



A Comprehensive Evaluation of India's Goods and Services Tax (GST) Regime: Structural Evolution, Sectoral Impacts, and the Transition to GST 2.0

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ABSTRACT

The Goods and Services Tax (GST) represents one of the most significant structural tax reforms in modern Indian history, aimed at transforming the country into a unified national market under the guiding philosophy of 'one nation, one tax, one market' (Deshmukh et al., 2022; M. V., 2020). Launched on July 1, 2017, via the 101st Constitutional Amendment, the dual-levy mechanism split tax administration between Central GST (CGST), State GST (SGST), and Integrated GST (IGST) (M. V., 2020). While the framework successfully minimized the cascading "tax on tax" effect, expanded the tax base, and improved cross-border logistical efficiencies, it simultaneously introduced compliance burdens, technological bottlenecks, and revenue shortages for state governments (M. V., 2020). This paper synthesizes empirical literature and data up to the landmark "GST 2.0" reforms, analyzing how recent rate rationalizations—particularly in the textile and essential wear sectors—have alleviated early distortions like the inverted duty structure while driving MSME profitability and consumer affordability (Mondal, n.d.; Venkatalakshmi, 2026).

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1. Introduction and Historical Trajectory

The historical trajectory of indirect tax reform in India spans multiple decades, moving from a highly fragmented system of independent central and state levies to a fully integrated digital tax network (Deshmukh et al., 2022; M. V., 2020).

The Evolution of Indian Taxation

- **1986:** Initial structural overhauls to the central excise system were proposed, planting the seeds for comprehensive value-added tax modeling (M. V., 2020).
- **2000–2004:** Official design committees and task forces formalized recommendations to replace legacy systems with a singular GST framework to elevate national economic efficiency (M. V., 2020).
- **2006–2014:** The reform was formally introduced into budget planning cycles, followed by prolonged legislative debates over constitutional frameworks and state revenue guarantees (M. V., 2020).
- **2015–2016:** The 122nd Constitution Amendment Bill was cleared by both houses of Parliament and subsequently ratified by state legislatures (M. V., 2020).
- **2017:** On midnight of June 30, the GST regime officially rolled out across India (M. V., 2020).
- **2025–2026:** The implementation of **GST 2.0** marked a major policy shift, introducing targeted rate adjustments and slab consolidations to boost the MSME ecosystem and consumer purchasing power (Mondal, n.d.; Venkatalakshmi, 2026).

2. Review of Literature

The theoretical and empirical groundings of a unified indirect tax system in India have been heavily scrutinized by economists and policy researchers.

Prior to its implementation, the Task Force on Goods and Services Tax (2009) emphasized that India's legacy tax structure caused severe misallocation of resources and hindered aggregate economic growth (M. V., 2020). This was driven primarily by un-creditable intermediate taxes that created a cascading "tax on tax" effect (M. V., 2020). Under the legacy system, a product manufactured in one state and sold to another accumulated non-setoffable layers of Central Excise, State VAT, and Central Sales Tax (CST), severely disrupting internal interstate supply logistics (M. V., 2020).



Following the 2017 implementation, early academic studies focused heavily on transitional bottlenecks. Shobha (2017) highlighted critical barriers in early GST return filings, observing that inefficient backend planning and constant postponement of due dates increased compliance workloads for tax practitioners by up to 50% (Ghosh, n.d.). Similarly, Kothari (2019) documented the technological challenges faced by small entrepreneurs interacting with the Goods and Services Tax Network (GSTN) portal (Ghosh, n.d.).

Global experiences compiled by Deshmukh et al. (2022) indicated that while destination-based VAT systems simplify tax administration in the long run, the short-run results vary heavily across different sectors of the same economy (Deshmukh et al., 2022; Kumar & Kumar, 2020). Recent literature evaluating the "GST 2.0" phase implemented in late 2025 shows a structural pivot. Venkatalakshmi (2026) evaluates how the shift from the original four-tier tax structure to a consolidated, rate-rationalized framework was designed to eliminate interpretational disputes, correct inverted duty structures, and lower the input tax burden for consumer goods and micro-enterprises (Venkatalakshmi, 2026).

3. Research Methodology

This study utilizes an **exploratory and analytical research design** to evaluate the structural transition from early GST (1.0) to the modernized GST 2.0 framework (Ghosh, n.d.; M. V., 2020).

