



International Journal of Research Publication and Reviews

Journal homepage: www.ijrpr.com ISSN 2582-7421

Excise Duty in the GST Regime: Critical Analysis of its Impact on Tax Uniformity in India

Arvind Rajan S¹, Darshanram Karthik S²

¹CSL 85231002, BA LLB (HONS)

²CSL 85231005, BA LLB(HONS)

Chettinad Academy of Research and Education

ABSTRACT

The introduction of the Goods and Services Tax (GST) in India in 2017 marked a paradigm shift in the country's indirect tax structure by subsuming a complex web of central and state taxes into a single unified tax regime. Before enforcement of GST there was several others taxes which was following the principle of CASCADING EFFECT which includes excise duty value added tax centre sales tax etc., Among the significant transitions was the near abolition of excise duty, a long-standing tax on the manufacture of goods, but after enforcement of GST which has now been retained only in a limited form for select products such as petroleum, tobacco, and liquor. This research paper critically examines the role and relevance of excise duty in the GST regime, evaluating its implications for the ideal of tax uniformity that GST set out to achieve. At the core of the study is the tension between the principle of "ONE NATION ONE TAX" and the continued existence of excise duty on limited commodities that remain outside the GST framework. By analysing legislative provisions, constitutional provisions under Articles 246A and 366(12A), and recent policy developments, the research highlights how dual applicability of excise duty and GST in certain sectors creates distortions in uniformity. The paper further investigates the economic and administrative impact of this coexistence, particularly in terms of compliance burdens, input tax credit restrictions, and revenue considerations for both the Union and the States. The paper concludes by suggesting potential reforms, including the rationalization of excluded goods and phased integration of excise into the GST system, in order to strengthen the coherence and efficiency of India's indirect tax regime.

KEY WORDS: Cascading effect; GST ACT 2017; Constitutional provisions; One Nation One Tax; Excise duty

I. INTRODUCTION

The evolution of India's indirect tax system has been transformative, culminating in the introduction of the Goods and Services Tax (GST) in 2017, which unified numerous overlapping central and state taxes into a single regime. Before GST, taxes such as excise duty, value-added tax (VAT), central sales tax (CST), and service tax created layered taxation, often resulting in the cascading effect where taxes applied on previously taxed amounts increased costs and complicated compliance. Excise duty was a crucial tax levied at the manufacturing stage, and while GST aimed to subsume such levies, it was selectively retained on certain goods including petroleum, tobacco, and liquor, leading to a parallel tax structure that challenges GST's ideal of "One Nation, One Tax." This coexistence raises significant constitutional questions, especially under Articles 246A and 366(12A), which allocate taxing powers between the Union and the States, creating tensions within the federal structure. Economically, this dual taxation creates inefficiencies like increased compliance burdens, restricted input tax credits, and market distortions as similar goods face inconsistent tax treatments. Administratively, enforcement overlaps worsen litigation risks and add to compliance costs affecting both taxpayers and authorities. This paper addresses these intersecting issues by critically analysing constitutional provisions, statutory enactments like the Central Excise Act and CGST Act, as well as recent policy directions and judicial interpretations. The study employs a doctrinal legal review combined with empirical economic assessments,. It investigates the economic and administrative consequences of excise duty's retention within the GST framework. Through this multidisciplinary approach, the paper proposes actionable reforms for the phased integration of excise duty into GST, aiming to uphold tax uniformity, ease compliance, and strengthen governance within India's indirect tax regime.

1.1-Research Problem:

The central research problem of this study arises from the complex coexistence of excise duty with the Goods and Services Tax (GST) in India, which challenges the foundational principles of the country's indirect tax system aimed at achieving uniformity and simplicity. While the GST, introduced in 2017, was envisioned as a comprehensive restructuring to subsume multiple indirect taxes under a single, unified regime, excise duty continues to be levied on select commodities such as petroleum products, tobacco, and alcoholic beverages. This selective retention disrupts the conceptual framework of "One Nation, One Tax" by creating a dual tax structure that raises several legal, economic, and administrative challenges.

This fragmentation results in economic inefficiencies including increased compliance burdens for businesses, complexities in availing input tax credits, and market distortions where similarly situated enterprises face unequal tax treatment. Administratively, the overlapping jurisdictions complicate enforcement, raise litigation risks, and impose greater compliance costs on both taxpayers and tax authorities. Constitutionally, the problem gains further depth in light of legislative competences provided under Articles 246A and 366(12A), which govern the division of taxing powers between the Union and States, leaving unresolved tensions in fiscal federalism and revenue allocation.

