



The Comprehensive Evolution of India's Indirect Taxation: A Strategic Analysis of GST 2.0 and the 2026 Economic Landscape

Dr.N.Sumathi*

Assistant Professor, Department of commerce PA, Nallamuthu Gounder Mahalingam College, Pollachi

*Correspondence : sumathimurugavel@gmail.com

To Cite this Article

The Comprehensive Evolution of India's Indirect Taxation: A Strategic Analysis of GST 2.0 and the 2026 Economic Landscape. (2026). Academic Research Journal of Science and Technology (ARJST), 3(04), 1-6. <https://doi.org/10.63300/arjst.2026.v3.i4.01>.

Article Info

Received on 01-Jan-2026,

Revised on 22-Jan-2026,

Accepted on 27-Jan-2026.

ABSTRACT

The Goods and Services Tax (GST) 2.0 framework, initiated following the 56th GST Council meeting in September 2025, represents the next phase of India's fiscal reform, focusing on structural optimization, revenue buoyancy, and technological integration. By consolidating rate slabs into a streamlined 5%, 18%, and 40% structure, the reform has significantly reduced administrative friction and improved affordability across key sectors such as automotive and infrastructure. As of February 2026, gross GST collections reached a record ₹22.08 lakh crore for FY 2024-25, indicating robust economic formalization. This paper examines the sectoral shifts, macroeconomic outcomes—including a projected 35 basis point reduction in retail inflation—and the technological leap toward AI-powered "Agentic Automation". Furthermore, it addresses the formal sunset of the compensation cess on February 1, 2026, and the resulting challenges for MSME compliance and cooperative federalism.

KEYWORDS: GST 2.0, Indirect taxation reform, Fiscal federalism, Tax rationalization, Input tax credit (ITC), Compliance burden, AI automation.

Copyright © 2025 Academic Research Journal of Science and Technology (ARJST) All rights reserved.

1. Introduction

The structural maturation of India's indirect tax regime, professionally designated as GST 2.0, represents a pivotal transition from the foundational unification of 2017 to a highly optimized, technology-driven fiscal architecture designed for a five-trillion-dollar economy. As of February 2026, the reform has transcended its initial objectives of simple tax subsumption to address deep-seated inefficiencies in resource allocation, compliance equity, and revenue buoyancy. By consolidating the previously fragmented four-tier slab system into a streamlined structure and integrating advanced intelligence layers, GST 2.0 seeks to harmonize India's tax environment with international best practices while navigating the complexities of cooperative federalism.

2. The Structural Genesis and Architecture of GST 2.0

The transition to GST 2.0 was formally codified following the landmark 56th GST Council meeting in September 2025, which introduced a comprehensive rate rationalization program effective from September 22, 2025. This overhaul was necessitated by persistent administrative friction and an "inverted duty structure" that previously penalized domestic manufacturing.

2.1. The Reconfigured Rate Slabs

The architectural centerpiece of GST 2.0 is the reduction of primary tax slabs from four to three: a merit rate of 5%, a standard rate of 18%, and a demerit rate of 40%. This consolidation involved moving approximately 99% of items previously taxed at 12% down to the 5% slab, while roughly 90% of items in the 28% category were lowered to the 18% standard rate.

GST Tier	Rate	Categorization and Key Goods/Services
Exempt / Nil	0%	Milk, Indian breads (roti, khakhra), life-saving drugs, and health/life insurance premiums.
Merit Rate	5%	Packaged food, dairy (butter, ghee, cheese), baby care items, and agricultural machinery.
Standard Rate	18%	Consumer durables (ACs, TVs), small cars, and mass-market motorcycles.
Demerit Rate	40%	Luxury SUVs, yachts, private aircraft, and specified "sin" goods like tobacco.

2.2. Legislative and Procedural Refinements

Beyond rate changes, GST 2.0 introduced critical amendments to the Central Goods and Services Tax (CGST) Act via Union Budget 2026-27. Amendments to Sections 15 and 34 have eliminated the requirement for a pre-existing agreement to claim benefits on post-sale discounts. Furthermore, the amendment to Section 13 of the IGST Act removed the special rule for "intermediary services," aligning the "place of supply" with the location of the recipient, which has significantly improved the clarity of export benefits for India's IT sector.

3. Sectoral Insights and Performance Dynamics

The granularity of GST 2.0 reveals a diverse impact profile, recalibrating incentives across primary industries.

3.1. Automotive and Sustainable Mobility

The automotive industry has been a primary beneficiary. The reduction of GST on small cars and motorcycles below 350cc from 28% to 18% lowered the cost of ownership significantly. The industry reported record January sales in 2026, with passenger vehicle dispatches reaching 4,49,616 units, a 12.6% increase over January 2025. However, the electric vehicle (EV) segment continues to grapple with an inverted duty structure where inputs are taxed at 18% while

finished EVs attract 5%.

3.2. Infrastructure and Real Estate Affordability

Real estate has leveraged the rationalization of materials like cement (reduced from 28% to 18%) to stimulate demand. Construction costs are expected to decline in the range of 2.5% to 4.4%, translating into savings of approximately ₹1,000 per square meter. Under-construction flats continue to attract 1% GST for affordable housing and 5% for non-affordable housing.

3.3. Agriculture, Food Processing, and the "Efficiency Tax"

A merit rate of 5% now covers a wide range of processed essentials, intended to reduce post-harvest wastage. A challenge persists in the "taxation of efficiency": while unprocessed produce is zero-rated, basic value-addition (washing, grading, cutting) triggers a 5% GST. This creates a disincentive for small-scale farmgate processing compared to large agribusinesses that can claim Input Tax Credits (ITC) efficiently.

