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Incentives distributed to dealers under promotional schemes constitute a supply, eligible for ITC – Karnataka AAR

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Summary

The Karnataka Authority for Advance Ruling (AAR) has held that the input tax credit (ITC) is eligible on the Goods and Services Tax (GST) paid on promotional goods procured for distribution to dealers upon achieving specified sales targets. The AAR elucidated that these promotional goods are not considered ‘gifts’ under the GST law since they are pre-agreed upon certain conditions and not voluntary. However, when dealers meet their sales targets, it is regarded as a non-monetary consideration flowing from the particular dealer, constituting it as a supply under GST. Even otherwise, distribution of promotional goods qualifies as permanent transfer or disposal of business assets, which constitute supply even without consideration in terms of Schedule I.

Facts of the case

- M/s. Orient Cement Ltd (the applicant) is engaged in manufacturing cement. To enhance its sales / promote the brand, the applicant launched target or performance-based discount schemes.
- Under these schemes, the benefit amount is credited to the dealer’s account based on the quantity and the grade of cement purchased.
- Subsequently, to pass on such benefits, the applicant distributes gold coins and white goods instead of adjusting it against the payment to be received from such dealers.
- The invoice for such goods is in the name of the applicant against which the ITC was availed.
- The applicant approached the Karnataka AAR regarding the admissibility of GST paid on the procurement of promotional goods and whether it constitutes as supply or qualifies as ‘permanent transfer or disposal of business assets’ under Schedule I of the CGST Act.

Applicant’s contentions:

- The inputs (promotional goods) procured for giving out credit have a direct nexus with the furtherance of business. Incentives are provided to dealers in the furtherance of business to promote and enhance sales.
- The applicant submitted that the object of the scheme is purely to promote the brand and not to offer any gifts voluntarily without conditions/eligibility criteria.
- From a supply perspective, the distribution of rewards cannot be regarded as the permanent transfer or disposal of business assets, as the said restriction is applicable only in respect of those assets that are capitalised in the books of accounts and not to the goods that are in the nature of revenue expenditure.

Karnataka AAR observations and ruling

[Advance Ruling No. KAR ADRG 27/ 2023; dated 24 August 2023]

- **Consideration for supply:** The achievement of marketing targets set by the applicant is an inducement from the dealer or can be viewed as a non-monetary consideration paid by the dealers. Since the transfer of goods (gold coins/white goods) is made for a consideration, it is covered in the definition of ‘supply’.
- **Scope of business assets** – The AAR noted that the goods are permanently transferred to the dealers on which the ITC was availed. Accordingly, it tantamounts to the ‘permanent transfer or disposal of business assets’ in terms of Entry 1 of Schedule I liable to GST. It opined that business assets include

inventory, and it does not necessarily be capitalised in the books of accounts.

- **Promotional scheme is in the furtherance of business:** In the present case, the goods/services procured as a reward are being supplied by them in the course of their business. Under the scheme, the benefit provided to the dealer is determined based on the amount credited to the dealer account, which is based on the quantity and the grade of cement purchased by such dealer.
- **Goods under the scheme do not qualify as 'gift':** The AAR opined that in normal parlance, a gift is something that is given without any conditions and stipulations. In the present case, rewards/promotional goods are issued as per the certain conditions mentioned in an agreement. Accordingly, the ITC is not restricted under Section 17(5)(h) of the CGST Act.

Our comments

The eligibility of ITC in the distribution of promotional goods has been a subject matter of litigation since the inception of GST law, with contradictory advance rulings in the past.

In the case of Biostadt India Limited, the Maharashtra AAR held that the ITC would not be available on goods given as 'gifts' when no GST is paid at their disposal.

In the case of GRB Dairy Foods Pvt Ltd, the Tamil Nadu Appellate Authority of Advance Ruling (AAAR) held that giving away goods/services under the promotional scheme is not a supply. Consequently, the ITC is not eligible on the GST paid on the goods/services procured for the scheme. The Karnataka AAAR took a similar stance in the matter of Page Industries Limited.

The present ruling contradicts with previous judgements, creating ambuiguity in the interpretation of GST laws. Treating distribution of promotional goods as a supply triggers the valuation implications, given no consideration is involved.

To address this ambiguity and avoid unnecessary litigation, it is advisable for the GST Council to provide further clarification on this matter.

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