This research problem focuses on evaluating whether India's current legal and policy framework effectively addresses these challenges or perpetuates inconsistencies that hinder the realisation of a seamless indirect tax system.

1.2-Research Objectives:

1. To analyse the constitutional and legal framework governing the coexistence of excise duty and GST in India, focusing particularly on Articles 246A and 366(12A), and enactments such as the Central Excise Act and the CGST Act.
2. To evaluate the impact of the retention of excise duty on select goods on the tax uniformity principle envisaged by GST, assessing how this dual taxation affects the ideal of "One Nation, One Tax."
3. To investigate the economic and administrative consequences of the dual tax system on businesses, government revenue, and fiscal federalism, including aspects such as compliance complexity, input tax credit restrictions, and revenue distribution.
4. To critically examine the operational challenges and market distortions caused by the selective application of excise duty alongside GST, including effects on competitiveness, cost structures, and consumer pricing.
5. To propose legislative and policy reforms for phased integration of excise duty into the GST regime, aiming to enhance the coherence, efficiency, and simplicity of India's indirect tax structure.

1.3-Research Question:

Whether constitutional and legislative framework support the coexistence of excise duty with GST, and how does this dual structure affect the uniformity of India's indirect tax system?

- i. How do Articles 246 and 246A of the Constitution define the legislative competence for excise duty and GST respectively?
- ii. What are the key legislative provisions allowing simultaneous levy of excise duty and GST on select goods?
- iii. How does this legal coexistence challenge or uphold the principle of "One Nation, One Tax" within India's federal structure?

Whether economic and administrative implications of retaining excise duty on certain commodities outside GST's ambit, particularly regarding compliance burdens and market distortions?

- i. How does dual taxation impact input tax credit availability and compliance costs for businesses in affected sectors?
- ii. In what ways does maintaining excise duty alongside GST affect pricing, competitiveness, and market efficiency?
- iii. What administrative challenges and enforcement overlaps arise from the simultaneous application of both taxes?

How do judicial interpretations and policy approaches shape the current coexistence of excise duty and GST, and what reforms could harmonize indirect taxation for improved fiscal federalism and economic efficiency?

- i. How does the GST Council address exclusion of certain goods from GST and dual tax levy concerns?
- ii. What legislative or policy reforms are feasible to integrate excise duty fully within GST and simplify India's indirect tax framework?

1.4-Hypotheses:

This research is premised on the hypothesis that the existing constitutional and legislative framework in India, including Articles 246A and 366(12A), along with enactments such as the Central Excise Act and CGST Act, sufficiently governs the coexistence of excise duty and GST while allowing for a legally permissible dual tax structure. The null hypothesis, however, posits that this framework is inadequate for resolving the underlying tensions related to tax uniformity and federal fiscal coordination, thereby perpetuating inconsistencies that hinder a seamless indirect tax system. It is further hypothesized that the selective retention of excise duty on certain goods significantly disrupts the principle of 'One Nation, One Tax' creating economic inefficiencies. Conversely, the null hypothesis suggests that excise duty's coexistence with GST does not materially affect economic efficiency or administrative simplicity. Moreover, this study hypothesizes that administrative complexities and overlapping enforcement challenges arising from the dual taxation framework contribute to litigation risks and fiscal uncertainty for governments at various levels. The null hypothesis challenges this by proposing that existing mechanisms adequately manage these issues. Finally, it is hypothesized that policy initiatives, including those by the GST Council, have not yet fully harmonized the indirect tax regime or resolved fiscal federalism conflicts, necessitating comprehensive legislative reforms for integration.

1.5-Research Methodology:

This research adopts a doctrinal and empirical methodology combining qualitative legal analysis with quantitative economic assessment. The study primarily utilizes secondary data from constitutional texts, statutes including the Central Excise Act and GST laws, government policy documents, and judicial pronouncements to analyse the legal framework of excise duty integration within the GST regime.

1.6-Chapterisation:

Chapter One, entitled titled Introduction which provides an overview of India's indirect tax structure, the implementation of GST in 2017, and the selective retention of excise duty on certain commodities. It outlines the research problem, research objectives, research questions, and hypotheses, Research Methodology.

