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Impact of Tax Regimes on Entrepreneurship and Economic Growth in India

Harshita Gireesh¹, Indu K², Reeth S³, Ritesh D⁴, Suhas M⁵, Tejaswini S⁶

Department of Finance, CMS Business School, Jain Deemed to be University, Bengaluru, India ^{1,2,3,4,5}

Project Guide, CMS Business School, Jain Deemed to be University, Bengaluru, India⁶

ABSTRACT: This piece is all about how India's tax system is changing and what that means for people starting and running businesses, as well as for the country's overall economic growth. We're taking a close look at two big changes: the Goods and Services Tax (GST) and the recent tweaks to corporate taxes. To figure things out, we're using a mix of methods. That means we're crunching numbers by taking a look at how companies are doing and what the government's data shows. Plus, we're also talking to real people – entrepreneurs, government officials, and business experts – to get their take on things. We want to know from their own experiences, what is really going on. What we're finding is kind of a mixed bag.

On the one hand, the GST seems to have made the tax system more organized, and more people are paying taxes now. But, here's the problem. It's also brought some headaches, especially for small and mid-sized businesses (SMEs). Many of them are finding it tough to keep up with all the rules and paperwork. It can be a bit overwhelming for them. Then there are those corporate tax cuts, which were supposed to make India more attractive to global companies and boost entrepreneurship. From what we can tell, they haven't made a huge difference in getting people to start new businesses. A lot of the people we talked to said that the tax breaks didn't really motivate them to create something new. We've also spotted some key issues that need attention. First off, the whole tax compliance process can be super complicated. It can feel like you need a PhD to figure it out.

So, what can be done? Based on all of this, we've got a few ideas which include:

- Make things simpler: The government should create easy-to-use digital tools to help businesses manage their taxes. Less paperwork is always a win!
- Spread the word: They need to do a better job of informing people about the tax breaks and programs that are out there. Maybe use social media, run workshops, or partner with business groups.

KEYWORDS: Goods And Service Tax, Entrepreneurship, Tax System, Tax incentives, Economic growth, Small and Medium-sized Enterprises (SMEs)

I. INTRODUCTION

Tax systems are among the most important drivers of a nation's economic trajectory, affecting entrepreneurship, business competitiveness, and economic growth. An efficiently structured taxation system improves a favorable business environment, draws in investment, and increases levels of productivity. Certain of the revolutionary recent tax regime changes in India include the enactment of the Goods and Services Tax (GST) in 2017, the cutting of the corporate tax and various incentives for startups and small businesses. These reforms promised to ease compliance with taxes, widen the base of taxation, and encourage business activity. Nonetheless, their ability to contribute towards entrepreneurship and growth is still being debated.

Tax changes have long-term implications that extend beyond compliance and include overall economic growth. The Ministry of Statistics and Programme Implementation (MoSPI) reported a 7.7% GDP for 2017–18 shortly after the GST was put into operation, as opposed to a 7.1% GDP for 2016–17. This might suggest that tax simplification had a beneficial impact on activity. However, some businesses continue to suffer the most, including manufacturing and

exports, due to high compliance costs, supply chain disruptions, and uneven policy implementation. Clothing exports decreased 11% during the preceding 10 years, and India's manufacturing sector only accounted for 13% of the nation's GDP in 2023, highlighting structural issues that tax changes alone have not resolved (World Bank, 2023).

In addition, steep corporate tax reductions of 22% for existing businesses and 15% for new manufacturing firms have been implemented recently to draw investments and enhance global competitiveness. Although these measures have enhanced India's position in the Ease of Doing Business Index, it is unclear whether they will indeed have a positive effect on entrepreneurship in the next few years. In addition, concerns such as industry-specific variation in tax incentives, small business compliance, and retaliatory tariffs from major trading partners continue to influence the extent to which changes in tax advance sustainable economic growth.

With varying degrees of success, various research studies have been done analyzing the relationship between taxation and economic growth, and entrepreneurship. However, there has not been much work in the post-GST scenario and how entrepreneurship has been driven by the new tax regime.

II. LITERATURE REVIEW

There has been extensive discussion about the impact of GST on entrepreneurship. Bhattacharya and Rao (2020) examined short-run effects of GST on SMEs and stated that the system is still difficult for many businesses, particularly due to frequent amendments of tax rules leading to ongoing compliance issues. Although, the money transfer tax may improve transparency, small businesses still struggled with regulatory compliance costs as well as digital compliance. Prasad (2020) found that while a more formalized tax and lower corporate tax rate may have supported investment growth, it was not a disincentive to new business. Additionally, he determined that new business formations were positively impacted more significantly by access to finance and regulatory compliance than assurance of a formalized tax codes and tax rate. Mukherjee (2018) discussed compliance challenges for GST, especially as pertains to filing GST returns and complexities of GST filing.

