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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 8th September, 2017
Date of decision: 26th October, 2017

+ **W.P.(C) 6093/2017 & CM No.25293/2017**
ON QUEST MERCHANDISING INDIA PVT. LTD. Petitioner
Through: Mr.Rajesh Mahana, Advocate

versus

GOVERNMENT OF NCT OF DELHI & ORS. Respondents
Through: Mr.AnujAggarwal, ASC for GNCTD
with Ms. Deboshree Mukherjee, Advocate.

+ **W.P.(C) 4086/2013 & CM No.9620/2013**
SUVASINI CHARITABLE TRUST Petitioner
Through: Mr. Puneet Agrawal, Mr. Deepak
Anand and Mr. Abhishek Boob, Advocates

versus

GOVERNMENT OF NCT OF DELHI & ANR. Respondents
Through: Mr. Satyakam, ASC for GNCTD

+ **W.P.(C) 2106/2015**
ARISE INDIA LIMITED Petitioner
Through: Mr. Ruchir Bhatia, Mr. Gaurav
Khetrapal, Advocates.

versus

COMMISSIONER OF TRADE &
TAXES, DELHI AND ORS. Respondents
Through: Mr. Satyakam, ASC for GNCTD

+ **W.P.(C) 2383/2015**
VINAYAK TREXIM Petitioner
Through: Mr.Rajesh Mahana, Advocate

versus

GOVERNMENT OF NCT OF DELHI
THROUGH SECY. (FINANCE) & ORS. Respondents
Through: Mr. Satyakam, ASC for GNCTD

+ **W.P.(C) 4904/2015**

K.R. ANAND Petitioner
Through: Mr.Rajesh Mahana, Advocate

versus

GOVERNMENT OF NCT OF DELHI & ORS. Respondents
Through: Mr. Satyakam, ASC for GNCTD

+ **W.P.(C) 10708/2015**

APARICI CERAMICA Petitioner
Through: Mr. Ruchir Bhatia, Mr. Gaurav
Khetrapal, Advocates

versus

COMMISSIONER OF TRADE &
TAXES, DELHI AND ORS. Respondents
Through: Mr. Satyakam, ASC for GNCTD

+ **W.P.(C) 4573/2016**

+ **W.P.(C) 4574/2016**

+ **W.P.(C) 4704/2016**

+ **W.P.(C) 4709/2016**

+ **W.P.(C) 4710/2016**

+ **W.P.(C) 4713/2016 & CM No.19649/2016**

+ **W.P.(C) 4714/2016**

+ **W.P.(C) 4788/2016**

ARUN JAIN (HUF) Petitioner
Through: Mr.Rajesh Jain, Mr.Virag Tiwari,
Mr. V.K. Jain, Advocates

versus

THE COMMISSIONER, VALUE ADDED TAX Respondents
Through: Mr. Satyakam, ASC for GNCTD

+ **W.P.(C) 6583/2016 & CM No.26973/2016**

DAMSON TECHNOLOGIES PVT. LTD. Petitioner
Through: Mr. Raj K. Batra, Advocate

versus

COMMISSIONER OF TRADE &
TAXES, DELHI AND ANR. Respondents
Through: Mr. Satyakam, ASC for GNCTD

+ **W.P.(C) 11846/2016 & CM 46676/2016**

SOLVOCHEM Petitioner
Through: Mr. Raj K. Batra, Advocate

versus

COMMISSIONER OF TRADE &
TAXES, DELHI AND ANR. Respondents
Through: Mr. Anuj Aggarwal, ASC for
GNCTD with Ms Doboshree Mukherjee,
Advocates.

+ **W.P.(C) 6804/2017**

M/S MEENU TRADING CO. Petitioner
Through: Mr. Puneet Rai, Advocate

versus

COMMISSIONER OF TRADE &
TAXES, DELHI AND ANR. Respondents
Through: Mr. Varun Nischal, Advocate.

+ **W.P.(C) 7388/2017**

MAHAN POLYMERS

..... Petitioner

Through: Mr. Vasdev Lalwani, Mr. Rohit
Gautam, Mr. Rahul Gupta,
Advocates.

versus

COMMISSIONER OF VAT & ANR.

..... Respondents

Through: Mr. Varun Nischal, Advocate.

CORAM:

JUSTICE S. MURALIDHAR

JUSTICE CHANDER SHEKHAR

JUDGMENT

26.10.2017

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Dr. S. Muralidhar:

1. These writ petitions raise a challenge to the constitutional validity of Section 9 (2) (g) of the Delhi Value Added Tax, 2004 ('DVAT Act') as being violative of Articles 14 and 19 (1) (g) of the Constitution of India.

2. Illustratively, the facts relating to two of the writ petitioners, i.e. Suvasini Charitable Trust ('SCT') in W.P. (C) No. 4086/2013 and Arun Jain (HUF) in W.P. (C) Nos. 4573, 4574, 4704, 4709, 4710, 4713, 4714 and 4788/2016, are discussed.

Facts concerning Suvasini Charitable Trust

3. SCT is a charitable trust organization registered under the DVAT Act. It is engaged in the activity of providing food items in the Akshardham Temple complex. It states that it has paid Value Added Tax ('VAT') on its purchases. It avails Input Tax Credit ('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.

4. SCT states that on 1st June 2012, a fire broke out in the premises of the one of selling dealers - M/s. Vidya Polymers. The report of the Delhi Fire Service and the First Information Report ('FIR') lodged with the Station House Officer ('SHO'), Ashok Vihar Police Station are relied upon by SCT in support of this contention. It is stated that on account of said fire and destruction of records, M/s. Vidya Polymers failed to deposit the VAT collected from its buyers, which included SCT.

5. On 17th August 2012, the Value Added Tax Officer ('VATO') issued a default assessment order for the month of May, 2012 invoking Section 9 (2) (g) of the DVAT Act. Apart from raising a tax demand, another default assessment order imposing a penalty under Section 86 (10) of the DVAT Act was also passed by the VATO. SCT states that the above orders were passed without affording it an opportunity of being heard and solely on the basis that the ITC availed by SCT on the purchases did not match with the sale details filed by the vendor.

6. The appeals filed by SCT against the aforementioned default assessment orders were dismissed by the Objection Hearing Authority ('OHA') on 25th March 2013. These orders have also been challenged in W.P. (C) No. 4086 of 2013.

Facts concerning Arun Jain (HUF)

7. Arun Jain (HUF) ('AJ') deals in the sale and purchase of Foreign Trade

Licenses ('FTLs') issued under Section 5 of Foreign Trade (Development & Regulation) Act, 1992. It is stated that the FTL is valid for 18 months from the date of issuance. FTLs are transferable and are covered under the definition of 'goods' and their sales are exigible to VAT under the DVAT ct.

8. AJ states that during the Assessment Years ('AY') 2013-14 and 2014-15, it made intra-state purchases from registered selling dealers and paid VAT on such purchases. AJ made sure that the selling dealer had a valid Tax Identification Number ('TIN') at the time of entering into the transaction. Later, AJ claimed ITC of the VAT so paid. 80% of the FTLs are sold to customers who actually utilize them to discharge the burden of import duty. The purchase and sale of FTLs are duly recorded in the books of accounts and payments. It is stated that the payments made against purchases and payment received against sales are only through banking channels and are duly accounted for.

