



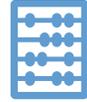
Cross Charge, Input Service Distributor - Issues & Precautions

- CA Ravi Kumar Somani

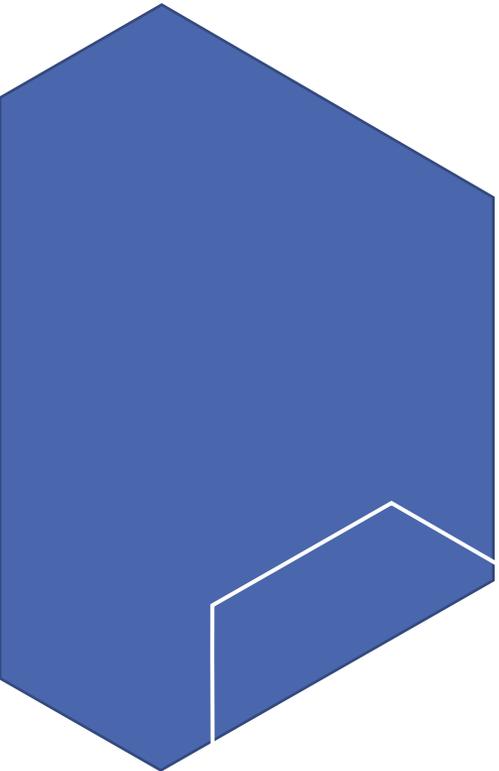


“GST has left women relieved. At least, now men have something other than them that they don’t understand but would still follow!”

