

50 Practical FAQs in Input Service Distributor (ISD) Compliance – Everything you must know



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Introduction:

The mandatory compliance for Input Service Distributor (ISD) has been made effective w.e.f. April 1st, 2025. As businesses begin to operationalize these requirements, several practical challenges and uncertainties are emerging. While the legal provisions may appear straightforward on paper, the true complexity of ISD is understood only when one ventures into its actual implementation. Businesses are required to juggle around many such issues pertaining to ISD right from vendor alignment and invoice handling to credit bifurcation, return filing, and cross-jurisdictional coordination.

Looking back, it's been almost eight years since the introduction of GST, a reform that promised to unify indirect taxes across India. Yet, the recent amendments related to ISD making it mandatory denotes one of the most significant and transformative changes in the GST framework. At the time of GST's rollout, few could have predicted that a compliance like ISD, once considered procedural and niche, would become a centre to credit distribution and tax discipline across multi-state organizations.

Importantly, the shift reflects a broader policy evolution—GST law is now evolving to protect the revenue interests of individual States. As a destination-based consumption tax, GST aims to ensure that tax revenue is rightly attributed to the States where

consumption occurs. The mandatory ISD mechanism is designed to facilitate this intent by ensuring that common input tax credit is accurately allocated across distinct persons i.e., different state-wise GST registrations of the same entity. This is not just a compliance exercise but a re-alignment that could be considered a turning point in the GST regime, as the law evolves to balance Centre–State interests more equitably.

From an organizational standpoint, ISD was traditionally seen as revenue neutral i.e., a mere redistribution of ITC within the entity. The entire focus of the industry or the tax consultants was to ensure that there is no short or excess claim of ITC on the organisation level.

However, with the introduction of mandatory provisions, this neutrality can quickly turn into a risk zone. Incorrect distribution, misclassification, or procedural lapses can trigger credit reversals, interest liabilities, and even penalties under various provisions of the GST law. The concept of revenue-neutrality may not be applied in the cases of ISD. As a result, businesses must shift their approach from procedural compliance to strategic control.

To assist in this transition, we've compiled a list of practical FAQs covering legal interpretation, procedural compliance, system readiness, and operational challenges under the new ISD framework. These FAQs are drawn from real-world queries and are aimed at helping tax teams navigate this evolving space with confidence and clarity.

Q1. Who is required to get registered under ISD?

Ans: As per Section 20 of CGST Act, 2017, there are three important elements to qualify as ISD:

- a. Any office of a supplier of goods or services or both,
- b. Receives tax invoices for input service, and
- c. On behalf of its distinct person's (as defined in Section 25),

Once an office of the supplier is identified to qualify as an ISD based on the above elements, the mechanism of distribution of ITC shall be done in accordance with Section 20 of the CGST Act, 2017 and the said office is mandatorily required to register as an ISD under Section 24(viii) of CGST Act.

Q2. *What is the key differentiation between the concept of ISD as per the erstwhile tax regime and as per the GST law?*

Ans: In the erstwhile tax regime, the concept of ISD was coined to facilitate the taxpayer so that the taxpayers can claim CENVAT credit across multiple registrations. Therefore, the primary intention was that the common credit can be accumulated at one place and then can be distributed on the basis of pre-defined basis. Thus, eliminating the need to take invoices at each registrations level.

On the other hand, the concept of ISD is introduced in the GST law to correctly allocate the ITC in the correct state treasury. Hence, it is important to note that the very objective of implementing ISD under erstwhile Central Excise and Service Tax laws and under GST laws is starkly different.

Q3. *Since GST applies to the whole of India then what was the requirement of ISD?*

Ans: It is correct that GST is a PAN-India tax, the nature of GST is that it is a destination-based consumption tax. Therefore, the tax shall be collected by the state in which the supplies are ultimately consumed. Without ISD, the offices in the HO state would retain the credit that is actually used even by the branches in other states also leading to a dis-proportionate distribution of credits. Implementing the ISD would ensure taxes flow to the consumption state.

Q4. *Whether having ISD registration before 1st April 2025 makes me liable to compulsorily distribute the ITC through ISD?*

Ans: As specified in Circular 199, the earlier provisions in relation to ISD mechanism did not make it mandatory to distribute credit through ISD. Therefore, it can be said that ISD was not mandatory before 01.04.2025 in the absence of enabling provisions mandating the said registration.

Alternatively, the department can also take the view that once the ISD registration was there, the ISD route should be the only permissible way of distributing the ITC. Circular 199 only provided an option not to register as ISD but once a taxpayer is registered, the option ends and the taxpayer is bound to follow the ISD mechanism. In

view of the authors, this view is not legally correct and would not stand the test of judicial scrutiny.

Q5. Since, ISD registration is to be obtained for an 'Office', what shall be construed as the term 'an office of the supplier of goods or services or both'?

Ans: The term 'office' has not been defined in the GST Law. It can include Head Office, Corporate office, Regional or Zonal office & even Branch office. As long as long as it involves the following:

- i. Receiving tax invoice towards receipt of input services
- ii. For or on behalf of distinct person's and liable for distribution

In this regard, the Hon'ble CESTAT of Madras has pronounced in the judgement of **The India Cement Ltd 2015-TIOL-1620-CESTAT-MAD** that the Definition of input service distributor using the term "an office" cannot be limited to a physical boundary but shall be interpreted as different boundaries which are offices and distribute the credit. This interpretation reinforces that any establishment which centrally receives the common input services from third parties and meeting the statutory criteria would qualify as an 'Office' for the purpose of compliance ISD under GST.