Chapter Two titled as Constitutional and Legal Framework analyses relevant constitutional provisions, notably Articles 246A and 366(12A), statutory provisions such as the Central Excise Act and CGST Act, and judicial interpretations affecting the coexistence of excise duty and GST.

Chapter Three titled as Economic and Administrative Implications of Dual Taxation investigates the impact of excise duty retention on tax uniformity, compliance complexity, input tax credit restrictions, market distortions, and challenges in tax administration and enforcement.

Chapter Four titled Policy, Fiscal Federalism, and Reform Perspectives focuses on fiscal federalism issues, revenue distribution, recent GST Council policies and reforms, and judicial rulings shaping the dual tax landscape.

Chapter Five titled Critical Analysis and Recommendations synthesizes insights from previous chapters, evaluates the effectiveness of the existing framework, and proposes legislative and policy reforms for phased integration of excise duty into GST to enhance uniformity and efficiency.

Chapter Six titled Conclusion summarizes the research findings, discusses policy implications,

II. CONSTITUTION AND LEGAL FRAMEWORK OF GST

2.1- Introduction

The constitutional and legislative architecture of India's indirect tax system provides the essential framework for understanding the coexistence of excise duty and Goods and Services Tax (GST). This chapter examines the constitutional provisions, statutory enactments, This chapter focuses on the extent to which the existing legal framework supports the coexistence of excise duty and GST and how the dual structure impacts the principle of tax uniformity envisioned under the "One Nation, One Tax" doctrine.¹

The introduction of GST through the Constitution (101st Amendment) Act, 2016, marked a transformative shift in India's indirect taxation by subsuming multiple central and state taxes under a unified regime. However, the selective retention of excise duty on certain commodities such as petroleum products, tobacco, and liquor has created legal complexities and administrative challenges.

2.2- Constitutional Provisions on Taxing Powers

2.2.1 Distribution of Legislative Competences Under Article 246

The Indian Constitution establishes a clear demarcation of legislative powers between the Union and the States, which directly impacts the administration of indirect taxes including excise duty and GST. Article 246 delineates the distribution of legislative competences by categorizing subjects into the Union List, State List, and Concurrent List, granting exclusive powers to Parliament and State Legislatures over their respective domains. Prior to the GST regime, excise duty fell under Entry 84 of the Union List, granting the Union exclusive authority to levy duties on goods manufactured or produced in India, excluding alcoholic liquor for human consumption.²

2.2.2 Article 246A and Concurrent Powers for GST

The Constitution (101st Amendment) Act, 2016, introduced significant changes by inserting Article 246A, which confers concurrent powers upon both Parliament and State Legislatures to legislate on GST with respect to goods and services. Article 246A(1) provides that "Parliament, and, subject to clause (2), the Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by such State." However, clause (2) reserves exclusive power to Parliament to legislate on GST concerning inter-state trade or commerce. This constitutional provision created a

¹Alok Prasanna Kumar, for a Mess of Potage: The GST's Promise of Increased Revenue to States Comes at the Cost of the Federal Structure of the Constitution, 28 NAT'L L. SCH. INDIA REV. 98, 108, 124 (2022).

² Hema Biswas, The Impact of GST on Fiscal Federalism, INT'L J. LEGAL RSCH. (July 3, 2024), <https://www.ijlrr.com/post/the-impact-of-gst-on-fiscal-federalism>.

unique cooperative federalism model where both the Union and States share taxing authority, reflecting a departure from the traditional exclusive domain approach.³

2.2.3 Article 366(12A) and Definition of GST

Article 366(12A), also inserted by the 101st Amendment, defines GST as any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption. It excludes alcoholic liquor, thereby allowing states to continue levying excise duty on alcohol independent of GST.⁴ Additionally, Article 279A establishes the Goods and Services Tax Council as a constitutional body responsible for making recommendations on GST-related matters, including the goods and services that may be subjected to or exempted from GST.⁵

Despite the constitutional framework enabling GST, certain goods remain outside its ambit. Goods listed under Article 279A states that GST shall apply to these goods from a date recommended by the GST Council. Until such recommendation and subsequent legislative action, excise duty continues to be levied on these petroleum products under the existing framework of the Central Excise Act, 1944.

