

# INPUT TAX CREDIT UNDER GST



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## Introduction

A smooth and consecutive chain of Input Tax Credit (ITC) is one of the important constituent of a good and simple tax system and Goods and Services Tax (GST) is the perfect example of such tax system. The system of charging 'tax on tax' can only be avoided with the mechanism of ITC. Under GST system the entire supply chain is subject to GST which will be levied by Central and state government respectively and the credit of the same taxes paid at every stage can be availed as set off in the subsequent stage.

The system of cascading effect can be understood with the help of following mentioned points:-

- a) The Central Excise duty paid on input for manufacturing of final products can be availed as credit for payment of Central Excise duty on final product.
- b) Let us take an example of manufacture of bicycle which requires seat, tire valve, tire, pedal, handlebars, brake cable head tube etc. Central Excise duty is paid on these inputs at the time of purchase and the final product i.e. bicycle is also chargeable to Central Excise duty.
- c) Let us assume that the cost of above input is Re. 100/- on which Central Excise duty is payable @ 10% means Rs. 10/- and the final cost of bicycle is Rs. 200/- and the Central excise duty payable on bicycle @ 10% is Rs. 20/-. Now the duty paid of Rs. 10/- on input can be adjusted against duty payable on cycle (output) and the final duty payable through cash is Rs. 10/-only. The final cost of bicycle will now become Rs. 220/-(Rs.200+ Rs.20).
- d) In effect we can say that the duty becomes payable on value added over and above the cost of input.
- e) Under the old scheme the manufacturer cannot take credit of Central Excise duty paid on bicycle for payment of VAT at the time of Intra-state sales. Hence now the VAT is payable on Rs. 220/. So we can say that there is a cascading effect of tax on tax as VAT is payable not only on Rs. 200 but also on Rs. 20.

Goods and Services Tax (GST) would mitigate such cascading of taxes. Under this new system, most of the

indirect taxes levied by Central and the State Governments on supply of goods or services or both, would be combined together under a single levy. GST is a value-added tax levied at all points in the supply chain, with credit allowed for any tax paid on input acquired for use in making the supply. It would apply to both goods and services in a comprehensive manner, with exemptions restricted to a minimum.

The major taxes/levies which are going to be clubbed together or subsumed in the GST regime are as under:-

### Centre Taxes

- Central Excise duty
- Additional duties of excise
- Excise duty levied under Medicinal & Toilets Preparation Act
- Additional duties of customs (CVD & SAD)
- Service Tax
- Surcharges & Cesses

### State Taxes

- State VAT/Sales Tax
- Central Sales Tax
- Purchase Tax
- Entertainment Tax (other than those levied by local bodies)
- Luxury Tax
- Entry Tax (All forms)
- Taxes on lottery, betting & gambling
- Surcharges & Cesses

Let us discuss the treatment of the above mentioned example under GST:-

The input purchased for manufacture of bicycle is treated as inward supply under GST. The cost of input for the manufacture of bicycle is Rs. 100/- and GST paid on the same @ 10% is Rs. Rs. 10/- and the final cost of bicycle is Rs. 200 and GST on the same at the time of sale by the manufacturer to dealer is Rs. 20 (@ 10% of Rs. 200). The GST paid on input can be taken as credit and GST payable through cash is Rs.10/-(Rs.20-Rs.10).

Now the final cost of cycle will be Rs.220/- for the dealer. If the dealer sales the same to the customer by charging a margin of Rs. 100/- then GST will be payable on Rs.300/-. Not on Rs. 320/-. So the amount of GST payable by the consumer is Rs. 30/- (@ 10% of Rs. 300). And the final burden of GST on consumer is only 10%.

From the above example we can say that there is no cascading effect under GST.

## GST comprises of the following levies

- a) Central Goods and Services Tax (CGST) [also known as Central Tax] on intra-state or intra-union territory without legislature supply of goods or services or both.
- b) State Goods and Services Tax (SGST) [also known as State Tax] on intra-state supply of goods or services or both.
- c) Union Territory Goods and Services Tax (UTGST) [also known as Union territory Tax] on intra-union territory supply of goods or services or both.
- d) Integrated Goods and Services Tax (IGST) [also known as Integrated Tax] on inter-state supply of goods or services or both. In case of import of goods also, the present levy of Countervailing Duty (CVD) and Special Additional Duty (SAD) would be replaced by integrated tax.

