



GST: Impact on the logistics industry in India

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The logistics industry in India was estimated to be worth USD 130 billion in 2013 and has been growing rapidly.¹ While the logistics sector could be among the primary bottlenecks in driving economic growth, it will also act as a catalyst to realising India's 'manufacturing dream' over the next decade.

Logistics companies in India have evolved over the years from being mere first-party logistics providers (1PL) to second-party logistics providers (2PL) to integrated fourth-party logistics providers (4PL) by providing a complete package of logistics services, including transportation, warehousing, pool distribution, management consulting, logistics optimisation, etc. and complementing them with advanced supply chain facilities. Alongside, the government has made considerable inroads into ensuring a favourable business climate. In one such initiative, the government has proposed to implement the Goods and Services Tax (GST), which promises to integrate India's multi-layered indirect tax system into a single unified one, unshackling India from its bureaucratic web and improving the ease of doing business. The changes in the proposed indirect tax system could reduce transportation cycle times, enhance supply chain decisions, lead to consolidation of warehouses, etc. which could help the logistics industry reach its potential in terms of service and growth.

In this article, we look at the various aspects of the logistics industry that may be affected by GST and how industry dynamics are likely to change once GST is implemented.

Warehouse Engineering

Warehouses and logistics are an integral part of an organisation's strategic business plan and operations. A multiple warehouse strategy works well for inter-state sales as organisations in India usually operate warehouses in multiple states (one in each state). The organisation then declares the transfer of goods as a stock transfer to negate the Central Sales Tax (CST) incidence on inter-state sales as a sale to one's own warehouse, under the aegis of declaration form F, is not a taxable event under the Central Sales Tax Act, 1956. Such stock transfers are completed through intra-state sales from the state warehouse to the customer. However, once GST is implemented, India will become a common market without any differentiation between inter-state and intra-state sales, thus ensuring a cumulative tax incidence with both the transactions being taxed equally (barring the temporary additional 1% tax on inter-state sales). Thus, the multiple warehouse strategy will be ineffective in reducing the inter-state tax incidence.

Thus, this tax reform could initiate a shift from multiple small warehouses to a large central warehouse in order to mitigate the additional administration cost of operating multiple warehouses. Over time, logistics companies may have to adapt to this evolved warehousing pattern followed by manufacturers/traders and re-engineer their services to be concentrated around major metropolises/areas such as Mumbai, National Capital Region (NCR), Kolkata and Chennai, where the central warehouses of the majority of companies may be situated. This will also shift the pattern of supply assignments, supplier channels and lead to a change in transport routes for logistics companies, accordingly.

Definition of 'Supply' for those in the Business of Supply

Most logistics companies operate in several models, which include a direct 'End to End Supply Model', 'Warehouse + Supply Model' and 'Manufacturing + Storage + Supply Model'. All of these models include the supply of goods (being the primary objective of the industry). With the rollout of GST, the taxable event under the GST regime will be the mere 'supply' of goods and services, as compared to the current taxable event being either manufacture, sale of goods or provision of service. A cursory reading of the GST Bill indicates that every supply of goods from Point C to Point D could be taxed under GST as it can be construed as supply. Thus, for instance, the service of warehousing acting as a checkpoint between Point C and Point D for temporary storage may be a taxable event under GST.

Although the GST Bill has not finalised the detailed definition of supply, the proposed GST Act is expected to expressly identify the services of the logistics industry and exclude them from the term 'supply of goods'. Also, a classification to clearly differentiate between the 'activity of providing services' and 'activity of supplying of goods' would be welcome.

¹ Indian Logistics Industry: Gaining Momentum, IBEF, November 2013, <http://www.ibef.org/download/indian-logistics-industry-gaining-momentum.pdf>

Hassle-free Supply of Goods and Reduced Transit Times

State-border checkpoints, which are tasked with material scrutiny and location-based tax compliance, negatively impact the overall production and logistics time and account for roughly 60% of a truck's transit time. These unproductive transit hours coupled with regulatory impediments reduce the efficiency of Indian manufacturers compared to their international counterparts. Having a unified market under the new GST regime would assist the smooth flow of goods within the country. Although border checkpoints may not be done away with immediately (as suggested in the First Discussion Paper on GST in 2009), reduced compliance scrutiny at these checkpoints will reduce transport hassles. This change will enable logistics companies to deliver goods more efficiently and optimise delivery times as compared to the present. The reduction in delivery time would also lead to a reduction in distribution costs by 10-15%, thereby lowering the final price of the goods.

Courier Service vs Goods Transport Agency (GTA)

The perennial question among various logistics service providers would be whether to classify themselves and their services under the bucket of Courier Services or Goods Transport Agencies. Although both of them fall within the service tax regime, the complex CENVAT Credit rules and procedures applicable on GTA services may influence services providers to avoid classifying themselves as GTA services. In addition, the requirements of issuing a consignment note and the applicability of the reverse charge mechanism for payment of service tax are differentiating factors pertaining to GTA services. The transport industry also enjoys certain thresholds/exemptions, which could be done away with in the GST regime. Accordingly, a clear understanding and bifurcation of the applicable classification of services is required under the present regime in order to address the relevant service-specific issues. It is expected that these classification issues may not continue under GST and a seamless flow on credit would be permitted in the entire supply chain.

Exemption on Petroleum

Although GST brings a sense of respite for the logistics industry, there is one major drawback – keeping petroleum outside the purview of GST. If corrected in time, this could give the logistics industry another reason to appreciate the GST regime. After much deliberation, petroleum has been brought under the purview of GST but it will be exempt until a date announced by the GST Council. In the defence of the logistics industry, as petroleum is one of the major inputs for this industry, it would be a welcome move if petroleum were to be 'non-exempt' right from the start. This would enable logistics companies to avail credit for the petroleum used in the course of providing logistics services.

Information Technology and CENVAT Credit

In today's fast-paced world, information technology has to keep abreast of new developments and change according to the changing needs. GST will entail a new set of compliance requirements for which companies will have to adopt new ERP accounting systems and inventory management systems to remain compliant during all stages. On the other hand, the industry will then be able to avail tax credits for all its purchases of goods and capital goods alike, be they motor vehicles or packing machinery. Also, tax credits on services will continue to be available under the GST regime.

Conclusion

GST has the potential to accelerate growth in the logistics industry. However, its complete impact can only be understood after the announcement of the draft GST Law and Rules. As rightly put forth by industry pundits, many contentious issues remain, such as the clear definition of supply, supply chain management through warehouse engineering, credit allowance during the transition phase, classification of goods and services under GST, etc. Answers to these issues must be sought at the earliest. With GST's imminent implementation, the logistics industry should start exploring different supply chain models with their clients and at the same time develop a completely synchronised ERP accounting system to support inventory supply management as required under the GST regime. Nevertheless, GST is still the change the logistics industry is eagerly awaiting as overall, the positive impact of GST far outweighs the disadvantages for this industry.

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