Q6. If we have multiple offices, then whether we need to obtain multiple ISD registrations?

Ans: The concept of Input Service Distributor (ISD) is defined under Section 2(61) of the CGST Act. As per this provision, the ISD registration becomes applicable when:

- An office receives third-party invoices for services used by multiple locations (distinct persons), and
- There is a requirement to distribute the ITC attributable to such other units.

Now, as far as the number of ISD registrations is concerned:

The law does not require multiple ISD registrations. A single ISD registration is sufficient, and any one eligible office can be designated as the ISD for the entire organization.

However, Section 2(61) uses the term "an office," which implies that more than one ISD registration is permissible, though not mandatory.

In practice, large organizations with wide geographical presence may opt to take multiple ISD registrations, especially when their structure is decentralized. For example:

Banking and insurance companies often have regional or zonal offices which act independently and receive region-specific common services. In such cases, they may choose to obtain separate ISD registrations for each regional office to simplify credit distribution and compliance.

Q7. Whether ISD registration would have a separate jurisdiction under GST department?

Ans: No, the ISD registration need not have the same jurisdiction as the regular GSTIN of the Head Office, even if both are registered at the same physical premises. Under GST, each registration, whether regular or ISD, is treated as a distinct entity for administrative purposes, and the jurisdiction is assigned independently by the department based on internal allocation criteria.

Q8. Whether there would be a separate audit/ investigation/ scrutiny for ISD registration. Also, who shall be the proper officer for ISD registration?

Ans: Yes, there can be a separate audit, investigation, or scrutiny for the ISD registration, independent of the regular GSTINs of the entity. The ISD registration is subject to its own compliance obligations including filing GSTR-6, maintaining distribution records, and proper documentation of invoices.

Hence, entities must ensure ISD specific proper compliance to avoid exposure during department audit, even if their regular GSTINs are otherwise compliant.

Q9. Whether the ISD registrations under earlier tax regimes automatically migrated into GST?

Ans: No. The registration of ISD under the existing regime (i.e. under Service Tax) would not be migrated in GST regime. All the existing ISDs will be required to obtain fresh registration under the new regime in case they want to operate as an ISD.

Q10. Is ISD registration eligible to claim a refund under GST?

Ans: It is important to note that the ISD mechanism is purely for distribution of ITC and not for utilization or output liability adjustment, and hence the scope of refunds is very limited. ISD can only claim refund of balance in the electronic cash ledger. This typically applies in cases where excess cash has been deposited or remains unused. The refund must be applied through Form RFD-01.

Q11. How to identify 'Common Services', what principles to be kept in mind to identify the same?

Ans: The definition of Input Service Distributor under section 2(61) read with section 20(1), states that the invoices from third party **"for or on behalf of"** other distinct persons need to be distributed. The term **'for or on behalf'** is not defined in the GST law. Looking at the dictionary meanings, it can be concluded that the term 'for' indicates direct benefit to another and the term 'on behalf of someone' has been defined to mean, done for another person's benefit or support, or because you are representing the interests of that person

Applying above in the context of ISD would mean that the term 'for' can be interpreted in situation where one branch receiving direct service or benefit from another branch or HO on the other hand 'on behalf of' implies representational actions taken by one unit for another.

Here, it is important to note that the above phrases trigger the ISD mechanism. This also means that if there is a very indirect nexus of the common third-party invoice, then it cannot be said to be for or on behalf of the other distinct person. However, since the term is very interpretational and prone to disputes, businesses must take proper care and advice while determining the same.

Q12. Once common services are identified whether any manner of distribution is provided in the GST Law?

Ans: The manner of distribution is provided in Rule 39 of CGST Rules, 2017.

- Firstly, distribution would be done only amongst those recipients of input tax credit to whom the input service being distributed are attributable.

- Secondly, distribution would be done amongst the units which are operational in the current year.
- Thirdly, distribution would be made in the ratio of turnover in a State or Union territory of the recipient during the period to the aggregate of all recipients to whom input service being distributed is attributable.
- Lastly, the credit distributed should not exceed the credit available for distribution.

Q13. Whether the term 'attributable' is defined in the law?

Ans: The provision dealing with distribution of ITC among the branches has used the term 'attributable' as a measure to determine the transactions requiring distribution of ITC under ISD.

The term 'Attributable' has not been defined under GST law. As per The Law Lexicon by P. Ramanatha Iyer, the term 'Attributable' has been defined to mean as follows:

“It is a plain English word involving some casual connection between the loss of employment and that to which the loss is said to be attributable. This connection need not be that of a sole, dominant, direct or proximate cause and effect. A contributory casual connection is quite sufficient.”

It further clarifies that the expression 'Attributable to' has a wider import than the expression 'derived from'. The expression of wider import, namely, "attributable to", was used when the legislature intended to cover receipts from sources other than the actual conduct of the business. This interpretation is also supported by Supreme Court in the case of *Cambay Electric Supply Industrial Co. Ltd. v. C.I.T.* (113 ITR 840).

In the context of ISD, this means that if an input service has even a marginal or incidental connection to multiple locations or GSTINs, the related ITC must be distributed among those units. This can be understood with the help of an example, say a legal consultancy is taken by the head office regarding a pan-India compliance issue, and it affects decision-making across various states, the ITC should not be retained at the HO but must be distributed through ISD to the relevant states based on turnover or usage, even if indirect.

