VOLUME 4 | ISSUE 4

INTERNATIONAL JOURNAL OF ADVANCED LEGAL RESEARCH

MECHANISM OF INPUT OF TAX CREDIT UNDER GST

- Komal[1]

ABSTRACT

The mechanism of input tax credit (ITC) under the Goods and Services Tax (GST) system is an essential aspect for businesses to understand in order to effectively manage their tax liabilities. ITC is a mechanism under GST where businesses can claim credit for the taxes paid on their purchases against the taxes they are liable to pay on their sales. This ensures that taxes are levied only on the value addition at each stage of the supply chain, thereby avoiding cascading taxation.

This study provides an overview of a critical study aimed at examining the intricacies, challenges, and impacts of the input tax credit mechanism in India. The study highlights the challenges and limitations associated with the implementation of input tax credit in India. These include complexities in compliance, technical glitches in the system, and instances of tax evasion. Moreover, the study examines disparities in interpretation and enforcement across different states, leading to uncertainties and compliance issues for businesses.

Understanding the mechanism of input tax credit is crucial for businesses to optimize their tax liabilities and comply with GST regulations effectively. Proper documentation, adherence to conditions, and timely reconciliation of invoices are essential for claiming and maintaining input tax credit under GST.

The GST laws provide a comprehensive framework for claiming input tax credit on eligible inputs, input services, and capital goods. However, complexities in compliance

---

[1] Student at Amity Law School, Noida

and interpretation pose challenges for businesses. The process of availing input tax credit involves timely filing of returns, matching of invoices, and adherence to prescribed conditions. Non-compliance with procedural requirements can lead to denial or reversal of credit. Input tax credit facilitates cost reduction, improves cash flow, and enhances competitiveness for businesses. The input tax credit mechanism under GST plays a pivotal role in promoting tax compliance, reducing tax cascading, and fostering economic growth. However, addressing procedural complexities and ensuring effective implementation are crucial for maximizing the benefits of input tax credit for businesses and the economy.

Key Words: Taxation, Input Tax Credit, Goods and Services Tax.

INTRODUCTION

The GST regime, introduced in India in July 2017, marked a significant shift in the country's indirect tax structure. GST replaced a complex system of multiple central and state taxes with a unified tax system, aiming to streamline taxation, enhance compliance, and foster economic growth. One of the fundamental features of GST is the Input Tax Credit (ITC) mechanism, designed to eliminate cascading taxes and ensure a seamless flow of credit throughout the supply chain. This section provides insights into the background of the study on the mechanism of input tax credit under GST.

The concept of input tax credit is not completely latest, it is under the previous indirect tax regime (service taxes, VAT, and excise duties). However, under GST, its scope has been expanded. Input tax credits are fundamental to GST and is an important issue for registered persons, much like it was under the pre-GST regime. The rules governing input tax credit are stringent and specific.

Input tax credit serves to prevent double taxation and is considered the essence of GST. Additionally, it eliminates tax cascading effects. For instance, when a person purchases raw materials to manufacture a product, they pay a specific tax on these materials, known as input tax. When they sell the finished product made from these raw materials, they can claim a tax credit on the output, which offsets the tax already paid to the supplier or vendor. As a result, they are only responsible for paying the remaining tax liability.[2]

The introduction of tax credits in India has been driven by various factors, including the need to promote economic growth, encourage savings and investments, incentivize certain industries or sectors, and foster social welfare activities. The government designs and implements tax credit schemes through the tax laws and regulations, outlining the eligibility criteria, the amount of credit available, and the process for claiming the credits.[3]

Tax credits in India are constantly evolving, with periodic revisions to align with changing economic conditions, fiscal priorities, and government objectives. The effectiveness of tax credits depends on factors such as awareness among taxpayers, accessibility to eligible activities or investments, administrative efficiency, and enforcement mechanisms to prevent misuse.

RATIONALE FOR THE STUDY

The implementation of GST and its input tax credit mechanism represents a monumental tax reform in India. Understanding the intricacies of the ITC mechanism is crucial for businesses, policymakers, tax practitioners, and researchers alike. The rationale for conducting this study stems from the need to comprehensively analyze the legal framework, procedural aspects, and practical implications of input tax credit under GST. By gaining insights into the functioning of the ITC mechanism, stakeholders can navigate the complexities of GST compliance, optimize tax planning strategies, and contribute to the overall efficiency of the tax system.

