15 -ാം കേരള നിയമസഭ

14 -ാം സമ്മേളനം

നക്ഷത്ര ചിഹ്നം ഇല്ലാത്ത ചോദ്യം നം. 2585 **06-10-2025 - ൽ മറുപടിയ്ക്ക്**

ജി.എസ്.ടി. പരിഷ്കരണത്തെ തുടർന്നുള്ള വരുമാന നഷ്ടം

ചോദ്യം		ഉത്തരം	
ശ്രീ. റോജി എം. ജോൺ		ശ്രീ കെ എൻ ബാലഗോപാൽ (ധനകാര്യ വകുപ്പ് മന്ത്രി)	
(എ)	ജി.എസ്.ടി. പരിഷ്കരണത്തിനെ തുടർന്ന് വരുമാന നഷ്ടം ഉണ്ടാകുന്നതിനാൽ സംസ്ഥാന സർക്കാർ കേന്ദ്രത്തിനോട് നഷ്ടപരിഹാരം ആവശ്യപ്പെട്ടിട്ടുണ്ടോ; വിശദാംശം വ്യക്തമാക്കുമോ; നഷ്ടപരിഹാരം ആവശ്യപ്പെട്ട് കേന്ദ്രസർക്കാരുമായി നടത്തിയ കത്തിടപാടുകളുടെ പകർപ്പ് ലഭ്യമാക്കുമോ?	(എ)	കേന്ദ്ര സർക്കാർ പ്രഖ്യാപിച്ച പുതിയ ജി.എസ്.ടി. നിരക്കുകൾ നിലവിൽ വരുമ്പോൾ സംസ്ഥാനത്തിനുണ്ടാകുന്ന സാമ്പത്തിക നഷ്ടം കണക്കിലെടുത്ത് പതിനാറാം ധനകാര്യ കമ്മീഷന് 2025 സെപ്റ്റംബർ മാസത്തിൽ ഒരു സപ്ലിമെന്ററി മെമ്മോറാണ്ടം നൽകിയിട്ടുണ്ട്. പ്രസ്തുത മെമ്മോറാണ്ടത്തിന്റെ പകർപ്പ് അനുബന്ധമായി ചേർക്കുന്നു.

സെക്ഷൻ ഓഫീസർ

Supplementary Memorandum

PRESENTED TO

The Sixteenth Finance Commission

FINANCE DEPARTMENT

SEPTEMBER 2025

GOVERNMENT OF KERALA

Supplementary Memorandum

PRESENTED TO

The Sixteenth Finance Commission

FINANCE DEPARTMENT

SEPTEMBER 2025

Supplementary Memorandum from the Government of Kerala to the 16th FC

Since December 2024, when the Government of Kerala submitted its Memorandum to the 16th Finance Commission, there have been dramatic shifts in the economic environment facing the state. Two of these changes- one completely exogenous, in the form of the punitive tariffs of 50 per cent imposed by the Trump administration on imports from India, and the other a shift almost wholly outside the control of the state government in the form of significant GST rate reductions – have implications that warrant the submission of this supplementary memorandum. This is because both developments have damaging effects on the State's finances: GST rate cuts will sharply reduce Kerala's SGST revenues, while higher US tariffs will hurt export-based industries, reducing the state government's tax base while necessitating mitigating expenditures.

I. GST Rate Rationalisation and Revenue Loss for the States

1. Background and Context

The 56th meeting of the GST Council was convened on 3rd September 2025 under the chairpersonship of the Union Finance Minister. The Council resolved to rationalise tax rates across a wide spectrum of goods and services. The rationalisation has led to significant reduction on the rates imposed on many commodities.

While several States, including Kerala, acknowledged the need to mitigate the adverse effects on prices, and therefore on the real incomes of ordinary consumers, of high GST imposts, serious concerns were expressed as to whether rate reductions would truly benefit consumers in the form of lower prices. More importantly, apprehensions were raised about the significant revenue losses likely to be incurred by the States as a result of these decisions.

Representatives from Kerala highlighted the fact that, with a per capita income of ₹2,63,945 in 2023-24 (ranking 8th nationally as per the Economic Survey), the State's consumption basket is disproportionately weighted towards higher-taxed items. Accordingly, the proposed reduction in taxes on about 30 items, following their shift from the 28% slab to the 18% slab, is expected to have a disproportionately high impact on Kerala's revenues compared to other States.