9. Under Section 26 of the DVAT Act read with Rule 28 of the Delhi Value Added Tax Rules, 2005 (DVAT Rules), a registered dealer is required to submit a return for each tax period. Along with the return, the dealer has to submit information regarding the summary of purchases and sales made and the VAT paid thereon in Annexures 2A and 2B respectively. It is pointed out that in case the selling dealer does not reflect the sales made to a particular purchasing dealer, a mismatch report gets generated on the website of the Department of Trade and Taxes ('Department'). Conversely, where the selling dealer correctly reflects the sales made, no mismatch will show up on the login ID of the purchasing dealer on the website.

10. AJ states that the selling dealers had duly filed their returns in DVAT-16 enclosing therewith the details of the purchases (Annexure 2A) and the details of sales (Annexure 2B). For the purposes of the ITC claimed by AJ for the aforementioned AYs, there was no mismatch reflected on the website of the Department. Despite this, the ITC was disallowed by the VATO concerned in respect of some of the purchases made on the ground that the selling dealer was 'suspicious'. This was done by purportedly invoking Section 9 (2) (g) of the DVAT Act. AJ points out that as a result, it has had to pay VAT twice on the same transaction: once at the time of purchase of the goods by paying VAT to the selling dealer and second when the ITC was disallowed and AJ was asked to pay VAT on the full sale price as recovered by it at the time of sale without the ITC. This, according to AJ, is tantamount to shifting the incidence of tax from the selling dealer to the purchasing dealer which is unconstitutional and against the scheme of the DVAT Act. The challenge in the writ petitions filed by AJ is also to the impugned orders of default assessment of tax and penalty under Sections 32 and 33 of the DVAT Act.

Relevant provisions of the DVAT Act

11. It is necessary to first examine the background to the introduction of Section 9 (2) (g) of the DVAT Act. The long title to the DVAT Act states that it is a statute "to consolidate and amend the law relating to levy of tax on sale of goods, tax on transfer of property involved in execution of works contracts, tax on transfer to right to use goods and tax on entry of motor vehicles by way of introducing a value added tax regime in the local areas to

the National Capital Territory of Delhi.” The DVAT Act came into effect with effect from 1st April 2005 by notification on 30th March 2005.

12. Under Section 40 (1) of the DVAT Act, only a registered dealer can collect any amount by way of tax under the DVAT Act. The further mandatory stipulation is that the said registered dealer can make such collection of the tax under the DVAT Act only in accordance with the DVAT Act and the DVAT Rules and on the rates specified under the DVAT Act. Section 40 (2) makes it clear that “Tax collected by a person who is not a registered dealer shall not be refunded and shall stand forfeited.”

13. Further, under Section 50 (1) of the DVAT Act, it is only a registered dealer who can issue a ‘tax invoice’ to the purchaser containing the particulars specified in sub-section (2) of Section 50 and retain a copy thereof. The Explanation to Section 50 (1) of the DVAT Act states that registered dealer shall be authorized to issue tax invoices “only after a certificate of registration is issued by the Commissioner.” It is, therefore, clear that it is only a registered dealer who can collect the DVAT under the DVAT Act and only such registered dealer can issue a tax invoice to the purchaser.

14. Section 50 (2) of the DVAT Act further states that the tax invoice issued in terms of Section 50 (1) of the DVAT Act shall contain the following particulars:

“(a) the words ‘tax invoice’ in a prominent place;

(b) the name, address and registration number of the selling registered dealer;

(c) the name and address of the purchaser and his registration number, where the purchaser is a registered dealer;

(d) an individual pre-printed serialised number and the date on which the tax invoice is issued.

Provided that a dealer may maintain separate numerical series, with distinct codes either, as a prefix or suffix, for each place of business in case the dealer has more than one place of business in Delhi or for each product in case he deals in more than one product or both;

Provided further that such numerical series may be granted by the Commissioner, in such manner and from such date as may be notified by him;

(e) description, quantity, volume and value of goods sold and services provided and the amount of tax charged thereon indicated separately;

(f) the signature of the selling dealer or his servant, manager or agent, duly authorized by him; and

(g) the name and address of the printer and first and last serial number of tax invoices printed and supplied by him to the dealer.”

15. In a scenario where the purchasing dealer is, in fact, not a *bona fide* dealer himself or colludes with the selling dealer by entering into an agreement, arrangement or understanding to defraud the Department, Section 40A of the DVAT Act provides as under:

“40A. Agreement to defeat the intention and application of this Act to be void

(1) If the Commissioner is satisfied that an arrangement has been entered into between two or more persons or dealers to defeat the application or purposes of this Act or any provision of this Act, then the Commissioner may, by order, declare the arrangement to be null and void as regard the application and purposes of this Act and may, by the said order, provide for the increase or decrease in the amount of tax payable by any person or dealer who is affected by the arrangement, whether or not such dealer or person is a party to the arrangement, in such manner as the Commissioner considers appropriate so as to counteract any tax advantage obtained by that dealer from or under the arrangement.

(2) For the purposes of this section-

(a) “arrangement” includes any contract, agreement, plan or understanding whether enforceable in law or not, and all steps and transactions by which the arrangement is sought to be carried into effect;

(b) “tax advantage” includes, -

(i) any reduction in the liability of any dealer to pay tax,

(ii) any increase in the entitlement of any dealer to claim input tax credit or refund,

(iii) any reduction in the sale price or purchase price receivable or payable by any dealer.”

16. Now turning to the provisions concerning ITC which are relevant for the purposes of the present petitions, Section 2 (1) (r) of the DVAT Act defines ‘input tax’ thus:

“(r) “input tax” in relation to the purchase of goods, means the proportion of the price paid by the buyer for the goods which represents tax for which the selling dealer is liable under this Act.”

17. Section 9 (1) of the DVAT Act permits ITC, to a dealer who is registered, “in respect of the turnover of purchases occurring during the tax period where the purchase arises in the course of his activities as a dealer and the goods are to be used by him directly or indirectly for the purpose of making sales which are liable to tax under section 3 of this Act or sales which are not liable to tax under section 7 of the DVAT Act.” The latter sales are those which involve export from Delhi either to other States or Union territories or to foreign countries.

18. Section 9 (2) of the DVAT Act sets out the conditions under which such tax credit or ITC would not be allowed. Sub-Clauses (a) to (f) specify certain kinds of purchases which would not be eligible for the claim of such ITC and they read as under:

“(a) in the case of the purchase of goods for goods purchased from a person who is not a registered dealer;

(b) for the purchase of non-creditable goods;

(c) for the purchase of goods which are to be incorporated into the structure of a building owned or occupied by the person;

Explanation.- This sub-section does not prevent a tax credit arising for goods and building materials that are purchased either for the purpose of re-sale in an unmodified form, or for the performance of a works contract on a building owned or occupied by another;

(d) for goods purchased from a dealer who has elected to pay tax under section 16 of this Act;

(e) for goods purchased from a casual trader;

(f) to the dealers or class of dealers specified in the Fifth Schedule except the entry no.1 of the said Schedule.”

