

Input Service Distributor (ISD) vs Cross Charge

[Section 20 of CGST Act read with rule 39 and 54]

Before you read the below alert, please note this alert is important for only the following taxpayers and that it is mandatory to be followed from 1.04.2025:

- a. Who has multiple GSTINs under one company
- b. Who incurs common expenses at one Head/Branch office(s)
- c. This applies only to expenses relating to services and not goods

I. Brief background of the issues involved

Many businesses hold multiple GST registrations across various states, they have an administrative office in one state which is called the head office and rest all branch offices (for ease of reference we will also address them as HO and Branch). Many expenses relating to marketing, logistics, legal or statutory requirements and the likes are incurred from the HO whereas branch related localized expenses are incurred from the branch offices.

Under GST by now we all know that one is required to take registration in every state where one is supplying goods or services, so a company having single PAN may have multiple GST registrations which as per section 25 are called 'distinct persons'. This gives rise to the fact that HO incurs COMMON expenses, benefit of which goes to all or more than one branch. All these common expenses bear GST which is eligible for Input Tax Credit (ITC), as the invoice of these COMMON ITC is received by the HO, it is the one which is required to avail the ITC thereof in its GST returns. States questioned this fact that one state is getting all the ITC whereas the benefit of the underlying service is accrued to some other state and therefore the state having the HO is at a loss as cash payment of taxes reduces due to excess ITC availments.

To cover these apprehensions, GST law has been amended to make ISD mandatory from 1.04.2025 onwards, this alert tries to explain the concept, compliances involved and simplify the issue as much as we can.

II. Input Service Distributor vs Cross Charge

a. Cross Charge:

Taxpayers used to raise invoices from say HO to branch saying that certain services which were received by HO from a vendor are now being further supplied to the branch, thereby passing on the ITC from HO to that branch, this way of raising invoice between distinct persons is known as 'Cross Charge'.

b. Input Service Distributor (ISD)

Another way of passing on ITC by one GSTIN to another GSTIN (under same PAN) is through the mechanism of ISD, whereby the ITC is availed in an ISD GSTIN and passed on to the relevant branch by way of an ISD invoice. The concept of ISD has been in the statute book since the old Service tax days, however it was never made mandatory like it has been done now.

Please note that under ISD mechanism one is required to distribute ITC relating to common Input SERVICES only and ITC relating to procurement of goods for common use would not be subjected to ISD.

III. What's changing from 1.04.2025:

Issue	Action Required
Registration as ISD	: Any taxpayer (having single PAN) fulfilling ALL the following conditions will have to register as an ISD (hereinafter referred to as an HO) a. having more than 1 GST registration b. in 1 or more states

		c. incurring common service expenses and receiving those invoices in one GSTIN
Invoicing by supplying vendors	:	HO will have to ask all its vendors supplying common ITC to raise invoices in new ISD GSTIN, this exercise is of the utmost importance.
RCM related GST Payments	:	All COMMON RCM related GST payments (like sponsorship expense) will have to be done in HO GSTIN (not in HO ISD GSTIN) (See Note Below)
ITC reconciliation Form like GSTR 2A/2B	:	As we have GSTR 2A/2B for normal ITC, we will have GSTR 6A for ITC in case of ISD. When vendor uploads any invoice in its GSTR 1 in HO ISD GSTIN, it will be reflected in GSTR 6A of HO.
Ratio for Transfer of ITC by ISD <u>for existing GSTINs</u>	:	Ratio of Turnover of past financial year of all GSTINs held by the taxpayer will have to be calculated, so for FY 2025-26 one will have to take the turnover ratio of FY 2024-25.
Ratio for Transfer of ITC by ISD <u>if new GSTIN is added</u>	:	In case a new state GSTIN is taken say in FY 2025-26, then past years turnover ratio will be of no use. Turnover ratio of last quarter for which details of such turnover of all the GSTIN recipients are available, previous to the month during which credit is to be distributed.
Turnover Value	:	Turnover value for the purposes of calculation of ratio would be taken without any GST component.

IV. RCM related GST Payments by HO for common expenses

There may be situations where a common expense is incurred by HO which requires GST to be paid under RCM, for example a partnership firm having multiple GSTINs incurs sponsorship expense. Benefit of this expense is for all its GSTINs, hence the same will be handled as under:

- a. Vendor will raise normal invoice (without GST) on the HO.
- b. HO will prepare an invoice for transferring the ITC to its ISD GSTIN
- c. HO will declare this invoice in its GSTIN in B2B section – this means that its overall outward tax liability will now include this ISD invoice
- d. HO will declare the outward tax (including ISD tax) in its outward liability in GSTR 3B – Table 3.1 (a)
- e. HO will also declare the RCM liability in its GSTR 3B – Table 3.1 (d)
- f. HO will avail ITC of the RCM liability so declared.
- g. HO will pay the RCM liability in cash as was being done earlier
- h. ISD will then avail the ITC thereof and transfer the same in turnover ratio to eligible GSTINs by filing GSTR 6 return.

