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Treading the GST Path – XXI

Rule 7 of ITC Rules.



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Present Rule 6 of the Cenvat Credit Rules, 2004 deals with a situation where a manufacturer is manufacturing both dutiable and exempted goods or a service provider providing both taxable and exempted service and hence it becomes necessary to determine the proportion of eligible cenvat credit admissible out of the common credits. Similar provisions are incorporated in Rule 7 of the GST ITC Rules (Draft), which appear to be more cumbersome than the present Rule 6 of the CCR, 2004. But one solace is that in GST era, the instances of exemptions would be highly limited and hence the application of this Rule 7 also would be limited. Further, the operation of this rule would mostly be automated though the requirement of human intervention in identifying the nature of various credits is not ruled out.

The basic facts and principles behind Rule 7 may be noted to understand it better.

It may be noted that when all suppliers correctly upload the details of their outward supplies, the Electronic Credit Ledger (ECL) of the recipient would exhibit all his inward supplies and corresponding Input Tax Credit (T).

But at this stage, the eligibility or otherwise of the credit has not been determined.

At the first level, the following invoices have to be identified and credit pertaining to such invoices should be eliminated from the ECL.

- i) Goods and services, exclusively used for non business purposes (T1).
- ii) Goods and services, exclusively used for making exempted supplies (T2).
- iii) Goods and services, for which credit is not allowed under Section 17 (5) (T3).

The balance credit would represent the total eligible credit (C1) , from which the ineligible portion pertaining to exempted supplies has to be identified.

Next step would be identifying those invoices, where the goods and services are used exclusively for making taxable supplies and zero rated supplies. This credit is fully entitled (T4).

(C1) – (T4) would be the common credit and denoted as C2

The proportion of value of exempted supplies to total turnover in every month, shall be applied to the common credit and this would represent the ineligible credit for that month. This should be added to the output tax liability of the month. In any month, if there is either no exempted supplies or no turnover, the previous month figures can be taken.

Credit attributable to exempt supplies $D1 = C2 * E/F$.

C2 = Common Credit.

E = Value of exempt supplies in the tax period.

F – Total turnover for the tax period.

D1 should be added to the output tax liability of the tax period.

Credit pertaining to goods and services used for non business purposes is to be taken as 5 % of the total common credit and the same shall also be added to the output tax liability (**D2**).

Once the financial year is over, the same exercise has to be done with reference to the value of exempted supplies and total turnover pertaining to the whole financial year. If the ineligible credit thus calculated at the year end is more than the amount already added to output tax liability every month, the differential amount has to be paid, before September. Interest has to be paid from 1st April of succeeding year till the date of payment. For example, for the year 2017-18, the final calculation has to be made and the shortage if any has to be paid before September 2018 and interest on the shortage has to be paid from 01.04.2018 to the date of payment of the shortage.

If the amount added to output tax liability every month exceeds the amount calculated for the whole year, the additional amount paid has to be claimed back as credit not later than September in the next financial year.

The below sample calculation would further explain the application of Rule 7



