



GST & cooperative federation: Through the eyes of Indian constitution

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Abstract

India as a nation has achieved Political Integration in 1950's with the integration of Princely States in Indian Union. Passing of Goods and Services Tax through 101st Constitutional Amendment has paved the way for economic integration of the country. In doing so, States and Centre have ceded their power to tax and come up with a single Tax system to realize, the dream of one Economic India with 'One Market'.

In our Federal System both Centre and States have power to impose taxes. The division of such taxation powers is given in Union and State List under 7th schedule. Part XII of the Indian Constitution contains detail provisions in this regard. However, the Constitution of India has now been amended and this fundamental reordering of federal fiscal relations for the cause of common good shows the strength and resolve of the federal structure. This convergence for the cause of larger public good has been made possible, initially, due to the mechanism of the Empowered Committee of Ministers and later the GST Council. Under the GST regime, the Centre & States will act on the recommendation of the GST Council which comprises of the Union Finance Minister, Union M.O.S. for Finance and all Finance Ministers of the States. 2/3 of voting power is with the States and 1/3 with the Centre which reflects the accommodative spirit of federalism.

However, Constitution still provides room for states to levy tariff and non-tariff barriers. Article 302 gives Parliament the power to restrict free trade between and within states one grounds of public interest. Similarly, Article 304 (b) allows state legislatures to restrict trade and commerce on ground of public interest.

Lastly, GST is a long awaited reform in the tax-structure prevailing in the country which should be given enough room to prove its mettle.

Keywords: GST, Cooperative Federalism, GST Council, Centre-State, Financial Relations

Introduction

In order to discharge their given responsibilities under the Constitution, both the Union and the States must have adequate financial resources. This is a significant indicator for any system of federation to become successful. Our constitution has made elaborate provisions in this regard taking a cue from the Govt. of India Act, 1935. These provisions relate to the distribution of the taxes as well as non-tax revenues and the power of borrowing, supplemented by provisions for grants-in-aid by the Union to the States. A complicated arrangement for the distribution of the financial resources of the country has been set up in order to provide an equitable distribution of the financial resources between the two units of the federation, instead of dividing the resources into two watertight compartments, as under the usual federal system ^[1]. In *Coffee Board Vs. C.T.O.*, ^[2] the Supreme Court has stated....." In other words, the Union and the States together from one organic whole for the purposes of utilisation of the resources of territories of India as a whole."

Genesis of G.S.T

Our Constitution empowers the Central Government to levy

excise duty on manufacturing and service tax on the supply of services. Further, it empowers the State Governments to levy sales tax or value added tax (VAT) on the sale of goods. This exclusive division of fiscal powers has led to a multiplicity of indirect taxes in the country. In addition, Central Sales Tax is levied on inter-state sale of goods by the Central Government, but collected and retained by the exporting states. Not only this, many states levy an entry tax on the entry of goods in local areas. This multiplicity of taxes at the State and Central levels has resulted in a complex indirect tax structure in the Country that is ridden with hidden costs for the trade and industry. In order to simplify and rationalize indirect tax structures, Government of India attempted various tax policy reforms at different points of time. According to Prof. Wheare: " There can be no final solution to the allocation of financial resources in a federal system. There can only be an adjustment and re-allocation in the light of changing circumstances." ^[3] In furtherance of the above objective, a system of VAT on services of the Central governments level was introduced in 2002. The States collect taxes through state Sales Tax VAT, introduced in 2005, levied on intra state trade and the CST on inter-state trade. Notwithstanding all the various changes the overall taxation system continues to be complex and has various exemptions.

¹Durga Das Basu, Introduction to the Constitution of India, 369, 22nd Edition, Lexis Nexis, Haryana, India, 2016.

² AIR 1971 SC 870, cited in Durga Das Basu, Introduction To The Constitution of India, 369, 22nd Edition, Lexis Nexis, Hayana, India, 2016.