Data Collection and Sources

The paper relies primarily on secondary data curated from institutional repositories, academic databases, and government reports (M. V., 2020). Key data sources include:

1. **Statistical Publications:** Data from the Ministry of Finance, Government of India, and official notifications from the Central Board of Indirect Taxes and Customs (CBIC) (M. V., 2020; Mukherjee, 2026).
2. **State-Level Fiscal Indicators:** Revenue collection reports and deficit tracking archives derived from individual state treasury dashboards and the GST Council (M. V., 2020).
3. **Macroeconomic Forecasts:** Consumption and manufacturing growth indices obtained from the National Statistical Office (NSO) and the Asian Development Bank (ADB) (Debate, 2026; India, 2026).

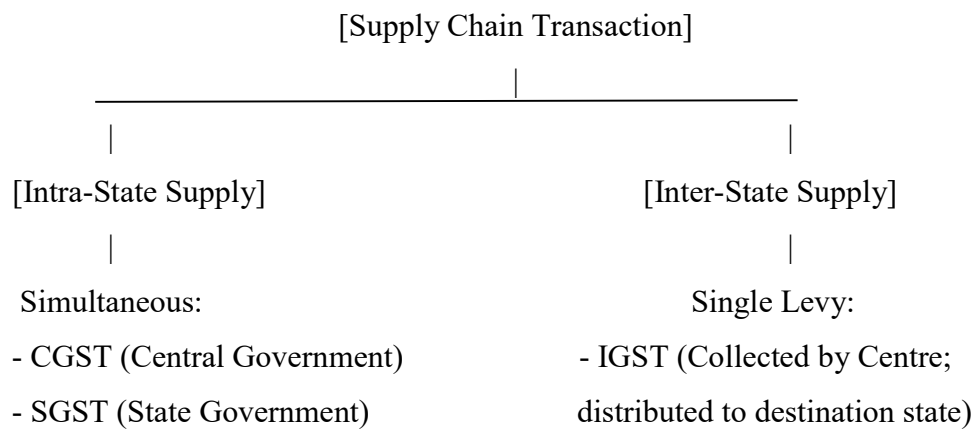
Data Analysis Framework



The research incorporates a comparative structure, evaluating operational tax attributes, macro revenue variations across select states, and longitudinal shifts in micro, small, and medium enterprise (MSME) profit dynamics (Mondal, n.d.; Venkatalakshmi, 2026). Empirical trend mapping is deployed to observe how the restructuring of rate slabs affects sectoral outcomes, with specific emphasis given to the textile value chain following the correction of the inverted duty structure (Mondal, n.d.; Venkatalakshmi, 2026).

4. Theoretical Framework and Working Mechanism

The core architecture of the Indian GST operates on a dual-control framework where the Centre and States concurrently levy taxes across a shared value chain (M. V., 2020).



Taxpayers track value addition chronologically, claiming credit for taxes paid on input supplies against their ultimate output tax liability via the **Input Tax Credit (ITC)** mechanism (M. V., 2020). Because output taxes are calculated strictly on destination-based consumption value, cross-utilization between CGST and SGST balances out perfectly across interstate channels via the IGST settlement pipeline (M. V., 2020).

5. Comparative Framework: Early GST vs. GST 2.0 Reforms

The structural design of tax slabs has undergone substantial adjustment between the 2017 rollout and the subsequent GST 2.0 framework (M. V., 2020; Venkatalakshmi, 2026).

Comparison of Slabs, Exemptions, and Targeted Revisions

Operational Attribute	Early GST Framework (2017–2024)	GST 2.0 Framework (Post-2025)
Primary Slabs	4 main slabs: 5%, 12%, 18%, 28%.	Rationalized into a core simplified system (5% and 18% as principal slabs).

Special Rates	0.25% on rough precious stones; 3% on gold.	Targeted adjustments to protect core artisanal crafts.
Demerit/Sin Levies	Up to 22% additional compensation cess on luxury and sin goods.	Consolidated higher tier (40% rate slab) explicitly targeting sin and luxury categories.
Exempted Segments	Crude petroleum, diesel, alcohol for human consumption, and electricity.	Preservation of standard structural exclusions; expanded cuts on essential items like health insurance.
Textile & Garment Slabs	Complex, variable rate brackets triggering structural tax distortions.	Flat 5% GST on manmade fibers, yarns, and garments priced up to ₹2,500 to correct structural issues.

6. Sectoral and Macroeconomic Impact Analysis

Industrial Sectors

- **Fast-Moving Consumer Goods (FMCG):** Distribution costs were reduced as regional storage depots were consolidated. Average tax incidence fell from a legacy 24% down to the 18% range, boosting corporate operating margins.
- **Automobile & Logistics:** Logistics integration minimized border crossing holdups, expanding long-haul fleet efficiency and reducing transit times (Mukherjee, 2026).
- **Technology & Service Sector:** Conversely, the service sector faced initial negative pressures as the standard tax rate climbed from a legacy 14–15% base up to a fixed 18% standard (M. V., 2020).

