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BA Economics Honours | Semester 3 | Calicut University

Tax Policy in India

Course Code: ECO3MN201 • Module 4

Module IV: Goods and Service Tax in India

The enactment of the Goods and Services Tax (GST) dissolved India's fragmented indirect tax regime, instituting a unified, digital, destination-based tax architecture that transformed 28 States and 8 Union Territories into the world's largest unified free-trade common market.

Unit 16 & 17: GST Definition, Core Concepts, and Supply Typologies

Under Article 366(12A) of the Constitution, GST is defined as *"any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption."* (Petroleum crude, high-speed diesel, motor spirit/petrol, natural gas, and aviation turbine fuel were temporarily kept outside GST, continuing to attract Central Excise and State VAT until the GST Council decides on their inclusion date).

The single statutory taxable event under GST is **SUPPLY** (Section 7 of CGST Act):

- **Composite Supply (Section 8(a)):** A supply consisting of two or more naturally bundled goods or services provided together in the ordinary course of business, where one constitutes a **principal supply** (e.g., booking a hotel room with complimentary breakfast; passenger air travel with checked baggage). The entire transaction is taxed at the rate applicable to the *principal supply*.
- **Mixed Supply (Section 8(b)):** A package of two or more individual goods or services supplied together for a single consolidated price, which do not constitute a naturally bundled composite supply (e.g., a festive gift hamper combining chocolates, canned juices, and watches). The entire transaction is taxed at the **highest statutory GST rate** applicable to any individual item in the bundle.

Unit 18 & 19: Interstate versus Intrastate Supply and GST Exemptions

Under the Integrated Goods and Services Tax (IGST) Act:

- **Intrastate Supply:** Occurs when the location of the supplier and the Place of Supply are within the **same State or Union Territory**. Attracts **CGST + SGST** in equal proportion.
- **Interstate Supply:** Occurs when the location of the supplier and the Place of Supply are in **different States or Union Territories**, as well as on all cross-border imports. Attracts **IGST**, which is collected centrally and seamlessly apportioned to the consuming destination State.

Statutory Exemptions from GST

To protect socio-economic welfare and maintain low living costs for poor households, the GST Council maintains extensive statutory exemptions:

- *Exempt Commodities:* Fresh fruits, vegetables, unbranded milk, curd, eggs, loose foodgrains, coarse cereals, salt, organic manure, judicial stamps, educational textbooks, and handloom khadi.
- *Exempt Services:* Health care services by registered medical clinical establishments, primary and higher educational services by recognized institutions, agricultural operations, postal services by India Post to common citizens, and residential dwellings rented for housing.

The Input Tax Credit (ITC) Mechanism and Digital GST Architecture

The foundational genius of the GST model is the **Input Tax Credit (ITC)** mechanism (Sections 16 to 18 of CGST Act). A registered business is entitled to take credit of GST paid on all inward purchases of goods and services used in the course of business, offsetting this credit against the output GST liability payable on final sales. This completely eliminates the historical "cascading effect" of taxes.

The technical backbone of this architecture is the **Goods and Services Tax Network (GSTN)**—a massive, cloud-based IT infrastructure processing billions of invoices, automated monthly return filings (GSTR-1, GSTR-3B), e-Way bills for freight movement, and mandatory B2B e-invoicing, ensuring complete electronic audit trails and combating fraudulent tax evasion.

GST Surcharge / Rate Tier	Standard Tax Rate	Representative Commodity / Service Categories
Exempt / Nil Tier	0%	Unprocessed foodgrains, fresh milk, vegetables, basic education, healthcare.
Concessional Tier	5%	Packaged food items, edible oils, tea, coffee, life-saving medicines, economy air travel.
Standard Lower Tier	12%	Processed dairy products, computers, business class domestic air travel.
Standard Upper Tier	18%	Capital goods, industrial machinery, IT software services, telecommunications, banking.
Demerit / Luxury Tier	28% + Cess	Automobiles, luxury motorcycles, aerated sugary drinks, pan masala, gambling.

Advanced Theoretical Formulations and Empirical Frameworks (Analytical Division 1)

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Behavioral Motivation	Hyper-rational agents maximizing expected utility with complete cognitive computational capacity.	Bounded rationality, behavioral heuristics, loss aversion, and institutional anchoring effects.	Choice architecture, behavioral nudges (NITI Aayog initiatives), and consumer financial protection mandates.
State Intervention	State role restricted to core public goods, contract enforcement, and national defense (minimalist state).	State acts as developmental catalyst, risk-absorber of last resort, and promoter of equitable distribution.	Strategic industrial policy (PLI schemes), counter-cyclical fiscal intervention, and universal public services.
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Comprehensive Empirical Analysis: The Kerala Model and Sub-National Development

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However, contemporary economic analysis also highlights structural challenges confronting this development paradigm: high educated unemployment, fiscal constraints stemming from escalating public debt servicing and pension obligations, and heavy reliance on external remittance inflows from migrant workers in the Persian Gulf. Sustaining this high-welfare equilibrium necessitates transitioning toward a knowledge-driven economy, incentivizing high-tech manufacturing, and mobilizing sustainable sub-national fiscal resources.

Policy Synthesis and Analytical Evaluation

Policy formulation in dynamic economic environments must therefore synthesize foundational deductive reasoning with robust inductive empirical inquiry. Economists must continuously evaluate the balance between market incentives and regulatory governance, ensuring that institutional frameworks promote both productive efficiency and distributive social justice.

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