GST CAFÉ

VAISH ASSOCIATES ADVOCATES
Delhi • Mumbai • Gurgaon • Bengaluru
Celebrating over 40 years of professional excellence

Vol. 1, No. 8 • August 16-31, 2015

Effect of taxing Inter-state Branch Transfers under the GST regime

Introduction

From the definition of 'goods and services tax' vide proposed insertion of Article 366(12A) by way of the 122nd Constitutional Amendment Bill, it is clear that under goods and service tax, the taxing event in relation to goods would be supply of goods as opposed to manufacture or sale of goods. Proposed Article 366(12A) of the Constitution reads: "goods and services tax means any tax on supply of goods, or services or both except taxes on the supply of alcoholic liquor for human consumption"

> **Do you Know:**
>
> The United States of America remains one of the few countries without a centralized consumption/ indirect tax like GST. Absence of GST is attributed to greater autonomy provided to states and local bodies with states and local bodies levying sales tax in respective jurisdictions.

This appears to have been done with the intent of taxing inter-state branch transfers and job-work transaction. Same was also proposed in the report of the Task Force on Goods and Service Tax of the Thirteenth Finance Commission. The report of the Thirteenth Finance Commission also noted the absence of Constitutional mandate to tax inter-state branch transfer.

Positive Effect oftaxing Branch Transfer

Currently, as inter-state branch transfers are zero rated under Central Sales Tax law, entities choose to maintain depots in various states. Branch transfers are affected between the manufacturing factory and depots and state VAT is paid on subsequent sale. However, in such a situation, state VAT paid on procurement of raw materials may not be passed on by the manufacturers.

Under the proposed regime, Interstate branch transfers have been proposed to be taxed in the same manner as if it is in the nature of sale between two independent dealers.

One of the tenets of an ideal GST framework is that business decisions should be motivated by economic rather than tax considerations. Maintaining different depots in different states goes against this objective. Further, unavailability of state VAT in the hands of the manufacturer increases tax costs. Making inter-state branch transfers subject to GST appears to have been made with the objective of presenting solutions to the abovementioned issues.

Negative Effect of taxing Branch Transfer

However, keeping in mind the proposed revenue neutral rate (RNR) which is in the higher side, it is required to be noted that GST would have to be paid upon inter-state supply of goods, whereas credit of such GST would be available in the destination state may only be utilized upon sale of such goods. This may cause blockage of funds, particularly in certain seasonal industries (Air Conditioners, woollen clothes, fertilizers etc.), where production of goods continue on continuous basis, but demand surges only during a limited period. Manufacturers in such cases may choose to stock finished goods in the state of manufacture itself rather than locations where zonal warehousing hubs may have been set up. This goes against the tenet of an ideal GST framework of business decisions being motivated by economic rather than tax considerations.

Conclusion

As far as the impacts of taxing inter-state branch transfers are concerned, the advantages clearly outweigh the lone disadvantage mentioned hereinabove. One idea that may be explored is to zero rate inter-state branch transfers and transfer credit related to the goods by the supplier to the receiving branch in the other state.

However, it should be considered that any process specially carved out for inter-state branch transfer should not be made extremely complicated.

Please revert with your comments and questions to:	
Shammi Kapoor, Delhi shammi@vaishlaw.com	**Shilpa Sharma,** Mumbai shilpa@vaishlaw.com

Disclaimer:

Contact Details :

www.vaishlaw.com

NEW DELHI	MUMBAI	GURGAON	BENGALURU
1st & 11th Floor, Mohan Dev Bldg. 13 Tolstoy Marg New Delhi - 110001, India Phone: +91-11-4249 2525 Fax: +91-11-23320484 delhi@vaishlaw.com	106, Peninsula Centre Dr. S. S. Rao Road, Parel Mumbai - 400012, India Phone: +91-22-4213 4101 Fax: +91-22-4213 4102 mumbai@vaishlaw.com	803, Tower A, Signature Towers South City-I, NH-8 Gurgaon - 122001, India Phone: +91-124-454 1000 Fax: +91-124-454 1010 gurgaon@vaishlaw.com	Unit No. 305, 3rd Floor Prestige Meridian-II, Building No. 30 M.G. Road, Bengaluru - 560001, India Phone: +91-80-40903581/ 88 /89 Fax: +91-80-40903584 bangalore@vaishlaw.com