

Rule 89(4)(c) is 'ultra-vires' to the provisions of GST law and held 'unconstitutional'

The Hon'ble Karnataka High Court in *M/s. Tonbo Imaging India Pvt Ltd v. Union of India [W.P.C No. 13185 of 2020] (T-RES) dated February 16, 2023* has held that, Rule 89 (4)(c) of the Central Goods and Service Tax Rules, 2017 ("the CGST Rules") which restricts the exports made without payment of tax (i.e., under Letter of Undertaking model ("LUT Model")) to 1.5 times value of like goods supplied domestically is unconstitutional and ultra vires of the provisions of the GST law.

Facts:

M/s. Tonbo Imaging India Pvt. Ltd ("**the Petitioner**") develops innovative micro-optic designs for real-world applications. The Petitioner exported various customized products during the period from May 2018 to March 2019.

Since, exports made by the Petitioner were "zero-rated supply" under Section 16 of the Integrated Goods and Services Tax Act, 2017 ("**the IGST Act**"), the Petitioner filed refund applications for the months of May 2018, July 2018, August 2018, November 2018, December 2018 and March 2019 on May 25, 2020, May 27, 2020, and May 28, 2020.

The Central Board of Indirect Taxes and Customs ("**CBIC**") vide **Notification No. 16/2020 Central Tax dated March 23, 2020** amended Rule 89(4)(c) of the CGST Rules, which restricted the refund of exports made through LUT to a maximum of 1.5 times the value of like goods domestically supplied by the same or, similarly placed supplier.

Revenue Department ("**the Respondent**") issued deficiency memos in regard to refund claims filed by the Petitioner on the ground that the Petitioner had not provided the value of like goods domestically supplied as required in terms of Rule 89(4)(c) of the CGST Rules. Thus, refund claims could not be considered.

In replies to such deficiency memos interalia, the Petitioner stated that the amended rule would not be applicable for the period for which the refund claim was sought and the Petitioner would be governed by the unamended Rule 89(4)(c) CGST Rules and not by the amended Rule 89(4)(c) of the CGST Rules.

The Respondent rejected the claims filed by the Petitioner vide an order dated 30.06.2020 ("**the Impugned Order**"), rejecting the claim of refund filed by the Petitioner.

Aggrieved by the Impugned Order, the Petitioner filed a writ petition before the Karnataka High Court.

Issue:

Whether Rule 89(4)(c) of the CGST Rules is liable to be held unconstitutional, being violative of Articles 19(1)(g) and 14 of the Constitution and ultravires to provision of GST law?

Held:

The Hon'ble Karnataka High Court in ***Writ Petition No. 13185 of 2020 (T-RES) dated February 16, 2023*** held as under:

- Noted that, on a combined reading of Section 54 of the CGST Act and Section 16 of the IGST Act, it can be said that intention of making exports zero-rated is to make the entire supply chain of exports tax-free. However, Rule 89(4)(c) restricts the refund in case of export made through the LUT model to 1.5 times the value of like goods domestically supplied, which is ultra vires in view of the well-settled principle of law that rules cannot override the parent legislation.
- Further noted that, Rule 89(4)(c) of the CGST Rules is violative of Articles 14 and 19(1)(g) of the Constitution being restricting the quantum of refund of unutilized Input Tax Credit ("**ITC**") in case of export made under LUT model. In contrast, in the case of refund sought under payment of the IGST model, there is no such limit.

- Observed that, Rule 89(4)(c) of the CGST Rules contains words “like goods” and “similarly placed supplier,” which are not defined anywhere in the CGST Act or IGST Act or rules made thereunder.
- Further observed that, in case where the domestic turnover is nil for a particular period or very less, the quantum of refund becomes nil or negligible where the exports were made under LUT model, thereby clearly cutting down the principle of zero-rating as specified in Section 16 of the IGST Act, 2017 which would mean that the taxes on exports do not get refunded adequately.
- Held that, Rule 89(4)(c) is ultra vires the provision of the IGST Act and CGST Act, including being violative of Articles 14 and 19 of the Constitution and the provision is arbitrary, unreasonable and vague.
- Directed the Respondent to accept the refund claims of the Petitioner.
- Allowed the Writ petition.

Our Comments:

Karnataka High Court has correctly held Rule 89(4)(c) unconstitutional as the rule restricts the exporters from claiming refund of ITC in case such exporter is making export via LUT model as the rule restricts the refund claim of unutilized ITC on the export of goods under LUT to the lower of actual value or 1.5 times the value of the same goods domestically supplied by the assessee. Further, it is challenging to ascertain the value of similar supplies in the case of customized products or where the goods are only manufactured for export and do not have a domestic market. In such cases, the genuine exporters would have to face inconvenience due to malpractices by others.

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