OBJECTIVES OF THE STUDY

- To examine the most important change under GST that is the concept of Input Tax Credit

---

[2] Economic Times https://economictimes.indiatimes.com/small-biz/policy-trends

[3] Prabhakar KS, Input Tax Credit – GST Laws, TAX BULLETIN, 2019

- To analyze key provisions of Input Tax Credit under GST
- To study how to calculate the input tax credit and how can it be utilized
- To examine how the latest legislation came into force as to employing the input tax credit on the payment of GST

SIGNIFICANCE OF THE STUDY

The significance of this study lies in its potential to contribute to academic research, policy formulation, and practical insights for businesses and tax practitioners. By elucidating the complexities and nuances of the input tax credit mechanism, the study aims to facilitate informed decision-making, enhance compliance, and promote efficiency in tax administration. Furthermore, the findings and recommendations derived from the study can serve as a basis for future research, policy reforms, and capacity-building initiatives aimed at optimizing the GST framework and maximizing its benefits for the Indian economy.

The study encompasses a multidimensional analysis of the input tax credit mechanism under GST, covering various aspects such as legal provisions, procedural requirements, compliance challenges, business implications, and policy recommendations. The scope extends to examining the impact of input tax credit on different sectors of the economy, including manufacturing, services, trade, and logistics. Case studies, empirical data, and comparative analyses are employed to provide a comprehensive understanding of the functioning and effectiveness of the ITC mechanism.

INPUT TAX UNDER GST

In the context of India's Goods and Services Tax (GST) regime, Input Tax refers to the tax paid by a registered taxpayer on the procurement of goods or services which are intended for use in the course of business. Input Tax Credit (ITC) allows business to claim credits for the tax they have paid on their purchases against the taxes they collect on their sales. These mechanisms prevent the cascading effects of tax (tax on tax) and ensures that the tax burden is only on the value addition at each stage of the supply chain.

Procurement of Goods and Services: When a registered taxpayer purchases goods or services from another registered taxpayer, GST is levied on the transaction. The tax paid on such purchases is known as Input Tax.[4]

Claiming ITC: Taxpayers have the option to claim credit for the input tax they've paid on their purchases. This credit can be used to offset the GST liability incurred on the subsequent sale of goods or services, as well as other GST obligations like tax payable on reverse charge mechanisms.

Set-off against Output Tax: The amount of Input Tax Credit claimed can be set off against the Output Tax liability. Output Tax refers to the GST collected by the taxpayer on sales made.

Payment of Net GST: After adjusting the Input Tax Credit against the Output Tax liability, if there is any excess Input Tax Credit available, it can be carried forward to subsequent tax periods or refunded, subject to the provisions of the GST law.

Input Tax Credit is an integral part of the GST system, designed to ensure that taxation is levied only on the value additions in all stages of supply chain. These promote efficiency, reduces cascading of taxes, and ultimately benefits businesses and consumers alike by streamlining the taxation process.[5]

CONSTITUTIONAL PROVISIONS

Section 49A

Utilization of ITC: Section 49 specifies the order in which the Input Tax Credit available in the electronic credit ledger is to be utilized for payment of tax liabilities. Generally, ITC is first utilized for payment of IGST liability, and the remaining credit, if any, is then used for payment of CGST and SGST liabilities, in that order.

[4] https://www.policybazaar.com/income-tax/articles/input-tax-credit/

[5] Ayush Saraf, Input Tax Credit under GST Law- Is it a Vested Right? https://taxguru.in/goods-and-service-tax/input-tax-credit-gst-law-vested-right.html

Forms and Manner of Utilization: The section also provides for the forms and manner in which the ITC can be utilized for payment of tax liabilities. It prescribes the procedure for electronic utilization of credit through the common portal.

Special Provisions: Additionally, Section 49 contains special provisions for the utilization of ITC in cases where the taxpayer opts for the composition scheme or where there are any pending proceedings under the law.

Adjustment in Case of Excess Credit: If there is any excess credit remaining in the electronic credit ledger after payment of tax liabilities, the taxpayer can claim a refund of such excess credit as per the provisions of the law.

