DEFINE RESEARCH JOURNAL
Online Open Access publishing platform for Multidisciplinary Research

Research Article **ISSN 3107 – 7927**

Goods and Services Tax in India: Issues, Challenges, and Implications for a Welfare Oriented Economy

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Abstract

In India, the implementation of the Goods and Services Tax (GST), effective from 1st July 2017, has led to the consolidation of various indirect taxes into a single taxation system with the objective of removing cascading taxation, enhancing compliance, revenue generation, and creating a common market in the country. This is possibly the biggest tax reform in independent India and has brought about a paradigm shift in the country's indirect taxation structure.

Though there have been notable success stories related to GST, some of the major challenges associated with the system include multiple tax slabs, ITC mismatch, compliance pressure on MSMEs, technical issues in GSTN, regulatory changes. Moreover, regressive nature of GST and lack of fiscal stability between the States are also relevant areas of discussion.

The research paper would adopt a descriptive and analytical approach using secondary data derived from government publications, GST council documents, GSTN analytics, Reserve Bank of India publications, and existing scholarly articles. Specifically, the paper will analyze GST revenue growth, compliance trends, impact on inflation, state level implications of GST, and compliance challenges encountered by SMEs under the system.

Keywords

GST, Indirect Taxation, Tax Compliance, SMEs, Welfare Economy, ITC, GSTN, Fiscal Federalism

1. Introduction

Taxation is a tool of public finance which helps in financing the development of infrastructure, social welfare schemes, health facilities, education, and economic development. Being a welfare economy, India needs to have a tax system which provides for adequate revenues and at the same time ensures fairness and efficiency in the economy.

Prior to the introduction of GST, there existed a complex indirect tax system in India including excise duty, service tax, VAT, CST, entry tax, and octroi collected separately by the central and state governments in India. The problem of multiple taxation, compliance, tax cascading, and restrictions on interstate trade were among the main disadvantages of this tax structure.

To overcome the aforementioned problems, the Government of India introduced Goods and Services Tax (GST) in India on 1st July, 2017. It is a destination based tax which applies to the supplies of goods and services. There are three forms of GST – CGST, SGST, and IGST.
It has greatly helped in tax administration and digitization of governance.

Nevertheless, various problems relating to the implementation remain persisting for both firms and customers. In case of SMEs, the cost of compliance is high, while the technology aspect poses problems. Likewise, price transmission remains a challenge in the case of consumers. States have also been concerned about fiscal autonomy and revenue sharing in such a taxation system.

This study highlights the challenges and implications of GST in the Indian economy and its effectiveness in a welfare perspective.

2. Review of Literature

GST being levied with different slabs increases complexity and compliance issues, according to Morris et al. (2018). As stated by Kumar (2015), exemptions and inverted duty schemes are causing cascade effects in the face of GST changes. Reduction in state fiscal freedom has been a concern raised by Rao (2010).

Sharma &Saini (2019) and Kumaraswamy (2020) note that SMEs experience a heavy cost burden arising out of complex filing and dependence on professionals. In relation to e-way bills and RCM, Lichchavi and Greeshma (2021) have indicated confusion.

In regards to technological challenges faced by GST, Sunitha and Madhav (2021) mention shortcomings, whereas Maniya&Shobha (2024) focus on tax evasion through fake invoices and ITC claims.

All in all, it can be concluded that GST has brought about greater transparency and efficiency in tax administration; however, it is surrounded by significant challenges.

3. Methodology of Research

The research follows a methodology that combines both the descriptive and analytical approach relying exclusively on the secondary sources of information. While the descriptive approach facilitates understanding of the functional framework and complexities of GST, the analytical one aids in understanding the economic and social implications of the same.

3.1 Sources of Data

Data for the analysis is obtained from:

- MoF Reports
- Publications/Notifications of GST Council
- GSTN Analytics Dashboard
- Reports of RBI & CAG
- Surveys conducted by MSME Ministry
- Academic Journals and Papers

3.2 Objectives of the Study

1. To examine structural and administrative issues in GST implementation.
2. To discuss socio-economic impacts of GST on business and consumers.
3. To measure the success of GST implementation based on financial analysis.
4. To point out key conclusions concerning GST implementation.
5. To recommend policy recommendations in the context of GST implementation.

4. Data Analysis

4.1 GST Revenue Growth and Collection Trends

Financial Year	Total GST Collection (₹ Lakh Crore)	Growth Rate (%)
2017–18	7.41	—
2018–19	11.77	58.8
2019–20	12.22	3.8
2020–21	11.37	-6.9
2021–22	14.83	30.4
2022–23	18.10	22.1
2023–24	20.14	11.3

Source: Ministry of Finance (2024)

There has been a marked rise in GST revenues from ₹7.41 lakh crore in 2017–18 to ₹20.14 lakh crore in 2023–24. The fall in 2020-21 is attributed to the economic downturn due to the COVID-19 virus outbreak. The subsequent rise is indicative of better compliance and economic growth.

