The impact of Indian tax reform on China’s and India’s economies and trade

Lairu Li*
International business school
Yunnan university of finance and economics
Yunnan kunming
67692019@qq.com

yang Lei
International business school
Yunnan university of finance and economics
Yunnan kunming
1317537378@qq.com

Abstract—In the past, tax management level and the kind of tax in India were various, tax rate was complicated, and regulatory was inefficiency, which is limiting the economic development. In order to reduce tax rates, expand the tax base, simplify tax process, coordinate the relationship between local and central tax, Modi government strongly launched GST reform, and formally implemented in July 1, 2017. This tax reform, with a wide range and depth, relates on the vital interests of almost every Indian people, the Indian businessmen, and the people who trade with India. This paper mainly analyzes the Indian tax system, GST tax reform, advantages and disadvantages of tax reform, and matters of attention for the Chinese enterprise when facing tax reform in India, with the hope that Chinese companies understand GST tax reform policies, actively adjust business strategy, go with the flow, and seize the opportunity.

Keywords—Indian tax system; GST tax reform; advantages and disadvantages of tax reform

I. INTRODUCTION

After the independence of India, the "introverted" economic development strategy has been implemented for a long time, with the result that contradiction between the dependence on imported capital goods and the ability of foreign exchange transactions has long restricted its economic development. In 1991, the Indian government launched a comprehensive economic reform, eased import restrictions, accelerated trade liberalization and eased government intervention in trade activities, and in 2001, trade liberalization was initially achieved [1]. On the one hand, India mainly relies on domestic demand to drive economic development. The government supported the development of domestic service industry, ignored the development of manufacturing industry, which makes it's industrial structure unbalanced. On the other hand, the tide of economic globalization was coming, which makes the government realize that India's domestic capital is insufficient to meet the needs of India's current economic and social development.

Thus, in 2012, the Indian government began to gradually ease restrictions on foreign investment. Modi was appointed prime minister of the Indian government in 2014, who actively promotes the economy system reform, with reconstruction India economic landscape around the "made in India", "digital India", "monsoon plan", "east action", ring seal industrial corridor and other major strategic. India's stable domestic political environment, positive and open foreign policy, perfecting tax system, the rapid economic development, tremendously potential market make more and more Chinese companies looking to India market. In recent years, the traditional industries between the two countries, as well as the cooperation between emerging industries, have developed further and there is more room for cooperation in the future. At China-ASEAN business and investment summit in 2015, Mr Modi promised that India would provide investors with a "transparent and stable tax system" [2]. For Chinese companies, Indian tax reform, will bring the influence of the immediate interests. And this requires them to pay attention to policy changes in time, to adjust overseas strategy actively, to adapt to the new tax environment, which is the meaning of this article.

II. THE BODY OF THE ARTICLE

A. Reform of Indian Tax Law

1) the Indian tax system

a) tax law management system

India's tax system is established on the basis of the constitution of India. According to the Indian constitution, India is a federal state, which has the government and the local level government. And the central and local government have two-level budget system, at the same time set up two levels of the central and local governments tax agency. Beside, the central government can formulate the national tax policy, the local government also can make their own state policy. Different local policies and different tax rates lead to a wide variety of taxes and complicated management levels. For example, central tax includes corporate income tax, capital income tax, individual income tax, inheritance tax and gift tax, sales tax, consumption tax, value-added tax, social security tax, registration tax, stamp tax, customs, etc. State taxes include vehicle tax, land value tax, agricultural income tax, occupational tax, VAT, etc.

b) Legal sources of major tax laws

Since it was independent in 1947, India had formed a tax structure with indirect tax as its main body, and had maintained this structure for more than 60 years. The central
sales tax and local sales tax are closely linked to merchants among them.