One of the challenges with the Indian taxation system that Rao (2021) pointed out is that entrepreneurs don't have the same awareness of tax incentives. Rao (2021) reported that 56% of startups were unaware of tax exemptions like those offered about the tax incentives for Startup India. The literature had even proposed that should the government improve advertisement, marketing, and ease of filling out applications, it might have the potential of allowing more entrepreneurs to access tax incentives or exemptions. Taxation can also have consequences on businesses depending on what business or industry the business occupies. Goyal (2019), when exploring tax burdens when assessing tax burdens across sectors, suggests that while a corporation may have advantageous tax incentives, the burden of compliance is more profound in the small and medium enterprise (SME) sector when compared to other sectors. Overall, the literature does generally agree that taxation should be constructed to be effective based on industries/sectors.

Another crucial aspect of reforming a tax system is compliance costs which create burdens on micro and small businesses. Ganguly (2020) focused on the impact tax compliance costs had on the growth of microenterprises in India. With respect to firm growth, the findings suggested that microenterprises experience high administration costs associated with tax compliance and that affects profitability and scaling of small firms. Businesses faced compliance costs from accessing accountants, costing software used to file taxes online, and costs from accidentally missing compliance. The authors suggested a system of tax compliance that is more flexible with respect to size and revenue to help reduce the burden on microenterprises and assist those enterprises into the formal economy.

Deb and Chakraborty (2020) studied the long-run associations between tax reform and economic growth in India for the period 1975 to 2017. Their empirical evidence using cointegration and causality tests suggest tax simplifications, like the GST, had a positive association with economic growth for the long run. However, for the short run, it was economic dislocations that businesses made the adjustment to because of sudden changes in tax policy. They recommended tax reforms be made in a gradual fashion to allow firms sufficient time to adjust all aspects of their business practices to conform with tax reform.

RESEARCH GAP

Although substantial research has been conducted on tax policies and growth, there are still some gaps in the literature. Most of the literature has examined macroeconomic consequences while limiting exploration of how tax policies impact small and emerging firms, and further, most of the literature did not provide adequate investigation of how different industries engage different levels of tax burdens, as understanding tax burdens and incentives within specific industries is critical for creating more targeted policy within most industries. Therefore, although the literature examined short-term impacts of GST, relatively little research on the long-term impact of GST on business sustainability and innovation. Further, the research shared another gap, which was the limited awareness of tax supports of regulations and compliance for entrepreneurs, which negatively impacted their capacity and use of tax benefits of tax-based government support programs. Recognizing these gaps in knowledge among policymakers, the literature can provide them with a better foundation for developing more effective taxpayer structures which can contribute to entrepreneurship and economic development.

OBJECTIVES OF THE STUDY:

1. To Explore the Relationship Between Taxation and Ease of Doing Business in India.
2. To Examine the Role of Tax Incentives in Promoting Startup Growth and Innovation.

III. RESEARCH METHODOLOGY

This study will use a mixed methods design, which includes both qualitative and quantitative research techniques. Primary data were collected through structured questionnaires and interviews conducted with entrepreneurs and business owners asked about their perceptions concerning the impact of the tax regimes on the performance and growth of their businesses across various industries. Secondary data were obtained from government reports, academic journals, and databases to establish the changes of economic indicators and tax revenues with time. Quantitative data will be analyzed, while qualitative data will be thematically coded in order to find common challenges and opportunities of businesses. Another part within the scope of the overall study will incorporate a comparative analysis between the pre- and post-GST eras with a view of examining the impacts of the tax reforms on entrepreneurship and economic growth. The results will help the task force formulate appropriate recommendations to policymakers on how to create an improved business climate through optimized tax policies.

IV. DISCUSSION OF RESULTS

2. How would you describe the overall impact of India's tax system on entrepreneurship?
100 responses

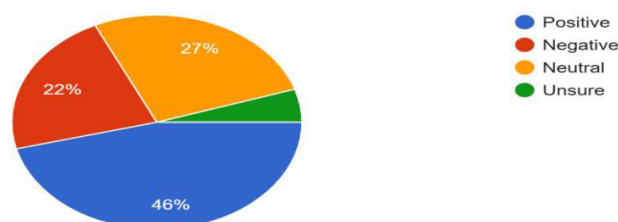


Figure 4.1

The response from the survey shows that out of all respondents, 46% claimed to hold a "Neutral" opinion regarding the impact which India's tax system has on the impact. This means that quite a significant number of people consider India's tax system to not be highly advantageous or obstructive. As for those holding a stance, 27% consider the tax system to have a "Positive" impact while 22% identify it as having a "Negative" one. This ratio suggests that the impact of the tax system is not very favorable or unfavorable for some of the entrepreneurs and depends upon their

industry, scale of business, and regulative norms in place. The ‘Unsure’ category being very small indicates that respondents are somehow informed but a reason strong enough to form an opinion or have relevant experience with tax regulations is missing.

