

# **GOVERNMENT OF PUNJAB**



## **MEMORANDUM TO GOVERNMENT OF INDIA**

**A Case for Extending  
Goods and Services Tax (GST) Compensation:  
Punjab**

# A Case for Extending Goods and Services Tax (GST) Compensation: Punjab

**1.1.** The provisioning of Government services and its maintenance expenditure necessitates the need of levying taxes. India, in its journey of progress, had implemented the Goods and Services Tax (GST) across the country w.e.f. 01<sup>st</sup> of July, 2017 subsuming a large number of indirect taxes earlier levied by Government of India and State Governments independently. The details of Central and State taxes subsumed into the GST are summarized in Table 1.

**Table 1: Central and State taxes subsumed in GST**

Central Taxes	State Taxes
Central Excise Duty	State Value Added Tax (VAT) (except VAT on petroleum and liquor)
Duties of Excise (Medicinal and Toiletries Preparations)	Central Sales Tax (CST)
Additional Duties of Excise (Goods of Special Importance)	Purchase Tax
Additional Duties of Excise (Textile and Textile Products)	Luxury Tax
Additional Duties of Customs (Commonly known as CVD)	Entry Tax
Special Additional Duty of Customs (SAD)	Entertainment Tax (except levied by local bodies)
Service Tax	Taxes on advertisements
Cesses and Surcharges related to supply of goods and services	Taxes on lotteries, betting and gambling.
State Cesses and Surcharges related to supply of goods and services	

Source: Department of Excise and Taxation

## 1.2 Taxes on Goods

**1.2.1** As far as the implementation of GST is concerned, both the Union as well as the States have ceded their fiscal autonomy to the GST Council with a long term objective of having uniform procedures and rate of taxes across the

country. Thus, the State Government no longer has the autonomy to change the tax rates either to compensate for the loss of the revenue or to augment its revenue.

**1.2.2** The net effect of taxes subsumed in GST in the State for 2015-16 is brought out in Table 2.

**Table 2: Net Effect of Taxes Subsumed in GST**

Item	Amount (Rs. crore)
VAT (includes Purchase Tax on food grains but excludes VAT on petroleum and liquor)	12532
CST	568
Entertainment Tax	174
Luxury Tax	
Lottery, Betting & Gambling	
Advertisement Tax	18
Entry Tax including Octroi and ETTSA Fee	138
Cesses and surcharges (ID Fee on food grains)	1042
Duties on Excise on medicinal and toilet preparations	0.06
Additional amount certified for compensation	504
<b>Total</b>	<b>14975</b>

Source: Department of Excise and Taxation; Figures rounded off to nearest rupee

**1.2.3 Consumption Pattern in Punjab:** A study of consumption pattern in both rural and urban Punjab reveals that in urban areas, 56% of the total value of per capita consumption per month is on food items, fuel & electricity and clothing which are either exempted under GST or are being taxed at a lower rate while 31% of the total value of per capita consumption per month is on services. Out of total value of per capita consumption on services, 22% is on health and education which are again exempted under GST.

**1.2.4** In rural areas, 60% of the total value of per capita consumption per month is on food items, fuel & electricity and clothing which are either exempted under

GST or are being taxed at a lower rate. 26% of the total value of per capita consumption per month is on services. Out of total value of per capita consumption on services, 57% is on health and education which are exempted under GST. Table 3 highlights the consumption pattern in both rural and urban areas of Punjab.

**Table 3: Consumption Pattern**

Commodity	Urban		Rural	
	Per capita consumption per month (Rs.)	Percentage	Per capita consumption per month (Rs.)	Percentage
Food Items	1145	41.1	1033	44.1
Fuel and Light	264	9.5	229	9.8
Clothing	149	5.3	132	5.6
Personal Transport	67	2.4	73	3.1
Other household consumables	56	2.0	52	2.2
Toilet Articles	59	2.1	48	2.1
Intoxicants	27	1.0	44	1.9
Footwear	36	1.3	32	1.4
Jewelry	10	0.4	21	0.9
Cooking and household appliances	18	0.6	19	0.8
Repairs of buildings	18	0.6	12	0.5
Bedding	10	0.4	9	0.4
Consumer Taxes and Cesses	4	0.1	9	0.4
Other personal goods	17	0.6	7	0.3
Utensils	4	0.1	4	0.2
Minor durables	5	0.2	4	0.2
Furniture	8	0.3	4	0.2
Goods for recreation	7	0.3	3	0.1
Therapeutics appliances	0	-	0	-
Tobacco	13	0.5	8	0.3
Pan	1	-	0	-
Services	871	31.2	603	25.7
<b>Total</b>	<b>2789</b>	<b>100.0</b>	<b>2345</b>	<b>100.0</b>

Source: Report by MOSPI- Household Consumption of Various Goods and Services in India 2011-12

It is evident from Table 3 that **the consumption pattern of the population in both urban and rural areas and the expenditure thereon is tilted towards the items which are either exempted under GST or are being taxed at a lower rate, whereas there is negligible spending on luxury and high end goods and services taxable at higher rate of tax.**

**1.2.5 Subsuming Purchase Tax in GST:** Punjab being an agrarian economy was deriving a significant portion of its revenue from agriculture sector in pre-GST era by imposition of tax on agricultural produce (mainly food grains). This was realized in the form of levy of Purchase Tax on agricultural produce, @ 5% of MSP of produce collected from the purchaser of such produce. In addition, an Infrastructure Development Fee (I.D Fee) @ 3% was also levied on purchase of food grains. The State collected Rs. 3094 crore during the financial year 2015-16 from the Purchase Tax and I.D. Fee alone, i.e. 16.55% of its Total Tax Revenue of Rs. 18692.89 crore during that year. With the implementation of GST, both the Purchase Tax and I.D. fee on food grains have been subsumed in GST. **Since the GST is a destination-based tax and agricultural produce is largely exempted under GST, therefore the State of Punjab has experienced a permanent loss of a significant portion of the State revenue.**

**1.2.6** Out of the total Protected Revenue under GST for the financial year 2021-22 of Rs. 32871 crore, the share of Purchase Tax and I.D. fee on food grains amounts to Rs. 6791 crore (applying 14% growth rate to the base year figure of Rs. 3094 crore). Thus, the **revenue under these two heads which constitutes around 21% of the Protected Revenue and have been subsumed under GST are in the nature of permanent loss for the State and will have a debilitating impact if the compensation regime under is not continued.**