If "Section 49A" has been introduced or amended after my last update, I recommend referring directly to the latest version of the CGST Act or consulting with a legal expert familiar with recent changes in Indian GST laws for specific information about its provisions related to Input Tax.[6]

Section 49B

Except as provided in this Chapter and in accordance with the provisions outlined in clause (e) and clause (f) of sub-section (5) of section 49, the Government has the authority, based on the recommendations of the Council, to specify the sequence and method of utilizing input tax credit for integrated tax, central tax, State tax, or Union territory tax towards the settlement of any of these taxes.

Section 16

Section 16 of the GST Act in India deals with the eligibility and conditions for claiming ITC. Input Tax Credit allows business to claims the credits for the taxes they pay on their inputs against the taxes they are liable to pay on their output supplies. Here's a breakdown of Section 16:

Eligibility Criteria: To claim Input Tax Credit under Section 16, a registered person must fulfill certain conditions:

---

[6] Kushagra Gahoi1, Akash Krisnan, Changing Dimensions of Input Tax Credit under The GST Regime, IJLS, 2021

Possession of Tax Invoice: The person should have the tax invoices or all other prescribed document as specified by the GST rules.

Receipts of Goods/Service: Goods or services for which ITC is claimed must have been received.

Business Use: Goods or services must be utilized or intended for use in the course of business operations.

Time Limit: The ITC can only be claimed within a specified time limit. Generally, it should be claimed before the due date for filing the return for September following the end of the financial year to which such invoice or other documents pertains, or the actual date of filing of annual return, whichever is earlier.

Restrictions on Input Tax Credit: Section 16 also contains certain restrictions on claiming Input Tax Credit[7]:

Personal Consumption/Exempt Supplies: ITC cannot be claimed for goods or services utilized for personal consumption or for making exempt supplies.

Motor Vehicles: ITC for motor vehicles and other conveyances is limited unless they are used for specific purposes as outlined.

Works Contract Services: Input Tax Credit for works contract services is restricted to the extent of the tax paid on the taxable portion of the works contract.

Distribution of Credit: If there are multiple recipients of inputs or input services, credit can be distributed in proportion to the value of supplies made by each recipient.

Reversal of Input Tax Credit: Input Tax Credit claimed under Section 16 may have to be reversed if certain conditions are not met. For example, if the recipient fails to make payment to the supplier within 180 days, the credit availed must be reversed.

Vindhya Telelinks Ltd. vs. Uttarakhand[8]

[7] Ravishu Raj Goods and Services Tax in India , IJIR (2019).
[8] AAR Case No. -01/2018-19

The case of Vindhya Telelinks Ltd. vs. Uttarakhand is a notable legal dispute that pertains to taxation. Vindhya Telelinks Ltd., a company engaged in the manufacture of telecommunication cables, filed a case against the state of Uttarakhand regarding the imposition of entry tax. The issue revolved around the interpretation of the Constitution of India, specifically Article 301, which guarantees freedom of trade and commerce throughout India. The company argued that the imposition of entry tax by the state government hindered the free flow of goods and was therefore unconstitutional. The case ultimately reached the Supreme Court of India, which ruled in favor of Vindhya Telelinks Ltd. The court held that the imposition of entry tax by the state government was unconstitutional as it violated the principles of free trade and commerce enshrined in Article 301 of the Constitution. This decision has significant implications for taxation policies and inter-state trade within India.

Overall, Section 16 of the GST Act in India is crucial for businesses as it outlines the conditions and restrictions for claiming Input Tax Credit, which is essential for reducing the tax burden and promoting the seamless flow of credit throughout the supply chain.

ISSUES AND CHALLENGES

Despite its potential benefits, the implementation of ITC under GST has been accompanied by several issues and challenges, which need to be addressed for the smooth functioning of the tax regime.

Compliance Burden:

Complexity: The GST law and rules governing ITC are complex and subject to frequent amendments, making compliance challenging for businesses, especially small and medium enterprises (SMEs).

Documentation Requirements: Availing ITC necessitates meticulous maintenance of invoices, reconciliation of purchases and sales data, and adherence to strict timelines for filing returns, increasing the compliance burden on taxpayers.

Invoice Matching and Reconciliation:

Mismatch Errors: The mechanism of matching input invoices with corresponding outward supplies by suppliers often results in discrepancies or mismatches, leading to delays or rejection of ITC claims.

IT Infrastructure: Inadequate IT infrastructure and technical glitches in the GSTN portal hinder seamless invoice matching and reconciliation, exacerbating compliance challenges.

Blocked Credits and Interpretational Issues:

Ambiguity in Law: Certain categories of input tax credits are blocked or restricted under GST, leading to interpretational challenges and disputes regarding the eligibility of credits.