³ Cited in T.K. Tope's Constitutional Law of India, 3rd Edition, pp. 1039-41

This led to the idea of "One nation One Tax" and introduction of GST in Indian financial system. After the Indian States having achieved Political Integration in 1950's with the integration of Princely States in Indian Union, passing of GST is a Great Leap Forward toward achieving Economic Integration of the Country. GST is one indirect tax for the whole nation, which will make India one unified common market. GST is a single tax on the supply of goods and services, right from the manufacturer to the consumer. Credits 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.

Under GST, both Centre and States have given up taxation powers and as a product following taxes have been eliminated:

Table 1

Central Taxes Subsumed under GST	State Taxes subsumed under GST
Central Excise Duty.	State value Added Tax/ Sales Tax,
Additional Excise Duty,	Entertainment Tax (other than the tax levied by the local bodies), Central Sales Tax,
Service Tax,	Octroi and Entry Tax,
Additional Customs Duty commonly known as Countervailing Duty,	Purchase Tax,
Special Additional Duty of Customs	Taxes on lottery, betting and gambling.

Co-Operative federalism in India and the G.S.T.

An American scholar, A.H. Birch, explains the concept of 'Co-operative federalism' in these words: ^[4] " the practice of administrative co-operation between general and regional governments, the partial *dependence* of the regional governments, by the use of *conditional* grants, frequently promote developments in matters which are *constitutionally assigned* to the regions."

In fact, the traditional theory of material independence of the two governments- federal and States, has given way to " Co-operative federalism' in most of the federal countries today ^[5].

Our Constitution has been subjected to a raging debate regarding its federal or unitary character. Sri K. Santhanam in his work Union- State Relations in India, 1960 ^[6] has urged that the unitary bias of our constitution has been accentuated, in its actual working, by two factors so much so that very little is left of federalism. These two factors are- (a) the overwhelming financial power of the Union and the utter dependence of the States upon Union grants for discharging their functions; (b) the comprehensive sweep of the Union Planning Commission, set up under the concurrent power over planning.

⁴Cf. Birch, Federalism, pp. 305-06, cited in Durga Das Basu, Introduction To The Constitution of India, 65, 22nd Edition, Lexis Nexis, Haryana, India, 2016.

⁵ Ibid.

⁶ pp. vii, 51, 59, 63. Cited in DurgaDasBasu, Introduction To The Constitution of India, 65, 22nd Edition, Lexis Nexis Haryana, India, 2016.

According to Durga Das Basu, ^[7] the criticism may be justified in point of degree, but not in principle, for two reasons. Firstly, both these controls are aimed at securing a uniform development of the country as a whole. It is true that the bigger states are not allowed to appropriate all their resources and the system of assignment and distribution of tax resources by the Union [Arts 269, 270, 272] means the dependence of the States upon the Union to a large extent. But, left above, the stronger ones lagging behind, to the detriment of our national strengths. Secondly the same complaint, as in India, has been raised in the United States. But even in a country like the United States, such factors have, in practice, strengthened the national Government to a degree which could not have been dreamt of by the fathers of the Constitution.

In a federalism, there is a divisions of functions between Centre and Units. Respective area of competence of each is earmarked. However, there are not water-tight compartments. A number of instrumentalities to promote inter-governmental co-operation come into existence ^[8].

According to Granville Austin, the Constitution of India was, perhaps, the first constituent body to embrace. Co-operative federalism from the start. The Learned author has said ^[9].

"The Assembly was perhaps the first constituents body to embrace from the start what A.H. Birch and others have called" co-operative federalism." This "new phase" that has emerged largely since world war-II, although its roots extends back to the thirties and early forties, has been characterized by the increasing interdependence of federal and regional governments- a development, it is usually argued, that has not destroyed the federal principle. This concept is clearly different from the one that was prevailing when the federal system of the United States or Australia was set up and which gave rise to Dr. Wheare's definition of 'federation'. The general and regional government of a Country shall be independent each of the other within its spheres. Co-operative federalism produces a strong central or general government yet it doesnot necessarily result in weak provincial government that are largely administrative agencies for the central policies. Indian federation has demonstrated this."

