Input Service Distributor and Concept of Cross Charge

1. Introduction.

As per section 2(61) of the CGST Act, "Input Service Distributor" has following characteristics

- It is an office of the supplier of goods or services or both
- It receives tax invoices issued under section 31 towards the receipt of input services
- It 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
- Such document is issued to a supplier of taxable goods or services or both having the same Permanent Account Number as that of the said office.

Section 24 of the CGST Act (read with rule 8 of CGST Rules, 2017), requires an office of the supplier which intends to act as Input Service Distributor (ISD), to separately obtain registration as ISD. In other words, a registration number of an establishment as an ISD is different from the registration number of such establishment u/s 22 of the Act. Rule 54 of the CGST Rules, 2017 deals with the prescribed document to be issued by ISD for the purpose of distribution of credit. Section 20 of the CGST Act(read with Rule 39 of GST Rules), contains provisions relating to manner of distributing the credit by ISD. Section 39(4) of the CGST Act read with Rule 65 of the CGST Rules, provides for filing of return by ISD, for every calendar month, within 13 days after the end of such month.

2. Concept of ISD

2.1. As explained above, ISD is an office of supplier of goods and services. A supplier may have number of establishments located in different States, however, as regards input services, a supplier may insist for obtaining invoices in the name of its one central location, irrespective of which establishment has actually received the services. The purpose could be centralized accounting or centralized payment system.

Ex: ABC Ltd may have head office in Mumbai and establishments in Delhi, Chennai and Kolkata. Although certain services are received at Delhi, an invoice may be issued in the name and address of Mumbai Head Office. Let's say a supplier P in Delhi makes an intra-State supply (CGST+SGST) and supplier Q of Gujarat makes an inter-state supply (IGST) to Delhi establishment, however, invoices are raised in the name of corporate office at Mumbai.

2.2. The provisions of section 16 of CGST Act provides that, no registered person shall be entitled to a credit in respect of any supply of goods or services or both to him unless, he is in possession of a tax invoice or debit note issued by a supplier registered under this Act, or such other taxpaying documents as may be prescribed. Therefore, in such case, although the services are received by various establishments (ex: Delhi), it would not be possible for such establishments to claim the credit, as the invoice will be issued in the name of central office of such person (i.e. Maharashtra). The head office also cannot avail the credit as they are not actual recipient of such inward services.

2.3. Under the scheme of ISD, Rule 36 of the CGST Rules permits such ISD to avail the credit on the basis of invoices issued to it. Further, it also permits, other establishments (having same PAN) of the said supplier, to avail the credit, on the basis of an Input Service Distributor Invoice in accordance with the provisions of sub-rule (1) of rule 54 of CGST Rules.

Thus, in the above example, ABC's head office at Maharashtra if obtains registration as ISD, it will be allowed to take credit on the basis of invoices issued by P and Q and immediately distribute such credit to Delhi establishment, by issuing ISD invoice to Delhi. Delhi can thereafter be able to claim credit on the basis of ISD invoices issued by head office.

Although, concept of ISD allows distribution of credit, such distribution is required to be made in certain manner. The Manner of Distribution of credit through ISD mechanism is explained below.

3. The Manner of Distribution of credit through ISD mechanism – Section 20of CGST Act and Rule 39 of CGST Rules, 2017

- ISD shall distribute *the credit available for distribution***in the same month** and details of such distribution shall be furnished in Form GSTR-6. (This condition was not there under the earlier service tax regime)
- Credit shall be distributed against a document issued in terms of Rule 54 of the GST Rules.Such invoice should, clearly indicate that, it is issued only for distribution of input tax credit. The contents of tax invoice to be issued by ISD are given below
  - name, address and Goods and Services Tax Identification Number of the Input Service Distributor
  - 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 (this condition is exempted in case of banking company and financial institutions)
  - date of its issue;
  - name, address and Goods and Services Tax Identification Number of the recipient to whom the credit is distributed
  - amount of the credit distributed
  - signature or digital signature of the Input Service Distributor or his authorised representative

- The amount of credit shall not exceed the amount available for distribution.
- The ISD shall first identify the credit which is not allowed in terms of section 17(5) ***or otherwise***and distribute the ineligible credit and eligible credit separately. The eligible quantum for distribution to recipient unit is explained later.
- The credit of tax paid on input services attributable **to a specific recipient** of credit shall be distributed only to that recipient only. Thus, in the above example, since P and Q have provided services to Delhi establishments, the credit in respect of services received from them shall be distributed to Delhi unit only and not to any other establishment.
- 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.

