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# Impact of GST on Logistic Sector

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RAHUL SURESH<sup>1</sup> AND SHARANYA<sup>2</sup>

## ABSTRACT

*The implementation of GST brought the most substantial change to the indirect tax system of India by introducing a tax platform that is more transparent and convenient in functioning. Logistics industry was one of the many industries which were affected by the introduction of new tax regimes and it is expected to grow at a better rate in the near future due to the reduced tax liability. The current generation prefers a tech-savvy approach to keep a track on all aspects of their life as it enables them to receive faster and accurate information that affords some free time in the soaring busy lifestyle of people. Implementation of GST was one of such actions taken by the government in order to develop a tech-friendly tax structure that would help them to reduce tax liability and support the competitive power of Indian industries. The logistics industry has started to show profiting results under the new tax regime with the functioning cost reduced nearly by 30%-40%. It is considered to be one of the major beneficiaries of the latest tax regime (i.e. GST). There is a wide scope for addition of several value-added services to the logistics industry after the implementation of GST and this is helping the Indian logistics companies to globally compete on a higher level. But the new tax regime has not been able to provide a foolproof structure, which has resulted in the continued exploitation of laws for personal benefits. So, the paper addresses both the benefits and limitations of logistics industry under GST and would determine the appropriate changes needed to be brought into our tax system by drawing a comparison between a developed and developing nation with well-developed logistics sector.*

**Keywords:** *Logistics Performance Index (LPI), Developed and Developing Nations, GST, Unified Market.*

## I. INTRODUCTION

The sector broadly comprises of road transport, warehousing and third party logistics. The growth of logistics sector in India has soared after the rising involvement of e-commerce in the business industry. They have provided new logistics companies with better business opportunities and it has led to the rise of start-ups in India. Online business platforms have

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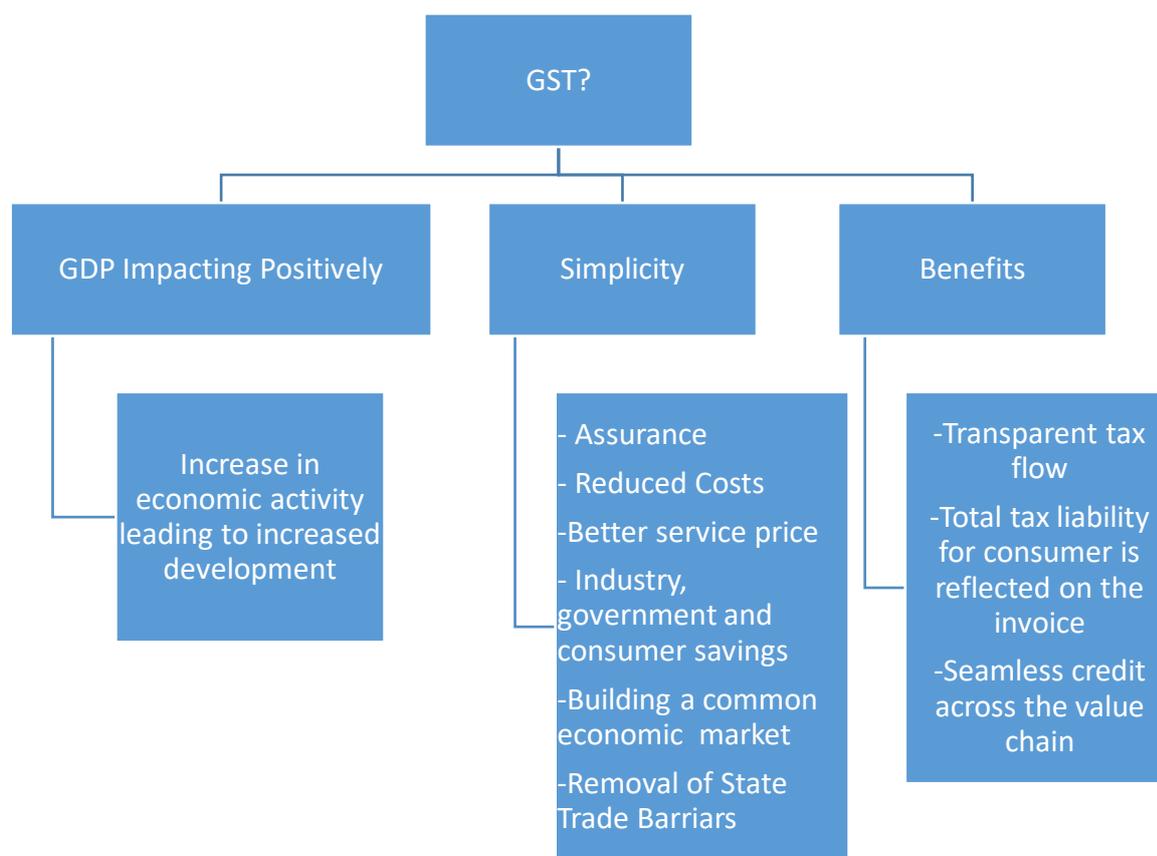
significantly helped in developing the logistics sector and reduced freight charges by providing real time data availability and transparent value chain. Deficiency of appropriate infrastructure, reliance on selected transportation modes and lack of skilled labour are some of the major hindrances in the path of development of Indian logistics. It is high time for the Indian logistics industry to adapt to the new technology in order to keep up with the global competition. Establishing an asset based business in India is not considered to be favourable due to its high entry taxes and capital investment in comparison to e-commerce business. At the same time, manufacturing in India is estimated to contribute 25%-30% towards GDP that would eventually lead to the development of our logistics sector. This sector is expected to grow at CAGR of 10.5% during the period of 2019-25<sup>3</sup>. With the implementation of GST, the previous tax rate on transport of 26.5% is brought down to 18%. The level of corruption in the transit of goods and services has reduced with the digitalization of several taxing services. The logistics industry was worth \$160 billion in the year 2017 and is currently valued at \$215 billion. According to the IBEF, the logistic industry is expected to attract investments worth \$500 billion by 2025 with the help of the newly adopted tax structure.<sup>4</sup>

