

Transitional Credit of stocks older than one year - whether available in GST?

Transitional provisions in GST law provides the tax treatment for transitional transactions and issues arising thereof. One of the key transitional issues is whether input tax credit can be availed in respect of stocks lying with the business on the appointed day (i.e. 01.07.2017). This issue does not bother much to the manufacturers since they were availing the input tax credit of Central Excise and local VAT in their returns filed and were also utilizing the same against the output tax liability.

However, traders or service providers were fully not able to avail the credits as there was no any output excise liability for traders and no VAT liability for service providers and therefore the credit of Central Excise duty, Additional Duties of Customs, VAT etc. lying in stock as on the appointed day was not available.

Therefore, in order to enable the taxpayers mainly traders and service providers or any such class of persons who did not avail the credit of duties, taxes on stocks in the earlier tax regime but will be paying output GST on sale of such stocks in the GST regime, government has provided section 140(3) to facilitate transit of these credits into the GST regime.

One important aspect to note here is that although section 140(3) has enabled the transit of these credits but it puts a restrictive condition that credit on goods purchased prior to **twelve months** from the appointed day cannot be transferred to GST i.e. if the goods lying in stock are older than one year then the credit will not be allowed to be transferred even if GST is paid upon sale of the same.

This article attempts to analyze the restrictions placed in section 140(3) from legal stand point and also provides a practical way out that a business may look at from the commercial stand point to deal with a situation where large value of goods aged more than one year are lying in stock as on appointed day.

Principle of Equality

Section 140(3) of the GST law provides elaborate provisions to take credit of eligible duties in respect of inputs/finished goods held in stock on the appointed day **where invoices were issued not earlier than twelve months immediately preceding the appointed day**. However, section 140(3) specifically restricts the credit on inputs/finished goods held in stock for more than twelve months.

However, proviso to section 140(3) states that **a person who is not in possession of an invoice**, can avail credit at such rate as is prescribed in rules.

Therefore, combined reading of the provisions gives clear interpretation that if a person is in possession of duty paying documents or invoice then credit shall be restricted to only those goods which are held for not more than twelve months in stock. However, if a person is not in possession of duty paying documents or invoice then there is no such restriction in law and credit can be availed in respect of stock held for more than twelve months as well from the appointed day.

This leads to a breach of principle of equality and legislation violates the fundamental principle as provided in article 14 of the constitution of India.

Similarly held in case of ***Union Of India Vs. N.S. Rathnam & Sons 2015 (322) E.L.T. 353 (S.C.)*** “When it is granted to particular class of persons, its benefit has to be extended to all similarly situated person. It has to apply to entire class and Government cannot create sub-classification thereby excluding one sub-category, even when both sub-categories are of same genus - If that is done, it would violate equality enshrined in Article 14 of Constitution of India - Hence, judicial review of such Notifications is permissible to prevent invidious discrimination between two persons belonging to same class.”

Similarly in case of ***Gujarat Paraffins Pvt. Ltd. Vs. Union Of India 2012 (282) E.L.T. 33 (Guj.)*** it was held that same rules of law and remedies should be applicable to all persons within Indian territory, irrespective of difference of circumstances. All persons similarly circumstanced shall be treated alike, both in privileges conferred and liabilities imposed.

Hence, based on the ratio of above judgments, one can state that there should be no discrimination between assessee’s possessing invoices and the ones who are not possessing invoices. If credit is allowed on entire stock for assessee’s not possessing invoices, the same cannot be denied for assessee’s having relevant documents for stock held for more than 1 year.

Defeats The Object Clause of GST Law

It is also important to note that the entire goods held as stock on 30.06.2017 including the stock held for more than one year will be sold in the GST regime and assessee will be levying and paying output GST on such sale. Therefore, blocking the credit on the stock and charging output tax on the goods will result into cascading effect of taxes which is very much against the object clause of the GST Act.

According to the Statement of Object and Reasons backing behind the 101st Amendment of the Constitution, the purpose for introducing Goods and Service Tax was to remove cascading effect of taxes levied by the Central Government which were not available as set off against the taxes levied by the State Government and to **broad base the input tax credit** by making it available in respect of any supply of goods or services or both used or intended to be used in the course of furtherance of business.

