

Mandatory implementation of ISD mechanism effective from 1st April, 2025

What is Input Service Distributor?

The concept of Input Service Distributor (“ISD”) under GST is borrowed from the erstwhile service tax regime. The objective of incorporating the concept of ISD mechanism under GST is to prevent accumulation of ITC in respect of services (consumed at multiple location) at one location and facilitate proper distribution of such ITC to the locations where the services consumed. Thus, the role of ISD is to receive invoices for services (and **not for goods**) at one registration of an entity and facilitate the distribution of ITC to other registrations of the said entity (having the same PAN) where the underlying services are actually consumed.

The term “Input Service Distributor” is defined under Section 2(61) of the Central Goods and Services Tax Act, 2017 (‘CGST Act’) as *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.*

Concept of Cross Charge

As per Schedule I of the CGST Act the supply of goods or services or both by one registration of an entity to another registration of the said entity (having the same PAN) is deemed as “supply” and is chargeable to GST. Accordingly, provision of any internally generated support by one registration of an entity to its another registration (e.g. marketing support, accounting support, HR support, etc.) is deemed as supply under GST legislation and is exigible to GST. Provision of such internally generated services by one registration to another registration is often referred as cross charge by the trade and industry.

Cross Charge vs. ISD - Confusion?

Since inception of GST, confusion persisted whether the distribution of common ITC shall be done as cross charge or through ISD mechanism. While a few taxpayers have distributed common ITC through ISD mechanism, other taxpayers have distributed ITC through cross charge route. C.B.I. & C. vide its ***Circular No. 199/11/2023-GST dated 17.07.2023*** provided

clarification in this regard and cleared the ambiguity. It was clarified that at present ISD mechanism is not mandatory for distribution of input tax credit (**‘credit’** or **‘ITC’**) of common input services procured from third parties to the distinct persons. Therefore, the taxpayers have the options to distribute common ITC either through ISD mechanism or through cross charge by issuing tax invoice.

Applicability

Necessary amendments were made in the GST legislations to make the ISD mechanism mandatory.

Vide **Notification No. 16/2024 - C.T. dated 06.08.2024**, the Government has made ISD mechanism mandatory w.e.f. 01.04.2025. Thus, w.e.f. 01.04.2025, the distribution of common ITC has mandatorily to be done through ISD mechanism only.

Registration of Input Service Distributor

As per Section 24 of the CGST Act every taxpayer, for whom ISD mechanism is applicable, is mandatorily required to obtain separate registration for ISD compliance. This registration is to be obtained even if the taxpayer has already obtained regular registration from the GST department.

Conditions for Distribution of Input Tax Credit

- The input tax credit available for distribution in a month shall be distributed in the same month.
- Details of ITC to be distributed shall be furnished in **FORM GSTR-6** (i.e. **ISD return**).
- The amount of the credit distributed shall not exceed the amount of credit available for distribution.
- The credit of tax paid on input services attributable to a recipient of credit shall be distributed only to that recipient.
- Credit shall also be distributed to offices not registered or supplying exempt supplies (but have consumed a portion of the third-party services).
- Eligibility of ITC shall be examined at ISD level only. After such determination, amount of eligible and ineligible ITC to be distributed separately by ISD to each unit.

- The credit of CGST, SGST and IGST shall be distributed separately.
- The input tax credit of IGST shall be distributed as input tax credit of IGST to every recipient.
- Where the recipient of ISD credit is located in the State of ISD, the input tax credit of CGST and SGST shall be distributed as input tax credit of CGST and SGST.
- Where the recipient of ISD credit is located in the State other than the State of ISD, the input tax credit of CGST and SGST shall be distributed as input tax credit of IGST.

