07 May 2019

EY Tax Alert

HC rules interest on delayed payment of tax to be computed on total tax liability

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Executive summary

This Tax Alert summarizes a recent ruling of the Telangana High Court (HC)[1]. The issue involved was whether the interest for delayed payment of tax is payable on the net tax liability (tax payable after adjusting input tax credit) or the total tax liability.

HC, while deciding the issue, made following observations:

- Until a return is filed, the taxpayer is not entitled for ITC and no entry of credit in the electronic credit ledger takes place. Consequently, the taxpayer cannot discharge the tax liability by utilizing the ITC balance.
- The tax already paid on the inward supplies is available with the taxpayer, but mere availability of the credit does not tantamount to payment of tax.
- The eligible credit should be tapped and brought in the form of a credit entry into the electronic credit ledger for payment of tax.
- Delay in filing of the returns results into delay in payment of tax liability (which may be payable partly in cash and partly by utilizing ITC).
- Only when the tax liability is discharged, the Government gets a right over the money available in the ledger, hence it is entitled to interest up to the date of payment.

Thus, HC held that interest is payable on the total tax liability including the amount paid by way of utilization of ITC.

[1] 2019-VIL-175-TEL

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Background

- The petitioner is engaged in the manufacture of MS Pipes and in the execution of infrastructure projects. It is registered as a dealer under the Central Goods and Services Tax Act, 2017 ('the Act').
- There was a delay on the part of petitioner in filing of the returns in Form GSTR-3B for the period October 2017 to May 2018. The petitioner claimed that the same was on account of shortage of available ITC, required to off-set the entire tax liability.
- The petitioner paid the tax liability party in cash and partly by utilizing ITC.
- The Superintendent of Central Tax issued letters to the petitioner demanding interest at the rate of 18% for delay in payment of tax liability in accordance with Section 50(1) of the Act.
- The petitioner responded to the letter indicating that interest was paid for delay in payment of tax liability, as per section 50(1) of the Act. The interest was computed on the net tax liability of the petitioner i.e. portion of tax liability paid in cash.
- However, the department demanded the interest on the total tax liability of the petitioner.
- Aggrieved by the demand, the petitioner filed writ petition before the HC.

Petitioner's Contentions

- Interest should be computed only on the net tax liability. In other words, interest under section 50(1) of the Act is not payable on the portion of tax liability which is paid by utilizing ITC.
- This contention is based upon presumption that ITC is lying with the Government Treasury in the electronic credit ledger. Thus, interest should not be computed on the same.
- It relied upon the in-principle approval given by the GST Council in its 31st meeting[2] for amending section 50. As per the amendment proposed, interest should be charged only on the net tax liability of the taxpayer, after taking into account the admissible input tax credit, i.e. interest would be leviable only on the amount payable through the electronic cash ledger.
- It also relied on the decisions of the Gujarat High Court in the case of *Dashmesh Hydraulic Machinery* [3] *and Nishi Communication*[4]. The judgements relied upon pertained to the erstwhile VAT regime.

Respondent's Contentions

- Section 50(1) imposes burden in the form of interest upon every person who is liable to pay tax, but has failed to pay the same within the prescribed due dates.
- The scope of interest cannot be confined only to the cash component of the total tax liability. Interest shall be calculated on the total tax liability, including the portion which is liable to be set-off against ITC.
- Since the interest liability is not penal in nature, the petitioner cannot escape from the same.

High Court Ruling

- For determining the issue under consideration, the HC broadly focused on the procedure of filing returns and payment of tax, eligibility and conditions for availing ITC and the wordings of Section 50.
- HC referred to the following statutory provisions of the Act in order to analyze the scheme of availment and utilization of the ITC:
  - Section 16(2) of the Act lays down the conditions subject to which a registered person will be entitled to avail ITC. One of the conditions stipulated under the said section is filing of the return under section 39. Thus, a person shall be entitled to ITC only upon filing of the return.
  - Further, section 41(1) of the Act provides that ITC shall be available provisionally, only upon filing of the return on self-assessment basis. In other words, till a return is filed, no credit shall be available in the electronic credit ledger of the person.
  - Section 49(2) of the Act stipulates that the ITC as self-assessed in the return should be credited to the electronic credit ledger and section 49(4) allows utilization of ITC for payment of output tax liability.
- Referring to section 50(1), HC observed that the liability to pay interest arises automatically, when a registered person, fails to pay tax to the Government within the period prescribed.

  Further, the liability to pay interest is in respect of the period for which the tax remains unpaid.
- Hence, it is relevant to understand when the tax has to be paid and in what manner.
- Section 39(7) read with section 39(1) provides that the tax shall be paid on or before the 20th day of the succeeding calendar month. Further, as per section 49, payment can be either in cash or by utilization of ITC.

[2] Press Release dated 22 December 2018

[3] 2015-VIL-45-GUJ

[4] 2015-VIL-96-GUJ

- HC observed that the scheme of the Act makes a distinction between the following:
  - (i) The entitlement to take credit as per section 16(2) of the Act;
  - (ii) The actual entry of credit in the electronic credit ledger as per Section 49(2) read with section 41(1) of the Act; and
  - (iii) The actual payment of tax liability, by utilizing the credit as per section 49(4) of the Act.

- Thus, until a return is filed, the taxpayer is not entitled for ITC and no actual entry of credit in the electronic credit ledger takes place. Consequently, the taxpayer cannot discharge the tax liability by utilizing the ITC balance.

- HC noted that while the tax paid on the inward supply is available with the taxpayer, the same is available in the air or cloud. Such tax becomes ITC only when a claim is made in the returns filed as self-assessed. Only after such claim is made, the amount can be utilized for payment of tax.

- HC took an example of banking transactions where an amount available in the account of a person, though available with the bank itself, is not taken to be the money available for the benefit of the bank.

  Similarly, the tax already paid on the inward supplies should be tapped and brought in the form of a credit entry into the electronic credit ledger and payment has to be made from the same. If no payment is made, mere availability of the same, there in the cloud, will not tantamount to actual payment.

- Therefore, delay in filing the returns results into delay in payment of tax liability (which may be payable partly in cash and partly by utilizing ITC).

- HC further observed that only when payment is made, the Government gets a right over the money available in the ledger. Since ownership of such money is with the taxpayer till the time of actual payment, the Government becomes entitled to interest up to the date of payment i.e., date of their entitlement to appropriate it.

- With reference to the proposed amendment to section 50 relied upon by the petitioner, HC commented that the recommendations of the GST Council have not been made effective by way of necessary amendments in the GST law. Thus, section 50 cannot be interpreted in the light of the proposed amendment.

- Further, on the court rulings referred by petitioner, the HC remarked that the said rulings pertain to the Gujarat VAT regime which differ substantially from the GST regime. Accordingly, the same cannot be relied upon.

- Thus, HC finally held that interest is payable on the total tax liability including the amount paid by utilizing ITC.

Comments

The HC ruling, although settling the ambiguity prevailing amongst the taxpayers since the enactment of the CGST Act, 2017, appears different from the Government's intent and the industry practice followed since the erstwhile indirect tax regime.

It may be crucial for the Government to carry out the amendment in the interest of taxpayers and issue necessary clarification in the interim.

Taxpayers however may need to be mindful about timely furnishing of returns to avoid interest burden despite input tax credits.

In case where the taxpayer has opening balance of input tax credit which can be utilized against output tax liability, the contention of revenue loss and rulings of Gujarat HC relied upon by the petitioner, needs to be analyzed.

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