**1.2.7 Impact of Agrarian Crisis on GST Growth:** Although the State economy is under structural transformation, yet agriculture sector is the largest contributor to the Gross State Value Addition (GSVA) of Punjab wherein agriculture and allied activities contributed 24.64% in 2019-20(Q)<sup>1</sup> and 27.25% in 2020-21(A)<sup>2</sup> to the GSVA of Punjab at constant prices and agriculture sector provides the employment to 36% workers of Punjab (Census 2011). Despite agriculture sector of Punjab being instrumental in ensuring National Food Security, agriculture in the State is in deep crisis and facing serious challenges such as over exploitation of scarce water resources, mounting debt on farmers, rising incidences of farmers suicides etc. **Owing to the serious agrarian crisis, the per-capita consumption expenditure in rural areas of Punjab is getting more and more skewed towards essential commodities that are either exempt or attract low rates of tax under GST. This trend does not augur well for the consumption-based GST growth of the State as 62.5% of total population of Punjab is rural (Census 2011) which is primarily engaged in agriculture and the allied activities.**

**1.2.8** Further, due to limited growth of employment opportunities caused by shifting of industries to tax holiday destinations and disadvantageous position of the State with regard to mineral resources, the consumption expenditure in the urban areas pertaining to the commodities other than essential items, is also not very encouraging. GST being the destination-based tax, this trend definitely has a bearing on the overall GST revenue collection of the State.

**1.2.9** Apart from this, in the earlier VAT regime, the inter-State sales were subject to CST @ 2%, which now stands subsumed in GST. Punjab earned Rs. 568 crore from CST in the year 2015-16. The application of expected annual growth rate @ 14% would have resulted in CST collection of Rs. 1247 crore in 2021-22. With GST being destination based consumption tax and inter-State

<sup>1 & 2</sup> Central Statistical Organization, New Delhi

supply being subjected to Integrated goods and Services Tax (IGST), the tax shall accrue to the State or Union Territory in which the goods or services are consumed. Furthermore, the IGST leviable on the inter-State sales, is available as Input Tax Credit (ITC) for discharging the tax liability on local sale. It is completely used to set off the liability in the destination State, whereby nothing accrues to the originating State. Since there is no CST, the above amount will be a complete loss of revenue for the State of Punjab after the end of the revenue compensation period.

**1.2.10** Under the VAT regime, States had different rates of taxation depending on the quantum of consumption of such items in the State. The rates of the taxes in the State of Punjab were comparatively on a higher side, and broadly the commodities were taxable at the rate of 6.05%, 6.87%, 14.30% and 15.95% (inclusive of 10% surcharge). As an example, tax rate on cold drinks was 30.25% and cigarettes was 33%. Large number of commodities taxed earlier @ 14.30% and @ 15.95% by the State of Punjab, have now under GST, been placed in the lower tax slabs. Similarly, a number of commodities taxable earlier @ 6.05% and @ 6.87% are now either exempted or are covered in the tax slab of 2.5% in GST, like milk products, medicines, tea, yarn, etc. **Thus, with the implementation of Goods and Services Tax, the effective rate of taxation has been significantly reduced in Punjab.** Since the tax rates are no longer within the ambit of the State Government, the State can in no manner make up for the losses on account of reduction in tax rates.

**1.2.11** There are other minor factors which have an impact on GST revenue for the State in comparison to the erstwhile VAT revenue. The Central Excise levied by the Central Government on manufacturing used to be included in the base price of the commodity to arrive at an assessable value for the purpose of calculation of VAT resulting in cascading effect of taxes. Secondly, the fitment of rates in GST has been done by adding the rate of Central Excise, Service Tax

and VAT. The cross utilization of these taxes as Input Tax Credit (ITC), which was hitherto not allowed, has been enabled under GST which has resulted in reduction of the net revenue.

**1.2.12 The cumulative effect of Purchase Tax, I.D Fee and CST combined has resulted in a revenue loss to the extent of Rs. 8038 crore during 2021-22 to the State of Punjab.** Though, presently the compensation regime envisaged under GST is providing for the said shortfall, but the same will be a major cause of worry for the State once revenue compensation is no longer available, after 30<sup>th</sup> of June, 2022.

## **1.3 Services**

**1.3.1** The GST regime has been facing the challenge of identification of revenue from various sources i.e. goods and services particularly on account of non-implementation of the originally envisaged return system. However, based on certain identified parameters efforts have been made to identify the revenue from services sector. The amount of tax collected from services during the financial year 2020-21 was Rs. 2339 crore. For the financial year 2019-20 the amount of tax collected from services was Rs. 2441 crore.

**1.3.2** Goods and Services Tax is essentially a Value Added Tax with services included. Before the implementation of the GST, it was expected that loss in terms of revenue will largely be compensated with the additional revenue from the services. However, even after more than four years of implementation of GST and despite putting best efforts, it has been noted that the additional revenue from the GST on services has not been able to make up for the loss that the State has suffered. The basic reasons for this are not very difficult to apprehend.

**1.3.3** Firstly, in pre-GST era, credit of the tax paid on services was not available for discharging the tax liability on goods. But under GST regime, cross utilization



of input tax credit of services is available for discharging the tax liability on goods and vice-versa. The cross utilization of ITC between goods and services is quite significant. Conversely, in the VAT regime, the credit of the tax paid on goods was also not available for discharging the tax liability on services. For example, the State was deriving revenue on account of entertainment tax on Dish TV service providers, and there was no input tax credit available to them. **Now, under GST regime, input tax credit of both goods and services is available to the service providers, hence, there will be a loss of revenue from this sector.**

**1.3.4** Secondly, **the disposable income in the hands of people residing in the metropolitan cities is more as compared to other cities, and consequently, spending is also significantly higher for metro-dwellers compared to others.** The expenditure on lifestyle and leisure services i.e. dining out, fitness, fashion and entertainment is more in metropolitan cities. The tax on services is going to the States where the services are being consumed. Thus, metropolitans are gaining from service sector. The revenue derived from GST from services is not equitably distributed amongst all the States in the country. The States with metropolitan and other bigger cities have gained disproportionately on account of GST on services, while the States like Punjab, which are primarily agrarian and rural in character, have heavily lost on this account.