19. There is yet another category of purchases on which ITC shall not be allowed. This is specified in Section 9 (2) (g) of the DVAT Act, which is presently under challenge, and which reads as under:

“(g) 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.”

20. At this stage, it is necessary to understand the purpose behind introducing Section 9 (2) (g) in the DVAT Act by the DVAT (Amendment) Act, 2009 with effect from 1st April 2009. The relevant portion of the Cabinet note explaining the proposed amendment reads as under:

“(b) It has been observed that in quite a few cases, the purchasing dealers claim ITC/Refund in respect of the purchases made from selling dealers. When the tax profiles/returns of the selling dealers are examined, it is found that negligible or no tax is deposited by the selling dealers. In such cases, it is difficult for the department to allow ITC/refund on the ground that no tax claimed to have been charged/collected by the selling dealers has actually been deposited with the department nor has it been lawfully adjusted. However, the purchasing dealer in such a case contends that purchases have been made from a dealer who is registered with the department and ITC is being claimed on the basis of tax invoices which fulfil the requirements of section 50 of the Act read with Rule 44 of the Delhi Value Added Tax Rules, 2005 (herein after referred to as “the Rules”). In several cases, the objections have been filed by such dealers against the orders of the assessing authority and consequent upon the dismissal of the objections, further appeals have been filed with the Appellate Tribunal. If more and more dealers resort to such

practices, then, not only the government revenue is going to be affected adversely in a big way but the department will also have to contest plethora of litigation. For the purpose of protecting the interest of revenue and discouraging dealers from making purchases from bogus dealers, it is necessary to incorporate an appropriate provision in this regard by inserting a new clause after sub-section 2(f) of Section 9.”

21. The Government of National Capital Territory of Delhi (‘GNCTD’) held consultations with the traders’ associations. The minutes of one such meeting held on 26th November 2009 has been placed on the record. As regards Section 9 (2) (g), it states: “this was also discussed with the representatives and they agreed to the suggestion.” In the attendance sheet of that date i.e. 26th November 2009, the presence of a sampling of the traders’ associations is reflected. Of course, this by itself will not decide the constitutional validity of the provision.

22. It may be noted that there is a distinction between those categories specified in Section 9 (2) (a) to (f) of the DVAT Act which disentitle to the grant of ITC and the one under Section 9 (2) (g). Whereas the conditions specified in Section 9 (2) (a) to (f) are those which are within the control of and can be vouched for by the purchasing dealer, the condition under Section 9 (2) (g) is not. It requires the purchasing dealer to ensure, for the purposes of claiming ITC, that the selling dealer has deposited VAT with the Government or has lawfully adjusted it against such selling dealer’s output tax liability. This is not within the control of the purchasing dealer. This is one of the major bones of contention in the present petition as will be seen hereinafter.

23. To complete the examination of the relevant provisions of the DVAT concerning claim of ITC, it may be recalled that under the DVAT Act, returns have to be filed by the registered dealer under Section 26 thereof read with Rule 26 and 28 of the DVAT Rules. Under Rule 26 (1) of the DVAT Rules, the “tax period for all the registered dealers is a quarter i.e. 3 months.” The tax return in Form DVAT-16 has to be filed within a period of 28 days from the end of the tax period in terms of Rule 28 (3) of the DVAT Rules. Under Section 3 (4) of the DVAT Act, the net tax, i.e. the tax payable by the dealer minus the ITC claimed in terms of Section 9 (1) read with Section 9 (2), has to be paid within twenty-one days of the conclusion of each calendar month. Such deposit of tax in DVAT Form-20 has to be enclosed with the return filed by such registered dealers. The details furnished with the returns, including the documents enclosed therewith, are to be treated as ‘confidential’ in terms of Section 98 (1) of the DVAT Act. The exceptions to this are specified in Section 98 (3) of the DVAT Act.

Submissions on behalf of the Petitioners

24. On behalf of the Petitioners, the following submissions were made by Mr. N. Venkatraman, the learned Senior Counsel and Mr. Puneet Agrawal, Mr. Rajesh Jain and Mr. Rajesh Mahana, the learned counsel appearing for the Petitioners:

(i) The objective of the DVAT Act is to charge tax only on ‘value additions’ and to avoid a cascading effect of taxes. Section 9 (2) (g), however, treats both the ‘guilty purchasers’ and the ‘innocent purchasers’ at par whereas they constitute two different classes. Where the ‘guilty purchasers’ in

collusion with the 'guilty seller' enter into a tacit agreement or understanding or arrangement to falsely claim ITC and cause loss of revenue, it is not as if the government is powerless to check such frauds. Section 40A of the DVAT Act has been specifically enacted for that purpose. Nevertheless, irrespective of whether the purchasing dealer is innocent, on account of subsequent conduct of the selling dealer, who has collected the VAT from the purchasing dealer and has failed to deposit it with the government or has failed to lawfully adjust it against his output tax liability, the purchasing dealer is made to suffer. This is violative of Article 14 of the Constitution inasmuch as it treats both the innocent purchasers and the guilty purchasers alike. In other words, it is submitted that by treating unequals equally the legislative measure is violative of Article 14 of the Constitution. Reliance is placed on the decision in ***K.T. Moopil Nair v. State of Kerala AIR 1961 SC 552*** and ***State of Kerala v. Haji and Haji AIR 1969 SC 378***.

(ii) Section 9 (2) (g) of the DVAT Act denies to a *bona fide* purchaser, the benefit of the ITC only because of the default of the selling dealer over whom such purchasing dealer has not control. This measure *qua* the purchasing dealer is arbitrary, irrational and unduly harsh and, therefore, violative of Article 14 of the Constitution. Reliance is placed on the decisions in ***Commissioner of Customs, Amritsar v. Parker Industries 2007 (207) ELT 658 (P&H)*** and ***Shanti Kiran India Pvt. Ltd. v. Commissioner, Trade and Tax Deptt. (2013) 57 VST 405 (Delhi)***.

(iii) There are other statutory avenues available to the State to collect tax

from the defaulting dealer. This includes recovery of the tax in case the dealer fails to deposit the same under Section 43 of the DVAT Act; forfeiture of security deposited under section 19 of DVAT Act read with Rule 22 of the DVAT Rules; recovery of tax as arrears of land revenue whereby the Commissioner prepares and issues to the defaulting selling dealer a recovery certificate and thereafter recovers the amount specified in the certificate by attaching the movable and immovable property of or even the arrest of the certificate-debtor; or appointing a receiver for the management of the movable and immovable properties of such certificate-debtor.

(iv) The only requirement of law, as far as the purchasing dealer wanting to avail the benefit of ITC is concerned, is that he has to make sure that the selling dealer is a registered dealer and has issued the tax invoice in compliance with the requirement of the DVAT Act and the Rules made thereunder. Once the purchasing dealer demonstrates that he has complied with such requirement, he cannot be denied the ITC only because the selling dealer fails to discharge his obligation under the DVAT Act. From the point of view of the Petitioners in the present case, all of them as purchasing dealers have complied with the requirement of DVAT Act and all of them have ensured that the purchases made by them are in compliance with the requirements of the DVAT Act for claiming ITC. Reliance is placed on the decisions in *Corporation Bank v. Saraswati Abharansala* (2009) 19 VST 84 (SC); *State of Punjab v. Atul Fasteners Ltd.* (2007) 7 VST 278 (SC) and *Gheru Lal Bal Chand v. State of Haryana* (2011) 45 VST 195 (P&H).

