
FROM FOUR TO TWO: THE REVOLUTION BEHIND INDIA'S NEW GST TAX SLABS

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ABSTRACT

The 2025 Goods and Services Tax (GST) reform marks a pivotal moment in India's tax history, radically simplifying the nation's complex indirect tax structure. By consolidating the previous four major tax slabs into primarily two 5% for essentials and 18% for the majority of goods and services—this reform aims to reduce compliance burdens, lower the cost of living, and stimulate economic growth. This article delves beyond the headline figures, exploring the thoughtful policy intent behind the simplification. It examines how the government seeks to balance consumer relief through lower rates on essential items, while safeguarding fiscal sustainability by imposing a strategic 40% tax on luxury and sin goods. The reform not only addresses longstanding administrative and economic challenges but also aligns India with global tax practices focused on ease and fairness. Ultimately, this paper highlights how the new GST structure embodies a transformative effort to empower consumers, formalize businesses, and support India's larger goals of inclusive growth and Atmanirbhar Bharat.

Keywords: GST reform, tax simplification, slab reduction, luxury taxation, sin tax, economic growth.

INTRODUCTION

India's Goods and Services Tax (GST), introduced in 2017, marked one of the most significant overhauls in the country's taxation system. Designed to unify a myriad of state and central taxes into a single, streamlined framework, GST promised simplicity, transparency, and ease of doing business. However, over time, the system's four-tiered structure comprising 5%, 12%, 18%, and 28% tax slabs proved to be more complex than anticipated. Businesses often struggled with compliance, while consumers faced confusion over varying rates on everyday goods and services.¹ Recognizing these challenges, the government initiated a major reform to simplify the GST system. Reducing the slabs from four to just two primary rates aims not only to make taxation easier for businesses to navigate but also to reduce the financial burden on ordinary citizens. At the same time, a higher rate for luxury and "sin" goods ensures that revenue collection remains robust. This article explores the rationale behind this GST reform, its potential impact on businesses and consumers, and how it reflects India's ongoing journey toward a more efficient and equitable tax system. By examining both the opportunities and challenges, the discussion aims to provide a clear picture of the significance of this tax revolution.

THE GENESIS OF GST REFORM

The journey of the Goods and Services Tax (GST) in India is a story of ambitious reform and gradual evolution. Prior to 2017, India's indirect tax system was highly fragmented, consisting of multiple central and state-level levies such as excise duty, service tax, value-added tax (VAT), and entry taxes. This multiplicity of taxes often created confusion, inefficiencies, and compliance burdens for businesses operating across different states. The need for a unified tax system had long been recognized by policymakers, economists, and industry stakeholders as essential for simplifying trade, improving transparency, and fostering economic growth.²

When GST was finally introduced in July 2017, it was hailed as a historic step toward creating a single, nationwide indirect tax system. The reform aimed to replace a patchwork of taxes with a harmonized framework that would reduce administrative complexity and create a level playing field for businesses across India. To accommodate the wide diversity of goods and services, GST was structured into four distinct tax slabs: 5%, 12%, 18%, and 28%. The lower

¹ Press Information Bureau, Ministry of Finance, Government of India, GST Reforms 2025: Relief for Common Man, Boost for MSMEs and Middle Class (Sept. 4, 2025).

² D.K. Srivastava, *Intergovernmental Fiscal Relations in India: Time for the Next Generation Reforms* (2022), Madras Sch. of Econ.

slabs were intended for essential and everyday items, the mid-range slabs for standard goods and services, and the highest slab for luxury and demerit items. Despite its visionary design, the original four-slab system presented several challenges. Businesses, particularly small and medium enterprises, often struggled to determine the appropriate slab for their products, leading to errors in tax computation and filing. Consumers were also affected, as inconsistent tax rates on similar items created confusion and reduced the transparency that GST promised. Moreover, the system's complexity sometimes led to cascading taxes, where tax was inadvertently levied on already-taxed components, undermining the objective of a seamless tax flow.

