

JB NAGAR CPE STUDY CIRCLE MEETING – ITC Blocked Credit

Day & Date : Sunday, 05th May 2024

Subject : ITC- Blocked Credit

Presented by : CA Naresh Sheth





ITC Mechanism - Relevance & Objectives

Relevance of ITC Mechanism

- Input tax credit mechanism (ITC mechanism) is a back-bone of any value-added taxation system such as GST
- Basic objectives of ITC mechanism:
 - Business entities in transaction chain are pass through entities and should not bear indirect tax incidence
 - GST, being a destination-based consumption tax, should be borne by ultimate consumer
 - Final Tax incidence on consumer should be on actual value of goods / services excluding taxes levied on intermediate stages in distribution chain
 - Elimination or minimizing possibilities of levy of tax on tax
- Seamless flow of credit is a prerequisite for any efficient VAT system of taxation.
- Any blockage of the credit defeats basic principle of taxing value addition in the transaction chain

Checklist for claiming ITC

- Whether goods or services procured fall under definition of 'Input', 'Input services' or 'Capital goods' as defined under Section 2(59), (60) and 2(19) of CGST Act respectively?
- Whether tax paid on above fall under definition of 'Input tax' as defined under Section 2(62) of CGST Act?
- Whether all conditions specified u/s 16 of CGST Act are complied with?
- Whether ITC is blocked u/s 17(5) of CGST Act? If blocked, no ITC can be claimed
- Whether ITC in respect of non-business use or exempt supplies? If yes, whether such ITC is reversed u/s 17 r.w. Rule 42 and 43 of CGST Rules?

Blocked Credits -Basics

Blocked Credits - Meaning

- The term 'blocked credits' is not used in GST legislation
- Non-permissible ITC is popularly known as 'blocked credits'
- Section 16 of CGST Act provides for tax credit of inputs (goods and capital goods) and input services used in course or furtherance of business **except certain blocked credits**
- Such blocked credits are specified u/s 17(5) of CGST Act and same are **blanketly disallowed** even though same are used in course or furtherance of business
- Legislative intent of blocking specified credit appears to prevent allowance of tax credit relating to:
 - Personal expenses
 - Non-business expenses
 - Investment in immovable property
 - Tax paid under composition scheme

Section 17(5) – Statutory Provision for Blocked Credit

➤ Section 17(5) of CGST Act reads as under:

*“**Notwithstanding** anything contained in **sub-section (1) of Section 16** and **sub-section (1) of Section 18**, input tax credit **shall not be available** in respect of the following, **namely:**”*

➤ Interpretations of important terms used in above provision:

- **Notwithstanding** - Section 17(5) would override Section 16(1) and Section 18(1)
- **Shall not** - ITC on certain goods or services would not be admissible in any case
- **Namely** - Section 17(5) would be applicable only to the goods or services specifically mentioned therein

➤ Some of the blocked credits u/s 17(5) have been challenged by the taxpayers at various forums

➤ Taxpayers have sought several Advance Rulings on blocked credits u/s 17(5)

➤ This presentation deals with the legal provisions u/s 17(5) and various vexed issues thereon

Provisions prescribing Blocked Credits – Validity ?

- As per **Statement of Object and Reasons of the Constitution** (One Hundred And Twenty-second Amendment) Bill, 2014, the purpose of GST (subsuming all indirect taxes) is to avoid the Cascading of taxes
- Same purpose is also mentioned in the **Statement of Object and Reasons** of CGST Bill, 2017
- Issues highly debated in professional circle:
 - Whether ITC is a constitutional right or statutory right?
 - Whether ITC can be blocked or restricted in GST legislation?
 - Whether Section 17(5) blocking ITC is ultra vires?

Provisions prescribing Blocked Credits – Validity ?

- The Hon'ble Supreme Court in case of ***Dai Ichi Karkaria - 1999 (112) ELT 352 (SC)*** held that ITC is an indefeasible right of the assessee
- ITC, though indefeasible right, is not an unconditional right. It is a concession given by the statute on fulfillment of prescribed conditions as held in following judicial pronouncements:
 - Jayam & Co. – (2016) 15 SCC 125
 - Osram Surya – (2002) 9 SCC 20
 - ALD Automative – (2019) 13 SCC 225
 - Mackinnon Mackenzie & Co. – (2015) 4 SCC 544
 - Godrej & Boyce – (1992) 3 SCC 624

Consequences of Availing Blocked Credits

- Payment of Interest u/s 50 (3) for ITC **wrongly availed and utilized**
- Rule 88B of CGST Rules provide the manner of calculating interest leviable u/s 50 (3) of CGST Act:

