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Gujarat High Court allows GST refund of input services under inverted duty structure

“Net input tax credit” for the purpose of GST refund under inverted duty structure, apart from inputs, includes refund of input services as well

Facts of the case:

- VKC Footsteps India Pvt. Ltd.¹ (Petitioner) was engaged in the business of manufacture and supply of footwear which is taxable under GST at 5%
- Inputs such as synthetic leather, polyurethane polyol, etc., and input services such as job work service, goods transport agency service etc., were procured in the course of business operations. Majority of these inputs and input services were taxable under GST at 12% or 18%
- Since the GST rate applicable on procurements was more than the GST rate on outward supply of footwear, input tax credit (ITC) was accumulated. Such situation is termed as inverted duty structure
- The Central Goods and Services Tax Act, 2017 (CGST Act) provides that refund of accumulated ITC is allowed under inverted duty structure
- The Central Goods and Services Tax Rules, 2017 (CGST Rules), which prescribe the procedure for refund under inverted duty structure, provide that in such a case, refund of only “inputs” is allowed. Refund of “input services” cannot be granted under this option
- The petitioner approached the Gujarat High Court challenging the constitutional validity of the provisions of the CGST Rules which exclude the refund of input services under inverted duty structure

Submissions of the petitioner:

The petitioner, while referring to the provisions of the GST law, discussion paper on GST released by the government and the international VAT/GST Guidelines (OECD guidelines), made the following submissions:

- The petitioner submitted that the provisions contained in the CGST Act provide that refund of accumulated ITC is allowed in certain specified cases. Further, ITC included credit availed on both inputs as well as input services
- The explanation inserted in the CGST Rules which prescribe that refund of only inputs would be allowed in case of refund under inverted duty structure is *ultra-vires* the provisions of the CGST Act

¹ R/Special Civil Application No. 2792 of 2019

which provide that the refund of entire accumulated ITC (consisting of inputs and input services) would be granted

- There are plethora of judgments which support the fact that the procedure laid down in the Rules cannot override the provisions of the Act and hence, the explanation provided in the CGST Rules is constitutionally invalid

Submissions of the Revenue:

- The Revenue submitted that the relevant Rules only provide the mode of calculation of refund available to the assessee on account of inverted duty structure and are not contrary to the provisions of the CGST Act
- The CGST Rules were framed by the government for effective implementation of the CGST Act. These powers were conferred upon under the CGST Act
- Hence, the provision prescribing the method of calculating the refund on account of inverted duty structure cannot be held to be ultra-vires the CGST Act

Judgment of the High Court:

- Based on a reading of the provisions of CGST Act, read with the CGST Rules, the definition of “input tax credit” includes credit of inputs as well as input services
- The intent of the law is not to deny the refund of input services as a part of accumulated ITC. Circular No. 79/53/2018 - GST dated 31 December 2018, which *inter-alia* clarified the calculation of refund amount for refund of accumulated ITC under inverted duty structure was held to be incorrect
- The provisions of CGST Rules, restricting the refund of input services in case of refund under inverted duty structure, was held to be ultra-vires the provisions of CGST Act

Our comments:

The judgment of the Gujarat High Court provides a major relief to taxpayers who had ITC of input services remaining unutilised due to inverted duty structure. Businesses would have to analyse the eligibility to claim refund on the accumulation of ITC on input services in cases of inverted duty structure.

It is likely that the Department would go in appeal to Supreme Court on this matter.

It is also important to note that the court has given a reasoned judgment, based on which the request of the Revenue to stay the operation, implementation and execution of the judgment, was also denied.

The judgment would also give a guiding principle in similar matters pending before other judicial forums (Madras High Court, Bombay High Court, and Rajasthan High Court) as well.



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