



India's GST Reform: Policy Perspectives

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Independence | Integrity | Impact

Outline

- The reform
- Expectations
- Reform outcomes, performance
- What worked, what didn't?
- Key lessons
- Way ahead

GST Reform:

Brief profile

- Integrated indirect tax for goods & services with input tax credit across India, July 2017. Nation-wide destination-based tax on final consumption to replace the cascading structure of domestic consumption taxes.
- From conception to actual : 1992/93-2017. Centre-states' agreement on design, constitutional amendment to integrate tax base, formation of the GST council (2016) & launch.
- Eventual design – 5 rates (0, 5, 12, 18, 28). Fully online. VAT system, Invoice-matching.
- Exclusions - petroleum products, electricity, & real estate from the base GST. Significant cascading element of past tax system remains, therefore.
- Revenue risk assumed by central govt. Legal guarantee of GST revenues - 14% pa (base 2015-16) to loss-proof states. Source: 5-year non-rebate compensation cess on sin/luxury goods.

India: GST inclusions and exclusions									
Included									
Centre					States				
Central Excise Duty					State VAT/Sales Tax				
Additional Excise Duties					Central Sales Tax				
Additional & Special additional customs duties					Purchase Tax				
Service Tax					Octroi and Entry Tax (all forms)				
Cesses and surcharges					Luxury tax (local bodies levy)				
					Entertainment Tax				
					Taxes on lotteries, betting, gambling				
					Taxes on advertisements				
					State cesses and surcharges				
Excluded									
Excise Duty on petroleum, tobacco products					CST on petroleum products				
					State Excise & VAT on potable alcohol				
					Entertainment Tax (for local bodies)				
					Duty on sale of electricity				
					Taxes on vehicles				

Note: Many cesses, surcharges abolished over time starting 2015-16 and continuing. Constitutional amendment does not address real estate, which would require another amendment for inclusion

What were the expectations?

- **Key reform objective:** Additional revenue mobilization with improved economic efficiency

Efficiency gains: Final product price, excl GST = 'true' input cost of production, better resource allocation. Unrestrained inter-state trade, lower costs, timings, burden.

(Chadha et al – 0.9-1.7% increase in GDP, 3.2-6.3% in exports, base 2008-09)

Revenue gains: Encourages compliance, widens base by aligning incentives, formalization. The set GST rates were revenue-neutral. However, increased revenue buoyancy was anticipated

["Our conservative estimate is that once it stabilizes, we should get another 1 to 1.5 percent of GDP extra revenue from the GST...we also expect this huge increase in trade within India,...like a kind of tariff cut in a sense...That should also add to trade and growth as well..." CEA Subramanian (2018)]

- **Experience** of predecessor state-level VAT - positive revenue impact at 5-yr lag with total state revenues 1-ppt higher in FY15 over pre-VAT FY05 (Rajaraman, 2019).

Seven years later: Reform outcomes, revenue performance

- Revenue estimates fluctuate. GST's revenue performance assessment varies depending on chosen data source until final audited accounts (2-years), lagged GDP revisions.

- Mukherjee (2023) for FY18-FY23

Gross GST/GDP reached pre-GST levels, 6.1% of GDP, in FY23.

Adjusted for compensation cess, annual average 0.48% of GDP,

GST revenues/GDP - 5.7%, well below pre-GST levels five years after reform

- Agarwal, et al (2024) for FY19-FY24 used actual refunds data (released Feb '24)

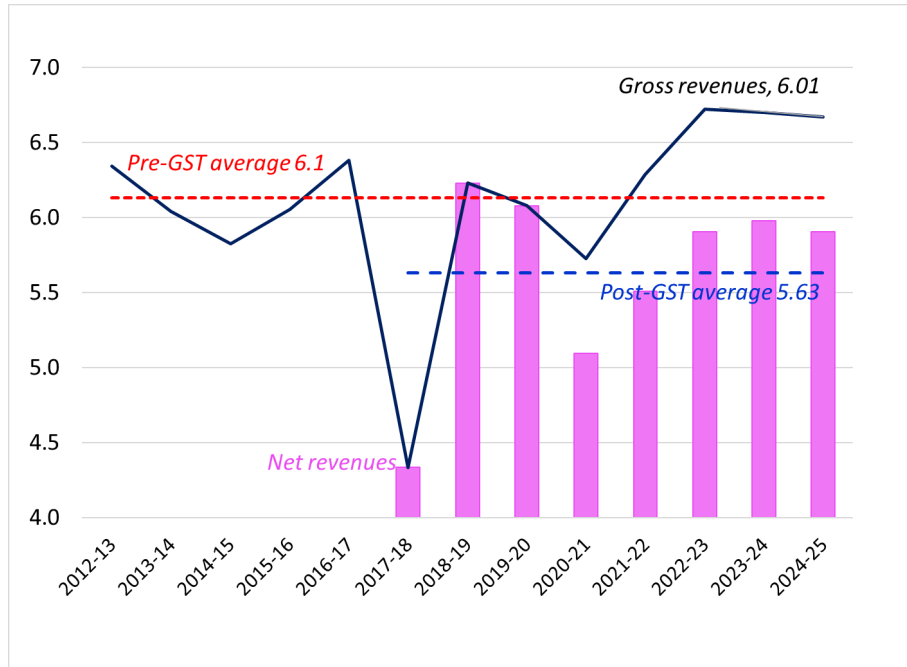
Revenue performance matched pre-GST 6.1% of GDP a year later (FY24)

