
INPUT TAX CREDIT UPON BUSINESS CLOSURE: ANALYSIS OF LEGAL MAXIMS AND PROVISIONS UNDER THE CGST ACT, 2017

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ABSTRACT

The Goods and Services Tax regime, introduced in India on 1 July 2017, was intended to consolidate the country's fragmented indirect tax architecture into a single, destination-based system predicated upon a seamless chain of Input Tax Credit.¹ The mechanism of Input Tax Credit operates by crediting the tax paid on inward supplies to a registered person's electronic ledger, from which it may be applied against the output tax liability arising on outward supplies. In principle, this arrangement eliminates the cascading effect of tax upon tax that characterised the pre-2017 order. In practice, however, the regime contains a structural lacuna of considerable equitable and constitutional consequence: upon voluntary cancellation of GST registration on account of genuine business closure, any unutilised Input Tax Credit remaining in the electronic credit ledger after the mandatory reversal is permanently extinguished, with no statutory mechanism for refund, transfer, or other form of recovery.²

This article examines the framework of established legal maxims and constitutional doctrine in relation to the aforementioned issue. It contends that the current statutory position, produced by the combined operation of Section 29(5) of the Central Goods and Services Tax Act, 2017 and Section 54(3) thereof,³ violates several foundational principles of law, including the prohibition on unjust enrichment (*nemo debet esse locupletior cum alterius jactura*), the protection of vested rights (*nemo dat quod non habet*), the requirement that a recognised right be accompanied by an enforceable remedy (*ubi jus ibi remedium*), the prohibition on State-caused prejudice to a blameless party (*actus curiae neminem gravabit*), the principle that legal impossibility excuses performance (*nemo tenetur ad impossibile*), the rule of

¹ Central Goods and Services Tax Act, 2017, No. 12, Acts of Parliament, 2017 (India) [hereinafter CGST Act].

² CGST Act § 54(3). Refund of unutilised input tax credit is restricted to two situations: zero-rated supplies made without payment of integrated tax under clause (i), and supplies in respect of which the credit has accumulated on account of the rate of tax on inputs exceeding the rate on output supplies under clause (ii).

³ CGST Act § 29(5). The provision requires payment of an amount equivalent to the credit of input tax in respect of inputs held in stock, inputs contained in semi-finished or finished goods held in stock, and capital goods or plant and machinery on the day of cancellation.

strict construction of taxing statutes (*contra proferentem*), and the foundational principle of fiscal neutrality. The article further submits that the framework raises substantial constitutional questions under Articles 14 and 265 of the Constitution of India. The Sikkim High Court's divided judgment in *SICPA India Private Limited v. Union of India*⁴ is examined as the principal judicial occasion on which these questions have been brought into focus. The article concludes with principled proposals for corrective legislative amendment, informed by comparative practice in Australia, Singapore, and the European Union.

Keywords: Input Tax Credit, GST, Business Closure, Unjust Enrichment, Section 54(3), Legal Maxims, Article 14, Article 265, Fiscal Neutrality, CGST Act 2017.

CHAPTER I: INTRODUCTION

India's system of indirect taxation underwent its most significant transformation in 2017 with the introduction of the Goods and Services Tax. Prior to this reform, the indirect tax landscape was characterised by a layered and fragmented structure in which excise duties, service tax, state-level value-added tax, central sales tax, and numerous ancillary levies operated concurrently at different stages of the supply chain. The well-documented consequence was a cascading effect: each successive levy was calculated on a base that already incorporated the tax paid at an earlier stage of production or distribution, with the result that the effective rate of taxation on final consumption significantly exceeded the nominal statutory rate. This distortion was widely recognised as both economically inefficient and contrary to basic principles of fiscal neutrality.

The constitutional amendment enabling the GST reform was enacted in 2016,⁵ and the Central Goods and Services Tax Act, 2017 came into force on 1 July 2017.⁶ The regime operates as a comprehensive, destination-based tax on the supply of goods and services, administered jointly by the Central Government and the States under a dual structure. The instrument through which the regime's central objective of cascading elimination is achieved is the mechanism of Input Tax Credit. Under this mechanism, the tax paid by a registered person on its inward supplies is credited to an electronic ledger maintained on the GST portal, and that credit is available to be applied against the output tax liability arising on the registered person's outward supplies.⁶ The

⁴ *SICPA India Pvt. Ltd. v. Union of India*, W.P. (C) No. 16/2022 (High Ct. Sikkim, Single Bench, 2022), rev'd, *Union of India v. SICPA India Pvt. Ltd.*, W.P. (C) No. 16/2022 (High Ct. Sikkim, Div. Bench, 2023).

⁵ The Constitution (One Hundred and First Amendment) Act, 2016, No. 101, Acts of Parliament, 2016 (India).

⁶ CGST Act §§ 2(59), 2(62) (defining 'input tax' and 'input tax credit' respectively).

result, in principle, is that the tax burden at each stage of the supply chain is confined to the value added at that stage, with the residual burden borne by the final consumer. It is this design that confers upon the Input Tax Credit mechanism its character as the structural foundation of the GST system.

When a registered business ceases to operate and seeks cancellation of its GST registration, Section 29 of the CGST Act governs the procedure.⁷ Section 29(5) imposes on the registered person an obligation to reverse the Input Tax Credit attributable to inputs held in closing stock, inputs contained in semi-finished or finished goods held in stock, and capital goods or plant and machinery held at the time of cancellation.⁹ The rationale for this reversal is coherent: Input Tax Credit availed on assets that remain unsold and unconsumed in taxable supply at the time of closure has not yet fulfilled its intended function within the credit chain, and its retention by the cancelling taxpayer would therefore represent an unwarranted benefit. The reversal mechanism is accordingly a legitimate anti-abuse provision, the logic of which is not in dispute.