3.4. Digital Economy and Cloud Computing

Budget 2026-27 introduced a tax holiday until 2047 for foreign cloud service providers operating through India-based data centers. In the OIDAR (Online Information and Database Access or Retrieval) regime, compliance has tightened for foreign providers, with data analytics now linking GST compliance more closely to platform data.

4. Macroeconomic Implications and Fiscal Health

4.1. Revenue Buoyancy and Economic Formalization

In FY 2024-25, gross collections reached a record ₹22.08 lakh crore, a 9.4% growth reflecting increasing formalization. The number of registered taxpayers has grown from 6 million at the start of GST to over 15.1 million by April 2025. Empirical evidence suggests a 1% growth in GST revenue correlates with a 0.56% growth in national GDP.

4.2. Disinflationary Impact and Consumption Stimulus

SBI Research projected that GST 2.0 reforms could reduce retail inflation by up to 35 basis points (bps) in FY 2025-26. By February 2026, the headline CPI inflation was recorded at 2.75% under a new series reflecting updated consumption weights. This "consumption dividend" increased household disposable income by an estimated ₹5.31 lakh crore.

5. Technology and Compliance: The Digital Frontier of 2026

5.1. AI and Agentic Automation in Tax Filing

By 2026, the ecosystem transitioned to "Agentic Automation". Platforms like *Clear* and *hisabkitab* offer autonomous

agents for data validation, transaction auditing, and real-time reconciliation. AI-driven OCR has reduced the manual accounting workload by 60-70%.

5.2. Blockchain and Supply Chain Integrity

Blockchain technology is addressing the "Trilemma" of speed, cost, and trust. "Provenanced AI" ensures every tax credit can be traced to verified, immutable data. Administrative costs have been reduced by up to 30% through blockchain-based instruments.

5.3. API-First Compliance and Real-Time Reporting

India's API-first digital economy has made real-time reporting a prerequisite for scalability. Data from ERP systems flows automatically to e-invoice IRP APIs and GSTN platforms, ensuring mismatches are identified at the source.

6. Fiscal Federalism and the Compensation Cess Milestone

6.1. The Sunset of the Transition Period

The formal discontinuation of the GST compensation cess became effective on February 1, 2026. The government met its ₹2.69 lakh crore loan repayment obligations ahead of schedule. The cess has been replaced by a combination of the 40% GST slab and enhanced Central Excise duties on sin goods.

6.2. State Finances and the "Risk-Sharing" Shift

FY 2026 is the first year states are managing GST volatility without a compensation framework. While Punjab saw a 21.5% increase in net collections, Kerala reported a revenue loss of ₹8,000 crore due to rate rationalization.

7. Challenges and Implementation Gaps

7.1. The MSME Compliance Trap

Small businesses spend an average of 28.6 hours per month on GST activities. Digital unreadiness remains a hurdle, with over half of MSMEs relying on mobile hotspots for operations.

7.2. Inverted Duty Structures and Working Capital

The inverted duty structure in segments like EVs continues to block working capital. Although a 90% provisional refund system was approved, many firms still have significant capital blocked in unutilized credits.

7.3. Ethical Governance and Privacy Risk

The FICCI-EY Risk Survey 2026 highlights that 64.5% of enterprises cite data governance and security as "very severe" risks. Under the DPDP Act 2023, penalties for data breaches can reach \$30 million (₹250 crore).

8. Future Outlook: The Path to 2030

8.1. Toward a "Force Multiplier" Economy

Budget 2026-27 designates AI as a "force multiplier," funding the IndiaAI Mission with over ₹10,000 crore. The goal is "Atmanirbhar Intelligence," anchored in domestic data and infrastructure.

8.2. Harmonization and "Viksit Bharat"

The endgame is complete harmonization, potentially including petroleum and alcohol in the GST net to eliminate cascading taxes.

9. Conclusion

The analysis of the GST 2.0 reform reveals a system that has transitioned from infancy to operational maturity. Record revenues and reduced inflation demonstrate its macroeconomic success, yet the compliance burden on MSMEs and the end of the compensation cess highlight the need for continued administrative empathy and federal coordination. The transition to AI and blockchain confirms that digital infrastructure is now the organizing principle of the Indian tax system, steering the nation toward its 2047 economic vision.

10. References

1. Alvarez & Marsal. (2025, September 4). *56th GST Council meeting alert*. <https://www.alvarezandmarsal.com/thought-leadership/56th-gst-council-meeting-alert>
2. Central Board of Indirect Taxes and Customs (CBIC). (2026, February 12). *Advisories and notifications for taxpayers*. <https://cbic-gst.gov.in/>
3. Clear. (2026, January 2). *GST news and announcements*. <https://cleartax.in/s/gst-news-and-announcements>
4. ICRA Research. (2026, February 12). *CPI inflation printed at 2.75% in January 2026 as per new series*. <https://www.icra.in/Research/ViewResearchReport/6775>
5. Ministry of Finance. (2026). *Union Budget 2026-27: Key proposals and highlights*. Government of India.
6. NITI Aayog. (2025, October). *Roadmap on AI for inclusive societal development*. Government of India.
7. Press Information Bureau (PIB). (2025). *Gross GST collections hit record ₹22.08 lakh crore in 2024-25*. Government of India.
8. SBI Research. (2025, December 13). *GST reforms may reduce retail inflation by 35 basis points in 2025-26*. *The Economic Times*.

9. Society of Indian Automobile Manufacturers (SIAM). (2026, February 14). *Auto industry logs record January sales on GST-led demand*. A2Z Taxcorp LLP.
10. Taxbuddy. (2026). *GST on cross-border online services (OIDAR)*. <https://www.taxbuddy.com/blog/gst-filing-oidar-online-services-taxbuddy>

ARJST