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File No. CBIC-20006/77/2026-GST/1071/10/11/26
Government of India
Ministry of Finance
Department of Revenue
Central Board of Indirect Taxes & Customs
GST Policy Wing
*****

16049-A,
Kartavya Bhavan-I, New Delhi
November, 2026

OFFICE MEMORANDUM

Subject: - Request for circulation of draft Agenda Note for amendment to section 16(2) and insertion of section 16A in the CGST Act, 2017 to address issues faced by bona fide recipients in respect of ITC-reg.

The undersigned has been directed to refer to thedeliberations of the 57th meeting of the GST Council regarding issues faced by bona fide recipients in respect of the provisions of section 16 of the Central Goods and Services Tax Act, 2017.

2. In this regard, the draft Agenda Note has been prepared and is enclosed as **Annexure A.** It is requested that the same may be placed beforethe Standing Committee of Officers for deliberation.

3. This issues with the approval of the Member (GST).

Digitally signed by
Manjeet Singh
Date: 10-11-2026
11:51:35
(Manjeet Suri)
Deputy Commissioner
GST Policy Wing

To,

The Joint Secretary,
GST Council Secretariat,
Tower-II, 5th Floor, Jeevan Bharati Building,
Connaught Place, New Delhi-110001.

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ANNEXURE - A

AGENDA NOTE

Subject: Amendment to section 16(2) and insertion of section 16A in the Central Goods and Services Tax Act, 2017 to address issues faced by bona fide recipients in respect of input tax credit – reg.

Kind attention is invited to Agenda Item No. 3(tt) of the 57th meeting of the GST Council regarding issues faced by bona fide recipients in respect of the provisions of section 16(2)(c) of the Central Goods and Services Tax Act, 2017 (hereinafter referred to as "the CGST Act").

2. In the said agenda, it was proposed to omit the words "*either in cash or through utilisation of input tax credit admissible in respect of the said supply*" from clause (c) of sub-section (2) of section 16 of the CGST Act. The intent was that the input tax credit of a recipient should not be denied merely because the input tax credit used for payment of tax by his supplier, or by any other person upstream in the supply chain, is later found to be inadmissible, as the recipient has no means to verify the same.

2.1 The agenda was deliberated in the 57th meeting of the GST Council. In the meeting, the State of Maharashtra stated that it fully appreciates that a genuine taxpayer, who has paid the tax, should not be penalised where somebody else in the chain has defaulted. It was suggested that, along with this (i.e. what was proposed in the Agenda), a mechanism may be worked out to identify the defaulter in the chain and recover the tax from him, so that there is no loss of revenue and the person who has rightly paid the tax is not penalised.

2.2 State of Karnataka supported the view expressed by the State of Maharashtra and stated that it was also in favour of improvement and rationalisation of the provision and of assisting genuine business entities, which are at times paying the price for the fault of somebody else in the chain. State of Karnataka also referred to the guidelines laid down by the Hon'ble Punjab and Haryana High Court for invocation of section 16(2)(c) and stated that it was open to working on a better solution.

2.3 Thus, while appreciating the difficulties faced by genuine taxpayers, the States were of the view that there must be a proper mechanism to deal with persons who knowingly collude with others to defraud the exchequer. The Council, therefore, decided that a Committee of Officers may be formed to come out with a framework or a better alternative within three months, which may be shared with the States before being placed before the Council.

2.4 Further, prior to the 57th meeting, State of Odisha had suggested that the drafting of clause (b) of sub-section (2) of section 16 of CGST Act may be improved to provide that the goods or services or both must have been received from the said supplier.

Statutory provisions:

3. Section 16(2) of the CGST Act provides that a registered person shall not be entitled to input tax credit in respect of any supply unless the following conditions are fulfilled:

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(a) he is in possession of a tax invoice or debit note issued by the supplier;

(aa) the details of the said invoice or debit note have been furnished by the supplier in the statement of outward supplies and communicated to the recipient;

(b) he has received the goods or services or both;

(ba) the details of input tax credit in respect of the said supply communicated to him under section 38 have not been restricted;

(c) subject to the provisions of section 41, the tax charged in respect of such supply has been actually paid to the Government, either in cash or through utilisation of input tax credit admissible in respect of the said supply; and

(d) he has furnished the return under section 39.

3.1 Section 16 of CGST Act is a part of Chapter V of the CGST Act, which deals with input tax credit. Section 41 of CGST Act provides that every registered person shall, subject to such conditions and restrictions as may be prescribed, be entitled to avail the credit of eligible input tax, as self-assessed, in his return. Where the supplier has not paid the tax, the recipient is required to reverse the credit along with interest under section 41(2) of CGST Act and may re-avail the same when the supplier pays the tax, in the manner provided in rule 37A of the CGST Rules, 2017. Further, section 155 of the CGST Act provides that where any person claims that he is eligible for input tax credit, the burden of proving such claim shall lie on such person.