The difficulty that this article addresses arises at a different point in the process. After the reversal mandated by Section 29(5) has been effected, there may remain in the electronic credit ledger a residual balance of unutilised Input Tax Credit. This residual credit represents tax paid on inputs that were fully consumed in the course of the registered person's taxable business operations, but in respect of which the accumulated credit could not be set off against output tax liability because the output tax generated in the final period of trading was insufficient to absorb it. The residual credit is, by definition, credit that has satisfied all the conditions of legitimate availing under Section 16 of the Act.⁸ It is the product of lawful commercial activity and scrupulous statutory compliance. Yet the CGST Act contains no provision for the refund of this amount. Section 54(3), which governs the refund of unutilised Input Tax Credit, confines such refunds to two specific situations: zero-rated supplies made without payment of integrated tax, and cases where credit has accumulated by reason of the rate of tax on inputs exceeding the rate on output supplies.¹¹ Business closure is not enumerated.

The practical consequence is that a registered person who has diligently discharged every statutory obligation, remitted tax on every inward supply, and closed their business in full compliance with the law, suffers the permanent and irrecoverable loss of tax that has already

⁷ CGST Act § 29 (cancellation or suspension of registration).

⁸ CGST Act § 16(1)–(4) (conditions precedent for availing input tax credit, including receipt of the supply, possession of a tax invoice, payment of tax by the supplier, and filing of the return).

been collected by the Government through the supply chain. The economic value represented by the residual Input Tax Credit is extinguished without compensation, and the Government retains the corresponding tax receipts without any legal basis for characterising that retention as a lawful fiscal impost. It is this structural outcome that the present article submits to sustained legal and constitutional analysis.

The central judicial occasion for examination of these questions is the Sikkim High Court's decision in *SICPA India Private Limited v. Union of India*.¹² The Single Bench, persuaded by the equitable force of the taxpayer's position, directed the processing of the refund claim. The Division Bench reversed that order, holding that neither Section 54(3) nor any other provision of the CGST Act authorises the refund sought, and that the court could not supply by interpretation a provision that the legislature had not enacted. The Division Bench expressly directed the legislature to address the lacuna. The judgment thus simultaneously identifies the problem with precision and delimits the judicial remedy available in its absence. It is to the legislative dimension of the problem that this article principally directs itself. The aforementioned case currently lies under appeal in front of the Supreme Court. Interpretation in this matter, would therefore address a major concern affecting the taxpayers.

CHAPTER II: LEGAL MAXIMS AS TOOLS OF STATUTORY INTERPRETATION AND CONSTITUTIONAL REVIEW

Legal maxims are distillations of principle developed through sustained adjudication across the Roman law, common law, and equity traditions. Their authority in modern legal systems derives not from any intrinsic force independent of positive law, but from their recurrent judicial endorsement as formulations of principles that the legal order is committed to upholding. In the Anglo-Indian tradition, they serve two analytically distinct functions.

The first function is interpretive. Where a statutory provision is ambiguous in its terms or produces, upon literal application, an outcome that conflicts with an established principle of law, courts invoke the relevant maxim as an aid to identifying the construction that is consistent with the broader legal framework within which the provision operates. The maxim supplies a presumptive orientation: in the absence of clear contrary legislative indication, it is presumed that Parliament did not intend to depart from foundational legal principles. On this approach, the maxim operates as part of the surrounding legal context against which the provision is to be read, rather than as an autonomous constraint upon legislative power.

The second function is evaluative in the context of constitutional review. Maxims that embody requirements of natural justice, equality, and rationality provide a vocabulary for the identification of constitutional deficiencies in legislative provisions. The Supreme Court of India has repeatedly employed maxims in this evaluative role in fiscal cases, recognising that while Parliament enjoys plenary discretion in matters of taxation, the exercise of that discretion is not immune from constitutional scrutiny where it produces results incompatible with the structural principles upon which the legal order rests.⁹

This dual function is of particular relevance to the present inquiry. The lacuna in the CGST Act that this article examines is not a matter of textual ambiguity amenable to interpretive resolution alone. It is a structural omission whose consequences are constitutionally significant. The maxims examined in the following Parts serve both to identify the interpretive arguments available to the taxpayer under the existing statutory text and to demonstrate that the current framework, viewed in constitutional perspective, is legally untenable in its present form.

2.1. NEMO DEBET ESSE LOCUPLETIOR CUM ALTERIUS JACTURA: NO ONE SHOULD BE ENRICHED AT ANOTHER'S EXPENSE

The principle that no one ought to be unjustly enriched at the expense of another is among the oldest and most pervasive in the Western legal tradition. Its origins lie in the Roman law doctrine of unjustified enrichment, where it was elaborated through three distinct *condictiones*: the *condictio sine causa*, addressed to enrichment received without legal foundation; the *condictio indebiti*, addressed to payments made in error; and the *condictio ob causam finitam*, addressed to enrichment whose legal basis had subsequently ceased.¹⁰ The reception of these principles into English common law is conventionally attributed to Lord Mansfield's judgment in *Moses v. Macferlan*, where his Lordship grounded the action for money had and received in the principle that the defendant ought not to retain money that in good conscience belongs to the plaintiff.¹¹ The recognition of unjust enrichment as an independent head of private law by the House of Lords in *Fibrosa Spolka Akcyjna v. Fairbairn Lawson Combe Barbour Ltd.*

⁹ *Safari Retreats Pvt. Ltd. v. Chief Commr. of CGST*, (2024) SCC OnLine SC 2692 ¶ 38 (reaffirming that ITC provisions must be construed purposively, consistently with the objects of the CGST Act, and that restrictions on the credit chain must be strictly construed against the Revenue).

¹⁰ P.S. Atiyah, *The Rise and Fall of Freedom of Contract* 764–65 (1979); Reinhard Zimmermann, *The Law of Obligations: Roman Foundations of the Civilian Tradition* 837–41 (1990) (tracing the *condictiones* in Roman law doctrine).

