GST compensation road map may stretch into FY26

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The all-powerful Goods and Services Tax (GST) Council, at its upcoming meeting on September 9, is expected to provide a roadmap for the compensation cess that will likely continue "well into" 2025-26 (FY26), and also discuss whether it should eventually be replaced with a tax or a cess, say government officials.

An internal assessment, these officials reveal, suggests that the compensation cess needs to continue till FY26 to meet the estimated shortfall of ₹1.37 trillion as of March 2025.

The GST Council, headed by Union Finance Minister Nirmala Sitharaman and with all state finance ministers as its members, has a packed agenda and might give relief to foreign airlines grappling with GST notices of more than ₹10,000 crore. The fitment panel, set up by the council and consisting of revenue officials from the Centre and states, has recommended an exemption and regularisation of the past period on an as-is-where-is basis.

GST Council agenda includes tax relief for foreign airlines, and clarity on a host of items such as car seats

The GST intelligence department has issued show cause notices to the India offices of at least 10 foreign airlines pertaining to services received by their headquarters and asked them to cough up GST at the rate of 18 per cent.

Besides, the council might clarify the GST rates on a host of items, including on seats of cars and two-wheelers. The fitment panel suggested an increase in tax rates on car seats to 28 per cent, from the current 18 per cent, to treat them on a par with two-wheeler seats.

On the compensation cess, a status report is expected to be tabled before the council, including the likely timeframe within which the loan of ₹1.1 trillion, borrowed by the Centre in FY21 under a special window and passed on to the states, could be repaid.

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GST Council may clarify taxes for data-hosting firms

In FY22, the Centre borrowed another ₹1.59 trillion from the markets. The status report may also highlight that the entire amount of provisionally admissible GST compensation for the period up to 30 June, 2022 has already been paid to all states.

While introducing the GST regime on July 1, 2017, states were assured of compensation for their loss of revenues till June 2022. The Centre later extended the levy, which is imposed on luxury, sin, and demerit goods, till March 2026 to repay the borrowings made in FY21 and FY22 -- the pandemic years -- to compensate the states.

Between July 2017 and July 2024, the net collection of the GST Compensation Cess stood at ₹7.61 trillion. By March 2025, the collection is expected to be at ₹8.6 trillion.

"Despite this, there will still be a shortfall in the compensation account as of March 31, 2025 after factoring in back-to-back loans, interests, and so on," the internal assessment is said to have observed. It underlined that to meet the shortfall, the compensation levy would have to continue beyond FY25 and well into FY26, say sources.

Though the states' protected revenues were growing at 14 per cent compound annual growth after GST came into effect, the cess collection did not keep pace. The pandemic further increased the gap between the projected revenue and actual revenue, including a reduction in cess collection.

Among other agenda items, the Council is expected to take up relief to data-hosting firms by clarifying the tax treatment for software, Cloud computing, and whether they are eligible for export of services benefits. It might also take up regularisation of past assessment of casinos, online gaming, and horse racing.

Clarity is expected on the tax rates on charging points and components of electrical vehicles. The fitment committee is of the view that the rates should stay at 18 per cent. Clarity could also come on tax treatment of snacks and namkeen items.