- 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.

- For the purpose of computing "*turnover*", the turnover of goods not taxable under this Act shall also be included. However, while computing such turnover, the amount of any duty or tax levied under entry 84 of List I of the Seventh Schedule to the Constitution and entries 51 and 54 of List II of the said Schedule, shall be excluded.

- The term '*relevant period*'is defined as under:

Situation	**What is relevant Period.**
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 preceding financial year.
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

- The credit that qualifies for distribution is to be computed using the formula given in Rule 39(1)(d) which is given below:

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

C = amount of total credit to be distributed.
t1 = turnover of recipient R1 during relevant period.
T = the aggregate of the turnover, during the relevant period, of all recipients to whom the input service is attributable.

C1= the input tax credit that is required to be distributed to recipient R1 (whether registered or not)

The above formula should be applied for every type of tax viz. Central Tax, State Tax, Union Territory Tax and Integrated Tax.

- The ISD shall be required to distribute thecredit as under:

Credit available with ISD	Recipient unit is located in same state as that of ISD	Recipient unit is located in different state than that of ISD
Central Tax	CGST	IGST
State Tax	SGST	IGST
UT Tax	UTGST	IGST
Integrated Tax	IGST*	IGST

**It's important to note that, section 20 permits distribution of Integrated Tax either as IGST or CGST or SGST. However, Rule 39(1)(e) permits distribution of ITC of integrated tax as IGST only.*

- It may be noted that, Rule 39 that mandates, distribution of the credit to all the recipients to whom credit is attributable, ***although such units are not registered under the Act, in spite of the fact that, registration under the Act is a condition for availment of ITC u/s 16***. Besides, it also mandates distribution of "ineligible credit". Such "ineligible credit includes ineligible credit under the provisions of section 17(5) *or otherwise*.

4. Credit Notes / Debit Notes to be issued by ISD

4.1. 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. ***This appears to be a very cumbersome provision.*** For this purpose, the ISD shall also be required to issue an "ISD credit note" to other establishments, in the same month in which the credit note issued to ISD by any supplier is included in GSTR-6 return of the ISD. 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, such amount is added to the output tax liability of the recipient. Where the amount of input tax credit distributed by an ISD is reduced later on for any other reason for any of the recipients, the same process shall be followed.

If any credit is distributed to a wrong establishment, it can be rectified by issuing ISD credit note to the recipient to which it was wrongly issued and issuing an ISD invoice for the said amount to the recipient which is correctly entitled for such credit. Both the documents should be reflected in GSTR-6 of the ISD in the same month.

4.2. Any additional amount of input tax credit on account of issuance of a debit note to an ISD by the supplier shall also be distributed to the recipients in the month in which the debit note issued to ISD-office is included in the return in FORM GSTR-6.In this case, unlike in the case of credit notes, it is not necessary to distribute the credit to other establishments in the same portion to which credit pertaining to original invoice was distributed.

4.3. Section 21 provides that, where the Input Service Distributor distributes the credit in contravention of the provisions contained in section 20 resulting in excess distribution of credit to one or more recipients of credit, the excess credit so distributed shall be recovered from such recipients along with interest.

5. Filing of Return by ISD

As per Rule 65 of the CGST Rules 2017, every ISD shall, on the basis of details contained in FORM GSTR-6A, and where required, after adding, correcting or deleting the details, furnish electronically the return in FORM GSTR-6, containing the details of tax invoices on which credit has been received and those issued under section 20. The details of invoices furnished by an ISD in his return in FORM GSTR-6 shall be made available to the recipient of credit in Part B of FORM GSTR 2A electronically through the common portal and the said recipient may include the same in FORM GSTR-2.

Following formats will be relevant for compiling information required for the purpose of making computation and filing of ISD return.