V. Method of Distribution of ITC by an ISD

- a. ITC available for distribution in a month shall be distributed in same month. One will not be allowed to carry forward any ITC to the next month.
- b. The amount of the ITC distributed shall not exceed the amount of ITC available for distribution.
- c. If an expense is incurred by HO exclusively for one branch then ITC relating to that expense will be distributed to that Branch only. Example – HO in Ahmedabad hired an interior designer to furnish an office in Mumbai. Designer raised an invoice on the HO ISD GSTIN. HO will have to transfer this ITC to Mumbai GSTIN only and not proportionately to all its GSTINs.

- d. ITC which relates to more than one branch but not all branches, will have to be distributed to only those branches which it relates to by taking a ratio of aggregate turnover of those branches only.
- e. ITC relating to all branches shall be distributed on pro rata basis to all branches in their respective turnover ratio.
- f. Formula for distribution of ITC would be as under:

$$C_1 = (t_1 / T) \times C$$

where,

"C" is the amount of credit to be distributed,

"t₁" is the turnover of the branch, and

"T" is the aggregate of the turnover, during the relevant period, of all recipients to whom the input service is attributable

- g. ISD shall have to distribute eligible and ineligible ITC to all the relevant branches. Once the branch receives an ineligible ITC say for example ITC relating to construction, will then have to first avail the ITC and then reverse the same in its GSTR 3B.
- h. Distribution of various taxes will happen as under:
 - A.** If the HO and Branch are in 2 DIFFERENT STATES:
 - a. IGST as IGST
 - b. CGST as IGST
 - c. UTGST / SGST as IGST
 - B.** If the HO and Branch are in SAME STATE:
 - a. IGST as IGST
 - a. CGST as CGST
 - b. SGST as SGST / UTGST as UTGST

- i. **ISD shall issue an ISD Invoice for transferring ITC to branch. See detailed note on invoice below.**
- j. In case a vendor issues a credit note to HO ISD GSTIN, it will further issue Credit notes to branches in same ratio as was the original ITC which was transferred earlier.
- k. Same shall be the case with debit note issued by a vendor.
- l. ISD will have to file return in form GSTR 6 every month to distribute the ITC, all ISD invoices will be reported in this return. Said return will have to be filed on or before 13th of the next month.

VI. Invoice or Credit Note of an ISD shall be as under:

Normal ISD Invoice or ISD Credit Note shall contain following details

- a. ISD Name, GSTIN and address
- b. Maximum 16 digits serial number unique to a financial year
- c. Date of issue
- d. Name, GSTIN and address of the Branch to whom credit is distributed
- e. Amount of credit being distributed
- f. Signature – Physical or digital, of the ISD or his authorised representative

Invoice, Debit Note or Credit note for transferring RCM ITC by HO GSTIN to an ISD

- a. Name, GSTIN and address of HO who has paid RCM tax
- b. Maximum 16 digits serial number unique to a financial year
- c. Date of issue
- d. GSTIN of original supplier (of the RCM related common service) and its original invoice number whose credit is sought to be transferred to the Input Service Distributor Amount of credit being distributed.

- e. Name, address and GSTIN of ISD
- f. Taxable value, rate and amount of the credit to be transferred
- g. Signature – Physical or digital
- h. The taxable value in the invoice issued by HO GSTIN to ISD shall be the same as the value of the common services on which RCM is paid.

One can choose to make one invoice for transferring RCM ITC to the ISD GSTIN which can have all the above information as an annexure.

Abstract of provisions from CGST Act and rules relevant to this alert are placed at **Annexure A** appended at the end.

VII. Suggestive list of common expenses which may be subjected to ISD:

The following is merely a suggestive list of expense heads, please note only ITC relating to those expenses will have to be transferred through ISD mechanism benefit of which accrues to 2 or more GSTINs of the organisation. If an expense is incurred by HO (invoice is received in HO GSTIN) and the benefit thereof accrues only to that HO, in that case ITC relating to it will not have to be transferred through ISD.