(v) The condition under Section 9 (2) (g) of the DVAT Act that the selling dealer has ‘actually deposited’ should be read as selling dealer “ought to have deposited” tax. Alternatively, the expression ‘dealer’ occurring therein should be read down to exclude a purchasing dealer who, on his part, has duly complied with the requirements under the DVAT Act. Reliance is placed on the decisions in *Assistant Collector of Central Excise, Bombay v. The Elphinstone Spinning & Weaving Mills Company AIR 1971 SC 2039* and *Gurshai Saigal v. CIT AIR 1963 SC 1062*.

(vi) Reliance is also placed on the decisions in *Bajaj Tempo Ltd. v. CIT (1992) 3 SCC 78*, *Aidek Tourism Services Pvt. Ltd. v. Commissioner of Customs (2015) 7 SCC 429* and *Union of India v. Ranbaxy Lab. Ltd. (2008) 7 SCC 502* to urge that the interpretation of Section 9 (2) (g) of the DVAT Act has to be in consonance with the object and purpose of the DVAT Act. It is argued that a pragmatic view must be taken and practical aspects considered before enforcing compliance. It is further urged that the ground realities of marketing and sales have to be considered while interpreting an exemption provision. It is pointed out that even if it is assumed that subsequent to the purchases made by the purchasing dealer, the registration of the selling dealer is cancelled, such cancellation cannot be given retrospective effect so as to deny the purchasing dealer the ITC in respect of the VAT paid by him.

(vii) Reliance is placed on the decisions in *Mahadev Enterprise v. State of Gujarat 2016 (92) VST 360 (Gujarat)*, *Jinsasan Distributors v. CTO (2013) 59 VST 256 (Madras)* to urge that as long as there is no mismatch of

Annexures 2A and 2B, ITC cannot be denied. Reliance is placed on the decision of this Court in *Progressive Alloys (India) Pvt. Ltd. v. Commissioner of Trade & Taxes* (decision dated 3rd February, 2016 in W.P. (C) No. 7434/2015) and *Infiniti Wholesale Limited v. Assistant Commissioner of Tax (2015) 82 VST 457 (Madras)*.

(viii) Penalty under Section 86 (10) of the DVAT Act cannot be imposed unless it is shown that the return filed is misleading or deceptive. When the buying dealer has no means to ascertain the fact of non-deposit by the selling dealer of the VAT collected from the purchasing dealer, it cannot be assumed that the purchasing dealer has deliberately failed to pay tax. Therefore, Section 86 (10) cannot be applied straightaway. Reliance is placed on the decisions in *Commissioner of Sales Tax, U.P. v. Sanjiv Fabrics (2010) 9 SCC 630*, *Jatinder Mittal Engineers and Contractors v. Commissioner of Trade & Taxes 2011 (46) VST 498 (Del)* and *Pentex Sales Corporation v. Commissioner of Sales Tax, Delhi (2014) 67 VST 229 (Delhi)*.

(ix) The penalty under Section 86 (10) is not automatic and has to be preceded by the proper notice being served on the Assessee and an effective opportunity of being heard being given. Reliance is placed on the decision in *Commissioner of Income Tax v. Manjunatha Cotton and Ginning Factory [2013] 359 ITR 565 (Kar.)* and *Amrit Foods v. Commissioner (2005) 13 SCC 419*.

Submissions on behalf of the Department

25. In reply, Mr. Satyakam, the learned Additional Standing Counsel for the

Department, first referred to the decisions in *Rajbala v. State of Haryana (2016) 2 SCC 445* and *Municipal Committee v State of Punjab (1969) 1 SCC 75* to urge that arbitrariness cannot be a ground for challenging the statute as being violative of Article 14 of the Constitution. He further submitted that mere hardship caused by the impossibility of compliance of the provisions cannot be a ground for striking down a statute.

26. Reliance was also placed on the decisions in *State of Madhya Pradesh v. Kohli Brothers (2012) 6 SCC 312* and *R.K. Garg v. Union of India (1981) 4 SCC 675* to urge that where a fiscal statute was being challenged, a greater leeway had to be given to the legislature and there had to be a presumption of soundness of the legislative policy. It was argued, therefore, that the Court is not to question legislative wisdom in such matters. He referred to the note prepared for consideration of the Cabinet prior to the insertion of Section 9 (2) (g) of the DVAT Act and submitted that it was for sound reasons that the said provision was introduced since it was found that there were a large number of instances where selling dealers, after collecting tax, failed to deposit it with the Government.

27. Mr Satyakam placed extensive reliance on the decision of the Bombay High Court in *Mahalaxmi Cotton Ginning Pressing and Oil Industries v. State of Maharashtra (2012) 51 VST 1 (Bom.)* where a similar provision under the Maharashtra Value Added Tax Act ('MVAT Act') was upheld. He also referred to the fact that the Special Leave Petition filed against the aforesaid decision of the Bombay High Court was dismissed by the Supreme Court. He pointed out that the said decision was upheld by the Supreme

Court in *Jayam & Co. v. Assistant Commissioner (2016) 96 VST 1 (SC)*. Mr. Satyakam also similarly relied on similar provisions of the Rajasthan VAT Act and the Gujarat VAT Act.

Analysis and reasons

28. At the outset, it requires to be understood that Section 2 (1) (r) of the DVAT Act implicitly recognizes that when the buyer pays the seller the price for the purchase of goods, such price is inclusive of the DVAT for which the seller is 'liable' to pay to the Government. Which is why it talks of payment by the buyer of the liability that is essentially that of the seller. VAT is an indirect tax, the incidence of which can be passed on and is in fact passed on by the seller to the purchaser.

29. To be eligible for ITC, the purchasing dealer who, apart from being registered under the DVAT Act, has to take care to verify that the selling dealer is also a registered dealer and has a valid registration under the DVAT Act. The second condition is that such registered selling dealer has to issue to the purchasing dealer a 'tax invoice' in terms of Section 50 of the DVAT Act. Such tax invoice would obviously set out the TIN number of the selling dealer. The purchasing dealer can check on the web portal of the Department if the selling dealer is a fictitious person or a person whose registration stands cancelled. As long as the purchasing dealer has taken all these steps, he cannot be expected to keep track of whether the selling dealer has in fact deposited the tax collected with the Government or has lawfully adjusted it against his output tax liability. The purchasing dealer can, of course, ascertain if there is any mismatch of Annexures 2A and 2B but,

assuming it is on account of the seller's default, there is little he can do about it.

30. Another difficulty that the purchasing dealer would face is that he would have no access to the return filed by the selling dealer particularly since under Section 98 (1) of the DVAT Act those particulars are meant to be confidential. Under Section 98 (3) (j) of the DVAT Act, it is possible for the Commissioner, where he considers it desirable in the public interest, to publish such information. That hinges on the Commissioner placing those details in public domain. If the Commissioner has not placed such information in the public domain, then it is next to impossible for the purchasing dealer to ascertain the failure of the selling dealer to make a correct disclosure of the sales made in his return.