The development of this industry would not only benefit logistics companies but would also play a key role in the upliftment of the “Make in India” initiative taken by the government. Since, a well-planned logistics and supply chain ensures the distribution of right good/service at the right time to the right place for the right price in the right condition to the right customer. In this paper, the research would be primarily focused upon a comprehensive analysis of the tax structure of Indian logistics sector and its impact in the growth of Indian economy. The paper compares the growth and efficiency of the logistics sector of China with our logistics industry in order to determine our level of competence with other developing nations by evaluating their strengths and weaknesses. The other comparison is made with Germany to analyse the functioning of the logistics sector of a developed nation to form appropriate suggestions for the development of our industry. The conclusions derived from this research are supported by relevant and accurate quantitative analysis in order to provide a better understanding to the reader.

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<sup>3</sup> India’s Logistics Market 2020 Research Report, Research and Markets (1<sup>st</sup> Apr, 2020)

<sup>4</sup> Madhuri Saripalle & Vijaya, GST impact on the logistics sector, Livemint (8<sup>th</sup> Aug, 2017)



## II. HISTORY

The logistics sector plays a significant role in the economic development of our country and it is currently holding the value of 160 billion US Dollars which is equivalent to 14.4% of the Indian economy. The Indian logistics sector has transformed significantly from providing mere transportation of goods from one place to another to high technology oriented service provider. Earlier, the manufacturers met the logistic needs on their own. Eventually, few basic aids of service including transportation and warehousing were handed over to companies which were specifically dealing with the logistics sector of business. At present, the services rendered by them have expanded to a much wider scope that includes management of customs procedures, setting up of assembly and manufacturing plants, warehousing, negotiation of tariff, etc.<sup>5</sup>

The logistics cost of the Indian logistics sector with respect to its GDP stands at 14% since the implementation of GST and it costs way more than other developing countries. The

<sup>5</sup> Sakshi Bahl, Evolution of Logistics Industry in India, My Story (12<sup>th</sup> July, 2017)

average logistics cost of a developing country is 9%. Pre-GST period, the logistics companies were burdened with a complex tax structure which consisted of five different types of tax *i.e. service tax, excise duty, sales tax, customs duty and entry tax*. In addition to this, malpractices like corruption and bribing senior officials paved a way to a business where other players of the logistics sector were incapable of providing quality service at a reasonable price. Companies with high net worth built warehouses in different states to avoid freight charges and reduce the cost of transport. After the implementation of GST, the prevalence of multiple taxes during transport were unified into one single tax, removing check-post related compliance and built a techno-friendly platform to manage taxes which has helped the business in saving both time and money. The need for building warehouse in every place of business in order to avoid central tax is also eliminated, leading to a more efficient use of vehicles that would help in reduction of transport cost and contribute towards the development of the Indian logistics sector. The elimination of the need to possess warehouse in every business state to provide cheaper service would help the industry in providing cost-effective service in the near future. The logistic cost is expected to reduce by 1.5%-2% with the change in warehousing pattern.<sup>6</sup>

