Govt may propose GST refunds on capital goods purchases to exporters

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In a bid to alleviate exporters' concerns amid an economic slowdown, the government is likely to propose changes to the goods and services tax (GST) policy to allow for the refund on taxes paid on capital goods purchases to exporters.

Though this will need a resolution from the GST Council, the finance ministry may announce the proposal in the upcoming Union Budget, scheduled on February 1, Business Standard has learnt. This will help those businesses which prefer the Letter of Undertaking (LUT) route to export their products or services.

Currently, under the LUT route, they need not pay tax on their export bills, but they stand to lose refunds on taxes paid on capital goods. Taxes on all other inputs get refunded.

They will save amounts equivalent to the taxes paid on capital goods, and improved liquidity will help boost their exports. This is being seen as one step that might help arrest the slowdown to some extent, as exporters will be more willing for new capital expenditure.

Businesses which deal with an inverted duty structure — wherein the tax rate on what they produce and sell is lower than the tax rates they pay on inputs such as capital goods — stand to benefit the most if this decision goes past all the levels in the government. For example, a fabric manufacturer who pays 5 per cent on the finished product but pays 18 per cent on dyes and chemicals (inputs) ends up being unable to utilise the credit available in the system.

The alternative route available, wherein the exporter pays Integrated GST (IGST) upfront, gets credit on taxes paid on inputs, as well as the refund of the remainder, is not suitable for businesses facing inverted duty structure. They prefer the LUT route. The catch was in the initial months under GST, when exporters had chosen the LUT route mostly to save themselves from the online GST system.

Industry players and experts said the proposed move would benefit a section of exporters engaged in capital-intensive sectors to a great extent.

"Most of the exporters opted to export under LUT as the refund process was manual, but the size of the refunds denied in lieu of taxes on capital goods has grown to quite a substantial level now," Siddhartha Rajagopal, executive director at Cotton Textiles Export Promotion Council of India (Texprocil), told Business Standard.

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Texprocil has been pushing for this change in policy in its representations to the finance ministry. Experts also said that policy should deal with both classes of exporters—those who choose the LUT route and those who choose IGST payment route—at parity.

“From a policy standpoint, treatment of GST paid on capital goods should be at par with other inputs and hence refund should be allowed to exporters. This will provide relief to industry, particularly IT/ITES sector,” Pratik Jain, leader, indirect tax at PwC India.

In this respect, corporate India is also demanding that capital intensive industries should not get dis-incentivised against labour intensive industries due to loss of taxes on capital goods.

Most of the primary exporters who imported capital goods preferred the Exports Promotion Capital Goods (EPCG) that obviated the need to pay tax on capital goods used in the business.

“Once taxes on capital goods start getting refunded, the preference towards the EPCG scheme would reduce,” said Ajay Sahai, director general and CEO at the Federation of Indian Export Organisations.

Observers also felt that this would bring the tax policy closer to global best practices, and make exports through all modes of compliance completely zero-rated.

“It is recommended that the upcoming Union Budget provides for refund of taxes paid on capital goods to exporters. This step will enable Indian manufacturers to compete globally, and help promoting the Make in India initiative,” said Pritam Mahure, a professional chartered accountant.

The issue primarily appeared as capital goods, which are the primary source of expanding the business, they are excluded from the definition of “inputs” under the GST law.

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