2. Past Experience with Rate Rationalisation Decisions

Kerala's earlier experience with rate cuts demonstrates their adverse fiscal impact. The rationalisation of November 2017, which covered 178 items, had a severe effect on the State's revenues. Consequently compensation to the State for revenue shortfall escalated from ₹2,102 crore in 2017-18 to ₹3,532 crore in 2018-19, and further to ₹8,111 crore in 2019-20. It peaked at ₹12,828 crore in 2020-21, clearly illustrating the magnitude of the revenue loss.

The Arvind Subramanian Committee had recommended a Revenue Neutral Rate (RNR) of 15–15.5%. However, States were assured of a 14.4% RNR at the time of GST introduction, in return for surrendering substantial taxation powers. In November 2017, a single stroke reduction of taxes on 178 items sharply lowered the average tax rate to 11.6%. Several further reductions followed, and with the present proposals, the average tax rate will fall even further. In the event, contrary to assurances, GST has not displayed the expected buoyancy even after eight years of implementation. The result has been a substantial weakening of the fiscal position of most States, including Kerala.

3. Kerala's Revenue Loss under the GST Regime

The very design of the GST regime put the States at a disadvantage due to the rates being apportioned on 50:50 basis between the Centre and the States. This 50:50 ratio was adopted even though 44% of taxes subsumed under the new regime were State levies, as against only 28% that were Union levies. A fair ratio should have been 60:40 in favour of States, implying higher SGST rates for the States.

Had Kerala's GST revenue continued to grow even at 12% from the protected base after the compensation period, revenues would have reached ₹51,892 crore in 2024-25. In reality, collections stood at only ₹32,773 crore. On a pre-GST trajectory, with an average growth of 15.2% (the CAGR during the preceding decade), revenues would have been around ₹60,377 crore. Nationally, GST revenues grew by 1.99 times between 2018-19 and 2024-25, whereas Kerala's grew by only 1.56 times. The divergence between national and State growth patterns is stark.

With the cessation of compensation and no provision for revenue protection, the current round of reforms will result in a further steep decline in Kerala's revenues.

4. Estimates of Revenue Loss from Current Reforms

The Gulati Institute of Finance and Taxation (GIFT), Thiruvananthapuram, based on e-way bill data for 2018-19 and 2019-20, has estimated a revenue loss of around Rs.6300 crore per annum. That compares with collections of Rs. 32,773 crore in 2024-25.

The above losses have to be seen in the background of the fiscal constraints faced by the States as a result of the cessation of the GST compensation paid to them to cover revenue losses, with effect from July1, 2022, despite demands that the payments financed with a compensation cess should be continued. The recent rate revision will severely worsen the fiscal weakness that resulted from that decision. The argument that the rate reduction will spur consumption and that the increase in sales volumes will neutralise the effects of the reduction in rates and keep revenues at their previous levels is unlikely to hold. There is no guarantee that the benefits of the rate cut will be passed on to the end consumer, and even if they are, the price elasticities of demand may be inadequate to stabilise consumption levels.

Kerala, along with other States, had urged that additional levies be permitted on demerit goods such as cigarettes and pan masala, in order to preserve effective tax rates. This was not accepted, nor has the Union Government clarified how the effective incidence on such goods will be safeguarded. Consequently, no mechanism presently exists to compensate States or prevent fiscal imbalance.

To meet the substantial revenue shortfall expected on these grounds, Kerala requests the Sixteenth Finance Commission to provide **rule-based support** instead of one-time relief. This should include:

- A **GST Rate-Cut Compensation Grant** under Article 275 to cover a large share of the revenue loss from GST Council decisions.
- Adoption of a rule under which any future GST rate cuts over 2026–31 will automatically trigger compensation to states, without the need for repeated requests.

5. Kerala's Consumption Pattern

The expectation that rate cuts will boost consumption, thereby offsetting revenue loss, would definitely not hold true for Kerala in particular. The State's demographic profile - characterised by a high proportion of elderly population - limits its Marginal Propensity to Consume (MPC). The elderly spend relatively less on incremental consumption, particularly on durable goods. Hence, though Kerala's absolute Private Final Consumption Expenditure (PFCE) remains high, incremental consumption consequent to tax reduction cannot be expected due to saturation of demand for household durables. This caps the rate elasticity of consumption for Kerala, even assuming that rate cuts result in lower prices.

6. Fiscal Implications

Kerala has consistently contributed about 4% to national GDP since 2016-17. Yet, its tax revenue-to-GSDP ratio has fallen from 3% in 2015-16 to 2.62% in 2024-25, revealing structural flaws in GST rather than deficiencies in tax administration. Simultaneously, Kerala's share in the Union divisible pool has consistently declined — from 3.9% under the 10th Finance Commission to 2.5% under the 14th, and further to 1.925% under the 15th Finance Commission.