Therefore, the understanding for "attribution" under ISD is not strict or narrow. The moment there is any slight nexus between the input service and multiple units, credit becomes distributable. This interpretation ensures that credit allocation aligns with the destination-based nature of GST.

Q14. In case of an Income Tax related consultancy services pertaining to the entire organization, the purchase order is entered for 3 years. On the face of the purchase order, the GSTIN of the regular office is recorded. Do we need to change the Purchase Order (PO) or the old PO still suffice?

Ans: It is necessary to amend the existing PO to have the ISD GSTIN recorded. This is important because if the PO is not changed then there is a possibility that vendor may continue to raise the invoice on the regular GSTIN. Further, a proactive communication must be made to the vendor to raise the invoice under the ISD GST number instead of the regular GST number.

Q15. What are the key factors to consider while determining whether an input service should be treated as a common expense or a specific expense?

Ans: There is no universal thumb rule to classify input services as common or specific. The determination must be made case-by-case, based on the following key factors:

- **Nature and purpose of the service:** If the benefit flows across multiple GST registrations (e.g., brand protection, corporate legal expenses, advertisement expenses), the expense is likely common.
- **Beneficiaries of the Service:** Identify the end recipients (in this case it would be distinct persons of the organisations only) who derive value from the service. If the benefit is flowing to multiple GST registrations, then even indirectly, the expense may qualify as common and must be routed through ISD.
- **Indirect or contributory nexus:** The term "attributable" under Section 20 has a broad scope. Even indirect benefit¹ to other units is sufficient to require ISD compliance. As discussed above, the term "attributable" carries a wider scope than 'derived from' and can include causal or incidental connections. Even a contributory connection is sufficient.

- **Practical Attribution Feasibility:** If it is difficult to quantify or isolate the portion of service used by each location (e.g., legal expenses defending brand reputation, pan-India advertisement, etc.), it is practical and legally safer to treat the expense as common.
- **Prior Tax Regime Learnings:** Under the erstwhile CENVAT regime, attribution and distribution were optional and taxpayer friendly. Under GST, the purpose has shifted. Now it ensures that States receive their rightful share of ITC. This makes correct attribution and ISD compliance mandatory, not discretionary.

Q16. Can you provide a list of expense categories that need consideration while evaluating whether an input service is 'for or on behalf of other units? Also, are there cases where the same expense head can be treated as both common and specific?

Ans: The test of “for or on behalf of” is fact-specific, and requires assessing:

- Who benefits from the input service?
- Is the benefit restricted to only one GSTIN, or spread across multiple?
- How to justify the attribution?

The same nature of expense may differ in treatment depending on the operational context, and businesses should document their attribution logic to defend it during audits. It is advisable to follow consistency on year-on-year basis to avoid litigation.

Following is the Dual-Treatment Scenarios:

Expense Type	Scenario as Common	Scenario as Specific
Legal Expenses	Consumer litigation impacting brand or PAN India product recalls	Local litigation for a branch office or property dispute
Advertisement	Brand promotion campaigns (TV, online, national)	Location-specific campaign or a region-specific campaign
Audit Fee	Statutory audit contract for the full company	Local stock audit for one warehouse

Software Subscription	ERP licenses used across branches or cloud-based tools with org-wide login	Accounting or PoS software used exclusively by branch or warehouse
HR Software	Cloud based HR software used by employees across multiple states	Location-specific software (e.g., factory shift tracking only for MH plant)

From the above, it can be seen that the classification of an input service as common or specific is not mechanical exercise rather it demands a careful, transaction-level evaluation of facts, functionality, and benefit flow. The guiding test is whether the service is received “for or on behalf of” other distinct persons, as defined under Section 2(61) of the CGST Act.

Q17. It can be seen that there is no mechanism to make the RCM payment through the ISD? Then how an ISD receiving common input services u/s 9(3) or 9(4) of CGST Act will proceed with the RCM payment.

Ans: RCM payment cannot be directly made from the existing ISD mechanism because an ISD registration does not have the facility to discharge tax liability, and there is no provision in GSTR-6 to pay tax like a regular taxpayer in GSTR-3B.

However, as per Rule 54(1A) of the CGST Rules, if the regular GSTIN of the supplier having same PAN & state code that of ISD receives invoice which are liable to RCM and discharges the tax under its regular registration, it can raise an invoice on the ISD unit for the proportionate value of services received on behalf of all units. The ISD can then take credit of that invoice and distribute it appropriately through the ISD mechanism.

Q18. Whether payment of tax under RCM and 54(1A) invoicing can happen in the same month?

Ans: No, in practice, payment of tax under RCM and the corresponding distribution of ITC via Rule 54(1A) cannot occur within the same tax period. This is primarily due to

the timing mismatch between when the credit becomes available and when the ISD return is due.

To illustrate this, let us understand through an example:

Suppose an input service invoice, attracting tax under reverse charge mechanism (RCM), is received by the organization in April 2025. Since ISD is not permitted to discharge RCM liability, the invoice is accounted for in the regular GSTIN of the entity.

The RCM tax of ₹1,00,000 is accordingly paid in the GSTR-3B of April, which is filed on 20th May 2025, and the ITC is availed in that return.

Now, the ITC becomes available for distribution only after filing GSTR-3B, i.e., after 20th May. However, the due date to file the ISD return (GSTR-6) for May is 13th June 2025. This means that although the RCM was paid and credit availed in April, the corresponding distribution of that credit via Rule 54(1A) can only be executed in June's ISD return, effectively pushing the credit distribution into the next month.