Scenario	Amount on which Interest is payable	Interest calculated @ 18% p.a.	
		From	To
Interest on ITC wrongly availed and utilized	ITC wrongly availed and utilized	Date of utilization of ITC	Date of ITC Reversal

- Penalty equivalent to input tax wrongly availed or Rs. 10,000 (whichever is higher) is prescribed u/s 122(2) of CGST Act
- Prosecution can be initiated for wrongful availment of ITC exceeding specified limits as prescribed u/s 132 of CGST Act

Disclosure of Blocked Credits in GSTR-3B

- Table 4(A)(5) of GSTR-3B requires assessee to disclose All other ITC **other than** :
 - IGST paid on import of goods
 - IGST paid on import of services under RCM
 - GST paid on inward supplies under RCM
 - ITC of inward supplies from ISD
- Blocked credits u/s 17(5) should be included and disclosed along with All other ITC in Table 4(A)(5) of GSTR-3B
- Thereafter, such blocked credits should be reversed in Table 4(B)(1) of GSTR-3B
- Many assesses account for blocked ITC as part of expenses and does not disclose the same in their GSTR-3B. This is not legally correct and such non-disclosure may trigger general penalty of Rs. 50,000 (CGST 25,000+ SGST 25,000 or IGST Rs. 50,000) u/s 125 of CGST Act



Blocked ITC
under GST
- Analysis of Section
17(5)

Section 17(5)(a) & (aa) - ITC on Motor Vehicle & Vessels

Particulars	Credit restricted on
Motor vehicles for transportation of persons [Section 17(5)(a)]	Motor vehicles for transportation of persons having approved seating capacity of not more than 13 persons (including driver), except when they are used for making following taxable supplies, namely: <ul style="list-style-type: none"> • Further supply of such motor vehicles; or • Transportation of passengers ; or • Imparting training on driving such motor vehicles
Vessels and aircraft [Section 17(5)(aa)]	Vessels and aircraft except when they are used for making following taxable supplies, namely: <ul style="list-style-type: none"> • Further supply of such vessels or aircraft; or • Transportation of passengers; or • Imparting training on navigating such vessels or flying such aircraft • Transportation of goods

Section 17(5)(ab) - ITC on Motor Vehicle Related Expenses

Particulars	Credit restricted on
General insurance, servicing, repair and maintenance [Section 17(5)(ab)]	Services of general insurance, servicing, repair and maintenance in so far as they relate to motor vehicles, vessels or aircraft referred to in clause (a) or clause (aa) Provided that the input tax credit in respect of such services shall be available: <ul style="list-style-type: none">• where the motor vehicles, vessels or aircraft referred to in clause (a) or clause (aa) are used for the purposes specified therein• where received by a taxable person engaged:<ul style="list-style-type: none">▪ in the manufacture of such motor vehicles, vessels or aircraft; or▪ in the supply of general insurance services in respect of such motor vehicles, vessels or aircraft insured by him

Section 17(5)(a), (aa) & (ab) - Relevant Definitions

➤ **Motor Vehicle:**

- Section 2(76) of CGST Act, 2017 defines the term “motor vehicle” where same meaning as assigned to it in clause (28) of section 2 of the Motor Vehicles Act, 1988 has been referred to
- Section 2(28) of Motor Vehicle Act, 1988 defines the term “motor vehicle” or “vehicle” **to mean any mechanically propelled vehicle adapted for use upon roads** whether the power of propulsion is transmitted thereto from an external or internal source and **includes** a chassis to which a body has not been attached and a trailer; but **does not include:**
 - a vehicle running upon fixed rails ;or
 - a vehicle of a special type adapted for use only in a factory or in any other enclosed premises; or
 - a vehicle having less than 4 wheels fitted with engine capacity of not exceeding 25 cubic centimetres

Section 17(5)(a), (aa) & (ab) - Issues & FAQs

- Whether ITC is available in respect of forklift or material cart used within the factory premises?
- Whether ITC is available in respect of golf carts purchased by Clubs, hotels, resorts, etc.?
- Whether ITC will be available in respect of a tempo traveler (originally having capacity of 15 persons) now modified to have 6 spacious seats?
- Whether ITC is available in respect of motor vehicles purchased for transportation of goods?
- Whether ITC is available in respect of insurance, repairs and maintenance for above vehicle ?
- Whether ITC in respect of cash van used by Bank is allowable?