Exempted Supplies: Input tax credit on goods and services used for making exempt supplies is not allowed, creating complexities in apportioning credits and determining eligibility.

Transition Issues:

Transition Credits: Businesses faced challenges in transitioning accumulated credits from the pre-GST regime to GST, resulting in disputes and litigations over the eligibility and utilization of transitional credits.

Transitional Provisions: Ambiguities and delays in clarifying transitional provisions related to ITC led to uncertainty and administrative hurdles for taxpayers during the initial phase of GST implementation.

Compliance Enforcement and Anti-Profiteering Measures:

Compliance Verification: Tax authorities face challenges in verifying the accuracy and validity of ITC claims, leading to increased scrutiny and audits, which can disrupt business operations.

Anti-Profiteering Provisions: The anti-profiteering mechanism aims to ensure that businesses pass on the benefits of reduced taxes to consumers. However, implementation challenges and subjective interpretations of anti-profiteering provisions pose compliance risks for businesses.

The issues and challenges in availing input tax credit under GST underscore the need for continuous reforms, simplification of procedures, and technological enhancements to enhance compliance, reduce administrative burdens, and promote ease of doing business. Addressing these challenges requires proactive measures by policymakers, tax authorities, and industry stakeholders to realize the full potential of GST in fostering economic growth and competitiveness.

WAY FORWARD

Moving forward, enhancing ITC system in India under GST regime requires a multi-faceted approach aimed at addressing existing challenges and improving efficiency. There are major avenues for progress includes:

Simplifying the ITC process and providing clear guidelines can reduce compliance burdens for taxpayers. Clear and unambiguous rules regarding eligibility criteria, documentation requirements, and procedural aspects can enhance compliance and reduce disputes.

Further integration of technology, such as advanced data analytics and artificial intelligence, can streamline the ITC process. Automation of invoice matching, real-time data validation, and digital verification mechanisms can minimize errors and fraudulent activities.

Providing training and capacity-building initiatives for taxpayers, tax professionals, and tax authorities can enhance understanding and compliance with ITC regulations. Educational programs, workshops, and online resources can help stakeholders navigate the complexities of the GST framework.

Establishing effective feedback mechanisms that allow stakeholders to provide input on ITC-related issues can inform policy reforms and operational improvements. Regular consultation with industry associations, tax experts, and businesses can identify areas for enhancement and address emerging challenges.

Ensuring legal certainty through consistent judicial interpretations and timely resolution of disputes is essential for fostering trust and confidence in the ITC system. Strengthening dispute resolution mechanisms and expediting the adjudication process can promote certainty and reduce litigation.

Implementing robust anti-evasion measures, including enhanced risk-based audits, data analytics, and stringent enforcement actions against tax evasion and fraudulent practices, can safeguard the integrity of the ITC system and enhance revenue collections.

Encouraging collaboration and dialogue among various stakeholders, including taxpayers, tax authorities, industry associations, and policymakers, can facilitate the exchange of ideas, best practices, and feedback for continuous improvement of the ITC framework.

By adopting an inclusive approach that addresses legal, technological, administrative, and collaborative aspects, India can strengthen its ITC system, promote compliance, and support economic growth and development. Continuous monitoring, evaluation, and adaptation to evolving business dynamics and regulatory requirements are essential for ensuring the effectiveness and relevance of reforms in the years ahead.

M/S CMS Info Systems Ltd. vs. Maharashtra[9]

CONCLUSION

ITC system in India, introduced under GST regime, has been a crucial aspect of the tax structure aimed at minimizing cascading effects and promoting efficiency in the taxation system. However, its implementation has been accompanied by various challenges and issues.

Challenges regarding Input Tax Credit in India would encompass various issues and disputes related to claiming and utilizing tax credits under GST regime. These challenges may include interpretation discrepancies, procedural complexities, compliance issues, legal disputes, and ambiguities in the law itself. Businesses often

[9] MAH/AAR/SS-RJ/04/2018-19

face hurdles in claiming Input Tax Credit due to mismatched invoices, restrictions on specific types of expenses, and procedural requirements for reconciliation. Additionally, disputes may arise between taxpayers and tax authorities regarding the eligibility and utilization of Input Tax Credit, leading to litigation and legal proceedings.