4.2 GST Slab Structure

GST Rate	Nature of Goods
0%	Essential goods and healthcare
5%	Basic necessities
18%	Majority of goods and services
40%	Luxury and demerit goods

The GST system in India is based on a tiered system of taxation. This tiering is done to achieve a balance between generating revenue and meeting welfare needs. There is ambiguity due to various rates applicable under the system.

4.3 GST Compliance Trends

Financial Year	GSTR-3B Filing Rate (%)
2018–19	68.3
2019–20	72.6
2020–21	70.1
2021–22	79.5
2022–23	85.2
2023–24	88.4

Source: GSTN Analytics Dashboard

Compliance rates rose tremendously after GST because of better monitoring, electronic filing, and automation processes. Yet, late compliance issues still exist that adversely impact revenue effectiveness.

4.4 ITC Mismatch and Fraud Cases

Year	ITC Mismatch Rate (%)	Fraudulent ITC (₹ Crore)
2018–19	23.4	10,000
2019–20	25.3	15,700
2020–21	22.5	18,900
2021–22	22.2	22,400
2022–23	20.4	26,500
2023–24	18.5	33,100

Source: GSTN and CAG Reports

Mismatch cases relating to ITC still pose one of the biggest compliance problems in GST. Though percentages of ITC mismatches have fallen, the amount of fraud in such cases has grown substantially owing to invoicing frauds and shell corporation dealings.

4.5 Compliance Burden on SMEs

Compliance Issue	SMEs Reporting Difficulty (%)
Complex return filing	78
ITC reconciliation	71
Frequent rule changes	68
High professional costs	65
GSTN technical issues	61

Source: MSME Ministry Survey (2023)

Survey results indicate that SMEs are still struggling with issues of non-compliance with regard to GST. Administrative problems for small businesses arise owing to electronic filing processes, invoice matching, and reliance on tax professionals.

4.6 State-Wise Revenue Impact

State	Pre-GST Revenue (₹ Cr, 2016-17)	Post-GST Revenue (₹ Cr, 2022-23)	Change (%)	State Type	Compensation Received (₹ Cr)
Maharashtra	1,05,420	1,41,800	34.5%	Producer	24,630
Tamil Nadu	72,340	92,160	27.4%	Producer	19,820
Gujarat	68,210	89,470	31.2%	Producer	16,540
Karnataka	58,790	82,310	40.0%	Mixed	18,970
Uttar Pradesh	47,560	76,280	60.4%	Consumer	8,430
Bihar	12,840	24,610	91.7%	Consumer	9,290
Rajasthan	31,420	47,890	52.4%	Consumer	10,850
Himachal Pradesh	4,820	6,940	44.0%	Producer	5,780
Kerala	28,140	51,620	83.4%	Consumer	14,280

Source: Finance Commission Reports; State Budget Documents; GST Council Secretariat.

The GST has brought about changes in the center-state fiscal equation. States that are consumption-driven have seen relatively better growth in revenues compared to producer states, owing to the destination-based character of the GST.

4.7 Inflation and Price Transmission

Commodity Category	Pre-GST CPI Growth (%) (2015–17 Avg.)	Post-GST CPI Growth (%) (2018–20 Avg.)	Change (Percentage Points)	GST Rate Applied	Price Transmission Assessment
Packaged Food Items	4.2	3.1	-1.1	5–12%	Partial Transmission
Consumer Electronics	3.8	2.4	-1.4	18–28%	Good Transmission
Restaurant Services	4.6	5.9	+1.3	5% (without ITC)	Inflationary Impact
Healthcare Services	5.1	5.8	+0.7	0–12%	Mixed Impact
Textile & Apparel	3.3	2.9	-0.4	5–12%	Marginal Transmission
Construction Materials	5.6	6.2	+0.6	18–28%	Cost-Push Inflation
FMCG Products	3.9	2.8	-1.1	12–18%	Moderate Transmission
Petroleum Products	8.2	9.1	+0.9	Outside GST	No GST Benefit

Source: RBI Monetary Policy Reports; MOSPI CPI Data; NIPFP Working Papers.

There have been some inconsistent impacts on prices following the introduction of GST. Although some manufactured products have become cheaper because of the absence of cascading taxes, there has been an increase in inflation in industries like the restaurant industry and the construction industry.

5. Major Challenges in GST Implementation

5.1 Multiple Slabs of GST

The presence of various GST slabs causes problems in identifying the correct rate applicable for taxation. Businesses often find themselves involved in legal disputes over applicable rates.

