Is the GST Composition scheme beneficial? Cost-impact analysis shows the risks:

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Composition levy is not a practical proposition. Composition levy almost resembles a direct tax and once you do a cost impact analysis, it is really hard to understand as to how the scheme is beneficial to the business community and the MSMEs.

One of the Central Board of Excise & Customs (CBEC's) flyers on composition levy scheme in GST says: "Composition levy scheme is a very simple, hassle-free compliance scheme for small taxpayers. It is a voluntary and optional scheme.

Benefits of composition scheme:

- Easy compliance as no elaborate accounts and records to be maintained
- Simple Quarterly Return
- Quarterly payment of tax

Provisions related to composition levy have been provided under section 10 of the Central GST Act, 2017 and Chapter 2 of the CGST Rules, 2017. Under this scheme, a registered taxable person, whose aggregate turnover does not exceed Rs 1 crore (Rs 75 lakh for special category states except J&K and Uttrakhand) in the financial year 2016-17 may opt for this scheme.

A taxpayer registered under composition levy scheme has to pay an amount equal to certain fixed percentage of his annual turnover as tax to the government. This tax has to be paid on quarterly basis. Such taxpayer does not have to maintain elaborate accounts and records and instead of two monthly statement and a return (which a normal taxpayer has to file under GST), he has to file a simple quarterly return in FORM GSTR-04. The time limit for GSTR-4 for the quarter July to September,2017 has been extended to 24th December, 2017 vide Notification No. 59/2017-CGST.

"However, upon opting for this scheme, he cannot issue taxable invoice under GST law and can neither collect GST from his customers nor can claim Input Tax credit on his purchases."

Now look at the last sentence of the above paragraph. There are two significant factors, which have been incorporated as if these are in the nature of a rider. One, that the ITC is not available to a person working under this scheme and two, whatever GST, he is to pay cannot be collected from the customers.

The impact of above two factors on the costing may be analysed. Any taxable person may buy the inputs from following three categories of suppliers:

- Non-taxable person
- Person working under composition scheme
- Taxable person

No GST is payable by (a) category of persons. Certain fixed percentage is payable by persons of (b) category and the applicable rate of GST is payable by a person under category (c). For supplier from persons in category (a), neither the GST is payable, nor is the question of availability of ITC.

This, in other words, the cost impact on account of non-availability of ITC is not there. The supplier of category (b) are paying a fixed percentage towards GST and the said amount is not to be collected. Here again, there is apparently no impact on costing, but it is obvious that the supplier working under composition levy had also procured inputs, the ITC of which is not available to him, which will increase the costing at his end, resulting in supply of goods at higher value.

Now coming to the most important category of suppliers under category (c), these persons will be raising taxable invoices paying GST @ of 5%, 12%, 18% or 28%, as the case may be, the ITC of which cannot be availed by recipient working under composition levy. This amount undoubtedly is going to affect the cost considerably. This may be understood by way of an illustration.

Assuming, the taxable supplier is paying GST @18%, and the invoice is valued Rs.100. The total amount payable by recipient will be Rs.118 [Rs.100+ Rs.18]. This procurement cost is now Rs.118. He further sells the same product, say at Rs.140, at the margin of Rs.22[140-118]. He is to compete with a person who has not opted for a composition scheme.

A normal taxpayer will avail the ITC of Rs.18 and if he sells the same product at Rs.140 the GST payable will be Rs.25.20 [@18% on Rs.140]. Out of Rs.25.20, he will utilise the ITC of Rs.18 and the balance amount of Rs.7.20 will be payable in cash. Since he is in a position to collect GST from the recipient, even this amount is recoverable from the customer. He has no impact on cost, on account of GST. His profit margin will be Rs.40 [Rs.140- Rs.100].

Can a person opting for composition levy be in a position to compete with a taxable person? No. There is no level playing field. As far as GST on outward supply is concerned, the same is payable at a fixed percentage, say 2%. This 2% is not to be collected from the customer. The person under composition scheme cannot fix a price inclusive of this 2% because if he goes on calculating backward then the price inclusive of GST, that would tantamount to changing the said 2% from the customer, which will be violative.

This tax becomes in the nature of a direct tax instead of an indirect tax. The burden of this tax has to be borne by the person working under composition levy, thereby reducing his profit margin by that much percentage.

A person under composition levy is being hammered from both sides. It is something which is not a practical proposition. It is really hard to understand as to how the scheme is beneficial to a business community under MSMEs. His only option to survive under the scheme is to procure goods from a non-taxable person, which choice is very limited.