¹¹ *Moses v. Macferlan*, (1760) 97 ER 676, 681 (KB) (Lord Mansfield CJ).

extended the principle to situations of total failure of consideration.¹²

In the Indian public law context, the doctrine was given constitutional dimensions by the Supreme Court in the Constitution Bench decision of *Mafatlal Industries Ltd. v. Union of India*.¹³ The Court held that the State is constitutionally precluded from retaining tax that is not lawfully due to it, subject to the qualification that refund is unavailable where the tax burden has been passed on to the consumer.¹⁴ In such circumstances, refund to the taxpayer would itself constitute unjust enrichment, since the taxpayer has not borne the economic incidence of the tax. The principle of unjust enrichment thus operates as a bilateral constraint: against the State where it retains tax not lawfully due, and against the taxpayer where refund would occasion a windfall at the consumer's expense.

The application of this principle to the business closure Input Tax Credit problem requires an analysis of the economic incidence of the residual credit. When a registered person pays GST on its inward supplies, the tax is embedded in the price paid to the supplier and is remitted to the Government by the supplier as part of the latter's output tax liability.¹⁵ The registered person receives, in exchange, a credit in the electronic credit ledger representing an entitlement to apply that amount against the output tax liability arising on its own taxable supplies. When the business closes and the residual credit is reversed without refund, the Government retains the tax originally remitted by the supplier. The registered person, for its part, has paid the tax-inclusive price to the supplier and has now lost the benefit of the corresponding credit. The economic burden of the residual Input Tax Credit falls entirely upon the registered person, not upon any consumer: the credit relates to inputs consumed in taxable business operations, not to tax collected from customers on outward supplies. The latter has been remitted to the Government separately through output tax filings. The residual credit therefore represents a net economic cost borne exclusively by the taxpayer, and its extinguishment without compensation enriches the State at the taxpayer's expense.

The qualification recognised in *Mafatlal Industries* accordingly has no application on these

¹² *Fibrosa Spolka Akcyjna v. Fairbairn Lawson Combe Barbour Ltd.*, [1943] AC 32, 61 (HL) (Lord Wright) (recognising unjust enrichment as an independent head of private law).

¹³ *Mafatlal Industries Ltd. v. Union of India*, (1997) 5 SCC 536 (Constitution Bench).

¹⁴ *Mafatlal Industries*, (1997) 5 SCC 536 ¶ 79. The Court further held that the unjust enrichment bar operates where the tax burden has been passed on to the consumer, since in that circumstance it is the consumer rather than the taxpayer who has borne the economic incidence of the tax.

¹⁵ CGST Act §§ 49(2), 49(4) (electronic cash ledger and electronic credit ledger respectively); § 2(82) (defining 'output tax').

facts. The residual Input Tax Credit has not been collected from any consumer; it has been borne by the registered person as the ultimate incidence of tax on its own business inputs. The unjust enrichment concern that the qualification addresses is absent. What is present, in contrast, is the paradigm case for which the doctrine was developed: an enrichment of one party, here the State, at the direct expense and loss of another, here the taxpayer, without any legal justification for the retention of the benefit.

2.2. NEMO DAT QUOD NON HABET AND THE LIMITS OF LEGISLATIVE POWER OVER VESTED RIGHTS

The maxim *nemo dat quod non habet* is classically stated as a principle of property law: a person cannot transfer title superior to that which they themselves hold. Its application in public law is analytically cognate but operates in a different dimension: where a statute has conferred a right upon a person, the legislature cannot, through omission or silence, cause that right to become unenforceable. It may, of course, revoke or modify the right, but only through clear and unambiguous legislative language directed to that end. An oblique extinguishment of a vested statutory right, achieved not through any express provision but through the combined effect of a mandatory obligation and the absence of any mechanism for its fulfilment, does not satisfy this requirement.

The characterisation of the right to avail Input Tax Credit as a vested right was definitively established by the Supreme Court in *Union of India v. VKC Footsteps India Pvt. Ltd.*, where the Court held that once the conditions prescribed by Section 16 of the CGST Act are satisfied, the registered person acquires an indefeasible right to the credit.¹⁶ The conditions in question require that the registered person have received the supply, possessed a valid tax invoice, paid consideration to the supplier, and that the supplier have discharged the corresponding output tax liability.²¹ Where these conditions are satisfied, the credit is recognised as a legally enforceable entitlement, recorded in the official Government register constituted by the electronic credit ledger. The right is not a contingent expectancy or a mere procedural facility; it is a substantive legal entitlement the extinguishment of which requires express legislative authority.¹⁷

¹⁶ *Union of India v. VKC Footsteps India Pvt. Ltd.*, (2022) 2 SCC 603 ¶ 47.

¹⁷ *VKC Footsteps*, (2022) 2 SCC 603 ¶ 47. See also *Godrej & Boyce Mfg. Co. Ltd. v. Dy. Commr. of Sales Tax*, (1992) Supp (3) SCC 98 ¶ 12 (holding that extinguishment of a vested statutory right requires clear and unambiguous legislative language).

The CGST Act contains no express provision extinguishing the right to Input Tax Credit upon cancellation of registration.¹⁸ Section 29(5) mandates the reversal of credit attributable to closing stock and capital goods, and Section 54(3) restricts refund to two enumerated categories. Neither provision declares a forfeiture. The effect of permanent extinguishment is achieved through the interaction of the reversal obligation and the absence of any refund provision, not through any direct statutory act of confiscation. This oblique mode of extinguishing a vested statutory right is precisely what the public law application of *nemo dat quod non habet* prohibits. If the legislature intended to extinguish the residual credit upon business closure, it was obliged to say so in unambiguous terms. Its failure to provide a mechanism for the enforcement of the vested right, once the ordinary mechanism of set-off has been rendered legally unavailable, is constitutionally indistinguishable from an unannounced confiscation.

