

## **Cross Charge Vs Input Service Distribution (ISD) under GST regime- An Analysis**

**Adv Ankit Kanodia**

**[ankit@advocateak.com](mailto:ankit@advocateak.com)**

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 on 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, centralized payment system, master agreement with head office or for any other reason.

The provisions of section 16 of CGST Act provides that, no registered person shall be entitled to input tax 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 goods /services of common nature which has been received by branches of establishment, it would not be possible for such branches to claim the input tax credit as single invoice will be issued in the name of Head office. The head office also cannot avail the credit as they are not actual recipient of such inward services. The concept of Input Service Distributor, hereinafter referred as "ISD," exists under the Indirect taxes from the 'Pre-GST' Regime. The idea behind the introduction of this concept was, laying down basis for distribution of Input tax credit in respect of services which are commonly consumed across various 'cost and profit centers' engaged in manufacture of goods or engaged in rendering taxable services. Under the GST regime, as well the concept of ISD has continued to exist.

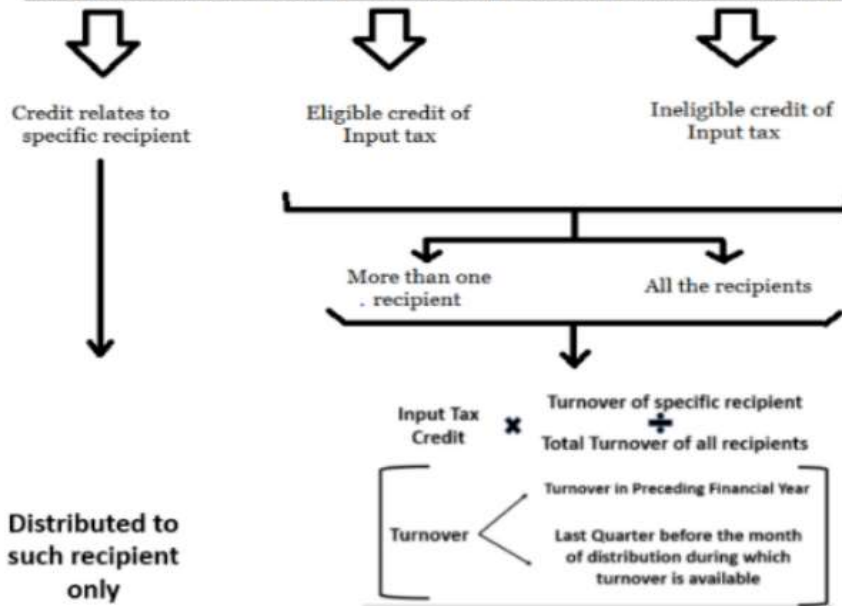
### **Relevant provisions and Rules:**

- 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 regular 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.

### **Manner of distribution of credit by Input Service Distributor – Sec. 20**

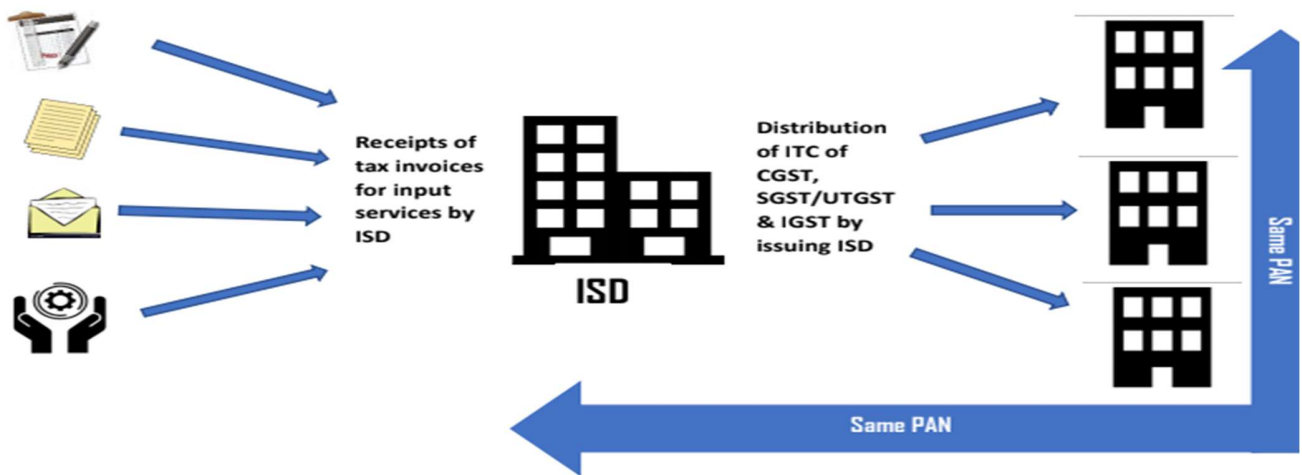
Credit Available With ISD	Recipient unit is located in State of as that of ISD	Recipient unit is located in different State than that of ISD
IGST	IGST	IGST
CGST	CGST	IGST
SGST	SGST	IGST
UTGST	UTGST	IGST