### III. LOGISTICS SECTOR OF CHINA (DEVELOPING COUNTRY)

The logistics sector of every country develops with the economic growth of the country. As a country with high-capital would invest more in building better infrastructure to ensure smooth functioning of the logistics sector and would also help them to provide quality services in a much better manner in the international market. Similarly, many new and innovative approaches have been seen to be taken by different developing and developed countries in their logistics industry. One of such revolutionary changes was the adoption of technology in providing logistics service. Several developing countries have gradually realised the importance it holds in providing better services and they have taken appropriate measures to adapt to the new conditions. China was one of the first developing countries to realise the importance of technological innovation in the logistics industry and they started focusing on building better infrastructure through their five-year plans from 2000. By 2006, China had built highways covering 3.4 million kilometres and railways covering the distance of 77,000 kilometres.

China began its journey towards the development of its logistics industry from their period of liberalization that began in the late 1970s and gradually removed the barriers laid down by

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<sup>6</sup> CA Hemant, Impact of GST on Logistic company, GST India (21<sup>st</sup> Jan, 2020)

the government to prevent business by foreign companies and support the growth of domestic companies. Towards the end of 1993, foreign investors were given access to invest in limited sections of the domestic market under strict surveillance by their regulatory bodies. In 2001, China became a member of the WTO resulting in the removal of barriers placed against foreign logistics investments. By the end of 2006, all the restriction put on foreign logistics investment was completely wiped out, allowing a much liberalized form of investments and the sector grew at a CAGR of 12.86%.<sup>7</sup> China has definitely come a long way in establishing a world renowned logistics industry with the following key features:

- It has one of the best logistics service connectivity in the world and the government provides adequate financial backup to ensure its development with its five years plans. The Chinese Belt and Road Initiative is one of such on-going developments.
- The urban as well as rural demand for specialized logistics services, especially for perishable items like vegetables and seafood has been growing profoundly.
- The companies are facing overcapacity issues and they would continue to outsource their logistics needs to third party logistics companies due to their cost efficient functioning.
- Enforcing effective five-year plans over the decades have played a significant role in developing a highly profitable logistics sector as it possesses today. The primary focus of the 13<sup>th</sup> five year plan (2016-2020) is to develop environment friendly infrastructure networks in addition to broadening the basic road, rail, aviation and shipping infrastructure.

In 2019, China made significant reforms in its VAT policies which reduced the prevalent 16% general VAT rate and 10% VAT rates on transportation and construction activities to 13% and 9% respectively. The Chinese VAT structure did not allow refunds for excess input VAT credits but only allowed it to offset output VAT in the future tax periods. With the latest VAT reforms the government has also introduced a VAT refund mechanism on a trial basis. These tax reforms would surely help the Chinese logistics sector in the long run to earn more profits and deliver its services at a reduced cost. Even though the Indian logistics sector is yet to meet the same level of logistics service demands but it has significantly developed since the implementation of GST, which has helped in the reduction and unification of taxes related to goods and services.<sup>8</sup>

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<sup>7</sup> Zeyan & Miguel, A Survey on China's Logistics Industry, Portland State University (Jan, 2010)

<sup>8</sup> Status of the value-added Tax Reform in the People's Republic of China, OECD (2018)

<b><u>Factors of Logistics Sector</u></b>	<b><u>CHINA</u></b>	<b><u>INDIA</u></b>
<b><u>Development</u></b>		
Present growth rate (%)	4.2	10.5
Logistics Cost to GDP (%)	14.7	14

However, the estimated economic development of every country has been dropped in a considerable manner after the rise of COVID-19 pandemic and due to the inter-connection between logistics sector and economic development, the growth of logistics sector has also been hit with a severe blow. According to IMF, the estimated global growth rate in 2020 is 4.9% i.e. 1.9% lower than the April, 2020 forecast. The latest estimate of growth rate of India is 6.4% less than the growth rate projected in April by the IMF. But on the positive side, faster development of vaccine would certainly lead to the rise of economic growth.

