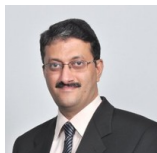


Input Service Distributor (ISD) under GST - Key Issues Explored

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The concept of an Input Service Distributor (ISD) under the Goods and Services Tax (GST) regime in India is a critical mechanism designed to streamline the distribution of Input Tax Credit (ITC) across various units of a business entity's units sharing the same Permanent Account Number (PAN). An ISD, typically an office, receives tax invoices for input services, like IT support or consultancy, and allocates ITC to other units (distinct persons) that benefit from these services. While designed for efficiency, the ISD framework poses interpretative and operational challenges.

This article delves into three key issues: the determination of the place of supply for invoices raised to an ISD, the scope and applicability of Rule 54(1A) for ITC transfer, and whether regular and ISD registrations should be treated as distinct persons, including the implications for invoicing between them.

Issue 1: Determination of Place of Supply for Invoices Raised on ISD

Determining the place of supply is central to GST, as it governs whether Integrated GST (IGST), Central GST (CGST), or State GST (SGST) applies and identifying the jurisdictional tax authority.

Section 2(61) of the CGST Act defines an ISD as *"an office of the supplier of goods or services or both which receives tax invoices issued under section 31 towards the receipt of input services and issues a prescribed document for the purposes of distributing the credit..."*

Defined under Section 2(61) of the CGST Act, an ISD facilitates ITC allocation for services like IT, audit, or advertising that benefit multiple locations, without consuming these services itself. This unique role raises a broader question: how should suppliers determine the place of supply when invoicing an ISD, given its procedural rather than substantive recipient status, and what are the implications across diverse supply scenarios?

The IGST Act governs the place of supply for services under Sections 12 and 13. For business-to-business (B2B) transactions, which apply when a supplier invoices an ISD (a registered person), Section 12(2)(a) of the IGST Act states: *"The place of supply of services, except the services specified in sub-sections (3) to (14), made to a registered person shall be the location of such person."*

Here, the ISD's location, tied to its distinct GSTIN, is typically treated as the place of supply. However,

this application assumes that the ISD is the "recipient" under Section 2(93) of the CGST Act, defined as *"where a consideration is payable for the supply of goods or services or both, the person who is liable to pay that consideration"* or, in other cases, the person to whom the supply is made.

Given that the ISD does not consume the service but merely receives invoices for distribution, it may not strictly qualify as the substantive recipient; the actual beneficiaries are the units receiving the service's benefit. This ambiguity renders the question of determining the place of supply open-ended. Section 20(1) mandates ISD registration for receiving invoices, suggesting a procedural recipient role, but if the ISD is not the true recipient, suppliers face uncertainty in applying Section 12(2)(a). Consequently, the place of supply defaults to the ISD's location in practice, yet this lacks clarity, necessitating explicit clarification from the GST authorities to resolve the inconsistency between the ISD's facilitative role and the IGST provisions.

Suppose a Mumbai-based supplier provides IT services worth ₹10 lakh to a company with an ISD in Delhi and operational units in Delhi, Maharashtra and Karnataka. The supplier issues an invoice to the Delhi ISD, charging 18% IGST (₹1.8 lakh), treating Delhi as the place of supply per Section 12(2)(a). The ISD then distributes ITC to the Maharashtra and Karnataka units, which actually use the IT services. If Delhi isn't the true recipient, should the supplier have issued separate invoices to Maharashtra and Karnataka instead, charging IGST based on their locations? This uncertainty leaves suppliers unsure of the correct tax regime, as the ISD's location is used in practice despite lacking clarity. GST authorities need to clarify whether the ISD's procedural role justifies it as the place of supply or if the benefiting units' locations should prevail.

Issue 2: Scope and Applicability of Rule 54(1A) for ITC Transfer to ISD

Rule 54(1A) of the CGST Rules, 2017, states: *"A registered person, having the same PAN and State code as an Input Service Distributor, may issue an invoice or, as the case may be, a credit or debit note to transfer the credit of common input services to the Input Service Distributor, which shall contain the following details..."* "Common input services" generally refer to services like audit fees, consultancy, IT support etc., which may or may not fall under Reverse Charge Mechanism (RCM) used by multiple units (distinct persons under Section 25) but invoiced to one office, such as a head office. Introduced on 23.01.2018 following the 25th GST Council meeting, Rule 54(1A) was intended to address a gap of no mechanism for an ISD to receive and pay tax on RCM services, nor for a normally registered entity to transfer ITC of such common RCM services to an ISD.

Rule 39(1A) specifically addresses RCM services under Section 9(3) or 9(4), stating: *"For the distribution of credit in respect of input services, attributable to one or more distinct persons, subject to levy of tax under sub-section (3) or (4) of section 9 [RCM], a registered person, having the same PAN and State code as an Input Service Distributor, may issue an invoice... to transfer the credit of such common input services to the Input Service Distributor..."*

However, Rule 54(1A)'s language is broader, not explicitly restricting its applicability to RCM services. Unlike Rule 39(1A), which targets RCM, Rule 54(1A) refers to "common input services" generally, suggesting it could encompass non-RCM services (e.g., forward-charge IT or consultancy services), provided the registered person and ISD share the same PAN and state code, and the invoice meets Rule 54(1A) requirements (e.g., GSTIN, taxable value). Until an amendment narrows its scope, a tentative view emerges: Rule 54(1A) may permit ITC transfer for both RCM and non-RCM services, with Rule 39(1A) providing specific guidance for RCM cases.

