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Refund of unutilised GST Input Tax Credit on Closure of Business

[Our Detailed Analysis post decision of Divisional Bench of Sikkim High Court]

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Introduction:

When the Goods and Services Tax (GST) was brought, the primary objective was to prevent the cascading effect of taxes, which occurs when tax is levied on tax at multiple stages of the supply chain. To achieve this the law provides a flow of credit from one stage of supply to the next. The cornerstone of this system is the mechanism of Input Tax Credit (ITC). ITC allows a registered person to adjust the taxes already paid on inputs such as goods or services used in the course of business against their output tax liability. In essence, it ensures that the tax burden falls only on the final consumer and not on intermediate businesses engaged in the supply chain.

While ITC is a statutory entitlement but its refundability from the department is generally understood to be ring fenced. The CGST Act, 2017 prescribes certain circumstances where refund of unutilised ITC is permitted. The legal dispute with respect to the statutory limits of section 54 providing for refund of taxes paid came to the fore in the decision pronounced by the Sikkim High Court in the case of ***SICPA India Pvt. Ltd. v. Union of India.***

In June 2025, a Single Judge of the Sikkim High Court directed refund of unutilised ITC on business closure based on the reasoning that denial of refund would amount to unauthorised retention of tax. However, in September 2025, a Division Bench of the same Court decisively overturned that ruling reaffirming the restrictive statutory framework.

Statutory Framework – Key Legal Provisions:

Before analysing the judgments, it is essential to set out the relevant statutory provisions.

- **Cancellation of Registration:** Firstly, Section 29(5), CGST Act in the context of cancellation of GST registration provides that every registered person whose registration is cancelled shall pay an amount, by way of debit in the electronic credit ledger or electronic cash ledger, equivalent to the credit of input tax in respect of inputs held in stock, inputs contained in semi-finished or finished goods held in stock and on capital goods or plant and machinery on the day immediately preceding the date of such cancellation.

- **Refund of balances in ECrL:** Further, Section 49(6), CGST Act in the context of refund of the balances lying with the tax authorities that the balance in the electronic cash ledger or ***electronic credit ledger*** after payment of tax, interest, penalty, fee or any other amount payable under this Act or the rules made thereunder may be refunded in accordance with the provisions of Section 54.

- **Refund of Unutilised Credit:** Further, Section 54(3), CGST Act in the context of refund of input tax credit states that **a registered person** may claim refund of any unutilised input tax credit, however no refund of unutilised input tax credit shall be allowed in cases other than—
  i. zero rated supplies made without payment of tax;
  ii. where the credit has accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies (other than nil rated or fully exempt supplies).

- **Incidence of Tax:** Further, Section 54(8)(e) in the context of the refund of tax paid, provides that the refund of the tax amount shall be credited to the taxpayer if the incidence of such tax and interest has not been passed on to any other person.

The Facts in the SICPA Case:

SICPA India Pvt. Ltd., engaged in the manufacture of security inks, operated a facility in Sikkim. With operations discontinued in 2019 and assets sold by 2020, the company cancelled its registration. At this time, an accumulated ITC balance of approximately ₹4.37 crore remained.

SICPA applied for refund of this balance under Section 49(6) categorising its claim as "any other" in Form GST RFD-01. The claim was rejected by the Assistant Commissioner (2022) and the Appellate Authority (2023) on the ground that Section 54(3) permits refunds only in specific cases and closure of business was not one of them. Aggrieved, SICPA filed a writ petition before the High Court.

Decision by the Sikkim High Court (Single Judge Bench):

The decision was rendered that the closing balance of input tax credit lying in the electronic credit ledger shall be refunded back to the taxpayer, the said decision was based on the following key reasons:

- No express prohibition exists in Section 49(6) read with Section 54 against refunds on closure of the business.
- Article 265 of the Constitution ("no tax shall be levied or collected except by authority of law") prohibits retention of taxes without legal sanction. Denial of refund would amount to unauthorised expropriation.
- Precedent from the pre-GST regime — particularly ***Union of India v. Slovak India Trading Co. Pvt. Ltd.*** **(Karnataka HC, 2006)** — Refund of unutilised CENVAT credit on business closure based on Article 265.

Decision by the Sikkim High Court (Divisional Bench):

Later, on an appeal (W.A. No. 2 of 2025) being filed against the decision of the single member bench, the Division Bench allowed the appeal and set aside the Single Judge's ruling, and held that SICPA was not entitled to refund of ITC upon business closure based on the following premise:

- The Bench stressed that Section 49(6) allows refund only "in accordance with Section 54." It cannot be read as a standalone source of refund entitlement.
- Refund of unutilised ITC u/s 54(3) is exhaustive and it expressly is confined to the following two situations:
  i. Zero-rated supplies without tax payment, and
  ii. Inverted duty structures.
- Closure of business does not fall within these categories. To allow such refunds would amount to judicial legislation.
- The Bench relied on the decision of Hon'ble Apex Court in the case of *Union of India v. VKC Footsteps India Pvt. Ltd.* (2022) 87 GST 257 (SC), where the Supreme Court held:
  - ✓ Refund is a statutory right, not a constitutional entitlement.
  - ✓ Section 54(3) is restrictive, and Parliament has legislative competence to limit refunds.

