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Supreme Court Takes Up Constitutional Validity of Section 16(2)(c) in Bona Fide Recipient ITC

Dispute

The Hon'ble Supreme Court in *M/s Prime Metals v. Central Board of Indirect Taxes and Customs & Ors. [Special Leave Petition (C) No. 18577 of 2026 dated May 22, 2026]* heard the submissions of the petitioner's counsel, directed that a copy of the petition be furnished to the learned Additional Solicitor General appearing for the Union of India and to the learned counsel for the State of Rajasthan, and listed the matter for further hearing on May 29, 2026, in a challenge to the order of the Hon'ble Rajasthan High Court relegating the petitioner to the statutory appellate remedy. The petitioner has pressed before the Apex Court that Section 16(2)(c) of the Central Goods and Services Tax Act, 2017 ("**the CGST Act**"), if read literally, compels an assessee to perform an impossible act, since the recipient of supply has no control over whether the supplier discharges the tax to the Government, and that denial of Input Tax Credit ("**ITC**") on this ground to a bona fide recipient — particularly where the immediate supplier had in fact paid the tax — cannot be sustained.

Facts:

M/s Prime Metals ("**the Petitioner**") is a registered person under the CGST Act / Rajasthan Goods and Services Tax Act, 2017 ("**the RGST Act**"), engaged through its unit at Matsya Industrial Area, Alwar, Rajasthan. The Petitioner availed ITC on inward supplies received from its suppliers.

A Show Cause Notice dated June 25, 2025 ("**the SCN**") was issued to the Petitioner proposing denial/reversal of ITC, which culminated in the Order-in-Original dated December 17, 2025 ("**the Impugned Order**") passed by the adjudicating authority confirming the demand. The substratum of the proceedings was that although the Petitioner's immediate/preceding supplier had actually paid tax to the Government, the supplier one step removed in the chain had allegedly either not paid the tax or was a fake entity.

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Aggrieved, the Petitioner approached the Hon'ble Rajasthan High Court by way of ***D.B. Civil Writ Petition No. 3729 of 2026***, inter alia praying that (a) Circular No. 3/3/2017-GST issued by the Central Board of Indirect Taxes and Customs be quashed as being without authority of law; (b) Section 16(2)(c) of the CGST Act / RGST Act be declared ultra vires the Constitution of India; and (c) the SCN dated June 25, 2025 and the Order-in-Original dated December 17, 2025 be quashed and set aside.

The Petitioner contended before the High Court that no opportunity of cross-examination of the witnesses/material relied upon was afforded, and that Section 16(2)(c) of the CGST Act could not be sustained insofar as it visits a bona fide recipient with the consequences of supplier-side default beyond the immediate supplier.

The Revenue opposed the writ petition on the ground that the Petitioner had an efficacious alternative remedy of appeal under Section 107 of the CGST Act before the appellate authority, and placed reliance on (i) the order of the Hon'ble Supreme Court in ***M/s Trillion Lead Factory Private Ltd. v. Superintendent of Central Tax [Special Leave Petition (C) No. 7101 of 2026 dated February 27, 2026]*** reiterating that ordinarily no writ lies against a show cause notice; and (ii) the Division Bench judgment of the Hon'ble Rajasthan High Court in ***Tanushree Logistics Private Limited v. State of Rajasthan [D.B. Civil Writ Petition No. 17550 of 2022 dated December 07, 2022]***, which had upheld the alternative remedy objection in the GST appellate scheme.

By order dated April 29, 2026, the Hon'ble Rajasthan High Court declined to interfere, dismissed the writ petition holding that the Petitioner has a statutory alternative remedy of appeal under Section 107(1) of the CGST Act, and granted liberty to the Petitioner to raise all grounds, legal and factual, before the appellate authority. The challenge to the vires of Section 16(2)(c) was not adjudicated on merits.

It is in these circumstances that the Petitioner approached the Hon'ble Supreme Court by way of the present Special Leave Petition.