Example: Consider a company with a regular registration (head office) and an ISD, both in Delhi (same PAN and state code). A vendor invoices the head office ₹5 lakh (plus ₹0.9 lakh CGST/SGST) for IT services (forward charge, not RCM) benefiting units in Delhi and Hyderabad. Under Rule 54(1A), the head office issues an invoice to the Delhi ISD for ₹5 lakh (plus ₹0.9 lakh CGST/SGST), transferring the ITC. The ISD then distributes it under Rule 39(1) to Delhi (IGST ₹0.6 lakh) and Hyderabad (IGST ₹0.3 lakh). Alternatively, if the service were under RCM (e.g., legal fees of ₹5 lakh), the head office would pay the tax (₹0.9 lakh CGST/SGST) and could still use Rule 54(1A) or Rule 39(1A) specifically to transfer ITC to the ISD for distribution. In either case, the head office could theoretically bypass the ISD by issuing credit transfer invoices directly to Delhi and Hyderabad, raising the question: why mandate an ISD under Section 20?

The broader interpretation of Rule 54(1A) suggests vendors could invoice regular registrations for both RCM and non-RCM services, with ITC flowing to ISD and then to other units. This flexibility, while efficient, overlaps with the ISD's intended role as a centralized ITC distributor, creating ambiguity. If Rule 54(1A) covers all common input services, its purpose aligns with compliance ease but dilutes the ISD's uniqueness. GST authorities must clarify whether Rule 54(1A) intentionally extends beyond RCM, consistent with its invoice content requirements, or if its scope should align strictly with the GST Council's original RCM-focused rationale.

The need for ISD provisions under Section 20 and Rules 39 and 54(1A) ostensibly lies in centralizing ITC distribution for compliance and efficiency. However, if Rule 54(1A) enables such a flexible transfer from regular registration to ISD for non-RCM services, it undermines the ISD's unique role, suggesting vendors could invoice regular registrations instead of ISDs without disrupting ITC flow. This overlap creates ambiguity about Rule 54(1A)'s intended scope and hence a clear clarification from the GST authorities is essential to delineate Rule 54(1A)'s scope and justify the ISD's relevance amidst such flexibility.

Issue 3: Are Regular Registration and ISD Registration Distinct Persons?

A key issue is whether a regular registration and an ISD registration, despite sharing the same PAN and state code, are distinct persons under GST, and if so, what prevents the former from issuing a normal invoice to the latter. Section 25(4) of the CGST Act provides: *"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 shall, in respect of each such registration, be treated as distinct persons for the purposes of this Act."* Thus, a regular registration and an ISD, even with the same PAN and state code, are distinct persons due to their separate GSTINs. This legal distinction enables transactions between them, raising a key question: can a regular registration issue a normal tax invoice to an ISD under Section 31, bypassing Rule 54(1A)? If so, what justifies the ISD-specific framework under Section 20 and Rules 39 and 54(1A)?

Consider a scenario where a vendor directly invoices a branch (a regular registration) instead of the ISD for common services, and that branch then invoices the ISD to transfer ITC. This possibility further complicates the ISD's role. Section 25(4) permits transactions between distinct persons, and Section 31 mandates tax invoices for supplies between registered entities, suggesting no inherent bar to such invoicing. If this approach is viable, the ISD's purpose as a centralized ITC distributor could be undermined, as regular registrations might handle ITC transfers independently.

Example: Imagine a company with an ISD in Delhi and branches in Gujarat and Rajasthan, all distinct persons under Section 25(4). A vendor in Ahmedabad provides consultancy services worth ₹8 lakh (plus ₹1.44 lakh IGST) for the benefit of Gujarat, Rajasthan, and Delhi units, but invoices the Gujarat branch directly, treating Gujarat as the place of supply under Section 12(2)(a) of the IGST Act. The Gujarat branch, a regular registration, then issues a tax invoice to the Delhi ISD for ₹8 lakh (plus ₹1.44 lakh IGST) as a supply between distinct persons, transferring the ITC. The ISD subsequently distributes it to Gujarat (IGST ₹0.48 lakh), Rajasthan (IGST ₹0.48 lakh), and Delhi (CGST/SGST ₹0.48 lakh) under Rule 39(1). Alternatively, the Gujarat branch could invoice Rajasthan and Delhi directly, bypassing the ISD entirely.

In a different approach, if the vendor had invoiced a Delhi head office (regular registration), it could issue a normal invoice to the Delhi ISD for ₹8 lakh (plus ₹1.44 lakh CGST/SGST, assuming intra-state), with the ISD distributing ITC similarly. Both scenarios, vendor to Gujarat branch to ISD, or vendor to head office to ISD, demonstrate that regular invoicing between distinct persons is feasible. This flexibility questions the need for ISD-specific provisions. If a branch like Gujarat can receive invoices for common services and pass ITC to the ISD, or if a head office can do the same, the ISD's role as an intermediary seems redundant. The framework, designed to standardize ITC distribution, loses purpose if regular invoicing suffices, highlighting a potential inconsistency in GST design that demands clarification.

The ISD framework under GST aims to streamline ITC distribution but grapples with ambiguities. The place of supply remains unclear when invoicing an ISD, Rule 54(1A)'s broad scope overlaps with the ISD's role, and the distinct-person status allows regular invoicing that could bypass ISD mechanisms. These issues, illustrated through practical examples, highlight the need for statutory or administrative guidance to ensure compliance and operational clarity.