#### **IV. LOGISTICS SECTOR OF GERMANY (DEVELOPED COUNTRY)**

Today, in this period of rapid development, Multi polar global economy, there are many countries that now have been changed into an economic power while some are still trying to chase the same path. With an aim to provide the needs of the economy an insightful change in the logistics is the need of the hour. One such example is Germany.<sup>9</sup>

Germany claims and stands to be one of the most successful and performing logistic market around the globe. One of its advantages in comparison to many nations is its geographical location in Europe. They also have greater technological advancements with immense civil infrastructural power. Logistics is Germany's third-biggest financial part post their accounting of automotive industry and the retail market. The market recorded approximately €279bn in exchange volume in 2019. The Logistics also gives employment to almost more than 3 million individuals. However, in spite of good execution they also pose greater issues and challenges at times.<sup>10</sup>

Germany also stands with providing and serving 82 million people of their own country with a counting ratio of 150 million users from its neighbouring countries and over 500 million users and European continents. They also serve as a link to and from the western and European markets that makes them stand out and be an ideal place for marketing. The intuitional investment and performance of Germany as a country is impressive too. The

<sup>9</sup> Dr Vasantha Gopal, GST in India, International Journal of Trade Economics and Finance (Apr, 2011)

<sup>10</sup> Ehtisham Ahmed & Satyam Poddar, GST reform and Inter Governmental Considerations in India, Department of Economic Affairs (Mar, 2009)

government has always been upfront in providing companies with any kind of support even at dynamic market situations creating wonders in IT and Telecommunication sectors.

The unchanging political, economical and social stability provides them with an absolutely perfect base for any entrepreneurial or developed business idea. Intellectual Property rights are also well maintained and thoroughly protected in Germany. The following are the key features of its logistics industry:

- Consecutively retained the first position for three times in World Bank's bi-annual Logistics Performance Index (LPI) evaluating 160 countries.
- Earned approximately EUR 280bn as revenue in 2018. Germany is considered as Europe's best logistics hub and its revenue is more than Europe's 2nd & 3rd largest logistics markets which is UK and France to be taken together.
- Germany is also considered to be Europe's 1<sup>st</sup> ranked economy and 4<sup>th</sup> largest worldwide, that has a capacity of generating goods and services worth EUR 3.0 trillion.
- Germany ranks third in import and export of goods.
- Germany is also called a world leader with respect to creativity and dynamic innovation which has more or less 3 million employees in more than 60,000 sectors.
- Germany is also said to be the best Intralogistics exporter with EUR 15.8bn

Germany's Logistics market revenue is similar or can be stated as equal to: Europe's total



**25 %**

The duty rates in the EU remains consistent but the VAT rates are different for every country within it. In Germany, VAT is a term that is defined as a sales tax which is imposed on the supply of all goods and services by a tax assessee while doing business in the country.<sup>11</sup> The standard VAT rate in Germany stands at 19% whereas the reduced VAT rate for few specified product categories is at 7%. As an economic measure to cope up with the devastating effects of COVID-19 pandemic on the economy, the German government

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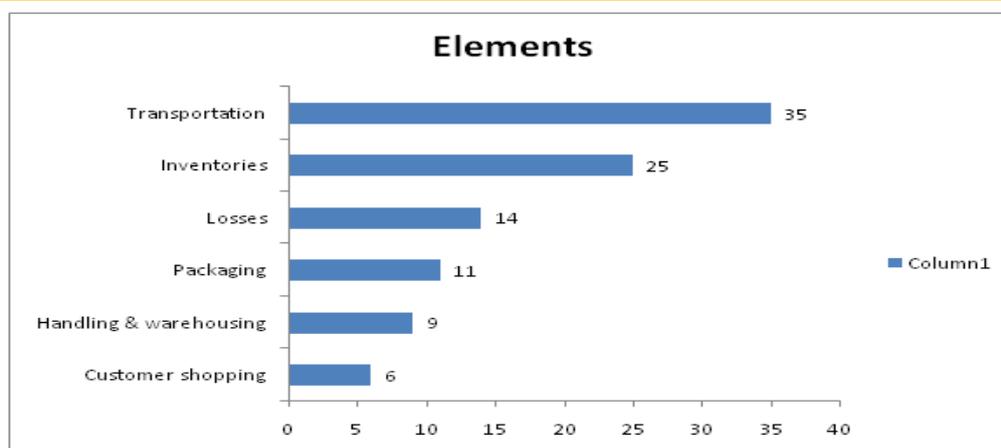
<sup>11</sup> Nitin Kumar, Goods and Service Tax – A Way Forward, Global Journal of Multidisciplinary Studies (May, 2014)

