TRILEGAL

UPDATES

Supreme Court makes ITC availment more onerous for taxpayers

17 April 2023

***Partner**: Samsuddha Majumder, **Senior Associate**: Kartikey Kulshrestha, **Associate**: Shreetama Ghosh.*

The Supreme Court, in *State of Karnataka v Ecom Gill Coffee Trading Pvt. Ltd.* (**Ecom Gill**), has held that the burden to prove the admissibility of any input tax credit (**ITC**) would lie on the taxpayer who is claiming such ITC. It held that tax invoices and payment details alone would not be sufficient proof and provided a list of documents/records that would need to be furnished in such cases.

This decision, while in the context of Section 70 of the erstwhile Karnataka Value Added Tax (**KVAT**) Act, 2003, is likely to have a significant impact on the ITC being availed by the taxpayers under the Goods and Services Tax (**GST**) regime, owing to its similarity to Section 155 of the Central Goods and Services Tax Act, 2017 (**CGST Act**).

The Supreme Court, in a recent judgement, held that the burden to prove the admissibility of credit would lie on the taxpayer claiming the ITC. This is likely to increase the compliance burden on the taxpayers and provide more grounds to the tax authorities to challenge the credit availed by the taxpayers.

Background

The decision in *Ecom Gill* arose from a situation where the taxpayers had purchased goods from various sellers, and had availed ITC on such purchases. Subsequently, these sellers either deregistered from the KVAT Act, filed a NIL return, or did not pay the VAT applicable to these purchases to the Government.

Consequently, the admissibility of ITC availed by the taxpayers who had purchased goods from such sellers was brought into question. While the taxpayers produced tax invoices and proof of payment for the purchases in support of their claims, the adjudicating authority and the first appellate authority denied ITC on the ground that the burden of proof under Section 70 had not been discharged. However, the second appellate authority and the Karnataka High Court upheld the taxpayer's claims and allowed the ITC. This decision of the High Court was challenged before the Supreme Court by the tax authorities.

The Supreme Court, while reversing the decision of the High Court, held that the burden to prove the admissibility of ITC lies on the taxpayers, and cannot be shifted to the tax authorities. Merely producing tax invoices and payment proofs is not sufficient to discharge this burden; satisfying such burden would require the production of additional records like: (i) names and addresses of the sellers, (ii) details of the vehicles which were used to deliver the goods to the taxpayers, (iii) proof of payment of freight charges, and (iv) acknowledgements of taking delivery of goods.

Observations

The *Ecom Gill* judgement casts a stringent requirement on the taxpayers, increasing their compliance burden, while also providing further avenues to tax authorities to be able to dispute the ITC on procedural grounds. Section 70 of the KVAT Act (and also, Section 155 of the CGST Act) provides that the burden to establish eligibility to avail any ITC lies on the taxpayer. The *Ecom Gill* judgement goes beyond this statutory mandate to prescribe a list of records that the taxpayer is required to maintain to establish such eligibility. This higher compliance is onerous for the taxpayers and inconsistent with the spirit of value added tax regimes such as GST, effectively diluting the value added or pass through nature of such tax systems.

For taxpayers, the higher level of compliance would mean a higher level of scrutiny and burden of proof for claiming ITC. Considering the analogous nature of Section 155 of the CGST Act with Section 70 of the KVAT Act, it is likely that the tax authorities would apply the principles laid down in the *Ecom Gill* judgement to test the validity of ITC availed under the GST laws as well. This is likely to result in a higher risk of denial of ITC to taxpayers in the GST regime.

To mitigate this risk, it would be crucial for taxpayers to review their vendor management practices and create robust documentation, in case they are faced with similar circumstances while availing ITC. They should ensure that they have sufficient safeguards in their existing contracts to requisition the necessary information from their vendors, if required. Further, given the significant look-back period under the GST laws, it would also be important for taxpayers to reconnect with their vendors and complete the additional documentation for the past periods, wherever required.

Importantly, this judgement does not comment on the admissibility of ITC in case of the seller's failure to deposit the tax with the government. Thus, this issue remains open.

If you require any further information about the material contained in this newsletter, please get in touch with your Trilegal relationship partner or send an email to alerts@trilegal.com. The contents of this newsletter are intended for informational purposes only and are not in the nature of a legal opinion. Readers are encouraged to seek legal counsel prior to acting upon any of the information provided herein.