**1.3.5** Thirdly, **very few big players of Service Sector are currently operating in Punjab, whereas majority of taxpayers of Service Sector would be covered under the category of the Micro, Small and Medium Enterprises (MSME), the Sector which is already coping up with the numerous problems under GST regime.**

**Punjab has a huge disadvantage with its Capital city, Chandigarh, being a Union Territory. Thus, while all the other states benefit from the large consumption in its Capital city, Punjab faces a huge loss. This is not only limited to GST but also has an impact when U.T. of Chandigarh decides to have a lower tax rate on goods outside the GST like petroleum product and liquor for human consumption.**

## **1.4 Compensation Cess**

**1.4.1** The genesis of the GST compensation lies in the deliberations of the GST Council where it emerged as an important convergence point for the States to agree with the rollout of GST. In fact, if the history of the introduction of GST is analyzed it may emerge that the solemn guarantee by the Central Government to provide for compensation to the States for any revenue loss that may arise on account of introduction of GST was the sole binding force that paved the way for the commitment by the States to agree to the introduction of GST in the country. The same was enshrined in the 101<sup>st</sup> Constitutional Amendment Act, 2016 and was thereby given a constitutional status. The legal obligation of the Central Government to provide for this compensation to the State has been captured in the GST (Compensation to States) Act which was enacted in 2017 on the recommendation of the GST Council. The Act empowers the levy of the Compensation Cess on goods and services the proceeds of which will be utilized for the payment of the compensation to the States. As per the Goods and Services Tax (Compensation to States) Act, 2017, the states are to be compensated for any loss of revenue arising on account of implementation of GST for the period of first five years.

**1.4.2** Before GST was implemented, it was presumed that GST will bring in increased compliance which will yield a significantly higher revenue and in turn

would compensate the short fall in revenue in all the states. **As evident from Table 4, State's revenue from the major commodities like automobiles and auto parts, cycle and cycle parts, hosiery, readymade garments, soft drinks and cement has decreased in comparison to the revenue being earned from the said goods in the pre-GST regime.**

**Table 4: Analysis of Revenue from Commodities (Rs. Crore)**

Name of the commodity	Tax rate under VAT	Tax rate under GST	Gross Turnover		VAT Collections*	GST Collections#
			VAT (9 months)	GST (9 months)		
Cement	14.30	14	8087.8	7350.01	528.66	426.71
Electronics	15.95	14	9753.00	10944.00	320.00	340.00
Chemists and Druggists	6.87	2.50	12999.04	26400.74	239.86	188.05
Yarn	3.63	2.5	18152.63	18180.66	138.35	179.95
Cycle and Cycle Parts	6.05	6	10101.71	11166.84	38.76	-170.67
Sewing Machines	6.05	6	981.44	1236.16	7.62	-10.15
Automobiles and Auto Parts	13.20	14	26960.45	34215.84	1230.93	980.46

Source: Department of Excise and Taxation

\* Pro-Rata Tax paid for 9 months under VAT

# paid for 9 months 2017-18(July-17 to March 18)

**1.4.3** GST revenue have, thus, not shown the kind of buoyancy that was expected. During the last four years, the revenue generation under GST regime is not as robust as was expected and has also been adversely impacted by the COVID-19 Pandemic. Further, the demon of OMICRON is staring at us and making future uncertain and unpredictable. If we look at the data of the GST revenue over the years, it emerges that for the year 2019-20 the growth rate was 4% over the year 2018-19 followed by negative growth of 7% in the year 2020-21. Thus, the revenue from GST has not come up to the expectations and therefore the premise on which the compensation period of five years was constructed is no longer relevant.

**Table 5: All India GST Collection over the years**

Year	GST Revenue	Percentage Growth
2018-19	1177370	
2019-20	1222131	4%
2020-21	1137119	-7%

Source: Department of Excise and Taxation

It is pertinent to mention here that the GST Council had endorsed the agenda in the 42<sup>nd</sup> meeting of the GST Council, for extension of levy of GST Compensation Cess beyond the transition period i.e. (beyond June, 2022) till the entire shortfall is covered with periodic review of the extension.

**1.4.4** The States are extantly being compensated from Goods and Services Tax Compensation Fund. Compensation Cess is levied on pan masala, tobacco and manufactured tobacco substitutes, including tobacco products, coal, briquettes, ovoids and similar solid fuels manufactured from coal, lignite, whether or not agglomerated, excluding jet, peat (including peat litter), whether or not agglomerated, aerated waters and motor cars and other motor vehicles principally designed for the transport of persons (other than motor vehicles for the transport of fourteen or more persons, including the driver), including station wagons and racing cars, specified motorcycles, other aircrafts for personal use, etc.

**1.4.5** The rate of Compensation Cess is different for different commodities. It is worthwhile to note that this Compensation Cess was earlier a part of the State taxes. For example, cigarettes attracted Basic Excise Duty (BED) and Additional Excise Duty (AED) as Central taxes in pre-GST regime and the rates were according to the length of cigarettes. VAT @ 33% was levied on cigarettes in the State of Punjab. Under GST regime, cigarettes are taxable @ 28%., while the rate of State Goods and Services Tax (SGST) is only 14%. This has also resulted in revenue shortfall for the State.

## 1.5 Fall off the Cliff

**1.5.1** The year-wise GST collections and shortfall w.e.f. July 2017 for Punjab have been delineated in the Table 6.

**Table 6: Year-wise Shortfall (July 2017 to December 2021) (Rs. crore)**

Month	Protected Revenue	SGST <sup>#</sup>	Shortfall against Protected Revenue	Compensation Received	Shortfall as % of Protected Revenue
	2	3	4 (2-3)	5	6 (4/2%)
July 2017-March 2018	12976	7897	<b>5079</b>	4037	<b>39%</b>
April 2018- March 2019	22188	13568	<b>8620</b>	7129	<b>39%</b>
April 2019- March 2020	25296	13294	<b>12002</b>	8805	<b>47%</b>
April 2020- March 2021	28836	12663	<b>16173</b>	18050*	<b>56%</b>
April 2021- December 2022	24651**	11676	<b>12975</b>	14737*	<b>52%</b>
<b>Total</b>	<b>113947</b>	<b>59098</b>	<b>54849</b>	<b>52758</b>	<b>48%</b>

Source: Department of Excise and Taxation.

