

Measuring the tax cost of investment in India: Through estimation of Marginal Effective Tax Rates (METRs)”

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Abstract

“The GST is the most far-reaching restructuring of the Indian tax regime since independence. Its impacts will ramify through all sectors of the Indian economy, from investment through production and consumption. We focus specifically on the impact of the GST on incentives to invest in India. To do this, we measure the tax cost of investment in the pre-GST and post-GST environments, and compare these costs across sectors and at the all-India level. Our metric for the tax cost of investment is the Marginal Effective Tax Rate (“METR”), a statistic measuring the tax wedge imposed upon a marginal investment, where the tax wedge is defined as the difference between the gross-of-tax return on capital and the net-of-tax return on capital for a marginal firm. The use of METRs to evaluate tax systems has a long history in many countries, but ours is its first implementation for the Indian economy. We find that the GST improves investment incentives by moderately reducing the tax burden. Further improvements can be made by streamlining the GST system, primarily by unblocking input tax credits in core sectors of the Indian economy. We also find that METRs vary significantly across Indian industries, and that the impact of the GST on investment incentives in these sectors is also heterogeneous.”

Speaker Profile

“Dr. Gaurav S. Ghosh is an economist with EY’s Economic and Policy Advisory Group. He’s currently based in Bangalore. He joined EY in 2012 in Düsseldorf, Germany, after spending two years as a post-doctoral researcher in energy economics and policy at RWTH Aachen University, Germany. Gaurav provides transfer pricing and economic advisory services in diverse areas, including public policy, competition economics, inter-company financing, IP valuation, business restructuring, M&A and demand estimation. Gaurav has worked with clients in government as well as the automotive, steel, power, leasing and alcohol industries. Gaurav received his PhD in Environmental Economics from the Pennsylvania State University, USA. He also holds a Masters in Economics from the Jawaharlal Nehru University, India. Gaurav has spoken often at international research conferences and published papers in academic journals. He used to write an economics column for The Economic Times.”