

IT'S ALMOST NO TO ITC.....?

Task Force on Implementation of the Fiscal Responsibility and Budget Management Act, 2003 was of the view that *high import tariffs, excises and turnover tax on domestic goods and services have enormous cascading effects, leading to a distorted structure of production, consumption and exports. This problem can be effectively addressed by shifting the tax burden from production and trade to final consumption, and from savings to consumption. Accordingly, the Task Force recommended that “a well-designed destination-based value-added tax on all goods and services is the most elegant method of eliminating distortions and taxing consumption.*

The Empowered Committee of State Finance Ministers in its report dated 10.11.2009, mentioned that *in the GST, both the cascading effects of CENVAT and service tax are removed with set-off, and a continuous chain of set-off from the original producer's point and service provider's point up to the retailer's level is established which reduces the burden of all cascading effects. This is the essence of GST, and this is why GST is not simply VAT plus service tax but an improvement over the previous system of VAT and disjointed service tax.*

Even the 13th Finance Commission Report submitted on 15th December 2009 also advocated allowing *credit for tax paid on all intermediate goods or services on the basis of invoices issued by the supplier.* As a result, all different stages of production and distribution can be interpreted as a mere tax pass-through, and the tax will effectively 'stick' on the final consumption within the taxing jurisdiction. *This will facilitate the elimination of the cascading effect at various stages of production and distribution.*

So, under the Goods and Services Tax (GST) Acts, Input Tax Credits (ITC) are provisioned to eliminate the cascading effects of taxes on the total cost of any product or service. Double taxation or tax on tax increased the cost of the products or services, and consumers have to pay an extra amount for no value addition. Also, products or services in international markets become unviable. In the overall



CMA Anil Sharma
Cost Accountant

scenario, it impacts economies adversely. So, to make products competitive in the market and also to make available cheap products or services to consumers, the concept of MODVAT/CENVAT/ITC was introduced way back in the late nineties. It also helps the economies to grow as it enhances the purchasing power of consumers.

Provisions of Input Tax Credit (ITC) are introduced in CGST Act, 2017, and Section 16 deals with such provisions. Section 16 empowers registered persons under GST to avail ITC for their inputs, capital goods and input services which can be set off against their outward tax liabilities later on. In some cases, if ITC is not utilized for tax liabilities, the same can be claimed as a refund. The concept of ITC gives big relief to business entities from working capital requirements and saves financial costs. But section 16 also imposes some conditions and restrictions on the registered person while availing the benefits of ITC.

These conditions are summaries as under:

- ★ Registered Person must have in his possession Invoices, DN/CN etc., issued by a registered supplier
- ★ The supplier, who is registered under law must have furnished details of such invoices in his GSTR-1 and must have been communicated to the recipient through GSTR-2B.
- ★ -NN39/2021 dt. 21.12.2021 w.e.f 01.01.2022 ref Finance Act 2021
- ★ Registered Person must have received Goods or Services or both
- ★ ITC on above supplies should not have been restricted u/s 38 (wef 01.10.2022)
- ★ Supplier of goods and/services must have deposited taxes on such supplies to the government accounts; otherwise, the recipient has to reverse the ITC with interest
- ★ Recipient must have filed his return i.e., GSTR-3B
- ★ Recipient must have paid to supplier consideration of such goods/services within 180 days from the invoice date
- ★ Recipient is not entitled to ITC for any invoice of the

respective Financial Year after 30th November of the next financial year.

No input tax credit shall be availed by a registered person in respect of any tax

that has been paid in pursuance of any order where any demand has been confirmed on account of any fraud, will full misstatement or suppression of facts –rule 36(3).

In addition to the restriction imposed u/s 16 of CGST Act, 2017, section 17 of CGST Act, 2017 further restricts or denies the ITC on certain inputs and input services where ITC can't be availed. It added cost to products manufactured/traded and services provided. On one side, it increases finance costs for the business entity on the other side; the consumer is forced to pay more for no value addition. Such goods and services or transactions are listed below:

- ★ ITC is available only if transactions are undertaken for business purposes only,
- ★ ITC for inputs used to manufacture/trade exempted goods or services is not available. It is a case of cascading effects of taxes and increases cost of production and prices of such goods. They may be called exempted goods, but actually, such goods or services have inbuilt taxes. So electricity, health and education services are exempted under GST but have inbuilt taxes and consumers pay more.
- ★ ITC is not available on motor vehicles having seating capacity less than thirteen seats (including driver) purchased for business purposes. However, for the following businesses ITC is available:
 - Trading of such vehicles, i.e., motor vehicle dealers
 - Transportation of passengers i.e., taxes operator/ tour operators/hotels
 - schools for such vehicles
- ★ Similarly, ITC on insurance paid, servicing, repair and maintenance or any other expense incurred on such motor vehicles is not available. However, if such expenses are incurred on motor vehicles used



in the above-mentioned businesses, ITC is available.