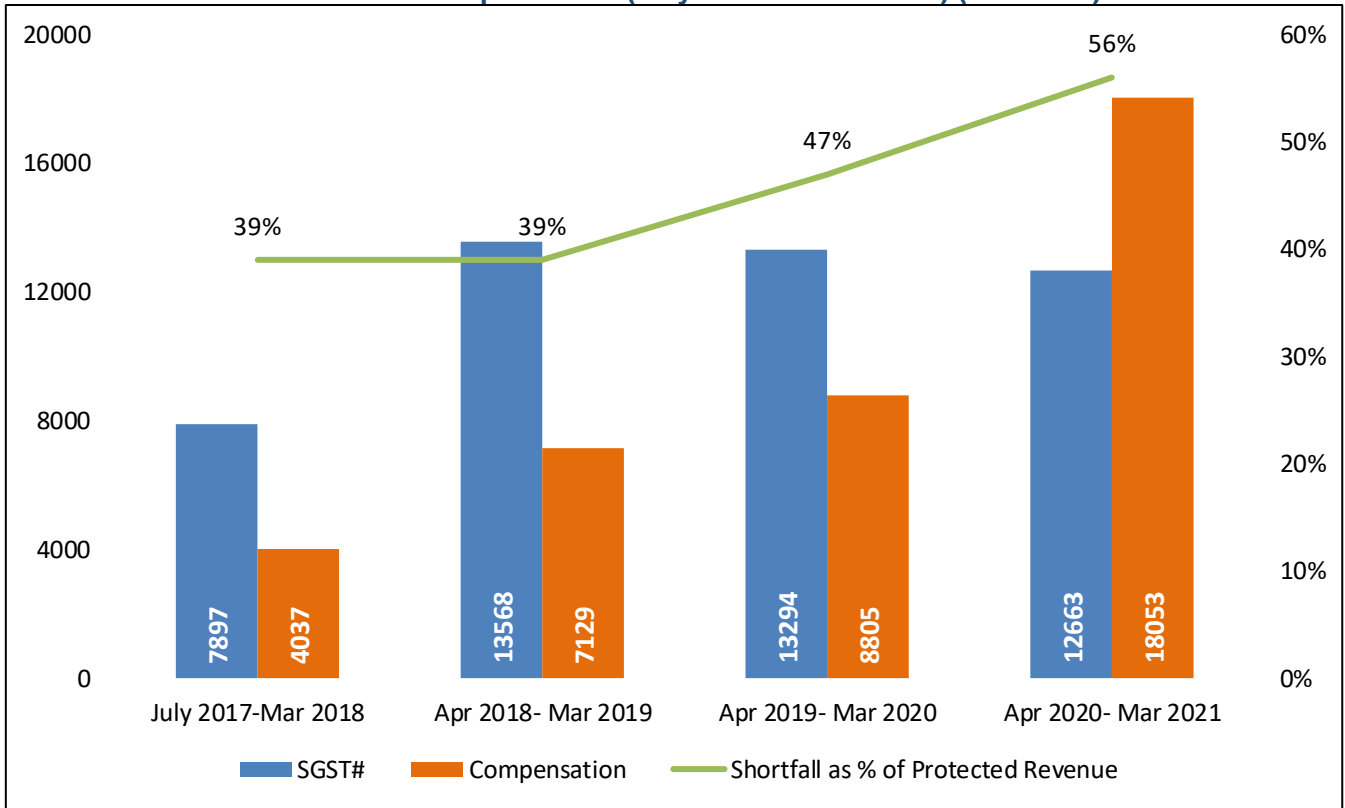
<sup>#</sup>SGST includes IGST Provisional and Adhoc IGST; <sup>\*\*</sup> Proportionate for 9 months

\* Includes Back-to-Back loans (in lieu of GST Compensation) of Rs. 8359 crore in 2020-21 and Rs. 12132 crore in 2021-22.

The average shortfall has been calculated after taking into consideration both provisional as well as ad-hoc settlement of Integrated Goods and Services Tax (IGST). The State of Punjab has experienced an average shortfall of 48% during the period July, 2017 to December, 2021.

**1.5.2** The year-wise SGST collections, Compensation and Shortfall (%) over the last four years is reflected in Chart 1.

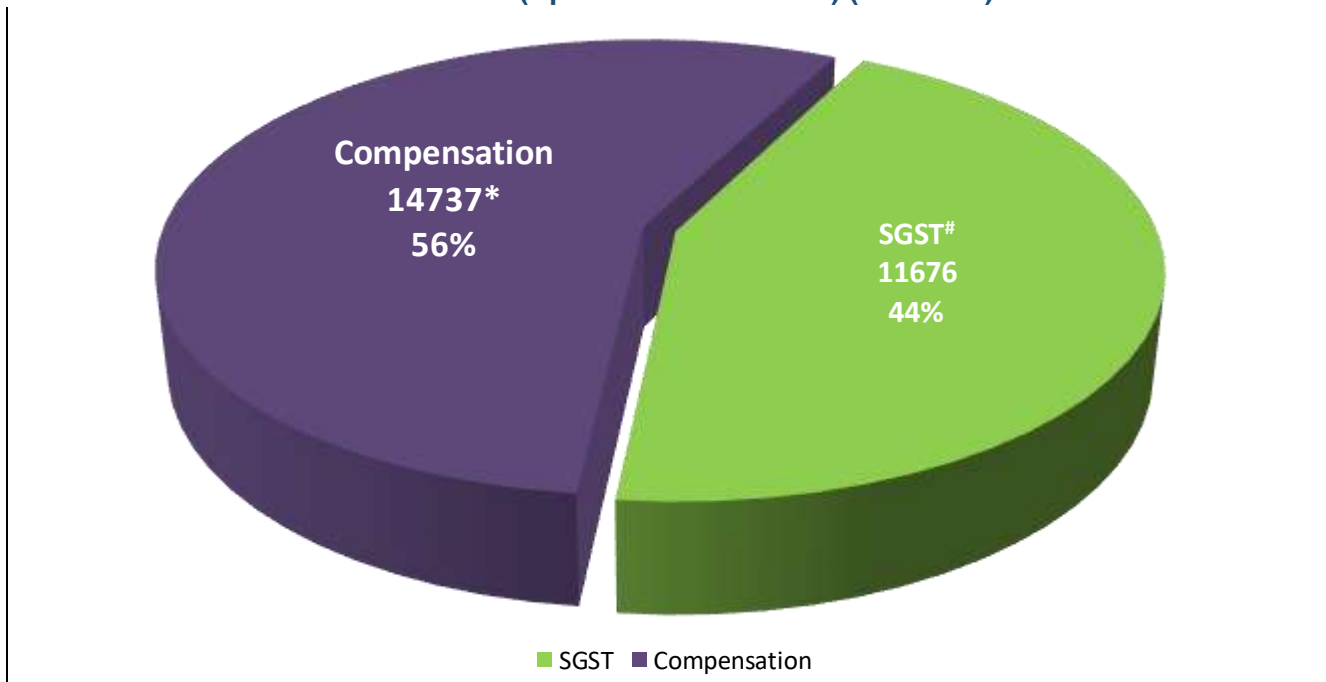
**Chart 1: SGST and Compensation (July 2017- March 2021) (Rs. crore)**



