Transitional VAT Credit Carried Forward to GST Regime Cannot Be Refunded under Section 54(3) but Re-credit to Electronic Credit Ledger is Permissible

The Hon'ble Gujarat High Court in ***Dilip Babubhai Patel v. State of Gujarat & Anr. [R/Special Civil Application No. 21685 of 2019 dated June 29, 2026]*** upheld the Department's rejection of refund of transitional SGST credit carried forward under Section 140 of the CGST Act, 2017 and the Gujarat GST Act, 2017 (**"the GST Acts"**) and held that once the accumulated credit of the erstwhile regime is carried forward and transitioned into the GST framework, the statutory bar under the second proviso to Section 142(3) of the GST Acts gets triggered, making refund of such credit impermissible. Mere transfer of credit through Form GST TRAN-1 will not *ipso facto* make the credit worthy of refund under Section 54(3) of the GST Acts. However, the Court partly allowed the writ petition by holding that the Assessee is entitled to re-credit of the said amount to its Electronic Credit Ledger (**"ECL"**) for utilization and directed the Revenue to pass an appropriate order for re-crediting under Form GST PMT-03 within a period of 12 weeks, if it is found that the ITC is required to be re-credited.

Facts:

Dilip Babubhai Patel, Proprietor of M/s Shree Umiya Timbers (**"the Petitioner"**) is engaged in the business of manufacturing wooden pallets and boxes. During the subsistence of the Gujarat Value Added Tax Act, 2003 (**"the VAT Act"**), the Petitioner purchased raw materials on payment of VAT at the rate of 15% whereas the finished goods were sold on payment of VAT at the rate of 5%. Owing to such inverted tax structure, the Petitioner had accumulated excess Input Tax Credit (**"ITC"**) of Rs. 23,74,689/- as on June 30, 2017, duly reflected in its return filed in Form-201 for the month of June 2017 under the VAT Act.

Upon introduction of the GST regime with effect from July 01, 2017, the Petitioner migrated its registration and carried forward the accumulated ITC of Rs. 23,74,689/- pertaining to SGST

(**"Transitional Credit"**) under Section 140 of the GST Acts by filing Form GST TRAN-1, whereupon the said credit stood reflected in the Petitioner's ECL in July 2017.

The inverted duty structure persisted under the GST regime as well, since the inputs suffered tax at the rate of 9% CGST and 9% SGST whereas the finished goods were liable to output tax at the rate of 6% CGST and 6% SGST. Consequently, for the period from July 01, 2017 to March 31, 2018, the Petitioner accumulated excess ITC aggregating to Rs. 28,54,987/-, comprising CGST credit of Rs. 2,40,802/- and SGST credit of Rs. 26,14,185/-, which included the transitional credit of Rs. 23,74,689/-.

The Petitioner filed an application for refund of SGST amounting to Rs. 23,50,000/- in Form GST RFD-01A under Rule 89 of the CGST Rules, 2017 and the Gujarat GST Rules, 2017 (**"the GST Rules"**) on account of inverted duty structure, upon which the said amount was debited from the Petitioner's ECL. However, vide communication dated October 09, 2019, the Department sanctioned refund of only Rs. 4,75,324/- and rejected the balance refund claim of Rs. 18,74,676/- on the ground that the said amount represented transitional SGST credit carried forward under Section 140 of the GST Acts, refund whereof is not admissible under Section 54(3) of the GST Acts. Neither any show cause notice was issued nor any opportunity of hearing was granted under Rule 92 of the GST Rules, nor was the rejected amount re-credited to the Petitioner's ECL as mandated under Rule 93 of the GST Rules.

Being aggrieved, the Petitioner filed the present writ petition praying for refund of Rs. 18,74,676/- along with applicable interest and, in the alternative, for re-crediting of the said amount to its ECL.

Issues:

- Whether refund of unutilized transitional VAT credit, carried forward to the ECL under Section 140 of the GST Acts, can be claimed under Section 54(3) of the GST Acts on account of inverted duty structure?

- Whether the Petitioner is entitled to re-credit of the rejected refund amount to its ECL in terms of Rule 93 of the GST Rules?