- More recently though, GST revenue performance disappoints

Seven years after reform, revenues still lag pre-GST levels

India: GST revenue performance

in percent of GDP



5.63 vs 6.1% of GDP

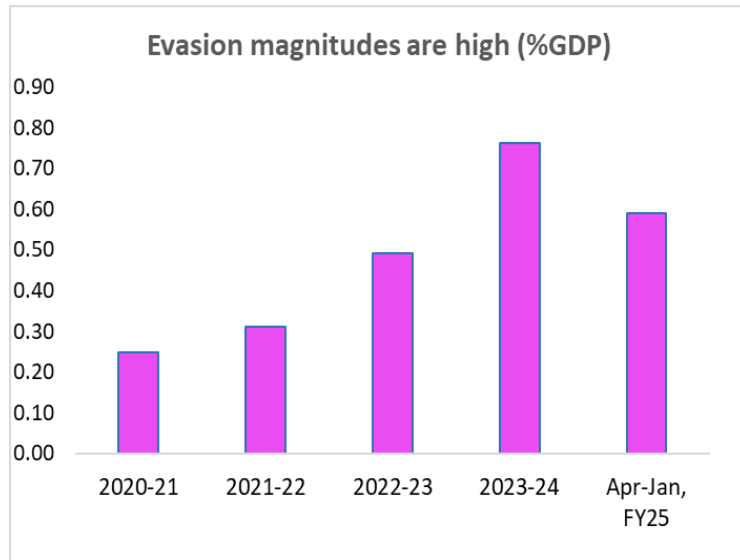
- Rebased to fresh GDP data – revenues depressed
- They'd be even lower if adjusted for compensation cess!
- Several influences: Rate reductions (2019); one-off factors (post-2020)

i. Pandemic: supply disruptions; uneven/non-linear recovery; demand rotation; temporary relief measures; commodity price shocks. *Linear tax base/revenue relationships can be disturbed by asymmetric price & volume effects.*

ii. Inflation: sustained, high, generalized, uneven relative price/sectoral shifts, nominal prices, Nominal GDP grew 14 & 12%, GST revenues grew 22.2 & 13.4. *Buoyancy non-neutral - Tax receipts, revenue composition can be impacted*

So we must wait some more

What worked, what didn't, what went wrong?