- The Court observed that SICPA had not shown proof of reversal under section 29(5) and refund was sought under the vague "any other" category without statutory support.

Our Detailed Analysis:

On a detailed study of the statutory provisions and both judgments in the SICPA matter, while the decision of the divisional bench is conclusive and backed by proper reasoning, however, based on a careful reading of the overall scheme of the CGST Act, one needs to evaluate if the decision is ***Per incuriam*** meaning if it misses certain key statutory provisions laid out in the GST law and an overall scheme of the GST law.

The decision is given on the ground that CGST Act, 2017 does not contain any express provision allowing refund of such unutilised credit on cancellation of registration. Further, the assessee's argument on constitutional principles of Article 265 were also quashed on the premise that Refund is a statutory right, not a constitutional entitlement.

In other words, the Division Bench rejected the refund, holding that refund is a statutory right confined strictly to the circumstances enumerated under Section 54(3). The constitutional argument, though attractive from an equity standpoint, was thus considered insufficient to override the legislative intent.

Various facets of GST law not brought out or considered in the above decision:

In our view, the court in its all wisdom while rendering the decision to restrict the refund purely on the reading of section 54 (3) of the CGST Act, 2017. However, in our view, it would be too narrow an understanding if the same were without analysing the overall scheme of the GST law and the various other relevant provisions.

We shall now endeavor to bring out various provisions of the GST law that also need to be interpreted in consonance with section 54(3) of the CGST Act to arrive at a more informed decision.

Implication of Cancellation of Registration u/s 29:

- As per the CGST Act, 2017 the liability to reverse ITC at the time of cancellation of registration is specifically dealt with under Section 29(5). This provision mandates that a registered person whose registration is cancelled shall pay an amount equivalent to the credit of input tax in respect of inputs held in stock, semi-finished or finished goods, and capital goods or plant and machinery on the day immediately preceding such cancellation.

- In other words, from the above it can be gauged that the law itself identifies the precise categories of credit that are required to be reversed upon closure of

business. This provision does not explicitly provide for what happens to the balance lying after the above reversal of credits.

- Therefore, a clear interpretation that can be derived from the above is that when there is an express provision u/s 29(5) providing for reversal of credit to the tune of goods lying in stock, then the reversal shall only and only be restricted to that amount only. In other words, if the refund is not to be granted for the balance over and above this reversal, then there no meaning to the existence of section 29(5). Meaning that the section could have simply stated that the any amount lying in the electronic credit ledger upon cancellation of registration be lapsed.

- Therefore, by not granting refund, the legislation is usurping its own obligation beyond Section 29(5) and is expanding its scope beyond the text of the statute.

- However, Section 29(5) is silent on the fate of the balance ITC that may remain in the electronic credit ledger after the mandated reversal. The provision is confined to identifying the categories of credit which must be neutralised upon cancellation of registration. It does not expressly provide for extinguishment of any surplus credit beyond that reversal. This legislative gap creates ambiguity once the statutory reversal has been carried out, the law does not clarify whether the residual balance should lapse.

Comparison of Section 18(4) with Section 29(5):

- Now, if one assumes that since the law u/s 29(5) is silent, hence it must be assumed that the balance in Electronic credit ledger would lapse, however a useful comparison may be drawn with **Section 18(4)** of the CGST Act, 2017 which explicitly provides that where a taxpayer switches from taxable to exempt supplies or opts for the composition scheme, the balance of **ITC remaining after the required reversal shall lapse**.

- In other words, in a similar situation, the legislature, therefore, made its intent clear in that context by expressly providing for lapse of the credit.

- Whereas, **no provision providing for lapse of input tax credit was incorporated in Section 29(5)**. This deliberate omission indicates that the scope of Section 29 is confined only to the reversal expressly prescribed therein, and not to the extinguishment of any residual balance. Accordingly, it can be argued that unutilised ITC left in the ledger after such reversal cannot be deemed to lapse automatically.

- If the lawmakers had an intention of lapsing the input tax credit, they would have expressly provided for the same as provided u/s 18(4).

