

Understanding the GST Model Law - Input Tax Credit - Part 8

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This is the eight in the series of proposed articles on the GST Model law. No 7 was on Input Services tax credit. The purpose is mainly to create awareness and enable one to look at the unintended impact as maybe applicable for each sector/ person. It could also aid in representation needed for amendment of the Model GST Law to make it tax payer friendly and meet the objective of clarity, certainty and transparency.

Background

Same as Part- 7 (Please see earlier article)

The GST law provides for credit of GST paid on all the inputs, barring some exceptions. This part has been borrowed from the Central Excise law and in regard to inputs the law is fairly developed. The exceptions include the goods used mainly for personal consumption of employees, goods used for construction of immovable property, etc. Supplies used for personal consumption are also ineligible for credit.

In this article the paper writer examines the provisions relating to input tax credit on **inputs** under the GST regime. Also input definition under Cenvat Credit rules is analysed herein.

Definition of Inputs - Section 2 (54)

“**Input**” means any goods other than capital goods, **subject to exceptions** as may be provided under this Act or the rules made there under, used or intended to be used by a supplier for making an outward supply **in the course or furtherance of business**.

Paper writer’s comment:

- *Inputs are any goods other than capital goods, used for making supply in course of business, subject to exceptions/restrictions. The goods of enduring nature therefore would automatically be covered under inputs.*
- *Business includes any trade, commerce, manufacture, profession, vocation or any other similar activity, whether or not for a pecuniary benefit, and covers activities incidental/ ancillary thereto. The liability as well as the credit would therefore get covered other than specific disallowances.*

- *Inputs include those which are intended to be used for making outward supply. **Example:** Inputs used for research/ trial run of production of taxable goods.*
- *Analysis of eligible capital goods on which credit could be taken would be discussed in next article in this series.*

Ineligible input credits:

- motor vehicles, except when supplied in the usual course of business or are used for providing taxable services of –
- Transportation of passengers
- Transportation of goods
- Imparting training or motor driving skills
- Goods provided in relation to -
- food and beverages,
- outdoor catering,
- beauty treatment,
- health services,
- cosmetic and plastic surgery,
- membership of a club,
- health and fitness centre,
- life insurance, health insurance and travel benefits extended to employees on vacation such as leave or home travel concession,
when such goods are used primarily for personal use or consumption of any employee
- Goods acquired by principal in the execution of works contract
- when such contract results in construction of immovable property,
- other than plant and machinery.
- Goods acquired by principal, the property in which is not transferred
- whether as goods or in some other form
- to any other person,
- which are used in construction of immovable property,
- other than plant and machinery.
- Goods on which composition tax has been paid (u/s 8- Composition Option)
- Goods used for private or personal consumption to the extent they are consumed.

It may also be noted that:

1. *Where the inputs are used by the registered taxable person partly for taxable and partly for non-taxable supplies, the credit attributable to the taxable supplies including zero-rated supplies [exports] could be availed. **Example:** Out of 10 racks purchased in name of HUF engaged in taxable supply of goods, 5 are used for storing non-taxable supplies such as agricultural produce at farm of HUF. Credit on racks used for non-taxable supplies cannot be availed.*
2. *Where the goods are used by the registered taxable person partly for the business and partly for other purposes, the amount of credit shall be restricted to credit attributable to the business purpose. **Example:** When umbrella purchased by firm is used for personal use of the partner of the business, credit restricted.*
3. **Credit on stocks to person liable to pay tax:** *A person who has applied for registration within 30 days from the date on which he becomes liable to registration and has been granted such registration shall, subject to prescribed conditions and restrictions, be entitled to take credit of input tax in respect of inputs held in stock and inputs contained in WIP or finished goods held in stock on the day immediately preceding the date from which he becomes liable to pay tax under this Act.*
4. **Credit on stocks for person who takes voluntary registration:** *A person, who takes voluntary registration shall, subject to such prescribed conditions and restrictions, be entitled to take credit of input tax in respect of inputs held in stock and inputs contained in WIP or finished goods held in stock on the day immediately preceding the date of registration.*
5. **Credit on stocks when taxable person ceases to pay composition tax:** *Where any registered taxable person ceases to pay composition tax, he shall, subject to prescribed conditions and restrictions, be entitled to take credit of input tax on inputs held in stock and inputs contained in WIP or finished goods held in stock on the day immediately preceding the date from which he becomes liable to pay tax under normal provisions.*
6. *A taxable person shall avail input tax credit specified under (c), (d), (e) above in respect of any supply of goods and / or services to him within 1 year from the date of issue of tax invoice relating to such supply.*

