

Can Non-Compliance of Suppliers Lead to a Loss of ITC?

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Input Tax Credit ("ITC") is considered to be the backbone of the GST. The GST regime promised seamless credit on goods and services across the entire supply chain regime, which was not available in earlier indirect tax laws. The purpose was also to determine that the cascading effect is rationalized so that the commodities' prices may not vary from State to State. ITC plays a decisive role in determining the effective production cost and determining every business working capital requirement. ITC is whatever tax you pay for procuring inward goods and services to render outward supply in layman's language.

Section 16 of the Central Goods and Services Act, 2017, deals with Eligibility and Conditions for taking ITC. Conditions, in brief, to be fulfilled for a claim of the input tax credit are as follows:

- The recipient shall be in possession of the taxpaying document (Invoice, debit note, or others).
- The recipient shall have received such goods and services.
- Payment of tax shall be made by the supplier.
- The recipient shall furnish the return under section 39.

Thereby section 16(2)(c) states that Input Tax credit in respect of supply is available to the recipient only if tax charged on such supply has been deposited with the Government by the supplier. Several notices have already been issued to the supply recipients, stating that credits are not eligible as the supplier has not deposited the due taxes.

The department has all the powers to inspect the genuineness of a claim made by a taxpayer but denial of ITC merely because the supplier has not paid the tax collected from an honest buyer is unfair. We have discussed several cases whereby the tax officer was stopped from pursuing the matter with the purchasing dealer.

Althaf Shoes (P) Ltd. Vs. Asst. Comm. (CT) Valluvarkuttam, Chennai. (2012) 50 VST 179 (Mad.)

Hon'ble High Court of Madras held that The buyer need not verify whether the tax was paid or not. For non-payment of tax by the suppliers, the purchasers cannot be held responsible. In the name of verification, the issuing of a refund should not be delayed by the authorities concerned.

Gheru Lal Balchand Vs. State of Haryana (2011) 45 VST 195 P&H.

Hon'ble High Court of Punjab & Haryana held that No liability can be fastened on the purchasing registered dealer on account of non-payment of tax by the selling registered dealer in the treasury unless it is fraudulent, or collusion or connivance with the registered selling dealer or its predecessors with the purchasing registered dealer is established.

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In this case, there is no dispute that a declaration was given by a manufacturer indicating that the excise duty has been paid on the said inputs. The only allegation is that at the time of MODVAT verification, it was found that the supplier of the inputs had not discharged full duty liable for the period covered under the

invoices.

Hon'ble Supreme Court held that when there is a prescribed procedure and that has been duly followed by the manufacturer of the final product, we do not perceive any justifiable reason to hold that the buyer had not taken reasonable care while entering a transaction with the seller.

Shanti Kiran India Pvt. Ltd. Vs. Commissioner, Trade & Tax Department (2013) 57 VST 405 (Del. HC)

Delhi High Court gave the opinion that "in the absence of any mechanism enabling a purchasing dealer to verify if the selling dealer deposited tax, for the period in question, and in the absence of notification in a manner that can be ascertained in business that a dealer's registration is canceled (as has happened in this case) the benefit of input credit, under Section 9(1) cannot be denied."

Corporation Bank vs. Saraswati Abharansala (2009) 19 VST 84 (SC)

In the case at hand, the rate of tax for the purchase of Gold was revised from 1% to 0.50%, which was given a retrospective effect. The original notification on the subject provided that tax, 'if any tax collected at a higher rate, shall be paid over to the Government and tax, if any, paid over to the Government shall not be refunded.' It was contended that the amendment was brought into force with retrospective effect.

Honorable Supreme Court held that The statute should be held in a manner to do justice to the parties. Construction of statute which leads to confusion must be avoided. In case of a change in the rate of tax retrospectively, when sales tax was collected from the purchasing dealer and deposited, High Court gave direction to the State to make refund along with interest to the purchasing dealer. Neither the state nor the agent is entitled to collect tax at a rate higher than specified.

Suvasini Charitable Trust vs Government Of Nct Of Delhi & Anr. W.P.(C) 4086/2013 & CM No.9620/2013

SCT is a charitable trust organization registered under the DVAT Act. It avails ITC on the VAT paid on its sales. SCT states that it has made purchases from selling dealers registered under the DVAT Act on the strength of tax invoices which prove the collection of tax by the vendor from the purchasing dealer and is a valid document for availing ITC. A fire broke out in the premises of the one of selling dealers. It is stated that on account of said fire and destruction of records, the seller failed to deposit the VAT collected from its buyers, which included SCT. VATO issued a default assessment order invoking Section 9 (2) (g) of the DVAT Act. Section 9(2) (g) of the DVAT Act which states as under " to the dealers or class of dealers unless the tax paid by the purchasing dealer has actually been deposited by the selling dealer with the Government or has been lawfully adjusted against output tax liability and correctly reflected in the return filed for the respective tax period."

