Big Relief ITC Cannot Be Denied to a Bona Fide Purchaser Merely Because the Supplier's Registration Cancelled Retrospectively

The Hon'ble Supreme Court in ***Additional Commissioner Grade 2 & Anr. v. M/s Safecon Lifescience Private Limited [SLP (C) No. 23993 of 2026 dated July 17, 2026]*** dismissed the Special Leave Petition filed by the Revenue against the judgment of the Hon'ble Allahabad High Court in ***M/s Safecon Lifescience Private Limited v. Additional Commissioner Grade 2 and Another [Writ Tax No. 389 of 2023 dated September 09, 2025]***, thereby affirming that proceedings under Section 74 of the Uttar Pradesh Goods and Services Tax Act, 2017 (**"the UPGST Act"**) cannot be initiated to deny Input Tax Credit (**"ITC"**) to a bona fide purchaser who has duly established the genuineness of the transaction through tax invoices, e-way bills, transport documents, payment through banking channels and filing of returns, merely on the ground that the registration of the supplier was subsequently cancelled or that irregularities were alleged in the supplier's own upstream purchases, in the absence of any finding of fraud, wilful misstatement or suppression of facts to evade tax on the part of the recipient.

Facts:

M/s Safecon Lifescience Private Limited (**"the Petitioner"**) is engaged in the business of trading and manufacturing of medicines/pharma products on a wholesale basis. The Petitioner purchased medicines/pharma products from M/s Unimax Pharma Chem, Bhiwandi, Thane (**"the Supplier"**) for the tax period April 2021 against Tax Invoice dated April 30, 2021, duly supported by e-way bill and transport bilty of M/s Vinay Road Lines Pvt. Ltd. At the time of supply, the Supplier was in existence and duly registered with the GST Department and was also a drug license holder. The entire payment towards the purchases was made through banking channels, and the Supplier had filed its Form GSTR-1 and Form GSTR-3B within time on the GST portal after discharging due tax on its turnover.

On the basis of information received from the office of the Pr. Chief Commissioner, Central Intelligence Unit, Central Excise & Central Tax, Vadodara Zone, the Deputy Commissioner, Commercial Tax, Agra (**"the Adjudicating Authority"**) issued a Show Cause Notice under Section 74 of the UPGST Act alleging that the Petitioner had incorrectly claimed ITC through Form GSTR-3B for the tax period April 2021 on purchases made from the Supplier, which had subsequently got its registration cancelled. The detailed reply filed by the Petitioner was rejected, and a demand was confirmed vide Order dated January 12, 2022 (**"the Adjudication Order"**) on the ground that, in terms of Section 16(2)(c) of the UPGST Act, the recipient can claim ITC only when the supplier has deposited the collected tax with the Government.

The appeal preferred by the Petitioner was also dismissed by the Additional Commissioner, Grade-2 (Appeal)-II, State Tax, Agra (**"the Appellate Authority"**) vide Order dated December 20, 2022 (**"the Impugned Order"**) on the ground that the Supplier had, in the month of March 2021, made purchases from firms which did not deposit tax on their sales, and therefore, the Supplier itself had claimed forged ITC, disentitling the Petitioner from claiming ITC on supplies received from the Supplier.

Aggrieved thereby, the Petitioner filed a writ petition before the Hon'ble Allahabad High Court, which allowed the writ petition and quashed both the orders. The Revenue thereafter assailed the said judgment before the Hon'ble Supreme Court by way of a Special Leave Petition.

<u>Issue:</u>

Whether proceedings under Section 74 of the UPGST Act can be initiated to deny ITC to a bona fide recipient, who has established actual movement of goods and payment of tax through banking channels, merely because the supplier's registration was subsequently cancelled and on the basis of unverified intelligence inputs, without any finding of fraud, wilful misstatement or suppression of facts to evade tax on the part of the recipient?

<u>Held:</u>

The Hon'ble Allahabad High Court in ***Writ Tax No. 389 of 2023 dated September 09, 2025*** held as under:

Observed that, the Petitioner had brought on record all the materials evidencing actual movement of goods, payment through banking channels and filing of returns, which were duly reflected in Form GSTR-3B of both the Petitioner and the Supplier on the portal showing payment of tax; these vital materials were neither disbelieved nor reversed, nor was any cogent material rebutting the same brought on record at any stage. Once actual movement of goods as well as payment of tax stood proved and unrebutted, proceedings under Section 74 of the UPGST Act could not be justified.

Noted that, the Impugned Order was passed "with closed eyes" solely on the basis of the information sent by the Central Intelligence Unit, Vadodara Zone; such information must be verified by the authority before being used against a registered dealer. Further, neither the report nor the material used against the Petitioner was ever provided to it, which ought to have been provided.

Further noted that, no finding was recorded at any stage that the Supplier, who sold the goods in question to the Petitioner, was involved in any irregularity. Relying upon the CBIC Circular dated December 13, 2023, it was reiterated that proceedings under Section 74 can be initiated only where there is fraud or wilful misstatement or suppression of facts to evade payment of tax, and not otherwise, as also held by the Court in ***M/s Khurja Scrap Trading Company v. Additional Commissioner Grade 2 (Appeal) and Another [Writ Tax No. 743 of 2023] [2025:AHC:151783]***.

Observed that, in terms of the law laid down by the Hon'ble Supreme Court in ***Continental Foundation Joint Venture Holding v. Commissioner of Central Excise, Chandigarh-I [(2007) 10 SCC 337]*** in the context of the pari materia Section 11A of the Central Excise Act, 1944, mere omission to give correct information is not suppression of facts unless it was deliberate with intent to evade payment of duty, and an incorrect statement cannot be equated with a wilful misstatement, which implies making of an incorrect statement with the knowledge that it was not correct.

