

## ITC - Around the World of GST in 180 Days: By Adv. K Vaitheeswaran

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The entire business community in GST is concerned with one provision namely the second proviso to Section 16(2) of the CGST Act, 2017. Section 16 deals with eligibility and conditions for taking input tax credit and Section 16(2) deals with the conditions for entitlement of credit. The 180 days condition flows through the second proviso to Section 16(2). The proviso reads as under:

*"Where a recipient fails to pay the supplier of goods or services or both, other than the supplies on which tax is payable on reverse charge basis, the amounts towards the value of supply alongwith the tax payable thereon within 180 days from the date of issue of invoice by the supplier, an amount equal to the input tax credit availed by the recipient shall be added to his output tax liability alongwith interest thereon in such manner as may be prescribed."*

#### **Two Sides of the Same Coin**

The GST statute mandates payment of GST by the supplier on a mercantile basis through various provisions such as time of supply and is not bothered about the inability of the supplier to realise the proceeds for supply of goods or services. A supplier who has charged GST is required to pay the GST by the due dates even though he is not in a position to realise the sale price or even the GST portion. When the Government is clear that it needs its taxes based on mercantile system, the proviso itself is contradictory since it brings in a payment basis system for availment of credit.

Sale and purchase are two sides of the same coin. The Supreme Court in the case of ***EID Parry Vs. ACCT (2000) 117 STC 457*** has held that amounts paid by the purchaser to the seller of goods in pursuance of the contract of sale can legitimately be regarded as purchase price while calculating turnover.

If the supplier is required to pay GST as soon as invoice is raised, then the recipient should be able to enjoy the GST charged as soon as the goods / services are received and the conditions in Section 16(2) are met. The requirement in terms of the second proviso to Section 16(2) for failure to pay the value of supply and GST is completely contradictory to the entire Scheme.

Viewed from another perspective, the supplier is required to pay the GST as soon as invoice is raised and one of the conditions in Section 16(2) for eligibility of credit in the hands of the recipient is the payment of GST by the supplier to the Government Account. Without entering into the debate as to the onerous nature of this condition, assuming a supplier has paid the GST, there is no justification whatsoever for denying ITC to the recipient under any circumstance. Therefore, in effect, the second proviso results in double taxation through the denial of input tax credit.

#### **What is 'Fails to Pay'?**

Covid - 19 has changed the business world and the business community is slowly recovering from the impact of the lockdown and loss of business. Some businesses are still under lockdown and on account of the pandemic and risks associated with it, business is still not as usual. Therefore, it is quite common for delay in realisation or requests for extension of time for payment of invoices or for renegotiation of credit period or for having a credit period or commercial terms which is more than 6 months. For example, where the payment itself is not due as per the commercial agreement or the invoice is payable say 9 months from the date of invoice, it cannot be said that *the recipient has failed to pay the supplier the value and the tax portion*.

Assuming there is delay in payment can it be said that there is 'failure to pay'? Failure and default are synonymous terms [***Dhan Singh Ram Krishna Chaudhri Vs. Laxmi Narayan Ramkishan (AIR 1974 SC 1613)***]. Failure connotes that there is an obligation which has not been carried out. If there was no

obligation then there is no failure was the view of the Bombay High Court in the case of **Panna Lal Nand Lal Bhandari Vs. CIT (1956) 30 ITR 57**.

### **No Mechanism for Implementation of Second Proviso to Section 16(2)**

Section 2(87) of the CGST Act, 2017 defines 'prescribed' to mean prescribed by Rules under the Act on the recommendation of the Council. While the proviso refers to the requirement of payment, the procedure is through the Rules and Rule 37 of the CGST Rules, 2017 comes into the picture.