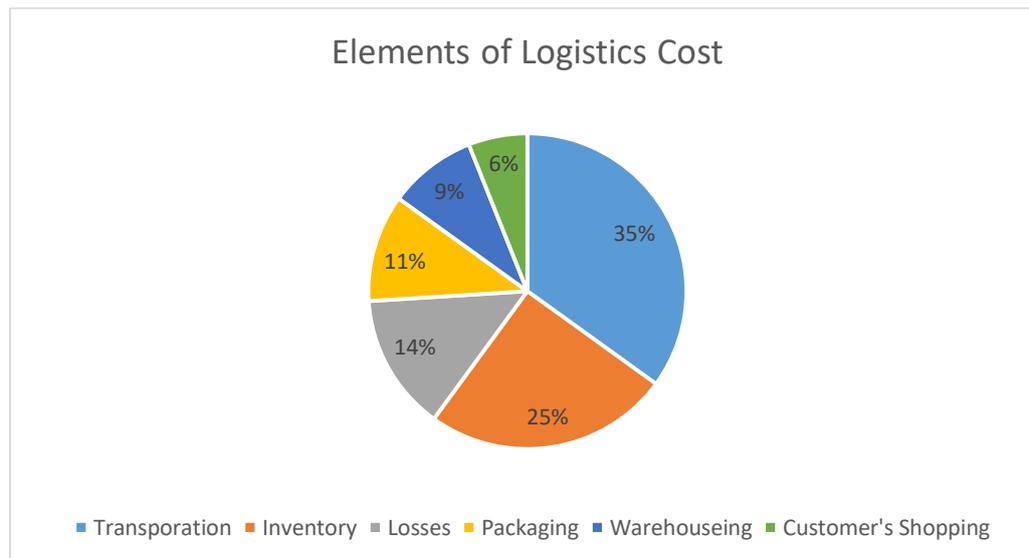
temporarily reduced the VAT rate from 19% to 16% and the reduced VAT rate from 7% to 5% from 1<sup>st</sup> July, 2020 to 31<sup>st</sup> Dec, 2020. The rate of development we could see in the German logistics sector is enormous and the Indian logistics sector definitely has a long way to come since a mere 10% of the total logistics market share represents the organised players within the sector. But with an effective analysis of the aforementioned comparison we are positive of the fact that the constant support through favourable political measures would help India to build better logistics networks to interconnect its vast population at a reduced cost.

## V. QUANTITATIVE ANALYSIS

Country	Logistics Cost/GDP (2020)	Growth rate of 3PL Companies (2020)
India	14%	11.5%
Germany	9-10%	4.5%
Europe	10%	4%
China	14.7%	15%

Fundamental features of Logistics Industry	Changes seen after GST implementation
Travel Time	Reduced by 20%
Cost incurred	Reduced by 30%-40%
Internal Trade/GDP ratio	54% (excluding agricultural products)





## VI. LIMITATIONS

After the implementation of GST, the logistics sector has experienced several tax benefits, but with a few limitations that have curbed the companies from receiving its true benefits. The following are the limitations prevalent in Indian logistics industry under GST regulation:

- Petrol and Diesel is the most commonly used raw material in the logistics sector. Both the state and central government have been desperately increasing fuel tax to earn more revenue as it does not fall under the purview of GST. On May, 2020, India became the country with the most taxes on fuel.
- The Enforcement Authority of transportation tends to ignore the definition of “GTA” under GST resulting in the imposition of tax on every transporter of goods. It has been clearly defined under GST that only the supplier of service who has been issued a consignment notice must come under the purview of GST. Hence, the CBIC must regulate such actions by GST officers taken against the interest of law.
- The services provided by GTA come under RCM (Reverse Charge Mechanism) and the service provider is not eligible for credits as they come within the definition of “exempt service” u/s 17(2) of GST. Due to this the government levy tax on GTA services under RCM and refuses tax credits for purchase of automobile, maintenance and other office work. This acts as a major financial burden on logistic companies.
- The logistics companies have the option under GST rules to charge 12% tax for its transportation services and claim ITC (Input Tax Credit). But the transporters of liquor and fuel are denied from charging 12% tax on their service as it does not come under GST. Hence, it’s difficult for them to reap the benefits like other transporters.