As the credit is restricted on the stocks held for more than one year, the input tax on the same will be get added to the cost of the goods and hence at the time of sale the output tax shall be levied on an inclusive of input taxes, resulting into cascading effect of taxes. Hence, this provision also violates the very object of introducing GST as stated in the 101st Constitution Amendment Act.

Obstructs Rights & Privileges Accrued Under Earlier Act

Section 174(2) of the GST law states that the repeal of the earlier Acts and the amendment of the Finance Act, 1944 shall not ***affect any right, privilege, obligation, or liability acquired, accrued or incurred***

under the amended Act or repealed Acts or orders under such repealed or amended Acts.

It is important to note that certain assesses got themselves registered under the Central excise law as import dealer or first stage/ second stage dealer and complied with the provisions of the excise law to pass on the benefit of Central excise duty and additional duty of customs to their customers.

Rule 9(4) of the erstwhile CENVAT Credit Rules' 2002 gives right to the import dealer to pass on the CENVAT credit on input or capital goods purchased subject to conditions that the Import dealer has maintained records, filed returns, issued proper invoice etc.

Therefore, the right which has accrued to such dealers under the erstwhile act cannot be affected by repeal of the earlier act and enforcement of the new act. Thus, the saving clause of section 174 preserves the right of the applicant to pass on the CENVAT credit as a registered Import dealer.

Interim Order Passed By Delhi High Court

Further, recently in the writ petitions filed by ***GMMCO Limited vs UOI (W.P.(C) 9539/2017, C.M. APPL.38777/2017) & ANR*** and ***Hafele India Private Limited Vs. Union of India & ANR (W.P.(C) 9572/2017, C.M. APPL.38984/2017)*** assessee contented that such restriction upon persons possessing invoice is arbitrary in as much as proviso thereto allows deemed credit at prescribed percentage without any restriction to persons not possessing invoice.

Therefore, Delhi High Court has allowed and heard the writ petition and passed an order on 11.12.2017 allowing interim relief by stating that ***“we have heard learned counsel for the parties and are of the opinion that the matter requires to be heard in greater detail. In the meanwhile, it is open to the petitioners to proceed and claim credit or pay duty, as the case may be. In case any duty amounts are paid, that will be subject to final outcome of the proceedings.”***

Various available options from commercial stand point:

However, in view of specific provision in the law restricting such credit, assesses may look at the option of availing the credit in the GST returns by filing/ revising the TRAN 1 form and later voluntarily reversing the same under protest with intimation to department. This step would ensure that the right of the company in case of favorable decision is protected and at the same time, there will not be any adverse consequences as to the interest or penalty.

Once the clarity emerges by way of final judicial precedents or course correction in the law, then one can apply for refund and claim the entire credits reversed. Needless to say that the limitation period for claiming refund of 2 years would not apply in cases where taxes are paid/ reversed under protest.

Further, one can also take a more aggressive stand of availing these credits in returns and instead of reversing the same, the same can be kept in abeyance by not utilizing the same and once clarity emerges, then the same can be later utilized for payment of output taxes. However, support of GST portal needs to be looked into before choosing this option

which may not allow the tax payers to pay taxes in cash with balance lying in credit account.

Another option can be to avail and also utilize these credits which may yield immediate benefits to the business but it would be more risky one and may lead to unnecessary interest and penalties in case the eventual decision is not favorable.

Further, if the time limit for claiming such credit in Form TRAN 1 is expired then one may also look at claiming the same directly in GSTR 3B as 'other credits' and account for the same in the same month in the books of accounts as procedural hurdles in transitional process cannot deny the substantial benefit available in earlier law. One may also look at filing of writ petition before the High court and avail ad interim relief on the matter.

Conclusion:

In light of the above legal stand point, one can arguably state that the restriction placed in section 140(3) denying the credit to assesses for goods lying in stock for more than one year is unfair and unjust and therefore considering the values and the risk appetite, businesses have to take a practical decision on the same from commercial stand point based on various options available at their disposal.

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