- a. Statutory Audit.
- b. Common IT infrastructure set up and maintenance expenses
- c. Advertisement / Sales promotion / Branding expenses
- d. Annual General Meeting Expenses
- e. CSR expenses
- f. Banking related Charges
- g. Internet Expense (if the same is utilized commonly for entire business)
- h. Legal & professional Fees (if common for all branches – one will have to sift through each invoice and mark it common for all, common for few branches or only for HO)

- i. License and Royalty Expenses
- j. Listing Fees
- k. Membership, Subscription charges
- l. Rent, Hire and Lease Expense
- m. Research and Development Expenses
- n. Software Expense (including AMC)
- o. Travelling Expense
- p. Website Handling charges

VIII. Conclusion / Opinion

Since tax was introduced by mankind, any policy change therein was driven by any one or both of the following attributes:

- a. Augmenting / increasing tax revenue
- b. Bringing qualitative and positive changes in taxpayer's experience

We personally don't see how any of the above attributes are being achieved by making this humongous policy change. It is a settled principle that ISD mechanism doesn't result in increase in revenue, I may concede this much that some consuming states may see small increase in cash revenue but then the question that must be answered by the policy makers is, was such a huge amendment in law like this warranted for such small distributive revenue change. Should the taxpayers who are already under a mountain of compliance be forced to comply with one more set of compliances? This in our view is completely unwarranted and asymmetric policy intervention. Come April 2025, taxpayers will soon be faced with unnecessary paperwork, mounting compliances and mistakes which are inevitable in this flawed law, will result in litigation for ages.

Who will decide whether an expense is 'common', whether it is beneficial to any or all branch, will the officers who assess have the requisite knowledge to make such decisions.

Dare one say “ONE NATION ONE TAX” – we are 32 state countries fighting for tax from one hapless taxpayer base.

Once these 32 state country governments realize the unforeseen outcome of this change, I believe it will be rolled back ‘in the larger interest of public’ on ‘as is where is basis’, it may take 2 years or more but it will be rolled back. It’s a prophecy we would really like to come true.

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Annexure A

Abstract of provisions from CGST Act and rules relevant to this discussion:

From 1.07.2017 to 31.03.2025

2(61) "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;"

From 1.04.2025 onwards

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;]

Section 20 From 1.04.2025 onwards

Manner of distribution of credit by Input Service Distributor.

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-section (3) or sub-section (4) of section 9, for or on behalf of distinct persons referred to in section 25, **shall be required to be registered as Input Service Distributor** under clause (viii) of section 24 and **shall distribute the input tax credit** in respect of such invoices.

(2) The Input Service Distributor shall distribute the credit of central tax or integrated tax charged on invoices received by him, including the credit of central or integrated tax in respect of services subject to levy of tax under sub-section (3) or sub-section (4) of section 9 paid by a distinct person registered in the same State as the said Input Service Distributor, in such manner, within such time and subject to such restrictions and conditions as may be prescribed.

(3) The credit of central tax shall be distributed as central tax or integrated tax and integrated tax as integrated tax or central tax, by way of issue of a document containing the amount of input tax credit, in such manner as may be prescribed.]

Procedure as per Rule 39

Rule 39. Procedure for distribution of input tax credit by Input Service Distributor.-

1[(1) An Input Service Distributor shall distribute input tax credit in the manner and subject to the following conditions, namely: —

- (a) the input tax credit available for distribution in a month shall be distributed in the same month and the details thereof shall be furnished in FORM GSTR-6 in accordance with the provisions of Chapter VIII of these rules;
- (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) the input tax credit that is required to be distributed in accordance with the provisions of clause (d) and (e) to one of the recipients "R1", whether registered or not, from amongst the total of all the recipients to whom input tax credit is attributable, including the recipients who are engaged in making exempt supply, or are otherwise not registered for any reason, shall be the amount, "C1", to be calculated by applying the following formula -

$$C1 = (t1 / T) \times C$$

where,

"C" is the amount of credit to be distributed,

"t1" is the turnover, as referred to in clause (d) and (e), of person R1 during the relevant period, and

"T" is the aggregate of the turnover, during the relevant period, of all recipients to whom the input service is attributable in accordance with the provisions of clause (d) and (e);