Distribution of Input Tax Credit

Input services attributable to one recipient	<ul style="list-style-type: none"> • ITC shall be distributed to such recipient only.
Input services attributable to more than one recipient	<ul style="list-style-type: none"> • ITC shall be distributed to all such recipients to whom input service is attributable and is operational in the current year. • The distribution shall be made <i>pro rata</i> on the basis of the turnover of such recipient to the aggregate of the turnover of all such recipients to whom such input service is attributable during the relevant period.
Input services attributable to all the recipients	<ul style="list-style-type: none"> • ITC shall be distributed to all the recipients to whom input service is attributable and is operational in the current year. • The distribution shall be made <i>pro rata</i> on the basis of the turnover of such recipient to the aggregate of the turnover of all such recipients to whom such input service is attributable during the relevant period.
Note: Relevant period means: <ol style="list-style-type: none"> 1. if the recipients of credit have turnover in their States in the financial year preceding the year during which credit is to be distributed, the said financial year; or 2. if some or all recipients of the credit do not have any turnover in their States 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 <u>all the recipients</u> are available. 	

Distribution of Credit of GST Payable under Reverse Charge

- Where ITC on any supplies is payable under reverse charge and to be distributed by ISD, then **the office in the same state in which ISD is located** shall receive such invoice from the supplier on which reverse charge is to be paid and shall discharge such liability under reverse charge.
- Thereafter such office shall issue an invoice or, as the case may be, a credit or debit note as per the provisions Rule 54(1A) of the Central Goods and Services Tax Rules, 2017 (“**CGST Rules**”) to transfer the credit of such common input services to the ISD.
- The taxable value in the invoice issued by said office shall be the same as the value of the common services.

Particulars to be Mentioned on the Invoice to be issued for Transferring RCM ITC to ISD

- Name, address and GSTIN of the registered person who have discharged RCM liability;
- A consecutive serial number not exceeding sixteen characters;
- Date of its issue;
- GSTIN of supplier of common service and original invoice number whose credit is sought to be transferred to the ISD;
- Name, address and GSTIN of the ISD;
- Taxable value, rate and amount of the credit to be transferred; and
- Signature or digital signature of the registered person or his authorised representative.

Documentation

A. Invoice

- For the distribution of ITC, ISD shall issue an ISD invoice.

B. Credit note

- The ISD shall issue an ISD credit note for reduction of credit in case the input tax credit already distributed gets reduced for any reason (including the reason that it was distributed to a wrong recipient by the ISD).
- Any ITC 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.

- The reduction of ITC 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.
- After issuance of relevant ISD credit note, and ISD invoice shall also be issued to the recipient entitled to such credit. The ISD invoice and ISD credit note shall be included in the return **FORM GSTR-6** for the month in which such credit note and invoice is issued.

Particulars to be Mentioned on ISD Invoice/Credit Note

- Name, address and GSTIN of the ISD;
- A consecutive serial number not exceeding sixteen characters;
- Date of its issue;
- Name, address and GSTIN of the recipient to whom the credit is distributed;
- Amount of the credit distributed; and
- Signature or digital signature of the Input Service Distributor or his authorised representative.

Consequence of Excess Distribution of Credit by ISD

- Distribution of excess ITC shall be recovered from the beneficiary recipients under section 73, 74 or 74A of the CGST Act.
- Penalty is leviable for an amount which is higher of Rs. 10,000/- or the amount ITC distributed irregularly.

List of certain services which can come under the ambit of ISD distribution

- Audit services
- Legal services
- Banking services
- Advertisement services
- Software services
- Staff insurance
- Recruitment services

Action Required

- Obtain separate ISD registration if not obtained earlier.
 - Identification and mapping of common input services attributable to more than one registration.
 - Communication with vendors for issuance of invoices on ISD registration.
 - Integration of ISD invoice/credit notes in the ERP system.
 - Provision for tagging of expenses in ERP system to extract data as per the ITC distribution requirements (i.e. the ERP system should be able to provide report whereby it can be ascertained what all are the common input services and at which locations such services have been consumed.
 - Creation of additional GL in the books for transfer and receipt of ISD ITC.
 - Training of relevant staff for proper recording of transactions.
 - Recording of proper terms in the purchase order and other relevant documents which can help in future to establish the locations at which the services are consumed.
 - Proper tracking and linkage of original invoices with the credit notes.
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