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GST in India: Lessons from Canada and Brazil

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ABSTRACT

Drawing lessons from Canada and Brazil, two federal nations with distinct GST models, this article explores how their experiences can inform India's ongoing GST journey. Canada's dual GST structure, characterized by cooperative federalism and a harmonized revenue-sharing system, offers valuable insights for India in terms of enhancing tax efficiency and promoting intergovernmental cooperation. On the other hand, Brazil's fragmented tax system, marred by decentralized tax powers and competitive "fiscal wars," serves as a cautionary tale for India, emphasizing the need for simplification and centralized coordination to avoid inefficiencies and regional disparities. This article advocates for incorporating these lessons into India's GST framework, suggesting that a more streamlined, predictable, and business-friendly tax regime will promote sustained economic growth and equity across states. By examining both successes and failures in Canada and Brazil, this study proposes strategies for refining India's GST system to ensure its long-term success.

Keywords: GST, India, federalism, Canada, Brazil.

I. INTRODUCTION

The Goods and Services Tax (GST) introduced on July 01, 2017, is a landmark reform which aims at unifying India's fragmented indirect tax system. As a federal nation with both central and state governments wielding taxation powers, India had to balance fiscal autonomy with harmonization. In this context, the experiences of Canada and Brazil—two other federal economies with GST-like systems—offer valuable insights into the successes and challenges of implementing a consumption-based tax in a multi-tiered governance structure.²

(A) Goods and Services Tax (GST) in India

India follows a *quasi*-federal system, where both the central government and state governments possess constitutionally defined powers, including the power to levy taxes. The introduction of GST represented an attempt to centralize certain indirect taxes to create a unified national tax

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² Rao, M. Govinda. "Goods and Services Tax in India: The Journey So Far and Road Ahead." *Economic and Political Weekly*, Vol. 52, No. 9, 2017.

structure while preserving the fiscal autonomy of states to some extent.³ In the GST system, both the Centre and states impose taxes on goods and services. While this dual structure ensures revenue collection at both levels, it also requires careful balancing to prevent fiscal imbalances. The implementation of GST in India required the establishment of the GST Council, a constitutional body that was tasked with ensuring cooperative federalism between the Centre and the states. The GST Council plays a central role in harmonizing tax rates, administering compensation mechanisms for revenue losses, and addressing disputes among states.⁴ This model, which blends the powers of both levels of government, has had significant implications for fiscal federalism in India⁵ particularly in terms of revenue-sharing and fiscal equity between states. Some states have voiced concerns that the GST system undermines their fiscal autonomy by limiting their ability to set their own tax rates. In India, the primary hurdle was reaching a consensus among states, which were reluctant to surrender their taxation powers. States feared losing their financial independence, particularly those heavily reliant on Value Added Tax (VAT) revenues. To address these concerns, the central government introduced a compensation mechanism to reimburse states for potential revenue losses for five years which has now been extended until March, 2026.⁶ The formation of the GST Council helped negotiate compromises, but disagreements over tax slabs, exemptions, and administration slowed the process.⁷ Political opposition, logistical challenges, and technological readiness further delayed GST's implementation, making it one of the most debated reforms in Indian history.⁸

II. FEDERAL STRUCTURES OF INDIA, CANADA, AND BRAZIL

India, Canada, and Brazil follow different models of federalism, which significantly impact their respective GST implementations. India's federal structure is *quasi*-federal, where both the Centre and states have constitutionally defined taxation powers. The GST Council, a unique institution, plays a critical role in harmonizing tax policies and ensuring cooperation between the Union and the states.⁹

Canada follows a decentralized federal model, where provinces enjoy considerable autonomy.

³ Chakraborty, Pinaki. "GST and Federalism: An Indian Perspective." National Institute of Public Finance and Policy, 2019.

⁴ Shah, Anwar. "Fiscal Federalism and Regional Equity in Brazil and Canada." World Bank Policy Research Working Paper, 2010.

⁵ Bird, Richard M., and Pierre-Pascal Gendron. "The VAT in Developing and Transitional Countries." Cambridge University Press, 2007.

⁶ Rao, R. Kavita. "Compensation Mechanism under GST." National Institute of Public Finance and Policy, 2018.

⁷ Keen, Michael. "The Anatomy of the VAT." International Monetary Fund, 2013.

⁸ Smart, Michael, and Richard M. Bird. "The Impact on Investment of Replacing a Retail Sales Tax with a Value-Added Tax: Evidence from Canadian Experience." National Tax Journal, vol. 62, no. 4, 2009.

