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Should the Buyer Pay for the Seller's Sin? Reading Down Section 16(2)(c) of the CGST Act, 2017**CA PARAG MEHTA**

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The GST regime was introduced with a bold promise: seamless flow of input tax credit (ITC) across goods and services throughout the supply chain, with only a handful of exceptions - supplies under the composition scheme, blocked credits, and exempt goods or services.

The Mechanism and Its Achilles' Heel

The seamless credit flow rests on one critical mechanism. For ITC to flow smoothly, the tax charged at each stage of the supply chain must actually reach the Government. Only then will the Government legitimately pass on the credit to the next recipient. This chain continues until the goods or services reach the end consumer, who bears the tax cost and does not receive any credit. The system is elegant—when everyone plays by the rules.

If even one link in this chain breaks i.e., if a seller collects tax but fails to deposit it, the Government would be granting credit **out of its own coffers**, leading to revenue leakage. From a policy standpoint, that is clearly untenable.

There are numerous instances where sellers collect tax from buyers but conveniently default to deposit it with the Government. Meanwhile, the buyer- having discharged their obligation in good faith - makes a bona fide claim for ITC. The problem? Unless the Government can verify that the seller actually paid the tax, it cannot grant credit to the buyer.

Role of Section 16(2)(c) of the CGST Act, 2017

To safeguard revenue and plug perceived loopholes, the legislature introduced several protective provisions. One such provision is **Section 16(2)(c) of the CGST Act**, which prescribes an additional condition for availing ITC.

Section 16(2)(c) provides that ITC shall be available only if *"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."*

On the face of it, the condition appears logical. The Government is not expected to fund ITC from its own pocket. However, the real difficulty lies elsewhere.

The Real Problem: Punishing the Innocent

How is a buyer supposed to ensure that the seller discharges his statutory obligation? If the Government assumes that buyers can force sellers to pay tax through constant follow-ups or by filing civil cases for recovery, is that assumption even realistic? Is the buyer supposed to constantly follow up with the seller? Is it practical to file a case for every default? Monitor the seller's compliance behaviour on a transaction-by-transaction basis?

Every commercial transaction has its own unique terms and conditions. Some require advance payments; others don't. Some buyers deal with new sellers daily; others have fixed vendor relationships. The permutations and combinations are endless. Placing the onerous burden on buyers to ensure, or rather, compel the sellers to discharge their statutory obligations is not just impractical; it's nearly impossible.

Judgement by Hon'ble Tripura High Court

This was precisely the issue taken up by the **Tripura High Court in *Sahil Enterprise v. Union of India***¹. The petitioner challenged the denial of ITC solely on the ground that the seller had failed to deposit GST, despite the buyer having acted bona fide and complied with all requirements under the law.

The challenge also extended to the constitutional validity of Section 16(2)(c), insofar as it penalised the buyer for the seller's default.

Two Sides of the Coin

At this stage, it must be acknowledged that the Government's concern is not entirely misplaced. The absence of such a provision would only enrich defaulting sellers at the expense of bona fide buyers and the Government. From this perspective, the provision serves a legitimate purpose.

But flip the coin, and another equally valid argument emerges: the Government is going after the wrong person. When the seller is the defaulter, why penalize the buyer?

The Court's Wisdom: Reading Down, Not Striking Down

This is where the Tripura High Court struck a careful balance. The Court observed that:

"Section 16(2)(c) of the Act is held not violative of Articles 14, 19(1)(g) or 265 or 300-A of the Constitution of India but Section 16(2)(c) of the Act ought not to be interpreted to deny ITC to purchasers in a bona fide transaction like the petitioner and it should be read down and applied only where the transaction is found to be not bona fide or is a collusive transaction or fraudulent transaction to defraud the revenue."

The court astutely noted that Parliament, while enacting Section 16(2)(c), failed to distinguish between:

- buyers who transacted in good faith, taking all precautions required under the Act, and
- those who were complicit or negligent in transacting with non-compliant sellers.

The court observed that there is a need to restrict the denial of ITC only to sellers who failed to deposit collected taxes, and not to punish bona fide buyers.

Importantly, the court did *not* hold Section 16(2)(c) as unconstitutional—and rightly so. Striking down the provision entirely would have opened floodgates for fraudulent minds. Instead, the court adopted a more nuanced approach: it "read down" the section, narrowing its scope to apply only to non-bona fide, collusive, or fraudulent transactions.

In other words, once a buyer establishes his bona fides, the focus of recovery must shift to the seller, not remain fixated on the easier target.

What This Means: Proof, Not Punishment

No doubt, buyers must be able to prove their bona fide claims. But once it is established that the buyer acted in good faith, the Government must pursue the defaulting seller, not penalize the innocent buyer.

This judgment strikes a delicate balance. It preserves the Government's ability to combat fraud while protecting genuine taxpayers from being collateral damage in the fight against defaulters.

What Lies Ahead?

This judgment may be challenged by the Government before the Supreme Court. If the Supreme Court agrees with the Tripura High Court's interpretation, it will significantly transform the landscape of the GST mechanism as it currently exists. The implications would be far-reaching, potentially requiring a fundamental rethinking of how ITC denials are approached.

Alternatively, the Government could choose not to challenge this order. Instead, it could return to the drawing board and redraft the provision to ensure that the real culprit—the defaulting seller, pays the price, not the innocent buyer who acted in good faith.

Conclusion: Justice, Not Just Revenue

Hon'ble Tripura High Court's judgment in *Sahil Enterprises* is a reminder that tax laws, while designed to protect Government revenue, must not trample upon the rights of honest taxpayers. The law should target wrongdoers, not innocent bystanders.

As the GST regime continues to evolve, this case will undoubtedly serve as a critical reference point. It underscores a fundamental principle: in the pursuit of revenue protection, fairness and justice must never be casualties.

The question now is whether the Government will heed this judicial wisdom or insist on making the innocent pay for the guilty's sins. Only time will tell.

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1. *Sahil Enterprises v. Union of India* [2026] 182 taxmann.com 144 (Tripura).