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The GST Conundrum: Unravelling Impacts on Economy, Society and the Way Forward

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1. Introduction

The Goods and Services Tax (GST), implemented in 2017, represents a fundamental shift in India's indirect tax system from a production-based to a consumption- or destination-based model. The reform aimed to replace a fragmented structure of multiple central and state taxes with a single, integrated system, creating a unified national market for the free movement of goods and services, optimise efficiency and equity in the tax system, and eliminate distortions such as cascading effects. Since then, significant GST reforms have been introduced to streamline compliance, broaden the tax base, prevent the export of taxes across jurisdictions, support economic growth and promote cooperative federalism (Roychowdhury, 2012). Key measures include simplified tax filings, e-invoicing, the establishment of dispute tribunals, and the rationalization of tax rates by moving many goods from higher slabs to lower slabs. While these steps did result in some improvement in higher transparency, substantial work remains to address emerging challenges impacting the economy and society. Existing evidence is scattered, leaving important gaps in the understanding of how GST has changed the character of fiscal federalism, burden of compliance & GST Governance, consumption baskets, discretionary spending, and the welfare of different income groups.

India's GST experience shows that GST is not a single event but a continuous development. Its implementation involved major administrative changes, such as creating a new IT system for registration and returns, reclassifying goods and services, and engaging a wide range of stakeholders (Dikshit et al., 2022; Shukla & Kumar, 2019). The evolution of GST continues to be shaped by political negotiations and decisions by the GST Council, which aims to improve and adapt the system over time. Many policy experts see GST as a resilient yet incomplete reform - one that will remain but still evolve (Prof. Govinda Rao & Najib Shah, address at ISEC, 2026).

In the Indian context, empirical literature on the distributional impact of GST, however, remains limited. The incidence of GST is not purely statutory but depends on market conditions, such as price elasticity of demand and the degree of competition, which influence how much tax businesses can pass on to consumers. These distributional effects are also shaped by which items are taxed at which rates and how exemptions are designed (Mukherjee, 2025). Therefore, the tax rate structure plays a significant role in determining whether the tax is progressive or regressive. The continuous evolution of GST through rate changes and compliance rules appears to have implications for price levels and consumption patterns. A large proportion of food items in India are either exempt or placed in the lowest GST slab 5% (Government of India, 2025), while higher GST rates (18%, 28% and 40%) are predominantly applied to non-food items. However, as per the Household Consumption Expenditure Survey 2023-24 (2025), there has been a significant shift in the consumption from food to non-food items. Top income quintile households do bear a disproportionately larger share of the tax burden in both rural and urban areas, so also the middle-income and bottom 40% households (Mukherjee, 2025; Ravi and Penumarty, 2025). Their spending on durable goods and assets and services, bearing a higher tax rate, have increased during the last two decades. Low and middle-income households during the period have been able to access durable goods/assets and services with the help of the states and union governments' policy and income transfer schemes.

2. The Challenges and Identified Issues

The two-day conference titled "The GST Conundrum: Unravelling Impacts on Economy and Society," organised by the Centre for Economic Studies and Policy

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(CESP) at ISEC, provided a comprehensive view of India's Goods and Services Tax (GST). It successfully brought together researchers, policymakers, tax officials, business leaders, and civil society to discuss key issues and suggest policy frameworks for future GST reforms. These reforms aim to boost growth and consumption across different socio-economic groups and economic actors, supporting India's long-term development. While acknowledging that GST reforms have achieved notable macroeconomic success, the discussions also highlighted various structural challenges. These are not just administrative or technical; they are deeply embedded in the tax's design, its impact on federal relations, the operational realities for businesses, and its overall effect on household welfare. The expert panels and researchers explored issues and themes, including:

i) Fiscal Federalism & GST

The idea of "One Nation, One Tax" is questionable without fiscal cooperative federalism. The erosion of state autonomy and the widening disparity were among the first two issues brought out by discussants. The Union government in past decades is strengthening its position relative to states by increasing the share of revenues outside the divisible pool such as cesses and surcharges. GST too is becoming a tool of centralisation and a cause for the prevailing tension between GST's promise of cooperative federalism and its actual impact on states' fiscal autonomy. The experts do not see this tension as just theoretical, but empirical evidence of a growing disparity among states due to the structure of GST. The destination-based tax system of GST shows a divide between "Production States" and "Consumption States," with the latter benefiting at the expense of the former. In the post-reforms period, the GST revenue of high-income consumption states shows higher improvement than that of low-income states. The structural factors widen such revenue gaps and institutional weaknesses disturb the balance of authority between the Finance Commission and the GST Council, affecting state representation. The perception that the Union holds too much influence in the Council undermines cooperative federalism. It raises governance concerns: a system in which states have lost autonomy yet lack equal influence over revenue rules.

India can benefit from both international experiences and local realities. Canada, the European Union, and Brazil in this regard offer valuable lessons. Canada's cooperative federalism model illustrates how provinces can retain fiscal independence while being part of a unified VAT system, providing India with insights into balancing national unity and state authority (Nayyar & Singh, 2018; Nidigattu, 2021; Mahesh, 2024), and strengthening its secretariat to produce data-driven impact analyses for all states. Federal systems such as Canada and the European Union permit subnational governments significant fiscal autonomy. GST's limits on states' revenue-raising weaken the principle of subsidiarity that decisions should be made at the lowest appropriate level. The EU example emphasises the importance of harmonised rules for easier cross-border trade, a key goal of GST, ensuring that "one nation, one tax" works effectively.

ii) The Incidence of Compliance Burden

The legal provisions of GST require the implementation at the ground level for MSMEs and other businesses. This involves certain crucial governance issues that initiate some micro-level struggles. While GST has formalised the economy and broadened the taxpayer base, it has also imposed very restrictive and complicated compliance structures on smaller businesses. The complexity of the law significantly contributes to the burden. The multiplicity of GST rates and classification disputes remains one of the key challenges. The introduction of complexity in the point of supply, e-way bills, and the reconciliation of multiple returns (e.g., GSTR-2A and 3B) makes a compliance framework difficult for small players to navigate and frequent changes in GST guidelines and policies put a significant burden on substantial number of MSMEs with limited manpower resources. A disconnect between the GST law and the GST portal, where the portal sometimes delays the implementation of legal provisions or performs functions beyond its legal scope (such as interest calculations), results in legal ambiguity for taxpayers. Although awareness has improved, issues such as portal difficulties, return-filing complexities, and the reverse charge mechanism remain significant. The continuous reforms in GST have brought moderate public favourability but also underline operational hurdles causing measurable stress, especially for traders and service providers. This issue is further exacerbated by the persistent "trust deficit" attitude of tax authorities treating businesses as potential evaders rather than as partners in revenue collection.

Furthermore, the narrow tax base, exclusion of petroleum and alcohol and other exemptions remain a part of structural weaknesses. For example, exemptions block the flow of credit, and the exclusion of petroleum creates a huge cascading effect. For MSMEs, such fragmentation of the input tax credit chain directly leads to working capital shortages.

iii) GST Administration & Governance

The reliance on the GSTN portal, e-invoicing, and e-way bills signifies major technological progress. These advancements highlight how AI-powered fraud detection and pre-filled data boost efficiency. However, the operational reality lags the 'digital promise'. The ambiguity in the law and excessive powers granted to departments have often led to baseless complaints against taxpayers. The tax department assuming all taxpayers non-compliant, causes compliant businesses to suffer due to the actions by a few defaulters. Such governance challenges cannot be fixed by technology alone.