GST - Current Trends

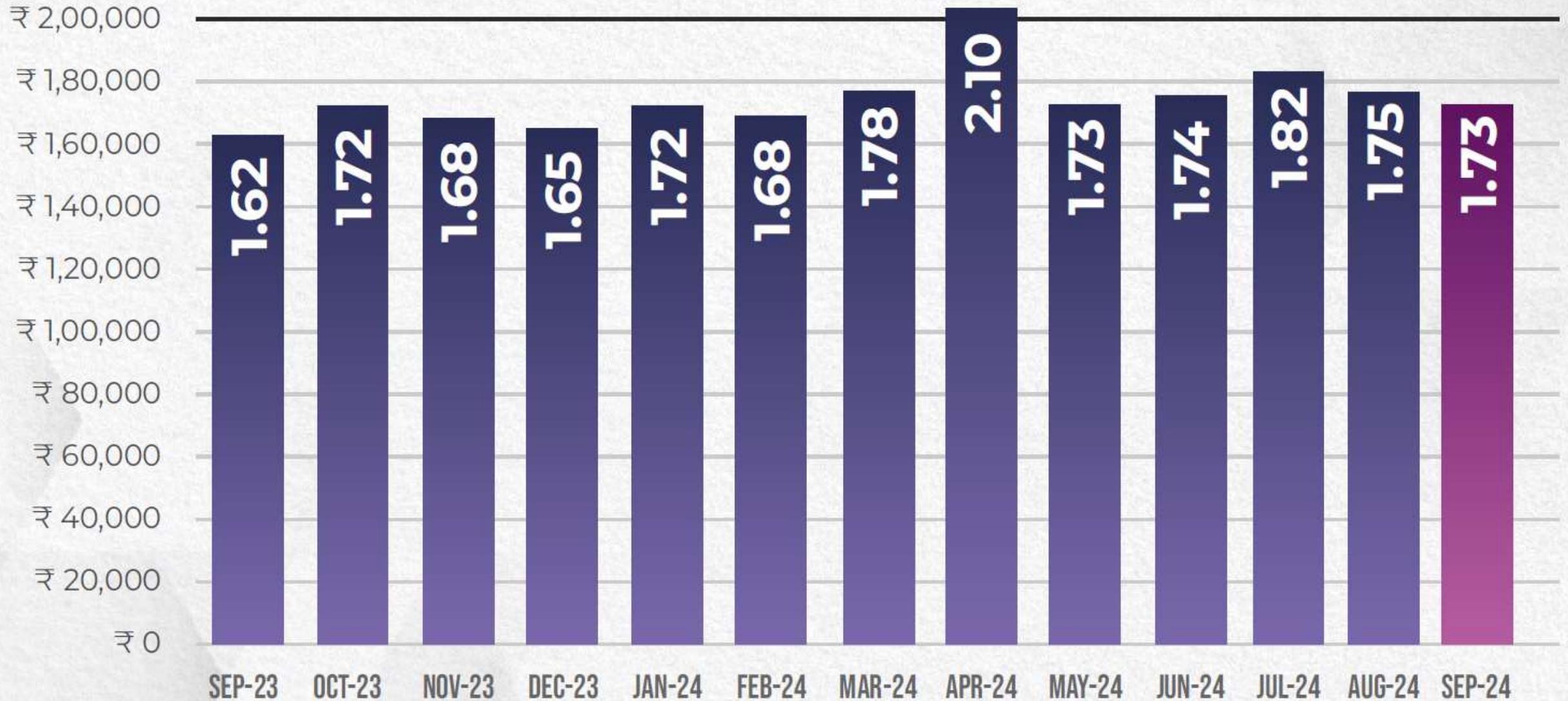


- ❑ Excessive litigation at all levels - GST officials issued a little under **1.13 lakh show-cause notices** to tax-payers in 2023-24, but classification disputes on tax rates were behind just **555 of those notices**.
- ❑ *Over the past three financial years the number of alleged evasion cases filed by just the Directorate General of GST Intelligence has **almost doubled to 23,000**, with a fourfold rise in the **amounts involved to 4.34 trillion rupees (\$51.9 billion)**.*
- ❑ *From PepsiCo, BMW, Uber, Infosys, Mahindra, gaming startups - they are all embroiled in GST litigation that could take years to resolve and add to the cost of doing business in India.*
- ❑ Design Challenge in Dual Administration –Unlimited Trouble.



GST COLLECTION TREND OF LAST ONE YEAR

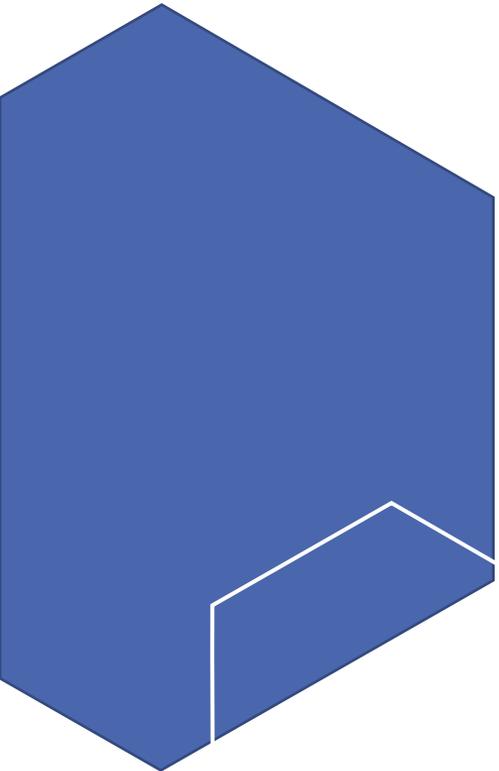
(IN RUPEES LAKH CRORE)



GST - Current Trends



- Excessive compliance burden – Only to increase.. ISD, Increased reporting, vendor/ customer follow-ups etc.
- B2C E-invoicing, Invoice Management System, GSTR 1A, Credit Notes matching functionality.
- Honeymoon of GST era now comes to end – Real party now begins!!!
- Have you taken back-up of GST Returns filed?? Old data to be archived - Data to be archived beyond 7 years.
- Supreme Court judgment by Safari Retreats - What is 'Plant'



ISD MECHANISM MADE MANDATORY FROM 01ST APRIL 2025

MINISTRY OF FINANCE

(Department of Revenue)

(CENTRAL BOARD OF INDIRECT TAXES AND CUSTOMS)

NOTIFICATION

New Delhi, the 6th August, 2024

No. 16/2024–Central Tax

S.O. 3161(E).—In exercise of the powers conferred by clause (b) of sub-section (2) of section 1 of the Finance Act, 2024 (8 of 2024), the Central Government hereby appoints, —

- (a) the 1st day of October, 2024, as the date on which the provisions of sections 13 of the said Act shall come into force;
- (b) the 1st day of April, 2025, as the date on which the provisions of sections 11 and 12 of the said Act shall come into force.