The Division Bench also fortified its reasoning by relying on the principle laid down in ***Commissioner of Sales Tax v. Modi Sugar Mills Ltd.***, where the Supreme Court

observed that *"the Court must look squarely at the words of the statute and interpret them. It must interpret a taxing statute in the light of what is clearly expressed; it cannot imply anything which is not expressed."*

Applying this principle, the taxpayer may contend that Section 29(5) must be read strictly in accordance with its text. The provision expressly requires reversal of ITC relatable to inputs, semi-finished goods, finished goods and capital goods on the date immediately preceding cancellation. Beyond this, the statute is silent.

Therefore, once these mandated reversals are effected, there is no legal basis to insist on extinguishment of the residual balance lying in the electronic credit ledger. To read into Section 29 an implied requirement of reversal or lapse of the balance would be to do precisely what the Supreme Court has cautioned against in fiscal statutes i.e., supplying words that the deliberately not chosen to be used in the statute.

Scope of section 54(3) is restricted only to Registered Persons and cannot be extended to unregistered persons:

We shall now do a plain reading of **Section 54(3)** which provides as under:

"Subject to the provisions of sub-section (10), ***a registered person*** *may claim refund of any unutilised input tax credit at the end of any tax period."…….*

Now, the simple plain term used here is "**registered person**." meaning thereby that the restriction laid out u/s 54(3) granting refund of unutilised ITC is restricted only to registered persons. In other words, an assesse when closes the business and cancels the GST number, it ceases to be a registered person and thereby, it needs to be first analysed whether at all the analogy of section 54(3) be even applicable in the present circumstances.

In order to appreciate the same, we shall now dwell upon **Section 2(95)** of the CGST Act, which defined the term registered person as under:

"*registered person" means a person who is registered under Section 25, but does not include a person holding a Unique Identity Number".*

Accordingly, until the effective date of cancellation, the taxpayer remains a "registered person" in the eyes of law and should, in principle, be entitled to invoke Section 54(3).

In the present case however, the taxpayer had already surrendered its registration. Once registration stands cancelled, the person ceases to fall within the ambit of a "registered person" under Section 2(95). Consequently, the department cannot seek refuge under Section 54(3) to deny the refund, as that provision extends the right of refund only to a "registered person" and subjects it to restrictive conditions.

In other words, section 49(6), clearly states that any balance lying in the electronic credit ledger shall be refunded back as per the provisions of section 54. It

does not say as per 54(3). Meaning thereby, the coverage of section 49(6) is wide to cover entire section 54 and not merely section 54(3).

Now, from the bare reading **of Section 54(1)** it is clear that the same is wide to cover any person. Further, the meaning of the term 'person' as defined u/s 2(84) also covers unregistered persons. The provision precisely states as under:

"Any person claiming refund of any tax and interest, if any, paid on such tax or any other amount paid by him, may make an application before the expiry of two years from the relevant date in such form and manner as may be prescribed."

It applies to "any person" and extends to refund of "any amount" paid under the Act. Which means a person who has surrendered his registration can also claim the refund.

Doctrine of Unjust Enrichment:

Further, this view can also be supported from Section **54(8)(e)**, which provides for various scenarios in which the refund of taxes paid shall be credited to the taxpayer where the incidence of such tax and the interest thereon has not been passed on to any other person.

This provision reflects the legislative intent that the Government should not unjustly retain amounts which, in substance, have been borne by the taxpayer and not shifted to consumers.

In the context of unutilised ITC remaining after business closure, it is clear that such credit represents tax already paid on inputs but not transferred down the supply chain. The incidence of tax has, therefore, remained with the taxpayer.

Reliance may be placed on the Constitution Bench judgment in ***Mafatlal Industries Ltd. v. Union of India*** **(1997) 5 SCC 536**, where the Supreme Court emphatically held that *"**The doctrine of unjust enrichment** is a just and salutary doctrine. The appellant cannot collect the duty from his purchaser at one end and also collect the same duty from the State on the ground that it has been collected from him contrary to law. … The doctrine of unjust enrichment is inapplicable to the State. State represents the people of the country. … Thus, the person claiming restitution should have suffered a 'loss or injury'. In cases where the assessee or the person claiming refund has passed on the incidence of tax to a third person, it can't be said that he has suffered a loss of injury. … It is for him to allege and establish that he has not passed on the burden of the duty to a third party. … The refund should really be made to the persons who have actually borne its burden."*

This ruling reinforces that refund claims must be tested on the touchstone of unjust enrichment. Where the taxpayer has borne the incidence of tax without passing it on, refund is consistent both with equity and statutory design. Applied to the present

case, the balance ITC stranded in the electronic credit ledger upon business closure clearly remained with the taxpayer, since it was never passed down the supply chain.

By a combined reading of Section 54(8) of the CGST Act and the principle of unjust enrichment laid down in *Mafatlal Industries Ltd. v. Union of India*, it is evident that refund cannot be denied where the incidence of tax has not been passed on to any other person.