Rule 37 of the CGST Rules, 2017 is titled as 'reversal of input tax credit in case of non-payment of consideration' and reads as under:

*(1) A registered person, who has availed input tax credit on any inward supply of goods or services or both, but fails to pay to the supplier thereof, the value of such supply along with the tax payable thereon within the time limit specified in the second proviso to sub-Section (2) of Section 16, shall furnish the details of such supply, the amount of value not paid to the supplier in Form GSTR - 2 for the month immediately following the period of 180 days from the date of issue of invoice.*

*Provided that the value of supplies made without consideration as specified in Schedule I of the said Act shall be deemed to have been paid for the purpose of the second proviso to sub-Section (2) of Section 16.*

*Provided further that the value of supplies on account of any amount added in accordance with the provisions of clause (b) of sub-Section (2) of Section 15 shall be deemed to have been paid for the purposes of the second proviso to sub-Section (2) of Section 16.*

*(2) The amount of input tax credit referred to in sub-rule (1) shall be added to the output tax liability of the registered person for the month in which the details are furnished.*

*(3) The registered person shall be liable to pay interest at the rate notified under sub-Section (1) of Section 50 for the period starting from the date of availing credit on such supplies till the date when the amount added to the output tax liability as mentioned in sub-rule (2), is paid.*

*(4) The time limit specified in sub-Section (4) of Section 16 shall not apply to a claim for reavailing of any credit, in accordance with the provisions of the Act or the provisions of this Chapter, that had been reversed earlier.*

### **Rule 37 itself cannot be complied with for the following reasons:**

(i) The second proviso to Section 16(2) of the CGST Act, 2017 provides that the recipient should add an amount equal to the ITC to his output tax liability along with interest in the manner as may be prescribed.

(ii) Rule 37 of the CGST Rules, 2017 expressly refers to the second proviso to Section 16(2) and thus the second proviso to Section 16(2) and Rule 37 are an integrated mechanism.

(iii) Rule 37 requires the recipient to furnish the details of such supply; amount of value not paid; amount of ITC availed of proportionate to such amount not paid to the supplier in **Form GSTR -2** for the month immediately following the period of 180 days from the date of issue of invoice.

(iv) GSTR -2 has been kept in abeyance and in the absence of a computation mechanism or a procedure to implement a provision, the provision would fail. As there is no mechanism for reversal of ITC as specified in terms of Rule 37, the requirement to reverse ITC cannot be mandated.

(v) In terms of the decision of the Supreme Court in **CIT Vs. B.C. Srinivasa Setty (1981) 128 ITR 294 (SC)** where computation fails, levy fails. Therefore, if the law has not provided for a mechanism to implement the provision, then the provision fails.

(vi) By now it is settled principle of law that when a law requires a particular thing to be done, in a particular manner, it has to be done in that manner alone and not at all. Reference could be made to the judgment of the Apex Court in the case of **Dhanajaya Reddy Vs. State of Karnataka reported in (2001) 4 SCC 9**

### **Applicability of Interest**

Without prejudice to the above, a question that can arise is in the context of applicability of interest when there is no loss of revenue. There is no loss of revenue to the Government when the GST has been

discharged by the supplier. The Supreme Court in the case of ***Pratibha Processors Vs. Union of India (1997) 88 ELT 12*** has held that levy of interest is geared to the actual amount of tax withheld and the extent of delay in paying the tax on the due date. Essentially it is compensatory and different from penalty. The Supreme Court in the case of ***State of Karnataka Vs. Karnataka Pawn Brokers Association (2018) 6 SCC 363*** has held that interest is basically compensation for the use or retention of money.

Further, Rule 37(3) of the CGST Rules, 2017 refers to interest at the rate notified under Section 50(1) for the period starting from the date of availment of credit till the date when the amount is added to the output tax liability as mentioned in Rule 37(2) is paid. Thus, Rule 37(3) is also connected with Rule 37(2) and suffers from the vice of GSTR -2 not being operational.

### **Way Forward**

Section 10A of the Insolvency and Bankruptcy Code, 2016 provides for a suspension in respect of defaults which have occurred on or after 25.03.2020. The suspension is applicable for a period of six months from 25.03.2020. The central government has the power to extend the suspension upto a period of one year. Further, the proviso to the newly inserted Section 10A states clearly that no application for initiation of insolvency proceedings shall ever be initiated for defaults that have occurred during the suspension period.

The Reserve Bank of India permitted moratorium on instalments on term loans. Various time limits under direct and indirect tax statutes were extended through the ordinance and subsequently through legislation. The time limit for realization of export proceeds was extended by RBI. When a number of measures have been initiated taking into account the impact of Covid-19, in the context of input tax credit, the GST Council should immediately take steps to either delete the second proviso to Section 16(2) or suspend its operations so that businesses who are struggling with cash flow issues are not further saddled with loss of input tax credit.