Hon'ble High Court held 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 where there is no mismatch of the transactions in Annexures 2A and 2B.

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.

Resultantly, the default assessment orders that create and affirm demands created against the petitioner purchasing dealers by invoking Section 9 (2) (g) of the DVAT Act for the default of the selling dealer, are hereby set aside.

Similar decision was also taken in case of On Quest Merchandising India Pvt. Ltd. Vs. Govt. of NCT of Delhi and ors. (Delhi HC) W.P. (C) No. 6093/2017 dated 26.10.2017.

Arise India Ltd & others Vs. Comm of Trade & Taxes, Delhi & others [[TS-314-HC-2017-\(Del\)-VAT](#)]

Section 9 (2) (g) requires the purchasing dealer to ensure, to claim ITC, that the selling dealer has deposited VAT with the Government or has lawfully adjusted it against such selling dealer's output tax liability.

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SLP was filed by the department against this case, which was rejected by hon'be Supreme court inter alia stating that "We are not inclined to interfere with the impugned order. The special leave petition is dismissed.

Khazanchand vs. State of Jammu & Kashmir (1984) 56 STC 214 (SC)

In the facts of the case, we have seen the tax due according to a quarterly return is to be paid by the dealer before filing such return and proof of payment of the tax so due is to accompany such return. The contention of the assessee had sold goods on credit and are not liable to pay quarterly tax until they have received the price of goods sold to them from their customers.

Honorable Supreme Court stated that it is clear from the Act the liability to pay sales tax is that of the dealer and not of the person who purchases goods from him, it is immaterial that the price of the goods is paid to him or is payable. When the liability to pay sales tax is cast by the statute on a dealer, he may pass on to its customer the amount of tax payable by him but he can only do so as a term of the contract of sale, but the purchaser is not bound to pay it to the vendor otherwise. The assessee is bound to pay the tax due before filing of return and the fact that their customer had not paid to them the sale price did not exempt them from their statutory liability.

Thereby in this case it was held that liability on selling dealer does not depend upon the tax payment by the purchasing dealer. Similarly we can stretch the argument to state that compliance by selling dealer should not impact the claim of ITC for purchasing dealers.

M/s. TVS Motor Company Ltd. Vs. State of Tamilnadu Civil Appeal No. (s) 10560 - 10564 of 2018 dated 12.10.2018

Hon'ble Supreme Court upheld Judgment of High Court and said where a dealer makes sales exclusively to the other State Government(s), the benefit of ITC would be allowed without insisting on the furnishing of Form 'C'. However, in order to avail this benefit, a certificate from said the State Government to whom the supplies are made would be obtained by the dealer claiming ITC and submitted to the VAT authorities.

Other similar judgments were given from time to time in several cases favoring innocent buyers.

Following the erstwhile principles, purchaser shall not be denied the benefit of ITC due to non-compliance of suppliers. However, there is one exception to this general rule, which states that if fraud, collusion, or connivance is established between the registered purchasing dealer and the immediate preceding selling dealer or the earlier dealer in the chain, the purchaser can be held liable for the Government dues. But until collusion is established, the purchaser shall not be denied the benefit of ITC.

In GST Law, the matching criteria was introduced to cover and trace transactions under the GST net and enhance transparency for all the stakeholders. The chain of transactions popularly known as bogus billing involves several parties that issue fake invoices without actual trade of underlying goods or services, for

availing ITC to which they are otherwise not entitled to. The purchaser involved in such transactions shall be held liable to the tax not paid on outward supplies.

Notices are being sent, and demands are made, despite numerous judicial decisions favoring the acquitted purchasing dealer. Writ petition challenging constitutional validity and vires of Section 16(2)(c) of the CGST Act have been filed with various High Courts which are pending for decision. Till the time no clarity is achieved, or no modus operandi is developed to trace culpable mind to evade tax, any stand taken on the current provision is harmful either to taxpayer or the exchequer. So one has to wait for a solution that will trap the defaulters and advance the provisions for honest taxpayers.