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Petitioner's Contentions before the Hon'ble Supreme Court:

- That the Hon'ble High Court erred in relegating the Petitioner to the alternative remedy of appeal, notwithstanding that the prayer clause of the writ petition specifically put in issue the constitutional validity of Section 16(2)(c) of the CGST Act, which the appellate authority has no jurisdiction to adjudicate;
- That Section 16(2)(c) of the CGST Act, if read literally, mandates the recipient to perform an impossible act, since the entitlement to ITC is made dependent upon the supplier having "actually paid" the tax to the Government, either in cash or through utilisation of admissible ITC — a matter wholly outside the recipient's control;
- That in the present case the immediate/preceding supplier had, undisputedly, actually paid the tax to the Government, and the only allegation is that the supplier one step removed in the chain either did not pay tax or was allegedly a fake entity; such an allegation against a supplier one removed cannot operate to the prejudice of the Petitioner-recipient; and
- That denial of ITC on this ground, in the absence of any allegation of fraud, collusion or connivance against the Petitioner, is contrary to the constitutional guarantees under Articles 14, 19(1)(g), 265 and 300A of the Constitution of India.

Issue:

Whether the Hon'ble Rajasthan High Court was justified in relegating the Petitioner to the statutory alternative remedy of appeal under Section 107 of the CGST Act without adjudicating the constitutional challenge to Section 16(2)(c) of the CGST Act, where a bona fide recipient is denied ITC on account of an alleged default by a supplier one step removed in the chain, despite tax having been paid to the immediate/preceding supplier?

Held:

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The Hon'ble Supreme Court in *Special Leave Petition (C) No. 18577 of 2026* held as under:

- **Noted that**, the order impugned before it was the order dated April 29, 2026 of the Hon'ble Rajasthan High Court in *D.B. Civil Writ Petition No. 3729 of 2026*, by which the writ petition was dismissed on the ground of availability of statutory alternative remedy under Section 107 of the CGST Act.
- **Observed that**, the Petitioner contended that the Hon'ble High Court erred in relegating it to the alternative remedy, since the prayer clause of the writ petition had also put in issue the validity of Section 16(2) of the CGST Act, which goes beyond the jurisdiction of the appellate authority.
- **Further observed that**, according to the Petitioner, Section 16(2)(c) of the CGST Act, if understood literally, mandates the assessee to do an impossible act, inasmuch as ITC can be availed only if the supplier has actually paid the tax to the Government either in cash or through utilisation of admissible ITC, and what happens at the supplier's end is not within the recipient's control.
- **Recorded that**, in the present case there was no dispute that the immediate/preceding supplier had actually paid the tax, and the allegation was that the supplier one removed in the chain either did not pay or was allegedly a fake entity, and that this cannot operate to the prejudice of the assessee.
- **Directed that**, a copy of the petition be furnished to the learned Additional Solicitor General appearing for the Union of India and to the learned counsel for the State of Rajasthan.
- **Listed the matter for further hearing on May 29, 2026.**

Our Comments:

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Relevant Provision — Section 16(2)(c) of the CGST Act, 2017:

Section 16(1) of the CGST Act embodies the eligibility principle that every registered person is, subject to such conditions and restrictions as may be prescribed and in the manner specified in Section 49, entitled to take credit of input tax charged on supplies used or intended to be used in the course or furtherance of business. Section 16(2) opens with a non-obstante clause and prescribes cumulative conditions for availment of ITC, namely — (a) possession of a tax invoice or debit note; (aa) furnishing of details of such invoice/debit note by the supplier and communication thereof to the recipient under Section 37; (b) actual receipt of goods or services; (ba) the ITC communicated under Section 38 not being restricted; (c) the tax charged in respect of such supply having been actually paid to the Government, either in cash or through utilisation of admissible ITC; and (d) furnishing of the return under Section 39.

The vice in clause (c) lies in the fact that whereas the recipient can control invoice possession, receipt of goods or services, payment of consideration with tax to the supplier, and its own return compliance, it has no statutory, contractual or factual mechanism to ensure that the supplier ultimately discharges the tax through cash or through admissible credit. The framework of Section 41 read with Rule 37A (inserted w.e.f. December 26, 2022) provides a calibrated mechanism of temporary reversal and re-availment where the supplier reports outward supply in GSTR-1 but does not furnish GSTR-3B by September 30 following the financial year. The constitutional question is whether the literal application of Section 16(2)(c) to a bona fide recipient, in the absence of collusion, satisfies the touchstone of Articles 14, 19(1)(g), 265 and 300A.