Section 17(5)(a), (aa) & (ab) - Issues & FAQs

- Whether ITC is available, if a company purchases a motor vehicle having approved seating capacity of 5 persons for giving it on lease / rent?
- Whether disposal as scrap can be regarded as "further supply of such motor vehicles"?
- Whether ITC is available in respect of car used as demo car?
- Whether ITC is available in respect of bus purchased for pick up and drop of employees or workers?
- Whether ITC is available in respect of hire charges paid for contract buses deployed for pick up and drop facilities of employees and workers?
- Whether ITC is available in respect of vanity vans used by actors during shooting?
- Whether ITC can be claimed in respect of ambulance purchased by a Manufacturing unit for its workers or employees and their families?

Section 17(5)(b) – ITC Blocked on Specified Goods / Services

- Food and beverages,
- Outdoor catering
- Beauty treatment,
- Health services
- Cosmetic and plastic surgery
- Life insurance and Health insurance
- leasing, renting or hiring of motor vehicles, vessels or aircraft referred to in clause (a) or clause (aa) except when used for specified purposes
- Membership of a club, Health and fitness center
- Travel benefits extended to employees on vacation such as leave or home travel concession

Except where said category of inward supply of goods or services or both are used for making an outward taxable supply of same category of goods or services or both or as a part of taxable composite or mixed supply

ITC will be available for above goods/services, if obligatory for employer to provide its employees under any law

Relevant Circulars

Clarification vide Circular No. 172/04/2022 – GST dt. 06.07.2022:

- The second proviso to Section 17(5)(b) provides that input tax credit in respect of goods or services shall be available which are obligatory for an employer to provide to its employees, under any law for the time being in force
- It is clarified that the above proviso after section 17(5)(b)(iii) is applicable to the whole of section 17(5)(b) and not only to clause (iii) of section 17(5)(b)

Section 17(5)(b) – Issues & FAQs

- What is the meaning of the phrase “**obligatory for employer to provide its employees under any law**” used in Section 17(5)(b)? Whether it covers facility given to employees under terms of contract?
- Whether ITC can be claimed in respect of expenses incurred for running a canteen for employees?
- Whether ITC is available on the reimbursement of lunch, dinner or snacks expenses (restaurant services) to employees especially marketing team or field staff?
- A professional association is organizing a conference wherein conference fee includes provision of breakfast, tea and lunch. Whether professional association is entitled to amount paid to hotel for food and beverages provided during the conference?

Section 17(5)(b) – Issues & FAQs

- Whether ITC is eligible where medical expenses (room charges exceeding Rs. 5000) are borne by the employer?
- If a film producer procures services of Dietician for monitoring diet of his actor & actress, whether he can claim ITC on such expenditure? Whether services of Dietician fall under “health services” as mentioned u/s 17(5)?
- Whether ITC is available to film producers, airlines, etc. in respect of makeup services?
- Whether ITC is available in respect of accidental insurance for their staff personnel?

Section 17(5)(c) & (d) – ITC on Construction

Particulars	Credit restricted on
Works contract services [Section 17(5)(c)]	When supplied for construction of immovable property (other than plant and machinery) except where it is an input service for further supply of works contract service
Goods or services or both [Section 17(5)(d)]	When it is received by a taxable person for construction of an immovable property (other than plant and machinery) on his own account including when used in course or furtherance of business

Section 17(5)(c) & (d) – Relevant Definitions

➤ **Works contract services:**

- Section 2(119) of CGST Act, 2017 defines the term “works contract” **to mean** a contract for
 - building, construction, fabrication, completion, erection, installation, fitting out, improvement, modification, repair, maintenance, renovation, alteration or commissioning
 - of any immovable property
 - wherein transfer of property in goods (whether as goods or in some other form) is involved in the execution of such contract

Section 17(5)(c) & (d) – Relevant Definitions

- **Construction** includes [explanation to Section 17(5)(d)]:

Re-Construction	Renovation	Additions	Alterations	Repairs
to the extent of capitalization to the said immovable property				

- **Plant and Machinery** means [explanation inserted after Section 17(6)]:

Apparatus	Equipment	Machinery
fixed to earth by foundation or structural support that are used for making outward supply and includes such foundation and structural supports but excludes :		
<ul style="list-style-type: none">• Land, building or any other civil structures• Telecommunication towers; and• Pipelines laid outside the factory premises		

Section 17(5)(c) & (d) – Issues & FAQs

- Definition of the term “construction” is based on accounting treatment given by the taxpayer. What would be the consequences if accounting treatment is not in consonance with Accounting Standards:
 - Capital expenditure written off as Revenue expenditure
 - Revenue expenditure capitalized to immovable property
- What would be ITC implications where following items are debited to “Plant & Machinery Account” and not to “Building Account”:
 - Lifts
 - Escalators
 - Fire fighting systems
 - Centralized Air conditioning system