[F. No. CBIC-20006/20/2023-GST]

RAGHAVENDRA PAL SINGH, Director

- ❑ Background of ISD provisions before the proposed amendment,
- ❑ Proposed changes in Legal provisions related to ISD,
- ❑ Analysis of changes due to amendments,
- ❑ Interplay between ISD and Cross Charge,
- ❑ Steps to be taken for implementation of the ISD mechanism,
- ❑ Compliances for ISD entity, Flow of ISD return, manner of distribution of ITC,
- ❑ Certain Issues in the implementation process

ISD Timeline (At a glance)



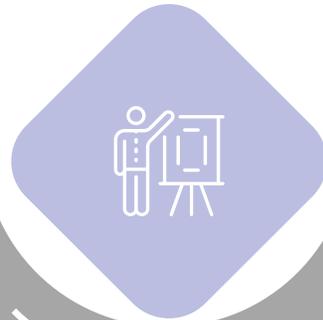
50TH GST COUNCIL

ISD NOT YET
MANDATORY



INTRODUCTION OF ISD

INTRODUCTION OF
ISD



52ND GST COUNCIL

ISD TO BE MADE
MANDATORY
PROSPECTIVELY



CIRCULAR 199/11/2023

CLARIFICATION ON
TAXABILITY OF
SERVICES -CROSS
CHARGE V/S ISD



FINANCE ACT, 2024

ISD MADE
MANDATORY IN
CASE OF MULTIPLE
REGISTRATION



ISD Definition as per Section 2(61) of CGST Act, 2017 (Old definition)

- *“Input Service Distributor” means **an office** of the supplier of goods or services or both which receives tax invoices issued under section 31 towards the receipt of **input services** and issues a prescribed document for the purposes of distributing the credit of central tax, State tax, integrated tax or Union territory tax paid on the said services to a supplier of taxable goods or services or both having the same Permanent Account Number as that of the said office;*

Proposed new definition:

- 2(61) *“Input Service Distributor” means **an office** of the supplier of goods or services or both which receives tax invoices towards the receipt of input services, **including invoices in respect of services liable to tax under sub-section (3) or sub-section (4) of section 9, for or on behalf of distinct persons** referred to in section 25, and **liable to distribute** the input tax credit in respect of such invoices in the manner provided in section 20;*

- The Input Service Distributor **may distribute** the credit subject to the following conditions, namely:
- a. the credit can be distributed to the recipients of credit against a document containing such details as may be prescribed;
 - b. the amount of the credit distributed shall not exceed the amount of credit available for distribution;
 - c. the credit of tax paid on input services **attributable to a recipient** of credit shall be distributed only to that recipient;
 - d. the credit of tax paid on input services **attributable to more than one recipient of credit** shall be distributed amongst such recipients to whom the input service is attributable and such distribution shall be pro rata **on the basis of the turnover in a State** or turnover in a Union territory of such recipient, during the relevant period, to the aggregate of the turnover of all such recipients to whom such input service is attributable and **which are operational in the current year**, during the said relevant period;

- e. *the credit of tax paid on input services **attributable to all recipients** of credit shall be distributed amongst such recipients and such distribution shall be pro rata on the basis of the turnover in a State or turnover in a Union territory of such recipient, during the relevant period, to the aggregate of the turnover of all recipients and **which are operational in the current year**, during the said relevant period.*

- f. *(g) the Input Service Distributor shall, in accordance with the provisions of clause (d) and (e), separately distribute **the amount of ineligible input tax credit** (ineligible under the provisions of sub-section (5) of section 17 or otherwise) and the amount of eligible input tax credit;*

- ITC in respect of a recipient located in the same State/ UT to be distributed as central tax and State tax or Union territory tax respectively and ITC in respect of a recipient located in a State/ UT other than that of the ISD, shall be distributed as integrated tax,
- Additions/ reductions to the originally distributed credit must be carried out by way of a debit note/ credit note,
- Credit Note to be shall be apportioned to each recipient in the same ratio in which the input tax credit contained in the original invoice was distributed,
- If ITC is to be reduced later or distributed to a wrong recipient, the same needs to be corrected by way of a DN/ CN
- For RCM transactions, a registered person, having the same PAN and State code as the ISD, may issue invoice/ CN/ DN to transfer the credit of such common input services, and such credit shall be distributed by the said ISD in the manner as provided above

