

Reverse Charge Mechanism (Rcm) Under Gst and its Impact on Bihar's Economy

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Abstract

The Reverse Charge Mechanism (RCM) under the Goods and Services Tax (GST) has transformed the tax structure in India by shifting the tax liability from suppliers to recipients in specified cases. This mechanism is particularly significant for Bihar, where the economy is driven by agriculture, small-scale industries, and inter-state trade. While RCM has enhanced tax compliance and broadened the tax base, it has also introduced challenges such as administrative burdens and liquidity constraints for small businesses. This article explores RCM's legal framework, its economic impact on Bihar, challenges in implementation, government perspectives, rules and regulations, penalties, and viewpoints from taxpayers. Additionally, it discusses policy recommendations to improve RCM's effectiveness and ease of compliance for businesses in Bihar.

Keywords: GST, Reverse Charge Mechanism, Bihar Economy, Tax Compliance, Small and Medium Enterprises, Agriculture, Taxpayer Burden, Formalization, Government Policy, Tax Penalties, Economic Impact

INTRODUCTION

The introduction of the Goods and Services Tax (GST) in India was a landmark reform that aimed to simplify the indirect tax structure, enhance compliance, and boost economic growth. One of the critical aspects of GST is the Reverse Charge Mechanism (RCM), which shifts the responsibility of tax payment from the supplier to the recipient of goods or services. This mechanism has significant implications for businesses and state economies, particularly for Bihar, which relies heavily on agriculture, small-scale industries, and inter-state trade. This article explores the concept of RCM, its applicability, and its economic impact on Bihar.

Legal Framework of RCM under GST

The Reverse Charge Mechanism is governed under the following legal provisions of the GST Act:

- Section 9(3) of the CGST Act, 2017:** Specifies categories of goods and services on which tax is payable by the recipient.
- Section 9(4) of the CGST Act, 2017:** Mandates RCM on procurement from unregistered suppliers by registered persons.
- Section 5(3) and 5(4) of the IGST Act, 2017:** Governs RCM on inter-state supplies and imports.
- Notification No. 13/2017-Central Tax (Rate):** Lists specific services (e.g., legal services, goods transport agencies) under RCM.
- Notification No. 4/2017-Central Tax (Rate):** Lists specified goods such as tobacco leaves and raw

cotton under RCM.

Rules and Regulations Governing RCM

1. **Compulsory Registration:** Businesses liable to pay tax under RCM must register under GST, regardless of their turnover threshold.
2. **Time of Supply Rule:** Under RCM, the time of supply is the date of payment or 60 days from the date of invoice, whichever is earlier.
3. **Input Tax Credit (ITC) Rules:** Tax paid under RCM can be claimed as ITC only if the recipient is eligible and complies with GST regulations.
4. **Record Maintenance:** Businesses must maintain proper documentation and tax invoices for RCM transactions to ensure compliance.

Government Perspective on RCM

From the government's point of view, RCM plays a crucial role in:

1. **Enhancing Revenue Collection:** By shifting tax liability to registered recipients, the government ensures tax is collected even from unregistered suppliers.
2. **Preventing Tax Evasion:** RCM helps curb tax evasion in sectors with high instances of under-reporting and cash transactions.
3. **Formalizing the Economy:** Encourages small businesses and suppliers to register under GST to avoid tax burdens on their buyers.
4. **Improving Compliance:** Businesses are required to maintain proper records and documentation, leading to better tax administration.

The government has also introduced periodic modifications to ease compliance, such as limiting RCM applicability to specific cases and simplifying tax filing procedures for small businesses.

Legal Effect of RCM

1. **Liability Shift:** Under RCM, registered businesses bear tax liability even for purchases from unregistered vendors, discouraging informal sector transactions.
2. **Denial of Input Tax Credit (ITC) in Certain Cases:** While businesses can claim ITC on RCM payments, certain sectors (e.g., composition scheme taxpayers) cannot.
3. **Legal Penalties:** Non-compliance with RCM provisions can lead to penalties, interest payments, and increased scrutiny from tax authorities.
4. **Enhanced Transparency:** RCM helps track taxable transactions, reducing tax evasion and improving the tax collection framework.

Penalties for Non-Compliance with RCM

1. **Interest on Late Payment:** If tax under RCM is not paid within the prescribed period, interest is levied at 18% per annum.
2. **Penalty for Incorrect Tax Payment:** If a taxpayer fails to pay RCM tax, a penalty equal to 10% of the tax due or ₹10,000 (whichever is higher) is imposed.
3. **General Penalty for Non-Compliance:** Under Section 125 of the CGST Act, a general penalty of up to ₹25,000 can be imposed for non-compliance.
4. **Prosecution in Case of Fraud:** If non-compliance involves fraudulent activities, higher penalties

and even imprisonment may be imposed under GST laws.