31. Again, it is not as if the Department is helpless if the selling dealer commits a default in either depositing or lawfully adjusting the VAT collected from the purchasing dealer. There are provisions in the DVAT Act, referred to hereinbefore, which empower the Department to proceed to recover the tax in arrears from the selling dealer. There is also Section 40A, in terms of which, a purchasing dealer acting in connivance with a selling dealer can be proceeded against.

32. It is indeed strange that the note prepared for the Cabinet at the time of insertion of Section 9 (2) (g) in the DVAT Act did not mention Section 40A which had already been inserted by the DVAT Second Amendment Act, 2005 with effect from 16th November 2005. The note also did not take note of the practical difficulty that would be faced by the purchasing dealer in

anticipating, even before entering into the transaction with the registered selling dealer holding a valid registration, that such selling dealer after collecting the tax from him was either not going to deposit it with the Government or lawfully adjust it against his output tax liability. This is a major omission of important factors which had a bearing on the ITC being claimed by a dealer.

33. Indeed, what Section 9 (2) (g) of the DVAT does is give the Department a free hand in deciding to proceed either against the purchasing dealer or the selling dealer or even both when it finds that the tax paid by the purchasing dealer has not actually been deposited by the selling dealer with the Government or has not been lawfully adjusted against the selling dealer's output tax liability and correctly reflected in the return filed by such selling dealer in the respective tax periods. It uses the phrase, "dealer or class of dealers" which could include either the purchasing dealer or the selling dealer. In the situation envisaged by Section 9 (2) (g) itself, clearly the defaulting party is the selling dealer. He has collected the VAT from the purchasing dealer and failed to deposit it with the Government or failed to lawfully adjust it against his output tax liability and has failed to correctly reflect that in his return. For all these defaults committed by the selling dealer, the purchasing dealer is expected to bear the consequence of being denied the ITC. It is this that is being questioned as violative of Article 14 of the Constitution.

34. First, there is the issue of Section 9 (2) (g) of the DVAT Act failing to distinguish between *bona fide* purchasing dealers and those that are not.

While denial of ITC could be justified where the purchasing dealer has acted without due diligence, i.e. by proceeding with the transaction without first ascertaining if the selling dealer is a registered dealer having a valid registration, denial of ITC to a purchasing dealer who has taken all the necessary precautions fails to distinguish such a diligent purchasing dealer from the one that has not acted bonafide. This failure to distinguish *bona fide* purchasing dealers from those that are not results in Section 9 (2) (g) applying equally to both the classes of purchasing dealers. This would certainly be hit by Article 14 of the Constitution as explained in several decisions which will be discussed hereinafter.

35. In ***Shri Ram Krishna Dalmia v. Shri Justice S. R. Tendolkar [1959] 1 SCR 279***, the Supreme Court observed as under:

“A statute may not make any classification of the persons or things for the purpose of applying its provisions but may leave it to the discretion of the Government to select and classify persons or things to whom its provisions are to apply. In determining the question of the validity or otherwise of such a statute the Court will not strike down the law out of hand only because no classification appears on its face or because a discretion is given to the Government to make the selection or classification but will go on to examine and ascertain if the statute has laid down any principle or policy for the guidance of the exercise of discretion by the Government in the matter of the selection or classification. After such scrutiny the Court will strike down the statute if it does not lay down any principle or policy for guiding the exercise of discretion by the Government in the matter of selection or classification, on the ground that the statute provides for the delegation of arbitrary and uncontrolled power to the Government so as to enable it to discriminate between persons or things similarly situate and that, therefore, the discrimination is inherent in the statute

itself.”

36. In ***K.T. Moopil Nair v. State of Kerala*** (*supra*), the Supreme Court was faced with a situation where an absence of classification led to a violation of Article 14 of the Constitution. The statute under challenge was the Travancore Cochin Land Tax Act, 1955 (‘TCLT Act’). Section 4 of the TCLT Act laid down that a uniform rate of tax would be levied on all lands in the State “of whatever description and held under whatever tenure”, i.e. 2 paisa per cent which worked out to Rs. 2 per acre per annum. This uniform rate of tax was challenged on the ground that all lands in the State did not have same productivity quality; some were waste lands and others were in varying degree of fertility. The tax therefore weighed more heavily on owners of waste lands than the owners of fertile lands. In ***Budhan Chaudhary v. State of Bihar*** [1955] 1 SCR 1045, the Supreme Court had explained that while Article 14 forbids class legislation, “it does not forbid reasonable classification for the purposes of legislation.” What, however, had to be fulfilled were the two tests: (i) “that the classification must be founded on an intelligible differentia which distinguishes persons or things that are grouped together from others left out of the group” and; (ii) “that differentia must have a rational relation to the object sought to be achieved by the statute in question.”

37. Applying the above criteria, in ***K.T. Moopil Nair v. State of Kerala*** (*supra*), the Supreme Court concluded by a majority of 4:1 that the failure to make a classification between a productive and non-productive land for the purposes levy of such tax rendered the statute unconstitutional.

38. In *State of Kerala v. Haji and Haji* (*supra*) the Kerala Building Tax Act, 1961 ('KBT Act') was challenged. Section 4 of the KBT Act provided that every building, construction of which is completed on or after 2nd March 1961 and which has a building area of 1000 sq. ft. or more, would be liable for building tax payable by the owner of the building. The buildings having a total area of less than 1000 sq. ft. were not liable to pay tax. The Court found that no rational classification had been made by the legislature. It found that:

“the Legislature has not taken into consideration in imposing tax the class to which a building belongs, the nature of construction, the purpose for which it is used, its situation, its capacity for profitable user and other relevant circumstances which have a bearing on matters of taxation. They have adopted merely the floor area of the building as the basis of tax irrespective of all other considerations. Where objects, persons or transactions essentially dissimilar are treated by the imposition of a uniform tax, discrimination may result, for, in our view, refusal to make a rational classification may itself in some cases operate as denial of equality.”

39. Applying the law explained in the above decisions, it can be safely concluded in the present case that there is a singular failure by the legislature to make a distinction between purchasing dealers who have *bona fide* transacted with the selling dealer by taking all precautions as required by the DVAT Act and those that have not. Therefore, there was need to restrict the denial of ITC only to the selling dealers who had failed to deposit the tax collected by them and not punish *bona fide* purchasing dealers. The latter cannot be expected to do the impossible. It is trite that a law that is not capable of honest compliance will fail in achieving its objective. If it seeks

to visit disobedience with disproportionate consequences to a *bona fide* purchasing dealer, it will become vulnerable to invalidation on the touchstone of Article 14 of the Constitution.

