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THE STORY OF INVERTED RATE REFUND.

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One Nation, One Tax is the tagline of GST, but in real sense, it is very difficult to have a single rate of GST for all goods and services, especially in a country like India, which is fraught with diversities. GST is often described as a "destination based consumption tax", which simply means that the ultimate burden of tax would only be on the consumer and till such time all intermediaries act only as a pass through. To effectuate this, the taxes paid in anterior stages is allowed as "credit" to be set off against the tax payable at the posterior stage.

It may so happen that in some cases, the rate of tax payable by a supplier on the supplies (goods or services or both) made by him, would be less than the rate of tax applicable on the inputs and input services received by him. This will lead accumulation of input tax credit (ITC) and defeat the very purpose of value added tax regime.

GST law provides for refund of such ITC accumulating on account of the rate of tax on "inputs" being higher than the rate of tax on the outward supplies. The moot question was, once any of the inputs is having a rate of tax higher than the rate of tax on outward supply, whether the refund would be limited only to the ITC accumulating on account of inputs or the ITC accumulating on account of input services would also be eligible for refund.

On this vexed question, two High Courts have held contrary view, Gujarat High Court, favouring the taxpayers and holding refund of credit accumulating on account of input services is also entitled for refund whereas the Madras High Court, holding otherwise. Thus the matter was before the Hon'ble Supreme Court.

Various arguments were put forth before the Supreme Court, such as, input and input services shall be treated equally; the term "Inputs" should cover "input services" also; denial of refund of input tax credit on input services is against the fundamental principles of GST; the retrospective amendment carried out in this regard to Rule 89 (5) of the GST Rules, is contrary to Section 54 of the Act, etc.

The Supreme Court has given categorical findings on all these issues and concluded that it is the policy decision of the Government to grant refund of ITC accumulating on account of inverted rate structure, only in respect of inputs and the Court cannot enter into the realm of policy making and direct sanction of refund for input services also.

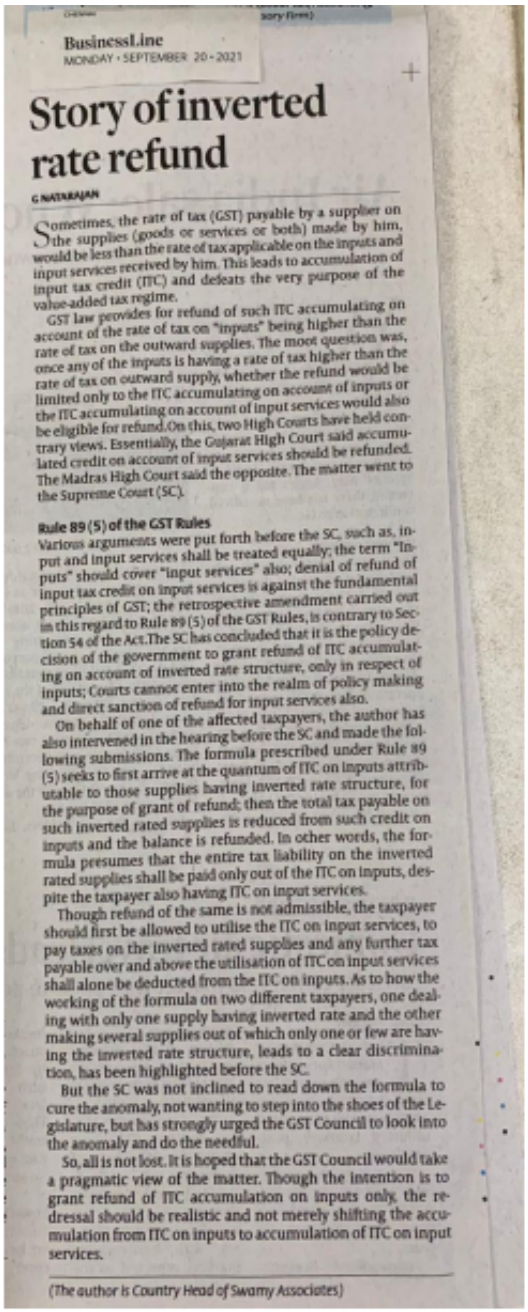
On behalf of one of the affected taxpayers, the author has also intervened in the hearing before the Supreme Court and made the following submissions. The formula prescribed under Rule 89 (5) seeks to first arrive at the quantum of ITC on inputs attributable to those supplies having inverted rate structure, for the purpose of grant of refund; then the total tax payable on such inverted rated supplies is reduced from such credit on inputs and the balance is refunded. In other words, the formula presumes that the entire tax liability on the inverted rated supplies shall be paid only out of the ITC on inputs, despite the taxpayer is also having ITC on input services. Though refund of the same is not admissible, the taxpayer should first be allowed to utilise the ITC on input services, to pay