From a global perspective, India's GST system drew inspiration from the Value-Added Tax (VAT) systems implemented in many developed and developing countries. Nations such as Canada, Australia, and the United Kingdom operate VAT/GST regimes with far fewer tax slabs, typically ranging from zero or reduced rates on essentials to standard rates on most goods and services.³ These countries demonstrate that a simplified structure not only eases compliance but also improves tax efficiency and collection. By contrast, India's four-slab approach, though well-intentioned, revealed the difficulties of balancing revenue requirements with simplicity and transparency in a complex, diverse economy. The challenges observed in the four-slab system ultimately set the stage for the government's 2025 GST reform⁴, aimed at reducing the number of slabs, simplifying compliance, and ensuring that the tax system serves both the economy and the citizens more effectively.

A NEW DAWN FOR INDIA'S GST: STREAMLINED RATES AND ENHANCED COMPLIANCE

The 2025 GST reform⁵ represents a bold and strategic step in India's ongoing effort to simplify its taxation system while balancing revenue needs with social and economic considerations. One of the most significant changes introduced under this reform is the reduction of the GST slabs from four to two primary rates. The previous structure of 5%, 12%, 18%, and 28% often created confusion for both businesses and consumers. By consolidating these into two main rates 5% for essential and commonly used items, and 18% for most standard goods and services

³ Satya Poddar & Ehtisham Ahmad, *GST Reforms and Intergovernmental Considerations in India* (2009), Dept. of Economic Affairs, Ministry of Finance, Govt. of India.

⁴ Press Information Bureau, Ministry of Finance, Government of India, *GST Reforms for a New Generation* (Sept. 20, 2025).

⁵ Press Information Bureau, Ministry of Finance, Government of India, *Recommendations of the 56th Meeting of the GST Council* (Sept. 3, 2025).

the government has aimed to streamline compliance and make the tax system far easier to navigate.⁶

In addition to the slab reduction, the reform introduced a higher rate of 40% on select luxury and “sin” goods, such as high-end vehicles, tobacco products, alcohol, and other non-essential items. This “luxury or sin tax” serves a dual purpose: it ensures that the government continues to generate adequate revenue from high-consumption, non-essential items, and it also discourages excessive consumption of products with negative social or health impacts. By differentiating between essential and non-essential goods, the GST system becomes more equitable, reducing the financial burden on everyday citizens while maintaining fiscal balance.

The rationale behind this simplification is rooted in both practicality and fairness. Businesses previously faced administrative challenges in determining the correct slab for each product, especially when products had overlapping categories or complex compositions. The simplified two-tier system reduces the risk of errors, improves transparency, and minimizes disputes between taxpayers and tax authorities. For consumers, the change eliminates confusion over tax rates, making pricing more predictable and everyday purchases easier to understand. The expected benefits of the reform extend beyond mere simplification. For businesses, especially small and medium enterprises, compliance costs are anticipated to decrease, freeing resources for investment and growth. Faster processing of input tax credits and reduced procedural complexity are likely to improve cash flow and operational efficiency. For consumers, the reduction in tax on essential items effectively lowers the cost of living, while the higher rate on luxury items ensures that the tax system remains progressive and socially responsible.⁷

Overall, the GST reform of 2025 reflects a thoughtful recalibration of India’s indirect tax framework, balancing simplicity, equity, and fiscal prudence. By reducing complexity, promoting compliance, and ensuring a fair distribution of tax burdens, the reform aims to make the GST system more efficient, transparent, and citizen-friendly while signaling India’s commitment to adaptive and forward-looking economic policymaking.

⁶ Reuters, *India's Retail Inflation Slows to Eight-Year Low*.