- The turnover computation for the purpose of distribution shall be as under:
 - i. if the recipients of credit have turnover in their States/ UT in the financial year preceding the year during which credit is to be distributed, the said financial year; or
 - ii. if some or all recipients of the credit do not have any turnover in their States/ UT in the financial year preceding the year during which the credit is to be distributed, **the last quarter for which details of such turnover of all the recipients are available, previous to the month during which credit is to be distributed;**
- The term “**turnover**”, in relation to any registered person engaged in the supply of taxable goods as well as goods not taxable under this Act, means the value of turnover, reduced by the amount of any duty or tax levied under [entries 84 and 92A] of List I of the Seventh Schedule to the Constitution and entries 51 and 54 of List II of the said Schedule.

- **Section 21 of CGST Act, 2017** explains the manner and procedure for recovery of wrong input tax credit distributed by the ISD.
- Where it is mentioned that in case ISD wrongly distributes excess ITC to the recipient then the excess credit shall be recovered from the recipient along with interest and the provisions of section 73 or section 74, as the case may be, shall, mutatis mutandis, apply for determination of amount to be recovered.
- **General penalty under section 122(1)(ix) of CGST Act, 2017 would also be applicable on ISD.**

- 50th GST Council meeting recommended to clarify through a circular no. 199 as under:-
 - ✓ ISD mechanism is not mandatory for distribution of ITC on common input services procured from third parties,
 - ✓ To clarify issues regarding taxability of **internally generated services** provided by one distinct person to another distinct person [branch offices of same entity].

- **Schedule-I:** Supply of goods or services or both between related persons or between distinct Persons as specified in section 25, when made in the course or furtherance of business
- **Schedule III:** Activities or transactions specified in Schedule III is treated neither as supply of goods nor as supply of service. Schedule III includes **services by an employee to an employer in course of furtherance of business.**
- **AAR:** Columbia Asia Pvt Ltd [2018 – TIOL – 113 – AAR – GST and upheld by the appellate authority in [2018-TIOL-31-AAAR-GST] - *Regarding the second issue related to the activities performed by the employees at the corporate office in the course of or in relation to employment, the employees employed in the Corporate Office are providing services to the Corporate Office and hence there is an employee-employer relationship only in the IMO. The other offices are distinct persons and therefore the employees in the IMO have no employer employee relationship with other offices.*

- CBIC clarified on various aspects surrounding the issue vide Circular 199/11/2023-GST dated 17th July 2023.
- **Scenario 1: Services procured from a third party**
 - HO would have an option to distribute such ITC either through cross charge or ISD mechanism.
 - In both the above mechanism, i.e., ISD and Cross Charge, the ITC could be distributed or transferred only if such services are attributable to the concerned BO's.
 - For the above option, it was clarified that BO is eligible for Full ITC: the value of supply declared in the invoice will be the final value whether employee cost, has been considered or not.
 - If BO is not eligible for Full credit - the value of supply per valuation rules to be taken excluding employee cost