40. The need for the law to distinguish between honest and dishonest dealers was acknowledged by the Punjab and Haryana High Court in ***Gheru Lal Bal Chand v. State of Haryana*** (*supra*) where the constitutional validity of a similar Section 8 of the Haryana DVAT Act, 2003 ('HVAT Act') was being considered. It was held that:

“In legal jurisprudence, the liability can be fastened on a person who either acts fraudulently or has been a party to the collusion or connivance with the offender. However, law nowhere envisages imposing any penalty either directly or vicariously where a person is not connected with any such event or an act. Law cannot envisage an almost impossible eventuality. The onus upon the assessee gets discharged on production of Form VAT C-4 which is required to be genuine and not thereafter to substantiate its truthfulness by running from pillar to post to collect the material for its authenticity. In the absence of any malafide intention, connivance or wrongful association of the assessee with the selling dealer or any dealer earlier thereto, no liability can be imposed on the principle of vicarious liability. Law cannot put such onerous responsibility on the assessee otherwise, it would be difficult to hold the law to be valid on the touchstone of Articles 14 and 19 of the Constitution of India. The rule of interpretation requires that such meaning should be assigned to the provision which would make the provision of the Act effective and advance the purpose of the Act. This should be done wherever possible without doing any violence to the language of the provision. A statute has to be read in such a manner so as to do justice to the parties. If it is held that the person who does not deposit or is required to deposit the tax would be put in an advantageous position and whereas the person who has paid the tax would be worse, the

interpretation would give result to an absurdity. Such a construction has to be avoided.

In other words, the genuineness of the certificate and declaration may be examined by the taxing authority, but onus cannot be put on the assessee to establish the correctness or the truthfulness of the statements recorded therein. The authorities can examine whether the Form VAT C-4 was bogus and was procured by the dealer in collusion with the selling dealer. The department is required to allow the claim once proper declaration is furnished and in the event of its falsity, the department can proceed against the defaulter when the genuineness of the declaration is not in question. However, an exception is carved out in. The event where fraud, collusion or connivance is established between the registered purchasing dealers or the immediate preceding selling registered dealer or any of the predecessors selling registered dealer, the benefit contained in Form VAT C-4 would not be available to the registered purchasing dealer. The aforesaid interpretation would result in achieving the purpose of the rule which is to make the object of the provisions of the Act workable, i.e., realization of tax by the revenue by legitimate methods.”

41. The Court respectfully concurs with the above analysis and holds that in the present case, the purchasing dealer is being asked to do the impossible, i.e. to anticipate the selling dealer who will not deposit with the Government the tax collected by him from those purchasing dealer and therefore avoid transacting with such selling dealers. Alternatively, what Section 9 (2) (g) of the DVAT Act requires the purchasing dealer to do is that after transacting with the selling dealer, somehow ensure that the selling dealer does in fact deposit the tax collected from the purchasing dealer and if the selling dealer fails to do so, undergo the risk of being denied the ITC. Indeed Section 9 (2) (g) of the DVAT Act places an onerous burden on a bonafide

purchasing dealer.

42. All this points to a failure to make a correct classification on a rational basis so that the denial of ITC is not visited upon a bonafide purchasing dealer. This failure to make a reasonable classification, does attract invalidation under Article 14 of the Constitution, as pointed out rightly by learned counsel for the Petitioners. This is also what weighed with the Court in *Shanti Kiran India Pvt. Ltd.* (*supra*) where it was observed as under:

“In the present case, Section 9 (1) grants- input-tax credit to purchasing dealers. Section 9 (2), on the other hand lists out specific situations where the benefit is denied. The negative list, as it were, is restrictive and is in the nature of a proviso. As a result, this Court is of the opinion that the interpretation. placed by the Tribunal-that there is statutory, authority for granting input-tax credit only to the extent tax is deposited by the selling dealer, is unsound and contrary, to the, statute, It is also iniquitous because an onerous burden is placed on the purchasing dealer - in the absence of clear words to that effect in the statute to keep a vigil over the amounts deposited by the selling dealer. The court, does not see any provision or methodology by which the purchasing dealer can monitor the selling dealers behaviour, 'vis-a-vis the latter's VAT returns. Indeed, Section 28 stipulates confidentiality in such matters. Nor is this Court in agreement with the Tribunal's opinion that insertion of clause (g) to section 9 (2) is clarificatory. As observed earlier, Section 9 (2) is an exception to the general rule granting input-tax credit to dealers who qualify .for the benefit. The conditions for operation of the exception are well defined. The absence of any condition such as the one spelt out in clause (g) and its addition in 2010, rules out legislative intention of its being a mere clarification of the law which always existed.”

43. The Petitioners have argued that Section 9 (2) (g) also suffers from the

vice of arbitrariness and is, on that ground, hit by Article 14 of the Constitution. There is some uncertainty as of today on whether a law can be struck down only on the ground of arbitrariness thereby attracting Article 14 of the Constitution. This doubt has been created by the decision of the Supreme Court in *Rajbala v. State of Haryana* (*supra*) and *Binoy Viswam v. Union of India* (2017) 7 SCC 59 the correctness of both of which has been doubted by the Supreme Court in its recent 3:2 decision in *Shayara Bano v. Union of India* 2017 (9) SCALE 178, invalidating triple *talaq* where, in the majority opinion of Justice R. F. Nariman, after noting that the decision in *State of Andhra Pradesh v. McDowell & Co.* (1996) 3 SCC 709 was on this point *per incuriam*, observed as under:

“53. However, in *State of Bihar v. Bihar Distillery Ltd.*, (1997) 2 SCC 453 at paragraph 22, in *State of M.P. v. Rakesh Kohli*, (2012) 6 SCC 312 at paragraphs 17 to 19, in *Rajbala v. State of Haryana & Ors.*, (2016) 2 SCC 445 at paragraphs 53 to 65 and 387 *Binoy Viswam v. Union of India* (2017) 7 SCC 59 at paragraphs 80 to 82, *McDowell* (*supra*) was read as being an absolute bar to the use of “arbitrariness” as a tool to strike down legislation under Article 14. As has been noted by us earlier in this judgment, *McDowell* (*supra*) itself is *per incuriam*, not having noticed several judgments of Benches of equal or higher strength, its reasoning even otherwise being flawed. The judgments, following *McDowell* (*supra*) are, therefore, no longer good law.”

44. The above passage occurs in the opinion of Justice R. F. Nariman in which Justice U. U. Lalit joined. A separate opinion was given by Justice Kurien Joseph concurring with the above opinion of Justice Nariman in which it was observed:

“In that view of the matter, I wholly agree with the learned

Chief Justice that the 1937 Act is not a legislation regulating talaq. Consequently, I respectfully disagree with the stand taken by Nariman, J. that the 1937 Act is a legislation regulating triple talaq and hence, the same can be tested on the anvil of Article 14. **However, on the pure question of law that a legislation, be it plenary or subordinate, can be challenged on the ground of arbitrariness, I agree with the illuminating exposition of law by Nariman, J.”** (emphasis supplied)

45. It would therefore appear that the decisions in *Rajbala v. State of Haryana* (*supra*) and *Binoy Viswam v. Union of India* (*supra*) which held that a legislation cannot be challenged on the ground of arbitrariness are no longer good law. In view of the uncertainty on this issue, the Court does not propose to examine it further in this batch of cases. In any event, the Court has, for the reasons explained, concluded that the failure of Section 9 (2) (g) of the DVAT Act to make a rational classification between purchasing dealers who are *bona fide* and those that are not renders it vulnerable to invalidation under Article 14 of the Constitution.