2.2.4 Fiscal Federalism and Constitutional Tensions

The constitutional provisions reflect a pragmatic approach to fiscal federalism, balancing the need for a unified tax system with the revenue concerns of both the Union and the States. However, this coexistence raises questions about the seamless application of the "One Nation, One Tax" principle, as the fragmented taxing power generates complexities in constitutional interpretation, enforcement, and fiscal coordination. The division of legislative authority creates a legal framework where the coexistence of excise duty and GST is constitutionally permissible, yet it leaves unresolved tensions related to fiscal harmonization, equal tax treatment, and administrative efficiency.

Judicial interpretation has further clarified the constitutional framework. In the landmark case of *Union of India v. Mohit Minerals Pvt. Ltd.*,⁶ the Supreme Court examined the interplay between IGST and customs duty in the context of imported goods, emphasizing the constitutional distinction between taxes on goods and taxes on services. While this case primarily addressed import taxation, its observations on constitutional powers and the recommendations of the GST Council have broader implications for understanding the legal basis of dual taxation structures in India's indirect tax regime.

2.3- Statutory Laws and Legal framework

2.3.1 Central Excise Act, 1944

The statutory framework governing excise duty and GST is rooted in legislative enactments that operationalize constitutional provisions. The Central Excise Act, 1944, has historically been the primary legislation empowering the Union Government to levy and collect excise duties on goods manufactured or produced in India. Section 3 of the Act provides the legal basis for levying duty as specified in the Fourth Schedule, while Section 4 deals with the valuation of excisable goods for the purpose of charging duty. Although GST subsumed most excise duties effective from July 1, 2017, the Central Excise Act remains in force for goods explicitly excluded from GST, particularly petroleum products and tobacco.⁷

2.3.2 Central Goods and Services Tax Act, 2017

The Central Goods and Services Tax Act, 2017 (CGST Act), along with the Integrated Goods and Services Tax Act, 2017 (IGST Act), and the State Goods and Services Tax Acts form the legislative foundation for GST in India. Section 9 of the CGST Act provides for the levy and collection of GST on intra-state supplies of goods and services.⁸ Also Section 5 of the IGST Act governs inter-state supplies. Importantly, notifications issued under these Acts specify the goods and services subject to GST, as well as exemptions. The selective exclusion of petroleum products, tobacco, and alcohol is codified in various notifications and schedules, reflecting both political considerations and the need to protect state revenues.⁹

III. Economic and Administrative Implications of Dual Taxation

The retention of excise duties alongside the Goods and Services Tax (GST) framework in India represents a significant deviation from the foundational objective of creating a unified, destination-based consumption tax system. While GST was implemented on July 1, 2017, with the vision of "One Nation, One Tax," certain commodities—particularly petroleum products (crude oil, motor spirit, high-speed diesel, natural gas, and aviation turbine fuel), tobacco products, and alcohol for human consumption—remain outside the GST ambit, continuing to be governed by pre-existing excise duty and state-level VAT regimes. This dual taxation structure creates a fragmented tax landscape that undermines the core principles of tax uniformity, seamless input tax

³ INDIA CONST. art. 246A.

⁴ INDIA CONST. art. 366(12A).

⁵ INDIA CONST. art. 279A.

⁶ *Union of India v. Mohit Minerals Pvt. Ltd.*, (2022) 6 SCC 389 (India).

⁷ Central Excise Act, No. 1 of 1944, §§ 3, 4 (India).

⁸ Central Goods and Services Tax Act, No. 12 of 2017, § 9 (India).

⁹ Integrated Goods and Services Tax Act, No. 13 of 2017, § 5 (India).

credit flow, and administrative efficiency that GST was designed to achieve. The constitutional framework under Article 279A(5) of the Constitution grants the GST Council exclusive authority to determine when petroleum products will be brought under GST,¹⁰

1. Impacts on Tax Uniformity and Market Efficiency:

The principle of tax uniformity under GST envisages a seamless, destination-based levy across jurisdictions to eliminate cascading taxation and foster an integrated national market. However, the continued imposition of excise duties on specified goods fundamentally fractures this uniform framework, reintroducing production-based taxation that varies by industry segment and central notifications under the Central Excise Act, 1944.¹¹

1. Fragmentation of the Common Market and Constitutional Implications:

The Constitution (One Hundred and First Amendment) Act, 2016 inserted Article 246A conferring concurrent jurisdiction on both Union and States to levy tax on supply of goods and services, thereby preserving the federal structure while enabling cooperative taxation. However, Article 279A (5) removed specific petroleum products from immediate GST applicability.¹² Manufacturers in high-excise sectors such as tobacco products encounter elevated cost burdens that incentivize production relocation to jurisdictions with favourable duty structures. The Kerala High Court in *Kerala Pradesh Gandhi Darshanvedhi v. Union of India*¹³ observed that the non-inclusion of petroleum products under GST creates arbitrary price differences across states, potentially violating Article 14's equality principle, though the Court ultimately deferred to the GST Council's policy discretion recognizing fiscal constraints.