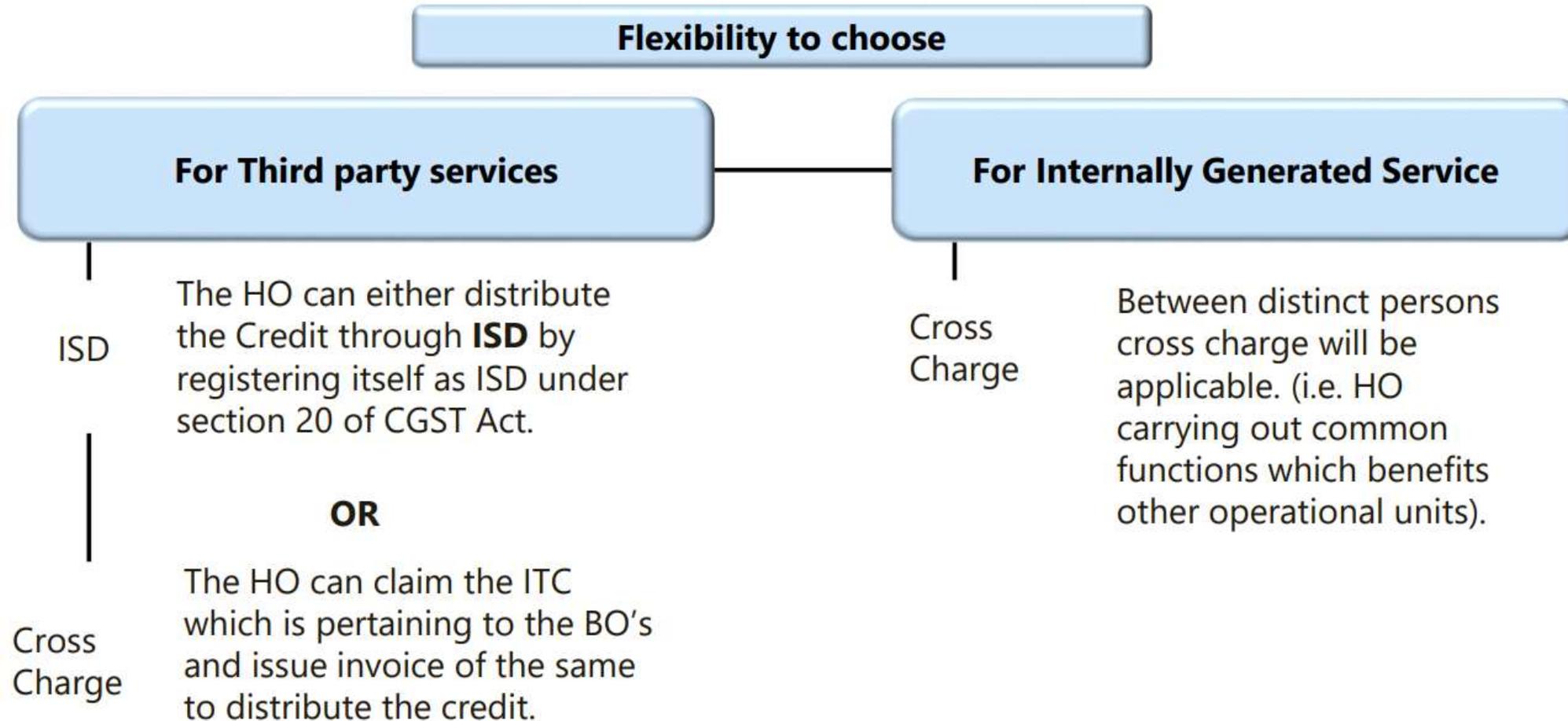
Scenario 2: In respect of Internally Generated Services, Where HO is providing certain services to BOs.

- It is clarified that the value of supply of service made by the registered person to a distinct person i.e., HO to BO will be determined as per rule 28 of CGST rules read with Section 15(4) of CGST Act, 2017 accordingly.
- **If BO is eligible for Full ITC:** the value of supply declared in the invoice will be the final value whether employee cost, has been considered or not.
- **If BO is not eligible for Full credit-** the value of supply per valuation rules is to be taken excluding employee cost.

- Taxpayers can follow the methodology of ISD, Cross Charge, or both, at their option,
- However, an invoice could be issued/ ITC could be distributed to the recipient BO's if such common expenses are attributable to them.
- Where full ITC is available, if no invoice is issued, the value would be accepted as “NIL”.
- In case where the recipient is not eligible for Full ITC, the valuation gets sticky – whether to be computed qua the transaction or qua the person??
- In the case of transfer of goods, the same is covered by a cross charge as ISD is restricted only for ‘Service’ distribution.

ISD v/s Cross charge (Current)

- Current valuation scenario



Manner of distribution of ISD as amended vide Finance Act, 2024

Proposed new law:

- 2(61) “Input Service Distributor” means **an office** of the supplier of goods or services or both which receives tax invoices towards the receipt of input services, **including invoices in respect of services liable to tax under sub-section (3) or sub-section (4) of section 9, for or on behalf of distinct persons** referred to in section 25, and **liable to distribute** the input tax credit in respect of such invoices in the manner provided in section 20;
- “20. (1) Any office of the supplier of goods or services or both which receives tax invoices towards the receipt of input services, including invoices in respect of services liable to tax under sub-sections (3) or (4) of Section 9, **for or on behalf of a distinct person or distinct persons** as specified in section 25, **shall be required** to be registered as Input Service Distributor under clause (viii) of section 24 of this Act and shall distribute the input tax credit in respect of such invoices.