taxes on the inverted rated supplies and any further tax payable over and above the utilisation of ITC on input services shall alone be deducted from the ITC on inputs. As to how the working of the formula on two different taxpayers, one dealing with only one supply having inverted rate and the other making several supplies out of which only one or few are having the inverted rate structure, leads to a clear discrimination, has been highlighted before the Supreme Court. The example given in this regard is also reproduced in para 97 of the judgement.

As can be seen from para 101 and 102 of the judgement, the above anomalies in the working of the formula have not been refuted by the Union Government.

But, the Supreme Court was not inclined to read down the formula to cure the anomaly and has felt that any move by the Court to recraft the formula would amount to the Court stepping into the shoes of the legislature and executive and avoided the same. However, the Court strongly urged the GST Council to look into the anomaly and do the needful.

So, it is not all is lost and still some hope is left. It is hoped that the GST Council should take a pragmatic view of the matter. Though the intention is to grant refund of ITC accumulation on inputs only, the redressal should be realistic and not merely shifting the accumulation from ITC on inputs to accumulation of ITC on input services.



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Story of inverted rate refund

G NATARAJAN

Sometimes, the rate of tax (GST) payable by a supplier on the supplies (goods or services or both) made by him, would be less than the rate of tax applicable on the inputs and input services received by him. This leads to accumulation of input tax credit (ITC) and defeats the very purpose of the value-added tax regime.

GST law provides for refund of such ITC accumulating on account of the rate of tax on "inputs" being higher than the rate of tax on the outward supplies. The moot question was, once any of the inputs is having a rate of tax higher than the rate of tax on outward supply, whether the refund would be limited only to the ITC accumulating on account of inputs or the ITC accumulating on account of input services would also be eligible for refund. On this, two High Courts have held contrary views. Essentially, the Gujarat High Court said accumulated credit on account of input services should be refunded. The Madras High Court said the opposite. The matter went to the Supreme Court (SC).

Rule 89 (5) of the GST Rules

Various arguments were put forth before the SC, such as, input and input services shall be treated equally; the term "Inputs" should cover "input services" also; denial of refund of input tax credit on input services is against the fundamental principles of GST; the retrospective amendment carried out in this regard to Rule 89 (5) of the GST Rules, is contrary to Section 54 of the Act. The SC has concluded that it is the policy decision of the government to grant refund of ITC accumulating on account of inverted rate structure, only in respect of inputs; Courts cannot enter into the realm of policy making and direct sanction of refund for input services also.

On behalf of one of the affected taxpayers, the author has also intervened in the hearing before the SC and made the following submissions. The formula prescribed under Rule 89 (5) seeks to first arrive at the quantum of ITC on inputs attributable to those supplies having inverted rate structure, for the purpose of grant of refund; then the total tax payable on such inverted rated supplies is reduced from such credit on inputs and the balance is refunded. In other words, the formula presumes that the entire tax liability on the inverted rated supplies shall be paid only out of the ITC on inputs, despite the taxpayer also having ITC on input services.

Though refund of the same is not admissible, the taxpayer should first be allowed to utilise the ITC on input services, to pay taxes on the inverted rated supplies and any further tax payable over and above the utilisation of ITC on input services shall alone be deducted from the ITC on inputs. As to how the working of the formula on two different taxpayers, one dealing with only one supply having inverted rate and the other making several supplies out of which only one or few are having the inverted rate structure, leads to a clear discrimination, has been highlighted before the SC.

But the SC was not inclined to read down the formula to cure the anomaly, not wanting to step into the shoes of the Legislature, but has strongly urged the GST Council to look into the anomaly and do the needful.

So, all is not lost. It is hoped that the GST Council would take a pragmatic view of the matter. Though the intention is to grant refund of ITC accumulation on inputs only, the redressal should be realistic and not merely shifting the accumulation from ITC on inputs to accumulation of ITC on input services.

(The author is Country Head of Swamy Associates)