GSTZONE

UTGST & Compensation Cess

The two Acts most people never read

The complete guide, plus all 44 sections and rules

Text sourced from the Central Board of Indirect Taxes and Customs

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A Khemchandani Finance initiative

Start here

The UTGST Act does for union territories without a legislature what the SGST Acts do for states. If you supply within Chandigarh, Lakshadweep, Andaman and Nicobar, Dadra and Nagar Haveli and Daman and Diu, or Ladakh, the state half of your tax is UTGST rather than SGST - mechanically identical, differently named.

The Compensation Cess Act funded the promise made to states when GST replaced their own taxes: that their revenue would be protected for a transition period. It is levied on a narrow list of demerit and luxury goods, on top of GST.

Cess has its own credit silo. Credit of compensation cess can only be used to pay compensation cess - it cannot be set off against CGST, SGST or IGST, which surprises businesses that assume all credit is fungible.

A worked example

Cess credit that could not be used

Compensation cess paid on inputs	**₹3,40,000**	Sits in its own credit silo
Output GST liability	**₹5,10,000**	CGST, SGST and IGST
Cess credit usable against it	**₹0**	Cess credit pays cess only

> **The point:** ₹3.4 lakh of perfectly valid credit, unusable against the liability the business actually had. If you deal in cess-bearing goods, the cess ledger has to be planned separately.

The mistakes that cost people money

- Charging SGST on a supply within a union territory that should carry UTGST.
- Planning cash flow on the assumption that cess credit can offset ordinary GST. It cannot.
- Overlooking cess entirely on notified goods, because the GST rate looked right on its own.

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Every provision, explained

CESS ACT S.1 · GST (COMPENSATION TO STATES) ACT, 2017

Short title, extent and commencement

The GST (Compensation to States) Act, 2017 extends to the whole of India and came into force from the date notified - 1 July 2017 for the operative provisions.

UTGST S.1 · UTGST ACT, 2017

Short title, extent and commencement

The UTGST Act applies to the Union territories without a legislature - Andaman and Nicobar, Lakshadweep, Dadra and Nagar Haveli and Daman and Diu, Ladakh, Chandigarh and other territories. Delhi, Puducherry and Jammu and Kashmir have their own SGST Acts instead.

CESS ACT S.2 · GST (COMPENSATION TO STATES) ACT, 2017

Definitions

Definitions for the compensation cess law; terms not defined here carry their CGST or IGST Act meaning.

UTGST S.2 · UTGST ACT, 2017

Definitions

Definitions for the UTGST Act; everything not defined here carries the meaning given in the CGST Act or the IGST Act.

CESS ACT S.3 · GST (COMPENSATION TO STATES) ACT, 2017

Projected growth rate

The projected growth of a State's subsumed revenue during the transition period is fixed at 14 per cent a year - the benchmark against which compensation was computed.

UTGST S.3 · UTGST ACT, 2017

Officers under this Act

The Administrator of the Union territory appoints the Commissioner and the other classes of officers needed to run the Act, and they are proper officers for their assigned functions.

CESS ACT S.4 · GST (COMPENSATION TO STATES) ACT, 2017

Base year

The base year for computing compensation is the financial year ending 31 March 2016.

UTGST S.4 · UTGST ACT, 2017

Authorisation of officers

The Administrator may authorise an officer to appoint UTGST officers below the rank of Assistant Commissioner.

CESS ACT S.5 · GST (COMPENSATION TO STATES) ACT, 2017

Base year revenue

Base year revenue is the State's and its local bodies' collections in the base year from the taxes subsumed into GST, excluding items such as entertainment tax retained by local bodies, cesses on supplies not subsumed, and taxes on alcohol and petroleum.

UTGST S.5 · UTGST ACT, 2017

Powers of officers

A UTGST officer exercises the powers and duties given by the Act subject to the Commissioner's conditions; a senior officer may exercise a subordinate's powers, and delegated functions are treated as exercised by the delegating officer.

CESS ACT S.6 · GST (COMPENSATION TO STATES) ACT, 2017

Projected revenue for any year

Projected revenue for a year is the base year revenue grown at 14 per cent compounded - the section carries its own worked illustration.

UTGST S.6 · UTGST ACT, 2017

Authorisation of officers of central tax as proper officer in certain circumstances

Central tax officers are also proper officers under the UTGST Act, and once one authority starts proceedings on a subject matter the other cannot start a parallel proceeding on the same subject - the cross-empowerment rule that prevents two departments running the same case.

- Cross-empowerment works the same way as section 6 of the CGST Act: once one administration initiates a proceeding on a subject matter, the other cannot start a parallel one.

CESS ACT S.7 · GST (COMPENSATION TO STATES) ACT, 2017

Calculation and release of compensation

Compensation is worked out provisionally every two months and finally after the CAG-audited figures, as the shortfall between projected revenue and the State's actual GST revenue for that period.