Summary of Above Provisions

Sr. No.	Nature of Transaction	Parameters	Existing Process	Process under ISD
1	Third Party Invoices which are common for one or more branches	Transactions liable for forward charge mechanism (FCM)	Cross charge is done from HO location on the basis of turnover for the month. Entire taxable value & taxes are cross-charged.	Merely GST component would be distributed among the branches whereby the ISD would act as a pass-through gateway.
		Transactions liable for reverse charge mechanism (RCM)	For common RCM services, the HO location would pay the RCM and cross charge the invoice to other locations.	Process given in Rule 54(1A) would be required to be followed whereby the regular registration in the state in which ISD is taken i.e., HO regular registration would pay the RCM and transfer the same to ISD for further distribution.
		Ineligible ITC (FCM)	At present the ITC on these transactions are not cross-charged to the branches and are consumed by HO state	The ineligible ITC would be required to be distributed among the branches on the basis of the turnover

Summary of Above Provisions

Sr. No.	Nature of Transaction	Parameters	Existing Process	Process under ISD
1	Third Party Invoices which are common for one or more branches	Ineligible ITC (RCM)	At present the tax is paid by the HO location & ITC on these transactions are not cross-charged to the branches and is consumed by the HO state	Process given in Rule 54(1A) would be required to be followed whereby the regular registration in the state in which ISD is taken i.e., HO regular registration would pay the RCM and transfer the same to ISD for further distribution. The said ITC would be required to first fully avail in HO state and then to be distributed. The receiving branches would avail & reverse the said credit.
		Documentation	Tax invoice as per Section 31	Invoice as per Rule 54 & 54(1A). One invoice for eligible transaction & another for ineligible transaction would be required for each state

Summary of Above Provisions

Sr. No.	Nature of Transaction	Parameters	Existing Process	Process under ISD
2	Internally Generated Services	Tax treatment	Cross-charge is done on the monthly basis through monthly returns.	<p>As provided in Circular 199/11/2023, the value of internally generated services can be nil if a full input tax credit is available to the recipients.</p> <p>Alternatively, if it decides to cross-charge certain common expenses then such expenses would exclude the third party common service invoices and the employee cost. The remaining expenses would be cross-charged to the recipients.</p> <p>We shall suggest entering into an MoU between HO & Branches.</p>

Comparison of expenses Covered in ISD or CC

- To identify that we need to bifurcate the common expenditure that externally procured expenses that are not directly attributable to branches and internally generated service.

Expenses	Category (Externally /internally)	ISD	Cross Charge	Remarks
Internal Audit services, Statutory/ Tax Audit Service,	External	Yes	No	
Legal Service, Consultancy Fees Professional service	External	Yes	No	
Director Sitting Fees(RCM)	External	Yes	No	
Payroll processing service, HR and admin services	Internal	Yes/No	No/Yes	Except salary cost
Bank Charges	External	Yes	No	
Use of Capital Goods(Server)	Internal	No	Yes	
Advertisement , marketing , Business Promotion	External/Internal	Yes/No	No/Yes	
Ineligible ITC under section 17(5)	External	Yes	No	
Head office Rent	External	Yes/No	No/Yes	

- How are the RCM payments routed – What if the HO location does not have any manufacturing plant or service supplying unit??
- Impact of 16(2)(aa) on ISD ITC - Reconciliation of Form 6A mandatory? 2A/2B vis-à-vis 6A? Static or Dynamic? Permanent/ temporary reversals?
- If a particular branch is no longer supplying the goods or services, is the distribution still needed to be done for such a branch also? – Rules state '*which are operational during the current year*'.
- How do Time of Supply provisions impact the billing for IGS cross-charge transactions?
- ISD Registration to be at HO, a major manufacturing plant, or both? Regional office can also be registered as ISD – Jaypee Rewa Plant - 2007 (218) ELT 576 (Delhi - Trib.)
- ISD implications and IGS applicability in case of centralized or decentralized billing??

- What if a common bill is received towards the related persons in a group company having distinct persons – Bill received in ISD regn?? Or Bill received in regular GSTIN??
- Whether there would be change in the valuation of IGS cross charge where the third party element is already distributed through ISD – Shared service centre v/s Pure Third Party Bills?
- Implication in case of common expenses in Events/ Hotel Accommodations/ Rentals or other immovable property related services taken in the ISD office for all the suppliers.
- Fate of the HO expenses? Rent, Security, Housekeeping? Attributable to specific state or common?
- Whether attributability-based distribution is still relevant, or any other new mechanism is going to be prescribed? What if certain common services have different cost drivers & distribution based on turnover basis is not correct. For ex: Cost Apportionment based on Employees Head count or some other basis.

