

Jumbo Trumpets...

A STITCH IN TIME

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In a path-defining judgement, the Hon'ble High Court of Madras, in the case of **Tvl. SAHYADRI Industries Ltd vs State of TN** as reported in **2023 (4) TMI 912 - Madras HC** has laid down three cardinal rules for the availment of Input Tax Credit (ITC) under the erstwhile TNVAT regime. In this piece, we have attempted to understand those golden rules and its applicability to the current GST regime.

The Hon'ble High Court has held that though the Input Tax Credit is a substantive right it is not an indefeasible right **BUT** contingent upon demonstration of **ALL** the three cardinal tests, namely, transfer of title, payment and transfer of possession. In other words, to claim ITC, the transaction shall be legitimate and bonafide, where there exists an invoice or any other specified document by the supplier to the buyer evidencing the transfer of title, a bank transfer or any other similar transaction by the buyer evidencing the payment to the supplier and any transportation document evidencing the delivery and transfer of possession. It also clarified that the delivery need not be to the buyer directly but can be delivered to the consignee.



Further, referring to the celebrated judgement of the Apex Court in the case of **CCE vs Dai Ichi Karkaria Ltd - 1999 (112) ELT 353 (SC)**, the Hon'ble High Court had concluded that, once the ITC is validly taken by the buyer answering the above three tests in affirmative, then it's an indefeasible right accrued to him and the same cannot be questioned **even if the supplying dealer fails to pay the tax**. It is further held that, for any such non-payment of tax at the supplier's end, the remedy available to the authorities is to recover such tax from the supplier under Section 27(1) of the TNVAT Act, 2006 (TNVAT Act) and not to deny the ITC at the hands of the buyer.

By holding so, the High Court has succinctly laid down the **"burden of proof"** to be discharged by the buyer does not include the payment of tax by the seller to avail ITC as required under Section 17(2) of the TNVAT Act. The High Court has also held that, till the above burden of proof is discharged, the ITC would be held **"provisional"** as per Section 19(16) of the TNVAT Act and till such time the officer is empowered to revoke the ITC, if there is a failure on such discharge.

The High Court further held that the **cancellation of Registration** at the supplier' end, (irrespective of the fact that such cancellation is retrospective or prospective), is not a ground to deny the ITC at the buyer's end, as long as the ITC has been validly availed by the buyer, adhering to the three cardinal aspects, as enumerated above.



It has been further held that, if the above three cardinal aspects are established by the buyer, then the ITC cannot be denied at the buyer's end alleging that there is any **mis-match at the supplier's end** regarding any credit information. In such a scenario, the only option available to the authorities is to invoke appropriate machinery provision under the Act and recover the tax at the suppliers end and not to deny the validly taken ITC at the hands of the buyer.

Now, applying these golden principles to the GST regime, we are of the following view:

ITC is an indefeasible right **BUT** contingent upon the following;

- Recipient is in possession of a tax invoice or debit note issued by the supplier as per Section 16(2)(a) of the CGST Act, 2017 (hereinafter the said Act) - (Cardinal Rule no. 1 - Transfer of Title - only applicable for Goods).
- Recipient has received the goods or services or both as per Section 16(2)(b) of the said Act - (Cardinal Rule no. 2 - Transport proof evidencing delivery and transfer of possession - only applicable for Goods).
- Recipient to pay the value with tax within 180 days to the supplier as per proviso to Section 16(2)(d) of the said Act - (Cardinal Rule no. 3 - Payment, applicable for Goods and Services or both).



Now to the moot question. What is the relevance and applicability of Section 16(2)(c) of the said Act, which stipulates **that the tax charged has been actually paid to the Government?** It had been always been a bone of contention between the department and the assesseees, whenever there is a default at the supplier' end on payment of tax. Despite being a genuine recipient, who had paid the tax to the supplier and has scrupulously followed the above three cardinal requirements, the authorities have been disputing /denying the ITC at the recipient' end, citing the above sub-section.

This provision is similar to that of the one contained in proviso to the amended Section 19(1) of the TNVAT Act, which has been dealt in this decision. The said proviso to Section (w.e.f 29.01.2016), reads as under;

“Provided that the registered dealer, who claims input tax credit, shall establish that the tax due on purchase of goods has actually been paid in the manner prescribed by the registered dealer who sold such goods and that the goods have actually been delivered”.

The Hon'ble High Court has thoroughly analysed the above provisions in detail on both logical as well as possibility matrix and had emphatically held that it would be **“impossible”** for the buyer to ensure as to whether the tax is paid or not by the seller and hence it cannot come in way as a condition precedent to avail ITC at the hands of the buyer, provided all the other three cardinal tests are met with (Invoice evidencing transfer of title / Payment and Transportation evidencing transfer of possession).



Applying the same logic and reasoning, even under the said Act, the condition cast under Section 16(2)(c) of the said Act is proprietary at the hands of the supplier and the recipient has no wherewithal or possibility to ensure the payment or default, at the supplier' end. Thus we are of the view, the said condition under Section 16(2)(c) can neither be a pre-condition for availment of ITC under Section 16 nor would constitute a “burden of proof” as per Section 155 of the said Act, to claim ITC at the recipient' end. Further, as held by the Hon'ble High Court, if there is any default at the hands of the supplier, the only option or remedy available to the authorities is to initiate action against the supplier and recover the tax **BUT NOT TO DENY THE ITC AT THE HANDS OF A GENUINE RECIPIENT.**

Further, we can also fortify the above conclusion taking a cue from the language employed in Section 16(2) of the said Act. A close reading to the said sub-section would reveal that the reference to the recipient in Section 16(2) as “he” is made available only under sub-sections (a), (b) and (d) and NOT under (c)).

Last but not the least, applying the ratio of this great judgement to the said Act, we can safely conclude that, ITC cannot be denied to a genuine recipient, if the transaction is legitimate and bonafide at his end and scrupulously following the three golden tests laid down by the Hon'ble High Court, even if:

- There is any default of payment of tax by the supplier.
- The registration of the supplier is cancelled (either retrospectively or prospectively).
- There is any mis-match at the supplier' end as against the original invoice.



Before Parting...

Section 43A(6) of the said Act made the supplier as well as the recipient “**jointly and severally**” liable to pay the tax or ITC availed. This Section has since been deleted. This further fortifies the view that the recipient is in no way concerned about the tax liability at the supplier’ end to avail his legitimate ITC. The authors are also of the opinion that the ratio of the Madras HC, supra, would be applicable even after insertion of Sub- Section 16 (2) (aa), (ba), amendment to Section 16(2)(c) and Section 41 of the said Act as well as Rule 37A of the GST Rules.