5.2 Compliance Challenges for SMEs

SMEs find the process of filing returns and reconciling invoices to be highly challenging and cumbersome. Compliance expenses are higher due to reliance on tax experts.

5.3 Mismatch of Input Credits

Mismatch issues related to input credits occur because of delayed submission of invoices, erroneous filing procedures, and lack of compliance by suppliers.

5.4 GSTN Operational Problems

Despite advancements made in GSTN facilities, taxpayers continue to struggle with the problem of portal downtime and high filing traffic.

5.5 Changing Rules and Tax Rates

Businesses are often affected by frequent changes in rules and tax slabs under the GST framework.

5.6 Reverse Charge Mechanism (RCM)

Most taxpayers have been struggling to grasp and apply provisions related to the reverse charge mechanism (RCM).

5.7 Weakness in IT and Skill Base

Lack of proper IT facilities and inadequate training among professionals in the rural areas pose a challenge in implementing the GST system.

6. Socio-Economic Implications

6.1 Regressive Characteristic of GST

GST is a tax based on consumption, and hence its incidence is more on lower economic strata. Even though essential commodities are free of tax or taxed very minimally, there is still GST on numerous other consumables.

6.2 Effect on SMEs

GST has added to the already existing procedural burden and compliance cost on SMEs, discouraging business entities from operating within the ambit of the formal sector.

6.3 Inflationary Consequence

GST has caused an unequal pass-through of prices. Though the prices of certain commodities reduced due to GST, there was an upward rise in the prices of some services.

6.4 Federal Disputes

GST, being destination-based, has caused financial worries for states involved in manufacturing activities. Expiry of compensation formulas has added to Centre-state disputes.

7. Findings of the Study

Some of the notable findings made by this study concerning the implementation of GST in India include:

7.1 Improving Revenue Collection

Indirect tax collection has seen substantial improvement as a result of GST. Consistent rise in GST revenue suggests that the GST base is expanding.

7.2 Rise in Compliance Rate

Tax compliance rate has risen considerably due to the adoption of digital surveillance, e-invoicing, and automated returns filing mechanisms. Full compliance is still yet to be attained.

7.3 Existence of ITC Fraud Problem

ITC fraud problem continues to persist under the GST regime despite advances in technology in terms of monitoring systems.

7.4 Large Compliance Costs for SMEs

Small and medium enterprises have continued to struggle with tax return filing, ITC reconciliation, and policy changes.

7.5 Complication Arising from Different Tax Rates

Multiple rates in GST have caused confusion, misclassification, and litigations contrary to the simplicity intended by GST system.

7.6 Advancement of Technology but Challenges Remain

Great progress has been recorded in the implementation of GSTN. Portal downtime and backlog at filing time still persists.

7.7 Inconsistent Socio-Economic Effect

GST has led to inconsistent socio-economic results. Even though some sectors enjoyed reduced costs, poor sections have been experiencing higher costs of consumption taxes.

7.8 National and Fiscal Issues

Destination basis of GST has raised issues about revenue among manufacturing states; therefore, the need for cooperative federalism and fiscal federalism has risen.

8. Policy Recommendations

8.1 Streamlining GST Structure

There is a need to streamline GST rates into fewer categories to help make compliance easier.

8.2 Petrol Products under GST

Petroleum products can be included within GST structure gradually to avoid any cascade effect and increase the efficiency of logistics and transportation.

8.3 Reduction in Return Filing Hassle

Single auto-filled return form needs to be introduced for taxpayers to simplify the process.

8.4 GSTN Infrastructure Upgrade

Government needs to upgrade its GST portal to ensure that it does not go down when there is heavy traffic on the site.

8.5 Supporting SMEs through GST

Various measures need to be taken to facilitate smaller companies regarding GST including awareness programs and simplification in procedures.

8.6 Social Welfare Measures

Essential items and services must be kept outside the ambit of GST or be levied at low rates.

8.7 Strengthening of Cooperative Federalism

Cooperative federalism requires GST Council to be efficient and stable compensation mechanisms.

9. Conclusion

The GST has been a major economic reform in the taxation history of India. The reform has led to the integration of the indirect tax structure, transparency, efficient digital governance, and higher revenues.

However, the research reveals several factors that have posed a challenge to the effective implementation of the GST regime. The existence of multiple slabs, ITC disparities, compliance requirements for SMEs, technological problems, and constant changes in the policy make GST difficult to operate for taxpayers. Moreover, the problem of regressiveness and the question of states' revenues under GST pose welfare and federation problems.

In order to make the long-term goals of the GST effective, it should be made technologically more advanced, easier to implement, and fair to ensure revenues along with welfare. Such a balanced GST regime will help in sustaining the welfare economy of India.

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