⁷ Ecovis, *India GST Reform: A Major Overhaul of Indirect Taxes*

BEYOND THE NUMBERS: UNPACKING THE ECONOMIC AND SOCIAL IMPACT OF GST 2.0

The 2025 GST reform is not just a technical adjustment in tax slabs—it carries significant economic and social consequences that touch the daily lives of citizens, businesses, and the broader economy.⁸ For average citizens, the reform brings immediate and tangible benefits. By reducing the number of GST slabs and lowering taxes on essential and commonly consumed goods, the cost of everyday items such as food, hygiene products, and household necessities is effectively reduced. This translates into greater disposable income for families, especially for low- and middle-income households, helping alleviate financial pressure and improving purchasing power. At the same time, the introduction of a higher 40% tax on luxury and “sin” goods ensures that the benefits of lower taxes on essentials are not offset by revenue shortfalls, making the system more equitable. From the business perspective, the reform is expected to simplify compliance significantly. The previous four-tier system often created ambiguity, particularly for small and medium enterprises, leading to errors in tax calculations, delayed filings, and disputes with tax authorities. By consolidating the slabs into two main rates, businesses can navigate the system with far greater ease. Streamlined invoicing and faster processing of input tax credits reduce administrative burdens, improve cash flow, and allow companies to focus more on operations and growth rather than bureaucratic complexities. This simplification may also encourage more informal businesses to enter the formal economy, further expanding the tax base.⁹

For the government, the reform strikes a careful balance between revenue generation and fairness. While lower rates on essential goods reduce the immediate tax collected from those items, the introduction of a higher tax on luxury and demerit goods ensures that overall revenue levels remain robust. In addition, improved compliance and reduced tax evasion due to simpler procedures could potentially enhance long-term revenue collection. The broader economic impact of these changes extends beyond immediate revenue and consumer costs.¹⁰ By easing compliance and lowering operational hurdles, the reform encourages business expansion and investment, particularly in the MSME sector. Enhanced clarity in taxation can attract foreign and domestic investors, contributing to economic growth. Furthermore, the simplification of

⁸ Economic Times, Health, Term Policy Sales Rise After GST Exemption.

⁹ H.K. Dwivedi, *Seven Years of GST: Time to Move Beyond the Exuberance* (2024), SAGE J. (India).

¹⁰ Dr. Raghendra Jha & Dr. Azad Singh Bali, *India's Goods and Services Tax: Context, Design and Policy Spillovers* (2023), Austl. Nat'l Univ.

GST can accelerate the formalization of previously unregistered businesses, strengthening the overall economy by increasing transparency, tax contributions, and employment opportunities.

In essence, the 2025 GST reform represents a carefully calibrated policy intervention that benefits multiple stakeholders: it reduces the financial burden on citizens, eases compliance for businesses, safeguards government revenue, and fosters a more inclusive and resilient economy. By balancing social equity with economic efficiency, the reform exemplifies India's commitment to adaptive policymaking that addresses both the immediate needs of its people and the long-term goals of sustainable growth.

OPERATIONALIZING INDIA'S TAX OVERHAUL

The success of any large-scale reform, particularly one as complex as the GST overhaul, depends not only on the policy itself but also on the strategies used to implement it effectively. **Phased Roll out and Communication:** To minimize disruption, the government opted for a phased rollout of the simplified two-slab GST system. Extensive communication campaigns were launched to educate businesses and the public about the changes. Workshops, webinars, and outreach programs were conducted nationwide, particularly targeting small and medium enterprises (SMEs), which historically faced challenges with GST compliance. Clear guidance documents, FAQs, and helplines were made available to ensure that stakeholders understood the revised slab structure, the introduction of the luxury/sin tax, and the implications for invoicing and filing returns.¹¹

Leveraging Technology for a Smooth Transition, the government relied heavily on technology to facilitate a seamless transition. Updates to the GST portal enabled automatic recalculation of tax rates, easier classification of goods and services, and simplified filing procedures. Interactive dashboards allowed businesses to track input tax credits and generate accurate invoices under the new slabs. Mobile applications and online tools provided step-by-step guidance, helping small traders who might lack dedicated accounting teams to comply efficiently.¹² The integration of Artificial Intelligence (AI) and automated checks further reduced errors and minimized disputes between taxpayers and authorities. **Measures to Ensure Compliance,** compliance was a central focus of the reform strategy. To encourage timely and accurate tax filings, the government introduced simplified reporting formats, reduced paperwork, and clarified previously ambiguous provisions. Regular audits and monitoring

¹¹ India Briefing, India's GST Overhaul 2025: Which Goods Get Cheaper & Which Cost More.