2. Distortion of Production and Consumption Decisions:

Dual taxation fundamentally alters relative prices through asymmetric tax treatment, fostering economic distortions that reduce allocative efficiency. Excise-levied goods become artificially expensive relative to GST-only commodities. This price distortion impedes the welfare gains projected under a comprehensive consumption-based GST regime and can trigger cascading market inefficiencies. The cascading effect inherent in excise taxation—where tax paid at manufacturing stage becomes part of the cost base for subsequent VAT/sales tax creates "tax on tax" scenarios that GST was explicitly designed to eliminate.

3. Revenue Volatility and Competitive Imbalance:

The 14th Finance Commission increased the states' share of central taxes to 42%, but subsequent reliance on cesses and surcharges (which are not shared with states) has eroded this devolution—creating tensions in India's fiscal federalism framework.¹⁴

Differential excise rates across product categories create competitive imbalances between domestic and imported goods, affecting export competitiveness. The cascading effect of excise duties is particularly detrimental to export performance because, unlike GST where full input credit ensures exports leave tax-free, excise duties paid on inputs used in exported goods cannot be fully refunded, violating the destination principle and handicapping Indian exporters.

2. Compliance Complexity and Input Tax Credit Constraints

1. Dual Filing and Record-Keeping Requirements:

Taxpayers engaged with excise-levied commodities must maintain segregated excise registers documenting manufacturing activity, raw material consumption, and finished goods clearances under the Central Excise Rules, 2002, while simultaneously maintaining comprehensive GST records for all other supplies ensuring accurate apportionment where goods or services serve dual purposes. Periodic return filing obligations compound this burden—businesses must submit monthly/quarterly excise returns (ER-1, ER-2, ER-3) to Central Board of Indirect Taxes and Customs (CBIC) alongside monthly GST returns (GSTR-1, GSTR-3B) and annual returns (GSTR-9) to GST Network.¹⁵

2. Input Tax Credit Blockages and Cascading Effects:

Section 16 of the CGST Act, 2017 establishes the foundational framework for input tax credit eligibility, stipulating that registered persons may claim credit for input tax charged on goods or services used in the course or furtherance of business, subject to prescribed conditions.¹⁶

Cases resulting in cascading effect:

- Excise duty paid on capital goods and raw materials used in manufacturing excise-levied goods cannot be credited against GST liability on final supplies. This creates manufacturers to pay GST on the cumulative value including unrecovered excise

¹⁰ GUJARAT UNIVERSITY, <https://hrdc.gujaratuniversity.ac.in/Uploads/EJournalDetail/27/36/26.pdf> (last visited Oct. 22, 2025).

¹¹ Moorthy & Sharma, Highlighting Two Crucial Issues of GST in India, 25 J. IND. TAX'N 67, 67-75 (2024).

¹² Constitution of India, arts. 246A, 279A

¹³ Kerala Pradesh Gandhi Darshanvedhi v. Union of India, WP(C) No. 12481 of 2021 (Ker. June 21, 2021).

¹⁴ FOURTEENTH FIN. COMM'N, REPORT OF THE FOURTEENTH FINANCE COMMISSION (2015-2020) (2015).

¹⁵ Central Excise Rules, 2002, S.O. 3492(E) (India).

¹⁶ Central Goods and Services Tax Act, No. 12 of 2017, §§ 16, 17(5) (India).

duty precisely the "tax on tax" phenomenon GST was designed to eliminate.

- Transportation sector operational costs could decline by 10-15% if petroleum products were brought under GST with full input credit availability. Similarly,
- Manufacturing industries using petroleum derivatives as feedstock—chemicals, pharmaceuticals, plastics—incur substantial unrecovered tax costs that inflate product pricing and reduce competitiveness.

3. Dispute Proliferation and Litigation Risks:

Appeals to the Customs, Excise and Service Tax Appellate Tribunal (CESTAT) and subsequent High Court petitions reveal significant inconsistency in judicial outcomes, escalating both litigation volumes and business uncertainty. CESTAT, which was established under Section 129 of the Customs Act, 1962 to provide independent appellate review of customs and excise matters, despite GST implementation. As of December 2016, approximately 91,635 appeal cases were pending with CESTAT, representing disputed revenue exceeding INR 93,163 crores many of these involve transitional issues requiring reconciliation of pre-GST and post-GST tax treatment.