### Distribution of Credit of Input services by ISD to Recipient



**Example-** The head office of M/s ABC Limited is located in Bengaluru which acts as ISD is having branches in Chennai, Mumbai, and Kolkata. The head office incurred annual software maintenance expense (service received) on behalf of all its branches and received the invoice for the same. Since the software is used by all its branches, the input tax credit of entire services cannot be claimed in Bengaluru. The same has to be distributed to all three locations.

### **Distribution of ITC by ISD**



### Conditions to be fulfilled by ISD

**Registration:** Input Service Distributor has to compulsorily register as “ISD” apart from its registration under GST as a normal taxpayer. Such taxpayer has to specify under serial number 14 of the REG-01 form as an ISD. They shall be able to distribute the credit to the recipients only after this declaration.

**Invoicing:** ISD can distribute the amount of tax credit to recipients as earlier stated by issuing an ISD invoice.

**Returns:** Amount of tax credit distributed should not exceed the amount of tax credit available with the ISD as at the end of a relevant month to be filed in GSTR-6 by the 13th\* of succeeding month by ISD. The ISD can get the information of the ITC from the GSTR-2B return.

## **\*\* HOW TO DISTRIBUTE ITC OF RCM**

Input Service Distributor is not a supplier of service but is only a distributor of ITC of services. 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.

## **❖ CROSS CHARGE**

### **Let us first understand meaning and implication of Cross Charge under GST:**

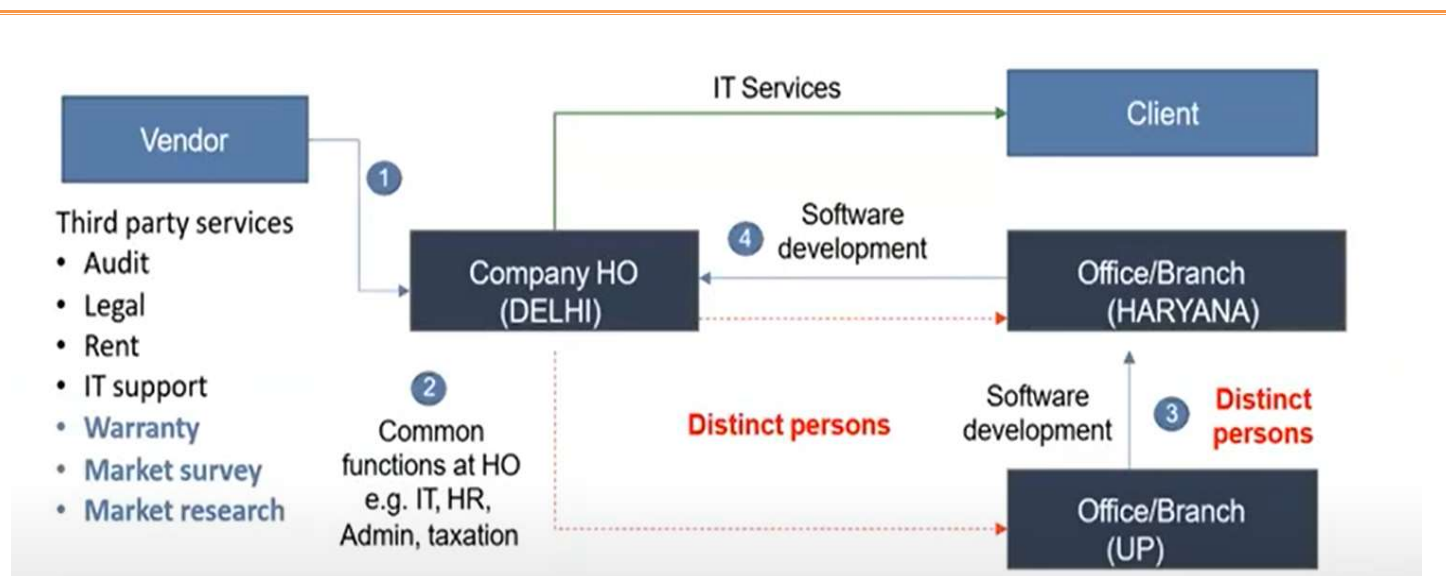
There is an irony, that the concept of "Cross Charge" is one of the most discussed concepts under the GST Laws. However, the word "cross charge" does not appear by itself under the CGST Act. With the introduction of GST law, the state-wise registration became mandatory for the entity holding place of business in more than one state. Also, the concept of "distinct person" was defined under the GST Laws. Any person who holds registration under the GST Act, in more than one state, bearing same "PAN," is recognized as a "distinct person."