Hence, the system of federal co-operation existing under the Indian Constitution, through allocation by the Union of the taxes collected, or direct grants or allocation of plan funds donot necessarily militate against the concept of federalism and that is why Granville Austin ^[10] prefers to call Indian federalism as "Co-operative federalism" ^[11].

GST: A threat to Indian Federalism?

Some quarters many voices of opposition have been raised from some granters that GST will sound the death-knell of Indian federalism or co-operative federalism. The main points

⁷Durga Das Basu, Introduction To The Constitution of India, 65, 22nd Edition, Lexis Nexis, Haryana, India, 2016.

⁸Durga Das Basu, Commentary on the Constitution of India, 93, 9th edition, Vol. 1, Lexis Nexis, Haryana, India, 2014.

⁹ Cite in Durga Das Basu, Commentary On the Constitution of India, 62, 9th Edition, Vol. I, Lexis Nexis, Haryana, India, 2014.

¹⁰ The Indian Constitution (1966), pp. 187 et seq.

¹¹Durga Das Basu, Introduction To The constitution of India, 66, 22nd Edition, Lexis Nexis, Haryana, India, 2016.

of their concerns are as following.

1. Concerns of states of losing control over financial autonomy due to tax impacts and the GST council being a constitutional body would have control over taxpayers in the new tax regime.
2. Loss of revenue: States argue that the recent demonetization move has resulted in loss of states revenue which needs to be compensated.
3. Administrative issues: As to who would have control over taxpayers having less than Rs. 1.50 crore annual revenue.

Here it is pertinent to note that GST has been introduced in India through the Constitution (One Hundred and First Amendment) Act, 2016 [8th September, 2016]. In this Act of 2016, Goods and Services Tax has been defined in Article 366 (12A). The most novel concept of this Act is the insertion of Article 279 A which says that the President shall, within sixty days from the date of commencement of the Constitution (One Hundred and First Amendment) Act, 2016, by order, constitute a Council to be called the Goods and Service Tax Council. The GST Council consists of:

1. The Union Finance Minister (as Chairman)
2. The Union Minister of State in charge of Revenue or Finance,
3. The Minister in Charge of Finance or Taxation or any other Minister, Nominated by each State government.

All decisions of the GST Council will be made by three-fourth majority of the Votes Cast; the centre shall have one-third of the Votes Cast, and the States together shall have two-third of the Votes Cast.

The GST Council will make recommendations on:

1. Taxes, cesses, and surcharges to be subsumed under the GST,
2. Goods and services which may be subject to, or exempt from GST,
3. The threshold limit of turnover for application of GST,
4. Rates of GST,
5. Model GST laws, principles of levy, appointment, of IGST and principles related to place of supply,
6. Special provisions with respect to the eight north eastern states, Himachal Pradesh, Jammu and Kashmir, and Uttarakhand.
7. And related matters.

One of the main objections to GST is related to GST Council. From above it is clear that GST council is a recommendatory body with regard to all aspects of Goods and Services Tax. Here, decisions taken by a minority of not less than three-fourths of the weighted votes of the members present and voting. The vote of the Central Government shall have a weightage of one-third of the total votes cast. Many critics of GST are apprehensive of this power of Central Government and foresee that in future the Central Government might have an upper hand in many deliberation of the GST Council. However, the present experience of the functioning of the GST Council has been otherwise. The decisions taken by the Council in about two dozen meetings held so far, have been arrived at by consensus. Secondly, Art 279 (A) (11) stipulates that the GST Council shall establish a mechanism to

adjudicate any dispute between the Government of India and the States, Government of India and any State or States on one side and other States on other side, and between two or more States. Therefore, in a case where Centre exerts its power and influence any decision of the council, the aggrieved State or States make rake up the issue before the grievance redressal body or mechanism. Moreover, the decisions taken by the council are based on due deliberations and discussions. Hence, to discard them whimsically by the Central Government appears to be a far cry. In a democratic set-up, as in India, one can hope for solutions which will ultimately bolster democracy in the Country. In this context, the following passage from M.P. Jain's Indian Constitutional Law is worth quoting:

"The framers of our Constitution did take a due note of the emerging trend of cooperative federalism in the older federation. They realised that government in a federation were arranged not heirarchically or vertically, but horizontally, that no line of command runs from the Centre to the States and that common policies among the various governments can be promoted not by dictation but by a process of discussion, agreement and compromise^[12]."