While GST envisages a Goods and Services Tax Appellate Tribunal (GSTAT) with Principal Bench and State Benches to hear GST appeals, CESTAT retains jurisdiction over customs matters and legacy excise/service tax disputes. The scheme under Section 109 of the CGST Act provides that appeals from State Benches of GSTAT lie to High Courts, while appeals from the Principal Bench go directly to the Supreme Court, introducing yet another layer of jurisdictional complexity.¹⁷

Section 140 of the CGST Act governs transitional provisions for input tax credit, but ambiguities in eligibility criteria, documentation requirements, and time limits for claiming credit have spawned numerous disputes.¹⁸

4. Administrative and Enforcement Challenges:

Dual taxation imposes significant organizational strain on revenue administration, diluting enforcement efficacy and complicating intergovernmental coordination within India's federal fiscal structure. The retention of excise duties administered centrally by CBIC alongside GST managed jointly by Centre and States through the GST Network creates parallel administrative hierarchies with distinct operational protocols, risk assessment methodologies, and audit procedures.

5. Coordination Deficits Between Central and State Authorities

Excise duties fall under exclusive central jurisdiction per Entry 84 of the Union List in the Seventh Schedule to the Constitution, administered by CBIC's Directorate General of GST Intelligence and field formations. Conversely, GST involves concurrent central-state administration under Article 246A, with the CGST Act governing central levies and corresponding State GST Acts governing state levies.

The GST Council, constituted under Article 279A as a federal body chaired by the Union Finance Minister with State Finance Ministers as members, makes recommendations on GST rates, exemptions, and administrative procedures through a weighted voting.¹⁹ However, excise matters fall outside the GST Council's formal purview, creating a policy coordination gap where decisions on excise rates, exemptions, and administration lack the consultative federalism framework that governs GST. This institutional separation can produce misaligned incentives.

IV. POLICY AND REFORM PERSPECTIVES

The implementation of the Goods and Services Tax (GST) in India on July 1, 2017 marked a watershed moment in the evolution of India's indirect tax regime and cooperative federalism. Envisioned as "One Nation, One Tax, One Market," GST sought to create a unified national marketplace.

India's fiscal federalism framework, enshrined in the Constitution and operationalized through successive Finance Commissions and the GST Council, embodies a delicate balance between central and state taxing powers, expenditure responsibilities, and revenue-sharing arrangements.²⁰

4.1 Revenue Dependency and the Political Economy of Exclusion:

The 15th Finance Commission (2021-26) reduced states' share in central taxes from 42% (recommended by 14th Finance Commission) to 41%, ostensibly to accommodate newly formed Union Territories of Jammu & Kashmir and Ladakh from central resources States like Karnataka, Tamil Nadu, and

¹⁷ Central Goods and Services Tax Act, No. 12 of 2017, § 109 (India).

¹⁸ Central Goods and Services Tax Act, No. 12 of 2017, § 140 (India)

¹⁹ Constitution of India, arts. 246A, 279A(5).

²⁰ GST COUNCIL SECRETARIAT, <https://www.gstcouncil.gov.in/sites/default/files/gst-knowledge/GST-and-Co-operative-Federalism.pdf> (last visited Oct. 22, 2025).

Kerala—major manufacturing hubs and net contributors to GST—have protested that the current revenue-sharing formula penalizes fiscally responsible, high-growth states while disproportionately benefiting lower-growth states, exacerbating regional disparities.²¹

4.2 GST Compensation Cess: Design, Implementation, and Expiry:

To secure state buy-in for GST adoption, the Constitution (101st Amendment) Act mandated that Parliament legislate compensation to States for revenue losses arising from GST implementation for five years. The GST (Compensation to States) Act, 2017 accordingly provided compensation guaranteeing 14% year-on-year revenue growth over 2015-16 base year revenues from taxes subsumed in GST. A GST Compensation Cess levied on luxury and demerit goods (tobacco products, luxury automobiles, aerated beverages, coal) credits into a dedicated Compensation Fund for disbursement to States experiencing revenue shortfalls.²²

The 56th GST Council meeting (September 2025) resolved to discontinue compensation cess for most goods effective September 22, 2025, retaining it only on tobacco products and coal until loan obligations are fully discharged.