The Indian government passed the central sales tax act in 1956 and introduced a sales tax in July 1957. A sales tax is a collection of documents that are used in the process of interstate trade or commerce, when the actual flow of goods or the transfer of the ownership of the goods is taken into effect. On March 1, 1986, India put forward the concept of manufacturing value-added tax, the levy range from the initial few commodities, gradually extended to all the manufacturing department except tobacco and several other departments. Later, in order to meet the international standards, India began to reform the value-added tax, gradually replacing the existing sales tax in various states with the universal value-added tax [3]. Since April 2005, the local sales tax had been converted into VAT levied on the retail link.

c) Reform of modi’s government tax law

Under such the various hierarchy, complicated tax kinds and tax rates, inefficient supervision tax system, for the government, it will make the Indian officials easier to implement corruption, local businessmen to evade tax, which eventually leads a fiscal deficit and tax base to be narrow, revenue to be low, economic development to be influenced. For taxpayers, the tax payment needs to be changed constantly according to different policies in different regions, leading to double tax and increasing tax burden. In addition, the complicated tax payment process makes it time-consuming and arduous for merchants, which creates a lot of opportunity cost and brings about commercial drawbacks leading some foreign investors avoid to invest in India.

In order to reduce the tax rate, expand the tax base, simplify tax process, coordinate the relationship between local and central tax, broaden the cross-border trade, the government of India merged taxes, made single rate to replace the cumbersome and chaotic states local taxes. India had been discussing the possibility of implementing the GST reform since 2003, and proposed a reform plan in 2006. After hard work, the modi government launched the GST reform in a strong way and implemented it on July 1, 2017. This tax reform, with its broad scope and deep strength, touches on the vital interests of almost every Indian people, Indian businessmen, and those who do foreign trade with India, and deserves enough attention.

B. GST Content and Tax Rate in India

Goods and Services Tax (Goods and Services Tax: GST) is to provide Goods and Services for all links, a kind of Tax in the last part of paying the input can be deductible in the next link, in short, in the process of commodity circulation, the government only for Goods in parts of the corresponding link to realize value-added Tax.

The GST replaces the multiple tax systems of the previous central and local governments to achieve the unification of the tax system. With the implementation of the GST tax, the following 11 taxes will be withdrawn from the Indian tax stage, which covers the central tax, additional consumption tax, tax services, additional tariffs and special additional tariffs, value added tax, sales tax, entertainment duty, the central sales tax (by the central administration and by the state to impose), octroi, entry tax, purchase tax and luxury tax, and lottery betting and gambling tax, etc.

C. GST’s Seven-file Tax Rate

The Indian government has set a total of 0%, 0.25%, 3%, 5%, 12%, 18% and 28%, among which 5%, 12%, 18% and 28% are the main commodity tax rates. The actual tax rate applicable to a project depends on its classification, and the tariff calculator will be available on the CBEC and ICEGATE sites. For example, the tax rate of fresh meat, live poultry and printed books is 0%; The tax rate on unprocessed diamonds is 0.25%; The tax rate on gold jewelry, silver and diamond processing is 3%; The tax rate on fish, butter, coal and medicine is 5%; The tax rate for frozen meat products, butter, cheese, umbrellas and mobile phones is 12%. Candy, pastries and cakes, paper towels, notebooks, steel products, cameras, monitors and most other goods are taxed at 18%. The tax rate on gum, shampoo, sunscreen, water heater, washing machine and car is 28%. On the whole, the rate of service tax increases.

D. “Double Track System” of GST

Generally speaking, the business entity may be involved in the payment of three types of taxes -- CGST, SGST, IGST, the central goods service tax (CGST) and the state goods services tax (SGST), and the integrated goods services tax (IGST). GST reform in India is not the central nationwide levying a unification of GST in lieu of all kinds of turnover tax, but in the basic safeguard state government taxation power and under the premise of fiscal revenue, implementing a flexible "double-track GST". [4] The so-called "double track GST", namely the central cargo service tax (CGST) and the state goods service tax (SGST) taxes all goods and services at the same time. Central collect and warehouse central goods services tax, and the state government levy the state of all transactions and warehouse state goods labor tax. The central goods service tax can be deducted from the central freight service tax. Similarly, the same is true for the tax deductibility of state goods, but the central goods service tax and the state goods service tax are not allowed to cross the deduction. Provincial and national taxes are required to pay for goods in circulation. For trans-state transactions, the central government collects the integrated goods service tax (IGST), and the state government no longer levies the state goods service tax.