UTGST S.7 · UTGST ACT, 2017

Levy and collection

The charging section: UTGST is levied on every intra-Union-territory supply, on the value fixed by section 15 of the CGST Act, at rates up to 20 per cent notified on the Council's recommendation, alongside an equal CGST. It carries the reverse charge and the section 9(5) e-commerce liability, and excludes alcoholic liquor for human consumption. Petroleum products enter the levy only from a date the Council recommends.

- UTGST applies only in the Union territories WITHOUT a legislature. Delhi, Puducherry and Jammu and Kashmir have their own SGST Acts, so a supply there attracts CGST plus SGST, not UTGST - getting this wrong misstates the tax heads on the invoice.
- The rate ceiling in section 7(1) mirrors the CGST ceiling, and the same rate notifications apply as UT Tax (Rate) notifications with the same numbers.

CESS ACT S.8 · GST (COMPENSATION TO STATES) ACT, 2017

Levy and collection of cess

The charging section for compensation cess: cess is levied on notified supplies - today essentially pan masala, tobacco products and specified goods - on the same value as GST, over and above CGST plus SGST or IGST. Composition taxpayers do not collect it.

- Compensation cess is charged over and above GST on the notified goods - today essentially pan masala, tobacco and tobacco products, aerated waters and specified motor vehicles - under Notification 01/2017-Compensation Cess (Rate) as amended.
- A composition taxpayer neither collects nor pays the cess on his outward supplies.
- Cess is also payable on imports, collected with customs duty, and on reverse-charge supplies of the notified goods.
- The rate structure for tobacco was revised alongside the 22-09-2025 GST reset - Notification 03/2025-Compensation Cess (Rate) dated 31-12-2025 amends 01/2025; check the current entry before quoting a figure.

UTGST S.8 · UTGST ACT, 2017

Power to grant exemption from tax

The Central Government may exempt goods or services from UTGST, absolutely or conditionally, by notification on the Council's recommendation, and may issue a special order in an individual case.

CESS ACT S.8A · GST (COMPENSATION TO STATES) ACT, 2017

Power not to recover cess not levied or short levied as a result of general practice.

Where a general practice of not charging or short-charging the cess prevailed across the trade, the Government may direct that the cess not be recovered for that period.

UTGST S.8A · UTGST ACT, 2017

Power not to recover Goods and Services Tax not levied or short-levied as a result of general practice.

Where a general practice of not charging or short-charging UTGST prevailed across the trade, the Government may direct that the tax not be recovered for that period.

CESS ACT S.9 · GST (COMPENSATION TO STATES) ACT, 2017

Returns, payments and refunds

Cess is paid, returned and refunded with the GST returns; the CGST machinery applies, and cess credit can be used only to pay cess.

- Cess credit can be used ONLY to pay cess - it cannot be set against CGST, SGST or IGST, which is why exporters of cess goods accumulate it and claim refund.
- Refund of accumulated cess credit is available on zero-rated supplies of cess goods made under an LUT (Circular 45/19/2018-GST).

UTGST S.9 · UTGST ACT, 2017

Payment of tax

Payment of tax: IGST credit is used first for IGST, then for CGST or UTGST; UTGST credit goes to UTGST and then to IGST; and CGST credit can never be used to pay UTGST or the other way round.

- Utilisation follows the same IGST-first sequence as the CGST Act, read with sections 9A and 9B and Rule 88A.

UTGST S.9A · UTGST ACT, 2017

Utilisation of input tax credit

UTGST credit may be used only after the IGST credit has been fully utilised, for IGST or UTGST as the case may be.

- Mirrors section 49A of the CGST Act - UTGST credit may be used only after IGST credit is exhausted.

UTGST S.9B · UTGST ACT, 2017

Order of utilisation of input tax credit

The Government may prescribe the order and manner in which credit is used - the rule behind the IGST-first utilisation sequence in Rule 88A.

- Mirrors section 49B - the power under which Rule 88A relaxes the order of utilisation within IGST.

CESS ACT S.10 · GST (COMPENSATION TO STATES) ACT, 2017

Crediting proceeds of cess to Fund

Cess proceeds go to a non-lapsable GST Compensation Fund, from which compensation is released to the States; the unutilised balance is shared as prescribed at the end of the transition period.

UTGST S.10 · UTGST ACT, 2017

Transfer of input tax credit

Where UTGST credit is used to pay IGST, the Centre transfers a matching amount from the UTGST account to the IGST account - a settlement provision.

CESS ACT S.11 · GST (COMPENSATION TO STATES) ACT, 2017

Other provisions relating to cess

The CGST Act and rules - assessment, input tax credit, short levy, interest, appeals, offences and penalties - apply to the cess as far as may be, so there is no separate procedure for cess disputes.

