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Opinion

TUESDAY, JULY 11, 2017

NO BIG BROTHER ON GST

Union commerce minister Nirmala Sitharaman

"The Centre did not play big brother role in fixing rates (under GST). If it (tax rate) has been agreed, it has been collectively agreed by the GST council ... a constitutional committee"

Don't ruin GST before it takes off

Maharashtra and Tamil Nadu are trying to vitiate the spirit of GST by levying new taxes

THE GOOD NEWS is that despite all the apprehensions, GST is off to a relatively smooth start and even J&K has decided to levy the tax. There have been no sharp increases in prices, nor have there been too many complaints of people not able to upload their invoices. Much of this, no doubt, has been due to the government decision to go ahead with GST but not impose any penalties on those not able to comply with all the formalities. While that was eminently sensible, many other pieces have also started coming together now and the government continues with its efforts to educate people on GST and to remove misconceptions that can derail the process. Revenue secretary Hasmukh Adhia has tried to address as many issues as possible in his series of Master Classes and did well, for instance, to point out that people didn't have to fill three forms every month, but had to fill one form that had three parts—and once you filled in the first, the others got filled up automatically. The government also showed how GST invoices could be generated manually, a GST app was readied and a series of software providers like Tally advertised services for a painless GST. While everyone cheered the abolition of border posts, the GST Council also showed tremendous flexibility in tweaking rates in response to industry representations—given how the ideal GST will have only 2-3 rates, such flexibility is critical in the years ahead.

What is unfortunate, in this context, is the attempt by a few states to try and subvert the GST process by coming up with new taxes. If the best part of GST was the fact of having the same tax rate across the country for any product—so it was one country, one tax—this will vitiate the process. It was bad enough that Tamil Nadu decided to impose a 30% entertainment tax over the 28% GST, Maharashtra has increased the one-time registration tax on private two-and four-wheelers by 2%. Ostensibly, this has been done to compensate for the losses due to levies like Octroi that were subsumed under the GST. This is unacceptable since it was always known that such duties would go once GST came in, but the compensation by the Centre was supposed to make up for it and, in any case, the tax buoyancy under GST would give the states more revenues. To the extent local bodies have to be compensated for losses, the states have to do this from their budgets. The GST Council has to discuss this issue and ensure that states don't start levying their own taxes even though the law allows this—if two states are allowed to get away, it is just a matter of time before others follow; Haryana and Punjab, for instance, would love to get back the mandi taxes under a new garb. Ironically, while some states try to unravel GST, a J&K is currently working on bringing in real estate under GST—this is a big lacunae that makes it easier for cash transactions to flourish in the sector—and finance minister Haseeb Drabu is confident it can be accomplished by the next budget. Co-operative federalism is at stake and it is only appropriate that the body representing it, the GST Council, gets more pro-active in defending it.

Get it right on fertilisers

AeFDS won't drive big reforms unless caps put on usage

WITH THE PRIME minister's office (PMO) quite firm that sales of subsidised fertiliser have to be linked to Aadhaar numbers of farmers, chances are the fertiliser ministry will have to stick to the target even though it wants the January 1, 2018, deadline extended. Under the scheme, fertiliser companies will have to authenticate the Aadhaar ID of farmers as part of the Aadhaar-enabled Fertiliser Distribution System (AeFDS) and, once this is done, they will get paid the subsidy based on the amounts sold. The plan is to, as in the case of LPG, use Aadhaar to remove fake users and save considerable sums in annual subsidies. According to a *Times of India* report, the pilot project has already started showing results—a survey by consulting firm MicroSave done for NITI Aayog found that nearly 300 fertiliser retailers in six districts of Madhya Pradesh, Rajasthan, Telangana and Andhra Pradesh have not renewed their licences after the launch of AeFDS.

While that is good news, for AeFDS to be truly useful, several more layers will need to be added to it. Right now, all farmers overuse urea because it is sold at a fraction of its market value—AeFDS will not stop this since the urea will continue to be heavily subsidised. If, on the other hand, the government moved to a proper Direct Benefit Transfer (DBT) and gave farmers a fixed per unit subsidy—as is done in the case of LPG—and forced them to buy urea at the market price, farmers would automatically reduce their consumption. To the extent the government has already issued 8.7 crore soil health cards, it could even give farmers information on how much the extra use is either ruining the soil or how much less could be used without it lowering productivity—that will only work when farmers benefit from lower use of urea, and that won't happen till they get the money in their hands.