#SGST includes IGST Provisional and Adhoc IGST

**1.5.3** The percentage share of SGST and Compensation in total GST collections received during 2021-22 is as highlighted in Chart 2.

**Chart 2: Total GST (April - December 2021) (Rs. crore)**



Source: Department of Excise and Taxation

\* Includes Back-to-Back loans (in lieu of GST Compensation) of Rs. 12132 crore

#SGST includes IGST Provisional and Adhoc IGST

**1.5.4** Table 7 depicts the Compensation Gap (Actual Revenue against the Protected Revenue) for the States. It clearly highlights the fact that the compensation under GST is no longer a regional concern but has reached a national crescendo on account of most of the States being in the red. There has been yawning gap between the protected revenue and actual revenue for all the States.

**Table 7: State wise GST Compensation Gap (in percentage)**

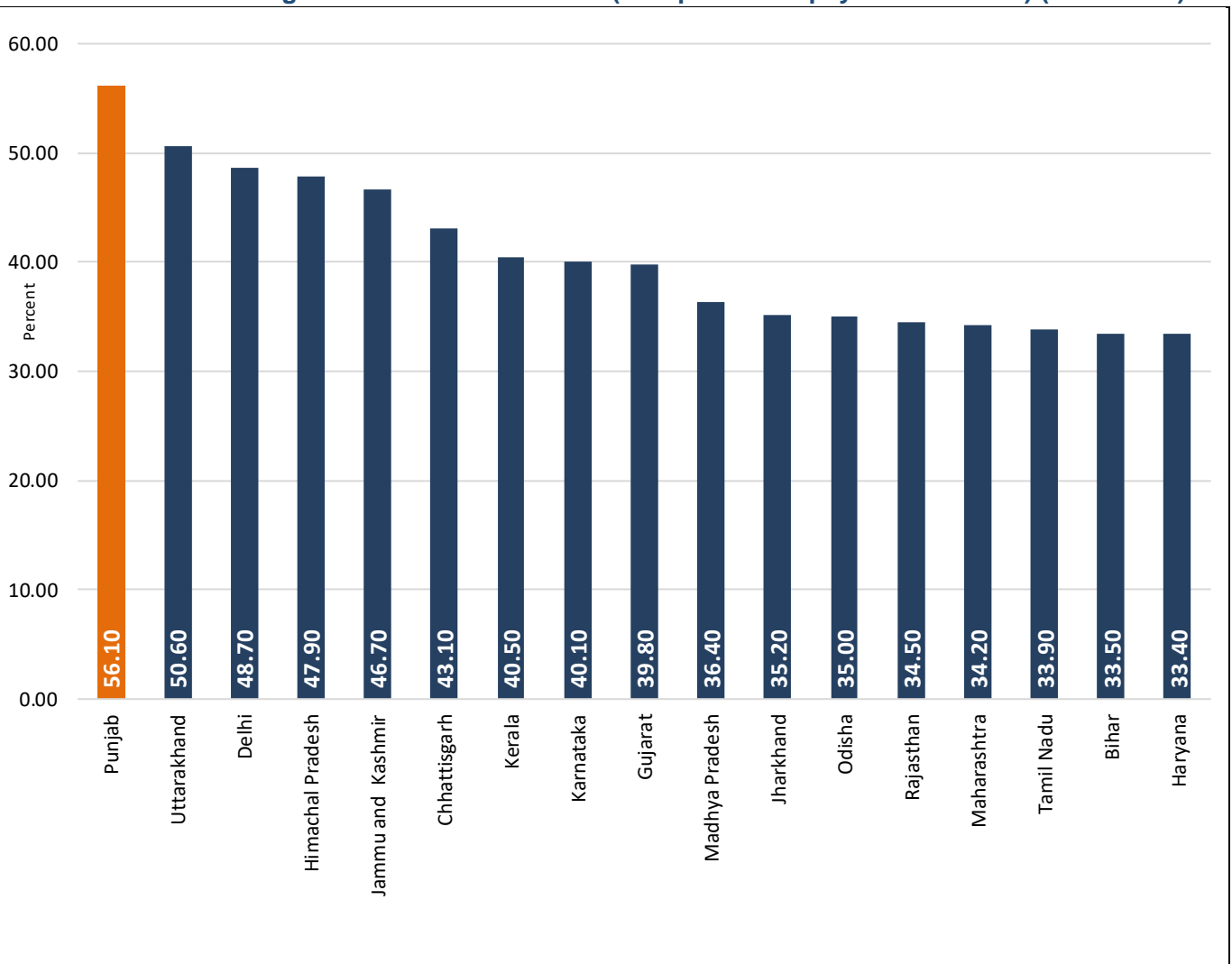
State	2017-18 (%)	2018-19 (%)	2019-20 (%)	2020-21 (%)
<b>Punjab</b>	<b>37.00</b>	<b>36.70</b>	<b>45.60</b>	<b>56.10</b>
Uttarakhand	39.00	33.60	40.30	50.60
Delhi	6.00	21.80	29.90	48.70
Himachal Pradesh	42.00	36.20	40.80	47.90
Jammu and Kashmir	37.00	27.20	40.90	46.70
Chhattisgarh	31.00	24.60	36.20	43.10
Kerala	16.00	15.30	29.30	40.50
Karnataka	22.00	19.90	28.50	40.10
Gujarat	14.00	14.10	26.30	39.80
Madhya Pradesh	26.00	14.30	25.10	36.40
Jharkhand	26.00	13.70	22.30	35.20
Odisha	31.00	24.30	27.90	35.00
Rajasthan	18.00	8.20	23.00	34.50
Maharashtra	3.00	4.20	16.40	34.20
Tamil Nadu	3.00	5.40	17.80	33.90
Bihar	38.00	18.20	25.80	33.50
Haryana	18.00	15.60	24.30	33.40
West Bengal	13.00	8.00	18.40	32.30
Uttar Pradesh	12.00	5.60	15.20	30.80
Andhra Pradesh	7.00	-4.10	13.20	28.20

