

## **Utilisation of Wrong ITC: Should Interest be levied When Overall Credit Is Sufficient?**

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When taxpayers wrongly avail input tax credit (ITC) under GST, the law mandates interest on such amounts if the credit is “utilised”. However, a key interpretational debate arises should this utilisation be seen ledger-wise (i.e., head-wise as IGST, CGST, SGST, Compensation Cess), or should the overall ITC balance be considered holistically to determine whether there has truly been a benefit or shortfall?

The explanation to Rule 88B of the CGST Rules, 2017, states that input tax credit (ITC) wrongly availed shall be deemed to have been utilised when the balance in the electronic credit ledger falls below the amount of such wrongly availed ITC. The extent of utilisation is determined by the amount by which the ledger balance falls short of the wrongly availed credit. Notably, neither the rule nor the explanation prescribes head-wise segregation when determining utilisation of ITC.

However, with the release of Circular No. 192/04/2023-GST, the Board partially addressed this issue but only in the context of IGST. This article argues that the same holistic approach should also extend to CGST and SGST, whereas Compensation Cess, by design, must continue to be evaluated separately.

### **1. IGST Credit Utilisation: Circular 192 and the Holistic Approach**

Circular No. 192/04/2023-GST clarified that interest under Section 50(3) will not be applicable on wrongly availed IGST credit if the taxpayer's total ITC balance (i.e., IGST + CGST + SGST) is sufficient to cover the said amount.

#### **Example 1: No interest when overall credit is sufficient**

- Wrongly Availed IGST Credit: ₹60,000
- Credit Balances:
  - IGST: ₹50,000
  - CGST: ₹30,000
  - SGST: ₹20,000

- Total ITC = ₹100,000
- No interest - even though IGST balance is ₹10,000 short, the total credit is sufficient.

### **Example 2: Interest on Shortfall Beyond Total Balance**

- Wrongly Availed IGST Credit: ₹120,000
- Total ITC Balance (as given in the above example): ₹100,000
- Interest is payable on ₹20,000 — the extent of overall shortfall.

## **2. CGST Credit Utilisation: A Need for Consistency**

Currently, departmental authorities are evaluating CGST utilization ledger-wise, despite being part of the same fungible ITC system (under Section 49B). This creates unintended interest liability even when sufficient credit exists in other heads. Before assessing the interest liability on wrong utilization of CGST Credit, we need to understand the relevant legal provisions for the same.

In terms of Section 49(5)(c) of the CGST Act which reads as **“The ITC on account of State tax shall be utilised towards the payment of integrated tax only when the balance of central tax is not available”**.

The **proviso** mandates that **SGST credit can be used for IGST only when CGST credit is exhausted**, making it mandatory to utilise CGST before SGST for IGST payments.

This sequencing creates a **technical hierarchy**, which may lead to compulsory utilisation of CGST Credit even though the registered person **is not intended to utilise the CGST Credit**.

Circular 192/04/2023-GST does not address this scenario directly. However, the underlying principle i.e., interest should arise only when the taxpayer derives actual benefit due to credit shortfall can be logically extended to CGST as well is the opinion of the author.

### **Example 3: Sufficient Overall ITC, Interest not applicable**

- Wrongly Availed CGST Credit: ₹70,000

- Credit Balances:
- IGST: ₹50,000
- CGST: ₹40,000
- SGST: ₹30,000
- Total ITC = ₹120,000
- No interest in the opinion of the author - even though the CGST balance is ₹30,000 short, the total credit is sufficient. The same aggregate balance logic used for IGST to CGST preventing interest where there is no undue benefit.

### **3. SGST Credit Utilisation: Similar Logic, Same Problem**

The balance in IGST needs to be utilized first in accordance with section 49A of CGST Act. The balance of IGST credit left after utilizing for IGST liability can be utilized for making payment of Central Tax or State Tax as the case may be in that Order. Even though the Order of utilization of specified, the extent of utilization is not specified. For example, If an IGST balance of ₹25,000 exists in after utilizing for IGST liability, we can utilize ₹5,000 for CGST liability and ₹ 20,000 for SGST liability subject to the condition that IGST credit is fully utilized first.

Considering the above conditions, the different permissible methods of utilization IGST credit results in different CGST and SGST closing balances. Taking an isolated view disregards the overall ITC position and imposes interest merely due to head-wise shortfall, not actual economic benefit.

Adopting the IGST approach from Circular 192/04/2023-GST, the interest should be triggered only when the total credit across all heads is insufficient, not just based on SGST ledger balance.

#### **Example 4: Technically Utilised, Practically Not – interest not liable**

- Wrongly Availed SGST Credit: ₹30,000
- Credit Balances:
- SGST: ₹10,000
- CGST: ₹40,000
- IGST: ₹60,000

- Total ITC = ₹110,000
- Under a holistic view, no interest should apply. Uniformly treat all fungible ITC (IGST, CGST, SGST) using total credit balance to determine whether a real shortfall exists.

#### **4. Compensation Cess: Ring-Fenced, Ledger-Specific Treatment Required**

Unlike other ITC heads, Compensation Cess is not fungible. As per Section 11 of the Compensation to States Act, it can only be utilised for payment of Compensation Cess, making a ledger-specific interest evaluation necessary.

##### **Example 5: Interest Applies Even if Other Ledgers Are Full**

- Wrongly Availed Compensation Cess Credit: ₹25,000
- Credit Balances:
- Compensation Cess: ₹20,000
- Other ITC (CGST/SGST/IGST): ₹150,000
- Interest on ₹5,000 applies because only ₹20,000 is available in the relevant ledger.

##### **Example 6: Sufficient Cess Credit**

- Wrongly Availed Compensation Cess: ₹10,000
- Cess Ledger Balance: ₹15,000
- No interest, as the ledger itself holds enough to cover the irregularity.

#### **Conclusion: A Case for Rational Uniformity**

The spirit of Circular 192/04/2023-GST recognises that interest should only arise when taxpayers actually derive an undue benefit from wrong ITC and not due to ledger sequencing or system restrictions. The rationale can be supporting by the Kerala High Court judgement in the case of *“Rejimon Padickapparambil Alex v. Union of India and Others [2024 (12) TMI 399 - KERALA HIGH COURT] and Star Roofs and Metals Vs. The Assistant Commissioner Tax Payer Ernakulam & Others” (W.P.(C). No.44100 Of 2024)*, held that, *“the alleged mistake committed by the petitioner is by availing the benefit of Input Tax Credit available in IGST, under the heads CGST and SGST. The said method of availing ITC cannot be said to be a wrong availment of Input Tax Credit warranting the imposition of any penalty as observed in the above referred judgment. Therefore, it is only appropriate*

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*that the order of assessment itself is set aside and a reconsideration be directed by the proper officer.”*

The author concludes as follows:

- **IGST, CGST, and SGST:** Interest under Section 50(3) should be triggered only when the combined credit pool is insufficient, not head-wise.
- **Compensation Cess:** Must continue to be treated ledger-specifically due to statutory restrictions on cross-utilisation.

Head-wise interest computation leads to artificial liability and undue financial burden, especially where the taxpayer had no intent to defraud and held sufficient credit overall.

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