- **Summary of Total Input Tax Credit available for distribution during month (including debit notes issued by the supplier to ISD).**

Description	IGST	CGST	SGST	UTGST
Total ITC available for distribution				
Eligible ITC				
Ineligible ITC				

- **Summary of Credit Noted issued to ISD by supplier during the month.**

Credit Note No.	Original Invoice No.	Month of Original Invoice	IGST	CGST	SGST	UTGST

- **Distribution of Credit Available for Distribution.**
  IGST

Description	Unit T1 (Maharashtra)	Unit T2 (Delhi)	Unit T3 (Chennai)	Unit T4 (Kolkata)
Total Credit available for Distribution				
Relevant period				
Total Turnover during relevant period				
Turnover of respective unit during relevant period				

Note:

1. Similar Table can be prepared for SGST,CGST and UTGST also.
2. There can be three such tables for each tax (i) for apportionment of ITC attributable to specific unit, (ii) for apportionment of ITC to more than one unit to which credit is attributable and (iii) for apportionment of credit to all units.

- **Distribution of Credit Notes issued to ISD during the month.**
  IGST

Credit Note No.	Original Invoice No.	Amount of Tax	Ratio (%)	Unit T1 (Maharashtra)	Ratio (%)	Unit T2 (Delhi)	Ratio (%)	Unit T3 (Chennai)	Ratio (%)	Unit T4 (Kol)

Note:

1. Similar Table can be prepared for SGST,CGST and UTGST also.

6. Some Issues concerning ISD

6.1. Is it necessary to have more than one ISD?

i. Input Service Distributor is defined as an office of the supplier of goods and services and it appears that it can distribute the credit to all the offices of the entity which are covered under Single PAN. It therefore appears that, it's enough for any supplier to take only one ISD registration in respect of all its units located across the India.

ii. In order to understand the concept of ISD, following examples may be considered:

Example: 1 - A service provider in Delhi (i.e. a place where ABC has a separate registered unit) provides certain intra-state services to ABC (which are used at Delhi office), charges CGST+SGST (Delhi) and issues invoice in the name of ABC-ISD Maharashtra, the question may arise as to whether ABC-ISD can avail the ITC as CGST+SGST (Delhi) as ISD and distribute the credit to Delhi Unit as per the provisions of the Act, or whether credit would be denied to ABC Maharashtra as the credit pertains to Delhi. In other words, can credit in respect of local services be availed by ISD registered in other States?

Possible Answer: A simple advice in such case would be to ask a Delhi vendor to issue the invoice directly in the name of Delhi Unit and not to go through ISD mechanism as the same is not necessary. However, it would certainly not mean that credit will be disentitled, if such invoice is routed through ISD mechanism. In short, ITC which is otherwise available to an entity should also be allowed to it through ISD mechanism.

Example: 2 - The question may become little complex, when service provided by the Delhi vendor has direct nexus with Kolkata unit and not Delhi unit. In such case, will it be permissible for ABC-ISD at Maharashtra to distribute the CGST+SGST (Delhi) credit to ABC-Kolkata as IGST credit?

Possible Answer: In this case, tax officials have expressed a view that, assuming there was no ISD and invoice was raised directly in the name of ABC-Kolkata, it would not have been possible for ABC-Kolkata to avail Input Tax Credit of CGST+SGST(Delhi). Therefore, possible answer in this case is that, mere availment of ISD facility would not entitle ABC-Kolkata to avail the ITC of CGST+SGST (Delhi), to which it's not otherwise entitle.

Example: 3 A supplier of Tamil Nadu (i.e. a place where ABC has no place of business) issues a CGST+SGST (TN) invoice to ABC ISD Maharashtra and such service is not specifically related to any registered unit of ABC, but a common service. In such case, can ABC-ISD avail the ITC in respect of such services or would it require another ISD registration in the State of Tamil Nadu, or whether ITC would not be available at all?

Possible Answer: As ABC does not have a registered place of business in Tamil Nadu, it would not be entitled to ITC in respect of CGST+SGST (TN). Therefore, as explained in Example 2 above, mere routing the transaction through ISD Facility may not entitle ABC to avail ITC.

Example 4: Whether, there is any way by which ABC shall be entitled to take ITC of CGST+SGST (TN) in respect of services availed from vendor in Tamil Nadu?

Possible Answer: Yes, ABC will be required to take registration in the State of Tamil Nadu in order to avail the ITC of CGST+SGST(TN), and then use a cross charging method, in order to transfer the benefit of such credit to other units of Maharashtra. Therefore, ABC- Tamil Nadu would be required to issue an invoice for business support services to ABC-ISD, which will enable ABC-ISD to avail the ITC and distribute the same to respective units.

6.2. What's the concept of Cross Charge?

Generally, ISD is a concept used ***for 'distribution' of ITC***to one or more supplying units, whereas cross charge is the concept for ***'accumulation' of ITC scattered at different location*** to a central location. The concept of cross charge enables the assessee to use the ITC effectively.