Source: Minutes of GST Council

**1.5.5** The above table clearly demonstrates that the compensation gap has been faced by most of the States and the same has increased over the period of time rather than receding. While on one hand this signifies the fact that the expected buoyancy in revenue under GST has not materialized, on the other hand it brings out the fact that the challenge of end of compensation regime will be faced by almost all the States. It is, therefore, imperative that the compensation regime continues at least for a certain defined period so as to provide some sense of balance and stability to the fiscal position of the States.

**1.5.6** The graphical representation of the State-wise GST Compensation Gap is as depicted in Chart 3.

**Chart 3: % Shortfall against Protected Revenue (Compensation payable to States) (FY2020-21)**



Source: Minutes of GST Council Meeting



**1.5.7** As the Compensation would stop coming from July 1, 2022 onwards, based on the above trend, **the State is likely to see a drastic fall in revenue in the range of Rs.14000- 15000 crore for FY23 itself i.e. Rs. 20000-21000 crore per annum. This is a “Fall off the Cliff” scenario for the State.**

## **1.6 Other Concerns**

**1.6.1 Revenue Neutral Rate (RNR) Fixation and reduction in Effective Tax Rate:** The potential of the State to earn revenue as compared to the pre-GST regime has been impacted due to the fixation of the tax rate under GST. This fact is corroborated from the recommendation of the RNR Committee on Revenue Neutral Rate (RNR) {which refers to that single rate, which preserves revenue at desired (current) levels} which estimated the same as 15%-15.5% for the country as a whole. While the internal calculations for the State point out a higher RNR of 18.3%. Compared to this, the weighted GST rate, according to Reserve Bank of India (RBI), is only 11.6% (June 2021). The continuous fall in the effective incidence of tax under GST (11.6%) has further complicated the matter especially when compared with the State’s RNR of 18.3%. This elucidates the fact that pre-GST the rate of tax on the goods under VAT was significantly higher than the rate that was fixed under GST.

**1.6.2 Streamlining of the IGST settlement process:** The edifice of GST is built on the keystone of destination based consumption tax with IGST model being the epitome of same. The provisions of section 17 of the Integrated Goods And Services Tax (IGST) Act, 2017 encapsulate the basic premise which defines the said principle and outlines the mechanism for settlement of funds between the Central Government and the consuming State Government. The IGST settlement reports for the State have been examined and it has been observed that although the taxpayers registered within the State of Punjab have carried

out reversal of huge amount of Input Tax Credit but the same has not been considered for the IGST settlement thereby depriving the State of its rightful share of revenue. These infirmities have been highlighted and taken up by the State with the Government of India at various level.

**1.6.3 Rightful devolution to the States:** The five petroleum products namely crude oil, motor spirit, diesel, aviation turbine fuel and natural gas are presently outside the ambit of GST. It has been observed that the nature of taxation over the said goods has been fundamentally changed. Levy of cess and surcharge has led to reduction in tax component of Excise Duty by 40% in petrol and by 60% in diesel in last 4 years as depicted in Table 8.

**Table 8: Breakup of Excise Duty (Rs. per litre)**

Excise Duty	Petrol				Diesel			
	Apr-17	% share of total	Feb-21	% share of total	Apr-17	% share of total	Feb-21	% share of total
Taxes devolved to States	9.48	44%	1.4	4%	11.33	65%	1.8	6%
Cess and surcharge levied by Centre	12	56%	31.5	96%	6	35%	30	94%
<b>Total</b>	<b>21.48</b>	<b>100%</b>	<b>32.9</b>	<b>100%</b>	<b>17.33</b>	<b>100%</b>	<b>31.8</b>	<b>100%</b>

**1.6.4** Since such levies do not form part of devolution as recommended by the 15<sup>th</sup> Finance Commission, such practice has resultantly led to a downward slide in devolution kitty of the States, even though the collection of excise duty from the said products has shown a remarkable increase over the said period and thereby there is a need to revisit this structure of levying cess/surcharge on excise duty of the said products.

**1.7 Initiatives undertaken by the State:** The State has undertaken a series of initiatives to reduce the shortfall and to decrease the dependence on compensation. The measures such as establishment of mobile-wings/ data-mining wing; imparting training on diverse modules; commencement of audit process under GST; etc. have been implemented to improve the compliance matrix under GST. The same have been outlined separately as **Annexure** attached to this document. These endeavors of the State underline the fact that utmost efforts are being made to enhance revenue under GST.

## **1.8 Collection Efficiency**

**1.8.1** Return filing by the taxpayer is an important indicator and contributor of the revenue collection of the State. It also implies that the tax administration has taken steps to enhance GST compliance by the taxpayer which results in the return filing on-time and revenue collection of the State. The tax administration in Punjab has been focused on implementing the GST regime with highest levels of efficiency and facilitation for the traders. The State Government, in order to facilitate traders having limited computer knowledge in registration, filing of returns and other online GST related tasks, has trained youth as "GST MITRA". Compliance levels in a State are evident from the percentage of return filing in the State. Punjab has been amongst the top three States in the furnishing of statement of FORM GSTR-1 since the implementation of GST.