Thus, a one-month lag is inherent in this mechanism, which can temporarily block working capital. This is a systemic limitation that businesses need to account for while planning RCM-related service procurements through ISD structures.

Q19. My Head office is in Delhi. Accordingly, the ISD is located in Delhi. I have received the legal services for the entire organization. The invoice for RCM has been raised on MH location. Now the organization wants to transfer this credit to the ISD.

Ans: No, the Maharashtra registration cannot transfer the RCM credit to the ISD located in Delhi using Rule 54(1A), because the rule specifically requires that both the regular registration and the ISD must be located in the same State. Therefore, all the common services attracting RCM liability should be accounted at the regular GSTIN having same state code that of ISD.

Q20. RCM Invoice is to be recorded in the regular GSTIN of the organization for transfer purposes and is to be included in GSTR 1 then subsequently in 3B as well. So, will it also be included in the aggregate turnover?

Ans: No, it shall not be included in the aggregate turnover because it is not a supply and only an arrangement to make RCM payment since the ISD registration cannot discharge RCM functions. Hence, it is suggested that this turnover be excluded for the purpose of refund computations or rule 42/ 43 common ITC reversals etc.

Q21. Rule 54(1A) permits a regular GSTIN to discharge RCM liability for common services on behalf of the ISD by reporting it in its monthly returns. However, merely because the transaction is reported in GSTR-1 and GSTR-3B, can it be treated as a 'supply' under GST?

Ans: In the current GST framework, there is no mechanism to discharge tax under RCM, since ISDs are only meant to distribute input tax credit and not to engage in taxable outward or inward supply transactions.

To address this gap, Rule 54(1A) of the CGST Rules provides a workaround - a regular GST registration in the same state as the ISD pays the RCM on such common input services, avails the ITC in its GSTR-3B, and then issues an invoice to the ISD to transfer the credit. The ISD, in turn, distributes the ITC to recipient units via GSTR6.

However, a key concern arises here is that when the regular GSTIN issues this invoice to the ISD, is this considered a "supply"? The answer is no. This invoice is not backed by any actual supply of goods or services. It is merely a pass-through or internal reallocation document, enabling credit transfer under Rule 54(1A).

Since Rule 54(1A) invoices do not represent actual supplies, reporting them as outward supplies in GSTR-1 could lead to disputes. While this mechanism is currently being followed and has administrative acceptance, it does not have direct legislative sanction as a "supply" under Section 7 of the CGST Act. Hence, this arrangement could be subject to litigation.

Q22. Can we use 54(1A) for my forward-charge invoices?

Ans: Upon the bare reading of Rule 54(1A), it can be seen that the said sub-section doesn't limit itself only w.r.t RCM invoicing. Secondly, the details which are required to be incorporated on the invoice as per Rule 54(1A) also do not give away any such condition which restricts itself only to the extent of issuing RCM invoices.

Therefore, in our opinion, one can use Rule 54(1A) even to transfer the vendor credits into ISD since there is no restrictions in the statutory provisions as laid down under rule 54(1A) of CGST rules.

Q23. *Rule 39(1)(a) requires ITC to be distributed in the same month in which it becomes available. But what if the conditions under Section 16 of the CGST Act are not yet fully met, can the ISD hold the distribution?*

Ans: Rule 39(1)(a) of the CGST Rules states that input tax credit available for distribution in a month shall be distributed in the same month and reported in FORM GSTR-6. However, this must be read harmoniously with Section 16 of the CGST Act, which governs eligibility to avail ITC.

For credit to be considered "available for distribution" the prerequisites under Section 16(2) must be fulfilled.

If any of such conditions remain unsatisfied, the credit cannot be said to be "available" in a legal sense, even if the invoice is reflected in GSTR-6A. Therefore, in such cases, it is prudent and legally defensible for the ISD to defer the distribution until all conditions are met.

Q24. *How are debit notes and credit notes treated under the ISD mechanism, and what are the key differences and challenges in their implementation?*

Ans: Under Rule 39(1) of the CGST Rules, both debit notes and credit notes received by an ISD from suppliers have distinct treatment for the purpose of ITC distribution:

- i. **Debit Note – Rule 39(1)(m):** If a supplier issues a debit note to the ISD, it is required to distribute the additional credit in the month in which the debit note is included in GSTR-6. Rule 39(1)(m) prescribes that the distribution must follow the same method applicable to normal input service invoices i.e., based on the proportion of turnover of the recipient units during the relevant period. Therefore, debit notes are to be treated as a fresh ITC and to be distributed based on current turnover proportions.

- ii. **Credit Note – Rule 39(1)(n):** When a credit note is issued to the ISD, the rule clearly provides that the reduced ITC must be apportioned among the recipient units in the same ratio as the original invoice.

If the credit to be reversed is more than the amount available for distribution in that month, the excess must be added to the output tax liability of the recipient branch. This ensures that the reduction matches the earlier benefit distributed.

Following can be the implementation challenges in the above –

- i. If a recipient unit is closed or deregistered at the time the credit note is received, distributing or reversing credit becomes difficult. The law is silent on whether the ISD or HO must bear the reversal in such cases.
- ii. Credit notes must follow original ratios, but debit notes can follow current turnover. This asymmetry creates confusion in businesses trying to implement consistent practices.
- iii. In cases of business reconstitution such as merger or demerger, how should the turnover of the relevant units be computed for distributing the credit while issuing debit notes?

While Rule 39 provides a structured approach for ISD to handle debit and credit notes, the difference in treatment, coupled with practical restructuring scenarios, makes implementation tricky. Businesses are advised to adopt clear internal policies where ambiguity persists.

