Gujarat HC allows refund of input services under inverted duty structure

Ruling to benefit companies, mainly e-comm firms, which are facing blocked credit

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The Gujarat High Court has upheld an assessee’s right to claim refund for input services under inverted duty structure under the Goods and Services Tax (GST). This ruling holds significance for many companies, particularly e-commerce ones, that are facing blocked credit due to the existing rules.

Inverted duty structure means higher duty on raw materials (inputs) and lower duty on final products (output). Several products such as furniture and footwear have inverted duty structure. Though there are provisions for refunds, companies often face difficulties in claiming full refund due to complex rules. The July 24 order came in a case filed by VKC Footsteps, a Gujarat-based firm engaged in the manufacture and supply of footwear.

Revised formula
The crux of this matter is the tax department’s revised formula for computing the refund on account of inverted duty structure, notified on June 13, 2018, and given with retrospective effect from July 1, 2017. The revised formula excluded input services from the scope of ‘net input tax credit’ for computation of the refund amount under the rule. Thus, the substituted rule (89(5) of the CGST Rules, 2017) denied refund on the input tax credit availed on input services and allowed relief of refund of input tax credit availed on inputs alone.

In the present case, the court noted, “tax department are allowing refund of accumulated input tax credit of tax paid on inputs such as synthetic leather, PU polyol, etc to the petitioner. However, refund of accumulated credit of tax paid on procurement of input services such as job work service, goods transport agency service, etc is being denied.”

After hearing the arguments, the Court read down Explanation (a) to the Rule 89(5) to the extent that it denies refund of ITC relating to input services (by defining ‘net ITC’ to mean input tax credit availed on inputs only) in case of inverted duty structure. It said that such an explanation is contrary to the provision (section 54(3) of the CGST Act) under the law.

‘Input tax’
It inferred that the provision under the law (Section 7 of the CGST Act, 2017), dealing with ‘scope of supply’ includes all forms of supply of goods or services. Further, ‘input tax’ as defined in law means the tax charged on any supply of goods or services or both made to any registered person. Thus, it explained ‘input’ and ‘input service’ are both part of the ‘input tax’ and ‘input tax credit’ and “therefore, by way of Rule 89(5) of the CGST Rules, 2017, such claim of the refund cannot be restricted only to ‘input’ excluding the ‘input services’ from the purview of ‘input tax credit’.”

According to Harpreet Singh, Partner at KPMG, the ruling once again endorses the interpretation that a subordinate legislation cannot go beyond the ambit and realm of the main enactment. “A lot of companies, especially e-commerce firms, were suffering on account of blocked credits for input services. They may now consider analysing the ruling in detail and see if the benefit of the same can be availed of in their case,” he said.