

## **Hon'ble Supreme Court of India upholds the constitutional validity of Section 17(5)(c) and (d) of Central Goods and Services Tax Act, 2017**

The Hon'ble Supreme Court of India ("Supreme Court") in an important judgement in the matter of *Chief Commissioner of CGST and Ors. vs. Safari Retreats Private Ltd. and Ors*<sup>1</sup> has ruled on the eligibility of the taxpayers to avail Input Tax Credit ("ITC") of Goods and Services Tax ("GST") paid on procurement of works contract services and other goods and services received for construction of immovable property, with reference to specific restrictions contained in Sections 17(5)(c) and 17(5)(d) of the Central Goods and Services Tax Act, 2017 ("CGST Act") in this regard.

### **Brief facts**

The issue stems from the interpretation of Sections 17(5)(c) and 17(5)(d) of the CGST Act, which restricts availment of ITC on: (a) works contracts services; and (b) goods and/or services, availed for construction of immovable property, as below:

1. **Section 17(5)(c) of the CGST Act:** Works contract services when supplied for construction of an immovable property (other than plant and machinery) except where it is an input service for further supply of works contract service.
2. **Section 17(5)(d) of the CGST Act:** Goods or services or both received by a taxable person for construction of an immovable property (other than plant or machinery) on his own account including when such goods or services or both are used in the course or furtherance of business.

Therefore, the statutory provisions outlined above draw a difference in the exceptions, as Section 17(5)(c) of the CGST Act uses the term 'plant and machinery' whereas Section 17(5)(d) of the CGST Act uses the term 'plant or machinery'. The explanation clause of Section 17 of the CGST Act defines the term 'plant and machinery' used in Section 17(5)(c) of the CGST Act but does not define the term 'plant or machinery' used in Section 17(5)(d) of the CGST Act.

Additionally, Section 17(5)(d) of the CGST Act restricts availment of ITC of GST paid on procurement of goods and services received for construction of immovable property for own account, which is not provided under Section 17(5)(c) of the CGST Act.

The dispute arose when the ITC of GST paid on inputs (goods) and/or services was denied to Safari Retreats Private Limited ("**Respondent**"), for construction of immovable property, even if goods and/or services were covered under

<sup>1</sup> Civil Appeal No. 2948 of 2023

the exceptions outlined above. Aggrieved by the denial, the Respondent filed a writ petition before the Hon'ble High Court of Orissa<sup>2</sup> ("**Orissa HC**").

The Orissa HC held that ITC of GST paid on procurement of goods and/or services used in construction cannot be denied under Section 17(5)(d) of the CGST Act if the immovable property is not used for own purposes and is used for fresh stream of GST revenue in the form of rental income. The Orissa HC further held that a narrow interpretation of Section 17(5)(d) of the CGST Act will frustrate the very intention of the CGST Act which is to avoid the cascading effect of multistage taxation.

By reading down the provision of Section 17(5)(d) of the CGST Act, the Orissa HC allowed claim of ITC accumulated on construction of an immoveable property provided that said immoveable property was used in the course or furtherance of business. Aggrieved by the decision of the Orissa HC, the revenue authorities challenged the same by way of an appeal before the Supreme Court.

### Key contentions of the taxpayers/assesseees

Before the Supreme Court, the taxpayers/assesseees contended the following:

1. Section 17(5)(d) of the CGST Act is violative of Article 14 of the Constitution of India as it classifies taxpayers/assesseees engaged in the business of constructing immovable properties and then renting/leasing/letting out etc. premises within the said immovable properties on the same footing as taxpayers engaged in the business of constructing immovable properties and then selling the immovable properties or premises within the said immovable properties;
2. parties involved in provision of leasing/renting services are subject to output GST. Thus, denying ITC in such scenarios disrupts the credit flow, thereby defying the entire intent of GST law. Additionally, taxpayers providing leasing/renting services cannot be equated with taxpayers that are engaged in the sale of immovable property;
3. the terms 'plant or machinery' appearing in Section 17(5)(d) of the CGST Act and the term 'plant and machinery' appearing in Section 17(5)(c) of the CGST Act indicate deliberate different legislative treatment, which should be read strictly; and
4. vagueness in Section 17(5)(d) of the CGST Act, on account of non-defined terms such as 'on its own account' leads to arbitrary interpretations thereof, thereby rendering it to be unconstitutional.

### Key contentions of the revenue department

The contentions of the Revenue Department are summarised below:

1. Section 17(5)(d) is constitutionally valid as the principle of equality permits the legislature to create different categories for tax legislations;
2. the term 'or' appearing in phrase 'plant or machinery' used in Section 17(5)(d) of the CGST Act should be interpreted as 'and'. The use of the word 'or' thereunder is a mistake of the legislature; and
3. ITC is not a fundamental right, but a statutory right. Accordingly, denial of ITC on construction-related activities is reasonable and in line with the statutory scheme of Section 17(5)(d) of the CGST Act.

