

## **GST - ITC on the construction of immovable properties – Orissa High Court**

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The Constitutional (101) amendment Act 2016 clearly states in the Statement of Objectives for ushering in GST that it is to remove the cascading effect of taxes and allow the seamless flow of the tax credit across the supply chain. It means that it should avoid tax on tax.

Conceptually, GST is levied on ONLY value addition at each stage of supply chain starting from manufacture or import and till the last retail level. This is with a facility of the Input credit ('ITC' for short) of taxes paid on the procurements (goods/services) made and allowing to utilise for payment of GST on the output. Any restrictions on ITC availment would result in the cascading effect of taxes and disturb the aforesaid object of GST. In case of export of goods or service, no tax is to stick with the value of supplies to make Indian exports competitive. The buildings/ factories/ shops are vital for the conduct of businesses as much as machines, raw material or services.

### **Past Judgements:**

In the landmark judgment of Dai Ichi Karkaria -1999(112) ELT 353(SC) it was observed that Cenvat credit once eligible is denied only if it is availed illegally or irregularly. In the Jawahar Mills case 2001(132) ELT 3(SC) it was observed in regard to what is a plant & machinery that the principles of the decisions in Income Tax ( more developed law) could be used as precedent in Central Excise. In Income tax a theatre ( Anand Theatre), sanitary fittings and pipelines ( Taj Mahal Hotel) building for power generation ( KPC) were considered as a plant.

Normally, taxes paid on all business procurements are allowed as ITC but certain credits are specifically restricted/blocked (popularly known as 'blocked credits'). One among them is the ITC on goods/services used for 'construction of immovable property' which is specifically restricted under section 17(5)(d) of CGST Act, 2017 which reads as under:

*“(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”*

In terms of the above restriction, the prevailing understanding is that ITC on goods/services used for the construction of immovable properties is allowed only if the immovable property is meant for sale/transfer and in all other cases, ITC is not allowed. That is to say, if the immovable property is not sold but let out, ITC is not available on the goods/services used for construction even though the supplier is made liable for payment of GST on the lease rentals. This provision was challenged before Hon’ble High court of Orissa which declared its verdict recently reported in [Safari Retreats Pvt Ltd Vs C.C Of CGST 2019-TIOL-1088-HC-ORISSA-GST](#). In this background, an attempt has been made in this article to explain the Orissa High Court decision and its implication.

#### **Facts of the case:**

Petitioner is mainly engaged in the construction of shopping malls for the purpose of letting out. For this purpose, the Petitioner has purchased various materials/services like Cement, steel, architectural services, etc., on which applicable GST has been charged by the vendors. Petitioner is desirous of availing the ITC of GST charged on the aforesaid procurements and utilize towards the payment of GST on the lease rentals. However, the revenue department had advised to deposit the GST on the lease rentals without taking the ITC in view of the restrictions placed under Section 17(5)(d), *ibid* and warned of penal consequences for availing ITC.

#### **Contentions raised by the Petitioner:**

The petitioners has contended that Section 17(5)(d) of the CGST Act, 2017 is to be read down for the purpose of interpretation to enable benefit to the assessee or to the person who has paid GST. Further, it has to be interpreted in the continuity of the transaction since rent income is arising out of the Malls which are constructed after paying GST on different items *inter alia* on the following grounds:

Ø GST has been introduced with the object of avoiding the cascading effect of various indirect taxes, therefore, the denial of ITC on goods and services used for further supply of services on which GST is payable is not correct as there is no break in the tax chain

Ø If immovable property is sold after issuance of completion certificate there is a break in the tax chain as there is no GST liability, therefore, the denial of ITC in case

of property sold after completion certificate may be valid as there is a break in the tax chain.

Ø However, the position is completely different if the immovable property is constructed for the purpose of letting out of the same as the tax chain will not get broken. Therefore, the denial of ITC is completely arbitrary, unjust and oppressive.

Ø To grant an input tax credit to a builder who sells the building where completion certificate has not been issued at the time of sale while denying it to a person like the Petitioner is patently and egregiously arbitrary and discriminatory under Article 14 of the Constitution.