**Table 9: GSTR-1 Furnishing Data for FY 2020-21 till March 31, 2021**

State	Eligible Taxpayers	Total Returns Filed	Filing %	Filing Before Due Date
Gujarat	9,35,950	9,09,304	97.15%	71.02%
Rajasthan	5,90,776	5,61,468	95.04%	55.46%
<b>Punjab</b>	<b>3,18,519</b>	<b>3,01,042</b>	<b>94.51%</b>	<b>69.67%</b>
Haryana	4,38,177	4,13,436	94.35%	63.14%
Maharashtra	13,63,993	12,79,716	93.82%	51.06%
Tamil Nadu	9,10,875	8,53,068	93.65%	55.00%
Kerala	3,14,391	2,92,653	93.09%	51.76%
Madhya Pradesh	3,78,386	3,44,133	90.95%	31.87%
Jharkhand	1,53,057	1,39,055	90.85%	42.98%
Uttar Pradesh	12,03,078	10,90,308	90.63%	48.67%
Karnataka	7,65,317	6,88,738	89.99%	50.41%
Chhattisgarh	1,16,311	1,03,798	89.24%	31.58%
Andhra Pradesh	2,90,704	2,57,156	88.46%	45.71%
Odisha	2,45,647	2,11,969	86.29%	38.07%
West Bengal	6,19,161	5,31,098	85.78%	50.22%
Goa	35,459	29,985	84.56%	47.77%
Telangana	3,72,165	3,08,395	82.87%	41.47%
Bihar	3,76,756	3,05,411	81.06%	33.19%

Source: GSTN

**Table 10: GSTR-3B Return Furnishing Data for FY20-21 till March 31, 2021**

State	Eligible Taxpayers	Total Returns Filed	Filing %	Filing Before Due Date
Madhya Pradesh	3,78,386	3,74,975	99.10%	53.30%
Gujarat	9,35,950	9,18,824	98.17%	76.14%
Rajasthan	5,90,776	5,78,893	97.99%	67.79%
Maharashtra	13,63,993	13,31,473	97.62%	65.05%
Chhattisgarh	1,16,311	1,12,993	97.15%	41.66%
Uttar Pradesh	12,03,078	11,67,901	97.08%	70.14%
Jharkhand	1,53,057	1,48,294	96.89%	66.30%
Tamil Nadu	9,10,875	8,82,208	96.85%	74.73%
<b>Punjab</b>	<b>3,18,519</b>	<b>3,07,190</b>	<b>96.44%</b>	<b>79.77%</b>
Odisha	2,45,647	2,36,888	96.43%	69.97%
Kerala	3,14,391	3,02,899	96.34%	64.36%
Uttarakhand	1,38,667	1,33,508	96.28%	70.17%
Karnataka	7,65,317	7,33,048	95.78%	73.65%
Haryana	4,38,177	4,19,490	95.74%	73.48%
Andhra Pradesh	2,90,704	2,70,147	92.93%	68.01%
Bihar	3,76,756	3,41,944	90.76%	65.80%
Goa	35,459	30,994	88.85%	56.87%
Telangana	3,72,165	3,30,685	87.41%	59.06%

Source: GSTN

The above data clearly brings out the fact that the compliance levels in terms of returns filed as a percentage of eligible taxpayers remain high for the State of Punjab and is consistently above the National average. In addition to the higher filing proportion, the proportion of return filing by the eligible taxpayers within due date is highest for GSTR-3B Returns and is significantly higher than National Average. This underlines the strong enforcement measures as well as compliance monitoring undertaken by the State. Thus, the amount of shortfall cannot be attributed to the collection inefficiency of the State and non-compliance of taxpayers. However, despite the high and timely return filing, the State continues to have muted growth in the GST revenues and is one of the biggest claimant of compensation regime. The main reason of revenue shortfall is, thus, the tax structure and decrease in the rates of tax which are beyond the control of the State Government, and not any laxity in collection efficiency.

**1.8.2** From Table 9 and 10, it may be noted that **the State has outperformed other General Category States in terms of collection efficiency, and it is noteworthy that the State's ability to generate revenues has been achieved to its fullest.** However, going forward, post the completion of the period of five years of Compensation Cess, the State would witness a drastic fall in the GST revenue and therefore requires special assistance.

**Punjab has lost a significant portion of its revenue permanently, post the implementation of GST, on various accounts. The discontinuation of State levies such as Purchase Tax and I.D. Fee, taxation of various commodities at uniform rates irrespective of the quantum and intensity of consumption of such goods across states, differential nature of consumption between metropolitan cities and agriculture dominated states like Punjab and additional borrowing stemming from the liquidity crunch, are just some of the issues plaguing the economy of the State.**

**Unless these issues and the increased Vertical Imbalance arising thereby, due to reduction/nullification of tax rates on the commodities previously subjected to higher rates, and loss resulting from equal apportionment of GST rates between the Union and the States are addressed in a justifiable manner, the fiscal situation of Punjab would further deteriorate beyond the point of containment.**

## **1.9 CONCLUSION**

**1.9.1** A portion of tax levy on food grains which are exempt under GST has been completely and permanently foregone by the State of Punjab which is primarily agrarian. On the other hand, Industrial states and the states rich in mining resources benefitted immensely from the GST implementation. On account of being an agrarian state, the State is staring a permanent hole in its books currently being funded by the compensation. The State was hopeful that the GST regime will continue to evolve and eventually revenue streams will catch up with the growth projections. However, the GST regime has taken a long period of time to partially stabilize, and revenues collected have been significantly lower than the expectations. In fact the State's reliance on GST Compensation has been unprecedented in FY21 on account of Covid-19 and 29.31% of total revenue receipts comprised of the same.

**1.9.2** The fact remains that the gap between the protected revenue and the actual revenue earned can only be mitigated not eliminated. There is need to start discussions on how exactly this gap is to be bridged in general together with the possibility of differential SGST rates for states which continue to have far greater deficits. **The State is of the view that the GST regime needs further time to stabilize and therefore, the current compensation regime be extended for a period of 5 Years till June, 2027 so as to provide some**

**sense of balance and stability to the fiscal position of the State.** Meanwhile, the GST Council should extend the support to states in policy matters aimed at enhancing GST revenue and lowering the reliance on compensation to less than 10% of total revenue receipts.

**1.9.3** In case of agrarian states like Punjab, a fixed amount of compensation grant out of Compensation Cess pool must be linked with its Revenue Receipts and be perpetually put in place. This will ensure that the agrarian States continues to take steps aimed at modernizing farming sector and contribute to the central pool of food grains consistently. Linking the compensation grant to the growth in revenue receipts will also act as an incentive for the States to bring reforms aimed at boosting the same.