Held:

The Hon'ble Gujarat High Court in ***R/Special Civil Application No. 21685 of 2019*** held as under:

- Observed that, Chapter-XX of the GST Acts, comprising Sections 139 to 142, constitutes the transitional provisions governing migration from the erstwhile indirect tax regime to the GST regime. Section 140 of the GST Acts protects the interest of taxpayers by enabling carry forward of ITC available under the existing law, whereas Section 142(3) of the GST Acts stipulates that every claim for refund of any amount of credit, duty, tax or interest paid under the existing law shall be disposed of in accordance with the provisions of the existing law and the amount accruing shall be paid in cash. The first proviso thereto provides for lapsing of the amount of credit which is fully or partially rejected, whereas the second proviso expressly debars refund of any amount of CENVAT credit (including VAT credit) where the balance of the said amount as on the appointed day has been carried forward under the GST Acts.

- Noted that, a combined reading of Section 49(4) and Section 54(3) of the GST Acts demarcates the utilization of ITC from the refund of ITC. Section 49(4) merely allows the amount available in the ECL to be utilized for making payment towards output tax, whereas Section 54(3) permits refund of unutilized ITC only in two circumstances, namely, zero-rated supplies made without payment of tax and accumulation of credit on account of inverted duty structure. Further, Section 49(6) permits refund of the balance in the ECL of amounts payable under "this Act" in accordance with Section 54, which shows that the Parliament never intended refund of credit accumulated under the erstwhile regime under Section 54 of the GST Acts.

- Observed that, a taxpayer migrating to the GST regime cannot pursue both avenues of cash refund and transition of credit concurrently or interchangeably. The taxpayer must either seek refund under the existing laws to be paid in cash under Section 142(3) of the GST Acts or choose to transit the credit for utilization towards discharge of output tax liability. If the taxpayer chooses the latter, the refund claim stands forfeited, though the right to utilize the credit is retained.

- Held that, once the accumulated credit is carried forward, the statutory bar under the second proviso to Section 142(3) of the GST Acts gets triggered, making refund impermissible. Merely because the transit/transfer of credit is permitted through Form GST TRAN-1 to the GST regime, such transfer will not *ipso facto* make the credit worthy of refund under Section 54(3) of the GST Acts and the Petitioner cannot insist upon refund of the transitioned credit *de hors* the statute.

- Distinguished the decision in ***Torrent Pharmaceuticals Ltd. v. Union of India*** **[2024 (22) Centax 431 (Guj.)]** on the ground that the said case was premised on refund of zero-rated supplies and the operation of Section 142(3) of the GST Acts was never in issue. Similarly, in ***Weatherproof Solution v. State of Gujarat [2025 (32) Centax 258 (Guj.)],*** the refund claim was directed to be processed under the provisions of the VAT Act read with Section 174(2)(c) of the GST Acts and not under the GST Acts, whereas ***Ford India Pvt. Ltd. v. Union of India [2025 (94) GSTL 84 (Guj.)]*** involved credit which was not transferred as on the cut-off date. Hence, none of the said decisions would rescue the Petitioner in light of the second proviso to Section 142(3) of the GST Acts.

- Noted that, paragraph 10 of *Circular No. 37/11/2018-GST dated March 15, 2018* issued by the CBIC also clarifies that it should be ensured that no refund of the amount of CENVAT credit is granted in case the said amount has been transitioned under GST, thereby making the intention of the Department of Revenue explicit that once the credit of the erstwhile regime is transitioned under GST, no refund of such credit is granted or allowed.

- Observed that, although no opportunity of hearing was afforded to the Petitioner under Rule 92 of the GST Rules prior to rejection of the refund claim, setting aside the impugned action and remanding the matter exclusively on this ground would be an exercise in futility, since the claim involves a pure legal issue which has been fully articulated through pleadings and submissions before the Court.

- Held that, in terms of Rule 93 of the GST Rules, the Respondent authorities, while partly rejecting the refund claim, ought to have re-credited the amount of credit to the ECL under an order made in Form GST PMT-03. Accordingly, the Petitioner is entitled to re-credit of the said amount to its ECL for utilization.