In the present case, the balance ITC stranded in the electronic credit ledger upon business closure represents tax already discharged on inputs and borne entirely by the taxpayer. Since this burden has not been transferred down the supply chain, the doctrine of unjust enrichment does not operate as a bar. Accordingly, on the grounds discussed above, the taxpayer has a legitimate claim to seek refund of the unutilised ITC balance.

Constitutional mandate does not allow collection of taxes without the authority of law:

While the GST framework does not expressly provide for refund of unutilised ITC on business closure, the matter must also be assessed in light of constitutional guarantees.

Article 265 of the Constitution of India lays down a fundamental principle of taxation by providing that *"no tax shall be levied or collected except by authority of law."* This constitutional mandate ensures that both the imposition and the collection of taxes must strictly flow from a valid legal enactment. In other words, the State cannot, on its own discretion, demand, collect, or retain any sum of money from taxpayers unless such authority is expressly conferred by a statute enacted by a competent legislature.

The scope of this Article extends not only to the initial levy and subsequent collection of taxes but also to situations where the State seeks to retain amounts already received. If there is no statutory backing for such retention, it would amount to an unauthorized exaction, which is constitutionally impermissible.

In the present case, the unutilised ITC balance is in substance, *as good as tax paid*. By refusing to grant refund of this amount, the authorities are effectively seeking to retain tax without any express statutory backing. Such retention not only undermines the neutrality principle of GST but also runs contrary to Article 265 of the Constitution, which prohibits collection or retention of tax without authority of law.

Reliance may be placed on the judgment of the Supreme Court in ***Collector of Central Excise v. Dai Ichi Karkaria Ltd.*** **(1999)**, wherein the Court categorically held that *"a credit under the MODVAT scheme was as good as tax paid."* The principle laid down is of enduring relevance input tax credit is not to be viewed as a conditional concession, but as representing taxes already discharged on inputs, bearing the same legal character as tax actually paid into the exchequer.

Reliance may also be placed on the decision of the Karnataka High Court in ***Union of India v. Slovak India Trading Co. Pvt. Ltd.*** **(2006)**, where it was held that refund of unutilised CENVAT credit should be allowed upon closure of business. The Court reasoned that when credit validly availed cannot be utilised due to discontinuance of operations, denial of refund would result in unjust retention of tax by the State. Though this ruling arose in the pre-GST regime, its underlying rationale remains relevant accumulated credit represents tax already discharged and its extinguishment without statutory sanction would offend both the scheme of value-added taxation and the mandate of Article 265 of the Constitution.

Support can further be drawn from ***Calcutta Electric Supply Corporation v. Income-Tax Officer*** **(1991)**, where the Calcutta High Court observed that *"This view is further entrenched by the well-known rule of interpretation of laws or taxing statutes which are interpreted in favour of the assessee, and that the State shall not tax more than it has given itself an express power for. If the taxing provisions are to be interpreted against the taxing authorities, the refund-giving provisions must as a logical corollary be interpreted liberally also in favour of the assessee."*

The above decisions provide a strong constitutional foundation as to why the taxes cannot be collected beyond authority and that the same is ought to be refunded back to the person who has borne its burden. In the present case, the argument laid out by the petitioner placing reliance of article 265 of the constitution and the decision of Karnataka High Court was not considered relying on the decision of apex court in VKC Footsteps.

The facts in the case of VKC footsteps in the realm of which the decision was given by the apex court were completely different. In that case, the business was continuous, and the assessee was still a registered person claiming refund of input services on account of tax rate inversion, whereas the facts in the present case are starkly different.

Hence, a decision rendered without any reasoning and based on simple reliance on another decision having totally different facts is incorrect application of a precedent. It is well-known legal principle that reasoning is the soul of any decision and a decision, and any order passed without proper reasoning can be considered as good as a non-speaking order.

Conclusion:

While the Division Bench of the Sikkim High Court has taken a strict view that refund is confined to the two situations specified under Section 54(3), a broader and a more wholistic reading of the CGST Act in light of constitutional principles suggests otherwise.

Section 29(5) mandates only specific reversals and does not provide for lapse of residual credit. Further, Section 54(1) read with Section 54(8)(e) permits refund where the incidence of tax has not been passed on. ITC is as good as tax paid, refund cannot

be denied without authority of law and refund provisions must be interpreted liberally in favour of the assessee. Further, the scope of section 54(3) cannot be expanded to unregistered persons.

In essence stranded ITC on business closure represents tax already borne by the taxpayer and not passed through the supply chain. Retaining such amounts without a statutory lapse provision risks violating Article 265 of the Constitution.

The matter now calls for either authoritative resolution by the Supreme Court or legislative intervention by the GST Council to ensure that the fundamental principle of GST as a consumption-based tax is upheld and no tax is retained without clear authority of law.

More specifically, for taxpayers can still seek justice by filing an application for refund and hope that the better sense prevails….!!

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