- (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;*
- (h) the input tax credit on account of central tax, State tax, Union territory tax and integrated tax shall be distributed separately in accordance with the provisions of clause (d) and (e);*
 - (i) the input tax credit on account of integrated tax shall be distributed as input tax credit of integrated tax to every recipient;*
 - (j) the input tax credit on account of central tax and State tax or Union territory tax shall—*
 - (i) in respect of a recipient located in the same State or Union territory in which the Input Service Distributor is located, be distributed as input tax credit of central tax and State tax or Union territory tax respectively;*
 - (ii) in respect of a recipient located in a State or Union territory other than that of the Input Service Distributor, be distributed as integrated tax and the amount to be so distributed shall be equal to the aggregate of the amount of input tax credit of central tax and State tax or Union territory tax that qualifies for distribution to such recipient as referred to in clause (d) and (e);*
 - (k) the Input Service Distributor shall issue an Input Service Distributor invoice, as provided in sub-rule (1) of rule 54, clearly indicating in such invoice that it is issued only for distribution of input tax credit;*
 - (l) the Input Service Distributor shall issue an Input Service Distributor credit note, as provided in sub-rule (1) of rule 54, for reduction of credit in case the input tax credit already distributed gets reduced for any reason;*
 - (m) any additional amount of input tax credit on account of issuance of a debit note to an Input Service Distributor by the supplier shall be distributed in the manner and subject to the conditions specified in clauses (a) to (j) and the amount attributable to any recipient shall be calculated in the manner provided in clause (f) and such credit shall be distributed in the month in which the debit note is included in the return in FORM GSTR-6;*
 - (n) any input tax credit required to be reduced on account of issuance of a credit note to the Input Service Distributor by the supplier shall be apportioned to each recipient in the same ratio in which the input tax credit contained in the original invoice was distributed in terms of clause (f), and the amount so apportioned shall be—*
 - (i) reduced from the amount to be distributed in the month in which the credit note is included in the return in FORM GSTR-6; or*
 - (ii) added to the output tax liability of the recipient where the amount so apportioned is in the negative by virtue of the amount of credit under distribution being less than the amount to be adjusted.]*

(1A) For the distribution of credit in respect of input services, attributable to one or more distinct persons, subject to levy of tax under sub-section (3) or (4) of section 9, a registered person, having the same PAN and State code as an Input Service Distributor, may issue an invoice or, as the case may be, a credit or debit note as per the provisions of sub-rule(1A) of rule 54 to transfer the credit of such common input services to the Input Service Distributor, and such credit shall be distributed by the said Input Service Distributor in the manner as provided in sub-rule (1).]

(2) If the amount of input tax credit distributed by an Input Service Distributor is reduced later on for any other reason for any of the recipients, including that it was distributed to a wrong recipient by the Input Service Distributor, the process specified in 3[clause (n)] of sub-rule (1) shall apply, mutatis mutandis, for reduction of credit.

(3) Subject to sub-rule (2), the Input Service Distributor shall, on the basis of the Input Service Distributor credit note specified in 4[clause (l)] of sub-rule (1), issue an Input Service Distributor invoice to the recipient entitled to such credit and include the Input Service Distributor credit note and the Input Service Distributor invoice in the return in FORM GSTR-6 for the month in which such credit note and invoice was issued.

Explanation. — For the purpose of this rule, —

(i) the term “relevant period” shall be—

(a) if the recipients of credit have turnover in their States or Union territories in the financial year preceding the year during which credit is to be distributed, the said financial year; or

(b) if some or all recipients of the credit do not have any turnover in their States or Union territories 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;

(ii) the expression “recipient of credit” means the supplier of goods or services or both having the same Permanent Account Number as that of the Input Service Distributor;

(iii) 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.]

Rule 54. Tax invoice in special cases.-

(1) An Input Service Distributor invoice or, as the case may be, an Input Service Distributor credit note issued by an Input Service Distributor shall contain the following details:-

(a) name, address and Goods and Services Tax Identification Number of the Input Service Distributor;

(b) a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters hyphen or dash and slash symbolised as "-", "/" respectively, and any combination thereof, unique for a financial year;

(c) date of its issue;

(d) name, address and Goods and Services Tax Identification Number of the recipient to whom the credit is distributed;

(e) amount of the credit distributed; and

(f) signature or digital signature of the Input Service Distributor or his authorised representative:

Provided that where the Input Service Distributor is an office of a banking company or a financial institution, including a non-banking financial company, a tax invoice shall include any document in lieu thereof, by whatever name called, whether or not serially numbered but containing the information as mentioned above.

[(1A) (a) A registered person, having the same PAN and State code as an Input Service Distributor, may issue an invoice or, as the case may be, a credit or debit note to transfer the credit of common input services to the Input Service Distributor, which shall contain the following details:-

(i) name, address and Goods and Services Tax Identification Number of the registered person having the same PAN and same State code as the Input Service Distributor;

(ii) a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters -hyphen or dash and slash symbolised as "-" and "/" respectively, and any combination thereof, unique for a financial year;

(iii) date of its issue;

(iv) Goods and Services Tax Identification Number of supplier of common service and original invoice number whose credit is sought to be transferred to the Input Service Distributor;

(v) name, address and Goods and Services Tax Identification Number of the Input Service Distributor;

(vi) taxable value, rate and amount of the credit to be transferred; and

(vii) signature or digital signature of the registered person or his authorised representative.

(b) The taxable value in the invoice issued under clause (a) shall be the same as the value of the common services.]