Ø Such an interpretation of Section 17(5) (d) of both CGST and OGST Act leads to double taxation, i.e., firstly, on the inputs consumed in the construction of the building and secondly, on the rentals generated by the same building.

Ø It would also be violative of the Petitioners' fundamental right to carry on business under Article 19(1)(g) of the Constitution as it would impose a wholly unwarranted and unreasonable and an arbitrary restriction which would render buildings now constructed for letting out uncompetitive, by imposing the burden of double taxation of GST on such buildings

Ø As the shopping mall is intended for letting out, the same shall not be considered as constructed 'on his own account' therefore the restriction under 17(5)(d) shall not be applied.

#### **Revenue department contentions:**

Ø The taxpayer cannot claim credit accumulated due to the supply of inputs (goods as well as services) used by them for construction of their project as a vested right for payment of GST on the output taxable supply of Renting of their said property;

Ø Powers to restrict the flow of credit also exist under Section 16(1) of the CGST Act which empowers the Central Government to impose conditions and restrictions on availing input tax credit. This shows a Legislative intent that input tax credit may not always be allowed partially or fully. Input tax credit provisions do not provide for that all the tax paid on inputs should be available as credit. Some credits have been denied under section 17 in the Act itself and to allow flexibility, the Act provides that restrictions can be placed on the availability of credit.

Ø Section 17(5)(d) of the CGST Act prescribes denial of credit for a certain class of taxpayers with certain conditions and limitations. This would mean that the legislature has decided in its wisdom the credit of taxes which would be allowed in credit as ITC and the tax that has not been allowed, as policy call of the Government, given effect through legislation, cannot be obtained through judicial review.

#### HC Decision:

ü The very purpose of the Act is to make the uniform provision for levy collection of tax and to prevent multi taxation;

ü The narrow construction of interpretation put forward by the revenue department is frustrating the very objective of the CGST Act as the assessee has to pay a huge amount without any basis. The assessee would have paid GST if the property is disposed of before the completion certificate is granted and in case the property is sold after completion certificate he would not be required to pay any GST. But in the instant case, the assessee is retaining the property and is letting out the same on which GST is being paid. Even though the assessee is not using the same for his own purpose still he has to pay a huge amount of GST which is not liable to be paid.

ü The provisions of Section 17(5)(d) is to be read down as the very purpose of the credit is to give benefit to the assessee. If the assessee is required to pay GST on the rental income arising out of the investment on which he has paid GST then the assessee is eligible to an input credit of GST paid on inward supplies used for the construction of such property.

#### Impact of the decision:

ü By virtue of the above HC decision, taxpayers are now allowed to avail ITC on the goods/service used for the construction of commercial properties as long as applicable GST has been paid on lease rentals.

ü It acts as the precedential value in the similar cases of ITC denial and also restrictions that frustrate the objective of GST like cascading effect, double taxation, etc.

**Possible Course of action:**

1. Taxpayers can avail ITC on the procurement made for the construction of commercial properties (Mall, shops, plug & play commercial properties or plain commercial properties. etc.,) meant for letting out. On the same logic the factory or office buildings used for providing taxable services or production of goods should also be able to make their claim.
2. The procurements made during FY 2018-19 can be safely availed on or before filing the return of September 2019.
3. The procurements made during FY 2017-18 may not be available as the time limit has expired ( which again maybe a matter for Court to examine) though there is a view that GSTR 3 is the due date and not GSTR 3B.
4. If the taxpayers do not wish to take risk of future interest/penal cost for 2) or 3) above, the ITC availed may be reversed immediately under protest with an intimation to the department providing reasons such as avoiding disputes, possible interest/ penalties on record. This would protect the time limit for availment later or claim a refund in the future when issue is clearer.
5. If amounts are larger and one wishes to avoid disputes at any cost, they can file a petition before the jurisdictional High courts and get similar directions /orders.

**Conclusion:**

This judgment would go to the apex court but appears to be in the authors views the correct direction in line with the pristine principles of GST.

Special thanks to CA Madhukar N Hiregange and CA Venkata Prasad for penning this article. For any further queries/comments please write to [madhukar@hiregange.com](mailto:madhukar@hiregange.com), [venkataprasad@hiregange.com](mailto:venkataprasad@hiregange.com).

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