A related problem is that of the bulk of the subsidy being cornered by rich farmers who have both larger land-holdings as well as those that are irrigated. Once again, unless a cap is put on the amount of fertiliser that will be made available to each farmer—irrespective of the size of the farm—richer farmers will continue to corner the benefit; in the case of LPG cylinders, since the same cap applies to all families, the rich don't corner the bulk of subsidies. Once again, the DBT route scores over AeFDS. AeFDS can be modified to plug most of these gaps, but when the DBT option is available, why not use that?

Checking FRAUD

RBI does well to put some onus on bank customers for fighting fraudulent transactions

BESIDES THE COMPLEXITY of online transactions *vis-a-vis* cash, one of the hurdles for online payments has been concerns over security. The rising number of hack attempts on banks has made people sceptical. While the government has tried to solve the first—it has launched three iterations of its payment service—the new guidelines released by RBI will probably address the second. The central bank, on Monday, notified limited liability rules in case of card fraud. RBI has highlighted that the customer will only be liable in case of her own fault, while in other cases, she would bear zero liability. Banks, if informed within three days of a third-party breach, would have to give the customer the entire amount in her account. On the other hand, if the customer is at fault—say, casually sharing information or clicking on phishing links—she will bear liability for all transactions until she reports the breach. A well-thought out move, this places some onus of security on customers, prodding them to check risky behaviour. RBI has also made mobile linking mandatory, and a failure to do so means all transactions other than ATM withdrawals being disallowed.

Most banks charge for the SMS alert facility. Though they are now required to have "reply" options to such messages, RBI does not specify who will bear the cost of this service. Surely charging banks for this can't be an option? The rules also leave a vacuum in terms of security of third-party e-wallets. More important, while the onus is on the bank to prove customer's liability within 90 days, this may not be an easy task with customers who try to game the system and refuse to settle their bills. What the central bank can do is make OTP mandatory for all transactions. That would ensure another layer of security, especially with mobile-linking becoming compulsory. Aadhaar can also be an answer to the bank's woes. As infrastructure improves, banks can look forward to fingerprint authentication at each terminal—in no case can people claim fraud if transactions are approved using biometrics.

EU-JAPAN FTA

IT AFFIRMS EUROPE'S COMMITMENT TO FREE TRADE AND GLOBALISATION AT A TIME WHEN BREXIT AND OTHER GLOBAL DEVELOPMENTS SEEM TO THREATEN THIS

A brave new deal

AMITENDU PALIT

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EU AND JAPAN recently reached political conclusion on an economic partnership agreement. The European Commission has described it as the 'most important' bilateral trade agreement concluded by the EU. Once implemented, the agreement will have far-reaching impact on various aspects of global trade. These would be felt on the leadership of global trade, the course of economic globalisation and the crafting of future global trade rules. The effects would also extend to the geostrategic spheres in Asia and Europe.

For some time now, globalisation is under attack for having created numerous losers and left-behinds. The anti-globalisation narrative has acquired considerable political legitimacy and led to tumultuous outcomes like Brexit in the UK and triumph of Donald Trump in the US presidential elections. It has also pushed the TPP into an uncertain future after the withdrawal of the US—the largest economy—from the agreement. Anti-globalisation sentiments in the US, Europe and several parts of the developed world allowed China to emerge as the vanguard for global trade. Nowhere was this more evident than the World Economic Forum earlier this year, when Chinese president Xi Jinping was the toast of the global business community.

China hasn't hesitated to express its eagerness in salvaging globalisation and leading the charge against protectionism and inward-looking policies in world trade. But its efforts to recharge globalisation through geographically motivated connectivity plans like the One-Belt-One-Road (OBOR) have created doubts among many countries about China's sincerity in shepherding a truly participative economic globalisation and global trade. Ongoing trade negotiations involving China, such as the RCEP, have been clouded by worries over China's efforts to fashion regional trade rules suiting its sovereign interests. The EU-Japan FTA is a significant advancement in this context as it puts the EU and Japan in commanding positions to lead globalisation and world trade by providing a credible alternative to China's plans.

