

Karnataka HC quashes amendment to Rule 89(4)(c) as being *ultra vires* to the GST Law and the Constitution of India

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Summary

Amendment to Rule 89(4)(C) of the Central Goods and Services Tax Rules (CGST Rules), 2017 restricting the amount of export turnover towards the calculation of refund amount has been held as *ultra vires* to the GST Law and the Constitution of India. The Karnataka High Court (HC) further held that the rule fails to prescribe the refund computation in cases where no similar goods are supplied in the domestic market and the value of like goods provided by other suppliers is unavailable.

Facts of the case

- M/s Tonbo Imaging India Pvt Ltd (petitioner) is engaged in developing innovative designs in micro-optics, lower-power electronics and real-time vision processing systems in a customised manner for its customers.
- The petitioner had filed refund claims of unutilised input tax credit (ITC) on account of exports made under the Letter of Undertaking (LUT) during the period May 2018 to March 2019 under Section 54(3)(i) of the CGST Act read with Rule 89 of the CGST Rules.
- In view of the amendment made in Rule 89(4)(c) vide Notification No.16/2020-CT effective from 23 March 2020, the authorities issued three show cause notices (SCNs) on the grounds that the petitioner has not submitted the proofs to substantiate that the value of export turnover mentioned in the instant claim is 1.5 times of 'like goods' as required to be computed under Rule 89(4)(c) of CGST Rules.
- In response to the SCNs, the petitioner contended that the amended rule (*supra*) would not be applicable in the instant case as the period for which the refund was claimed (i.e., May 2018 to March 2019) is much prior to the amendment of Rule 89(4)(c). Further, the petitioner submitted that they are engaged in the export of customised goods and hence furnishing the proof of like or similar goods supplied domestically in India is not possible.
- The authorities rejected the submission of the petitioner and issued an order disallowing the refund claims.
- Aggrieved by the order of authorities, the petitioner filed a writ petition before the HC.

Karnataka HC observations and ruling [Writ Petition No. 13185 of 2020 (T-RES) dated 23 March 2023]

- **Amended rule is violative of Article 14 and Article 19(4) of the Constitution of India:** The HC noted that Rule 89(4)(c) only restricts the refund quantum where the exports are made under LUT as opposed to refund claimed where goods are exported after the payment of tax. Therefore, the said rule seeks to create discrimination between two classes of exporters and therefore is violative of Article 14 and Article 19(1)(g) of the Constitution.
- **Rule 89(4)(C) defeats the purpose of Section 16 of the Integrated Goods and Services Tax (IGST) Act and Section 54 of the CGST Act:** The HC opined that Section 16 of the IGST Act aims to make the exports tax-free by 'zero-rating' them. However, Rule 89(4)(c) attempts to restrict the same by including domestic turnover in the definition of zero-rated supplies for the computation of refund claim, which should only cover export turnover.
- **Prejudicial to exporters:** The HC observed that placing unreasonable restrictions on refund claims would ultimately discourage the exporters who account for the export incentives while quoting prices to foreign customers. The HC further emphasised that taking away or restricting the benefit of unutilised ITC would also adversely affect the availability of the rotation of funds, which is essential for the business to thrive.

- **Amended Rule 89(4)(c) is unreasonable and arbitrary:** The HC has stated that Rule 89(4)(c) prescribes undertaking the value of 'like goods' domestically supplied by the exporter or similar supplier. In this regard, the HC opined that the use of terminology such as 'like' or 'similar' indicates vagueness in the aforesaid rule. Further, referring to the facts of the instant case, the HC also noted that the rule fails to prescribe the refund computation in cases where no similar goods are supplied in the domestic market and the value of like goods provided by other suppliers is not available.
- **Rule 89(4)(C) is *ultra vires* of Section 16 and Section 54 of the CGST Act:** The HC has held that Rule 89(4)(c) attempts to take away the right of the exporter to obtain a refund, which is entrusted vide Section 16 of the IGST Act and Section 54 of the CGST Act. Thus, the said rule is *ultra vires* to the said sections and liable to be quashed. In view of the same, the HC has allowed the refund claims of the petitioner.

Our comments

The amendment restricted the turnover of zero-rated supply of goods to 1.5 times the value of like goods domestically supplied by the same or similarly placed supplier to compute the refund of ITC. This affected the exporters' working capital, especially where the exporters already had accumulated credit.

Thus, this is a significant and welcome judgement by the Karnataka High Court. As a result, the taxpayers whose refund claims were rejected or who claimed lower refunds may evaluate the possibility of claiming the differential refund.

In this regard, it is pertinent to note that on a similar issue earlier, the Apex Court, in the case of VKC Footsteps Pvt. Ltd, had held that while recognising an entitlement to a refund, it is open to the legislature to define the circumstances in which a refund can be claimed.

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