## The protocols to avail and utilize the credit of these taxes

| Credit of  | To be utilised for the payment of | May be utilised further for ment of |
|------------|-----------------------------------|-------------------------------------|
| CGST       | CGST                              | IGST                                |
| SGST/UTGST | SGST/UTGST                        | IGST                                |
| IGST       | IGST                              | CGST, then SGST/UTGST               |

Credit of CGST cannot be used for payment of SGST/UTGST and credit of SGST/UTGST cannot be utilised for payment of CGST.

## Some technical aspects of the Scheme of Input Tax Credit

- A. Any registered person can avail credit of tax paid on the inward supply of goods or services or both, which is used or intended to be used in the course or furtherance of business.
- B. The pre-requisites for availing credit by registered person are:
  - a) He is in possession of tax invoice or any other specified tax-paying document.
  - b) He has received the goods or services. "Bill to ship" scenarios also included.
  - c) Tax is actually paid by the supplier.
  - d) He has furnished the return.
  - e) If the inputs are received in lots, he will be eligible to avail the credit only when the last lot of the inputs is received.
  - f) He should pay to the supplier, the value of the goods or services along with the tax within 180 days from the date of issue of invoice, failing which the amount of credit availed by the recipient would be added to his output tax liability, with interest. However, once the amount is paid, the recipient will be entitled to avail the credit again. In case part payment has been made, proportionate credit would be allowed.

## Documents needed to avail input tax credit

- a) Invoice issued by a supplier of goods or services or both
- b) Invoice issued by recipient along with proof of payment of tax in case of purchase from unregistered person.
- c) A debit note issued by supplier.
- d) Bill of entry or similar document prescribed under Customs Act
- e) Revised invoice
- f) Document issued by Input Service Distributor

The Input Service Distributor (ISD) may distribute the credit available for distribution in the same month in which, it is availed based on turnover.

### **Some of the cases in which ITC cannot be availed**

- a)** Motor vehicles and other conveyances except under specified circumstances.
- b)** Goods and/or services provided in relation to:
  - i. Food and beverages, outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, except under specified circumstances;
  - ii. Membership of a club, health and fitness centre;
  - iii. Rent-a-cab, life insurance, health insurance except where it is obligatory for an employer under any law;
- c)** Services taken under work contract in case of construction of immovable property but if the same service is taken as input services for further supply of work contract then ITC can be availed by service receiver.
- d)** Goods or services received by a taxable person for construction of immovable property on his own account, other than plant & machinery, even when used in course or furtherance of business.
- e)** If a person enjoys the supply of goods or services on which tax has been paid on composition scheme then no ITC can be availed on the same.
- f)** If the goods/services are consumed for private or personal purpose.
- g)** Goods lost, stolen, destroyed, written off, gifted, or free samples;
- h)** Any tax paid due to short payment on account of fraud, suppression, mis-declaration, seizure, detention.

### **Special circumstances under which ITC is available**

- a)** A person who has applied for registration within 30 days of becoming liable for registration is entitled to ITC of input tax in respect of goods held in stock (inputs as such and inputs contained in semi-finished or finished goods) on the day immediately preceding the date from which he becomes liable to pay tax.
- b)** A person who has taken voluntary registration is entitled to ITC of input tax in respect of goods held in stock (inputs as such and inputs contained in semi-finished or finished goods) on the day, immediately preceding the date of registration.
- c)** A person switching over to normal scheme from composition scheme under section 10 is entitled to ITC in respect of goods held in stock (inputs as such and inputs contained in semi-finished or finished goods) and capital goods on the day immediately preceding the date from which he becomes liable to pay tax as normal taxpayer.
- d)** Where an exempt supply of goods or services or both become taxable, the person making such supplies shall be entitled to take ITC in respect of goods held in stock (inputs as such and inputs contained in semi-finished or finished goods) relatable to exempt supplies. He shall also be entitled to take credit on capital goods used exclusively for such exempt supply, subject to reductions for the earlier usage as prescribed in the rules.
- e)** ITC, in all the above cases, is to be availed within 1 year from the date of issue of invoice by the supplier.
- f)** In case of change of constitution of a registered person on account of sale, merger, demerger etc, the un-utilized ITC shall be allowed to be transferred to the transferee.
- g)** A person switching over from composition scheme under section 10 to normal scheme or where a taxable supply become exempt, the ITC availed in respect of goods held in stock as well as capital goods will have to be paid.