2.3. UBI JUS IBI REMEDIUM: WHERE THERE IS A RIGHT, THERE MUST BE A REMEDY

The principle that every recognised legal right must be accompanied by an enforceable remedy is one of the foundational axioms of common law jurisprudence. It received its authoritative formulation in the judgment of Holt CJ in *Ashby v. White*, where the Chief Justice observed that it is a vain thing to imagine a right without a remedy, since the want of right and the want of remedy are reciprocal.¹⁹ The principle was subsequently adopted into constitutional discourse by Chief Justice Marshall in *Marbury v. Madison*, where it was treated as a foundational element of constitutional governance.²⁰ In Indian law, the maxim has been consistently applied in both private and public law contexts, including as a basis for the exercise of constitutional jurisdiction under Articles 32 and 226.²¹

The tension between right and remedy in the GST context is analytically stark. The right to Input Tax Credit has been characterised as a vested right by the Supreme Court.²⁷ Section 49 of the CGST Act provides the mechanism through which that right is exercised, namely by

¹⁸ No provision of the CGST Act expressly declares that unutilised input tax credit is forfeited to the State upon cancellation of registration. The non-refundability results from the combined effect of the reversal obligation under § 29(5) and the restrictive enumeration in § 54(3), not from any express forfeiture provision.

¹⁹ *Ashby v. White*, (1703) 92 ER 126, 136 (QB) (Holt CJ).

²⁰ *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 163 (1803) (Marshall CJ).

²¹ *D.K. Basu v. State of West Bengal*, (1997) 1 SCC 416 ¶ 14 (applying the maxim in the public law context as a foundational principle of constitutional governance).

applying the credit in the electronic ledger against the output tax liability on outward supplies.²² However, this mechanism presupposes the existence of an ongoing output tax liability. Upon cancellation of registration consequent upon business closure, there is no further output tax liability, no further outward supplies, and no further occasion upon which the credit could be set off. The statutory mechanism of utilisation is rendered legally unavailable by operation of the very same statute that conferred the right. No alternative mechanism, such as refund, is provided. The registered person accordingly holds a vested right that has become, through the operation of statute, permanently incapable of exercise.

The procedural posture of the *SICPA India* litigation gives concrete expression to this analytical difficulty. The Single Bench, confronted with a registered person whose residual Input Tax Credit had become permanently unenforceable upon cancellation, directed the processing of the refund in the absence of an express statutory pathway, reasoning that the existence of the right demanded the availability of some remedy.²³ The Division Bench, by contrast, held that it was not open to the court to create by interpretation a remedy that the legislature had not enacted, and directed legislative intervention.²⁴ The Division Bench's position reflects a correct understanding of the constitutional limits of judicial power in relation to fiscal legislation. However, it also renders the legislative lacuna the determinative fact: unless and until the legislature acts, the taxpayer's vested right is without remedy. The maxim *ubi jus ibi remedium* identifies this as a legal deficiency of the most fundamental order, and places the obligation to remedy it squarely upon the legislature.

2.4. ACTUS CURIAE NEMINEM GRAVABIT: THE ACT OF THE STATE SHALL PREJUDICE NO MAN

The maxim *actus curiae neminem gravabit* originated in procedural law as a protection for litigants against prejudice caused by the court's own acts or omissions: a party should not be made worse off by reason of a procedural error, delay, or failure attributable to the court rather than to any conduct of the party itself.²⁵ The principle has been extended in Indian

²² CGST Act § 49(5) (prescribing that amounts available in the electronic credit ledger may be utilised towards payment of output tax liability under the Act).

²³ *SICPA India Pvt. Ltd.*, W.P. (C) No. 16/2022 (Single Bench, 2022) (directing the tax authority to process the refund application filed upon cancellation of registration).

²⁴ *Union of India v. SICPA India Pvt. Ltd.*, W.P. (C) No. 16/2022 (Div. Bench, 2023) (holding that the absence of a statutory provision for refund on account of business closure precluded judicial grant of such relief, and directing the legislature to address the lacuna).

²⁵ *Manohar Lal Sharma v. Principal Secretary*, (2014) 2 SCC 532 ¶ 18.

jurisprudence to encompass situations in which the act or omission of the State, in its legislative or executive capacity, directly occasions loss to a party who has not contributed to the circumstances giving rise to that loss.²⁶ On this broader formulation, the maxim requires that where State action or legislative choice is the proximate cause of prejudice to a blameless person, the State bears a responsibility to make good that loss.

In the present context, the prejudice suffered by the business closure taxpayer is attributable entirely to the architecture of the statute as enacted by the State. Section 29(5), by mandating the reversal of Input Tax Credit on closing stock and capital goods, creates the operative condition for the extinguishment of the credit.²⁷ The failure to enact any mechanism for refund of the residual credit ensures that the extinguishment is permanent. Both the legislative act and the legislative omission are attributable to the same legislative authority. The registered person, for its part, has done nothing that could be characterised as conduct contributing to the loss: it has complied with every registration obligation, availed credit within the statutory conditions, filed all required returns, and cancelled registration in accordance with the procedure prescribed by law. The prejudice is a direct and foreseeable consequence of the statutory scheme, and the scheme is the product of the State's legislative choices alone.

The principle *actus curiae neminem gravabit*, as applied to State action, requires that the State make the injured party whole. The precise mechanism of redress is, of course, a matter of legislative design: it may take the form of a refund, a credit transfer, or some other compensatory mechanism. What the principle does not permit is the continued absence of any form of redress. The current statutory scheme, which visits a direct and quantifiable financial loss upon a blameless taxpayer through the operation of a mandatory statutory provision enacted by the State, and which provides no mechanism of relief, is in direct conflict with this principle.

2.5. NEMO TENETUR AD IMPOSSIBILE: NO ONE IS BOUND TO PERFORM AN IMPOSSIBILITY

The principle that the law does not require the impossible is operative in both private and public law. In contract law, it provides that a party is discharged from a contractual obligation that has

²⁶ *Topline Shoes Ltd. v. Corporation Bank*, (2002) 6 SCC 33 ¶ 9 (extending the maxim to encompass loss caused by State administrative action beyond the procedural context in which it originated).

