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INPUT TAX CREDIT (ITC) AND BLOCKED CREDITS UNDER GST: EXPLAINED SIMPLY

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Imagine you are running a small business. Every time you buy raw materials or services, you pay GST to your supplier. When you sell your product, you collect GST from your customer. Without any relief, you would end up paying tax on tax — which is unfair and increases the final price for everyone.

The **Input Tax Credit (ITC)** mechanism solves this problem. It lets you subtract the GST you paid on your purchases (inputs) from the GST you collect on your sales (outputs). You pay tax to the government only on the value you actually added. This is the heart of the Goods and Services Tax (GST) system in India.

The rules for ITC are given in **Chapter V of the CGST Act, 2017** (Sections 16 to 18). Section 16 tells you when you can take credit, Section 17 explains when you have to share or cannot take credit, and Section 18 gives some special relaxations. Since GST started in 2017, these rules have been improved many times through changes in law, GST Council decisions, and court judgments. In 2026, everything is more digital — the GST portal automatically helps match invoices and track credits.

When Can You Claim ITC? (Section 16 – The Basic Rules)

You can claim ITC only if you meet **four important conditions**:

1. You must have a proper **tax invoice** or debit note from a registered supplier.

2. You must have actually **received** the goods or services (there is a special rule for "bill-to-ship-to" where goods are sent directly to someone else on your instruction).

3. The supplier must have **paid** the GST to the government (the system now checks this automatically).

4. You must have filed your GST return (usually GSTR-3B).

There are a few extra practical rules:

• If goods come in parts (installments), you can claim ITC only after the last part arrives.

• If you do not pay your supplier (including GST) within 180 days, you have to reverse the ITC and pay interest. You can take it back later when you make the payment.

• You cannot claim ITC on the tax part if you have already claimed depreciation on it under Income Tax law.

You must claim the ITC within a time limit — usually by the September return of the next financial year or when you file your annual return (GSTR-9), whichever is earlier. Courts have said that ITC is a real right of the taxpayer, but you still have to follow all conditions properly. Just having an invoice is not enough.

Only **registered** businesses can claim ITC. If you are under the composition scheme (a simple tax scheme for small businesses), you generally cannot take ITC.

Apportionment and Blocked Credits (Section 17 – When You Cannot Take Full Credit)

Sometimes the things you buy are used for both business and personal purposes, or for taxable and tax-free sales. In such cases, you have to divide (apportion) the credit fairly using simple turnover-based calculations.

More importantly, Section 17(5) lists **blocked credits** — expenses on which you **cannot** claim ITC at all. These are like "red zones" created to stop misuse of the system.

Common blocked items include:

• Normal cars, vans, or vehicles for carrying people (exceptions if you are in the business of selling vehicles, running transport, or giving driving training).

• Food, catering, beauty treatments, health services, life/ health insurance, or club memberships for employees (unless the law forces the employer to provide them, like canteen facilities in big factories).

• Travel benefits given to employees for holidays.• Construction of your own office, factory, or any immovable property (you cannot claim credit on cement, steel, labour, or architect fees for your own building). However, if the building works like essential "plant and machinery" for your business, courts may allow credit after checking its actual use.

• Goods or services used for Corporate Social Responsibility (CSR) activities.

• Personal use items, gifts, free samples, lost or stolen goods.

• Credit on tax paid under the composition scheme or in fraud cases (with some relaxations for older periods).

The government made some clarifications in recent years. For example, they clearly added a block on CSR expenses and fixed the wording for "plant and machinery" so that everyone understands the same rule.

In September 2025, the GST Council introduced **GST 2.0 reforms**. They simplified tax rates into mainly 5% and 18% slabs. This change makes life easier but sometimes requires businesses to reverse old ITC when items move to a lower rate or become exempt. You may need to adjust your stock and claim refunds in some cases.

Special Situations Where ITC is Allowed (Section 18)

The law gives some relaxations during important changes in your business:

• When you newly register for GST.

• When you move from composition scheme to normal GST scheme.

• When your tax-free supplies become taxable.

• When your GST registration is cancelled. In these cases, you can claim credit on the stock and capital goods you already have, by filing simple declarations in prescribed forms within the given time.

What Have the Courts Said?

Indian courts have played a balancing role — protecting government revenue while being fair to honest taxpayers.

In the important **Safari Retreats case (2024)**, the Supreme Court said that the blocking rules for construction are generally valid. However, if a building or structure is truly essential for your taxable business (for example, a shopping mall that you rent out), you can claim ITC after checking its real function. This "functionality test" has helped many businesses. Later legislative amendments clarified the law retrospectively to align with the original intent.

High Courts have also protected genuine buyers. They have ruled that you cannot lose ITC just because your supplier made a mistake in uploading invoices, as long as you can prove the transaction was real through invoices, bank payments, and proper records.

Overall, courts say ITC is a valuable right, but it must be claimed by strictly following the law.

Practical Challenges in 2026

Even with digital systems, businesses face some difficulties:

• You have to actively match and accept/reject invoices on the GST portal using GSTR-2B and the Invoice Management System.

• When tax rates change under GST 2.0, you may need to reverse or adjust credits.

• Identifying blocked credits (especially for construction, employee benefits, or vehicles) needs careful checking.

From January 2026, there is more flexibility in using CGST and SGST credits against IGST liability, which helps cash flow.

To handle these issues, businesses use good accounting software (ERP), regularly check vendors, keep proper records, and take expert help or advance rulings when in doubt.

Recent Changes and the Road Ahead

GST 2.0 has made the rate structure simpler. The GST Appellate Tribunal (GSTAT) is now working faster to resolve disputes. The government is also adding more digital tools and artificial intelligence to make compliance easier, especially for small businesses. In the future, we can expect better coordination between the Centre and States, wider use of e-invoicing, and solutions for new challenges in the digital economy — all while keeping the main goal of smooth credit flow intact.

Conclusion

The Input Tax Credit system is one of the best features of GST. It removes the old problem of tax-on-tax and makes business fairer and more competitive. Blocked credits act as necessary guardrails to prevent misuse.

Success depends on careful compliance, proper record- keeping, and staying updated with changes. Just like IBC and SARFAESI aim for fair resolution of financial problems, ITC aims for fair and efficient tax payment in day-to-day business.

If you treat ITC as an important part of your financial planning and take professional help when needed, it becomes a powerful tool for your business.

Reference

1. Central Goods and Services Tax Act, 2017 (as amended up to 2026), particularly Sections 16, 17, and 18.

2. Recommendations of the 56th GST Council Meeting held on 3 September 2025 (GST 2.0 reforms and rate rationalisation).

3.*Chief Commissioner of Central Goods and Service Tax & Ors. v. M/s Safari Retreats Private Ltd. & Ors.* (Civil Appeal No. 2948 of 2023, Supreme Court of India, decided on 3 October 2024).

4.Notifications, Rules, and advisories issued by the Central Board of Indirect Taxes and Customs (CBIC) and GST Network (GSTN) during 2025–2026, including updates on ITC set-off rules effective January2026.

5. Institute of Chartered Accountants of India (ICAI), *Handbook on Blocked Credit under GST* (revised edition, December 2025).

6. Judicial rulings from various High Courts (2025–2026) on ITC eligibility, reconciliation, blocked credits, and utilisation.

7. GST Portal updates and clarifications on GSTR-2B, Invoice Management System (IMS), Electronic Credit Reversal and Reclaim Statement (ECRS), and operationalisation of the GST Appellate Tribunal (GSTAT) in 2025–2026.

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