- Distribution towards exempt supply turnover in HO itself viz., Interest on loan and other incomes??
- Distribution of ineligible credits required? As per rule 39, it is to be separately distributed.
- What is the periodicity of distribution – monthly/ quarterly? What if the same is breached?
- Whether distribution required to be made to the distinct persons who are making the exempt supplies, what if HO also possesses certain specific exempt supplies??
- Whether the provisions of E-invoicing are applicable to the ISD invoice? – No as per FAQ dated 11.11.2020

- What happens if the supplier issues a credit note after the distribution of the credits – In the same ratio as that of the original invoice, to be adjusted in the month of CN and if negative, it gets added as an outward tax liability in the hands of the recipient.
- Jurisdiction of the regular registration & ISD registration? Needs to be same?
- Whether there would be a separate audit/ investigation/ scrutiny for ISD registration. Also, who shall be the proper officer for ISD registration?.
- Whether the distribution mechanism to be based on previous years turnover or would there be any change in the same.
- How to deal with incorrect distribution of credit subsequently noted viz., Short distribution, excess distribution etc. – Circular 71/45/2018 - GST

- Late Fees – Rs. 25/- per day per Act – N/N -7/2018-CT
- Reversal of common ITC used towards taxable and exempt - Rule 42/43 compliance
- Reversal of credits on account of delay in payment to vendors beyond 180 days - Rule 37.
- How to incorporate a nexus of input service with the concerned GST Number in the course of accounting itself.
- Mechanism of distribution of credits to SEZ.
- Changes needed in the agreements before the new provisions are implemented.

- Step 1: Download the monthly auto-populated return GSTR 6A. Which is auto-populated based on the invoices filed by the supplier in their GSTR 1. The tentative date on the 12th of next month for current month.
- Step 2: Reconcile the invoice booked in the current month with the current month GSTR 6A.
- Step 3: Reconcile the mismatched invoices of the previous month with the current month's GSTR 6A. Upon matching take the invoices in computation.
- Step 4: Eliminate the remaining mismatch entries from the computation of the current month ITC.
- Step 5: On the reconciled invoice list in the current month. Divide the invoices into eligible and ineligible credits.
- Step 6: Compute the ITC distribution based on the mechanism given in rule 39 of CGST₃₁ rule, 2017.

- Step 7: Raise the ISD invoice with a consecutive serial number on the last date of the month.
- Step 8: Report the identified invoices in step 5 in GSTR 6 of the current month in the respective table of form.
- Step 9: Report the details of the ISD invoice (eligible and ineligible) in the distribution table of Form GSTR 6.
- Step 10: Invoice reported for ITC available for distribution and ITC distributed (eligible or ineligible) should be equal.
- Step 11: Click on the compute ITC and file the return for the month.
- Step 12: Maintain the YTD reconciliation file between invoice booked and GSTR 6A.

- **GL Creation** -New GL's need to be created under ISD Registration being output ISD , input ISD and net ISD ledgers wherein at the end of each month the net ISD ledger needs to be nullified after disbursing the credit and liability.
- **Need to take a new registration under ISD**-A separate registration needs to be taken for ISD compliance.
- **Identification and communication to common vendors**-We will need to first identify vendors providing common services and accordingly communicate to them so that invoice is rightly raised on ISD number.
- **Monthly returns** - There will be a need to file separate returns under ISD in Form GSTR-6 along-with existing returns.

- **RCM transactions** - At present there is no existing provision laying out the distribution of ISD for RCM related transactions, thus the HO will need to communicate with the vendors accordingly and raise the invoice on HO, so that the HO can distribute the common RCM credit to respective BO's.
- **Training** - Requisite training will be needed to be given to the employees in this area.
- **IT changes** - We will need to undergo a lot of changes in IT like raising PO on ISD number, modifying the masters according to the new ISD GL created, new cost centre for common pool of ITC credit under ISD needs to be created.
- **Cut off date** - A cut off date is to be decided and the cut off procedures are required to be performed to ensure smooth transition.



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Thank you
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