Example of ISD: ABC India has three supplying units at Delhi, Chennai and Kolkata, and head office at Maharashtra. In such case, ABC India can avail all the services at Maharashtra as ISD, and distribute the same to its various supplying units using ISD Mechanism.

Example of Cross Charge: ABC India has a plant at Maharashtra, but representative offices at Delhi, Chennai, Kolkata and Tamil Nadu which is only engaged in marketing activities. All supplies are happening directly from Plant at Maharashtra to customers across India. In this case, ITC of local taxes (CGST+SGST) in respect of services obtained at local offices at Delhi, Chennai and Kolkata shall be accumulated at those respective offices unless the cross charging is not adopted. If cross charging is adopted, then such offices will do cross charge on their plant at Maharashtra for business support services and consequently, accumulated ITC at those offices will be used effectively. A view is possible that, in such cases, mere obtaining ISD registration at Delhi, Chennai and Kolkata may not entitle Maharashtra plant to avail ITC of local taxes of those respective states.

6.3. How to distribute ITC of RCM.

i. Input Service Distributor is not a supplier of service, but is only a distributor of service. Instructions appended to Form GSTR-6 provides that, ISD cannot make any payment under RCM and that if it has to make payment under RCM, it will be required to obtain a regular registration. GSTR-6 also does not provide for showing any particulars for reflecting details of inward supplies on which payment is made under RCM. It therefore, appears that, merely obtaining registration as ISD in a State would not make the assessee "registered person" under that State for the purposes of payment of GST under section 9(3) or 9(4) of the CGST/SGST Act or as the case may be section 5(3) or 5(4) of the IGST Act. Therefore in such case, an assessee shall neither be entitled to any ITC not shall be liable to pay any tax under RCM in respect of any local supplies (CGST+SGST) in that State.

ii. As regards IGST, the assessee shall be first required to issue invoice u/s 31(3)(f) from any of its registered office to its ISD Office and pay tax under RCM from such registered office. On the basis of such invoice, ISD shall avail the ITC and distribute the ITC to the concerned unit/s.

Example: 1. ABC India has three supplying units namely at Delhi, Chennai and Kolkata, and head office at Maharashtra. ABC India received an intra-state service from a dealer in Tamil Nadu. In this case, in the absence of any registration in Tamil Nadu, ABC may not be entitled to ITC of CGST+SGST(TN). Consequently a view can be taken that there is no need for any RCM payment on anyRCM services by ABC India in TN.

However, if a dealer from Tamil Nadu makes an inter-state supply of service (which is liable for reverse charge), such supply will attract IGST. ABC-India, in such case shall be required to issue invoice for such service from any of its registered units namely, Delhi, Chennai and Kolkata and pay IGST under reverse charge. Suppose invoice is raised from Chennai office, then in such invoice "ABC-Chennai" will be shown as 'person liable to pay tax' and ABC-ISD will be regarded as "receiver" of such service. ABC-ISD will take ITC on the basis of such invoice and then distribute the same to the concerned units or all units as per provisions of Section 20.

7. Sum up

Input Service Distributor is merely a facility given to the dealers, especially for those who have multi- state presence but a centralized procurement unit. In such case, combination of ISD and Cross Charge Mechanism will enable the dealer to efficiently use the ITC credits in respect of procurements happening at various places. The manner of distribution of ITC through ISD is very much rigid, especially the condition that, ISD is required to distribute the ITC in the same month or that, credit note of ITC should be given in the same proportion in which original ITC was distributed. An ISD is required to file the return on 13th of the next month, hence he will be required to undertake the reconciliation of ITC in respect of inward supplies between 11th to 13th. Unless, ISD files its return, other units will not be able to get the ITC. These rigidities contained in the Act, make the concept of ISD prone to implementation challenges. Hence, wherever possible, it's advisable to raise the invoice directly on the concerned unit, than on ISD, for routing every transaction through ISD will certainly increase the cost of compliance. Last, but not the least, ISD is applicable only in respect of input services, and hence, as regards procurement of goods, business entities will have to follow a disintegrated model in order to reduce the cost of compliance. Therefore, business entities dealing in goods, may prefer to shift from centralized to decentralized model, in respect of services also, and in that case, concept of ISD may not be really useful to them, except for distribution of common credits.

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- Indirect Taxes Committee