²⁷ CGST Act § 29(5). The debit to the electronic credit ledger produced by the reversal obligation is economically equivalent to a cash payment by the registered person to the Government.

become impossible of performance through circumstances not of its making. In public law, it establishes that a statutory obligation must be interpreted and applied in a manner that does not demand performance that is objectively impossible. Where compliance with a statutory requirement has become impossible through no fault of the person subject to it, the law must provide either an excuse from performance or an alternative mode of compliance.²⁸ Indian courts have applied this principle in the context of tax obligations where the performance required by the statute has been rendered unavailable through supervening circumstance.²⁹

The impossibility that arises in the business closure context is of a legal, rather than a physical, character, and is produced by the operation of the statute itself. Section 49(5) of the CGST Act provides that the amounts available in the electronic credit ledger may be utilised towards payment of output tax liability.³⁰ This provision defines the exclusive mechanism by which Input Tax Credit may be employed. Upon cancellation of GST registration following business closure, however, the registered person ceases to undertake outward supplies and therefore ceases to incur any output tax liability. The sole mechanism of utilisation prescribed by Section 49(5) accordingly becomes legally unavailable.³⁰ The registered person is not in breach of any statutory obligation; it is not refusing to utilise the credit; it is not attempting to circumvent the utilisation requirement. It is simply in the position of being unable to employ the statutory mechanism because the precondition for that mechanism, namely the existence of output tax liability, has ceased to obtain. The impossibility is absolute, legally determined, and attributable entirely to the structure of the Act.

It follows that to hold the registered person responsible for the economic consequence of this impossibility, namely the permanent extinguishment of the credit, is to impose a penalty for the non-performance of an obligation whose performance the statute itself has made unavailable. This is precisely the outcome that *nemo tenetur ad impossibile* prohibits. The obligation to utilise Input Tax Credit against output tax liability cannot be enforced when there is no output tax liability. The appropriate legal consequence is either to excuse the non-utilisation or to provide an alternative mechanism, specifically refund, that permits the economic substance of the right to be realised by other means.

²⁸ *Bharat Sanchar Nigam Ltd. v. Union of India*, (2006) 3 SCC 1 ¶ 91.

²⁹ *State of Tamil Nadu v. Hind Stone*, (1981) 2 SCC 205 ¶ 6 (applying the maxim to statutory compliance obligations and holding that the law does not demand what is objectively impossible).

³⁰ CGST Act § 49(5). Upon cancellation of registration, there is no further output tax liability against which credit may be set off, rendering the statutory mechanism of utilisation legally unavailable.

2.6. CONTRA PROFERENTEM AND THE PRINCIPLE OF STRICT CONSTRUCTION OF TAXING STATUTES

The rule of *contra proferentem* provides that ambiguity in a document is to be resolved against the party who was responsible for its drafting. In the context of taxing statutes, this principle takes the form of the established rule of strict construction: where a fiscal provision is genuinely ambiguous, admitting of two or more equally tenable interpretations, the interpretation more favourable to the taxpayer is to be preferred. The legislature, as the drafter of the taxing statute, must bear the interpretive consequences of ambiguities it has introduced. The taxpayer, as the person subject to the statute, is entitled to the benefit of any doubt that the legislature's drafting has generated.

The Supreme Court has stated this rule with consistency across a series of decisions. In *Commissioner of Income Tax v. Vegetable Products Ltd.*, the Court held that where two constructions are reasonably possible, the one more beneficial to the assessee should be preferred.³¹ In *Kedarnath Jute Manufacturing Co. Ltd. v. CTO*, the Court confirmed that in cases of genuine ambiguity, the benefit of doubt is to be extended to the taxpayer rather than the Revenue.³² These are not merely interpretive preferences; they are rules of law that constrain the manner in which fiscal provisions may be construed.

Two sources of textual ambiguity are relevant to the business closure Input Tax Credit problem. The first arises from the CBIC Circular No. 125/44/2019-GST, which specified the categories of refund claims eligible for processing under the GST framework and included a residual 'any other' category.³³ Read in isolation, this residual category created genuine uncertainty as to whether business closure refund claims might fall within its scope. The rule of strict construction required that this ambiguity be resolved in the taxpayer's favour. However, the force of this argument was substantially attenuated by the subsequent notification of 31 March 2020, which clarified that the circular framework was intended to supplant rather than supplement the statutory provision and confirmed the restrictive effect of Section 54(3)'s two-

³¹ *CIT v. Vegetable Products Ltd.*, (1973) 88 ITR 192, 196 (SC).

³² *Kedarnath Jute Mfg. Co. Ltd. v. CTO*, (1975) 2 SCC 660 ¶ 11.

³³ Circular No. 125/44/2019-GST, Central Board of Indirect Taxes and Customs (Nov. 18, 2019) (specifying categories of refund claims eligible for processing under the GST framework, including a residual 'any other' category).

category enumeration.³⁴ This subsequent clarification is itself of significance, insofar as it reveals a deliberate administrative choice to foreclose the 'any other' interpretation and to restrict refund claims to the two enumerated situations. That a specific administrative act was considered necessary to foreclose the broader interpretation is itself evidence that the original statutory text was genuinely ambiguous, which is precisely the condition that triggers the rule of strict construction in the taxpayer's favour.

The second source of ambiguity is statutory and arises from the text of Section 54(1), which entitles a registered person to claim refund of 'any tax and interest paid on such tax or any other amount paid by him.'³⁵ The phrase 'any other amount paid by him' is susceptible of an interpretation broad enough to encompass Input Tax Credit, which represents, in economic substance, tax already paid through the supply chain on the registered person's inward supplies. On this interpretation, the general refund entitlement under Section 54(1) would operate independently of the specific restriction in Section 54(3), providing a statutory basis for refund of residual Input Tax Credit upon business closure. Whether this interpretation would ultimately prevail is debatable; courts have divided on the question. But the existence of a genuinely arguable construction that benefits the taxpayer is, under the rule established in *Vegetable Products* and *Kedarnath Jute*, itself a sufficient basis for preferring that construction over the more restrictive alternative.