Background — The Rajasthan High Court Order in Prime Metals:

The Hon'ble Rajasthan High Court, by order dated April 29, 2026, declined to entertain the writ petition on the ground of availability of the statutory remedy of appeal under Section 107 of the CGST Act, following the order of the Hon'ble Supreme Court in ***M/s Trillion Lead Factory Private Ltd. v. Superintendent of Central Tax [SLP (C) No. 7101 of 2026 dated February 27,***

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2026] — wherein it was reiterated that no writ ordinarily lies against an issuance of show cause notice — and the Division Bench in *Tanushree Logistics Private Limited v. State of Rajasthan [D.B. Civil Writ Petition No. 17550 of 2022 dated December 07, 2022]*. In Tanushree Logistics, the Division Bench, after surveying *Assistant Commissioner of State Tax v. Commercial Steel Limited [2021 SCC OnLine SC 884]*, *State of Maharashtra v. Greatship (India) Limited [2022 SCC OnLine SC 1262]* and *State of Madhya Pradesh v. Commercial Engineers and Body Building Company Limited [2022 SCC OnLine SC 1425]*, had held that a writ under Article 226 against an order of assessment in a fiscal matter is ordinarily not entertainable save for breach of fundamental rights, violation of natural justice, excess of jurisdiction or a challenge to the vires of the statute.

Significantly, the Petitioner's writ petition in Prime Metals specifically incorporated a challenge to the vires of Section 16(2)(c) of the CGST Act — a head of jurisdiction which the appellate authority under Section 107 cannot exercise. The Hon'ble Supreme Court has prima facie taken note of this distinction, and the listing of the matter and the direction to furnish a copy of the petition to the ASG and State counsel on May 22, 2026 indicates that the constitutional dimension of Section 16(2)(c) requires substantive examination.

Pari Materia Judgments — Pro-Taxpayer Line:

The pro-taxpayer line traces its doctrinal foundation to *On Quest Merchandising India Pvt. Ltd. v. Government of NCT of Delhi [(2018) 56 GSTR 177 (Delhi); 2017 SCC OnLine Del 11286 dated October 26, 2017]*, where the Hon'ble Delhi High Court read down Section 9(2)(g) of the DVAT Act so as to exclude bona fide purchasing dealers, holding that “as long as the purchasing dealer has taken all these steps, he cannot be expected to keep track of whether the selling dealer has in fact deposited the tax collected with the Government.” The Special Leave Petition against the said decision was dismissed by the Hon'ble Supreme Court in *Commissioner of Trade and Taxes Delhi v. Arise India Limited [SLP (C) No. 36750 of 2017 dated January 10, 2018]*, and the underlying principle was further reinforced in *Commissioner, Trade and Tax,*

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Delhi v. Shanti Kiran India (P) Ltd. [Civil Appeal No. 9902 of 2017 dated October 09, 2025], where the Hon'ble Supreme Court affirmed grant of ITC to bona fide purchasing dealers where the selling dealer was registered at the time of transaction and the genuineness of invoices was not disputed.

In the CENVAT regime, the Hon'ble Supreme Court in *Commissioner of Central Excise, Jalandhar v. Kay Kay Industries [2013 (8) TMI 772 (SC) dated August 26, 2013]* protected the recipient where the goods were received under duty-paid documents and no collusion was shown. Under the GST regime, the Hon'ble Madras High Court in *D.Y. Beathel Enterprises v. State Tax Officer (Data Cell) [2022 (58) G.S.T.L. 269 (Mad.) dated February 24, 2021]* remanded the matter holding that the Department must first proceed against the defaulting supplier; the Hon'ble Calcutta High Court in *Suncraft Energy Private Limited v. Assistant Commissioner, State Tax, Ballygunge Charge [MAT 1218 of 2023 dated August 02, 2023]* held that absent collusion, ITC cannot be denied to a bona fide recipient merely for non-reflection in GSTR-2A; the Hon'ble Allahabad High Court in *R.T. Infotech v. Additional Commissioner, Grade-2 [Writ Tax No. 928 of 2024 dated December 16, 2024]* held that a purchasing dealer cannot be left at the mercy of a selling dealer who fails to file returns or deposit tax; and the Hon'ble Gauhati High Court in *National Plasto Moulding v. State of Assam [(2024) 8 TMI 836 = 2024 (89) G.S.T.L. 82 (Gau.)]* read down Section 16(2)(c) for bona fide purchasers. This pro-taxpayer line was most recently affirmed by the Hon'ble Tripura High Court in *Sahil Enterprises v. Union of India [W.P.(C) No. 688 of 2022 dated January 06, 2026]* and the Hon'ble Karnataka High Court in *Instakart Services Private Limited v. Union of India [W.P. No. 4917 of 2021 dated February 09, 2026]*, both reading down Section 16(2)(c) (and Rule 36(4), in Instakart) to save bona fide recipients.