- The CGST machinery applies to the cess, so demands, appeals, interest and penalties on cess follow the same sections - there is no separate cess procedure.

UTGST S.11 · UTGST ACT, 2017

Officers required to assist proper officers

Police, Railways, Customs, land-revenue, central tax and State tax officers must assist the proper officers in carrying out the Act.

CESS ACT S.12 · GST (COMPENSATION TO STATES) ACT, 2017

Power to make rules

The Central Government makes the rules under this Act on the Council's recommendation.

UTGST S.12 · UTGST ACT, 2017

Tax wrongfully collected and paid to Central Government or Union territory Government

If you treated a supply as intra-UT and paid CGST plus UTGST and it is later held to be inter-State, you get a refund of what you paid and pay IGST with no interest; the same protection works in reverse. This is what saves an honest classification error from becoming an interest exposure.

- The UTGST counterpart of section 77 of the CGST Act and section 19 of the IGST Act - refund of the wrongly paid head with no interest on the correcting payment.

CESS ACT S.13 · GST (COMPENSATION TO STATES) ACT, 2017

Laying of rules before Parliament

Every rule made under this Act must be laid before both Houses of Parliament for thirty days.

UTGST S.13 · UTGST ACT, 2017

Recovery of tax

Where an amount is unpaid under the UTGST Act, a central tax officer recovering CGST dues from that person may also recover the UTGST amount and credit it to the Union territory account.

CESS ACT S.14 · GST (COMPENSATION TO STATES) ACT, 2017

Power to remove difficulties

Removal of difficulties: the Central Government may pass orders to resolve a difficulty in giving effect to the Act, within the period allowed by the section.

UTGST S.14 · UTGST ACT, 2017

Definitions

Definitions for the advance-ruling chapter of the UTGST Act - advance ruling, applicant, application and the Authority - read with sections 95 to 106 of the CGST Act.

UTGST S.15 · UTGST ACT, 2017

Constitution of Authority for Advance Ruling

The Central Government constitutes an Authority for Advance Ruling for each Union territory, with one member from the central tax side and one from the UT tax side; smaller UTs may be notified to use another UT's Authority.

UTGST S.16 · UTGST ACT, 2017

Constitution of Appellate Authority for Advance Ruling

The Central Government constitutes the Appellate Authority for Advance Ruling for the Union territory - the Chief Commissioner of central tax and the Commissioner of UT tax - which hears appeals against an advance ruling.

UTGST S.17 · UTGST ACT, 2017

Migration of existing tax payers

Migration: every person registered under an earlier law with a valid PAN was issued a provisional registration on 1 July 2017, made final on furnishing the prescribed information, with an option to cancel where the person was not liable to register.

UTGST S.18 · UTGST ACT, 2017

Transitional arrangements for input tax credit

Transitional credit: a registered person (other than a composition taxpayer) could carry the closing balance of eligible earlier-law credit into the electronic credit ledger, subject to the conditions and the time limits in the transitional rules.

UTGST S.19 · UTGST ACT, 2017

Transitional provisions relating to job work

Transitional relief for job work: inputs or semi-finished or finished goods lying with a job worker on the appointed day carry no tax if returned within six months (extendable by two months), otherwise the credit is recovered.

UTGST S.20 · UTGST ACT, 2017

Miscellaneous transitional provisions

Miscellaneous transitional provisions - goods returned after the appointed day, price revisions, refunds and pending claims under the earlier law, and contracts entered into before GST.

UTGST S.21 · UTGST ACT, 2017

Application of provisions of Central Goods and Services Tax Act

Most of the CGST Act - supply, composition, time and value, input tax credit, registration, invoicing, returns, payment, refunds, assessment, audit, demands, appeals, offences - applies to UTGST as well, with the changes stated here.

- Because most of the CGST Act is borrowed, a UTGST question is usually answered by reading the CGST provision - only registration, levy, credit utilisation and advance ruling have their own UTGST text.

UTGST S.22 · UTGST ACT, 2017

Power to make rules

The Central Government may make UTGST Rules on the Council's recommendation, with retrospective effect where stated.

UTGST S.23 · UTGST ACT, 2017

General power to make regulations

The Board may make regulations, consistent with the Act and rules, to carry out its purposes.

UTGST S.24 · UTGST ACT, 2017

Laying of rules, regulations and notifications

Every rule, regulation and notification must be laid before both Houses of Parliament for thirty days; Parliament may modify or annul it, and anything already done stays valid.

UTGST S.25 · UTGST ACT, 2017

Power to issue instructions or directions

The Commissioner may issue orders, instructions or directions to UT tax officers for uniform implementation, and those officers must follow them.

UTGST S.26 · UTGST ACT, 2017

Removal of difficulties

Removal of difficulties: the Central Government may pass orders to resolve a difficulty in giving effect to the Act. The window for such orders has closed, so the existing orders stand but no new one can be issued.