Genuine purchasers cannot be denied ITC or subjected to custodial interrogation for supplier's default absent prima facie collusion

The Hon'ble Karnataka High Court in ***Abdul Majid & Ors. v. The Assistant Commissioner of Commercial Taxes [Criminal Petition No. 9260 of 2026 c/w Criminal Petition No. 9244 of 2026 and Criminal Petition No. 9306 of 2026 dated August 05, 2026]*** granted anticipatory bail to three registered purchasers who were apprehending arrest under Section 132 of the Central Goods and Services Tax Act, 2017 (**"the CGST Act"**) on the allegation of availing bogus Input Tax Credit (**"ITC"**) from allegedly fictitious suppliers, and held that a purchaser who is in possession of tax invoices, has paid the invoice value along with GST to the supplier through banking channels and has periodically filed returns, cannot ordinarily be denied ITC or be subjected to custodial interrogation merely on account of supplier-side default, unless fraud or collusion with the supplier is *prima facie* established.

Facts:

Mr. Abdul Majid, Mr. Awaze T.M. and Mr. Mujaseem Ulla (**"the Petitioners"**) are the proprietors of M/s. ANZ Traders, M/s. AF Trading and M/s. ZMS Enterprises respectively, holding valid GST registrations for dealing in steel and old scrap materials. The Petitioners had purchased aluminium scrap material from M/s. KH E-Waste Recyclers and M/s. SKS Traders (**"the Suppliers"**).

The Revenue Department (**"the Respondent"**) conducted a raid on the business premises of the Suppliers and arrested their proprietors, alleging that the Suppliers were fictitious firms which had issued concocted invoices without any actual supply of goods, had availed ITC to the tune of approximately Rs. 231.70 crores and Rs. 567 crores respectively, and had returned part of the said amount to the Petitioners in cash through hawala transactions. Thereafter, summons under Section 70 of the CGST Act were issued to the Petitioners directing them to appear with supportive documents relating to the purchases.

Apprehending arrest in proceedings under Section 132(1) of the CGST Act and the Karnataka Goods and Services Tax Act, 2017 (**"the KGST Act"**), the Petitioners filed anticipatory bail applications before the jurisdictional Sessions Court, which were dismissed on June 19, 2026. Hence, the Petitioners approached the Hon'ble High Court under Section 482 of the Bharatiya Nagarik Suraksha Sanhita, 2023.

The Petitioners contended that they hold valid GST registrations, are in possession of the tax invoices raised by the Suppliers, have paid the invoice value along with GST through bank transactions, have periodically filed their returns, appeared before the authorities on May 22, 2026 in response to the summons, have no antecedents and are ready and willing to co-operate with the investigation. It was further pointed out that the Suppliers themselves were granted regular bail by the Sessions Court on July 09, 2026, and that the alleged offence carries a maximum punishment of five years and is compoundable in nature.

Per contra, the Respondent contended that the Petitioners are involved in a large-scale organized economic offence of fraudulent availment and passing of bogus ITC running into hundreds of crores of rupees, that the arrested Suppliers had admitted their guilt, and that custodial interrogation of the Petitioners was necessary to unearth the involvement of other firms forming part of the wider racket.

Issue:

Whether a registered purchaser who is in possession of tax invoices, has paid the invoice value along with GST to the supplier through banking channels and has periodically filed returns, can be denied ITC or subjected to custodial interrogation and arrest under Section 69 read with Section 132 of the CGST Act merely on account of default committed by the supplier, in the absence of *prima facie* material establishing fraud or collusion?

Held:

The Hon'ble Karnataka High Court in ***Criminal Petition No. 9260 of 2026 c/w Criminal Petition No. 9244 of 2026 and Criminal Petition No. 9306 of 2026*** held as under:

- Observed that, a registered person is entitled to ITC only upon satisfaction of the conditions viz. possession of a tax invoice, actual receipt of goods or services, payment of tax charged under the invoice by the supplier, filing of returns along with the invoice, and payment of the invoice value plus tax within the prescribed period. In the present case, it was not in dispute that the Suppliers held valid registrations and were active on the dates of the transactions, and that the Petitioners had paid them the value of the invoices and GST through banking channels and had periodically filed their returns along with copies of the invoices.

- Observed that, it is trite that in such a case, ITC cannot be denied to the purchasers unless fraud and collusion is proved; the subsequent cancellation of the GST registration of the suppliers or their non-existence after the transactions is, by itself, not sufficient to deny the benefit of ITC to the purchasers, and unless exceptional circumstances are found, the recovery can be made only against the defaulting supplier.

- Noted that, actual receipt of goods and services can be established through documentary evidence such as e-way bills, transport vehicle receipts, weighbridge receipts, stock and sale records etc., which the Petitioners were ready and willing to produce; further, a reading of Section 132 of the CGST Act shows that the principal offender for the purposes of the said provision would be the supplier, who in the present case had already been granted regular bail.

- Noted that, in terms of the judgment of the Hon'ble Supreme Court in ***Radhika Agarwal v. Union of India [(2025) 6 SCC 545]***, an arrest under Section 69 of the CGST Act must proceed on the Commissioner's reasons to believe, duly recorded and supported by material evidence establishing that the conditions of Section 132(5) of the CGST Act are satisfied, and cannot be made merely to investigate whether such conditions are met; further, relying on ***Akram Pasha v. Senior Intelligence Officer, DGGI [2025 SCC OnLine Kar 30886],*** against which the Special Leave Petition was dismissed by the Hon'ble Supreme Court on March 25, 2026, custodial interrogation is not warranted merely because the alleged offence is an economic offence carrying imprisonment up to five years.