EU has always been a major actor in global and regional trade. This is evident from the large number of trade agreements it has with various countries and regions of the world. It has the most notified trade agreements in force and is involved in the largest number of trade negotiations across the world. The US withdrawal from a prominent leadership role in global trade should have had the EU filling up the vacuum 'naturally'. But the setback over Brexit and the growing prominence of anti-globalisation political voices in different parts of the continent gave rise to the impression that Europe would retreat from the pro-trade, outward-oriented policies it has followed for decades. The worries were substantially put to rest by the results of the recent French presidential elections that had Emmanuel Macron's pro-globalisation campaign overthrowing the challenge of the far-right anti-globalisation opposition. It's clear now that the EU remains committed to free trade and its leadership is ready to tread a path different from that preferred by the US. The political conclusion of the EU-Japan FTA affirms the commitment.

Apart from being significant in economic size, the EU-Japan FTA can mark the beginning of a new phase of rule making in global trade. Three issues are notable in this regard. The agreement upholds the commitment of both Europe and Japan to the Paris agreement on climate change. This is a 'first' for bilateral deals given that while some existing US and EU FTAs have environmental standards, none have as specific commitment to climate change as this deal. By taking the Paris climate commitments within its fold, the FTA has set an example for other deals being negotiated. Many future FTAs, particularly those being negotiated by India and other G20 members committed to the Paris action plan might incorporate climate change.

> **The EU-Japan FTA puts the EU and Japan in commanding positions to lead globalisation and world trade, providing a credible alternative to China's plans to tailor agreements to suit its sovereign interests**

The second important point to be noted is the approach of the EU-Japan FTA towards investment issues. There is a conscious effort to move away from the contentious investor-state-dispute-settlement (ISDS) provisions in various BITs to a framework that emphasises more on liberalisation of foreign investment in each other's territories as opposed to investment protection. The FTA is expected to follow the EU's framework of an Investment Court system with judges being appointed by both countries for deciding disputes. This might again become the norm for many future FTAs uncomfortable with binding ISDS provisions. Finally, the FTA has maintained high data protection standards, which, again, has been a point of contention in agreements like TPP where some countries have been reluctant to lower data protection standards for enabling greater cross-border data flows. Of course, it remains to be seen how the FTA eventually enables effective digital trade notwithstanding high data protection.

The new approach to trade rule making is in particular contrast to the US mode of negotiating FTAs. The investment and data rules are different from those that the US has been advocating in its own FTAs, including the TPP. The distance of the EU-Japan FTA from the US worldview on trade has increased through its commitment to climate change. The new approach and framework also steals the thunder from China's efforts to contribute significantly to trade rule making, as China would need to search for a more acceptable alternative. Finally, geopolitically, the FTA shows that the world can work very well on free trade and globalisation without the US, and also without China.

Maharashtra's farm distress, on loop

Poor data & waiver contagion sparked farmer agitation this time. MSP would seem like a solution, but better to make farmers market-ready

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HISTORY REPEATS ITSELF, and does so when it is least expected. In 1979, Maharashtra saw its first farmer movement, led by Sharad Joshi in an area near Pune for a single crop, onion, that then expanded to cotton, sugar and tobacco. The recent strike, that subsided after the announcement of the state's loan waiver, emanated precisely from the same belt of comparatively prosperous western Maharashtra with richer, accessing better irrigation, more market-clued and progressive farmers. The monsoon this year has also been benign. The irony is that it is the better-off farmers that were agitating, not the ones from suicide-stricken Vidarbha.

What has gone wrong? No one can quite put their finger on the right explanatory button, but there were several triggers. A few are discussed here.

Loan waiver contagion after UP: Since the policy announcement by Uttar Pradesh's Yogi Adityanath government, if anyone thought that the waiver would be UP's internal affair, he or she was surely mistaken. Farmers across states had been agitating for similar waivers. A leading Marathi newspaper, Loksatta, published an article claiming that tax revenue from Maharashtra is helping UP and implicitly questioned why Maharashtra did not have loan waiver herself. The contagion effect was surely salient as farmers in Madhya Pradesh presented similar demands. The winding up of agitation after announcement of loan waiver highlights this.

