase and output sales which varies considerably. This has implications for the input tax credit. While vehicle manufacturing takes place in a few states with supply to other states (local sales account for less than 10% of total domestic sales), the majority of components (around 70% - 80%) are procured from vendors within the state. If tax rate of components/inputs is more than the tax rate at the time of supply of complete vehicles (Completely Built Units), then refund would arise.

Suggestions of Tax base & Levy

1. Uniform rate of tax should be charged on complete vehicles (whether by way of sale or by way of transfer) and inputs, against which input credit should be allowed.
2. Tax paid on complete vehicles on movement from factory should be made available as input credit to the vehicle dealers.
3. Manufacturers could give state-wise break-up at periodically to respective state governments who may settle it through the appropriate clearing house mechanism.
4. Considering the current level of taxation, a suitable tax rate may be adopted. Tax rates should be uniform across states and there should be one authority to which payment would be made by way of one Challan.
5. Goods and services should be classified on the basis of HSN and GATTS (at both central and state levels).
6. A common base should be adopted for taxation of both Central and State GST. Under the present taxation system, interstate sales tax and local sales tax is levied on excise duty in respect of the manufactured goods resulting in cascading of taxes.
7. In case of non-sale, where the transaction value of goods or services is not determinable and when GST is charged, a simple mechanism of valuation could be adopted on the basis of cost.
8. Under GST, it is suggested that the basis of tax credit should be on 'Cost to Business', i.e. tax, which is paid and forms cost to business should be allowed as a tax credit, both at the Central & State level.
9. The document based credit should also be dispensed with and could be substituted by appropriate certification by an independent Chartered Accountant (or the Appointed Company Auditors). The same could be subject to appropriate audits by trained government officers and could be IT enabled.
10. Diesel and motor spirit should be brought under GST with input tax credit and mechanism to avail the same. VAT on diesel and motor spirit constitutes a significant element of cost for the transport industry.
11. In the proposed GST system, it is not known whether the stock transfer would remain exempted from tax (at present, sales tax is not levied on Stock Transfer) or would be made taxable in the importing state; the industry needs to understand the treatment of stock transfers for the purpose of input tax credit.
12. There should be no distinction between input and capital goods. Presently, definition of Capital Goods under Central excise law and state VAT is not uniform. Under State VAT, definition of capital goods and also the rate of taxation vary from state to state. As regards periodicity of taking credit, excise and VAT laws differ.
13. In respect of existing exemptions having sunset clause, appropriate transitional provisions should be introduced to ensure continuity of existing benefits. A clarification is needed on how the existing sales tax benefit schemes e.g. loan, deferral would be affected.

14. The State Goods and Services Tax Act, State GST Act should be a common Act operated/implemented by all the states and Union Territories (similar to present Central Sales Tax Act) covering transactions related to goods, services and exports.
15. Concept of 'Tax Invoice' should be continued for availing State GST credit.
16. To ensure viability of EOU under severe competition, timely refund of tax is needed. Effective refund system should be in place for smooth operations of EOUs. Presently, EOUs are eligible to get refund of CST on interstate purchase of inputs used in the production of export goods and local VAT content of the export product is allowed to be deducted against the DTA Sales and the balance, if any, is allowed as refund.
17. Under a dual GST structure (a Central GST and a State GST), there could be a situation where the Input Tax credits which remain assizes would be refunded to the assizes. Since the cross utilization of credits between the Central GST and State GST is not permitted, there could be a situation of payment on the one hand and a refund situation on the other. In order to avoid this situation cross utilization of input tax credits should be allowed.
18. Procedural changes should be notified in advance. The industry should be given 6 months lead time before the introduction of GST.
19. State specific incentives should be protected under GST.

IV. CONCLUSION

The implementation of GST, taxes moves from the origin state to the consumption state due to which overall economic activity is expected to increase and it could expect a better GDP growth that should push demand for vehicle across categories. Impact of tax cascading will also go away that will reduce overall cost of vehicle manufacturing as all taxes on input paid will be offset with the output liability of GST.

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