- ★ ITC is not available for vessels and air crafts purchased for business purposes. But if these are purchased for following business, ITC is available:
 - further supply of such vessels or aircraft; or
 - transportation of passengers; or
 - imparting training on navigating such vessels; or
 - imparting training on flying such aircraft;
 - for transportation of goods;
- ★ ITC on insurance paid, servicing, repair and maintenance or any other expense incurred on such vessels and air crafts is not available. provided such expenses are incurred in the course of the above-mentioned businesses, ITC is available.
- ★ Further, ITC is also available to a registered person engaged in the services of general insurance with respect to such motor vehicles, vessels and aircraft.
- ★ ITC is also not available for expenses incurred for:
 - food and beverages,
 - outdoor catering,
 - beauty treatment,
 - health services,
 - cosmetic and plastic surgery,
 - leasing, renting or hiring of motor vehicles, vessels or aircraft referred to in the above clauses except when used for the purposes specified therein,
 - life insurance and health insurance

However, ITC is available to a registered person if he is engaged in above said businesses to provide taxable supplies by using such inputs or inputs services.

- ★ ITC for expenses incurred to acquire membership

of club, health and fitness center is also not available for business houses

- ★ ITC for travel expenses incurred for its employee is also not available provided such expenses are incurred to comply with any statute.
- ★ ITC is also not available for expenses (capital in nature) incurred by having “works contract services” from a contractor in relation to the construction, reconstruction, renovation, repair, addition, alteration etc., of immovable property. The immovable property does not include Plant and Machinery.
- ★ However, ITC is available to service provider/ contractor who is engaged in providing taxable “works contract services”.
- ★ ITC not available on expenses incurred for telecommunication towers, pipeline installed outside factory premises

ITC not available for expenses (capital in nature) incurred by a registered person on the purchase of goods and services for construction, re-construction, renovation, repair, addition, alteration of immovable property (other than plant and machine ry) for his business.

- ★ ITC is not available to a composite dealer registered u/s 10 of CGST Act.,2017
- ★ goods or services or both received by a non-resident taxable person except on goods imported by him
- ★ goods or services or both used for personal consumption by a registered person
- ★ goods lost, stolen, destroyed, written- off or disposed of by way of gift or free samples
- ★ any tax paid in accordance with the provisions of sections 74, 129 and 130.

Section 18(2) of the CGST act put restriction of one year to avail ITC in certain cases as liste u/s 18(1)

In spite of all above restrictions under different provisions,



cases of wrongly availing and/or availing ITC by a fraudulent manner are increasing. Fake registrations and/or fake invoicing keep the Government agencies on their toe. Though the Government is using all the latest techniques, including artificial intelligence (IA) to curb the cases but struggling hard.

As per one of the reports, during the financial year, 2020-21, the CGST zones and the Directorate General of GST Intelligence (DGGI) have registered around 8000 cases of fake ITC claims of over Rs. 35000 crores. 426 persons, including 14 professionals, such as CAs, Lawyers and masterminds, beneficiaries, directors, etc., were arrested. It is still going on.

Considering all, the Government has decided to impose further restrictions to avail ITC on normal business transactions. Accordingly, section 38 has been redrafted completely (the old section has been omitted) vide Notification no 18/2022 dt 28/09/2022 and is effective from 01.10.2020.

Though omitted but for ready reference, original section 38 is reproduced as under:

38. Furnishing details of inward supplies.

Every registered person, other than an Input Service Distributor or a non-resident taxable person or a person paying tax under the provisions of section 10 or section 51 or section 52, shall verify, validate, modify or delete, if required, the details relating to outward supplies and credit or debit notes communicated under subsection (1) of section 37 to prepare the details of his inward supplies and credit or debit notes and may include therein, the details of inward supplies and credit or debit notes received by him in respect of such supplies that have not been declared by the supplier under sub-section (1) of section 37.

Every registered person, other than an Input Service Distributor or a non-resident taxable person or a person paying tax under the provisions of section 10 or section 51 or section 52, shall furnish, electronically, the details of inward supplies of taxable goods or services or both, including inward supplies of goods or services or both on which the tax is payable on reverse charge basis under this Act and inward supplies of goods or services or both

taxable under the Integrated Goods and Services Tax Act or on which integrated goods and services tax is payable under section 3 of the Customs Tariff Act, 1975, (51 of 1975) and credit or debit notes

received in respect of such supplies during a tax period after the tenth day but on or before the fifteenth day of the month succeeding the tax period in such form and manner as may be prescribed: Provided that the Commissioner may, for reasons to be recorded in writing, by notification, extend the time limit for furnishing such details for such class of taxable persons as may be specified therein: Provided further that any extension of time limit notified by the Commissioner of State tax or Commissioner of Union territory tax shall be deemed to be notified by the Commissioner.

The details of supplies modified, deleted or included by the recipient and furnished under sub-section (2) shall be communicated to the supplier concerned in such manner and within such time as may be prescribed.

The details of supplies modified, deleted or included by the recipient in the return furnished under subsection (2) or sub-section (4) of section 39 shall be communicated to the supplier concerned in such manner and within such time as may be prescribed.