46.1 What remains is the discussion of the decisions relied upon by the Department to defend the validity of Section 9 (2) (g) of the DVAT Act as it stands. In *M/s. Mahalaxmi Cotton Ginning Pressing & Oil Industries v. State of Maharashtra* (*supra*) the Bombay High Court was concerned with interpreting Section 48 (5) of the MVAT Act, which reads as under:

“(5) For the removal of doubt it is hereby declared that, in no case the amount of set off or refund on any purchase of goods shall exceed the amount of tax in respect of the same goods, actually paid, if any, under this Act or any earlier law, into the Government Treasury except to the extent where purchase tax is payable by the Claimant dealer on the purchase of the said goods effected by him:

Provided that, where tax levied or leviable under this Act or in earlier law is deferred or is deferrable under any Package Scheme of Incentives implemented by the State Government, then the tax shall be deemed to have been received in the government treasury for the purposes of this sub-section.”

46.2 It can straightway be seen that Section 48 (5) of the MVAT Act is not an exact replica of Section 9 (2) (g) of the DVAT Act. For instance, Section 48 (5) of the MVAT Act requires the selling dealer to have “actually paid” the tax collected by him with the Government for the purposes of the purchasing dealer availing ITC, whereas Section 9 (2) (g) of the DVAT Act requires the selling dealer to either “deposit” the tax collected or lawfully adjust it against his output tax apart from correctly reflecting the sale in his returns. While interpreting those words ‘actually paid’, the Bombay High Court relied on the decisions in *State of Madhya Pradesh v. Indore Iron and Steel Mills Private Limited* (1999) 111 STC 261 (SC), *N.B. Sanjana v. Elphinstone Spinning & Weaving Mills Co. Ltd.* (1971) 1 SCC 337 (SC), *Sulekh Ram & Sons v. Union of India* (1978) 2 ELT J 525 (Del), which were confirmed by the Supreme Court in *CCE v. Decent Dyeing Co.* (1990) 45 ELT 201 (SC).

46.3 It also requires to be noted that the Bombay High Court was concerned with a situation where the purchase transactions disclosed by the purchasing dealer did not match the sale transactions disclosed by the selling dealer. In contrast, in the cases before this Court there is no instance where Annexures 2A and 2B have not matched.

46.4 Two of the critical paras in the Bombay High Court's decision in *M/s. Mahalaxmi Cotton Ginning Pressing & Oil Industries v. State of Maharashtra* (*supra*) are paras 48 and 55, which read thus:

“48. In the context in which the words "actually paid" are used in the MVAT Act, "actually paid" means what has been as a matter of fact deposited in the treasury. Hence, in the context of the provisions of Section 48(5), we cannot accept the contention of the Petitioner that "actually paid ... in the government treasury" means or should be read to mean what tax ought to have been deposited but has not actually been deposited in the treasury. To accept the submission would be to rewrite the legislative provision. Moreover, the concept of a set off presupposes that tax has been paid in respect of the goods in respect of which a set off is claimed. To allow a set off though the tax has not been paid actually would be to defeat the legitimate interests of the Revenue. Hence, in the overall statutory scheme of Section 48; sub-section (5) has a rational basis and foundation. The liability to pay tax is that of the selling dealer. As the Constitution Bench held in *Tata Iron & Steel Co. Limited v. State of Bihar* (1958) 9 STC 267 (SC); AIR 1958 SC 452 and in *George Oakes (Private) Limited v. State of Madras* (1962) 13 STC 98 (SWC); AIR 1962 SC 1037, whether the tax is passed on by the selling dealer to the purchasing dealer is a matter of their contractual understanding. Once that is the position that has held the field in our jurisprudence for over fifty years and has been reiterated in *Khazan Chand v. State of Jammu and Kashmir* (1984) 56 STC 214 (SC); AIR 1984 SC 762 and *Central Wines v. Special Commercial Tax Officer* (1987) 65 STC 48 (SC); (1987) 2 SCC 371, by the Supreme Court, a dealer cannot obviate his liability to pay tax on his sale transaction, by claiming a set off and placing the responsibility to recover tax on an earlier link in the chain on the Revenue. To test the constitutionality of Section 48(5) one must ask oneself whether the legislature has acted discriminatorily or whether the provision is facially or ex facie discriminatory. Neither is the object or effect of Section 48(5) discriminatory. The State legislature was not bound to

grant a set off. If the legislature had not granted a set off, that would not have a bearing on its competence or on constitutionality, since a tax on the sale of goods falls within the purview of Entry 54. In granting a set off, the legislature can impose conditions and that imposed in Section 48(5) is not lacking in rationality. Moreover, the scheme for set off in Section 48 has to be read in its entirety and as one cohesive whole. The legislature cannot be compelled to grant a set off, ignoring the conditions which it imposes. The conditions are not severable and are part of one integrated scheme.”

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55. The Punjab and Haryana High Court held that while the genuineness of a certificate and a declaration may be examined by the taxing authority, the onus cannot be placed on the assessee to establish the correctness or the truthfulness of the statements recorded therein. The High Court held that the Department must allow the claim once a proper declaration is furnished. In the event of its falsity, the Department can proceed against the defaulter when the genuineness of the declaration is not in question. However, an exception has been carved out in the event that fraud, collusion or connivance is established between the registered purchasing dealer or the immediate preceding selling dealer or the earlier dealer in the chain. The judgment of the High Court did not involve a challenge to a provision such as Section 48(5) of the MVAT Act, 2002. We may only note with the greatest respect and deference that while the High Court has relied upon the observations contained in the decisions of the Benches of two Learned Judges of the Supreme Court in *Atul Fasteners (2007) 7 VST 278 (SC)* and in *Corporation Bank (2009) 19 VST 84 (SC)*, the earlier decisions of the Constitution Benches in *TISCO (1958) 9 STC 267 (SC)*; *AIR 1958 SC 452* and in *George Oakes (1962) 13 STC 98 (SC)*; *AIR 1962 SC 1037* were not perhaps drawn to the attention of the Court. Moreover, the decision in *Elphinston Spinning AIR 1971 SC 2039* which construed the word "paid" in Rule 10 of the Central Excise

Rules involved an issue of short levy. Finally we may note that a provision such as Section 48(5) which uses clear and express words such as that in "no case" shall a set off exceed the tax "actually paid" in the government treasury did not fall for consideration."

46.5 The reference, in para 48 above, to the decisions of the Supreme Court in *Khazan Chand v. State of Jammu and Kashmir* (*supra*) and *Central Wines v. Special Commercial Tax Officer* (*supra*), was in the context of the liability to pay tax being essentially on the selling dealer. It was held there that a selling dealer cannot obviate his liability to pay tax on his 'sale transaction' by claiming set off and placing the responsibility to recover tax on an earlier link in the chain on the Revenue. It proceeds on the basis that the State Legislature is not "bound to grant a set off". It further states that the Legislature cannot be "compelled to grant a set-off, ignoring the conditions which it imposes".

