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Writ admitted for examining validity of provisions restricting ITC on construction of building for letting out on rent

The Hon'ble HC, Karnataka in ***Bagmane Developers v. Union of India [W.P. No. 9430/2020 dated October 22, 2020]*** stayed demand of Rs. 62 crore in a writ petition challenging credit restriction under Section 17(5)(c) and (d) of Central Goods and Services Tax Act, 2017 ("**CGST Act**") on construction of building used for letting out wherein GST is paid on rent.

Facts:

Bagmane Developers ("**the Petitioner**") is engaged in taxable services such as commercial/industrial construction service, works contract services, repair services and renting of immovable properties. The Petitioner has filed returns in GSTR – 3B and GSTR – I for the period between July 2017 and April 2019 but without availing input tax credit ("**ITC**") on goods and services utilized in construction of commercial complexes which are rented after completion. The Petitioner has filed GSTR – 3B for the month of May 2019 availing substantial ITC prompting the GST department to issue notice dated March 6, 2020 ("**Impugned notice**") to show cause as to why ITC availed amounting to Rs. 62 crore (approx.) in GSTR-3B for the month of May, 2019 should not be held as ineligible and demanded and recovered from the Petitioner along with interest and penalty.

Issues:

- Challenged the validity of Section 17(5)(c) and (d), 16(4), 61(5), 50 and 164(3) of the CGST Act.
- Whether Section 17(5)(c) and (d), 16(4) of the CGST Act can be read down to permit the use of ITC on goods and services used in the construction in "business-to-business" cases with the denial for ITC only in "business-to-consumer" cases.

Petitioner's contentions:

- The Petitioner for the period between July 2017 and April 2019 filed its returns in Form GSTR-3B and GSTR- 1 and availed ITC on the costs incurred for construction of the land owners' share where the properties are developed under Joint Development Agreement with such land owners, but without reporting availment of ITC on goods and services used in the construction of commercial complexes which are rented out because of lack of clarity.
- Relied on the Hon'ble HC, Orissa in ***Safari Retreats Private Limited v. Chief Commissioner of CGST [2019 (25) G. S. T. L. 341 (Ori.)]*** to read down Section

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17(5)(c) and (d) of the CGST Act. Further contended that he has filed GSTR – 3B availing the ITC as per the Safari Retreat case.

- Section 17(5)(c) and (d) of the CGST Act are unreasonable and arbitrary inter alia for the reason that these provisions deny the advantage of ITC though there is continuity of transaction without break in chain. Section 16 of GST Act entitles a registered person to the use of ITC on any supply of goods or services to him which are used or intended to be used in the course of the business as part of a transactional chain. Thus, the continuity of transaction without break in chain is the essence of the scheme under GST.
- Section 17(5)(d) of the CGST Act makes an unreasonable discrimination between those assesses who could avail ITC when the goods and services availed are utilized in the course of or in furtherance of their business as contemplated under Section 16(1) of the CGST Act and those who are engaged in the business of construction of immovable property in the course of or in furtherance of their business only because the business of the assessee is construction or works contract. Section 17(5)(c) of the CGST Act are also arbitrary and unreasonable as these provisions create an artificial distinction.
- The Petitioner has a vested and an accrued right to avail ITC once the conditions as contemplated under Section 16(1) of the CGST Act are satisfied with a simultaneous right to claim adjustment of tax on outward supply of goods and services. This right would be an indefeasible right and therefore such right cannot be taken away in any manner that is impermissible in law. The law of limitation can only bar a remedy and cannot negate an accrued or a vested right. Section 16(4) of the CGST Act in imposing a negation of the accrued and vested rights violate this seminal proposition and as such, Section 16(4) of the GST Act is in violation of Article 300A of the Constitution of India.

Departmental Contentions:

- The Petitioner has in effect challenged only Impugned notice under the guise of challenging the constitutional validity of Section 17(5)(c) and (d), 16(4) and other provisions of the CGST Act. The contention that Section 17(5)(c) and (d), 16(4) of the CGST Act and the other provisions thereof are unconstitutional and contrary to the scheme under the CGST Act, when not well grounded, is impermissible.

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- The Petitioner cannot rely upon the decision in Safari Retreats supra as the same is challenged by the Department before the Hon'ble Apex Court as admitted by the Petitioner and mentioned in the Impugned notice.
- The ITC, in the scheme of the CGST Act, is only a concession and the same cannot be categorized as a vested right or an accrued right or a substantive right. The constitutional validity of Section 16(4) of the CGST Act has been upheld by HC, Bombay in **Nelco Limited v. Union of India [W.P. No. 6998/2018 dated March 20, 2020]**.

Held:

The Hon'ble HC, Karnataka in **W.P. No. 9430/2020 dated October 22, 2020** stated as under:

- The Court shall examine the validity of Section 17(5)(c) and (d), 16(4) of the CGST Act and the other provisions thereof in the light of the decision by the Division Bench of the Orissa High Court in Safari Retreats supra.
- This Court shall also have to examine whether the ITC under the CGST Act is contemplated as a mere concession or as a right that accrues if the conditions stipulated under Section 16 of the CGST Act are satisfied, and if it is a right that accrues, whether such right could be extinguished prescribing the time limit within which such right has to be exercised.
- Granted stay to the Impugned notice on the condition that the Petitioner shall maintain a minimum of the 10% of the disputed availment in its electronic credit ledger subject to the outcome of the writ petition.
- The matter is next listed on November 20, 2020

Relevant provisions:

Section 17(5)(c) and (d) of the CGST Act:

"17. Apportionment of credit and blocked credits- Notwithstanding anything contained in sub-section (1) of section 16 and subsection (1) of section 18, input tax credit shall not be available in respect of the following, namely:-

(5) Notwithstanding anything contained in sub-section (1) of section 16 and subsection (1) of section 18, input tax credit shall not be available in respect of the following, namely:-

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(c) works contract services when supplied for construction of an immovable property (other than plant and machinery) except where it is an input service for further supply of works contract service

(d) goods or services or both received by a taxable person for construction of an immovable property (other than plant or machinery) on his own account including when such goods or services or both are used in the course or furtherance of business.

Explanation.—For the purposes of clauses (c) and (d), the expression “construction” includes re-construction, renovation, additions or alterations or repairs, to the extent of capitalisation, to the said immovable property”

Section 16(4) of the CGST Act:

“16. Eligibility and conditions for taking input tax credit.

(4) A registered person shall not be entitled to take input tax credit in respect of any invoice or debit note for supply of goods or services or both after the due date of furnishing of the return under section 39 for the month of September following the end of financial year to which such invoice or debit note pertains or furnishing of the relevant annual return, whichever is earlier.

Provided that the registered person shall be entitled to take input tax credit after the due date of furnishing of the return under section 39 for the month of September, 2018 till the due date of furnishing of the return under the said section for the month of March, 2019 in respect of any invoice or invoice relating to such debit note for supply of goods or services or both made during the financial year 2017-18, the details of which have been uploaded by the supplier under sub-section (1) of section 37 till the due date for furnishing the details under sub-section (1) of said section for the month of March, 2019.”

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