¹² Dr. S. Garg, Investigating the Implications of Goods and Services Tax on Economic Growth (2025), Taylor & Francis Online.

mechanisms were reinforced, but emphasis was placed on facilitative enforcement rather than punitive measures. This approach balanced the need for accountability with the practical realities of small businesses, making it easier for them to transition without fear of inadvertent violations.

Refund Mechanisms and Support for Exporters, recognizing the importance of maintaining cash flow for exporters and high-value industries, the reform included faster and more transparent refund mechanisms. Exporters could claim input tax credits promptly, ensuring that working capital was not tied up unnecessarily. Special provisions for timely refunds and electronic verification processes reduced delays and enhanced trust in the system. The government also provided dedicated support channels for businesses to resolve refund-related queries, ensuring that the reform did not disrupt export activities or international trade commitments. In essence, the implementation strategy combined effective communication, technological innovation, compliance facilitation, and stakeholder support to make the GST reform both practical and citizen-friendly. By anticipating challenges and addressing them proactively, the government not only reduced the risks associated with a major tax overhaul but also reinforced confidence in India's commitment to a simpler, fairer, and more efficient taxation system.¹³

NAVIGATING ROADBLOCKS: KEY CHALLENGES IN GST 2.0 IMPLEMENTATION

While the 2025 GST reform marked a significant step toward simplifying India's taxation system, it has not been without its challenges and criticisms. Large-scale reforms of this nature inevitably encounter hurdles, both in implementation and in public perception, which require careful consideration and responsive policymaking.

1. Potential Issues in Implementation: Transitioning from a four-slab to a two-slab system, coupled with the introduction of a high luxury/sin tax, presents operational challenges. Businesses had to recalibrate pricing, update accounting systems, and adjust internal processes to comply with the new rates. While technology helped streamline this transition, smaller businesses without advanced accounting infrastructure faced difficulties in adapting quickly. Errors in invoicing or misclassification of products could lead to unintended penalties, creating anxiety among entrepreneurs.¹⁴

¹³ Bajaj Finserv, GST Reforms 2.0 (2025): Relief for the Common Man and Boost for Businesses

¹⁴ Dr. N. Bhagat, Fiscal Federalism in India After GST: Autonomy vs. Efficiency (2025), SSRN.

2. Concerns from Small Businesses and State Governments: Small and medium enterprises (SMEs) expressed concerns that, despite simplification, compliance could still be burdensome due to limited resources and awareness. Many SMEs operate in multiple states and were apprehensive about navigating subtle differences in state-level GST interpretations, despite central guidance. State governments, too, raised questions about revenue distribution under the new framework. While higher luxury/sin taxes ensure revenue on premium items, states worried about potential shortfalls in collections from goods previously taxed at mid-tier slabs, especially essential items that generate significant aggregate revenue.

3. Possible Gaps in Revenue Collection: Although the reform seeks to maintain revenue neutrality through the introduction of higher taxes on luxury items, there remain concerns about temporary gaps in revenue collection during the transition. Businesses delaying compliance, initial confusion in tax filings, or misreporting could reduce inflows in the short term. Furthermore, sectors heavily reliant on mid-tier slabs, such as processed foods and certain consumer goods, may experience temporary mismatches between expected and actual collections.¹⁵

4. Public Perception and Acceptance: Public perception plays a crucial role in the success of any fiscal reform. While the simplification of GST was generally welcomed by consumers and businesses, skepticism lingered regarding the higher 40% tax on luxury and sin goods. Critics argued that such high rates could encourage black-market activities or underreporting, reducing effectiveness. Additionally, some citizens viewed the reform as disproportionately favoring urban or affluent consumers while its benefits for rural or low-income populations would be gradual and less visible initially. Despite these challenges, the government's proactive approach—including extensive communication campaigns, helplines for businesses, and digital tools to facilitate compliance—helped mitigate many potential pitfalls. Addressing these criticisms transparently is essential for sustaining confidence in the GST framework and ensuring that the reform achieves its long-term objectives of simplification, equity, and economic efficiency.