Judicial pronouncements:

4. The Hon'ble Gujarat High Court in *Maruti Enterprise vs. Union of India (2026) 42 CENTAX 256 (Guj.) [01.05.2026]* declined to read down section 16(2)(c), but observed in para 87 as under:

> *"87. It is not the case of the Government/department that it is destitute or is vulnerable to the inaction of the seller who has not paid the tax. The Act provides the authorities with enough power to proceed against the selling dealer for recovery of tax. Sections 73 and 74 of the GST Act also empower the department to proceed against the defaulting parties in case of non-payment, short payment, and wrongful utilization of credit. A balanced approach is needed, which finds place in the decision expressed by the European Court of Justice ('ECJ') in the case of Axel Kittel (supra). Under this principle, the availment of ITC can be denied only if it is shown that the recipient knew or ought to have known that their purchase was connected with a fraudulent evasion of tax."*

The Hon'ble Court further expected the Government to address the issue of genuine purchasers.

4.2 The Hon'ble Punjab and Haryana High Court in *Shaurya Alloys Pvt. Ltd. vs. State of Punjab (CWP-34296-2024) [01.10.2026]* also upheld the validity of the provision but held that it cannot be invoked in a routine or mechanical manner. At the same time, the Hon'ble Court made it clear that cases of fraud and collusion

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stand on a different footing, and observed in para 87 as under:

> *"87. The position however would stand on a different footing, in cases where the material on record indicates collusion, fraud, non-existent selling dealer, where the goods or services have not in fact been received, or where other circumstances are established which otherwise render the claim to ITC inadmissible. In such circumstances, the issue is not only one of the subsequent non-payments of tax by the selling dealer, but of the underlying entitlement of the purchasing dealer to the ITC itself."*

The Hon'ble Court has also laid down guidelines for invoking section 16(2)(c) of CGST Act, which, inter alia, provide that cancellation of registration of the selling dealer may be the starting point of an inquiry but cannot by itself be the basis for denial of credit, that the investigation should establish a direct link of the recipient with the supplier, and that the fraud of the selling dealer shall not be attributed to the purchasing dealer unless facts connecting him with such fraud are disclosed in the notice.

5. VAT era jurisprudence

5.1. In the erstwhile VAT regime, Hon'ble High Courts had consistently held that a purchasing dealer who transacted bona fide with a validly registered selling dealer could not be denied ITC merely because the seller failed to deposit the tax collected. They also held that the Department's remedy lays against the defaulting seller. In *On Quest Merchandising India (P.) Ltd. v. Government of NCT of Delhi*, {2018 (10) GSTL 182 (Del.)}, the Hon'ble Delhi High Court read down section 9(2)(g) of the Delhi VAT Act, 2004 on the grounds that the purchaser was being asked to do the impossible, and held that where the selling dealer fails to deposit the tax, 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. Collusion between the two dealers was left to be dealt with separately under section 40A of DVAT Act which empowered Commissioner to declare an arrangement null and void when an arrangement had been made to defeat the purpose of the Act. The Supreme Court declined to interfere with it as held in *Commissioner of Trade & Taxes v. Arise India Ltd.*, {2022 (60) GSTL 215 (SC)} with liberty to the Revenue to pursue cases where the transactions were not bona fide.

5.2. The same principle was followed in **Shanti Kiran India (P.) Ltd. v. Commissioner, Trade and Tax, {(2025) 35 Centax 222 (S.C.)}.** Hon'ble Supreme Court dismissed the Revenue's appeals while noting that the selling dealer was registered on the date of the transaction and that neither the transactions nor the invoices had been doubted on inquiry. The courts have held that no liability can be fastened on the purchasing dealer for the seller's non-payment unless fraud, collusion or connivance is established. These decisions show that the settled judicial position under the VAT laws was that the bona fide recipient is not to be acted against for the supplier's default, and that action lies first against the defaulting supplier.

International practice:

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6. The European Court of Justice in *Axel Kittel vs. Belgian State (C-439/04 and C-440/04) [06.07.2006]* has held that a taxable person who did not know, and could not have known, that the transaction was connected with a fraud committed by the seller cannot be denied the right to deduct input VAT. However, where it is established on the basis of objective factors that the taxable person knew or should have known that, by his purchase, he was taking part in a transaction connected with fraudulent evasion of VAT, the right to deduct is to be refused. In the United Kingdom, this is applied by examining the general awareness of the taxable person, the contrived features of the transaction chain and whether warning signs from due diligence were ignored.

Discussion and proposal:

7. The matter has been examined further in light of the views expressed in the 57th meeting of the GST Council and the above judgments.

