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Impact of GST on Small Traders in India

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Abstract

The introduction of the Goods and Services Tax (GST) on 1 July 2017 marked a major transformation in India's indirect taxation system. GST replaced several central and state-level indirect taxes with a unified, destination-based tax system intended to reduce tax cascading, promote a common national market, improve transparency and simplify tax administration. Small traders constitute an important part of India's retail and distribution network and therefore the effects of GST on this sector are significant.

This research paper examines the impact of GST on small traders, with particular emphasis on compliance costs, digitalisation, input tax credit, working capital, business transparency, market competitiveness and the Composition Scheme. The study is based primarily on secondary data obtained from government sources and recent academic literature. The evidence suggests that GST has produced both positive and negative effects. On the positive side, it has encouraged formalisation, digital record keeping, tax transparency and a more integrated market. On the negative side, small traders have faced difficulties related to digital compliance, return filing, accounting costs, technical issues and working-capital pressures. The paper concludes that GST has created a more transparent and integrated taxation environment, but its benefits for small traders depend heavily on simplified compliance procedures, digital literacy, timely input-tax-credit mechanisms and effective taxpayer support.

Keywords: GST; Small Traders; MSMEs; Tax Compliance; Input Tax Credit; Composition Scheme; Digitalisation; Working Capital; India.

1. Introduction

Small traders play an important role in the Indian economy by providing employment, distributing goods, supporting local markets and connecting producers with consumers. Before the introduction of GST, businesses in India were subject to several indirect taxes administered by different authorities. The multiplicity of taxes and procedures often resulted in cascading taxation, different compliance requirements and difficulties in conducting interstate business.

The Goods and Services Tax was introduced in India on 1 July 2017 with the objective of creating a unified indirect tax system. It replaced a number of indirect taxes and introduced a common framework for the taxation of goods and services.

For small traders, GST represented both an opportunity and a challenge. On the one hand, the system provided greater tax transparency, input-tax-credit mechanisms and opportunities to operate in a wider national market. On the other hand, traders accustomed to relatively simple paper-based accounting had to adapt to online registration, invoicing, return filing and digital record keeping.

2. Objectives of the Study

1. To examine the impact of GST on small traders in India.

2. To analyse the positive effects of GST on small trading businesses.
3. To identify the major problems faced by small traders under GST.
4. To examine the effect of GST on compliance costs and working capital.
5. To study the role of digitalisation in GST compliance.
6. To examine the usefulness and limitations of the Composition Scheme.
7. To suggest measures for reducing the compliance burden on small traders.

3. Research Methodology

The present study is descriptive and analytical in nature. It is based primarily on secondary information collected from Government of India and CBIC publications, GST Council materials, official GST-related information, recent academic research papers and published studies concerning small traders and SMEs.

Recent empirical studies have been used to understand the experiences of small traders after GST implementation. The paper therefore combines conceptual analysis with findings reported in recent literature.

4. GST and Small Traders

GST is a destination-based indirect tax imposed on the supply of goods and services. It aims to reduce the cascading effect of taxes by allowing eligible registered businesses to claim input tax credit.

Small traders were given a simplified alternative through the Composition Scheme, subject to eligibility conditions. The purpose of the scheme is to provide a simpler tax-payment mechanism for eligible small taxpayers. However, composition taxpayers operate under restrictions that differ from regular taxpayers. Therefore, the choice between the regular GST scheme and the Composition Scheme can be important for a small trader.

5. Positive Impact of GST on Small Traders

5.1 Creation of a Unified Market

GST has helped create a more integrated national market. For small traders, this can make interstate business comparatively easier and reduce complications associated with multiple indirect-tax systems.

5.2 Reduction in Cascading of Taxes

GST introduced an input-tax-credit mechanism designed to reduce cascading taxation. Eligible traders can generally claim input tax credit on purchases against output tax liability, subject to applicable conditions.

5.3 Increased Transparency

GST has encouraged businesses to maintain invoices and transaction records systematically. Digital reporting has increased the visibility of business transactions and reduced opportunities for tax evasion.

5.4 Formalisation of Small Businesses

GST has encouraged businesses to enter the formal tax system. Registration, invoicing and digital records create a clearer financial history that can potentially help small businesses obtain credit and expand.

5.5 Better Business Records

GST encourages traders to maintain proper purchase and sales records. Systematic accounting can help traders understand sales, purchases, margins and tax liabilities more accurately.

5.6 Wider Business Opportunities

GST-compliant small traders may find it easier to supply larger companies and organised businesses that require tax-compliant invoices.

6. Negative Impact of GST on Small Traders

6.1 Increased Compliance Burden

Small traders often do not have specialised accountants or tax departments. Registration, invoicing, return filing, reconciliation and digital records may require outside professional assistance.

6.2 Cost of Professional Services

Many small traders depend on accountants, tax practitioners or GST consultants, making professional fees an additional operating cost.