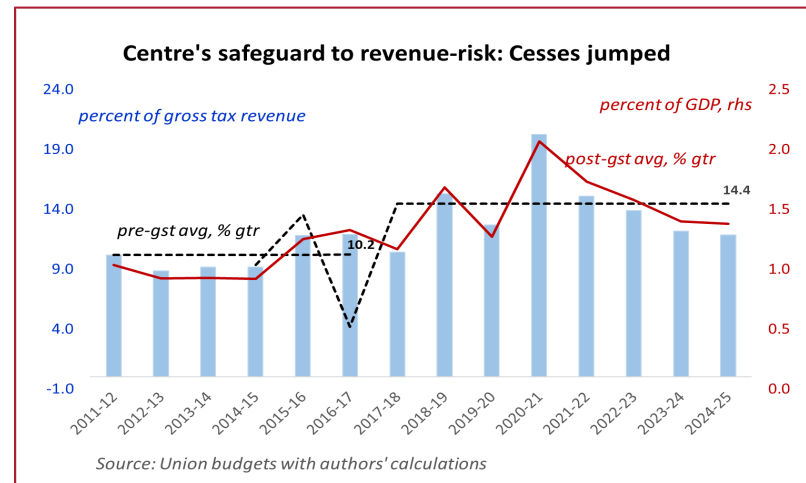


- **Positives:** agreement, cooperation, consultative process. Both its strength and weakness!
- Eliminated inter-state trade barriers, strong info tech infrastructure, away bills system
- **Design flaws:** Multiple & complex rate structure, high standard rate (18% vs 10.9 & 15.3% Asian & Global avg*), numerous exemptions, complex compliance mechanism. Policy gaps also from non-taxation (financial services, real estate).
- **Many problems, teething & fundamental:** *inter alia*, technical & other glitches arising from difficulties in comprehending structural intricacies. Tiered returns & filing procedures, order/invoice-matching, forward/backward-tracking, input credit refunds, etc.
- Overall, revenue underperformance created and uncovered **serious policy and compliance gaps**. E.g., fraudulent input tax credit claims, delayed and challenging refund settlements.
- Created GST-aversion, lowered compliance, business exits or understated turnover, substantial evasions.
- Led to continuous rate adjustments, reductions, alteration of turnover thresholds
- Promise of 14% nominal revenue growth - *blunder?*

Perverse fallout: Jump in central cesses, extended tenure of compensation cess

Who gained, who lost, how much? Centre-State revenues after reform (% GDP)				
	Mukherjee (2023)		Agarwal et al (2024)	
	Pre GST	Post GST	Pre GST	Post GST
	<i>FY13-FY17</i>	<i>FY19-FY23</i>	<i>FY13-FY17</i>	<i>FY18-FY24</i>
A. States' shares (excl comp cess)	3.0	2.6	na	na
Gain/loss	-0.4			
B. States' share (incl comp cess)	4.1	4.4	3.0	3.2
Gain/loss	0.23		0.20	
C. Centre's share	3.1	2.5	3.1	2.5
Gain/loss	-0.64		-0.60	
Total (A+C)	6.1	5.1	na	na
Gain/loss	-1.05			
Total (B+C)	7.2	6.8	6.1	5.7
Gain/loss	-0.41		-0.40	

Source: Mukherjee S. (2023) "Revenue Performance Assessment of Indian GST", NIPFP working paper 392, April; Agarwal et al (2024) "GST Revenue Performance: Gainers and Losers after Seven Years" E P W, VOL.



- Revenues underperformed, growth slowed.
- Rates lowered (2019). Pandemic
- Compensation cess incl covid-loans extended (Mar'26)
- Revenue disappointment, uneven burden-sharing
- Jump in union govt cess to offset revenue loss!
- Adverse real effects? Indirect taxes inherently regressive, additional impositions possibly resulted in excessive taxation, unlinked from economic cycle

What could have been done differently? Key lessons

- **Timing:** Preceded by demonetization (Nov 2016). During economic downturn.
 - Economy was already slowing: CSO lowered FY17 GDP growth estimate, May 2017.
 - June 2017: RBI flagged “...new data reveal...slowdown in activity in both industry and services set in as early as Q1 of 2016-17...became pronounced in Q4” (MPC resolution).
- **14% revenue growth guarantee to the states:**
 - Nominal GDP growth 5-yr annual avg (FY13-FY16) – 12%. States GSDP averaged 10.89-11.09%
 - Revenue-protection buoyancy range 1.262-1.286!
 - Gupta & Rajaraman (2020):
 - Aggregate state revenues (subsumed taxes) grew avg 7.59-7.67% annually (FY12-FY16), nearly half the revenue-protection growth!
 - TB averaged 0.685-0.704 (median 0.799-0.839), much lower
 - Only 5 states >14% revenue growth; most in 5-12% region
 - Conclude that “*There seems to have been no discussion in the public domain...how ...compensation rate of 14% was arrived at,...whether alternate scenarios and rates were considered. A more transparent and inclusive process involving all the stakeholders and domain experts would have resulted in savings...been more equitable...*” “*To the best of our knowledge, in no other federation at any point in time has a national government given a similar kind of guarantee*”

Conclusion

- Wide-ranging review essential to improve revenue performance – single lower rate, less complex, ease refund problems, administrative efficiency improvements, create more positive environment for taxpayers to stabilize the system.
- India's C-efficiency score falls short of its peers – 0.42 in FY23 < global average 0.45 (Modi, 2025). Therefore improvements in tax administration and more effective technology applications for enforcement are must to close the current policy and compliance gaps.
- Exclusions undermine both efficiency and compliance. E.g., petroleum products excise duties by the Centre & sales tax, motor vehicles, passenger and goods taxes and electricity duty levied by states estimated ~41% of total indirect taxes in FY23. Not zero rated in exports, so also undermines competitiveness as the cascading effect of transport is high, gets into all the cracks.
- Realization of above at both Centre-State levels and more effort to simplify the overall edifice, widen inclusion, move to a single rate is likely.
- In the long-run, a simpler and more comprehensive GST system could no doubt enhance productivity and public revenues.



Thank you