Impact of GST 2.0 on Textiles and MSMEs

Prior to the recent rate rationalizations, the textile ecosystem suffered from an **inverted duty structure**, where raw materials faced a higher tax rate than finished apparel, trapping credit assets inside un-refundable electronic ledgers (Mondal, n.d.).

[Pre-Correction: Inverted Structure] Raw Materials (Higher Tax) ----> Finished Apparel (Lower Tax)
[Credits Trapped]

[Post-Correction: GST 2.0 Unified] Raw Materials & Apparel up to ₹2,500 Unified at 5% GST [Liquidity Unlocked]



By unifying the value chain under a flat 5% slab for garments up to ₹2,500, small and medium enterprises experienced faster capital turnarounds (Mondal, n.d.). Longitudinal data documents a positive shift in MSME profit margins following these structural updates:

- **2023 MSME Average Profit Margin:** 8% (Mondal, n.d.)
- **2024 MSME Average Profit Margin:** 10% (Mondal, n.d.)
- **2025 MSME Average Profit Margin (Post-GST 2.0):** 14% (Mondal, n.d.)

Lower operational production costs have also strengthened global market integration, helping drive total Indian textile export values from ₹32,000 crores in 2023 up to ₹38,200 crores by the close of 2025 (Mondal, n.d.).

7. Structural and Compliance Challenges

Despite macroeconomic gains, structural vulnerabilities persist across multiple operational layers (M. V., 2020; Venkatalakshmi, 2026).

Technological Disparities and Compliance Inflation

The requirement for digital record-keeping via the GSTN portal has created friction for small-scale retail networks (M. V., 2020). The expansion of mandatory e-invoicing to lower turnover thresholds (e.g., ₹5 crore aggregate annual turnover) has brought a significantly larger number of businesses under strict compliance nets, raising administrative expenses for micro-enterprises due to professional accounting dependency (Prabha, 2026).

Macro Revenue Deficits and State Fiscal Imbalances

A key challenge centers on the gap between state revenue projections and actual collections. While the *GST (Compensation to States) Act, 2017* originally cushioned states, post-compensation revenue analysis highlights significant deficits across major state economies relative to their projected collection targets:

State Jurisdiction	Revenue Deficit Realized (Actual vs. Expected Collections)
Punjab	-49.55%
Uttarakhand	-42.38%
Kerala	-36.49%
Chhattisgarh	-34.41%

Gujarat	-30.23%
All-States Average	-26.18%

These gaps indicate that the early standard rate allocations were not entirely revenue-neutral, putting ongoing pressure on state budgets (Venkatalakshmi, 2026).

8. Strategic Recommendations

To resolve these remaining structural bottlenecks, the following targeted policy interventions are recommended:

1. **Resolve Inverted Tariff Configurations in Remaining Sectors:** Emulate the successful textile framework changes across other misaligned manufacturing industries to unlock trapped input credits and improve corporate cash flows (Mondal, n.d.).
2. **Deploy Free Government-Sponsored Compliance Tools:** Enhance the auto-population of data and provide micro-retailers with free, automated reconciliation platforms to reduce external accounting dependency (M. V., 2020; Prabha, 2026).
3. **Establish Permanent Digital Training Centers:** Launch accessible regional training initiatives to support digital accounting literacy for small traders, independent merchants, and traditional artisans (Ghosh, n.d.; Mondal, n.d.).
4. **Incorporate Missing Commodity Classes:** Gradually bring petroleum products, natural gas, and electricity into the unified tax network to eliminate broken credit chains across the broader industrial economy (M. V., 2020).

9. Conclusion

The introduction of the Goods and Services Tax completely reshaped India's fiscal landscape, removing complex internal trade barriers and creating an integrated national market (M. V., 2020). While structural challenges like state-level revenue deficits and acute digital compliance demands remain, the transition to GST 2.0 demonstrates that proactive policy fine-tuning can successfully minimize capital constraints, improve MSME liquidity, and lower consumer costs (Mondal, n.d.; Venkatalakshmi, 2026). Moving forward, the ultimate stability of the regime will depend on its ability to support its smallest business



stakeholders while maintaining predictable revenues across both central and state governments (M. V., 2020; Venkatalakshmi, 2026).

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