Q25. *Whether there is a requirement to distribute the ineligible credit or can it be expensed out at the initial level itself?*

Ans: The ineligible input tax credit (ITC) must be distributed through the ISD mechanism and cannot be expensed out directly or reversed centrally at the ISD level. As per Rule 39(1)(g) of the CGST Rules, the Input Service Distributor ISD is required to separately distribute ineligible ITC to the respective recipient GST registrations.

This is essential because GST is a destination-based consumption tax, meaning the tax revenue accrues to the state where consumption occurs.

For example: if the employee medical insurance premium is related to employees across various states but the ITC on the same is reversed only in one state (e.g.,

Maharashtra), it results in consumption and reversal being recorded solely in that state, thereby misleading the actual credit flow and distorting state-wise tax revenue allocation.

Q26. Who is required to reverse the ineligible ITC? The HO or the receiving branches?

Ans: The ISD is required to claim the ineligible credit also in the GSTR 6, upon claiming, the ISD is required to distribute the said ineligible credit among the branches and the respective branches are required to reverse the said credit in their respective GSTR3B.

Further, a separate ISD invoice is required to be issued for the eligible and ineligible credits. Further, businesses are required to keep a proper track and trail of the ineligible credits to establish the eventual reversal of the same.

Q27. In cases where the eligible & ineligible ITC is recorded in the same invoice, how is the ISD required to distribute the said ITC?

Ans: It is suggested to have separate distribution and invoices for ineligible credits. This is important to maintain the documents pertaining to reversal and for the department during audits. Alternatively, one can also take a view to distribute the ineligible credit as eligible from ISD and to reverse the same at respective branches.

Q28. Whether the common input credit reversal as per rule 42/43 is required to be done in the ISD registration?

Ans: The implications of common input credit reversal as per rule 42/ 43 are to be made at the individual branch level and not at the ISD level. This is because the criteria to reverse the credit in accordance with rule 42 & 43 have to be applied at each registration separately.

Q29. Upon introduction of ISD can it be said that the concept of cross charge has become redundant?

Ans: The concept of cross-charge does not become redundant. In fact, both ISD and cross charge serve different purposes under the GST regime.

This is because ISD mainly focuses on the third-party invoices that are received by the office for or on behalf of other branches or units. On the other hand, if the HO or one branch of organization provides service to the other location then it can be said to be “supply” between the distinct person which is liable for cross-charge. Therefore, both mechanisms are mandatory in their respective scenarios.

In other words, if there is a clearly defined inter-se ‘supply’ of goods or ‘supply’ of service, then one has to mandatorily cross charge instead of distributing the credits through ISD. This can be understood from the below mentioned examples –

ISD Scenario:

Head Office (Delhi) receives an invoice from a third-party audit firm for statutory audit of the entire company, including branches in Maharashtra, Karnataka, and Gujarat. Since the service benefits multiple units and the invoice is from a third party, the ITC must be distributed via ISD registration based on turnover or usage.

Cross Charge Scenario:

The in-house IT team located in the Bengaluru office develops and maintains software systems for the entire organization, including the Delhi and Mumbai offices. Since there is an internally generated service being rendered between distinct persons, Bengaluru office must raise a tax invoice and cross charge GST to other locations.

Q30. *If a supplier has two registrations in the same state, then what shall be the fate of ISD compliances?*

Ans: As per Section 25(4) of CGST Act, a person who has obtained or is required to obtain more than one registration, whether in one State or Union territory or more than one State or Union territory, then it shall, in respect of each such registration, be treated as distinct persons for the purposes of this Act.

Secondly, the requirement to register under ISD comes from Section 20 of CGST Act, 2017 which specifies that whenever any office receives a tax invoice for or on behalf of the distinct persons then the office can be said to be an ISD.

Therefore, since the registration within the same state is also being treated as distinct person, and as long as an office receives common services by way of third-party invoices, the supplier having two registrations within same state shall have to comply with the ISD provisions.

Q31. Whether all the third-party invoices will compulsorily go into ISD or is there any scenario where even the third-party invoices can be considered as Internally Generated Services?

Ans: Considering the definition of the ISD, if the ISD only receives the tax invoice for the purpose of distribution then it can be said that the third-party invoice has to be booked under ISD for distribution.

However, if the HO receives the services and does some processing on those services to make it usable & workable for other branches then a stand can be taken that HO has consumed these third-party services to provide 'Internally Generated Services' to its branches and thus to be cross charged rather than routed through ISD.

This can be understood from the below mentioned examples –
If HO receives a third-party license for raw financial data and directly distributes access to branches, it is a classic ISD case. But if HO receives the data, analyzes and processes it, builds a customized dashboard, and then provides those insights to other branches, it is no longer a mere distributor. It provides a service and should therefore cross-charge the branches for the value of such Internally Generated Services

Q32. If a taxpayer has not done cross charge for the earlier period, then what remedy does the taxpayer have now?

Ans: Circular 199/13/2023 has provided that distribution of credit through ISD is optional since the earlier provisions did not make it mandatory. The circular further provided that the taxpayers could alternatively use the cross-charge route for distribution of common services.

Therefore, before the amendment the taxpayer was eligible to use the cross-charge method. Additionally, it was clarified in the circular that the valuation for cross charge can also be set to be nil if the recipient is eligible for full input tax credit.

To summarize, if the taxpayer is eligible for full ITC, then there is no need to cross-charge also since the valuation can be nil.