Section 17(5)(c) & (d) – Issues & FAQs

- Whether ITC can be claimed in respect of internal roads of a commercial complex?
- Whether ITC can be claimed in respect of landscaping and garden making?
- Whether ITC is available in respect of goods or services procured for construction of special purpose buildings:
 - Cold storage
 - Theatre
 - Hotel
 - Telecommunication towers

Section 17(5)(c) & (d) – Issues & FAQs

- Whether one can claim ITC on goods or services procured for construction of Shopping Mall where:
 - Shops are to be given on rent
 - Shops are to be sold before receipt of completion certificate
 - Some shops are to be sold and balance are to be given on rent
- Section 17(5)(c) and 17(5)(d) restrict ITC where goods or services procured are to be used for construction of immovable property. What does the term “Immovable property” mean? Whether following will be movable or immovable:
 - Telecommunication towers
 - Glass and furniture partitions (used in offices, Co-Workspaces, etc.)

Section 17(5)(e), (f), (fa),(g), (h) - Others

Particulars	Credit restricted on
Goods or services or both [Section 17(5)(e), (f), (fa), (g), (h)]	<ul style="list-style-type: none">➤ Goods or services on which tax is paid u/s 10 [Composition levy]➤ Goods or services received by a non-resident taxable person except on goods imported by him➤ Goods or Services or both received by a taxable person, which are used or intended to be used for activities relating to his obligations under corporate social responsibility referred to in section 135 of the Companies Act, 2013 (w.e.f. 01st Oct 2023)➤ Goods or services used for personal consumption➤ Goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples

Section 17(5)(i) - Others

Particulars	Credit restricted on
Goods or services or both [Section 17(5)(i)]	<p>➤ Any tax paid in terms of the following:</p> <ul style="list-style-type: none">• Tax not paid or short paid or erroneously refunded or input tax credit wrongly availed or utilized by reason of fraud or any wilful – misstatement or suppression of facts [Section 74]• Detention or seizure and release of goods and conveyances in transit [Section 129]• Confiscation of goods or conveyance and levy of penalty [Section 130]

Relevant Circular and FAQ

Gist of Circular No. 92/11/2019 dated 07.03.2019:

- No ITC in respect of Inputs, input services and capital goods distributed as gifts or free samples
- In case of scheme of “Buy one get one free”:
 - It is a case of supply of two or more individual supplies for a single price
 - It is not a case of an individual supply of free goods
 - It should be taxed either as composite supply or mixed supply
 - ITC is **not blocked** under Section 17(5)(h)

Sectoral FAQ:

- No ITC reversal is required in respect of parts replaced under warranty since value of warranty services includes the charges to be incurred for parts replacement during the warranty period

Section 17(5)(e), (f), (fa), (g), (h) & (i) - Issues & FAQs

- Whether the taxpayer is eligible for ITC on CSR expenses before the effective date of the amendment?
- Whether the taxpayer who voluntarily reversed ITC or not availed ITC on CSR activities, either due to ambiguity or caution can re-avail or avail the ITC once the amendment is in effect?
- Section 17(5)(g) provides that ITC will not be available where goods or services are used for personal consumption. What does the term “personal consumption” mean?
- Whether there can be any “personal expenses” in case of incorporated entities (Artificial juristic person)?
- If a company takes residential flat on rent for director, whether ITC is blocked as personal consumption?
- Whether reversal of ITC u/s 17(5)(h) applies where finished goods are lost, stolen, destroyed, written off?

Section 17(5)(e), (f), (fa), (g), (h) & (i) - Issues & FAQs

- Whether ITC will be available, or Section 17(5)(h) will apply in following cases:
 - Natural loss of goods while manufacturing process
 - Abnormal loss of goods while manufacturing process
 - Abnormal loss of goods due to natural calamity
 - Loss of goods while testing process
 - Goods become obsolete or expired

Section 17(5)(e),(f), (fa), (g), (h) & (i) - Issues & FAQs

- Under section 17(5)(h):
 - Whether a registered person is required to reverse ITC attributable to goods lost in transit?
 - What does the term “destroy” mean? Whether it refers to complete destruction or damaged goods will also be covered under said sub-section?
 - What does the term “written off” mean? Whether written off should be full or a partial written off is also covered under said sub-section? What if goods are not actually written off rather provision is made for reduction in value of goods?
 - Treatment of ITC in respect of goods given to dealers or distributors pursuant to sales promotion schemes?
 - If a company distributes its goods free of cost to its customers / dealers as a part of sales promotion, whether ITC on procurement / production of such goods can be claimed?



THANK YOU

naresh.sheth@jtco.co.in