

Input Tax Credit availment under the GST Law

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India is heading towards the Goods & Service Tax (GST) regime. The Model GST law, Central / State Goods & Service Tax Act (hereinafter referred to as the GST Act) has been released by the Finance Ministry on 14th June, 2016.

One of the biggest advantages which is expected from the implementation of GST Act is that it would remove cascading effect by facilitating seamless flow of credit. This would be given effect by providing for the availment of Input Tax Credit (ITC) to the purchasing dealer in respect of the tax (GST) paid by the supplying dealer.

Section 16(1) of the GST Act (which is part of Chapter V) provides that subject to the conditions and restrictions as may be prescribed, every taxable person shall be entitled to avail credit of the input tax available to him.

Section 16(11) of the GST Act stipulates conditions to be satisfied for claiming ITC, failing which the credit can be denied to the purchasing dealer. One of the stipulations provided for availing ITC is stated in Section 16(11)(c) of the GST Act wherein it is provided that the purchasing dealer shall not be entitled the credit of the input tax paid by him unless the tax paid by him has been deposited by the supplying dealer to the credit of the appropriate Government.

Sub-section (11) of section 16 reads as under:-

“16 (11) Notwithstanding anything contained in this section, but subject to the provisions of

section 28, no registered taxable person shall be entitled to the credit of any input tax in respect of any supply of goods and/or services to him unless:

(a)

(b)

(c) the tax charged in respect of such supply has been actually paid to the credit of the appropriate Government, either in cash or through utilization of input tax credit admissible in respect of the said supply.....”

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The provision seems to be enacted with the intention to make purchasing dealer more vigilant in their dealings with supplying dealers and thereby ensure compliance by all the dealers in the chain of supply. It seems to be enacted with the intention to prevent dealings in invoices without movement of goods so as to check tax evasion by dealers. However, it may have far reaching ramifications and open a pandora's box of litigation.

Firstly, the provision has the effect of denying credit to a bona fide purchasing dealer even if he has paid GST to the supplying dealer because the tax has not been deposited to the Government exchequer by the latter. This tantamounts to punishing a bona fide person for the fault of some other person. It is a trite law and an accepted principle of natural justice that a person cannot be punished for the fault of another. Such a law would, on the face of it, be against the principles enshrined in Article 14 of the Constitution.

As per Section 7 of the GST Act, the liability to pay tax is on the supplying dealer [unless tax on such supply is notified to be paid on reverse charge basis as per Section 7(3) of the GST Act]. In the event of the supplying dealer not depositing tax to the appropriate Government [whether deliberately or otherwise] after having collected the same from the purchasing dealer, it is the purchasing dealer who suffers on account of the act of the supplying dealer as he would be denied input tax credit. Further, this gives the supplying dealer a window to collect tax from the purchasing dealer and deliberately not pay the same to the Government. Since, the provision is such that the purchasing dealer suffers by being disentitled to ITC, the fraudulent supplying dealer may be let off the hook. Therefore, this provision can also be misused by supplying dealer as he may affect the supply and abscond with the tax collected from the purchasing dealer.

It is stated that the issue whether a bona fide purchasing dealer can be denied credit in case of default of supplying dealer is no longer res-integra. In the case of **M/s Gheru Lal Bal Chand v. State of Haryana & Another [2012 (2) SCC 781 (P&H)]** the Hon'ble Punjab & Haryana High Court considered the provisions of Section 8(3) of the Haryana VAT Act, 2003 (HVAT Act) and the rules framed under the Act. The question before the Court was whether a purchasing dealer can be held liable and denied ITC for input tax which has been recovered from him by the registered selling dealer but has not been paid by the latter to the Government treasury. The Court held that it would be an absurd interpretation of law to read it as one which seeks to penalize a bona fide purchasing dealer and deny him credit and put the defaulting selling dealer in an advantageous position. It is difficult to hold that such a law would be constitutionally valid. The provisions were read down to deny input tax credit only in the event of collusion between the buyer and seller. The Court held as follows:

“In legal jurisprudence, the liability can be fastened on a person who either acts fraudulently or has been a party to the collusion or connivance with the offender. However, law nowhere envisages to impose any penalty either directly or vicariously where a person is not connected with any such event or an act. Law cannot envisage an almost impossible eventuality. The onus upon the assessee gets discharged on production of Form VAT C-4 which is required to be genuine and not thereafter to substantiate its truthfulness by running from pillar to post to collect the material for its authenticity. In the absence of any mala fide intention, connivance or wrongful association of the assessee with the selling dealer or any dealer earlier thereto, no liability can be imposed on the principle of vicarious liability. Law cannot put such onerous responsibility on the assessee otherwise, it would be difficult to hold the law to be valid on the touchstone of articles 14 and 19 of the Constitution of India.....A statute has to be read in such a manner so as to do justice to the parties. If it is held that the person who does not deposit or is required to deposit the tax would be put in an advantageous position and whereas the person who has paid the tax would be worse, the interpretation would give result to an absurdity. Such a construction has to be avoided.....

.....To conclude, no liability can be fastened on the purchasing registered dealer on account of non-payment of tax by the selling registered dealer in the treasury unless it is fraudulent, or collusion or connivance with the registered selling dealer or its predecessors with the purchasing registered dealer is established.”

Further, it would be exorbitantly onerous to require a purchasing dealer to ascertain and ensure that tax has been paid by the supplying dealer to the appropriate Government. This provision tantamounts to fixating the supplying dealer's responsibility of paying tax to the Government exchequer on the purchasing dealer. A purchasing dealer may deal with numerous supplying dealers in the course of business. Further, he may even deal with “casual taxable person” as defined in section 2(21) of the GST Act. Such a dealer is one who occasionally engages in supply of goods or services and does not have a fixed place of business. In such a case, expecting him to trace all the defaulting dealers and ensure they pay tax to the appropriate Government is an impossible task. The law cannot be said to be imposing an onerous condition which is impossible of compliance. The maxim “*lex non cogit ad impossibilia*” meaning the law does not compel a man to do that which he cannot possibly perform, is a well-recognized doctrine in legal jurisprudence. This scenario coupled with the fact that the Court is required to presume the existence of a culpable mental state unless the same has been established beyond reasonable doubt by the accused [as per Section 75 (1) and (2) of the GST Act] makes the situation of the purchasing dealer all the more grave.

It is pertinent to note that Section 29A (3) of the GST Act provides that where the ITC claimed by a recipient [purchasing dealer] in respect of inward supply is in excess of tax declared by the supplier for

the same supply or the outward supply is not declared by the supplier in his valid returns, the discrepancy shall be communicated to both the persons. The said subsection is reproduced below:

“ Where the input tax credit claimed by a recipient in respect of an inward supply is in excess of the tax declared by the supplier for the same supply or the outward supply is not declared by the supplier in his valid returns, the discrepancy shall be communicated to both such persons in the manner as may be prescribed.”

Section 29(7) of the GST Act further provides that the recipient / purchasing dealer shall be entitled to reduce from his output tax liability the amount which has been subsequently declared by the supplying dealer. This again leads to a situation where the recipient / purchasing dealer is dependent on the declarations made by the supplying dealer and if the output tax is not paid / declared or incorrectly paid /declared by the latter, then the same unfairly prejudices the purchasing dealer as it results in denial of credit to him.

As of now, the law does not seem to provide for any measures which will compel the Department to take the necessary measures to recover the tax collected by the supplying dealers but not deposited the Government exchequer. However, even if such measures are provided, the effectiveness of such measures may be highly questionable. There is great likelihood that the Department would lack the initiative to chase the defaulting supplying dealers as the said tax has already been recovered albeit from the bona fide purchasing dealer by way of denying him the ITC.