### Issues

Based on the arguments advanced by both the parties, the Supreme Court formulated 3 (three) broad issues for consideration, namely:

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<sup>2</sup> Safari Retreats Private Limited vs. Chief Commissioner of Central Goods and Services Tax, Orissa (2019 (5) TMI 1278).

1. whether the definition of 'plant and machinery' as appended to explanation clause to Section 17 of the CGST Act applies to the expression 'plant or machinery' appearing in Section 17(5)(d)?
2. if the definition of 'plant and machinery' does not apply to the term 'plant or machinery' what is the meaning of the term 'plant'? and
3. whether clauses (c) and (d) of Section 17(5) are constitutionally valid?

## Analysis and findings

Based on the arguments advanced by the parties, the Supreme Court analysed clauses (c) and (d) of Section 17(5) of the CGST Act as follows:

1. Section 17(5)(c) of the CGST Act restricts the benefit of ITC in cases of works contract services when supplied for the construction of an immoveable property, unless the goods or services are used in the construction of an immoveable property in the nature of 'plant and machinery' as defined in Section 17(5) of the CGST Act, or where the works contract service supplied for the construction of an immoveable property is for further supply of the works contract;
2. Section 17(5)(d) restricts the benefit of ITC in cases where goods or services are used to construct an immoveable property, on its own account, unless such goods or services are used in the construction of an immoveable property in the nature of 'plant or machinery' or where such goods or services are used for constructing an immoveable property to be used not on its own account;
3. while explanation clause to Section 17 of the CGST Act defines the term 'plant and machinery', the same cannot be equated with the expression 'plant or machinery' appearing in Section 17(5)(d). Accordingly, plain interpretation should be accorded to Section 17(5)(d) of the CGST Act;
4. the use of the term 'plant or machinery' is used only in Section 17(5)(d), as opposed to use of term 'plant and machinery' in Section 17(5)(c), indicates the intent of the legislature to use different terms. Accordingly, 'plant and machinery' and 'plant or machinery' cannot be read to entail a same meaning. Since 'plant' isn't defined in the CGST Act, it should be understood in its common commercial meaning;
5. the term 'plant' used in Section 17(5)(d) cannot be given a restrictive meaning as per the definition (in the explanation) appended to Section 17(5). Accordingly, to understand the term 'plant' functionality test is to be applied to determine whether an immoveable property can be considered a 'plant'. This determination of whether an immoveable property qualifies as 'plant' is of a factual nature and is required to be tested on merits on a case-by-case basis;
6. the term construction for 'own account' (an exception to Section 17(5)(d) of the CGST Act) will mean:
  - a) when made for personal use and not for service; or
  - b) it is to be used by the person constructing as a setting, in which the business is carried out.

It is clarified that construction cannot be said to be on a taxable person's own account, if the same is intended to be sold or given on lease or licence.

Based on the aforementioned reasonings, the Supreme Court observed that if the construction of a building is essential for carrying out the activity of supplying output services, such as renting or giving on lease or other transactions in respect of the building or a part thereof, the building can be held to be a plant and ITC of GST paid on procurement of goods and/or services thereof can be availed, subject to satisfaction of conditions prescribed under the CGST Act. However, in the facts of the case, given that the Orissa HC had not evaluated if the mall (immoveable property under the original dispute) constructed by the Respondent qualifies as a 'plant', the Supreme Court has remanded the matter to the Orissa HC.

In terms of the challenge to constitutional validity of clauses (c) and (d) of Section 17(5), the Supreme Court upheld the validity thereof and observed the following:

1. immoveable property and immoveable goods constitute a class by themselves. Clauses (c) and (d) of Section 17(5) apply to the said class only; and
2. in terms of clauses (c) and (d) of Section 17(5), unequals are not treated equally therefore not being discriminatory in nature.

## Conclusion

While the Supreme Court has ruled to apply the functionality test to determine whether an immoveable property qualifies as 'plant' and consequently ITC to be available on the same, the same will have to be tested on a case-to-case basis.

Further, even though the Supreme Court has held that a taxpayer can avail ITC of GST paid on procurement of goods and/or services for construction of immovable property, if it qualifies as a 'plant', it is likely that the revenue authorities will dispute such determination of the taxpayers and a dispute as to what ultimately constitutes a 'plant' is likely to come up.

For the past periods, taxpayers will have to evaluate their position whether to take benefit of this decision and avail ITC, as per the statutory timeframe provided under Section 16(4) of the CGST Act. It is apposite to mention that such claim of ITC will be subject to all conditions and restrictions of availment as prescribed under the CGST Act.

Additionally, a view may be adopted by the taxpayers that the ambiguity in Section 17(5)(d) of the CGST Act has been clarified by the Supreme Court and any consequent limitation is to be computed from the date of the order of the Supreme Court. However, the present argument will have to be tested in a court of law.

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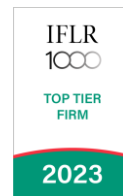


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