- Held that, in a genuine case where the purchaser has paid the invoice value and GST and has periodically submitted returns, he cannot be held liable or penalized for the default of the supplier except under exceptional circumstances, and denial of judicial protection in such a case would amount to injustice; where the only purpose is to ascertain actual receipt of goods or services, which can be proved by producing the necessary documents, custodial interrogation of the purchaser would not ordinarily be necessary unless there is some *prima facie* material to show his collusion with the supplier.
- Directed that, the Petitioners shall appear before the authorities on August 10, 2026, on which date the authorities shall be at liberty to take them into custody, if necessary, for the purpose of interrogation, but shall release them on the same day on or before 6:00 p.m., subject to each Petitioner executing a personal bond of Rs. 5,00,000/- with two sureties, co-operating with the investigation, not tampering with evidence or influencing witnesses, keeping their mobile phones operational, sharing their location and surrendering their passports, failing which the authorities would be at liberty to seek cancellation of the anticipatory bail.

Our Comments:

Section 69 of the CGST Act empowers the Commissioner to authorise arrest only where he has "reasons to believe" that a person has committed an offence specified in clauses (a) to (d) of Section 132(1) which is punishable under clause (i) or (ii) of Section 132(1) or Section 132(2) of the CGST Act. Section 132(1)(c) of the CGST Act penalises availment of ITC on invoices issued without any underlying supply, and by virtue of Section 132(5), such offences become cognizable and non-bailable only where the amount involved exceeds Rs. 500 lakhs. Correspondingly, Section 16(2)(c) of the CGST Act makes the recipient's ITC conditional upon actual payment of tax to the Government by the supplier, and it is precisely this condition that is invoked against purchasers whenever the supplier is later found to be non-existent or defaulting.

The present decision is a welcome reiteration of the settled principle that a bona fide purchaser cannot be visited with the consequences of the supplier's default. In ***On Quest Merchandising India Pvt. Ltd. v. Government of NCT of Delhi [2017 SCC OnLine Del 11286],*** the Hon'ble Delhi High Court read down a pari materia provision of the DVAT Act to protect bona fide purchasers, and the SLP against the said judgment was dismissed by the Hon'ble Supreme Court in *Arise India Ltd.* Similarly, in ***D.Y. Beathel Enterprises v. State Tax Officer [W.P. (MD) No. 2127 of 2021 dated February 24, 2021],*** the Hon'ble Madras High Court held that where the tax has been paid to the supplier, recovery proceedings must first be initiated against the defaulting supplier. The Hon'ble Calcutta High Court in ***LGW Industries Ltd. v. Union of India [W.P.A. No. 23512 of 2019 dated December 13, 2021], Sanchita Kundu v. Assistant Commissioner of State Tax [W.P.A. No. 7231 of 2022 dated May 05, 2022] and Gargo Traders v. Joint Commissioner, Commercial Taxes [W.P.A. No. 1009 of 2022 dated June 12, 2023]*** has consistently held that ITC cannot be denied to a purchaser whose transactions are genuine and supported by payments through banking channels merely because the supplier's registration was cancelled subsequently. Further, in ***Suncraft Energy Pvt. Ltd. v. Assistant Commissioner of State Tax [M.A.T. No. 1218 of 2023 dated August 02, 2023],*** the Hon'ble Calcutta High Court held that reversal of ITC from the recipient without first proceeding against the supplier is impermissible except in exceptional circumstances such as collusion, and the SLP against the said decision was dismissed by the Hon'ble Supreme Court.

At the same time, a note of caution flows from the contrary strand of jurisprudence. In ***State of Karnataka v. Ecom Gill Coffee Trading Pvt. Ltd. [Civil Appeal No. 230 of 2023 dated March 13, 2023],*** the Hon'ble Supreme Court, in the context of Section 70 of the KVAT Act, held that the burden of proving the genuineness of the transaction squarely lies on the purchaser, and mere production of invoices and proof of payment through banking channels is not sufficient; the purchaser must also establish the actual physical movement and receipt of goods. The present judgment itself acknowledges this dimension by emphasising e-way bills, transport receipts, weighbridge records and stock and sale records as the evidentiary foundation for actual receipt of goods. It may also be noted that the constitutional validity of Section 16(2)(c) of the CGST Act has recently been upheld by the Hon'ble Supreme Court, which makes the protective enforcement-level safeguards recognised in decisions such as the present one all the more significant for genuine taxpayers.

On the arrest front, the decision faithfully applies the safeguards laid down in ***Radhika Agarwal v. Union of India [(2025) 6 SCC 545],*** wherein the Hon'ble Supreme Court held that the power of arrest under Section 69 of the CGST Act cannot be exercised on mere suspicion or as a tool of investigation, and must be founded on the Commissioner's recorded reasons to believe supported by material evidence. Read with ***Siddharam Satlingappa Mhetre v. State of Maharashtra [(2011) 1 SCC 694],*** which mandates that custodial interrogation should be avoided where the accused has joined the investigation and is fully co-operating, the message for the field formations is clear: coercive action against recipients of supplies must be the exception, reserved for cases where *prima facie* material of collusion exists, and not the default response to supplier-side fraud.

For taxpayers, the practical takeaway is to maintain a robust documentary trail for every inward supply, viz. tax invoices, e-way bills, transport and weighbridge records, stock registers, and proof of payment of the invoice value along with GST through banking channels, since it is this evidentiary matrix that both protects the ITC claim and shields the purchaser from coercive action in cases of supplier default.

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