Q33. In allocating and distributing credits to various states, how the term ‘turnover’ to be construed?

Ans: As per Rule 39 of CGST Rules, the turnover for the purpose of distribution of attributable credit shall be distributed based on turnover in a state.

The definition of ‘**turnover in a state**’ is provided Section 2(112) of CGST Act which means the aggregate value of all taxable supplies (excluding the value of inward supplies on which tax is payable by a person on reverse charge basis) and exempt supplies made within a State or Union territory by a taxable person, exports of goods or services or both and inter-State supplies of goods or services or both made from the State or Union territory by the said taxable person but excludes central tax, State tax, Union territory tax, integrated tax and cess.

Further, the Explanation to Rule 39 provides that the turnover must also exclude any duties or taxes levied under the following constitutional entries:

- **Entry 84 of List I (Union List):** This refers to excise duties on products that are still outside GST, such as petroleum, tobacco, and alcohol.
- **Entry 92A of List I:** Refers to Central Sales Tax (CST), which applied to inter-State sales of goods under the earlier tax regime.
- **Entry 51 of List II (State List):** Refers to State excise duties, again covering alcoholic liquor and similar non-GST goods.
- **Entry 54 of List II:** Deals with State VAT on petroleum products and other items still outside the GST purview.

However, it’s important to note that Rule 39 only requires exclusion of the duties or taxes levied under those entries, not the turnover itself from such goods or services. So, for example:

- If a unit is dealing in alcohol or petroleum products (which are currently outside GST), the revenue from such sales may still be included in turnover under Section 2(112),
- But any excise duty, VAT, or CST charged on such turnover — those specific tax amounts — must be excluded when computing the final turnover base for ITC distribution.

Q34. Many a times it can be seen that the HO is earning certain incomes such as interest on securities, dividend income and gain on sale of securities. What shall be the fate of these incomes? Will it also be included in the definition of the turnover?

Ans: To evaluate the treatment of such incomes in the context of ISD credit distribution, we first refer to Section 2(6) of the CGST Act, which defines "aggregate turnover" to include the aggregate value of all taxable supplies, exempt supplies, exports of goods or services, and inter-State supplies made by all registrations under a single PAN across India. It expressly excludes taxes such as CGST, SGST, IGST, and cess.

The term "exempt supplies" under Section 2(47) includes supplies that are wholly exempt under notifications, attract nil rate of tax, or are "non-taxable supplies." In turn, Section 2(78) defines "non-taxable supply" as a supply of goods or services or both, which is not leviable to tax under this Act.

However, both Section 2(52) (definition of goods) and Section 2(102) (definition of services) specifically exclude "securities" from their scope. Therefore, transactions in securities such as dividends on shares, sale or redemption of mutual funds, or capital gains on bonds and stocks are neither considered goods nor services under GST. Consequently, they do not qualify as "supply" at all and thus cannot be categorized even as "non-taxable supplies."

However, interest income stands on a different footing. Entry No. 27 of Notification No. 12/2017 – Central Tax (Rate) dated 28th June 2017 specifically exempts services by way of extending loans, advances, or deposits where consideration is in the form of interest or discount. This means that interest income is a supply of service, and therefore, it does fall within the definition of exempt supply and must be included in the aggregate turnover for ISD purposes.

Q35. Whether there is any requirement to reconcile the ITC as per GSTR 6 along with GSTR 6A?

Ans: Under the current GST law, there is no statutory requirement that mandates reconciliation between GSTR-6A (auto-populated details of inward supplies for ISD)

and GSTR-6 (the filed return by ISD). However, while this reconciliation may not be legally compulsory, it is highly advisable as good compliance practice.

While discrepancies between GSTR-6 and GSTR-6A may not automatically trigger any liability, they can draw attention during audits, scrutiny, or departmental assessments, especially where the distribution of credit impacts multiple states. A timely and routine reconciliation helps ensure that credits are properly attributed and distributed, and that no eligible credit is left undistributed or wrongly allocated.

Therefore, even though not mandated by law, reconciliation between GSTR-6 and GSTR-6A is important for ensuring accuracy, and effective compliance in the ISD process.

Further, similar to GSTR 2B, presently government has not proposed any GSTR 6B document, thereby making the reconciliation process difficult, this is mainly because GSTR 6A is a dynamic document and GSTR 2B is a static document.

Q36. If one of my vendors is registered as QRMP then how can the ISD claim the credit since both ISD & QRMP have same date of filing of returns?

Ans: Since both ISD (GSTR-6) and QRMP vendors (GSTR-1) have a return filing due date of the 13th of next month, there's a possibility that invoices from QRMP vendors may not appear in GSTR-6A in time for ISD to distribute credit in the same month.

In such cases, the ISD will need to wait until the next tax period to distribute the credit, once the vendor uploads the invoice. This results in a one-month delay and temporary working capital blockage.

Q37. Whether the invoice issued for the purpose of ISD is different than the tax invoice as per Rule 46? And whether there is a requirement to issue E-invoice?

Ans: Tax invoice under GST law is governed by Rule 46 of CGST Rules. Whereas the provisions of ISD invoicing are governed by Rule 54(1) & 54(1A) of CGST Rules. The invoicing to be done for the ISD compliance prescribes a simplified format that differs from a standard tax invoice. E.g., ISD invoices are not required to include taxable value, rate of tax, or HSN codes.

