National Plasto Moulding The State of Assam & Ors.

Constitutional validity of Sections 16(2)(c) and 16(2)(d) of the Central Goods and Services Tax Act, 2017 and the Assam Goods and Services Tax Act, 2017 — whether Input Tax Credit (ITC) can be denied to a bona fide purchasing dealer on account of the fa

Date of Order: August 5, 2024
Case Law No: GIB-GHC-2024-14
Source: GST INDIA Biz (www.gstindia.biz)

CASE DESCRIPTION / SUMMARY

Background

A batch of writ petitions was filed by multiple registered dealers before the Gauhati High Court challenging the constitutional validity of Sections 16(2)(c) and 16(2)(d) of the CGST Act, 2017 and the Assam GST Act, 2017, along with show cause notices issued to the petitioners. The core grievance in all the petitions was common — the Department sought to deny ITC to purchasing dealers on the ground that their respective selling dealers had failed to deposit the tax collected from them into the Government Treasury, despite the purchasing dealers having entered into genuine and bona fide transactions supported by valid tax invoices issued by validly registered selling dealers.

Facts

The petitioners, being registered dealers, had purchased goods from registered selling dealers who had issued tax invoices in accordance with the provisions of the GST law. The purchasing dealers had duly paid the tax component to the selling dealers as part of their purchase transactions. However, the selling dealers failed to deposit the said tax into the Government Treasury. On this basis, the Department issued show cause notices to the purchasing dealers proposing to deny ITC claimed by them. The petitioners challenged both the constitutional validity of Sections 16(2)(c) and 16(2)(d) of the CGST Act, 2017 and the Assam GST Act, 2017, as well as the show cause notices and consequential orders issued thereunder. The senior counsel for the petitioners submitted that the controversy was squarely covered by the judgment of the Delhi High Court in On Quest Merchandising India Private Limited v. Government of NCT of Delhi & Ors. (2017 SCC OnLine Del

11286), wherein it was held that a purchasing dealer cannot be punished for the act of the selling dealer who failed to deposit tax collected. The respondents' counsel could not dispute that the controversy was covered by the said Delhi High Court judgment.

Court Observations (Verbatim — Crucial Extracts)

Delhi High Court in On Quest Merchandising India Private Limited v. Government of NCT of Delhi & Ors. (as quoted and adopted by the Gauhati High Court):

"*Applying the law explained in the above decisions, it can be safely concluded in the present case that there is a singular failure by the Legislature to make a distinction between purchasing dealers who have bona fide transacted with the selling dealer by taking all precautions as required by the DVAT Act and those that have not. Therefore, there was need to restrict the denial of ITC only to the selling dealers who had failed to deposit the tax collected by them and not punish bona fide purchasing dealers. The latter cannot be expected to do the impossible. It is trite that a law that is not capable of honest compliance will fail in achieving its objective. If it seeks to visit disobedience with disproportionate consequences to a bona fide purchasing dealer, it will become vulnerable to invalidation on the touchstone of Article 14 of the Constitution.*" — Para 39

"*The court respectfully concurs with the above analysis and holds that in the present case, the purchasing dealer is being asked to do the impossible, i.e., to anticipate the selling dealer who will not deposit with the Government the tax collected by him from those purchasing dealers and therefore avoid transacting with such selling dealers. Alternatively, what section 9(2)(g) of the DVAT Act requires the purchasing dealer to do is that after transacting with the selling dealer, somehow ensure that the selling dealer does in fact deposit the tax collected from the purchasing dealer and if the selling dealer fails to do so, undergo the risk of being denied the ITC. Indeed section 9(2)(g) of the DVAT Act places an onerous burden on a bona fide purchasing dealer.*" — Para 41

"*The court hereby holds that the expression 'dealer or class of dealers' occurring in section 9(2)(g) of the DVAT Act should be interpreted as not including a purchasing dealer who has bona fide entered into purchase transactions with validly registered selling dealers who have issued tax invoices in accordance with section 50 of the Act where there is no mismatch of the transactions in Annexures 2A and 2B. Unless the expression 'dealer or class of dealers' in section 9(2)(g) is 'read down' in the above manner, the entire provision would have to be held to be violative of Article 14 of the Constitution.*" — Para 53

"*The result of such reading down would be that the Department is precluded from invoking section 9(2)(g) of the DVAT to deny ITC to a purchasing dealer who has bona fide entered into a purchase transaction with a registered selling dealer who has issued a tax invoice reflecting the TIN number.*

In the event that the selling dealer has failed to deposit the tax collected by him from the purchasing dealer, the remedy for the Department would be to proceed against the defaulting selling dealer to recover such tax and not deny the purchasing dealer the ITC. Where, however, the Department is able to come across material to show that the purchasing dealer and the selling dealer acted in collusion then the Department can proceed under section 40A of the DVAT Act." — Para 54

Supreme Court Order on SLP (as quoted by the Gauhati High Court):

"*On hearing learned Additional Solicitor General appearing for the petitioner, we are not inclined to interfere with the impugned order. The special leave petition is dismissed.*"

Gauhati High Court's Own Conclusion:

"*Having gone through the above referred judgments, we are of the view that the controversy raised in this batch of writ petitions is squarely covered by the decision of the Delhi High Court in the case of On Quest Merchandising India Private Limited (supra). Hence, the show cause notices impugned in the present writ petitions and the consequential orders are set aside. However, the Department is free to act in those cases, where the purchase transactions are not bona fide, in accordance with law.*"

Final Verdict

The Gauhati High Court disposed of the batch of writ petitions by setting aside all show cause notices and consequential orders issued to the purchasing dealers. It was held that the controversy was squarely covered by the Delhi High Court judgment in On Quest Merchandising (supra) affirmed by the Supreme Court, and that ITC cannot be denied to bona fide purchasing dealers for the default of the selling dealer in depositing tax. However, the Department was expressly granted liberty to proceed against those purchasing dealers where the purchase transactions are found to be not bona fide.

ADDITIONAL FOOTNOTES

Cases Referred by the Court

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#	Case Name	Citation
1	On Quest Merchandising India Private Limited v. Government of NCT of Delhi & Ors.	2017 SCC OnLine Del 11286
2	SLP against On Quest Merchandising (dismissed by Supreme Court)	SLP No. 36750/2017, dismissed on January 10, 2018

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