Challenges in Implementation

- 1. Lack of Awareness:** Many small traders and business owners are unaware of RCM provisions, leading to non-compliance and penalties.
- 2. Administrative Burden:** Businesses must maintain detailed records and file additional tax returns under RCM, increasing compliance costs.
- 3. Cash Flow Issues:** Since tax liability under RCM falls on the recipient, businesses face liquidity constraints, especially SMEs with limited financial resources.

Taxpayer's Perspective on RCM

- 1. Compliance Burden:** Many businesses, especially SMEs, struggle with record-keeping and additional tax payments under RCM.
- 2. Cash Flow Constraints:** Paying tax upfront under RCM affects working capital, leading to liquidity issues.
- 3. Availing ITC:** Taxpayers prefer transactions with registered vendors to claim ITC rather than dealing with unregistered suppliers.
- 4. Reduced Business with Unregistered Suppliers:** Many businesses avoid unregistered suppliers, impacting smaller vendors and local supply chains.

Impact of RCM on Bihar's Economy

Bihar is a predominantly agrarian state with a significant portion of its population engaged in farming, small-scale industries, and unorganized businesses. The introduction of RCM under GST has had several implications for the state's economy, both positive and negative.

1. Increased Tax Compliance and Revenue Generation

One of the primary benefits of RCM is increased tax compliance, which has led to higher revenue collection. Bihar, which depends heavily on central tax allocations and GST compensation, has benefited from the additional tax collected under RCM. By ensuring that businesses pay taxes even on purchases from unregistered suppliers, RCM has widened the tax base.

2. Impact on Small and Medium Enterprises (SMEs)

Bihar's economy consists largely of SMEs and micro-businesses, many of which operate in the informal sector. Under RCM, registered businesses must pay tax on purchases from unregistered suppliers, which discourages transactions with small, unregistered vendors. This has led to compliance burdens and increased costs for SMEs, potentially affecting their profitability and growth.

3. Agriculture and Unorganized Sector

Agriculture plays a crucial role in Bihar's economy. Many agricultural products, such as raw cotton and unprocessed food grains, are subject to RCM. Farmers and small traders often find it challenging to comply with GST regulations, leading to difficulties in accessing markets and formal credit. Additionally, since many farmers are unregistered under GST, their buyers (wholesalers and manufacturers) must bear the tax burden, leading to increased costs in the supply chain.

4. Boost to Formalization of Economy

RCM has encouraged businesses in Bihar to formalize their operations to avail input tax credit (ITC). This has led to a gradual shift from informal to formal business structures, improving transparency and

economic stability. However, the transition has been slow due to the lack of awareness and digital infrastructure in rural areas.

5. Challenges in Implementation

While RCM has potential benefits, its implementation in Bihar has faced several challenges:

- 1. Lack of Awareness:** Many small traders and business owners are unaware of RCM provisions, leading to non-compliance and penalties.
- 2. Administrative Burden:** Businesses must maintain detailed records and file additional tax returns under RCM, increasing compliance costs.
- 3. Cash Flow Issues:** Since tax liability under RCM falls on the recipient, businesses face liquidity constraints, especially SMEs with limited financial resources.

6. Impact on Employment and Investment

The increased compliance burden and higher costs due to RCM have affected employment in Bihar. Many small businesses, unable to bear the additional tax burden, have reduced their workforce or slowed down expansion plans. Moreover, investors are cautious about setting up businesses in Bihar due to the complex tax structure, which affects industrial growth and job creation.

Conclusion and Way Forward

RCM under GST has both positive and negative implications for Bihar's economy. While it has enhanced tax compliance and formalized business activities, it has also posed challenges for SMEs, farmers, and the unorganized sector. To maximize the benefits of RCM while mitigating its adverse effects, the following steps can be taken:

- 1. Awareness Campaigns:** The government should conduct training programs and workshops to educate small businesses and farmers about RCM.
- 2. Simplification of Compliance:** Reducing paperwork and simplifying tax filing procedures will help ease the burden on small businesses.
- 3. Financial Support for SMEs:** The government can introduce subsidies or incentives for SMEs to manage the additional tax liability under RCM.
- 4. Infrastructure Development:** Improving digital infrastructure in rural areas will facilitate better tax compliance and economic growth.

Bihar's economic future under GST depends on how effectively RCM is implemented and whether supportive measures are introduced to assist businesses and the agricultural sector. A balanced approach will ensure that the benefits of GST and RCM contribute positively to the state's overall economic development.

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