The hurt is more intense when things are expected to be good, but they turn out differently: With good rains and record food-grain production, expectations were high. The cobweb model in economics—who all know heuristically, but rarely realise its brutal footprints—then came into play. With a glut in production, prices crashed to levels that seriously threatened livelihoods. That this happened when hopes and aspirations were running high naturally caused immense hurt. Pulses are representative of what went wrong or what can go wrong. In spite of a full-fledged policy on pulse pricing and procurement by ministry of finance, the tur situation in Maharashtra was precarious. The government faltered by starting procurements very late. If the government were to start early, the prices might not have crashed. Note that we use might instead of would because we do not believe MSP to be the panacea. The experience in tur certainly eroded the faith in government machinery.

Inept data: Area, production and yield are three levers for advance policy planning in agriculture. Getting these right is the most important task of the statistics office of agriculture department which uses dual sources. For area under the crop, revenue department is the source, and is supposed to validate with Taluka agriculture officer, while yield estimates are obtained from crop cutting experiments (CCE) by the agriculture universities. Overall, a tenuous and error-prone process for advance estimates.

Indeed, the second estimate of tur for 2016-17 spoke of 15.33 lakh hectare under cultivation with associated 11.71 lakh tonne (lt) production. The Maharashtra Economic Survey, released on March 17, 2017, used the second estimate figures. A fortnight later, the state's agriculture department revised the estimates with March tur yield projection much higher based on CCE. The third estimate showed no change in area, but production projection was revised to 20.35 lt, most likely due to new yield figures. This meant that tur output had nearly doubled, but the government realised this only by March 31, 2017. By not getting the data right and in time resulted in policy ambiguity and reflected in delayed procurement.

> **The second estimate of *tur* for 2016-17 was of 15.33 lakh hectare, with a 11.71 lakh tonne (lt) production. The third estimate showed no change in area, but the production projection was revised to 20.35 lt. This meant that *tur* output had nearly doubled, but the govt realised this only by March 31, 2017**

Maharashtra's farmers are more market oriented: Maharashtra might be a victim of its own success. It has become major producer of horticulture crops, and volatility in prices for these have always been more pronounced. A history of cobweb repeats in horticulture crops year after year, as it happened for onions and tomatoes this year, plagues the state.

What do these stylised facts augur in terms of solutions? There are only three possible ways for escaping the price collapse: a price guarantee system like MSP, market integration linking surplus and deficit areas and processing to prevent distress sale of perishables. The e-NAM was announced recently but progress has been tardy. It is a no-brainer that without a system of gradation and certification, such long-distance transactions would not take off. One should ask how many kilograms of onions were sold on e-NAM portal and how much of it was processed? The answers to these questions provide the key, and the solution need not lie in riding another MSP bus. If MSP were the solution *per se*, Punjab would not be working on its own loan waiver.

MSP is not a magic wand because there are no magic wands. Yet, if it were to be adopted, we need a proper system of farmer registration for traceability and eligibility. It is informative that agitation was focused on price support (apart from loan waiver). We did not see demands such as set up a processing facility, provide seed capital for transitioning to e-NAM. Unless we help farmers get market-ready that includes getting to produce differentiated products, history would get repeated. Unless each onion is not the same, it would bring tears when squeezed.

LETTERS TO THE EDITOR

Get past GST's teething troubles

Apropos of "Cos face jail term for not reprinting revised MRP (*FE*, July 8), discerning the problems of a hasty entry, the Union consumer affairs minister's brief instruction to reprint the new maximum retail prices on the unsold inventory, and the Kerala finance minister's—who incidentally is the chairman of the GST Council—terse statement that the existing printed prices of the pre-GST stock should stay unchanged should be construed as the birth pangs of the new tax regime. The yet to be set up National Anti-Profiteering Authority, a three-tier structure, is basically a machinery to monitor the transfer of the reduction in the rate of tax on the supply of goods or services or the benefit of input tax credit to the consumers. The silence of the Rules framed under the CGST Act 2017 on the arbitrariness in fixing MRP, exploiting the demand and supply, and in disregard to cost of production, is unexplained. Pricing in the service sector, principally to bill the voice and data transfers, has never been transparent and simple to comprehend for the interested party, the recipient of services. Among the myriad issues that crave for urgent resolution, the case of works contract stands out. With multiple contractors and sub-contractors engaged in the construction process, factoring input tax credit in the pricing of apartments is stuck in the whirlpool of uncertainty.

— Haridasan Rajan, Kozhikode

CJI under RTI

Apropos of "Transparent justice" (*FE*, July 10), kudos to the Supreme Court for realising that the CJI's post should come under the RTI Act. The apex court has so far resisted it and is hearing a clutch of appeals against rulings that say the CJI is subject to the provisions of the transparency law. While the apex court inviting RTI scrutiny for the CJI's office is welcome, the need is to get political parties to come under the law given how their members shape all policies.