The administrative burden is also tied to system complexity. A study from West Bengal, for example, highlights that almost 17% of small retailers viewed GST negatively, citing 'unresolved ITC claims' and the 'digital divide.' This divide refers to limited digital engagement in semi-urban and rural areas, despite the promise of seamless digital governance. Smaller and rural businesses struggle to adapt.

iv) Distribution, Welfare, and Consumption Effects of GST

The final, and possibly most important, challenge concerns GST's long-term effects on household welfare. The studies presented in the seminar on distributional effects revealed a detailed picture of differential tax burden on different households, asymmetric price transmission, and firms' price behaviour post GST reductions.

Section 171(1) of CGST Act, 2017 states that the supplier shall pass on to the recipient by way of commensurate reduction in prices. The evidence suggests that GST reductions do not lead to equivalent price decreases. Large firms with pricing power often retain the benefits of rate cuts in the form of higher profits, partly due to weak enforcement of anti-profiteering measures. National Anti-Profiteering Authority (NAPA), which was established to examine the cases of compliance operated with very meagre staff against massive number of firms to regulate. Effective from 1st April 2025, NAPA was dissolved and its functions were briefly transferred to Competition Commission of India (CCI). However, since anti-profiteering was not a core function of CCI, it was later shifted to National Bench of Goods and Services Tax Appellate Tribunal (GSTAT). GSTAT has only 5 members and 5 assisting staff to handle all pending as well as future cases of non-compliance.

3. Towards a Transparent Policy

The two-day conference on "The GST Conundrum: Unravelling Impacts on Economy and Society" made it clear that India's GST reform is an ongoing, evolving process. Although GST 2.0 introduced key reforms to correct the course, issues such as federal tensions, compliance challenges, and distributional effects indicate that the system remains a "work in progress." Building on the conference's findings, future policies should be planned across three timeframes: short-term operational solutions (to be implemented within 18 months), medium-term structural reforms (which need legislative approval and political agreement over 2–5 years), and institutional strengthening to create a solid foundation for long-term reform. The conference's discussions led to specific short-term and medium-term policy recommendations.

I. ShortTerm Priorities

1) **Strengthen the GST Council Secretariat to rebalance federal relations:** The conference highlighted the ongoing tension between cooperative federalism and state autonomy. To resolve this, it is essential to build trust, promote consistency, and support evidence-based decisions. India can learn from Canada's model. There provincial autonomy exists within a unified VAT system. India should enhance the Council's secretariat to provide independent, data-driven analysis. This would support and empower states during negotiations, fostering cooperative federalism and addressing concerns about state autonomy.

2) **Fast-track refunds and correct inverted duties:** The GST Council needs to act quickly to tackle refund delays and inverted duties impacting small traders and MSMEs. Slow Input Tax Credit (ITC) refunds strain their working capital, while inverted duties lead to inputs being taxed more heavily than finished products. These problems undermine their confidence in the system. Accelerating refunds and properly adjusting inverted duty structures would help reduce the pressure on their financial stability.

3) **Enhancing compliance and administration through Technology:** The digital infrastructure is vital for the success of GST reforms, but it currently falls short in serving India's diverse groups. Small businesses, MSMEs, and retail traders in rural and semi-urban areas face more operational challenges than large firms with skilled staff and legal support. While emerging tools such as AI-based fraud detection, e-invoicing, and e-way bills help prevent tax evasion, they must also support small businesses in achieving higher compliance through fair, user-friendly solutions. The goal is to create a genuinely "faceless, technology-driven system" that minimises discretionary human intervention. This digital effort should be complemented by capacity-building programs, especially for MSMEs and traders in semi-urban and rural areas, to bridge the "digital divide," address issues of "frivolous complaints," and foster the persistent "trust deficit." Proposed solutions include publicly sharing GST data, and creating a "faceless, tech-driven system" to reduce discretionary human interaction. These steps are vital to closing the gap between the digital framework and on-the-ground governance.