4.3 GST Council Policies, Reforms, and Cooperative Federalism Dynamics:

The GST Council, meeting regularly since its September 2016 constitution, has functioned as the primary forum for federal consultation and decision-making on GST rates, exemptions, compliance procedures, and system reforms. While the Council embodies cooperative federalism ideals, its functioning has revealed tensions between consensus-building and the Centre's preponderant influence, particularly regarding petroleum inclusion and compensation.

4.4 Evolution of GST Rates and Rationalization Efforts:

Initially, GST adopted a four-tier rate structure (5%, 12%, 18%, 28%) plus compensation cess on select goods, with 0% rate for essential commodities. The 56th GST Council meeting (September 2025) undertook major rationalization, simplifying the structure to three primary slabs: (i) Merit rate of 5% for essential items and priority sectors; (ii) Standard rate of 18% for most goods and services; and (iii) Demerit rate of 40% for sin goods and luxury items (replacing the previous 28% + cess structure for most products).

V. Critical Analysis and Recommendations

The implementation of Goods and Services Tax (GST) in India on July 1, 2017, marked a watershed moment in the nation's fiscal architecture, heralding the dawn of "One Nation, One Tax" through the Constitution (101st Amendment) Act, 2016. This transformative reform subsumed multiple indirect taxes levied by the Centre and States, including Central Excise Duty, Service Tax, State VAT, and entry taxes, into a unified destination-based consumption tax system. However, the integration of excise duty—a manufacturing stage levy traditionally governed by the Central Excise Act, 1944—into the GST framework remains incomplete, particularly for commodities such as petroleum products, alcohol for human consumption, and certain tobacco products that continue to attract residual excise duties and compensation cess.

5.1-Evaluation of Existing Framework Effectiveness

Partial Subsumption Analysis:

The GST framework envisaged comprehensive subsumption of all indirect taxes into a seamless value-added tax system, yet critical exclusions persist. Petroleum crude, high speed diesel, motor spirit, natural gas, and aviation turbine fuel remain outside the GST ambit, continuing to attract Central Excise Duty and State VAT, thereby perpetuating cascading taxation contrary to GST's foundational objective. Alcohol for human consumption was constitutionally excluded from GST's definition under Article 366(12A), preserving States' exclusive power to levy State Excise Duty.²³ The 56th GST Council decided to retain compensation cess on tobacco products until full discharge of borrowing obligations, estimated to extend until March 2026.²⁴

5.2 Compensation Cess Mechanism:

The GST (Compensation to States) Act, 2017, established a compensation fund credited with proceeds from cess levied on specified goods including tobacco, coal, aerated beverages, and motor vehicles. States were guaranteed compensation for revenue shortfalls below a projected 14% annual growth trajectory from base year revenues (2015-16), computed bi-monthly for five years until June 30, 2022. However, the COVID-19 pandemic precipitated a

²¹ Gurmeet Singh, Fiscal Centralization through GST: Challenges to Cooperative Federalism and State Autonomy in India, 3 THE ACADEMIC 289, 289-301 (Aug. 2025).

²² PRS LEGISLATIVE RES., Report of the 15th Finance Commission for 2021-26 (Feb. 1, 2021), <https://prsindia.org/policy/report-summaries/report-15th-finance-commission-2021-26>.

²³ Dr. Geetanjali Sharma & Mrs. Miriam George, GST-A Game Changer in Indian Tax Structure, 19 IOSR J. BUS. & MGMT. 55, 57, 59-61 (Apr. 2017), <https://www.iosrjournals.org/iosr-jbm/papers/Vol19-issue4/Version-1/H1904015562.pdf>.

²⁴ Press Info. Bureau, Ministry of Fin., Recommendations of the 56th Meeting of the GST Council (Sept. 3, 2025), <https://www.pib.gov.in/PressReleaseDetail.aspx?PRID=2163555>.

compensation crisis, with the Centre borrowing approximately ₹2.7 lakh crore through back-to-back loans to States and market borrowings by States guaranteed by future cess proceeds.²⁵

5.3 Sectoral Analysis: Tobacco and Petroleum Products

Tobacco Products - Excise and Compensation Cess:

Tobacco products attract a cumulative tax burden comprising 28% GST, compensation cess (₹0.36 to ₹0.61 per unit for various tobacco forms; ₹2,076 to ₹4,170 per thousand for cigarettes), Central Excise Duty, and NCCD, aggregating to approximately 53% tax incidence. The 56th GST Council's decision to retain compensation cess until full loan repayment necessitates legislative clarity on the transition timeline, as the Union Finance Minister's discretion to notify cessation dates creates uncertainty.²⁶

Petroleum Products - Exclusion from GST:

Petroleum crude, motor spirit (petrol), high speed diesel (HSD), natural gas, and aviation turbine fuel (ATF) remain constitutionally excluded from GST, attracting Central Excise Duty and State VAT, which together constitute approximately 50-60% of retail prices. This exclusion perpetuates cascading taxation, as manufacturers cannot avail ITC on petroleum inputs, increasing production costs across sectors.

The GST Council has not recommended inclusion of petroleum products despite repeated demands from States, primarily due to the Centre's revenue dependency on excise duties States similarly rely on petroleum VAT for 15-20% of own tax revenues, creating a mutual veto situation where neither Centre nor States are willing to forego lucrative petroleum levies.²⁷

5.4 Legislative and Policy Reforms - Recommendations

Changes Needed in the GST Law (CGST Act)

- Include a new rule (Section 9A): This would allow the government, guided by the GST Council, to gradually add petroleum products (like petrol and diesel) into GST over a maximum of five years. There will be minimum tax rates and temporary extra taxes (cess) during this period to ensure smooth change.
- Allow Input Tax Credit (ITC) on petroleum inputs earlier: Change the law to let businesses claim credit for taxes paid on petroleum used in manufacturing before petroleum is fully included in GST, to avoid tax-on-tax piling up.
- Limit the anti-profiteering rule's time: Introduce a rule (Section 171A) to apply anti-profiteering provisions only for three years after any GST rate changes, with clear methods to check unjust price increases, addressing legal concerns.
- Allow government to waive small tax recoveries: Add a rule (Section 11B) that lets the government waive recovering small amounts of unpaid taxes from normal business errors, based on GST Council advice.

Strengthening the GST Council's Role

- Make GST Council decisions on interstate trade and petroleum taxes binding: Amend the Constitution so that GST Council's recommendations in these areas must be followed by both Centre and States, while still allowing States control over taxes within their territories.
- Set up a special GST dispute resolution body (DRC): This body, with retired top court judges, would solve disputes between Centre and States on GST rates and revenue sharing, and its decisions would be final.

VI. CONCLUSION

The integration of excise duty into GST represents an unfinished agenda of India's tax reform journey, essential for realizing the vision of "One Nation, One Tax" enshrined in the Constitution (101st Amendment) Act, 2016. This chapter's critical analysis reveals that while GST has succeeded in eliminating cascading taxes for most goods and services, the exclusion of petroleum products and incomplete subsumption of tobacco have perpetuated complexities, revenue leakages, and compliance burdens.

The discontinuation of compensation cess without establishing sustainable revenue-sharing mechanisms threatens to undermine cooperative federalism, as States face projected revenue losses of ₹60,000 crore to ₹2.5 lakh crore from rate rationalization, uncompensated by the Centre. The retention of cess proceeds (₹1.8 lakh crore annually) outside the divisible pool exacerbates vertical fiscal imbalances, contradicting the federal spirit of Article 279A.

²⁵ Hema Biswas, The Impact of GST on Fiscal Federalism, INT'L J. LEGAL RSCH. (July 3, 2024), <https://www.ijllr.com/post/the-impact-of-gst-on-fiscal-federalism>.

²⁶ Taboola, GST Council Retains 28% Tax and Cess on Tobacco, Sin Goods, ECON. TIMES (Oct. 16, 2025), <https://economictimes.com/industry/cons-products/tobacco/gst-council-retains-28-tax-and-cess-on-tobacco-sin-goods/articleshow/123689256.cms>.

²⁷ Anil S. Dhanorkar, The Impact of GST on Fiscal Federalism, INDIAN J.L. & LEGAL RES. (2024), <https://www.ijllr.com/post/the-impact-of-gst-on-fiscal-federalism>.

It concludes that the dual tax system creates significant economic inefficiencies, undermines the principles of tax uniformity and transparency, and generates administrative complexities that hinder effective enforcement. The selective retention of excise duty on certain goods results in cascading tax effects, drives compliance costs higher, distorts market pricing, and affects competitiveness adversely.