— Sumona Pal, Kolkata

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STOCK PRICE MOVEMENTS

Finding method in madness

A major anomaly was FY17, when GDP growth slowed down quite distinctly from 8% to 7.1%. Yet, the Nifty has increased by 5.6% and this enthusiasm carries on even today with the market moving by an average of 12% in the three-months period over 2016-17

STOCK MARKETS ARE always an enigma as very often it is hard to rationally explain price movements. Market transactions which determine the final price on a real time basis could be driven by several factors and often it is difficult to distinguish between a forward looking view and a contemporary one. A press conference on GST can buoy the markets either way, but it would be back to normal the next day. This is what makes it challenging to take a view on prices.

Add to this the plethora of advice that the reader or viewer gets on individual stocks every day, and one can be confused about investing for a long term horizon, as one can never be sure whether it is the right time to buy or sell. And, much like the economic forecasts where economists have an array of numbers for the same variable, two experts could be advising differently—one to buy and the other to sell the same stock.

Is there any sense in these numbers? For example, if one looks at the banking stocks today, the NSE sectoral index shows that since April there has been an upward movement in banking stocks even though the banking problem has been very much deep rooted. The talk is on merging PSBs and infusing capital, and there was gloom when uttering the word 'banks'. But the announcement that there could be a solution in the offing on NPAs through the IBC has spurred a revival in confidence in these stocks and the sentiment is positive. Otherwise, for a sector which is still looking for the proverbial light at the end of the tunnel, there should be despondency everywhere.

FY17 was surprising for market dichotomy because it came at a time when the govt went for demonetisation, which pushed back growth to a significant extent

A way out is to see if stock indices reflect the core strength of the economy and the best way out is to look at the GDP. This can be done over a longer period of time logically, and annual numbers make sense. In fact, even monthly data on variables like industrial growth, inflation, interest rates, primary issuances, etc, do not link well with stock movements, though FPIs have a better fit. Very short-run influences would be nebulous as with stagnation in the industry, growing NPAs, limited private investment and a decline in credit growth, stock market sentiment cannot logically be positive or change that soon. Of course, experts aver that stock prices are forward looking and if the expected earnings justify a forward looking number then they should also be ahead of the curve. At times it is argued that as future earnings matter more than the past; hence rising stock market heralds only better times.

At the other end, mutual funds are singing a lilting tune with almost every scheme showing fabulous returns over five years, which gives the impression that any such investment would have beaten the market. This is intuitively not surprising because if the Nifty is reigning at an all-time high, any comparison with earlier years would necessarily denote such high returns and would increase if one moved back in time.

Therefore, ideally, an average index for the year is more appropriate as it isolates these end point swings which can kill the good mood. This average movement in the Nifty can be compared over time to gauge whether or not it has kept pace with GDP growth. This would be a pragmatic way of looking at such relationships.

The table alongside provides information on GDP growth since 2006-07 and average Nifty for each of the years up to 2016-17.

The table shows that up to 2015-16, in general, the stock market movements were in line with the GDP growth rate of higher growth in the latter being associated with higher Nifty movements. 2012-13 was the only exception where the Nifty went up by 5.3%, even as GDP growth slowed down from 6.7% to 5.5% (this would hold even with the earlier base year of 2004-05). The year 2015-16, witnessed virtual stagnancy in the Nifty on an average basis, but GDP growth increased at a higher rate. Very significantly in 2008-09, following the global financial crisis, the Nifty had almost crashed by around 24% as GDP growth also slowed down by a little over 250 bps.

The major anomaly was 2016-17 when GDP growth slowed down quite distinctly from 8% to 7.1%. Yet, the Nifty has increased by 5.6% and this enthusiasm carries on even today with the market moving by an average of 12% in the three-months period over 2016-17, which is remarkable. Growth indicators have not quite started looking up as yet though there is the ubiquitous hope that it should happen in the second half of the year.

The movement in 2016-17 was surprising because it came at a time when the government went in for demonetisation, which did push back growth to a significant extent. However, if a reason has to be ascribed, the credit for higher FPI funds coming in, which is the main driver, can be attributed to the reforms agenda of the government especially with the expected determined implementation of the GST. Also, the demonetisation move could have been interpreted positively as a frontal attack on black money which is expected to yield long term gains when combined with GST. Therefore, the rise can be attributed more due to positive sentiment than any parallels being witnessed in the growth canvas.