5. In your opinion, how does India’s tax regime compare to other emerging economies in terms of supporting business growth?

101 responses

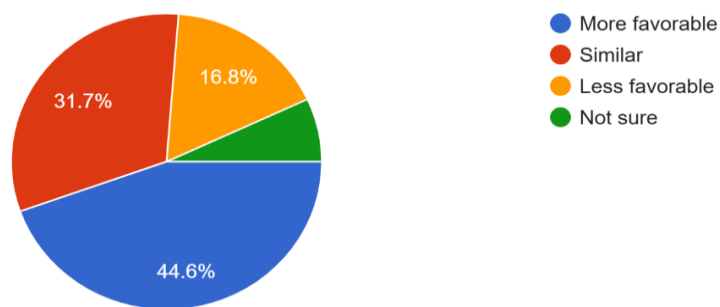


Figure 4.2

The survey says many (44.6%) see India's tax system as worse for business growth than other similar countries. This raise worries about how competitive India is, tax burdens, and regulations. About 31.7% think India's tax system is on par with its peers, which means it's not top-notch, but not far behind. Only 16.8% think it's better, showing little faith in tax policies boosting business growth.

6. Do you believe India’s current tax structure makes it easier or harder for new businesses to start and sustain operations?

101 responses

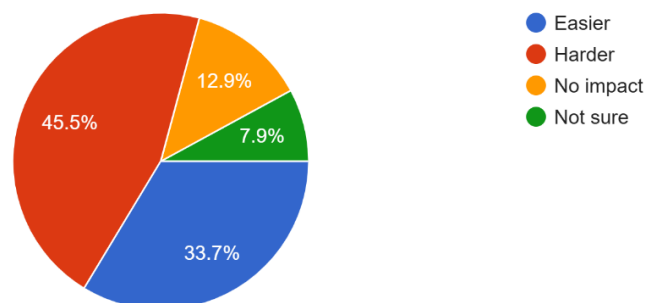


Figure 4.3

About 33.7% don't think the tax system matters for new businesses, saying things like the market, competition, or money are more crucial. Only about 12.9% think taxes help new businesses, so most don't see taxes as a plus. Around 7.9% aren't sure, maybe because they haven't dealt with it directly or aren't clear on how taxes affect startups.

7. What is the biggest taxation-related challenge businesses face when starting in India?

101 responses

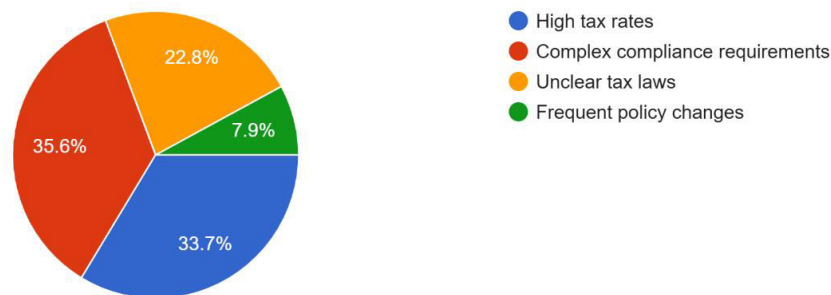


Figure 4.4

A survey says that for new Indian businesses, the biggest tax problem is dealing with tough compliance rules (35.6%). This means red tape and following the rules can really stop people from starting companies. Another big worry is how often the rules change (33.7%). It's hard for businesses to plan when they must keep up with new tax laws all the time. High tax rates are also a problem (22.8%), but not as big as the other two. It's interesting that only a few people (7.9%) think unclear tax laws are their main issue. So, it's not that the laws are confusing, just that they're a pain to follow.

8. How effective do you think government initiatives (e.g., GST, digital tax filing) have been in improving the ease of doing business?