**1.9.4** GST Council may also re-organize the Compensation regime by apportioning 50% of Compensation Cess being levied on sin goods and luxury items, permanently towards agrarian states that have lost a significant portion of their revenue on account of implementation of GST. This Compensation Cess receipt may be spent mandatorily on agriculture sector aimed at farmer-friendly initiatives and income enhancement schemes. This will be true to the spirit, objectives and rationale laid out for Compensation Cess with respect to agrarian states.

**1.9.5** It is also suggested to harmonize tax rates and exemptions so that opportunities of evasions are eliminated, and tax credit chain simplified.

**1.9.6** It is reiterated that the State will have an off-the-cliff situation if the compensation regime comes to a screeching halt in June, 2022, especially after Covid-19 wherein waves after waves of virus variant has led to regional as well as state-wide restrictions multiple times since March, 2020. To avert this situation, the State humbly requests the Union Government to favorably



consider the proposals laid out in this Memorandum.

**1.9.7** The following extracts have been taken from an **article titled “Extending GST compensation as a reform catalyst” written by M. Govinda Rao, presently Chief Economic Adviser, Brickwork Ratings, published in The Hindu dated 12.01.2022**, which advocates the necessity of extending the GST Compensation period for next 5 years.

*“.....In the first two years of its implementation, the amount of compensation to be paid to the States was modest and the compensation Cess was sufficient to meet the requirements. In fact, the Cess collections exceeded the compensation requirements.*

*However, in 2020-21, due to the most severe lockdown following the novel coronavirus pandemic, the loss of revenue to States was estimated at ₹3 lakh crore of which ₹65,000 crore was expected to accrue from the compensation Cess. Of the remaining ₹2.35 lakh-crore, the Union government decided to pay ₹1.1 lakh crore by borrowing from the Reserve Bank of India under a special window and the interest and repayment were to be paid from the collections from compensation Cess in the future.*

*Although it was hoped that the tax structure would stabilize in the first five years, the reform is still in transition. First, the technology platform could not be firmed up for a long time due to which the initially planned returns could not be filled. This led to large-scale misuse of input tax credit using fake invoices. The adverse impact on revenue collections due to this was compounded by the pandemic-induced lockdowns. Second, this is the only major source of revenue for the States and considering their increased spending commitments to protect the lives and livelihoods of people, they would like to mitigate revenue uncertainty to the extent they can. They have no means to cushion this*

*uncertainty for the Finance Commission which is supposed to take into account the States' capacities and needs in its recommendations has already submitted its recommendations; the next Commission's recommendations will be available only in 2026-27.*

***Thus, extending the compensation payment for the loss of revenue for the next five years is necessary not only because the transition to GST is still underway but also to provide comfort to States to partake in the reform. GST is the most important source of revenue to States and any revenue uncertainty from that source will have a severe adverse effect on public service delivery.....”***

## Annexure

### Initiatives undertaken by State to decrease dependence on Compensation

7 **Mobile Wings** are working 24X7 to stop tax evasion. As compared to first 10 months of financial year 2020-21 in which Rs. 42.41 crore were recovered as tax/penalty/fine, in the extant financial year 2021- 22, Rs. 77. 06 crore have been recovered till now which reflects an impressive growth of 82%. Apart from this, the Data Mining Cell is actively engaged in carrying out the analysis of revenue leakage. The said effort results in good inspection, leading to recovery to evaded taxes. Moreover, the impact of enforcement activities is actually to create deterrence effect on tax evaders. The Department is deploying SAS tool to further strengthen the data mining effort through machine learning and analysis.

**Data Mining Wing** is a specialized wing established in 2017-18 to help the field formations in detecting tax evasion activities with the help of State's own Excise and Taxation Technical Services Agency (ETTSA) and various platforms that includes Boweb Portal, E-way bill portal, SAS tool, BIFA and JPAL etc. The said Wing prepares reports upon irregularities and discrepancies detected in the returns filed by the Taxpayers based upon data provided by GSTN and ETTSA. These reports are being shared with concerned wings of the department for necessary action and compliance. Since the implementation GST regime, based upon the reports generated by Data Mining Wing, the Taxation Commissionerate has collected revenue worth crores as depicted below:

(Rs. Crore)			
Year	Tax recovered	ITC reversed	Total Revenue collection
till March 2019	515.86	269.51	785.37
2019-20	787.89	197.46	985.35
2020-21	341.99	18.85	360.84
2021-22 (till Oct 2021)	230.09	152.61	382.70
Total Revenue collection	1875.83	638.43	2514.26

Major reports generated by Data Mining Wing that contributes to the above said performance includes Report on GSTR3B return defaulters, Report on ITC mismatch as per GSTR 3B & GSTR 2A, Report on Liability mismatch as per GSTR 3B & GSTR 1, Report on Interest calculation of late GSTR 3B filers, Report of Inward (purchases) and Outward (sales) mismatch of newly registered dealers and more such reports. Besides, Data Mining Wing is also providing all necessary help to all field formations and providing them with the information and data required by them for detecting tax evasion activities through its two dedicated wings established at Mohali and Patiala respectively for this purpose. Data Mining Wing is also doing 360-degree analysis of the selected taxpayers to find out bogus dealers to plug the revenue leakages.

The Directorate of Training has organized/ coordinated **trainings on diverse modules/topics**. The detail of trainings organized since 2018 is as below:

Year	Number of Trainings organized	Total Participants Officers/officials	Man days
2018-19	31	5631	14923
2019-20	39	3942	18023
2020-21	54	1716	3003
2021-22 (Upto Sept)	49	2146	2719

The registration under GST regime is being granted with utmost caution. In the month of October, 2021, 1887 registration applications were rejected while 1660 new registrations were granted by the State tax authorities. The rate of deemed approvals of registrations is less than 0.5%. Similarly, Refunds are being granted after due verification. A detailed SOP is being followed by the department to approve any Refund.

The process of audit under GST has been initiated by the department to enhance the compliance verification. Nearly 450 taxpayers have been identified for the year 2017-18. Audit of 104 taxpayers have been completed which has resulted in creation of demand of nearly Rs. 31 crore with approximate recovery of Rs 3 crore.