These numbers, hence, do indicate that if stocks have to be correlated with GDP growth over a longer period of time of say a year, on an average they would reflect well the state of the economy. Can the Nifty then be taken to be a leading indicator of the economy? Probably, yes, because in seven of the 10 years, the relation did hold and in another one, 2015-16, one would not have lost. The current situation, however, still warrants raised eyebrows, but as all expectations are that the economy will do only better than 7.1% this year, then rising stock prices must signal the same, though the extent may be interpreted as being a trifle exaggerated. But for long term investors, getting in may not be a bad idea still if one is looking at a longer time horizon when GDP growth should be ascending the scale and move towards the 8-9% mark. To put it conversely, if we expect higher growth in future, then the returns on the bourses must also get better.

Short-term investors, however, can never be sure, but probably that is the thrill about such investing.

Real vs the market economy

Year	Nifty	GDP growth	Nifty change (%)
2006-07	3,572	9.6	10.4
2007-08	4,896	9.3	37.1
2008-09	3,726	6.7	-23.9
2009-10	4,664	8.6	25.2
2010-11	5,584	8.9	19.7
2011-12	5,240	6.7	-6.2
2012-13	5,520	5.5	5.3
2013-14	6,010	6.5	8.9
2014-15	7,972	7.2	32.6
2015-16	7,981	8.0	0.1
2016-17	8,424	7.1	5.6
2017-18*	9,428	?	11.9

*June 30

BIT BY BIT

Yes, TV has a problem

NANDAGOPAL RAJAN

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TV audiences are increasingly going digital, but are television stations in India waking up?

I AM WHAT SOME call a cord cutter. I am not fully there yet as there are still cords coming into my house with television content, meant primarily for the kid of the house. Despite these paid television subscriptions at home, I have not watched it for a year and am unlikely to watch anything until the next season of MasterChef Australia. I do consume a lot of content on my television, but they are all internet-based. At the moment there is nothing on Indian television that would make it watch it, not even news (not that there is news on Indian television either). I think herein lies a problem for television in general.

At home, I have multiple options to watch content. An LG smart TV that has YouTube and Netflix. An old TV connected to Apple TV with a whole bunch of apps that stream content—for the rest I can just play on the phone or Mac and mirror to this screen. I have also tried Google Chromecast, which lets me stream from an Android smartphone and there was my old Amkette EvoTV that gave me access to a whole bunch of Android apps as well to my entire collection of videos. The choice is endless, especially now since the Amazon Fire Stick has also been introduced in India.

To see what the future of TV looks like, you just need to plug in an Apple TV and see the apps that reside on this small box. The most telling one is Facebook.

It is time that Indian TV houses start thinking ahead like HBO has, by creating content primarily for a digital audience. The TV audience is moving and it is time companies started looking beyond the idiot box

We all use the social network, but its avatar on TV has just video, and it is a web of content that is hard to come out of as the platform knows what you like to watch. Then there are apps like Hyper and Big Story which just decide that this is the best of what you can watch at the moment. This is the curation of content based on themes and topics, and often the selection is good enough to have you hooked. And it works, drawing you into a pool of content that you love and or had no idea you loved.

For those who still need their dose of straightforward old fashioned television, but at their convenience and timings, there is always Hotstar, which is now becoming the go to place for live sports. For those looking for made for digital content—by that I mean content that is made for binge watching and thus using up your monthly quota of data in a few days—there is Netflix and Amazon Prime.

Once these two entities start creating more Indian content there is a possibility that Indian television will feel the pressure, at least in the urban households. Cheaper hardware and data is only making the transition smoother for a lot of households. Once exposed to this content, it is only a matter of time before they realise the inferiority of what they are being served at the moment. Even for cheap soaps, YouTube is a better platform these days as you get all episodes on a platter and can easily skip the ones that don't take the story further.

If you ask me, the future of television is digital and by that, I don't mean flat panels of the move away from analogue. The future is content that has been created for consumption over digital pipelines, for people who are used to digital consumption patterns and know the power of choice is what makes these content creators weed out stuff that has no chance of working.

