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# Treading the GST Path – XXXI

## ITC on Capital Goods & Rule 43



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Under the erstwhile Cenvat Credit Rules, 2004, Rule 6 of the said Rules, dealing with a manufacturer manufacturing both dutiable and exempted goods and service provider providing taxable and exempted services, did not apply to capital goods. But, under Rule 43 of the CGST Rules, 2017, the concept of proportionate disallowance of Input Tax Credit (ITC) for use in exempt supply is made applicable for capital goods also. Let us see how it works.

To the extent capital goods are used for any non business purposes or for making any exempt supplies, ITC is not entitled.

If any capital goods are exclusively used for any non business purposes or for effecting any exempt supplies, ITC is not entitled and no credit would be credited to Electronic Credit Ledger. {Rule 43 (1) (a)}

If any capital goods are exclusively used for effecting taxable supplies / zero rated supplies (Exports and supplies to SEZ), ITC is entitled in full and such credit would be credited to the Electronic Credit Ledger. {Rule 43 (1) (b)}

ITC in respect of capital goods, other than those covered under clauses (a) and (b) of sub rule (1) of Rule 43, i.e. capital goods which are commonly used for non business purposes and / or effecting exempt supplies on the one hand and taxable supplies and / or zero rated supplies on the other hand shall be entitled to the extent of their use in effecting taxable supplies / zero rated supplies. The ITC on such common capital goods, shall first be credited to the Electronic Credit Ledger. Let us assume that in the month of July 2017, certain common capital goods have been purchased and the ITC thereon is Rs.1,20,000, which would be credited to the Electronic Credit Ledger.

If any capital goods are exclusively used only for non business purposes or for effecting only exempt supplies and hence no ITC was availed, were subsequently started being used for effecting taxable supplies also, then the following procedure should be followed. It may be noted that if the GST paid on such capital goods has already been capitalised and depreciation claimed for such value, then no ITC can be taken for such capital goods. Assuming that no depreciation benefit has been claimed for the GST paid on such capital goods, let us assume that certain capital goods were purchased in July 2017, on payment of GST of Rs.50,000. The capital goods were used only for effecting exempt supplies until January 2017 and only from 15<sup>th</sup> January 2018, the capital goods were started being used for effecting taxable supplies also. It may be noted that for 3 quarters or part there of (July 17 to Sep 17; Oct 17 to Dec 17; and part of Jan 18), the capital goods were used exclusively for effecting exempt supplies. So ITC to an extent of 5 % of the GST paid, per quarter or part of thereof is not entitled, i.e. Rs.50,000 x 5 % x 3 = 7,500. The balance credit of Rs.42,500 can be availed in January 2018. {Rule 43 (1) (c)}.

If certain capital goods were initially used exclusively for effecting taxable supplies and hence full ITC has been availed. But subsequently, the assessee has started using the said capital goods even for effecting exempt supplies also. In such case, after reducing 5 % of the ITC originally availed for every quarter or part thereof for the period from the date of original availment of ITC and the date on which the capital goods has been started to be used commonly, the balance ITC should be considered as common credit.

Useful life of common capital goods shall be presumed as 60 months. In other words, one sixtieth of the total credit availed on common capital goods would be considered as the credit availed per month. The proportion of ineligible credit out of such one sixtieth amount shall be calculated with reference to value of exempt supply and total supply (taxable supply and exempted supply) in each month.

The above exercise has to be undertaken individually for CGST, SGST and IGST.

The following example would help in understanding the provisions.

S.No.	Details	Jan 18	Feb 18	Mar 18	Remarks
1	Total GST paid on capital goods purchases during the month	Rs.2,40,000	Rs.3,00,000	Rs.1,20,000	
2	Out of (1) above, GST on capital goods, which are exclusively used in effecting exempt supplies	Rs.12,000	Rs.15,000	Rs.12,000	ITC is not entitled for these items.
3	Out of (2) above, GST on capital goods, which are exclusively used in effecting taxable supplies and zero rated supplies	Rs.18,000	Rs.15,000	Rs.12,000	Full ITC is entitled for these items.
4	GST paid on Capital goods purchased in July 2017, which were used only in effecting exempt supplies (and hence no ITC availed), but started to be used in effecting taxable supplies also, from the Month of March 2018				Rs.30,000
5	GST paid on Capital goods purchased in July 2017, which were used only in effecting taxable supplies (and hence full ITC				Rs.15,000

	availed), but started to be used in effecting both exempted and taxable supplies, from the Month of March 2018				
6	Value of exempt supply made in the month	Rs.50,00,000	Rs.60,00,000	Rs.75,00,000	
7	Value of taxable supplies and zero rated supplies made in the month	Rs.1,50,00,000	Rs.2,40,00,000	Rs.1,25,00,000	
8	ITC in respect of common capital goods, received in the month (1) - (2) - (3)	Rs.2,10,000	Rs.2,70,000	Rs.96,000	Credited to Electronic Credit Ledger as per Rule 43 (1) (c). Tc
8.1	Addition to common capital goods (4)			Rs.25,500	Rs.30,000 - 15 % for three quarters
8.2	Addition to common capital goods (5)			Rs.12,750	Rs.15,000 - 15 % for three quarters
8.3	Total Common Credit	Rs.2,10,000	Rs.2,70,000	Rs.1,34,250	
10	Cumulative common capital goods credit	Rs.2,10,000	Rs.4,80,000	Rs.6,14,250	
11	Common credit for the month	RS.3,500	Rs.8,000	Rs.10,238	Common credit divided by 60
12	Credit attributable to use of capital goods in effecting exempt supply	Rs.3,500 X Rs.50,00,000 / Rs.2,00,00,000 = Rs.875	Rs.8,000 X Rs.60,00,000 / Rs.3,00,00,000 = Rs.1,600	Rs.10,238 X RS.75,00,000 / Rs.2,00,00,000 = Rs.3,839	This has to be added to the output tax liability for the month
13	Net ITC availed in the month	Rs.2,27,125	Rs.2,83,400	Rs.1,42,411	(3) + (8.3) - (12)

It may be noted that the common credit of Rs.2,10,000 availed in July 2017, shall form part of the common credit and subjected to proportionate disallowance for the next 60 months, i.e. upto June 2022. From July 2022 onwards Rs.2,10,000 shall not form part of the common credit. Similarly the common credit availed in August 2017, i.e. Rs.2,70,000 shall form part of the common credit and subjected to proportionate disallowance for the next 60 months, i.e. upto July 2022. From August 2022 onwards Rs.2,70,000 shall not form part of the common credit.

Though the above exercise seems to be highly complicated, since the same would be done automatically in the GSTR 2 return based on the information furnished, this may not pose much of difficulty in compliance.

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