- Directed that, upon the Petitioner making an application for re-credit, the Respondent authorities shall examine the Petitioner's case after due verification of the relevant facts and records and, in the event it is found that the ITC is required to be re-credited, an appropriate order for re-crediting such amount under Form GST PMT-03 shall be passed within a period of 12 weeks from the date of receipt of the certified copy of the order. The writ petition was accordingly allowed in part.

Our Comments:

Section 142(3) of the CGST Act prescribes that every claim for refund of any amount of CENVAT credit, duty, tax, interest or any other amount paid under the existing law shall be disposed of in accordance with the provisions of the existing law and any amount eventually accruing shall be paid in cash. The second proviso thereto, which formed the fulcrum of the present decision, mandates that no refund shall be allowed of any amount of CENVAT credit where the balance of the said amount as on the appointed day has been carried forward under the GST Acts. The legislative scheme thus places the taxpayer at an irreversible fork at the time of transition –

either claim cash refund of the accumulated credit under the erstwhile law or carry it forward through Form GST TRAN-1 under Section 140 of the CGST Act for utilization towards output tax liability. The election of one remedy operates as a statutory forfeiture of the other.

The judgment also reinforces the settled distinction between utilization of ITC under Section 49(4) of the CGST Act and refund of ITC under Section 54(3) thereof. The Hon'ble Supreme Court in ***Union of India v. VKC Footsteps India Pvt. Ltd. [2021 (52) GSTL 513 (SC)]*** has authoritatively held that refund of unutilized ITC is purely a statutory right, confined to the two contingencies enumerated in the proviso to Section 54(3) of the CGST Act, and that there is no constitutional entitlement to refund beyond what the legislature provides. Equally, the Hon'ble Supreme Court in ***Jayam & Co. v. Assistant Commissioner [(2016) 15 SCC 125] and ALD Automotive Pvt. Ltd. v. Commercial Tax Officer [(2019) 13 SCC 225]*** has held that ITC is in the nature of a concession which can be availed only in accordance with, and subject to, the conditions of the statute. Viewed through this prism, the denial of refund of transitional credit, while preserving its utilization, is consistent with the restrictive statutory architecture of refunds under GST. Further, in the pre-GST regime as well, the Larger Bench of the Hon'ble Bombay High Court in ***Gauri Plasticulture (P) Ltd. v. Commissioner of Central Excise, Indore [2019 (30) GSTL 224 (Bom.)]*** held that cash refund of unutilized accumulated credit cannot be granted in the absence of an express statutory provision.

Pertinently, the Hon'ble Gujarat High Court itself, in ***M/s. Intas Pharmaceuticals Ltd. v. Union of India & Ors. [Special Civil Application No. 12712 of 2019 decided on January 10, 2024, against which the SLP was dismissed by the Hon'ble Supreme Court],*** followed in *Torrent Pharmaceuticals Ltd.* (supra), *Ford India Pvt. Ltd.* (supra) and *Weatherproof Solution* (supra), had recognized the entitlement of an assessee to refund of accumulated credit notwithstanding its transitional origin. The present decision, however, distinguishes the said line of rulings on facts, holding that the interplay of the second proviso to Section 142(3) of the GST Acts was never examined therein. This divergence within the same High Court on the refundability of transitioned credit may eventually warrant an authoritative pronouncement by a Larger Bench or the Hon'ble Supreme Court.

From a compliance standpoint, three practical takeaways emerge. First, taxpayers saddled with transitional credit which remains unutilized owing to an inverted duty structure cannot monetize such credit through a refund claim under Section 54(3) of the CGST Act read with Rule 89(5) of the CGST Rules, since the transitional component does not constitute "Net ITC" availed during the relevant period. Second, where a refund claim is rejected either fully or partly, the taxpayer must insist upon re-credit of the rejected amount to the ECL through an order in Form GST PMT-03 in terms of Rule 93 of the CGST Rules, failing which the taxpayer stands deprived of both the refund and the credit. Third, the ruling underscores that the rejection of a refund claim without issuance of a show cause notice and grant of an opportunity of hearing under Rule 92 of the CGST Rules is a serious procedural infirmity, although the Court, on the facts of the present case, declined to remand the matter on this ground alone, having conclusively answered the pure question of law.

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