III. THE IMPACT OF TAX REFORM

A. GST Reform Dividend

1) Expand tax base and promote economic development

If the government wants to expand fiscal revenue and reduce fiscal deficits, it can only raise taxes, or expand the tax base. Raising taxes would lift local prices and lost their price advantage. Broadening the tax base, while reducing the tax burden on the industry, would also increase government revenue, making the tax base a preferred option.

GST’s "transferability" makes it a self-reinforcing mechanism. Downstream businesses in order to offset the tax,
will take the initiative to ask for GST voucher, thus make the whole supply chain cycle. Upstream and downstream businesses to supervise each other to pay taxes, to reduce tax evasion, systematically expand the tax base in India. The GST reforms will help raise taxes as a share of GDP, boost GDP growth and boost India's economic growth.

2) **Reduce the cost of doing business and avoid trade barriers between states**

On the one hand, GST simplified tax procedures, incorporated taxes, harmonized tax rates, effectively avoiding double taxation and reducing the cost of doing business. On the other hand, IGST avoid the cumbersome tax process that was originally traded across the state, and companies don't have to pay a lot of taxes because of cross-border transactions. IGST reduced across the bond trading material cost and time cost, broked the India trade restrictions between different nations, changed the separation between the state, promoted the flow of goods across the country better, which is conducive to the unity of the national market.

Reduction of the tax burden and the unity of the market will make companies in India can have a lower price in the global market, which make it more advantages in the international market so that it will promote the export trade of India.

3) **Digital precise management**

India's science and technology technology is still underdeveloped. In terms of tax payment, the information level of enterprises, businesses and government is low. This brings a lot of inconveniences to personal taxes and government taxes, and raises many of the ills of tax evasion. To make GST better in India, the government has set up a third-party agency, the Goods and Services Tax Network (GSTN). GSTN connects taxpayers, federal and state tax authorities, intermediaries, Banks and treasuries by using technology such as the Internet, which using the information platform to provide technical services related to tax refund, tax registration, auditing and evaluation, etc. for the state government, and tax refund, tax payment, tax registration and other functions for taxpayers.

The digital service makes the tax system transparent and can be inquired, and the tax payment is implemented to every specific link, which avoid corruption and greatly improved the efficiency of government tax authorities. For taxpayers, each Indian taxpayer must register the national tax code, and the system will help the taxpayer complete the tax related operation. Each taxpayer's tax code is unique. On the one hand, it is conducive to tax deduction in the supply chain. On the other hand, this facilitates the formation of tax query directory, improves the efficiency of the tax authorities, and reduces the cost of government tax collection.

**B. Matters needing Attention of Chinese Enterprises in Tax Reform in India**

1) **Expand tax base and promote economic development**

For the export of Chinese companies from India, under the GST system, although the exporter applies the zero tax rate, he still has to pay GST in every link, and only after the export, can he apply for the tax refund according to relevant vouchers. It usually takes 3 months to 12 months to get the tax rebate, so the opportunity cost of the funds will be discounted.

For Chinese companies exporting to India, it will also be hit by the implementation of GST. On the one hand, because of the lower cost of local enterprises in India, the profit of goods imported from Chinese enterprises is reduced because the market was shared. On the other hand, according to the GST tax guidelines, for air conditioners, washing machines, televisions, cars and other industries, it has been classified as "luxury goods", with a tax rate of 28 percent, which is 2 percentage points higher than before. Tax increases will increase their export costs and undermine their competitiveness.