The State's tax structure, earlier designed to align revenues with its high living standards, has been fundamentally altered, resulting in fiscal compression. While Kerala continues to maintain high developmental and per capita income levels, its fiscal capacity has been eroded. The current restructuring of GST rates threatens to worsen this imbalance.

The Finance Commission, is constitutionally empowered and mandated to recommend grants to States in need of assistance under Article 275 of the Constitution. In the earlier Memorandum, Kerala had detailed the Vertical Fiscal Imbalance (VFI) between the Union and the States. The present rate reduction, will worsen the VFI for the next quinquennial period starting from 2026-27. Since the compensation from cess levied on items falling under the 28 percent rate has stopped, an appropriate constitutional way to prevent worsening of VFI in the next quinquennium is to recommend further grants under Article 275, taking into consideration the immediate revenue loss to the State.

II. The Challenges posed by the recent US reciprocal tariff which have impacted export-oriented sectors of Kerala

Prior to the GST rates modification, Kerala had to contend with the fallout of the punitive tariffs on imports from India imposed by the Trump administration. With tariffs on Indian exports set at 50 per cent as compared to 10-20 per cent in the case of most competitor nations, US imports from India are expected to fall significantly with attendant effects on production and employment. The presence of multiple sectors with exports directed at the US in Kerala is expected to impact the State across sectors. These include:

- ✓ **Marine Sector:** This is likely to be one of the worst-affected sectors, with an added immediate impact on working capital access due to stricter bank scrutiny and recovery actions on US shipment bonds. Besides the effects across dependent populations, the social impact of potential job losses, as for example on women workers engaged in activities like shrimp peeling, is also a significant concern.

- ✓ **Spices Sector:** Forty per cent of the exports from this sector is estimated to go to the US market. That would affect demand and earning. Simultaneously the sector has been hit by the reduction of the RoDTEP (Remission of Duties and Taxes on Exported Products) benefit from 3% to 1% by the central government.

- ✓ **Cashew Sector:** With 50% of value-added cashew exports destined for the US, this sector is likely to be heavily impacted, especially during the peak festive season. Competitors like Vietnam, Indonesia, and Ivory Coast enjoy lower tariffs, and new contracts have already been curtailed.

- ✓ **Textiles Sector:** With 30% of exports to the US market impacted, this sector anticipates oversupply and reduced orders from manufacturers in the domestic market.

- ✓ **Coir Sector:** The coir industry, facing demand that is highly price-sensitive and being labour-intensive in nature, cannot absorb tariff hikes. The demand for coir products is highly seasonal in the US market with December being the peak demand period. So, the sector is likely to experience an immediate reduction of orders leading to the build-up of unsold inventory in the godowns.

- ✓ **Plantation Sector (Tea):** US demand for iced tea is expected to decline, with attendant consequences, and the supply of tea fibre—a byproduct used as a raw material for pharmaceutical and cosmetic industries—will also be impacted.

- ✓ **Rubber Industry:** The rubber sector, which exports 60-70% of its value-added products to the US, will for obvious reasons also be severely impacted.

The total revenue loss due to US reciprocal tariff is estimated to be Rs. 2400 Crore during 2025-26.

Submission

The recent rate revision in Goods and Services Tax will result in loss of revenue to the States. As elaborated in the Memorandum already submitted by Kerala to the 16th Finance Commission, Vertical Fiscal Imbalances have been worsening due to various factors including a rising share of surcharges and cesses in the Gross Tax Revenue of the Union and the fall in revenues from items included under the GST. The present revision of rates in GST will exacerbate the gap between own and devolved revenues and the expenditure obligations of the States including Kerala. This needs to be compensated through the provision of grants.

In view of these developments, the 16th Finance Commission should factor in the revenue loss to the States in its report and recommend Supplementary Grants under Article 275 of the Constitution of India to offset the loss arising from the GST slab rationalisation and the recent US reciprocal tariff which has impacted Kerala's export-oriented industries. To facilitate that, the it is requested that the Commission reassess State Finances and consequent resource needs for the next five years to re-estimate the resource needs of the States to arrive at its recommendations on the level of vertical devolution and revenue deficit grants.

In addition, in the medium term Kerala should be made eligible for a temporary extra borrowing limit of 0.5% of GSDP, to be used for export-related infrastructure like ports, cold chains, etc. to help absorb the impact of US tariffs and develop new markets.

These measures will give Kerala the fiscal space to keep essential services running, protect jobs and livelihoods, and continue investing in growth-oriented infrastructure.

GOVERNMENT OF KERALA