Also, the internet lets Indian viewers expose themselves to content from all over the world and it is only a matter of time before more content players like Hulu make a beeline for the country. This is why it is time that India television houses start thinking ahead like HBO has, for instance, by creating content primarily for a digital audience. The television audience is moving and it is time companies started looking beyond the idiot box.

GOODS AND SERVICES TAX

Building on the new tax regime

GST will boost infra sector by eliminating multiple taxes and simplifying the law, but it will also impact the cost of goods and services used in construction and increase compliance

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"Difficult roads lead to beautiful destinations." -Anonymous.

THE NEW TAX reform will pose several challenges for the infrastructure sector such as treating of works contracts as service contracts, the imposition of new tax rates on ongoing projects, and change in the costs of construction materials. However, the advent of GST is also expected to boost the infrastructure sector with the elimination of ´tax on tax' and the introduction of input tax credit (ITC).

Under the previous tax regime, it was a litigious issue of whether infrastructure contracts have to be treated as 'supply of goods' or 'provision of service' contracts, or as a composite works contract involving the supply of both goods and services. While Value-added Tax (VAT), a state tax, was applicable to the 'supply of goods', a service tax, a central tax, was applicable to 'provision of service'. With the implementation of GST, these litigations will come to an end. The Central GST Act, 2017 (GST Act), specifically provides that 'works contract' as well as 'construction of a complex or a building, civil structure or a part thereof' shall be treated as the supply of services. Even though this provision will provide clarity to a great extent, it may not be able to eliminate ambiguity completely. Contracts in the infrastructure sector can be quite complex, and determining the nature of these contracts would be difficult.

Under the previous regime, a majority of construction contracts, being work contracts, were subject to a combination of both service tax and VAT. A service tax of around 4.5% (assuming taxable component of the service contract is 30%) and VAT ranging from 1-15%, depending upon the state, was applicable to construction contracts. Thus, under the earlier regime, the effective tax incidence for an average construction contract, ranged from 11-18%. Moreover, there were several construction activities, such as the construction of roads, dams, irrigation, that were exempt from service tax.

With the rollout of GST, the rate of 18% for works contracts is higher, and the difference is more prominent for construction activities falling under the service tax exemption category. However, this higher GST rate could be set off by the benefit of input tax paid and ITC on the raw materials. On the other hand, a higher GST rate could also result in higher costs, if there is limited scope for renegotiating construction contracts, and contracts that do not account for contingency factors.

The cost of construction services will also be impacted due to credit restrictions provided under Section 17(5) of the GST Act. According to the aforesaid section, a contractor will not get ITC for the supply of works contract service for construction of an immovable property but can avail the benefit of ITC on construction services availed from the sub-contractor. Furthermore, the aforesaid section also provides that ITC shall not be available for goods or services or both received by a taxable person for construction of an immovable property (other than plant or machinery) on his own account, used in the course or furtherance of business. Thus, these provisions are complicated and contradictory.

We can see that implementation of the above-mentioned credit restrictions can have an adverse impact on the infrastructure sector. However, this does not seem to be the intent of the lawmakers, as seen from the 'Schedule of GST Rates', which clearly provides that full ITC will be available for the composite supply of works contracts. Thus, we cannot conclude that higher GST rate on works contracts will be neutralised by ITC until explanation and clarity are sought with respect to the aforesaid credit restrictions.

GST would also make compliance easier by eliminating multiple indirect taxes. However, it would require contractors to register in multiple states owing to the requirement of registering at the place of supply of service. Contractors would also have to compulsorily register in a state where it supplies services but has no fixed place of business, owing to the concept of "casual taxable person". These provisions will increase the compliance costs for construction companies. Furthermore, companies will have to incur the costs of upgrading their IT systems, as input credit would be available only after an online reconciliation of tax invoices.

With the advent of GST, there will also be a change in the cost of construction materials. For example, a higher GST rate of 28% imposed upon cement would adversely impact construction cost. Similarly, electricity is not within the ambit of GST and input tax will be an additional burden for the infrastructure industry.

We cannot conclusively comment on the impact of higher GST rate on the infrastructure sector, as there is still ambiguity with respect to credit restrictions. GST will boost the sector by eliminating multiple taxes and simplifying the law, but it will also impact the cost of goods and services used in construction and increase compliance costs. It is still very early to make a judgment on the new tax reform. We should wait till it concretises.