6.3 Digital Literacy Problems

GST compliance is technology-driven. Traders need access to digital devices, internet connectivity and appropriate accounting or filing knowledge. Limited digital skills can create dependence on accountants and service providers.

6.4 Working-Capital Pressure

GST can influence the timing of cash flows. Traders may have to pay suppliers, hold inventory and manage tax liabilities before receiving customer payments. This is particularly significant for businesses with limited financial reserves.

6.5 Technical Problems

Online tax systems can create difficulties when traders experience technical problems, errors, connectivity issues or unfamiliarity with digital procedures.

6.6 Difficulty in Understanding GST Rules

GST involves tax rates, classification, invoices, input tax credit, returns and other procedural requirements. Changes in rules or procedures can make compliance difficult for traders without professional tax knowledge.

7. Impact on Business Costs

The effect of GST on business costs varies according to the size, sector and nature of the trader. For some traders, input tax credit and streamlined taxation may reduce tax-related costs. For others, accounting fees, software expenses, professional charges and time spent on compliance can increase operating costs.

Therefore, GST should not be evaluated only by considering the tax rate. The total cost of compliance is equally important for small traders.

8. Impact of GST on Competitiveness

GST has influenced competition among small traders in several ways. Formal GST-registered businesses may benefit from better documentation, access to organised supply chains and input-tax-credit mechanisms. At the same time, small traders may face competition from businesses operating outside the formal tax system.

The Composition Scheme provides a simplified option for eligible small taxpayers, but its restrictions may affect the ability of some traders to compete with regular taxpayers.

9. Role of Digitalisation

Digitalisation is one of the most important features of GST. The system has encouraged digital registration, electronic tax returns, electronic invoices, digital accounting, online tax payments and electronic documentation.

Digitalisation can improve efficiency in the long term. However, it can also create barriers for traders with limited digital skills. Digitalisation should therefore be accompanied by training, accessible help facilities and simple user interfaces.

10. GST and Formalisation of the Economy

An important long-term impact of GST has been the movement towards formalisation. When traders issue GST-compliant invoices and maintain digital records, transactions become more traceable. This can improve tax compliance and reduce the informal component of the economy.

Formalisation can create benefits for small traders by providing documented financial records useful for credit applications and business expansion. However, formalisation also means that businesses must bear compliance costs.

11. Major Challenges Faced by Small Traders

The major challenges are compliance requirements, accounting expenses, digital filing, working-capital pressure, input-tax-credit issues, frequent procedural changes, technical problems, lack of GST knowledge, competition and record-keeping requirements.

12. Findings of the Study

1. GST has improved tax uniformity by creating a common indirect-tax framework.
2. Input tax credit has the potential to reduce cascading taxation for eligible regular taxpayers.
3. Digitalisation has increased transparency but has also created adjustment costs.
4. Compliance costs remain a major concern for smaller businesses.
5. Working-capital management is important because tax compliance can influence cash flows.
6. The Composition Scheme provides simplification for eligible taxpayers, but its restrictions may limit its usefulness for some businesses.
7. GST has encouraged formalisation and systematic record keeping.
8. Digital literacy and GST knowledge can reduce compliance difficulties.
9. Technical problems and changing procedures remain concerns for some small traders.
10. The overall impact of GST is mixed and depends on the size, sector, turnover and technological capacity of the trader.

13. Suggestions and Recommendations

13.1 Simplification of Compliance

GST return filing and related procedures should remain as simple as possible for small taxpayers.

13.2 Strengthening Digital Training

Regular GST awareness programmes should be organised for small traders, particularly in semi-urban and rural areas.

13.3 Reduction in Compliance Costs

Low-cost and user-friendly digital solutions should be developed so that small traders do not have to rely heavily on expensive professional services.

13.4 Timely Resolution of ITC Issues

Efficient processing and resolution of input-tax-credit issues can help reduce working-capital pressure.

13.5 Better Taxpayer Support

Help desks, facilitation centres and regional-language educational material can assist traders who have difficulty understanding GST procedures.

13.6 Stable Tax Procedures

Frequent procedural changes can increase uncertainty. Changes should be communicated clearly and implemented with adequate transition time.

13.7 Special Support for Micro Traders

The smallest traders require more support because they generally have limited financial resources, accounting expertise and digital skills.

14. Conclusion

The Goods and Services Tax has significantly changed the operating environment for small traders in India. It has introduced a unified tax framework, improved transaction transparency, encouraged formalisation and created a more systematic input-tax-credit mechanism.

At the same time, GST has imposed new responsibilities on small traders. Digital compliance, accounting requirements, professional expenses, working-capital pressures and difficulties in understanding tax procedures can create significant challenges.

The long-term success of GST for small traders depends not merely on tax rates but also on the simplicity, predictability and cost of compliance. Simplified procedures, stronger digital support, taxpayer education and timely resolution of tax-credit issues can help ensure that small traders receive the benefits of formalisation without facing disproportionate compliance costs.

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