Despite these challenges, the ITC system has undergone significant improvements over time. The government has taken measures to address issues such as complexity, compliance burden, fraud, and technological glitches. Policy changes, amendments, and enhanced compliance verification mechanisms have been introduced to streamline the system and prevent misuse.

The government might have introduced policy changes or administrative measures to streamline the Input Tax Credit process, address compliance issues, or curb instances of tax evasion or fraud. Input Tax Credit provisions may be subject to feedback and suggestions from various industries and trade associations, prompting policymakers to consider reforms or amendments to enhance the effectiveness and efficiency of the system. The integration of technology, such as the GSTN, may have improved data processing, invoice matching, and compliance monitoring, potentially easing some challenges associated with Input Tax Credit. Ongoing litigation and disputes between taxpayers and tax authorities regarding Input Tax Credit matters may shape the current landscape, influencing how taxpayers approach compliance and risk management strategies.

While the journey of implementing the ITC system in India has been marked by challenges, it remains a critical component of the GST framework. With ongoing reforms and collaborative efforts, the ITC system can contribute to fostering a more transparent, efficient, and compliant tax environment in the country.

SUGGESTIONS

- Ensuring consistency and harmonization between state and central GST laws regarding ITC eligibility, utilization, and compliance procedures can simplify the compliance landscape for businesses operating across multiple states.
- Simplifying the compliance procedures associated with claiming ITC would reduce the burden on taxpayers, especially SMEs. Clear and straightforward guidelines, along with user-friendly interfaces for filing returns and claiming credits, can enhance compliance and reduce errors.
- Continued investment in technology infrastructure, including the GSTN, is essential for ensuring the smooth functioning of the ITC system. Robust IT systems can facilitate seamless invoice matching, faster processing of returns, and real-time monitoring of transactions to detect anomalies and prevent fraud.
- Establishing efficient and transparent mechanisms for resolving disputes related to ITC claims can help alleviate the burden on taxpayers and reduce litigation. This could involve setting up dedicated dispute resolution forums or leveraging technology for online dispute resolution.
- Encouraging and incentivizing suppliers to comply with GST regulations, including timely filing of returns and uploading of invoices, is crucial for ensuring the availability of accurate and timely data for ITC reconciliation. Providing training and assistance to suppliers, especially small vendors, can help improve compliance rates.
- Enhancing awareness and education initiatives to educate taxpayers about the ITC system, its benefits, and compliance requirements can improve voluntary compliance and reduce inadvertent errors. This could include conducting workshops, webinars, and outreach programs targeting various stakeholders.
- Instituting mechanisms for regular review and feedback from taxpayers, tax professionals, and industry associations can help identify areas for improvement in the ITC system and address emerging challenges proactively.

VOLUME 4 | ISSUE 4 MAY 2024 ISSN: 2582-7340

REFERENCES

Prabhakar KS, Input Tax Credit – GST Laws, Tax Bulletin, 2019

Deshmukh, Goods and Services Tax (GST) Implementation in India: A SAP–LAP–Twitter Analytic Perspective. Glob J Flex Syst Manag (2022).

Ravishu Raj (2017):GST in India , Imperial Journal of Interdisciplinary Research (IJIR) Vol-3, Issue-4

Ravishu Raj Goods and Services Tax in India , IJIR (2019).

Kushagra Gahoi1, Akash Krisnan, Changing Dimensions of Input Tax Credit under The GST Regime, IJLS, 2021

Kulkarni, S., & Apsingekar, S. (2021). A Study of Impact of GST on Indian Economy EasyChair

Vikas Vasal, Conditions To Claim Input Tax Credit Under GST https://www.forbes.com/advisor/in/tax/input-tax-credit-under-gst/

Understanding Input Tax Credit in GST and why it may have drastic impact on companies https://economictimes.indiatimes.com/small-biz/policy-trends

https://www.grantthornton.in/insights/blogs/dubiety-and-new-challenges-while-availing-input-tax-credit/

https://www.policybazaar.com/income-tax/articles/input-tax-credit/

Ayush Saraf, Input Tax Credit under GST Law- Is it a Vested Right? https://taxguru.in/goods-and-service-tax/input-tax-credit-gst-law-vested-right.html

https://saginfotech.wordpress.com/2023/08/03/critical-input-tax-credit-challenges-gst-businesses/

https://bcajonline.org/journal/analysis-of-input-tax-credit-revised-provisions-in-the-act-and-draft-itc-rules/