2.7. THE PRINCIPLE OF FISCAL NEUTRALITY

The principle of fiscal neutrality is foundational to the design and operation of any value-added or goods and services tax system. It requires that the tax system not distort the economic decisions of participants in the market, and that economically equivalent situations be treated equivalently for tax purposes. The structural mechanism through which this principle is realised in a GST system is the credit chain: the tax at each stage is limited to the value added at that stage, and any residual tax borne at the inputs stage is neutralised through the credit mechanism. Where the credit mechanism fails to neutralise the tax on inputs, fiscal neutrality is compromised and the system imposes an effective tax burden on business activity beyond the

³⁴ Notification No. 16/2020-Central Tax (Mar. 23, 2020); Circular No. 135/05/2020-GST, CBIC (Apr. 1, 2020) (clarifying that the Circular No. 125/44/2019-GST framework is exhaustive and supplants rather than supplements the statutory provision, thereby confining ITC refund to the two situations expressly enumerated in § 54(3)).

³⁵ CGST Act § 54(1). The phrase 'any other amount paid by him' is the source of genuine textual ambiguity as to whether residual ITC upon business closure falls within the general refund provision independently of the restriction in § 54(3).

value added at the relevant stage.

The European Court of Justice has treated fiscal neutrality as a fundamental principle of the common VAT system, the derogation from which requires express authorisation by the governing legal framework.³⁶ Comparative GST jurisdictions, including Australia and Singapore, embed the same principle in their legislative frameworks, each providing mechanisms to ensure that businesses exit the tax system without bearing an uncompensated residual tax burden.³⁷ The Supreme Court of India has affirmed that fiscal statutes must be read purposively, in light of their objects, context, and text together,³⁸ and the objects of the CGST Act explicitly include the elimination of the cascading effect and the creation of a seamless credit chain, both of which are expressions of the fiscal neutrality principle.

The denial of Input Tax Credit refund upon business closure violates fiscal neutrality in two analytically distinct respects. The first concerns the distortion of the economic decision to close. Where a business cessation occasions the permanent forfeiture of accumulated Input Tax Credit, the closing taxpayer bears an economic cost of exit that does not arise for a business that continues to operate. A business with accumulated Input Tax Credit faces an artificial incentive to continue operating beyond the point of commercial viability, or alternatively to structure its exit as a business transfer rather than a clean closure, solely to avoid the tax consequence of closure. Neither of these outcomes reflects an economically rational response to commercial conditions; both are distortions attributable exclusively to the tax treatment of business closure Input Tax Credit. Such distortions are antithetical to the fiscal neutrality that the GST regime is designed to achieve.

The second violation concerns horizontal equity among taxpayers in economically equivalent positions. Section 54(3) provides for refund of unutilised Input Tax Credit in two categories of cases: zero-rated supplies and inverted duty structure situations.³⁹ In both categories, the rationale for refund is that the registered person has borne input tax that cannot be absorbed against output tax liability, and that the system should not impose a net tax burden in those circumstances. The business closure taxpayer is in precisely the same economic position: they

³⁶ *Case C-110/98, Gabalfrisa SL v. AEAT*, [2000] ECR I-1577 ¶ 44 (ECJ).

³⁷ A New Tax System (Goods and Services Tax) Act 1999 (Cth) (Austl.) §§ 9-20, div. 138; Goods and Services Tax Act 1993 (Sing.) s 19.

³⁸ *Vodafone International Holdings BV v. Union of India*, (2012) 6 SCC 613 ¶ 73.

³⁹ CGST Act § 54(3)(i)–(ii). The refund mechanism under both clauses has been operationalised through Central Goods and Services Tax Rules, 2017, rr. 89–97 and Form RFD-01.

have borne input tax on lawfully acquired inputs that cannot be absorbed against any output tax liability because the business has ceased. The mechanism and the administrative infrastructure for processing Input Tax Credit refunds already exist within the system established by Section 54(3). The application of that mechanism to the business closure case would require no structural innovation. The differential treatment of these three categories of taxpayer, all of whom are in materially indistinguishable economic positions, is not grounded in any coherent policy rationale and cannot be defended as a principled application of the fiscal neutrality that the system purports to embody.

CHAPTER III: CONSTITUTIONAL DIMENSIONS: ARTICLE 14 AND ARTICLE 265

3.1. ARTICLE 14: EQUALITY BEFORE LAW AND THE DOCTRINE OF NON-ARBITRARINESS

Article 14 of the Constitution guarantees to every person equality before law and equal protection of the laws. In its original formulation, the guarantee was interpreted primarily through the doctrine of reasonable classification, under which a legislative distinction was valid under Article 14 if it rested upon an intelligible differentia that bore a rational nexus to the object of the legislation.⁴⁰ The scope of Article 14 was significantly broadened through a line of decisions from the 1970s onwards. In *E.P. Royappa v. State of Tamil Nadu*, Bhagwati J. articulated the proposition that equality and arbitrariness are mutually exclusive, and that any State action that is arbitrary in character violates Article 14 irrespective of whether it can be characterised as discriminatory in the classification sense.⁴¹ This development culminated in the formulation adopted by Nariman J. in *Shayara Bano v. Union of India*, where the Court held that legislation that is manifestly arbitrary, excessive and disproportionate, and lacking in guiding principles, is constitutionally vulnerable under Article 14.⁴²

The business closure Input Tax Credit framework exhibits manifest arbitrariness in three independently cognisable respects. The first is the differential treatment of the electronic cash ledger and the electronic credit ledger upon cancellation of registration. An excess balance in the electronic cash ledger is refundable to the registered person upon cancellation under Rule

⁴⁰ *Budhan Choudhry v. State of Bihar*, AIR 1955 SC 191 ¶ 5.

⁴¹ *E.P. Royappa v. State of Tamil Nadu*, (1974) 4 SCC 3 ¶ 85 (Bhagwati J.).

⁴² *Shayara Bano v. Union of India*, (2017) 9 SCC 1 ¶ 101 (Nariman J.).