Contrary Judgments — Pro-Revenue Line:

The contrary line draws upon *Mahalaxmi Cotton Ginning Pressing and Oil Industries v. State of Maharashtra [2012 SCC OnLine Bom 733 dated May 11, 2012]*, where the Hon'ble Bombay

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High Court, under the MVAT regime, held that the words “actually paid” meant factual deposit into the treasury, and ***State of Karnataka v. Ecom Gill Coffee Trading Private Limited [(2023) 18 SCC 809 dated March 13, 2023]***, where the Hon’ble Supreme Court held that the burden under the KVAT Act lay on the dealer claiming ITC to establish actual movement and receipt of goods through corroborative evidence. Under the GST regime, this strict view was adopted by the Hon’ble Andhra Pradesh High Court in ***Thirumalakonda Plywoods v. Assistant Commissioner [2023 SCC OnLine AP 1476 dated July 18, 2023]***, the Hon’ble Patna High Court in ***Aastha Enterprises v. State of Bihar [2023 SCC OnLine Pat 4395 dated August 18, 2023]*** (holding that payment to the supplier is a private contractual act and not equivalent to payment to the exchequer), the Hon’ble Kerala High Court in ***Nahasshukoor v. Assistant Commissioner [2023 SCC OnLine Ker 11369]*** and ***M. Trade Links v. Union of India [2024 SCC OnLine Ker 2744 dated June 04, 2024]***, the Hon’ble Madhya Pradesh High Court in ***Shree Krishna Chemicals v. Union of India [2025 SCC OnLine MP 1301]***, the Hon’ble Madras High Court in ***Baby Marine Eastern Exports v. Union of India [2025 SCC OnLine Mad 15588]***, and most recently, the Hon’ble Gujarat High Court in ***Maruti Enterprise through its Authorised Partner Jigneshbhai Bharatbhai Tarpara v. Union of India [R/Special Civil Application No. 18080 of 2023 and batch dated May 01, 2026]***, which upheld the constitutional validity of Section 16(2)(c), declined to read it down, and expressly distinguished the DVAT framework, holding that actual payment of tax by the supplier is an intrinsic statutory condition for ITC.

Concluding Comments:

The Hon'ble Supreme Court's decision to hear the matter, record the petitioner's submissions, and list Prime Metals for further hearing on May 29, 2026 is a significant development. The conflict between the High Courts is now sharp — the Hon’ble Tripura, Gauhati and Karnataka High Courts have adopted the reading down approach for bona fide recipients, whereas the Hon’ble Gujarat, Andhra Pradesh, Kerala, Patna, Madhya Pradesh and Madras High Courts have upheld a stricter statutory approach. The Apex Court’s prima facie observation that supplier-side default at a stage one removed in the chain “cannot operate to the prejudice of

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the assessee”, particularly where the immediate supplier has paid tax, lends weight to the constitutional argument grounded in *lex non cogit ad impossibilia* and the principle that bona fide recipients ought not be made guarantors of supplier compliance. The matter, listed for further hearing on May 29, 2026, may well provide the long-awaited authoritative resolution of the divergence among the High Courts on Section 16(2)(c).

Until the Hon’ble Supreme Court delivers a definitive ruling, taxpayers are well advised to preserve a robust documentary trail, including valid tax invoices containing supplier GSTIN, e-way bills, lorry receipts, delivery challans, weighment slips, stock and consumption registers, banking proofs of payment of value plus GST, downloaded copies of GSTR-2A/2B at the relevant time, supplier registration screenshots and contractual indemnities, so as to be in a position to discharge the burden of bona fides as enunciated in *Ecom Gill Coffee*, while simultaneously preserving the right to invoke the constitutional protections recognised by the pro-taxpayer line of authorities. Where notices are issued, taxpayers should insist that the Department first proceed against the defaulting supplier and demonstrate that recovery from the supplier has been duly attempted before fastening liability on the recipient.

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(Author can be reached at info@a2ztaxcorp.com)

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