⁹ Supra Note 3

This is reflected in its taxation system, where provinces can choose whether to integrate their sales taxes with the federal GST. This autonomy allows for regional flexibility but requires strong intergovernmental cooperation for effective tax administration.¹⁰

Brazil, in contrast, has a highly fragmented federal structure where both federal and state governments levy overlapping indirect taxes. The lack of a uniform administration and the presence of state-level fiscal competition create inefficiencies in tax collection and compliance. The Brazilian system illustrates the challenges of excessive decentralization in a federal tax system.¹¹

(A) The Canadian Model: Dual GST with Revenue Sharing

Canada's experience with the Goods and Services Tax, introduced in 1991, provides valuable lessons for India. Like India, Canada has a federal structure with both central and provincial governments responsible for taxation.¹² Canada's GST system operates through a dual structure, with the federal government imposing a national GST, while provinces have the option to harmonize their sales taxes with the federal GST to create a single, unified tax. Provinces such as Ontario, New Brunswick, and Nova Scotia have adopted the Harmonized Sales Tax (HST), which combines both federal and provincial levies, while others, such as Alberta, continue to impose their own separate taxes.¹³

Canada's GST journey was also fraught with challenges. When introduced in 1991 by the federal government, several provinces resisted adopting the Harmonized Sales Tax (HST) due to fears of losing taxation autonomy.¹⁴ Quebec, for instance, opted to implement its own Quebec Sales Tax (QST) rather than merging it with the federal GST. Similarly, Alberta refused to impose any provincial sales tax, resulting in disparities across the country.¹⁵ Public opposition to GST was intense, leading to political backlash and contributing to the defeat of the government that introduced it.¹⁶ It took years of negotiations and financial incentives for some provinces to adopt the HST model.¹⁷

¹⁰ Supra Note 5

¹¹ Supra Note 4

¹² Supra Note 7

¹³ Supra Note 8

¹⁴ Varsano, Ricardo. "Subnational Taxation and Treatment of Interstate Trade in Brazil: Lessons for India." *International Tax and Public Finance*, Vol. 7, No. 3, 2000.

¹⁵ De Mello, Luiz. "Fiscal Decentralization and Intergovernmental Transfers: A Comparative Perspective." *OECD Economics Department Working Papers*, 2000.

¹⁶ Afonso, José Roberto. "Tax Reform in Brazil: Main Issues, Challenges, and Proposals." *Inter-American Development Bank*, 2016.

¹⁷ Perry, David B. "The Political Economy of the Goods and Services Tax in Canada." *Canadian Tax Journal*, Vol. 49, No. 5, 2001.

Lessons from Canada's GST System

One of the key lessons from Canada's experience is the importance of a revenue-sharing mechanism to address regional fiscal disparities. In Canada, provinces that adopt the HST receive a portion of the revenue collected by the federal government. This system promotes greater tax efficiency by streamlining compliance and reducing administrative costs for businesses.¹⁸ Additionally, the revenue-sharing model ensures that smaller provinces receive adequate compensation, helping to maintain fiscal balance across regions. For India, a similar mechanism could be explored to ensure that states with lower economic output do not suffer from the implementation of GST, thereby promoting equity in tax distribution.¹⁹

For India, the Canadian model underscores the importance of cooperative federalism in tax administration. India's GST follows a similar dual structure, with both the Centre and states levying taxes. However, unlike Canada, where revenue-sharing is voluntary and negotiated, India's GST Council—a constitutional body—mandates consensus-based decision-making.²⁰ The Canadian experience suggests that revenue-sharing mechanisms should be periodically reviewed to maintain fiscal balance and address regional disparities.²¹

(B) The Brazilian Model: A Complex Federal Structure

Brazil's experience with its Value-Added Tax (VAT) system offers a cautionary tale for India. Unlike Canada's relatively streamlined system, Brazil's tax regime is highly fragmented, with multiple layers of taxation at the federal, state, and municipal levels. The Brazilian system includes the *Imposto sobre Circulação de Mercadorias e Serviços* (ICMS) levied by states, the *Imposto sobre Produtos Industrializados* (IPI) imposed by the federal government, and the *Imposto Sobre Serviços* (ISS) charged by municipalities.²²

The major issue in Brazil's system is the prevalence of tax competition and cascading effects, as different states impose varying rates and exemptions. The ICMS, in particular, has led to This system has led to inefficiencies, including tax competition between states, known as 'fiscal wars,' where states reduce tax rates to attract business. These fiscal wars not only create uneven tax burdens but also lead to administrative complexities for businesses operating across state borders.²³ The lack of a unified administration further complicates compliance and

¹⁸ Supra Note 14

¹⁹ Supra Note 15

²⁰ Supra Note 2

²¹ Supra Note 3

²² International Monetary Fund, 'Brazil: Selected Issues' (IMF Staff Country Reports, 2023, Issue 289) <https://doi.org/10.5089/9798400249266.002> accessed December 25 2024

²³ Supra Note 3

enforcement, increasing litigation between states and businesses. Brazil's attempt to implement a unified GST system has faced significant challenges due to the lack of coordination between federal and state governments. The Brazilian federal government attempted to introduce a national VAT system in the 1990s, but disagreements over revenue-sharing and the distribution of tax powers between the federal and state governments resulted in the failure of these reforms.²⁴ Unlike India's GST Council, Brazil lacks a strong intergovernmental body that can resolve disputes and negotiate compromises between states and the federal government. This lack of coordination has hindered the effectiveness of Brazil's indirect tax system and has led to inefficiencies in revenue collection.²⁵