89(1)(i) of the CGST Rules.⁴³ An unutilised balance in the electronic credit ledger is not. Both balances represent, in economic substance, tax paid: the cash ledger balance reflects amounts remitted directly by the registered person in cash, while the credit ledger balance reflects tax paid through the supply chain by the registered person's suppliers on inward supplies acquired by the registered person. The distinction between direct cash payment and payment through the supply chain does not, in any principled analysis, constitute a rational basis for differential treatment in the context of refund. The taxpayer's economic position at the point of cancellation is identical in respect of both balances.

The second instance of arbitrariness is the differential treatment of taxpayers in materially identical economic circumstances. An exporter whose Input Tax Credit cannot be absorbed against output tax receives a refund. A manufacturer subject to an inverted duty structure whose Input Tax Credit cannot be absorbed against output tax receives a refund. A business closure taxpayer whose Input Tax Credit cannot be absorbed against output tax receives no refund.⁴⁴ The economic predicament in all three cases is the same. No provision of the Act articulates a principled basis for treating the business closure case differently. The asymmetry is a product of legislative inadvertence, and inadvertence is not a constitutional justification for differential treatment.

The third instance arises from the conversion of a neutral event into a fiscal liability event by operation of the statutory architecture. Business closure, in the ordinary course, is a lawful exercise of the registered person's commercial autonomy. Under the current framework, however, it occasions the permanent forfeiture of accumulated Input Tax Credit. The registered person who closes the business is placed in a materially worse position than a registered person who continues to operate, solely by reason of having exercised the legal right to cease trading. There is no policy rationale within the objects of the CGST Act that supports the imposition of this financial disadvantage on the exercise of a lawful commercial choice.

3.2. ARTICLE 265: NO TAX WITHOUT AUTHORITY OF LAW

Article 265 of the Constitution of India provides that no tax shall be levied or collected except

⁴³ Central Goods and Services Tax Rules, 2017, r. 89(1)(i).

⁴⁴ CGST Act § 54(3)(i)–(ii). An exporter whose ITC cannot be absorbed against output tax receives a refund; an inverted-duty-structure taxpayer in identical circumstances receives a refund; the business closure taxpayer in the same economic position receives no refund. No statutory provision articulates a principled basis for this asymmetry.

by authority of law.⁴⁵ The provision has been construed broadly by the Supreme Court, its scope extending beyond the initial imposition of a levy to encompass the continued retention of amounts by the State. Where the State retains tax that it is not lawfully entitled to retain, such retention is constitutionally as objectionable as an unlawful levy. In *Godfrey Phillips India Ltd. v. State of Uttar Pradesh*, the Court held that the State cannot retain money paid by a taxpayer in the absence of a specific provision of law authorising such retention.⁴⁶ This principle was further elaborated in *State of Kerala v. Aluminium Industries Ltd.*, where the Court held that Article 265 requires a legal foundation not merely for the levy but for the retention of amounts collected.⁴⁷

The constitutional question arising in the present context is whether there exists any provision of law that authorises the permanent retention by the Government of the amount represented by the reversed Input Tax Credit. Section 29(5) provides the authority for the reversal itself: it creates the obligation to reverse Input Tax Credit attributable to closing stock and capital goods.⁴⁸ However, Section 29(5) does not purport to authorise the permanent appropriation of the reversed amount. It does not characterise business closure as a taxable event. It does not declare the reversed credit to constitute a levy, a forfeiture, or a fiscal impost. The permanent retention of the reversed amount is not the product of any express fiscal provision; it results from the reversal obligation combined with the absence of any refund or recovery mechanism.⁴⁹

On the authority of *Godfrey Phillips* and *Aluminium Industries*, an authority of law that is implied or achieved obliquely through the combination of an express obligation and an absence of relief does not satisfy the requirement of Article 265. The legislature that wishes to impose a fiscal burden, including the burden of Input Tax Credit forfeiture upon business closure, must do so in clear and express statutory language. The current CGST Act does not contain any such provision. The permanent retention of the reversed Input Tax Credit by the State accordingly lacks the authority of law that Article 265 requires and rests upon constitutionally insecure

⁴⁵ India Const. art. 265.

⁴⁶ *Godfrey Phillips India Ltd. v. State of Uttar Pradesh*, (2005) 2 SCC 515 ¶ 19.

⁴⁷ *State of Kerala v. Aluminium Industries Ltd.*, AIR 1965 SC 1429 ¶ 9 (holding that art. 265 requires not merely a law authorising the initial levy but equally a law authorising the continued retention of amounts collected).

⁴⁸ CGST Act § 29(5). The debit entry in the electronic credit ledger upon reversal constitutes, in economic substance, a payment by the registered person to the Government equivalent in value to the input tax credit reversed.

⁴⁹ No provision of the CGST Act identifies business closure as a taxable event or declares the reversal of ITC upon cancellation to constitute a levy, tax, fee, or fiscal impost. The permanent retention of the reversed amount results from statutory silence rather than from any express appropriating provision.

foundations.

CHAPTER IV: PROPOSED PRINCIPLES FOR A CORRECTIVE LEGISLATIVE FRAMEWORK

The analysis undertaken in the preceding Parts of this article converges upon a clear prescriptive conclusion: the CGST Act requires amendment to provide a specific, express mechanism for the refund of unutilised Input Tax Credit upon genuine business closure. The analysis of the legal maxims and constitutional provisions violated by the current framework establishes not merely the desirability but the legal necessity of such an amendment. The following principles, drawn from the doctrinal analysis and comparative experience, are submitted as the appropriate basis for the design of the corrective provision.

