

K-9 Enterprises vs. State of Karnataka

Legality of blocking of Electronic Credit Ledger (ECL) under Rule 86A of CGST Rules, 2017 without pre-decisional hearing and without independent application of mind.

Date of Order: April 2, 2024
Case Law No: GIB-KHC-2024-11
Source: GST INDIA Biz (www.gstindia.biz)

CASE DESCRIPTION / SUMMARY

Background

The appellants — GST-registered businesses dealing in lead, lead scrap and allied goods — had availed Input Tax Credit (ITC) on purchases from GST-registered suppliers, which stood credited in their Electronic Credit Ledgers (ECL). The tax authorities, acting on a field visit report of the Assistant State Tax Officer, Vasco-da-Gama, Goa (an officer from another jurisdiction), which found certain suppliers to be non-existent or not conducting business from their registered place, issued orders dated 27.06.2023 blocking the ECL of the appellants by invoking Rule 86A of the CGST Rules, 2017. No pre-decisional hearing was granted to the appellants before blocking the ECL. The appellants challenged these orders before the Single Judge by way of writ petitions, which were disposed of rejecting the appellants' contentions. Aggrieved, the appellants filed the present intra-court writ appeals before the Division Bench.

Court Observations (Verbatim / Near-Verbatim)

On Pre-Decisional Hearing (Point No. 1):

"Though Rule 86A does not expressly/specifically provide for adherence to principles of natural justice, the same would necessarily have to be read into Rule 86A and complied with while invoking the said provision."

"When the ECL of the appellants was sought to be blocked and such credit cannot be utilised for upto 1 year, the said blocking would entail and result in serious civil consequences for the appellants warranting compliance with the principles of natural justice and providing an opportunity of hearing to the appellants."

"Ordinarily, a post-decisional hearing is not a substitute for pre-decisional hearing and that pre-decisional hearing is important especially when the respondents-revenue passed the impugned orders which would entail and visit the appellants with serious civil consequences."

"It was not physically possible for the appellants to immediately/forthwith encash/withdraw the ITC available in its ECL so as to warrant emergent/urgent blocking of the ECL without providing a pre-decisional hearing to the appellants."

"Respondents-revenue committed a grave and serious error/illegality/infirmity in not providing/granting a pre-decisional hearing to the Appellant before passing the impugned order blocking its Electronic Credit Ledger under Rule 86A of the CGST Rules."

On 'Reasons to Believe' and Independent Application of Mind (Point No. 2):

"Rule 86A, which in effect is the power to block ECL is drastic in nature which creates a disability for the taxpayer to avail of the credit in ECL for discharge of his tax liability which he is otherwise entitled to avail and therefore, all the requirements of Rule 86A would have to be fully complied with before the power thereunder is exercised; when this Rule requires arriving at a subjective satisfaction which is evident from the use of words, 'must have reasons to believe', the satisfaction must be reached on the basis of some objective material available before the authority and cannot be made on the flights of ones fancies or whims or caprices."

"The electronic credit ledgers have been blocked solely on the basis of communication from another officer [Field visit report by the Asst. State Tax Officer, Vasco-D-Gama, (Goa)]. There was no tangible material to form any belief that the ITC lying in the appellants' ECL was on account of any fake invoice; it had proceeded to take action solely on the basis of a direction issued by another authority."

"The impugned orders have been passed based on the communication received from other officers, without any independent application of mind. This shows that exercise of power under Rule 86A was not because he was independently satisfied about the need for blocking the ECL but, was due to the fact that he felt compelled to obey the command of another officer."

"The impugned order discloses that the same has been passed mechanically and is based on borrowed satisfaction and does not meet the test of formation of an opinion... the impugned orders are bald, vague, cryptic, laconic, unreasoned and non-speaking and deserve to be set aside."

"It is quite possible that the transaction, when entered into in 2017 or 2018 could be genuine and when the officer visits in 2020 or 2021, the business could have been closed and therefore the mere closure of business in 2020 or 2021 cannot be a basis for denying credit availed earlier."

"A bonafide purchaser cannot be denied ITC on account of a supplier's default and the recipient

cannot be made to suffer denial of ITC for the wrong doings of the supplier."

Final Verdict

All six writ appeals were allowed. The common order of the Single Judge dated 27.07.2023 and all the ECL blocking orders dated 27.06.2023 / 02.06.2023 were set aside and quashed. □

ADDITIONAL FOOTNOTES

Cases Referred / Citation of Cases

Sr.	Case Name	Citation
1	Samay Alloys India (P) Ltd. vs. State of Gujarat	(2022) SCC OnLine Guj 2595
2	C.B. Gautam vs. Union of India	1992 (65) Taxman 440 (SC)
3	Sahara India (Firm) vs. Commissioner of Income Tax	2008 (226) ELT 22 (SC)
4	K.I. Shepherd vs. Union of India	(1987) 4 SCC 431
5	H.L. Trehan vs. Union of India	(1989) 1 SCC 764
6	Xiaomi Technology India (P) Ltd. vs. DCIT	2022 (145) Taxman.com 501 (Kar)
7	State Bank of Patiala vs. S.K. Sharma	(1996) 3 SCC 364
8	Canara Bank vs. Devasis Das	(2003) 4 SCC 557
9	New Nalbandh Trader vs. State of Gujarat	2022 (66) GSTL 334 (Guj)
10	Rajanandini Metal Ltd. vs. Union of India	2022 (64) GSTL 301 (P&H)
11	Parity Infotech Solutions (P) Ltd. vs. Govt. of NCT of Delhi	2023 (151) Taxman.com 349 (Del)
12	Dee Vee Project Ltd. vs. Government of Maharashtra	2022 (135) Taxman.com 189 (Bom)
13	LGW Industries Ltd. vs. Union of India	WPA No. 23512/2019 (Cal)
14	Suncraft Energy Pvt. Ltd. vs. AC-State Tax	2023 (9) Centax 48 (Cal)
15	M/s. DY Beathel Enterprises vs. State Tax Officer	2022 (58) GSTL 269 (Mad)
16	Sanchita Kundu vs. Asst. Commissioner of State Tax	2022 (63) GSTL 413 (Cal)
17	Bright State Plastic Industries vs. Addl. Commr. of Sales Tax	2022 (57) GSTL 226 (Ori)
18	Arhaan Ferrous and Non-Ferrous Solutions (P) Ltd. vs. DAC-1 (ST)	2023 (9) Centax 171 (AP)
19	On Quest Merchandising India Pvt. Ltd. vs. Govt. of NCT of Delhi	(2018) 10 GSTL 182 (Del)
20	Eicher Motors vs. Union of India	1999 (106) ELT 3 (SC)

Sr.	Case Name	Citation
21	Collector of Central Excise vs. Dai Inchi Karkaria Ltd.	1999 (112) ELT 353 (SC)
22	CBIC Circular No. CBEC-20/16/05/2021-GST/1552	Dated 02.11.2021

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