From bare perusal of the Act of 2016, it is abundantly clear that the existing scheme of financial relations between Union and States is largely untouched. However, with the clear objective of one Nation One Tax, many taxes, cesses etc. imposed by States have been subsumed under the GST.

Further, as far as loss of revenue to the States, there is not much possibility because of the expansion of GST tax-payers network. However, to alleviate such fears, Article 18 of the Act of 2016, provides for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for a period of five years.

Lastly, the administrative challenges can be overcome if the States receive revenue what they were receiving at present and even more because in that case they will be able to cater to the developmental needs of the people much better than what they presently are in a position. After all, the fiscal system is deemed to be designed to serve the people better and better with the passage of time.

In the backdrop of above noted objections to the overall concept of GST and its impact on Co-operative federalism, some provisions of the Constitution are worth consideration. First of all, Constitution still provides room for States to levy tariff and non-tariff barriers. Article 302 gives Parliament the power to restrict free trade between and within States on grounds of public interest. Similarly, Article 304 (b) allows State legislatures to restrict trade and commerce on grounds of public interest. Of course, states can only impose restrictions in areas that are either on the State or Concurrent list. The gist of these provisions is that both the Centre and the States have considerable freedom to restrict trade and commerce that hinder the creation of one India. Such strong power is not found in other international experiences. Even in the United States where the Constitution has a very strong interstate

¹² M.P. Jain, Indian Constitutional Law, 6th Edition, 2010, Vol. I, p. 1014 and D.D. Basu, Comparative Federalism, 2nd Edition, 2008, pp. 471-72, cited in Commentary on the Constitution of India, 94, Vol. I, Lexis Nexis, Haryana, India, 2014.

commerce clause, States are constitutionally barred from regulating interstate trade and commerce as it was felt that such power would fundamentally hamper free trade and movement. Similarly, under European Common Market it is accepted norm that EU countries must not restrict the four freedoms of movement: of goods, services, capital and the people, except under narrow circumstances.

The 101st Constitutional Amendment has been adopted by the Jammu and Kashmir State Assembly thereby paving the way for further economic integration of the Indian States as a whole.

Conclusion

The Goods and Services Tax (GST) is the most significant reform since liberalisation commenced in 1991, and envisages, " a one Economic India" which is expected to lead to a more efficient and productive economy. It might lead to several macroeconomic gains also. The passing of the Hundred and One Constitutional Amendment Act, 2016 which has paved the way for GST regime in India, has been a spectacular example of parliamentary democracy in India. Ruling or opposition, both political parties have contributed to it. GST council is also a good example of mutual cooperation among Centre and States irrespective of party affiliations. Till now, it does not appear that with the advent of GST Act in India, the concept of cooperative federalism has been dented even to a minimum. Hopefully, it will be implemented in the same spirit. Moreover, GST roll out could be a template for the future of cooperative federalism. It can also serve as a template for reforming other such institutions of cooperative federalism, starting with the interstate council. Like political integration, the GST regime may well prove to be a harbinger of "One Economic Nation" that is a cherished goad of our Country.

Reference

1. Basu, Durga Das. Commentary on the Constitution of India, 9th Edition, Lexis Nexis, Haryana, India, 2014, 1.
2. Basu, Durga Das. Introduction to The Constitution of India, 22nd Edition, Lexis Nexis, Haryana, India, 2016.
3. Jain MP. Indian Constitutional Law, 1014, Vil.1, 6th edition, Lexis Nexis, Haryana, India, 2010.