Held that, since the authorities had neither recorded any finding of fraud, nor of wilful misstatement, nor of suppression of facts to evade payment of tax, the proceedings under Section 74 of the UPGST Act ought not to have been initiated against the Petitioner. Accordingly, the Adjudication Order and the Impugned Order were quashed and the writ petition was allowed.

Now:

The Hon'ble Supreme Court, in ***SLP (C) No. 23993 of 2026 dated July 17, 2026***, dismissed the Special Leave Petition filed by the Revenue at the admission stage itself, observing that "we do not find any good ground to entertain this petition", thereby leaving the judgment of the Hon'ble Allahabad High Court undisturbed and allowing it to attain finality between the parties.

Our Comments:

Section 74 of the CGST Act/UPGST Act (**"Determination of tax not paid or short paid or erroneously refunded or input tax credit wrongly availed or utilised by reason of fraud or any wilful-misstatement or suppression of facts"**) can be invoked only when the ingredients of fraud, wilful misstatement or suppression of facts with intent to evade tax are present on the part of the taxpayer. This position stands clarified by the CBIC vide Instruction No. 05/2023-GST dated December 13, 2023, which categorically states that Section 74(1) cannot be invoked merely on account of non-payment of GST without the specific element of fraud, wilful misstatement or suppression, and that such evidence must form part of the Show Cause Notice itself. It is pertinent to note that for demands pertaining to FY 2024-25 onwards, Section 74A of the CGST Act, inserted vide the Finance (No. 2) Act, 2024, provides a common limitation period, though the intent-based ingredients continue to remain relevant for determining the quantum of penalty.

The present ruling addresses a recurring controversy under Section 16(2)(c) of the CGST Act, whereby the Department seeks to recover ITC from the recipient whenever the supplier defaults in payment of tax or its registration is subsequently cancelled. The judgment is in line with a consistent body of precedents. The Hon'ble Delhi High Court in ***On Quest Merchandising India Pvt. Ltd. v. Govt. of NCT of Delhi [W.P. (C) No. 6093 of 2017 dated October 26, 2017]*** read down the pari materia Section 9(2)(g) of the Delhi VAT Act to protect bona fide purchasers who had actually paid tax to the selling dealer, and the SLP filed by the Revenue thereagainst was dismissed by the Hon'ble Supreme Court. Similarly, the Hon'ble Madras High Court in ***D.Y. Beathel Enterprises v. State Tax Officer [W.P. (MD) No. 2127 of 2021 dated February 24, 2021]*** held that when the recipient has paid the tax to the supplier, recovery proceedings must first be initiated against the defaulting supplier. The Hon'ble Calcutta High Court in ***Suncraft Energy Pvt. Ltd. v. Assistant Commissioner of State Tax [MAT No. 1218 of 2023 dated August 02, 2023]***, against which the Revenue's SLP was also dismissed by the Hon'ble Supreme Court, held that ITC cannot be reversed in the hands of the recipient without any inquiry against the defaulting supplier. Further, in ***LGW Industries Ltd. v. Union of India [W.P.A. No. 23512 of 2019 dated December 13, 2021]*** and ***Gargo Traders v. Joint Commissioner, Commercial Taxes [W.P.A. No. 1009 of 2022 dated June 12, 2023]***, it was held that where the transactions were genuine and made prior to the cancellation of the supplier's registration, the benefit of ITC cannot be denied to the purchaser. The Hon'ble Allahabad High Court itself, in ***M/s Solvi Enterprises v. Additional Commissioner Grade 2 [Writ Tax No. 1287 of 2024 dated March 24, 2025]*** and ***M/s R.T. Infotech v. Additional Commissioner Grade 2 [Writ Tax No. 1330 of 2022 dated May 29, 2025]***, held that once the selling dealer was duly registered at the time of the transaction, no adverse inference can be drawn against the purchaser.

A note of caution, however, flows from the judgment of the Hon'ble Supreme Court in ***State of Karnataka v. Ecom Gill Coffee Trading Pvt. Ltd. [Civil Appeal No. 230 of 2023 dated March***

13, 2023], rendered in the context of Section 70 of the Karnataka VAT Act, wherein it was held that the burden of proving the genuineness of the transaction and actual physical movement of goods lies on the purchasing dealer, and mere production of tax invoices and proof of payment through banking channels is not sufficient. The present case is distinguishable precisely because the taxpayer discharged this burden in full – with tax invoices, e-way bills, transport bilty, banking channel payments and matching returns of both parties – and the Department failed to bring any material in rebuttal.

It is also relevant to note that dismissal of an SLP *in limine* without a reasoned order does not amount to a declaration of law under Article 141 of the Constitution, nor does the doctrine of merger apply, as held in ***Kunhayammed v. State of Kerala [(2000) 6 SCC 359]***. Nevertheless, with the Supreme Court declining to interfere, the Allahabad High Court's ruling stands undisturbed and would carry significant persuasive value in similar ITC disputes across the country. The key takeaway for the trade and industry is that robust contemporaneous documentation – tax invoices, e-way bills, transport documents, banking channel payments and reconciled returns – remains the strongest defence in ITC litigation, and the Department must establish the ingredients of fraud, wilful misstatement or suppression against the recipient itself, on the basis of verified and disclosed material, before invoking Section 74.

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