4) **Establish a mechanism for uniform interpretation and taxpayer awareness:** The growth of state tribunals and advance ruling committees has caused conflicting interpretations of GST laws. This inconsistency, along with lengthy litigation and significant uncertainty, has diminished confidence, especially among small and medium-sized businesses. The GST Council can tackle this by establishing a centralised authority to ensure uniform GST interpretations and promote consistency for businesses operating across states. They can also issue straightforward circulars, run awareness programs, and develop a digital platform with simplified rulebooks, interactive guides, and video tutorials. These efforts should be customised to address the specific needs of MSMEs, small businesses, and retail traders. Additionally, streamlining dispute resolution processes and setting strict timelines for appeals can reduce litigation and boost taxpayer confidence.

II. MediumTerm Priorities

The conference's findings on asymmetric price transmission and the vulnerability of middle-income and farm households highlight the need for policy tools that extend beyond rate-setting. The following steps are recommended to address distributional and welfare concerns:

i) **Strengthen anti-profiteering enforcement:** The asymmetric transmission of GST tax cuts and rate rationalisation reveals a significant market failure. The GST regulatory body lacked a sufficient workforce to monitor companies across sectors that benefited from these changes. Strengthening the anti-profiteering mechanism with better staffing and institutional backing is essential for effective regulation and enforcement. Without these improvements, the objectives of GST reforms and the intended benefits from rate reductions reaching consumers are unlikely to be achieved. This effort should include stricter enforcement, greater pricing transparency, and a requirement for firms to submit documentary evidence. Possible measures could involve mandating quarterly compliance reports to show price pass-through or deploying automated audit alert systems.

ii) **Monitor and mitigate cost of living pressures:** The finding that middle-income households have become the most vulnerable group due to structural changes in consumption patterns underscores the importance of active policy monitoring. Future rate rationalisation exercises should include a welfare impact assessment, with particular focus on services that constitute an increasing share of household spending for middle-class and farm households. This analysis should guide rate adjustments to protect discretionary spending savings.

iii) **Provide targeted relief for farm households**: Explore mechanisms to counteract the indirect GST impact on small and marginal farmers, such as a refundable input tax credit for agricultural supplies or direct income support, ensuring the tax does not unintentionally harm the agriculture sector.

iv) **Institutionalise a biennial GST welfare review:** Establish an independent panel of economists and social scientists to review the impact of GST biennially across different income groups, consumption categories, and sectors. The panel will present their findings to the GST Council to inform rate-setting and ensure policy adjustments account for evolving consumption patterns, particularly the vulnerabilities of middle-income households.

4. Looking Forward

India's experience with the Goods and Services Tax (GST) highlights a key insight into modern tax reform: significant fiscal restructuring is rarely a one-time event but an ongoing process involving learning, negotiation, and adjustment. The discussions at the ISEC conference confirm that while GST has successfully created a unified national market and broadened the tax base, it remains an incomplete project. Ongoing challenges include federal tensions limiting state fiscal autonomy, compliance burdens that hit MSMEs and small traders hardest, digital governance infrastructure that still does not fully address issues in semi-urban and rural areas, and distributional effects that mainly impact middle-income and farm households. These issues show that the system, even after eight years, is still a "work in progress" needing further strengthening.

Building on the conference's findings, the future approach should be a carefully designed strategy that addresses operational inefficiencies in the short term, structural distortions in the medium term, and institutional weaknesses over both periods. Important steps include speeding up refund processes, adopting a faceless, technology-driven administration, strengthening the GST Council secretariat with independent analytical capacity, and institutionalising regular welfare evaluations. These measures are vital in creating a tax system that is simple, equitable, and cooperative. Ultimately, GST's success should be judged not just on revenue collection but also on its ability to build taxpayer trust, preserve the fiscal independence of states, and safeguard household welfare. As India continues to implement this landmark reform, the key principle should be that GST is a dynamic institution, not a static framework to be finalised but one that is continuously improved—responsive to real-world conditions, guided by evidence, and committed to the principles of cooperative federalism that underpin it.

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