The first and foundational principle is that the refund should be conferred as a matter of statutory right rather than administrative discretion. A registered person who has satisfied the conditions for the availing of Input Tax Credit under Section 16, who has complied with all return filing obligations, and who has cancelled registration on account of genuine business closure, should be entitled as of right to a refund of the residual credit remaining after the Section 29(5) reversal. The entitlement should not be dependent upon the exercise of any discretion by the revenue authority, although verification of the claim's legitimacy is entirely appropriate as a precondition to payment.⁵⁷

The second principle is that the reversal obligation under Section 29(5) should be preserved without modification. That obligation, as noted above, rests upon a coherent rationale: Input Tax Credit attributable to assets still held at the time of closure has not yet been consumed in taxable supply and its retention would represent an unearned benefit. The proposed refund mechanism applies only to the residual credit remaining after the Section 29(5) reversal has been effected, that is, to credit in respect of inputs already fully consumed in the registered person's taxable business operations.⁵⁸

The third principle requires the incorporation of appropriate safeguards against abuse of the refund mechanism. These should include a mandatory audit of claims above a prescribed threshold; a requirement that the claimant demonstrate by documentary evidence that the Input Tax Credit relates to inputs consumed in taxable supply and that the economic incidence of the tax has not been transferred to any consumer; a limitation period of two years from the date of

the cancellation order within which a claim must be made; and the application of the unjust enrichment verification established by Section 54(8) of the CGST Act to all business closure refund claims.⁵⁰

The fourth principle is that the GST portal's technical infrastructure must be configured to accept post-cancellation refund applications under the new provision. The portal, as currently constituted, does not accommodate refund applications filed after cancellation of registration. A dedicated application form, whether an amended Form RFD-01A or a new Form RFD-11, should be developed for this purpose and integrated into the portal's workflow.⁵¹

The fifth principle draws upon the comparative experience of jurisdictions that have confronted and resolved analogous problems in their GST and VAT systems. The Australian Division 138 mechanism, which provides a comprehensive and administratively workable framework for the treatment of Input Tax Credit upon cessation of enterprise activity within a dual Federal-State tax architecture comparable to the Indian CGST-SGST structure,⁵² is particularly instructive. The Singapore deregistration framework⁵³ and the European Union's VAT adjustment provisions upon cessation of taxable activity⁵⁴ provide further models from which the design of an Indian corrective mechanism may be developed. The common feature of these comparative frameworks is the recognition that a business exiting the consumption tax system should not be required to bear a residual tax burden in respect of inputs lawfully acquired and consumed in the course of taxable activity.

Finally, consideration should be given to the establishment of an adjudicatory or administrative mechanism dedicated to the resolution of disputes arising under the new provision, together with waiver or settlement schemes for cases in which the quantum of the refund is contested but the entitlement to it is not in doubt. The acknowledgment of the right in clear statutory language is the essential and unavoidable first step. The procedural infrastructure required for

⁵⁰ CGST Act § 54(8) (requiring the proper officer to determine, before issuing a refund order, whether the amount is due and whether the applicant has passed on the incidence of tax to another person).

⁵¹ Central Goods and Services Tax Rules, 2017, r. 89; Form RFD-01. A dedicated post-cancellation form, provisionally designated Form RFD-11 or an amended Form RFD-01A, would be required to operationalise a business closure ITC refund mechanism on the GST portal.

⁵² A New Tax System (Goods and Services Tax) Act 1999 (Cth) (Austl.) div. 138 (addressing GST consequences of cessation of enterprise activity, including adjustment of input tax credits and cancellation of registration).

⁵³ Inland Revenue Authority of Singapore, *GST Guide on Deregistration and Treatment of Assets on Hand at Deregistration* (4th ed. 2022) (providing for output tax adjustments and ITC treatment upon GST deregistration).

⁵⁴ Council Directive 2006/112/EC of 28 November 2006 on the Common System of Value Added Tax, arts. 184–186 (governing the adjustment of deductions upon cessation of taxable activity in EU member states).

its effective exercise is the necessary complement.

CHAPTER V: CONCLUSION

The Goods and Services Tax was introduced to India with the promise of a coherent, seamless, and equitable indirect tax system. The Input Tax Credit mechanism was designed to be the structural foundation of that promise, the means by which the longstanding cascading distortion of the prior system would be definitively eliminated. That promise remains unredeemed in the specific and significant context of business closure.

A registered person who has operated within the GST system for the duration of their business activity, who has diligently remitted tax on every inward supply, who has filed every return, and who has exercised the lawful right to cease business operations, discovers upon cancellation of registration that the accumulated Input Tax Credit in their electronic credit ledger is permanently extinguished. The Government retains the corresponding tax receipts. The taxpayer receives nothing in return. The statutory framework, as it presently stands, affords no remedy.

This article has sought to demonstrate, through systematic application of established legal maxims and constitutional doctrine, that this outcome is legally indefensible. It constitutes unjust enrichment of the State at the taxpayer's expense. It extinguishes a vested statutory right through oblique means rather than express provision. It denies a remedy to a right that the Supreme Court has affirmed as indefeasible. It visits prejudice upon a party whose conduct has been, in every respect, compliant with the law. It demands the legally impossible. It perpetuates textual ambiguity that the rule of strict construction requires to be resolved in the taxpayer's favour. It violates the foundational principle of fiscal neutrality that the GST regime is expressly designed to uphold. And it raises constitutional questions of substance under both Article 14 and Article 265 of the Constitution of India.

The judicial response to the problem, as illustrated by the *SICPA India* litigation, has been divided. The Single Bench gave effect to the equitable force of the taxpayer's position. The Division Bench correctly identified the limits of judicial power in the face of a clear statutory restriction and directed the legislature to act. It is to the legislature, therefore, that the conclusions of this article are ultimately addressed.

The corrective amendment proposed in this article requires no structural innovation. The legal basis for a refund of unutilised Input Tax Credit is already present in the conceptual framework of Section 54. The administrative infrastructure for processing such refunds is already operational. The comparative experience of analogous jurisdictions demonstrates that a workable mechanism can be designed and implemented without difficulty. What is required is legislative will: the express recognition, in the text of the CGST Act, that a registered person who closes a business in good faith is entitled to recover tax that has been lawfully paid and cannot, through no fault of their own, be utilised in the manner that the statute prescribes.

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