Furthermore, as clarified in the FAQs on e-Invoicing issued by GSTN, e-invoicing is not applicable to invoices issued by an Input Service Distributor. Therefore, ISD invoices are subject to a separate invoicing regime and do not attract e-invoicing compliance, even if the entity otherwise crosses the e-invoicing threshold under regular GST registrations.

Q38. Whether invoices relating to ISD registration be reflected on the Invoice Management System (IMS)?

Ans: No, invoices pertaining to ISD will not appear in the Invoice Matching System (IMS). As clarified in the GSTN FAQs dated 22.09.2024, any ITC distributed through GSTR-6 by an Input Service Distributor will bypass IMS and instead flow directly into the recipient's GSTR-2B. This means ISD credits will be visible only in GSTR-2B, and not in the IMS summary.

(Source: https://tutorial.gst.gov.in/downloads/news/final_faqs_on_ims_22_09_2024.pdf)

Q39. In cases where the ITC pertaining to Goods & Services is recorded on the same invoice then how the ISD is required to distribute the said ITC?

Ans: Since the invoice will have ISD's GSTIN on it, once GSTR-1 is filed it will get populated with the entire amount in GSTR-6A. The ISD shall be required to bifurcate the credit into two parts and consider only the input services' ITC and discard the goods related ITC.

To avoid such wastage of credit it is advisable to communicate with the vendor to issue separate invoices for goods and services wherein goods will be invoiced to the registered persons concerned directly and services will be invoiced by ISD.

Q40. If an invoice is pertaining to FY 2024-25 however the ITC is availed in 2025-26 then whether the ITC is to be routed through ISD or not?

Ans: Such ITC should not be routed through the ISD and should be taken in regular returns only. This is because the mandatory applicability of the ISD mechanism is from 1st April 2025. Therefore, only those invoices received after 1st April 2025 should be routed through the ISD.

Q41. What are the late fees payable in case of a delay in filing ISD returns?

Ans: As per Notification No. 7/2018–Central Tax dated 27.01.2018, in case of delay in filing GSTR-6 by an ISD, a late fee of ₹50 per day is applicable i.e., ₹25 under CGST and ₹25 under SGST.

Q42. Whether the conditions of Section 16(4) are also applicable to ISD invoices?

Ans: In 16(4) w.r.t ISD, there can be two situations -

- i. **ISD issuing invoices** - As for the expiry of credit u/s 16(4), due date of 30th November applies to 'invoice and debit note'. Although ISD invoices flow from section 31 and Rule 54 is for invoice under special cases, Rule 36(1)(e) differentiates between 'invoice' and 'ISD invoice'. Additionally, once the eligibility and timeline check has been performed on the vendor invoice, the credit accrues (assuming conditions satisfied). ISD is only meant to distribute such accrued credit, imposing a time limit again on the ISD issuing invoice would be incorrect.
- ii. **ISD receiving invoices** - The invoices received by ISD are tax invoices as provided in Section 31 read with Rule 46. Therefore, the conditions provided in Section 16(4) shall be applied.

Q43. Section 20(3) of the CGST Act permits integrated tax credit to be distributed as either IGST or CGST, whereas Rule 39(1)(i) mandates that IGST credit shall be distributed only as IGST. How should this be interpreted and what should the taxpayer follow?

Ans: Section 20(3) of the CGST Act, 2017, provides that credit of integrated tax (IGST) can be distributed as either IGST or CGST, thereby offering a legislative flexibility in terms of the nature of credit that may be passed on.

However, the same section also states that this distribution must be done “*in such manner as may be prescribed.*” It is this prescribed manner, laid down under Rule 39(1)(i) of the CGST Rules, that restricts the distribution of IGST credit strictly as IGST only.

Thereby, while the Act permits IGST to be distributed as IGST or CGST, the Rule narrows the application by allowing only one method, i.e., distribution as IGST.

Therefore, this is a case where the rule making authority has chosen to operate this flexibility in a constrained way.

In practice, the GST portal is built to comply with Rule 39, and it only permits IGST credit to be distributed as IGST. Therefore, unless and until this rule is amended or struck down as ultra vires by a court, taxpayers are bound to follow Rule 39(1)(i) and distribute IGST credit only as IGST, despite the wider language in the parent Act.

Q44. *What if there is excess or short distribution of ISD credit by HO to its branches?*

Ans: If there is an excess or short distribution of input tax credit (ITC) by the ISD, the law provides a clear mechanism to address it through Section 21 of the CGST Act, 2017. As per the said section, any excess credit distributed by an ISD is recoverable from the recipient unit, along with interest and penalty under section 73 or 74, depending on whether the distribution involved fraud or not.

Additionally, the ISD itself may be liable for a general penalty under Section 122(1)(ix) for incorrect or irregular distribution of ITC. To provide clarity on such situations, the CBIC issued Circular No. 71/45/2018-GST dated 26.10.2018, which outlines the recovery process and emphasizes that the liability for wrongly availed credit lies with the recipient GSTIN, even though the error originated at the ISD level.

Therefore, accurate and proportionate distribution of ITC is critical to avoid disputes and compliance exposure.

Q45. *What are the penal consequences in case of failure to comply with ISD provisions?*

Ans: As per Section 122 (1)(ix) of CGST Act, if a taxable person takes or distributes the credit in contravention of Section 20 or rules made thereunder then he shall be liable for penalty of Rs. 10,000/- or tax evaded or ITC passed on.

Q46. *ITC has to be distributed among the various recipients. What shall be the fate be if one of the recipients is SEZ?*

Ans: Yes, SEZ units are also to be treated as distinct persons and accordingly, ITC must be distributed to them through the ISD mechanism based on their turnover ratio, as prescribed under Rule 39 of the CGST Rules.