7.1 Under the present return filing system, tax is not paid by the supplier invoice-wise. A recipient, therefore, cannot verify whether the tax on a particular invoice has been paid in cash or through input tax credit, much less whether such credit was admissible. The requirement in section 16(2)(c) of CGST Act, as it stands, makes the credit of the recipient depend upon facts which are neither known to him nor within his control. Accordingly, the conditions in section 16(2)(c) of CGST Act of "*payment of tax by the supplier in respect of the said supply, either in cash or through utilisation of input tax credit admissible in respect of the said supply*" neither appers to be within control of the recipient, nor does he possess any mechanism or facility on GST portal to know about ensuring fulfilment of the said conditions. Therefore, it is desirable that the words "*either in cash or through utilisation of input tax credit admissible in respect of the said supply"* may be omitted from section 16(2)(c) of CGST Act as proposed in Agenda Item No. ------- of the 57th meeting of the GST Council.

7.2 At the same time, the concern of the tax administrations that persons who knowingly collude to defraud the exchequer should not get the benefit of input tax credit is valid. As held by the Hon'ble Punjab and Haryana High Court, such cases go to the root of the entitlement of the recipient to the credit itself.

7.3. A uniform thread running through all the judgments in the VAT era as well as under GST have been that ITC cab be denied if it is established that the recipient acted in fraud, collusion or connivance with the supplier. The proposal to omit the phrase "through utilisation of input tax credit admissible in respect of the said supply", which was placed before the GST Council, was leading to denial of ITC in case the supplier at any stage defaulted. A recipient can be held responsible for the actions of his immediate supplier but cannot be asked to reverse ITC on account of default by a supplier at any stage of the supply chain in case he is not involved in the violation. The international jurisprudence discussed above also denied ITC benefit is the recipient had active knowledge or had not undertaken due diligence while conducting the transaction. Even the Hon'ble Gujarat High Court in the *Maruti Enterprise case* (supra) while upholding section 16 (2) (c) had stressed on the need to have a balanced approach. However, the present formulation under section 16 does not have any express provision for denial of ITC in case of involvement of recipient in the fraudulent supply chain. Therefore, it is proposed that an explicit provision may be provided for the denial of ITC in case the recipient

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had deliberately indulged in the fraudulent transactions at any stage of the supply chain. Further, as a safeguard and in accordance with judicial principles set forth in the Shaurya Metal case *(supra)*, the same should be established through a process of investigation. It is, therefore, proposed to insert a new section 16A in Chapter V of the CGST Act, to provide that a registered person shall not be entitled to input tax credit where it is established through an investigation that he was knowingly involved in the issuance of invoices without actual supply of goods or services or both at any stage of the supply chain. Being a part of Chapter V, the said section would operate as a condition of eligibility to input tax credit, along with section 16, and would be read with sections 41 and 155 of the CGST Act. The proposed formulation also takes care of the principle laid down by the Hon'ble Gujarat High Court in the Maruti Enterprise case (supra) as it requires that tax needs to be paid by the immediate supplier. By retaining the payment of tax by the supplier in the proposed formulation, the protection regarding the first stage payment has been retained in the proposed formulation.

7.4. **Suggestion from the State of Odisha:** Clause (b) of section 16(2) of CGST Act presently requires only the receipt of the goods or services or both. Adding the words "from the said supplier" would ensure that the goods or services have been received from the same supplier who has issued the invoice and would address cases where goods are received from one person and the invoice is obtained from another.

7.5 It may be noted that the proposal does not affect the powers of the proper officer to recover the tax from the defaulting supplier under the CGST Act.

8. Accordingly, the following amendments are proposed in the CGST Act:

(a) Amendment of clause (b) of sub-section (2) of section 16 of CGST Act:

*"(b) he has received the goods or services or both*from the said supplier.

Explanation. — ..."

(b) Amendment of clause (c) of sub-section (2) of section 16 of CGST Act:

"(c) subject to the provisions of section 41, the tax charged in respect of such supply has been ~~actually~~ paid to the Government~~, either in cash or through utilisation of input tax credit admissible in respect of the said supply~~; and"

(c) Insertion of section 16A:

"16A. Notwithstanding anything contained in this Chapter, a registered person shall not be entitled to take input tax credit in respect of any supply of goods or services or both, where it is established through an investigation that such registered person has, knowingly assisted, or knowingly involved or concerned in, or knowingly been a party to, the issuance of invoice or bill without supply of goods or services or both, in respect of the said supply of goods or services or both, or at any antecedent stage within the chain of supply relating to the said goods or services or both."

9. To bring in specificity, amendments are proposed to section 41 and section 155 of the CGST Act as under: -

Section 41 Availment of input tax credit

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(1) Every registered person shall, subject to such conditions and restrictionsas may be specified in Chapter V, be entitled to avail the credit of eligible input tax, as self-assessed, in his return and such amount shall be credited to his electronic credit ledger.

Section 155. Burden of proof. -

Where any person claims that he is eligible for input tax creditunder Chapter V, the burden of proving such claim shall lie on such person.

10. The agenda note is placed before the Standing Committee of Officers for deliberation.

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