2) **The cost of GST adaptation period**

The long period of mismanagement of the tax burden has resulted in the long-term accumulation of tax problems. Some habitual business models have been difficult to change for a while. The society and the government will have a stress response to GST. For example, businesses can quickly sell products that have already paid high taxes, which may lead to a vicious price war. In order to adapt to the implementation of GST, the government constantly adjusts relevant political and economic policies to create an unstable environment. And the change of partners to obtain tax receipts from the supply chain. These policy risks and economic risks can bring losses to Chinese enterprises.

Objectively, the GST system itself may be defective. The implementation of GST has not been conducted in individual pilot regions before, and many practical problems are not expected. All of a sudden, the reform of the whole country was implemented. Once there was a problem, it was the loss of the whole country. On the whole, it will take time for India to fully adapt to the GST system, and Chinese enterprises will be affected by it and will experience the painful period of reform and pay a certain price.

3) **Adjust the way of entering the Indian market**

The change in tax rates has raised some industry taxes. For these industries, companies can rethink the way they enter the market. In particular, emerging industries can also get tax breaks in combination with local preferential policies. As to the specific way of foreign direct investment, enterprises can choose according to their own situation, which can effectively avoid tariffs and effectively use local advantages. For example, if a Chinese company directly exports finished products to India, because of the loss of price advantage due to the adjustment of the finished product tax rate, it will be possible to consider local investment in India, where raw materials can be sourced locally or imported from the home country. Local materials can effectively avoid customs duties. The import of raw materials from the home country, the tax rate of raw materials is lower than the finished product, and after the production of finished products in India, it can also be used to pay the tax deduction of the raw materials, reducing the cost. Moreover, for industries with less important core technologies, they can cooperate with local enterprises in joint ventures and outsourcing. Because wholly foreign-owned companies pay a high tax rate on joint ventures with Indian companies, joint ventures can reduce costs and spread risks.
IV. Conclusion

India's economy has developed rapidly in recent years and its potential market is huge. However, due to the previous Indian government's excessive investment in the tertiary industry, the secondary industry in India's economic development structure is weak. The most prominent problem is its weak infrastructure construction, which is equivalent to the level of China in the late 1980s, restricts the economic development and weakens the attraction to foreign capital. As a result of the underdeveloped manufacturing industry, many electronic products and industrial products are dependent on imports and have a low penetration rate. Therefore, the government actively publish relevant policy, increase the intensity of construction, construction of telecommunications, electricity, roads, ports, airports, railway projects such as perfecting the infrastructure, to support the development of other industries. In order to develop the secondary industry, the government of India proposed "made in India" and issued corresponding policies to support industrial development.

Combined with the GST reform, it can be seen that the service tax has increased and the industrial tax has decreased. For example, the construction tax rate of infrastructure and other projects is 12% to 18%, and the current GST system breaks the rule that VAT can only be deducted from VAT and service tax can only be deducted from service tax. For engineering construction such as containing a large number of material purchasing, and includes design, construction and so on a large number of service projects, suppliers and subcontractors can put the project as a whole, its no longer divided into goods and services tax, overall planning the whole project process, better able to choose different suppliers into the maximum output tax. The implementation of GST will be beneficial to India's economic development in general, but the final result is still to be verified. Tax policy is the sovereign behavior of a country, the enterprise cannot control, but the tax is directly related to the economic and trade costs. In terms of Chinese enterprises, it is suggested to improve the product strategy according to the relevant tax rate and tax deduction regulations of GST tax reform. On the other hand, GST training should be conducted for the relevant personnel of the enterprise, and tax or financial personnel shall be arranged to be responsible for the GST compliance work of the enterprise.

In a word, enterprise should look at the big picture.

Acknowledgment

In the process of completing this paper, I encountered many obstacles, and the article stood on the shoulders of many predecessors, grateful. In addition, I would like to express my gratitude to my tutor Li for the professional guidance and support and encouragement of my family, friends and classmates. Be grateful for life and be grateful for it.

References

[1] Shenghao, the adjustment and enlightenment of India's foreign trade policy in the new century, China's circulation economy, July 2017.