However, since SEZ supplies are zero-rated under GST, distributing ITC to SEZ entities may result in credit accumulation, as there may be limited or no output tax liability against which the ITC can be utilized.

To mitigate this accumulated ITC, it is advisable to ensure that vendors directly invoice the SEZ units under LUT, thereby making the supply zero-rated at the vendor level itself, subject to proper procedural compliance. This allows the vendor to either claim a refund of unutilized ITC or make the supply without payment of tax. The principle was affirmed in the judgement of ***Britannia Industries Limited v. Union of India 2020 (42) G.S.T.L. 3 (Guj.)***, where it was recognized that zero-rated treatment should not result in denial of refund or blockage of credit at the SEZ level. Therefore, careful structuring of procurement and invoicing is essential when SEZ units are among the recipients in ISD distribution.

Q47. What is the requirement of the cash ledger in ISD portal when there is no payment mechanism?

Ans: Although ISD is not required to discharge tax liability, the cash ledger is still maintained on the ISD portal. This is because certain payments like late fees for delayed filing of GSTR-6 must be made through the ISD's electronic cash ledger.

Q48. What can be the common errors that can happen while implementing the ISD?

Ans: Following are the common errors that can happen while implementing the ISD –

- An invoice for common services which is meant for the ISD can be booked under non-ISD GSTIN
- Incorrect allocation of ITC among the branches – either calculation error or basis of distribution itself is wrong.
- Receiving RCM invoice for common services in the state other than in which ISD is situated.
- Lack of audit trail showing link between input services, recipient and the ratio applied.

Q49. In case where a taxpayer is having very minimal common expenses such as audit fees. Still mandatory for ISD?

Ans: To qualify as ISD, the following are the key elements as per Section 2(61) -

- a. An office of the Supplier,
- b. Which received tax invoice towards receipt of input services,
- c. For or on behalf of distinct persons and liable for distribution

Therefore, even a single common input service is procured and used across multiple registrations, the office receiving the invoice becomes liable to distribute the credit, and hence, ISD registration becomes mandatory. Therefore, even in cases of minimal or occasional common services, the entity is required to comply with ISD provisions once the ISD criteria are met.

Q50. *Now that it's been nearly two months since ISD became mandatory, how should businesses approach system implementation, and what are the key factors to re-evaluate their strategy?*

Ans: With nearly two months having passed since the mandatory ISD regime took effect (from April 1, 2025), many businesses have now experienced the real-world operational impact of distributing input tax credit (ITC) under Section 20 read with Rule 39 of the CGST Rules. This is an ideal time to revisit and refine ISD implementation strategies based on what's working, what's not, and what can be simplified or automated.

A sound ISD framework begins with a robust system of classification using organizational factors like:

- Business Place, Business Area
- Plant Code
- Cost Centre
- Document or Transaction Type
- Vendor Category / Risk Profile

These parameters help determine whether an expense is common or specific. The taxpayers must also focus on following cross-verification pointers:

- PO-level tagging of expenses as common or specific
- Vendor-level mapping, particularly for known common vendors (e.g., statutory auditors, consultants)

- Use of common cost centres to trigger ISD logic
- Handling of blocked/ineligible credits through dedicated temporary GLs to maintain clean audit trails

For many companies, the initial setup was done under time pressure, often resulting in manual workarounds or overly complex logic. This is the time to streamline and automate wherever feasible, particularly for recurring, high-value, or policy-bound expenses like audit fees, software licenses, legal retainers, etc.

However, automation should not come at the cost of clarity. Over-engineered workflows with too many variables can lead to inconsistencies, internal confusion, and litigation risks. Because an effective ISD implementation includes interplay between multiple departments of an organization who may not be well versed in GST law.

In summary, this post-implementation phase offers a timely opportunity to reassess ISD structures, simplify wherever possible, and align systems ensuring that input tax credits flow to the right state, for the right reason, and with the right compliance.

Conclusion:

Now that it has been nearly two months since the mandatory implementation of ISD compliances, businesses are entering a critical phase where initial setups must be evaluated not just for completion, but for sustainability. While many organizations may have invested significant time and effort into building their ISD frameworks, mere implementation is not successful, especially if the structure is impractical, over-engineered, or heavily dependent on manual processes.

In large organizations, where ISD touches multiple functions such as tax, finance, procurement, HR and IT, a system that is too complex will eventually break down, leading to inconsistencies, reversals, compliance failures, and increased litigation risk. A framework that works on paper but fails in day-to-day execution is a risk in itself.

This is the ideal time to pause, reassess, and simplify. Whether it's cost center mapping, PO tagging, or vendor-level controls, your ISD model must be practical, scalable, and clearly understood across functions.

And if, in this journey, you discover that a certain stand or interpretation taken earlier was incorrect or difficult to sustain, it is absolutely acceptable and wise to change course. As the Japanese saying goes, *"If you have boarded the wrong train, the best thing you can do is get off at the very next station."* The longer you wait, the more costly and complicated it becomes to return to the right path. Correcting early is not a weakness; it's strategic prudence.

These FAQs are curated to serve as a practical guide. It is not just to explain the law, but to help you navigate the operational nuances of ISD compliances with clarity and confidence. Use them as a living reference point as you refine your processes in the months ahead.

(For feedback or queries, reach out to us at ravikumar@hnaindia.com or vyankatesh@hnaindia.com)