Any registered person, who has furnished the details under sub-section (2) for any tax period and which have remained unmatched under section 42 or section 43, shall, upon discovery of any error or omission therein, rectify such error or omission in the tax period during which such error or omission is noticed in such manner as may be prescribed, and shall pay the tax and interest, if any, in case there is a short payment of tax on account of such error or omission, in the return to be furnished for such tax period: Provided that no rectification of error or omission in respect of the details furnished under sub-section (2) shall be allowed after furnishing of the return under section 39 for the month of September following the end of the financial year to which such details pertain, or furnishing of the relevant annual return, whichever is earlier.

New Section 38, as redrafted is reproduced:

38. Communication of details of inward supplies and input tax credit.

(1) The details of outward supplies furnished by the

registered persons under sub-section (1) of section 37 and of such other supplies as may be prescribed, and an auto-generated statement containing the details of input tax credit shall be made available electronically to the recipients of such supplies in such form and manner, within such time, and subject to such conditions and restrictions as may be prescribed.

(2) The auto-generated statement under sub-section (1) shall consist of—

(a) details of inward supplies in respect of which credit of input tax may be available to the recipient; and

(b) details of supplies in respect of which such credit cannot be availed, whether wholly or partly, by the recipient, on account of the details of the said supplies being furnished under sub-section (1) of section 37,—

(i) by any registered person within such period of taking registration as may be prescribed; or

(ii) by any registered person, who has defaulted in payment of tax and where such default has continued for such period as may be prescribed; or

(iii) by any registered person, the output tax payable by whom in accordance with the statement of outward supplies furnished by him under the said subsection during such period, as may be prescribed, exceeds the output tax paid by him during the said period by such limit as may be prescribed; or

(iv) by any registered person who, during such period as may be prescribed, has availed credit of input tax of an amount that exceeds the credit that can be availed by him in accordance with clause (a), by such limit as may be prescribed; or

(v) by any registered person, who has defaulted in discharging his tax liability in accordance with the provisions of sub-section (12) of section 49 subject to such conditions and restrictions as may be prescribed; or

by such other class of persons as may be prescribed.

The newly drafted section 38 has been notified and is effective from 01.10.2022, but rules are yet to be notified. So as of now, it will be difficult to say how this section will work and restrict the registered person from availing ITC. However, for the benefit of readers, we summarized section 38 as under:

A summary of section 38:

- ✳ Details of Invoices and Debit Notes as furnished in GSTR-1 and IFF shall be available to the recipient in GSTR-2B (auto-generated statement) with such restrictions and conditions as prescribed,
- ✳ GSTR-2B is divided into two parts, i.e. ITC available and ITC not available or partly available
- ✳ ITC is not available on account of:
 - If supplies have been received from a newly registered person (up to a prescribed time limit)
 - Supplier has defaulted in payment of taxes for a given period of time
 - Taxes paid in GSTR-3B are less than the taxes calculated in GSTR-1 by a prescribed limit
 - Supplies have been received from a supplier who has availed ITC in GSTR-3B more than GSTR-2B by a limit prescribed,
 - Supplier has paid taxes from Credit Ledger more than a prescribed limit
 - Any other notified person

So now, after having section 38 in place, the Government has put more restrictions in addition to section 16 and section 17 conditions/restrictions to avail ITC. The idea is to reduce the cases of fake invoices and availing ITC through fraudulent means.

The probable impact of section 38 on regular business transactions is as under:

- ✳ Government may deny ITC to the recipient of goods and services if such supplies are received from a



registered person who has obtained registration under GST

- ★ six months back or so. In other words, registration of such a supplier is less than six months.
- ★ ITC may be denied if the supplier of such goods and services has defaulted in payment of taxes continuously for a period of three months or so.
- ★ ITC may be denied, if the supplier has paid less tax in his GSTR-3B as compared to liability declared in GSTR-1 for a certain period of time which may be for three months or so. It may be harsh on the recipient as he does not have access to the supplier's workings. It is quite possible that the supplier has done some accounting adjustments while paying his taxes in GSTR-3B.
- ★ Government may deny ITC if the supplier has claimed more ITC in GSTR-3B in comparison to his GSTR-2B for a certain period of time which may be

three or six months. In other words, if ITC availed/ claimed by the supplier in his GSTR-3B is more than the prescribed limit what has been communicated to him in his GSTR-2B.

- ★ ITC can be denied if the supplier has paid his tax liabilities from Electronic Credit Ledger beyond prescribed limits.

Conclusion:

In a total scenario, the Government is going to be tough for ITC benefits. But for any wrong or miscalculated action of the supplier, the recipient will lose his eligible funds. It will, on one side, be against the true spirit of GST laws which talked about the elimination of cascading effects of taxes in the complete supply chain and on the other side will increase the financial burden on the recipient of goods and services. Because of less than one percent of miscreants in the economy, ninety-nine percent of genuine buyers will be hanged for no reason.

TB