The government should provide them with some sort of tax benefits even if it's a reduced percentage of credit.<sup>12</sup>

## **VII. OUTLOOK OF THE FUNCTIONING OF LOGISTICS INDUSTRY UNDER GST**

The impact of GST on the logistics sector of India has been quite helpful to provide their services in a cost-effective manner. In fact, it is not the only industry which has been benefited with the adoption of a unified tax structure with the implementation of GST. Several factors of functioning within the logistics sector have taken a positive turn including its bookkeeping activities, accounting methods and the form of its operation as a whole. GST was implemented in order to make the collection of indirect taxes in a well-organised fashion. Over the years, the logistics companies have been facing difficulties in providing their services in an efficient manner due to poor connectivity, weak infrastructure facilities, multiple entry fees and a few other hindrances which have acted as a barrier against their development. Through the global comparison of logistics sector, we have seen that the compatibility of infrastructure, better logistic connectivity and tech-savvy methods of functioning acts as a major strength for the development of these logistics companies. GST was introduced with similar goals and has started to prove the level of efficiency it can bring into these sectors by adopting digital mechanisms and gradually unifying the Indian markets by providing easier opportunities for better connectivity.

GST empowers the logistics industry to avail efficient market practices including bulk-breaking and cross-docking from a central location. Practices like these would create soaring investments from retail as well as warehousing companies considering the benefits of GST and eventually transforming the country's logistics business as a whole. For transport services, the impact of GST with respect to cost would probably be minimal since important inputs like fuel falls outside the purview of GST. But the removal of trade barriers would certainly prove to be beneficial. Businesses hiring the services of transporters cannot claim input tax credit, so there is a possibility of big players leaving business which is strictly into transportation and prefer to get into more value-added services. Fundamentally, GST clearly has the potential to strengthen the efficiency of value chain players in the logistics sector, making the sector comprising of increased organised members. The GST regime will only become matured and progressive, when its prevailing loopholes (including corruption and different malpractices seen to be committed by the logistics parties) are taken into serious consideration by the government and rectified immediately. Moreover, the transportation and

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<sup>12</sup> CA Anil, Critical Issues in GST on Logistics Sector, Tax Guru (14<sup>th</sup> Apr, 2020)

logistics sector would be progressively adopting the value-added services to its functioning in order to receive better and increased business opportunities. Hence, the most common and rightful opinion about the impact on the logistics industry after the implementation of GST is that it would take time to show the practical results.

## VIII. CONCLUSION

This research paper analysis has portrayed the powerful impact that the GST would have on the Indian logistics industry in the coming years. Setting up of GST will have a powerful impact on the logistics sector, which would lead to the reduction of prices and value cost and the logistics companies would be able to perform more efficiently in India. It would also help in increasing the exports. The primary motive of the sector is to meet the demands of the customers at a reduced and easily affordable price and the same can be achieved with the implementation of GST. Today in this period of globalisation, logistics play a vital role in the development of the economy; hence the GST will shape up the economies of scale.<sup>13</sup>

GST has all the requirements to tremendously boost the growth of this particular industry. However, the true benefits of GST could only be reaped after a few financial years from its implementation and we have already begun to witness the rise in profit margin and efficiency of logistics sector. It is also said to be the new era for the logistics industry and the overall impact will be immensely beneficial for a country like India. The above comparison with the developing and the developed countries also states the same. Also, while keeping all these things in mind, it has become clear that there are far more advantages of GST in the logistics industry than the disadvantages and it's a very smart step taken by the government. We all hope that the Indian logistic sector would soon achieve results similar to the logistic sector of Germany. With the adoption of advancing technology like Big Data and cloud-based application platforms for better consumer satisfaction by the logistics companies in addition to the supportive government policies, we could assure a long-term advancement of the Indian logistics sector.<sup>14</sup>

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<sup>13</sup> Girish Gang, Basic concepts and features of GST in India, *International Journal of Scientific Research and Management*, Vol.2 Issue 2 (2014)

<sup>14</sup> Monika Sehrawat & Upasna Dhandha, *GST in INDIA: A Key Tax Reform*, Ideas (2017)