Comments:

1. *In view of paper writer the input tax credit on all inputs/materials should be permitted when directly/indirectly used in relation to business of supply of taxable goods and/or services.*

2. *Restricting credit on goods used mainly for business use by employees unjustified. Similar restrictions are put in place for input service as well. This could lead to litigation / disputes under GST law.*
3. *Restriction on employee related credit is copy pasted from current input definition given in Cenvat Credit Rules.*
4. *Goods used in construction of immovable property is restricted. This once again could lead to fresh round of litigation under GST law.*
5. *Composition tax paid credit being restricted leads to cascading of composition tax. In construction contracts there are multiple levels of contractors. Therefore tax at each stage would cascade.*
6. *Restriction on credit on inputs used solely for private consumption is reasonable. Similarly restriction is in place for input services.*

Comparison with the present regime:

Definition of input under present Cenvat Credit Rules as under:

The term input is defined in Rule 2(k) of CCR: "input" means:

Eligible Credit:

- *(i) all goods used in the factory by the manufacturer of the final product; or*
- *(ii) any goods including accessories, cleared along with the final product, the value of which is included in the value of the final product and goods used for providing free warranty for final products; or*
- *(iii) all goods used for generation of electricity or steam or pumping water for captive use; or*
- *(iv) all goods used for providing any output service;*
- *(v) All capital goods having value upto Rs.10000 per piece*

Restriction on availment of credit on inputs

Excludes:

- *light diesel oil, high speed diesel oil or motor spirit, commonly known as petrol;*
- *any goods used for -*
 1. *construction or execution of works contract of a building or a civil structure or a part thereof; or*
 2. *laying of foundation or making of structures for support of capital goods,*
except for the provision of service portion in the execution of a works or construction service as listed under clause (b) of section 66E of the Act;

- *capital goods except when (i) used as parts or components in the manufacture of a final product or (ii) value of such capital goods is upto Rs. 10000 per piece;*
- *motor vehicles;*
- *any goods, such as food items, goods used in a guesthouse, residential colony, club or a recreation facility and clinical establishment, when such goods are used primarily for personal use or consumption of any employee; and*
- *any goods which have no relationship with the manufacture of a final product.*

It maybe noted there is specific restriction to avail credit on inputs used for executing works contract service [material plus labour contract] set out in ST Valuation Rules.

Landmark Decisions on indicative list of eligible credit on inputs under Cenvat Credit Rules

Raw materials: In TELCO vs. State of Bihar (1994 (74) E.L.T. 193), the Supreme Court held that the term raw material varies from industry to industry and decided that items like tyres and tubes, which, though are finished products in themselves, can be considered as raw materials for vehicles.

1. **Goods used for testing:** In the case of Flex Engineering Ltd vs. CCE, U.P 2012 (276) ELT 153 (SC) wherein it was held that goods used for testing machines were inputs used in relation to manufacture of final product, eligible for Cenvat/Modvat credit. Physical presence in final product is not pre-requisite to claim credit. They may very well be indirectly related to manufacture and still be necessary for completion of manufacture of final product, which is complete only when product is rendered marketable
- **Credit on accessories:** The Supreme Court in HMM Ltd. vs. CCE - 1994 (74) E.L.T. 19, wherein it was held that metal screw cap put on Horlicks bottle is a component part of the finished product.
1. **Furnace oil:** In the case of CCE, Meerut-I vs. Silvertone Papers Ltd., 2013 (287) ELT 478 (Tri. Del.) Furnace oil procured and used in boiler on trial basis. Assessee is entitled to credit of duty paid on it.

Recommendations:

1. *Goods used for employees – credit should be allowed when it is mainly for business use.*

2. *Goods acquired in execution of works contract/for immoveable property used for business should be allowed.*
3. *Composition tax paid input credit should be allowed unless a low merit rate option provided.*

Conclusion:

In this article, the paper writer has sought to examine implications on availment of input tax credit on inputs under the GST regime. The model law could be referred for further details.

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