As per Schedule-I to the CGST Act 2017, supplies without consideration amongst "distinct persons", is liable to be taxed. For this purpose, the value is to be determined in accordance with the provisions of CGST act and the CGST Rules (to be determined per Section 15(4) read with Rule 28). There may be transaction of stock transfer amongst the branches of a same company located across two different states. In such case, by virtue of provisions of Schedule-I to the CGST Act 2017, the same is liable to be taxed. The reason for the same is that GST is a "**destination-based consumption tax.**" Thus, if the goods were to be consumed in some different state, even if belonging to the same company, for the purpose of GST it was consumption by a distinct person in a different state. Thus, tax is liable to be paid. As far as this transaction is concerned there cannot be a concept of deemed supply coming into picture.

However, let us now understand how "Cross Charge" works. ABC Ltd is registered under GST Act in Mumbai (Maharashtra) which is its head office & having branches in Surat (Gujarat), Indore (Madhya Pradesh). The company has procured Audit services. Now the auditor would be providing audit services for the entity "ABC Ltd." It is important to note that the benefits of services received would be for all the branches. However, the Auditor has raised an invoice only in the name of "ABC Ltd" Mumbai. In this case, the consumption of audit services is actually done by all the branches. Thus, if we think from the "**Destination based consumption tax**" point of view, one may say that the consumption of audit services is in the states of Maharashtra, Gujarat, and Madhya Pradesh. Thus, under the GST Act, it would be necessary, based on some logical equitable manner that the consumption of services should be passed on to the respective states. Now if we refer to the provisions of "**Place of Supply,**" the auditor has correctly charged GST and issued the bill in the name of Maharashtra office with its GSTIN. However, for the purpose of GST laws the consumption has taken place in all those states where the services are consumed. Thus, the Maharashtra unit will have to raise a **Cross charge** invoice for the deemed services provided to the units in other states.

**Example:** From the below mentioned Chart we can understand that –

- 1- Third Party Cost Attributable to the Multiple Offices/Branches.
- 2- Other common expenses incurred for HO Related Activities.
- 3 & 4 Branches undertaking services for ultimate servicing to Client.



## Value of services – to be determined per Section 15(4) read with Rule 28

### **I. Valuation mechanism: -**

- Open Market Value (OMV)
- The value of Supply of Service of like kind and quality
- 110% of cost of provision of services/reasonable means consistent with the principles and general provisions.
- If full ITC available, value declared is deemed OMV.

**II. Need to Apportion Expenses Incurred by HO to Another Office** – To be done based on information maintained in its normal Course of work, only exception is ISD.

### ISD vs Cross Charge

SL. No	ISD	Cross-Charge
I.	The concept of ISD is governed by the provisions of section 20 of the CGST Act, 2017	Whereas the cross charge finds mandate from Para 2 of Schedule I read with section 25 of the CGST Act, 2017
II.	The ISD mechanism is limited to the extent of distribution of ITC on input services	It is an outward supply
III.	There is absence of services being rendered by one establishment to another of the same entity	The presence of supply of goods or services is sine quo non
IV.	ISD do not create any outward supplies as such, it can merely distribute ITC on inward services to its respective branches	Cross charge create outward supplies for which necessary invoicing is required

## Frequently Asked Questions FAQ'S

### 1. Whether there is a "supply" by HO to branches for common functions such as HR, IT etc.?

- GST is leviable on '**Supply**' of goods or services or both made for a consideration by a person in the course or furtherance of business.
- Schedule I: Supply of goods or services between distinct persons when made in the course or furtherance of business: Liable even if made without consideration.

- Elements of '**Supply**' first need to be satisfied, '**Supply**' not defined: In Common Parlance "**Supply**" means "**to provide**".
- Contractual Arrangement /Obligation 'to provide' services by a supplier of services to a recipient of services' is necessary.
  - No Agreement/Obligation 'to provide' any services to the branch (s)
  - Services received by HO and not distributed are consumed by HO /used for own self for performing its Obligation as the HO.
  - Mere incidental use by branches cannot be treated as an activity of '**Supply**.'

