



Tax alert: Supreme Court holds that input tax credit under Delhi VAT Act cannot be denied due to supplier's default

17 October 2025

The Supreme Court (SC) has upheld that bona fide purchasing dealers are entitled to input tax credit (ITC) where tax was paid to registered sellers, irrespective of the sellers' subsequent default in depositing the tax.

In a nutshell



The SC has held that under Delhi Value Added Tax Act, 2004 (Delhi VAT Act), the benefit of ITC is available to the registered purchaser dealers who paid taxes to registered seller dealers in terms of valid invoices.



The SC reiterated the principles laid down in Delhi High Court (HC) judgement in the case of **On Quest Merchandising India Pvt. Ltd.** where under Section 9(2)(g) of DVAT Act was read down to exclude bona fide purchasers and that the remedy would be to proceed against the defaulting seller dealers.



The SC found no infirmity in the impugned HC order that directed to allow ITC after due verification, even though the seller dealers' registration was subsequently cancelled. The seller dealers had defaulted in tax payment but were registered on the date of transaction, and transaction and invoices are not in question.



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Background

- The issue for consideration before the Delhi HC was whether under Delhi VAT Act, the benefit of ITC is available to the registered purchaser dealers who paid taxes to registered seller dealers, in terms of invoices raised by them.
- On the date of transaction, the seller dealers were duly registered. However, later, their registration was cancelled, and they defaulted in depositing the tax to the Government.
- The HC allowed ITC to the purchaser dealer after due verification of invoices as they had paid taxes in good faith to registered seller dealers.
- The Revenue filed an appeal before the SC against the said Delhi HC judgement.

Supreme Court judgement¹

- The SC referred to Delhi HC judgement in the case of **Quest Merchandising India Pvt. Ltd**² reiterating the following observations –
 - The HC had read down section 9(2)(g) of DVAT Act to exclude bona fide purchasers. The section allowed ITC benefit to a purchasing dealer only when, the selling dealer has deposited the tax with the Government or has lawfully adjusted it against output tax liability and correctly reflected in the returns filed.
 - The remedy for the Department would be to proceed against the defaulting selling dealer to recover such tax and not deny ITC to the purchasing dealer.
 - However, where the purchasing dealer and the selling dealer acted in collusion, then the Department can proceed under Section 40A of the DVAT Act.
 - This HC order was challenged before the SC and the special leave petition was disposed of without interfering with the order of the HC.
- The SC noted that in this case, the selling dealers were duly registered at the time of the transactions and there was no dispute regarding genuineness of the transactions and invoices.
- The SC found no infirmity in the impugned HC order that directed to allow ITC after due verification and, accordingly, dismissed the appeals.

Deloitte Comments

The Honorable Supreme Court has upheld ITC eligibility on bona fide purchase transactions, despite supplier's subsequent default in depositing tax with the Government, under the DVAT laws. The ruling also has a positive impact on GST jurisprudence, particularly in the interpretation of Section 16(2)(c) of the CGST Act, which similarly links ITC entitlement to the supplier's actual tax payment.

Under GST Act, while there are various favourable HC judgements like **D.Y. Beathel Enterprises [2021-VIL-308-MAD]**, **LGW Industries Ltd. [2021 (4) TMI 280 - Calcutta High Court]**, **Lokenath Construction Pvt. Ltd. (2024) 18 Centax 97 (Cal.)**, **Suncraft Energy Pvt. Ltd. (2023) 9 Centax 48 (Cal.)**, **R.T.Infotech v. Additional Commissioner (2025) 31 Centax 204 (All.) etc.** that have ruled that the department must proceed against the defaulting supplier before denying ITC to the buyer in cases of bona fide purchases i.e., there is a valid tax invoice, goods/services have been received and payment has been made to the supplier.

With this judgement, the position is strengthened as it would be possible to argue that section 16(2)(c) should also be read down to exclude bona fide purchases, and ITC should be allowed in genuine transactions despite the fact the supplier subsequently fails to deposit the tax to the exchequer.

¹ The Commissioner Trade and Tax Delhi v. M/s. Shanti Kiran India (P) Ltd. 2025-VIL-83-SC

² On **Quest Merchandising India Pvt. Ltd. vs. Government of NCT of Delhi and Ors., 2017 SCC OnLine Delhi 13037 - 2017-VIL-544-DEL**

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