Rule 86B: A Barrier to Free Flow of Input Credit Tax in GST

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Abstract— **It is paper presented not only to gain knowledge of Rule 86B of CGST but to have an understanding of its impact on free flow on input credit on Goods & Service Tax Act. This rule will not only affect the organization financially but also enhance the compliance requirement of the organization. It is important to understand the Rule that ought to have increase cash liability and compliances. This will not only help to comply with Rule 86B but also helps in avoiding consequences for non-compliant to Rule 86B on your organization. The implementation of Rule 86B is a strategic plan to curb fake invoicing by requiring taxpayers to pay tax in cash.**

Key Words: Goods and Service Tax Act, Input Tax Credit, Financial Impact, Cash Liability, Electronic Cash Ledger, Electronic Credit Ledger, Output Tax Liability.

Rule 86B of CGST Rules:

Yes, it is the latest limitation in taking the ITC in GST now. It is introduced via CGST fourteenth amendment rules 2020. Rule 86A is already there to restrict the ITC. Now, this new rule goes to further increase the restriction on the use of GST Input Credit. The rule to curtail ITC is introduced in chapter IX of payment of Tax of CGST Rules. Rule 86B of CGST rules goes to cause tons of money crunches within the businesses.

Reason for Implementation of Rule 86B:

It is stated that the Government assumes that fake companies might not have paid income tax of more than ₹ 1 Lakh in the last 2 financial years, therefore, this rule shall not apply to those registered persons who have paid income tax more than ₹ 1 Lakh in last 2 financial years. However, it is also important to note that an income tax of ₹ 1 Lakh would not be a big deal if a fake company is dealing in crores.

Applicability:

Rule 86B of CGST is not applicable to every taxpayer. Rule 86B is applicable only on the taxpayers having a turnover of ₹ 50 lakhs in that month. Rule 86B is not applicable to every taxpayer every month. Only if the turnover other than exempted goods and zero-rated goods turnover is more than ₹ 50 lakhs in a month, then Rule 86B is applicable in that month only.

- **Example-1:** M/s Innobiz has a turnover of ₹ 3 Crores in a previous financial year. They are filing their GST return in the month of January 2021. They have entered the following amount in return-Export Turnover (Zero-Rated Goods) - ₹ 150 lakhs, Exempted Turnover – ₹ 75 lakhs, and Taxable Turnover - ₹ 35 lakhs. Rule 86B is **Not Applicable** in this case. As the taxable turnover in a month is less than ₹ 50 lakhs.

- **Example-2:** M/s SVK has a turnover of ₹ 2 Crores in a previous financial year. They are filing their GST return in the month of January 2021. They have entered the following amount in return-Export Turnover (Zero-Rated Goods) - ₹ 50 lakhs, Exempted Turnover – ₹ 35 lakhs, and Taxable Turnover - ₹ 65 lakhs. In this case, Rule 86B is **Applicable**. As the taxable turnover in a month is more than ₹ 50 lakhs.

Impact of Rule 86B on Goods and Service Tax Act:

ITC means claiming the credit of the GST paid on the purchase of goods and provisions of Services that are used for the furtherance of business. The Mechanism of ITC is the backbone of GST and is one of the most important reasons and features for the implementation of GST. As GST is a single tax levy for the sale of goods and provisions of service across India (covering manufacturer of goods, traders of goods, and service provider till it reaches the ultimate users), without breaking the chain and every participant is able to take benefit of the input and there is a free flow of credit.

Under the previous indirect tax regime of levy of Service Tax, Value Added Tax, and Excise Duty – a lot of input tax credit was not properly utilized. Earlier there were various types of indirect taxes and the input tax credit of one tax could not be adjusted against the input tax credit of another tax.

- **Example:** Retailers who used to pay Service Tax on Rent for their Shops were not able to claim Input Tax Credit of Service Tax with the VAT which they used to charge on the sale of goods to their customers.

However, such issues were removed with the introduction of GST as there is only a single indirect tax that would be levied and there would free flow of input credit.

Notwithstanding anything contained in these rules, the registered person shall not use the amount available in electronic credit ledger to discharge his liability towards

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output tax in excess of ninety-nine percent of such tax liability, in cases where the value of taxable supply other than exempt supply i.e. nil rated goods and zero-rated supply i.e. exported goods, in a month exceeds fifty lakh rupees. This will increase the financial impact on businesses as the businesses will have to pay tax without availing their full input tax credit which was available to them.

Impact of Rule 86B on Business:

Different industries have different business scenarios. Many times businessman purchases additional stock to get the additional purchase discount then sell it slowly. In some cases the business is seasonal. In that case, the Input Tax Credit will be carry forwarded for a longer period and the businessman needs to make the payment in cash despite having sufficient input tax credit. This will result in the blockage of working capital for the businesses and the businesses will be financially impacted by having to pay tax in cash.

- **Example:** Supposes dealer purchases goods having input tax worth ₹ 95 Lakhs and he sold the goods having output tax worth ₹ 75 Lakhs in a month. Earlier the dealer does not need to pay anything as tax liability because he will adjust his ₹ 75 Lakhs output liability against ₹ 95 Lakhs input tax credit. He will still be able to use ₹ 20 Lakhs input credit in next month as well. But with the implementation of Rule 86B the dealer will only be able to set off ₹ 74.25 Lakhs (99%) of total output liability against input tax credit available in electronic credit ledger and the dealer will have to pay ₹ 0.75 Lakhs from electronic cash ledger.

Remarks:

One percent of the liabilities will always remain unveiled. The refund of tax for which will also not be granted.

Conclusion:

Goods and Service Tax Act was introduced to enable the businessman to claim input of different indirect taxes paid by him. This will help the business to reduce their cost related to taxation. As input of Excise duty paid, Service tax paid, Central Sales Tax paid and Value Added Tax Paid are eligible to set off the output liability. But with introduction of Goods and Service Tax Act there is a single tax and all the input tax are eligible for setting off output liability of Businessman. This will help in reducing Tax burden and working capital requirement. But Rule 86B puts a restriction in availing the input credit freely and increases the tax burden on business. It will also increases the compliance requirement as failure to comply with Rule 86B will result in GST registration being cancelled or suspended under CGST Rules, 2017 21A. Rule 86B of CGST will thus be a barrier in free flow of Input Tax Credit. We need to take care and keep some extra cash for tax payment. Expect some relaxation and abatement in the rule. But the government is resolute in making it strict.

Objective of Paper:

1. To understand the importance of Rule 86B of CGST.
2. To know the financial impact of Rule 86B of CGST on Business.
3. To gain knowledge and how to comply with Rule 86B of CGST.
4. To make research more realistic with present scenario.

Research Methodology:

The method used in research is using of secondary data. The method used is views presented by Various Tax Consultants, Tax Professional and Researchers in the field of Goods and Service Tax Act. Besides this, following Secondary Data would also be used to cover existing documents and data that were originally collected for other purposes by various agencies like government department, websites, journals, magazines and existing reports on goods and service tax Sector.

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