100 responses

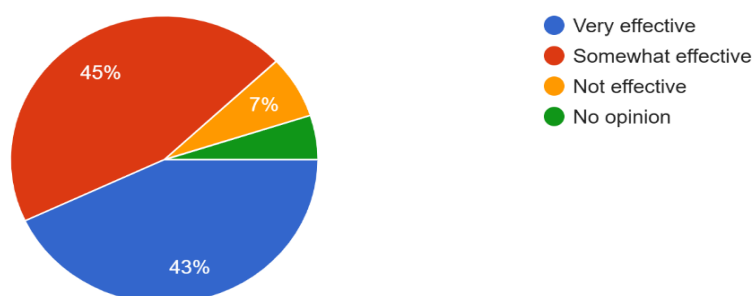


Figure 4.5

The survey shows mixed opinions on how well government programs like GST and online tax filing are making it easier to do business. About 45% think the programs are somewhat helpful, but issues persist. Around 43% don't think

they've made things any better, pointing to regulatory problems and gaps. Only 7% find them very helpful, suggesting the programs haven't reached their full potential.

9. Would a more simplified and transparent tax structure encourage more people to become entrepreneurs?

100 responses

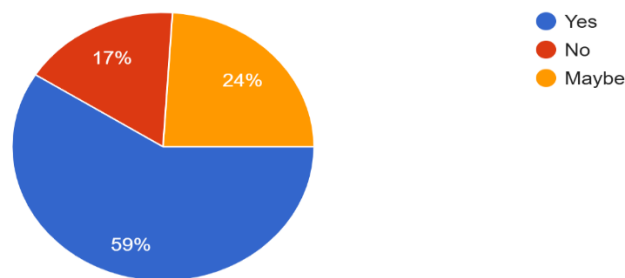


Figure 4.6

A recent survey shows that simplifying taxes could really help entrepreneurs in Bengaluru and India. A large majority (59%) think simpler, clearer taxes would boost new businesses. About a quarter (24%) aren't sure, noting that funding, rules, and the market also matter. Only a small group (17%) don't think tax changes would make a difference. For Bengaluru's businesses, this means cutting red tape and making tax rules easier to understand. This could make it easier to start a business, spur new ideas, and grow the economy.

V. FINDINGS, SUGGESTIONS, AND CONCLUSION

FINDINGS:

1. **Effect of GST on Entrepreneurship:** Ever since the Goods and Services Tax (GST) came into effect in 2017, its impact on entrepreneurship in India has been a mixed bag. While it simplified the tax regime by merging multiple indirect taxes into one, it also created additional compliance issues, particularly for small and medium enterprises. Statistics reveal that 43.6% of respondents identify high frequency in tax policy adjustments as one of the serious barriers to growth and stability. Approximately 44% of businessmen think indirect tax, especially GST, has seriously impacted economic transactions. This confirms that although GST has made it easier and helped improve tax returns, it brought about extra levies which also hurt small-sized businesses severely.
2. **Corporate Tax Cuts and Investment Climate:** The lowering of the corporate tax rate, from 30% to 22% for existing businesses and to 15% for new manufacturing facilities, was to make India competitive in the global market. Survey evidence indicates that 35% of the respondents consider rates of corporate taxes as among the drivers of business growth. However, there is limited evidence that these tax cuts have enhanced entrepreneurship since 58.4% of those asked think that the current tax incentives do not lead to the creation of new businesses.
3. **Volatility and Complexity of Compliance:** Compliance is still a huge challenge for entrepreneurs. Around 35.6% of the people asked said that complicated rules and regulations are the biggest obstacle to new business start-ups. The remaining 33.7% mentioned that policy volatility is a concern. Policy volatility destroys business confidence and hinders long-term planning, particularly for small businesses.

4. Unawareness of Tax Incentives: There is a broad knowledge gap about tax incentives for startups. More than 56% of entrepreneurs interviewed had no clue about Startup India program incentives, and just 12% were aware of them. This unawareness prevents firms from capitalizing on financial assistance that could make them grow.

SUGGESTIONS:

1. Simplify Tax Compliance Processes: Simplification through online systems can decrease administrative costs for small businesses. Facilitating automated filings and enhanced support can ease compliance.
2. Increase Awareness of Tax Incentives: The government needs to conduct targeted campaigns and workshops for entrepreneurs to raise awareness of existing tax incentives so that they may take advantage of financial support.
3. Stabilize Tax Policies: A stable tax regime with fewer changes can reduce business uncertainty. Regular reviews based on stakeholder input can keep the regulatory environment stable.

VI. CONCLUSION

The report shows that while reforms like GST and slashing corporate tax have simplified things and expanded the tax base, they still present real challenges to entrepreneurs. Bureaucratic compliance processes and ongoing policy tweaks take a greater toll on small enterprises, bringing their growth to a halt. To solve these problems, we need to simplify compliance, enhance awareness of tax incentives, and stabilize policy. By focusing on sectoral solutions and creating a more stable regulatory environment, India can create a tax system that supports entrepreneurship and enables sustained economic growth.

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