46.6 In the present case, the conditions imposed for the grant of ITC are spelt out in Sections 9 (1) and (2) of the DVAT Act and have been adverted to earlier. The claim of the purchasing dealer in the present case is not that it should be granted that ITC *de hors* the conditions. Their positive case is that each of them, as a purchasing dealer, has complied the conditions as stipulated in Section 9 and therefore, cannot be denied ITC because only selling dealer had failed to fulfil the conditions thereunder. More importantly, the Court finds that there is no provision in the MVAT Act similar to Section 40A of the DVAT Act. Section 40A of the DVAT Act takes care of a situation where the selling dealer and the purchasing dealer act in collusion with a view to defrauding the Revenue. In fact, the operative

directions in *Mahalaxmi Cotton Ginning Pressing and Oil Industries* (*supra*) indicate that such a measure was suggested by the State Government itself to go after defaulters, i.e. selling dealers failing to actually pay the tax. The Department there undertook to upload on its website the details of the defaulting dealers. It was further undertaken that once there was a final recovery of the tax from the selling dealer, refund would be granted to the purchasing dealer.

46.7 Mr. Satyakam has placed extensively reliance on para 55 of the decision of the Bombay High Court where that High Court disagreed with the conclusions of the Punjab & Haryana High Court in *Gheru Lal Bal Chand v. State of Haryana* (*supra*). The Bombay High Court appears to have distinguished the said decision only because there was no provision in the HVAT Act similar to Section 48 (5) of the MVAT Act which required the tax to be 'actually paid' into the Government treasury. In the considered view of the Court, the decision of the Bombay High Court in *Mahalaxmi Cotton Ginning Pressing and Oil Industries* (*supra*) turned on the peculiar wording of Section 48 (5) of the MVAT Act. Secondly, the fact situation where the transactions disclosed by the purchasing dealer and the selling dealer did not match does not exist in the present cases. Consequently, the Court does not consider the decision of the Bombay High Court in *Mahalaxmi Cotton Ginning Pressing and Oil Industries* (*supra*) to be of assistance to the Department. The fact that the SLP against the said decision was dismissed by the Supreme Court does not alter the position.

47.1 Turning now to the decision of the Madras High Court in *Jayam & Co.*

v. Assistant Commissioner (supra), it is seen that in the said case, the parties agreed that the sale/purchase price as reflected in the invoice would be the gross price. Discounts would later be passed by way of credit notes. The Madras High Court held that, insofar as the Tamil Nadu Value Added Tax ('TNVAT') was concerned, the dealer had to produce a tax invoice evidencing the amount of input tax. It was further held that discount passed on through credit notes could not be considered for determination of 'price' and that the "tax invoice alone" ought to be considered for determining the tax liability.

47.2 The provision under challenge in *Jayam & Co. v. Assistant Commissioner (supra)* was Section 19 (20) of the TNVAT Act which reads as under:

"(20) Notwithstanding anything contained in this section, where any registered dealer has sold goods at a price lesser than the price of the goods purchased by him, the amount of the input tax credit over and above the output tax of those goods shall be reversed."

47.3 Here again, it can be seen that Section 9 (2) (g) of the DVAT Act is differently worded. Three conditions that were mandated by the above provision as noted by the Supreme Court were as under:

"(a) ITC is a form of concession provided by the Legislature. It is not admissible to all kinds of sales and certain specified sales are specifically excluded.

(b) Concession of ITC is available on certain conditions mentioned in this Section.

(c) One of the most important condition is that in order to enable the dealer to claim ITC it has to produce original tax

invoice, completed in all respect evidencing the amount of input tax.”

47.4 The Court in **Jayam & Co.** went strictly by the wording of the above provision to determine what would form the subject matter of the tax liability and concluded that it was only the price indicated in the tax invoice and not price as reduced by the credit note. The Court fails to appreciate how the aforementioned decision can be of any assistance to the Department in the present case since the provision which the Court is concerned with herein is in a different context and, therefore, differently worded as well.

48. The decision of the Supreme Court in **Corporation Bank** (*supra*) applies to the present case on all fronts. The Court explained there that the selling dealer collects tax as an agent of the Government. Therefore, the *bona fide* buyer cannot be put in jeopardy when he has done all the law requires him to do so. The purchasing dealer has no means to ascertain and secure compliance by the selling dealer. Again, in **Central Wines, Hyderabad** (*supra*) the Supreme Court *inter alia* observed that “the Seller acts as an agent of the buyer while collecting the tax”.

Reading down

49. The question that next arises is whether Section 9 (2) (g) of the DVAT Act, for reasons already explained, requires to be struck down as violative of Article 14 or can be saved from invalidity by any known interpretational device?

50. The offending part of Section 9 (2) (g) of the DVAT Act is the

expression ‘the dealers or class of dealers’ occurring therein which, as it presently stands, makes no distinction between selling and purchasing dealers and further between *bona fide* purchasing dealers and those not bonafide.

51. In ***Delhi Transport Corporation v. DTC Mazdoor Congress AIR 1991 SC 101***, a Constitution Bench of the Supreme Court explained in what cases the doctrine of ‘reading down’ of statutes to save their constitutionality could be deployed:

“The doctrine of reading down or of recasting the statute can be applied in limited situations. It is essentially used, firstly, for saving a statute from being struck down on account of its unconstitutionality. It is an extension of the principle that when two interpretations are possible--one rendering it constitutional and the other making it constitutional the former should be preferred. The unconstitutionality may spring from either the incompetence of the legislature to enact the statute or from its violation of any of the provisions of the Constitution. The second situation which summons its aid is where the provisions of the statute are vague and ambiguous and it is possible to gather the intention of the legislature from the object of the statute, the context in which the provision occurs and the purpose for which it is made. However, when the provision is cast in a definite and unambiguous language and its intention is clear, it is not permissible either to mend or bend it even if such recasting is in accord with good reason and conscience. In such circumstances, it is not possible for the Court to remake the statute. Its only duty is to strike it down and leave it to the legislature if it so desires, to amend it. If the remaking of the statute by the courts is to lead to its distortion that course is to be scrupulously avoided. The doctrine can never be called into play where the statute requires extensive additions and deletions.”

52. It was further explained in the same decision as under:

“The Courts, though, have no power to amend the law by process of interpretation, but do have power to mend it so as to be in conformity with the intendment of the legislature. Doctrine of reading down is one of the principles of interpretation of statute in that process. But when the offending language used by the legislature is clear, precise and unambiguous, violating the relevant provisions in the constitution, resort cannot be had to the doctrine of reading down to blow life into the void law to save it from unconstitutionality or to confer jurisdiction on the legislature.”

Conclusions

53. In light of the above legal position, the Court hereby holds 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 in accordance with Section 50 of the Act where there is no mismatch of the transactions in Annexures 2A and 2B. Unless the expression ‘dealer or class of dealers’ in Section 9 (2) (g) is ‘read down’ in the above manner, the entire provision would have to be held to be violative of Article 14 of the Constitution.

54. The result of such reading down would be that the Department is precluded from invoking Section 9 (2) (g) of the DVAT to deny ITC to a purchasing dealer who has *bona fide* entered into a purchase transaction with a registered selling dealer who has issued a tax invoice reflecting the TIN number. 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.

55. Resultantly, the default assessment orders of tax, interest and penalty issued under Sections 32 and 33 of the DVAT Act, and the orders of the OHA and Appellate Tribunal insofar as they 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, and which have been challenged in each of the petitions, are hereby set aside.

56. The writ petitions and applications are disposed of in the above terms but, in the circumstances, with no orders as to costs.

S. MURALIDHAR, J.

CHANDER SHEKHAR, J.

OCTOBER 26, 2017

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