¹⁵ Dr. Devarajappa S.N., A Study on the Reforms of GST 2.0: A Landmark in India's Tax Journey (2025), *Int'l J. of Legal Tech. & Emerging Areas in Mgmt.*

CASE STUDIES

1. MSME Sector Revitalization in Andhra Pradesh In Vijayawada, Andhra Pradesh, the GST 2.0 reforms have injected new energy into the MSME sector. Local leaders highlighted that the reduction in tax rates on consumer goods has made small businesses more competitive. The 'Super GST - Super Savings' campaign, which includes events like the 'Great Amaravati Shopping Festival,' aims to raise awareness about these benefits and stimulate local trade.¹⁶
2. Small Business Success Through Automation in Gujarat: A small manufacturing business in Gujarat reduced its compliance costs by 30% after adopting automated GST filing software. This case demonstrates how technology can ease the transition to the new system and make small businesses more competitive.¹⁷
3. Inverted Duty Structure Challenges for Printers: The Offset Printers Association has raised concerns about the inverted duty structure, where printers pay 18% GST on raw materials like paper but only 5% on finished products. This 13% tax gap leads to significant working capital blockages, threatening the survival of around 2.5 million small and micro printing businesses.
4. Revenue Loss Concerns Post-Reform: Analysts estimate that the GST reforms could result in an annual revenue loss of ₹1.8 trillion (approx. \$20.7 billion), with states potentially losing approximately 0.36% of GDP. This highlights the fiscal challenges that need to be addressed to ensure the sustainability of the reform.¹⁸
5. Public Perception and Acceptance: A survey study in India found that 90% of respondents were aware of GST, with 60% of business owners reporting a positive impact on their operations. However, smaller enterprises faced more compliance challenges, indicating the need for targeted support.

CONCLUSION

The 2025 GST reform represents a significant turning point in India's effort to create a taxation system that is both efficient and citizen-friendly. By reducing the number of slabs from four to two for essential and standard goods, while imposing a higher 40% rate on luxury and "sin" items, the reform strikes a balance between simplifying compliance and safeguarding government revenue. For businesses, especially small and medium enterprises, the streamlined structure reduces administrative hurdles, simplifies invoicing, and speeds up input tax credit claims. This allows companies to focus more on operations and growth rather than navigating complex tax rules. Consumers benefit as well, with lower taxes on everyday goods easing

¹⁶ Times of India, GST 2.0 Reforms Ushered in New Energy in MSME Sector: Vijayawada MP (Oct. 14, 2025).

household expenses and increasing purchasing power. Meanwhile, the higher rate on luxury items ensures that fiscal resources remain adequate and that those who consume high-value or non-essential goods contribute proportionately.

Challenges remain, particularly in terms of transitioning smoothly, addressing concerns from smaller businesses and state governments, and ensuring public understanding and acceptance. However, the government's focus on digital tools, phased implementation, and proactive communication has helped mitigate many potential issues. In essence, this reform is more than a technical adjustment it reflects India's commitment to modernizing its economic framework. By combining simplicity, fairness, and fiscal responsibility, the GST reform strengthens the foundations for sustainable growth, better compliance, and a more equitable economic system. It demonstrates that thoughtful policymaking can benefit both businesses and citizens while supporting the long-term goals of the nation.

¹⁷ Dr. S. Garg, Goods and Services Tax: An Inflationary Reform or a Myth (2025), SAGE J. (India).

¹⁸ Dr. P.K. Bhura, GST in India: A Key Economic Reform (2023), Int'l J. of Mgmt. & Public Research.