Lessons for India from Brazil's GST Experience

For India, the Brazilian example underscores the risks of excessive decentralization in a federal tax system. Without proper coordination between the Centre and the states, the GST system could face challenges similar to those seen in Brazil, where overlapping taxes and tax competition undermine the effectiveness of the system.²⁶

India's GST has attempted to avoid Brazil's pitfalls by ensuring uniformity through the GST Council's decision-making.²⁷ However, challenges such as multiple tax slabs, frequent rate changes, and compliance burdens continue to create complexities.²⁸ The Brazilian example highlights the need for simplification and predictability in taxation, which India must address through long-term structural reforms.²⁹

(C) Key Lessons for India

From Canada, India can learn the importance of a cooperative approach to federalism in tax administration. The revenue-sharing model used in Canada can be adapted to India's GST system to address regional disparities and ensure that all states benefit from the reform. By streamlining tax administration and reducing the compliance burden on businesses, India can ensure a more efficient and business-friendly GST regime.³⁰

From Brazil, India must take caution and avoid excessive decentralization. The fragmented nature of Brazil's indirect tax system demonstrates the risks of allowing states to have too much autonomy in setting tax rates and administering taxes. India's GST Council must remain a

²⁴ Supra Note 14

²⁵ Supra Note 4

²⁶ Supra Note 16

²⁷ Supra Note 2

²⁸ Supra Note 4

²⁹ Supra Note 22

³⁰ Supra Note 15

powerful body capable of resolving disputes, harmonizing tax policies, and ensuring equitable revenue-sharing across states. Additionally, India must avoid the tax competition that has plagued Brazil and ensure that states do not engage in fiscal wars that undermine the national tax framework.³¹

Both Canada and Brazil offer critical lessons for India's GST framework. The Canadian model emphasizes cooperative federalism, efficient tax administration, and a structured revenue-sharing system, which India can further refine by enhancing the role of technology in compliance. Conversely, Brazil's fragmented system serves as a warning against excessive state autonomy in tax matters, underscoring the necessity of a harmonized structure to prevent regional disparities and economic inefficiencies.³²

III. CONCLUSION

India's implementation of GST is still evolving, and the lessons from Canada and Brazil offer valuable guidance. By drawing on the cooperative federalism model of Canada and ensuring that regional disparities are addressed through effective revenue-sharing mechanisms, India can ensure the success of its GST system. At the same time, India must be cautious of the risks of decentralization, as demonstrated by Brazil's experience, and ensure that the GST Council remains empowered to resolve conflicts and promote effective tax coordination. In doing so, India can create a more equitable, efficient, and sustainable tax system that fosters economic growth and development across all states.³³

The Goods and Services Tax (GST) reform in India, like in Canada and Brazil, reveals both the opportunities and challenges of implementing a consumption-based tax system within a federal structure. The experiences of these countries offer crucial lessons for India, which continues to refine its GST framework. By integrating these lessons, India can work toward a more efficient, equitable, and sustainable taxation system that promotes economic growth.

One key lesson from Canada is the importance of cooperative federalism in tax administration. Canada's dual GST structure, where both federal and provincial governments impose taxes, emphasizes the benefits of a harmonized tax system that requires strong intergovernmental cooperation. The success of the Harmonized Sales Tax (HST), where provinces share revenue with the central government, demonstrates how revenue-sharing mechanisms can reduce compliance costs and improve tax efficiency.³⁴ For India, while the GST Council plays a vital

³¹ *Supra* Note 2

³² *Supra* Note 22

³³ *Supra* Note 2

³⁴ *Supra* Note 5

role in harmonizing tax policies, periodically revisiting the structure of revenue-sharing to address regional disparities is necessary to maintain fiscal balance.³⁵

In contrast, Brazil's fragmented tax system highlights the risks of excessive decentralization. Brazil's "fiscal wars" and inefficiencies in tax administration due to overlapping state and federal levies have created significant barriers to a unified GST.³⁶ This underscores the importance of avoiding excessive decentralization and empowering intergovernmental bodies like the GST Council to resolve conflicts effectively. India must ensure that decentralization does not undermine the system's efficiency and fairness, as seen in Brazil's prolonged struggles with tax reform.³⁷

The Canadian model's approach to public education provides another valuable lesson. Effective communication about the benefits of GST helped Canada overcome public opposition and political backlash after its introduction.³⁸ Similarly, India could benefit from enhanced public education initiatives to ease the transition, particularly for small businesses and consumers unfamiliar with the new tax system.³⁹

In conclusion, while India's GST implementation is still evolving, lessons from Canada's cooperative federalism, Brazil's fragmented system, and public education strategies provide critical guidance for refining the tax regime.⁴⁰ By improving intergovernmental cooperation, addressing decentralization issues, and implementing robust public education campaigns, India can create a more efficient, equitable, and business-friendly GST system that fosters long-term economic growth and fairness in taxation.⁴¹

³⁵ Supra Note 3

³⁶ Supra Note 16

³⁷ Supra Note 4

³⁸ Supra Note 17

³⁹ Supra Note 2

⁴⁰ Supra Note 7

⁴¹ Supra Note 14