## CASE STUDY

### **KARNATAKA APPELLATE AUTHORITY FOR ADVANCE RULING (AAAR) IN CASE OF COLUMBIA ASIA HOSPITALS**

**(Order No: KAR/AAAR/05/2018-19)**

The India Management Office (IMO) (Head office of Columbia Asia) is providing a service to its other distinct units by way carrying out activities such as accounting, administrative work etc. with the use of the services of the employee working in the IMO, the outcome of which benefits all the other units and such activity is to be treated as taxable supply. Cost of Employees working in the IMO is an integral part of the cost of services rendered by IMO.

#### **Brief Facts of the case–**

Indian Management Office (IMO) – (Head Office), applied before the AAR to clarify whether if



IMO providing supply of services such as Accounting, HR, Admin, Tax etc. to other distinct units (Branch offices under same PAN) will constitute as Supply under the purview of G.S.T.



As per Advance Authority Ruling (A.A.R.), - IMO of the Appellant is providing service to its other distinct units by way of carrying out activities such as accounting, administrative work, etc. with the use of the services of the employees working in the IMO, the outcome of which benefits all the other units and such activity is to be treated as a taxable supply in terms of the entry 2 of Schedule I read with Section 7 of the CGST Act."



#### **SKKA Comments**

It is noteworthy that Entry 1 to Schedule III to the CGST Act 2017 which takes services by an employee to the employer in the course of or in relation his employment out of the GST ambit uses the words "services by an employee to the employer" and not "services by an employee to a person". The concept of distinct persons as envisaged under Section 25(4) of the CGST Act 2017 is applicable in context of a person and not in context of an employer.

## **Conclusion**

If we consider from the GST point of view, "**Cross charge**" concept is not an option to be considered. It is imperative and mandatory in nature. However, one may take a call if he is really in need of an ISD registration.

ISD registration shall be preferred, if there is a unit which is merely a head office or corporate office, wherein there are no outward supply transactions. In such case whatever expenses are incurred at such office are meant for the common purpose for all the units across the entire country. Thus, the benefits of the common expenses such as Audit Fees, Rent of Head Office or Corporate Office, Advertisement agency fees, Outsourced HR services etc. can be enjoyed by units across all the states. In such case, it would be ideal to hold a "ISD" registration, wherein all the common cost can be borne at the head office and the tax credit relating to it can be

distributed across all the beneficiary units. Over here more than the deemed consumption it would be necessary that the passing of tax credits is taking place.

One may decide to go for an ISD registration only if he holds a specific office or place of business which is just to facilitate the smooth functioning of business but is not engaged in providing any outward supply. However, if only there is an existence in multiple state, but no one dedicated cost center like a head office, then the deemed consumption of services can be passed by way of “Cross Charge Invoices.”

On the other hand, where there is no ISD registration, but there is only a deemed rendering of services by one “Distinct person” to another, in such case the same can be dealt with by way of raising a cross charge invoice. Usually in this scenario if the common services are identified to be consumed only in a single state, then the factual position in respect of such services will be required to be studied and based on the same, the relevant share of consumption over the distinct person, can be passed on by way of raising a cross charge invoice.

Cross Charge vis-à-vis ISD (Mandatory or optional) For every provision of law has an underlying intent behind its legislation, both Cross Charge and ISD aim to transfer Input Tax Credit to the State to which it pertains. Doubts are raised as to whether taxpayers have an option to choose between available alternatives or necessarily comply with any one or both. In this regard, whereas ISD mechanism has been given as an option which a taxpayer may or may not choose, transactions between HO and BOs have been mandatorily made taxable under GST law. Furthermore, ISD mechanism can only be used to transfer ITC of input services and not of inputs and capital goods. Interestingly, for input services, CBIC FAQs clarify that ITC availed on services procured at a registration which are used for business in more than one State, should be appropriately invoiced or distributed through ISD mechanism to other States.

When a company having multiple registrations in various states but procures various input service in a single state then ISD is beneficial. When a company having multiple registrations in various states and procures various input across various states then Cross Valuation is beneficial because in case of ISD, SGST of the State in which ISD is registered is only eligible for credit. Company desirous of distributing the credit relating to goods (e. g Stationery), as ISD is restricted to services only, the credit relating to goods commonly used can be distributed under Cross Charge only. Cross Charge turnover gets added to aggregate Turnover, However, ISD is just a distribution mechanism.

Lastly the 35<sup>TH</sup> GST Council meeting also had an Agenda Item 6(iv) covering the above issue and draft circular was also proposed to provide Clarification regarding taxability of services provided by an office of an organization in one State to the office of that organization in another State, both being distinct persons, however the same has not seen the light of the day yet and thus one more clarificatory circular awaits the stakeholders under the GST regime on the above issue.

*Assisted by Ms. Jyoti Jaiswal*