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SHAPING A VIBRANT INDIA

# Implications of GST on post-sale discounts

## For consumer sector

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# Executive summary

## Fast-moving consumer goods (FMCG) sector is the fourth largest sector in the Indian economy with food and beverages, household and personal care and provides employment to around three million people in this country.

FMCG companies are bringing together suppliers, inventory management and distributor management within one ecosystem with the help of digital capabilities. E-commerce companies are making FMCG products more readily available, especially with their predominantly fulfilled time-bound delivery promises. Digital payments like e-wallets and UPI are making payment transactions smoother and extremely convenient.

Goods and service Tax (GST) has been quite favourable for FMCG companies. It brought the entire national market under the same umbrella. The GST Council reduced the tax rates down to 5% on most of the processed food items, which will make food products more consumer friendly, and might lead to an increase in consumption. Any reduction in the rate of tax on any supply of goods or services, or the advantage of input tax credit must be passed on to the recipient by way of commensurate reduction in prices, according to Section 171 of the CGST Act, 2017, which provides for anti-profiteering measures. Further, the Production Linked Incentive (PLI) scheme announced for food processing, white goods, and textile products, having an overall outlay of INR 27,821 crore, has turned out to be extremely beneficial for the sector. This is expected to boost capacity and exports.

Sales promotions have been used to expand the consumer base and enhance competitiveness. One of the purposes of a consumer promotion is to elicit a direct impact on the purchase behaviour of the companies. Consumers are very price-sensitive when it comes to consumer-packaged goods as these products make up a major part of their monthly spending and FMCG brands have always competed aggressively on prices.

# Indian FMCG sector: Overview

## FMCG, retail and e-commerce growth are projected to be aided by technological innovations, digital payments, hyperlocal logistics, analytics-driven customer engagement and digital marketing.

The revenue for FMCG sector grew at around **10-12%** in FY22 driven by a price-led growth and favourable base from the previous fiscal year. Additionally, the industry is projected to grow to a market size of USD 220 billion by 2025, propelled by digitisation, consumer-centric approach (such as direct doorstep delivery), government support (such as PLI schemes) and robust FDI inflow. Currently, urban markets of India account for **66%** of total FMCG consumption, whereas the rural areas account for **34%**.

With the rural consumption increasing at around two times the urban consumption, the rise in rural consumption will be key in driving the market. In addition to improved distribution channels and penetration of internet in Tier II-IV areas, demand for quality goods has maintained an upward trajectory in rural areas.

India's household and personal care is the leading segment, accounting for **50%** of the overall market. Healthcare accounts for **31%** and food and beverages comes in at **19%** in terms of market share.

Going forward, India has huge potential for e-commerce growth. Consumers have shown acceptance towards e-commerce model, as spending has shifted online now than it did in the pre-pandemic world. Furthermore, many home-grown e-commerce platforms are joining hands with Open Network for Digital Commerce (ONDC) to connect buyers with hyperlocal sellers. The integration will allow the discoverability of products for consumers and create a wider market for hyperlocal suppliers. The e-commerce market is expected to reach USD 99 billion by 2024, growing at a **27%** CAGR over 2019-24, with grocery and fashion/apparel likely to be the key drivers of incremental growth. In the quarter ended September 2022, e-commerce witnessed 37 deals valued at USD 704 million, according to Grant Thornton Bharat Dealtracker. The sector contributed to **10%** of overall deal volume in the quarter and **11%** of overall deal values. In addition, GST on FMCG products has also impacted the sector on several other fronts, such as logistical costs, warehousing, business operations and pricing of goods.

# Legal background on commercial credit notes under GST laws

To understand the GST applicability on commercial credit notes, it is imperative to understand related provisions under the CGST Act 2017.

**1.1** As per Section 15 of the CGST Act, 2017, value of a supply shall be transaction value which is the price actually paid or payable for such supply where supplier and recipient are unrelated and price is the sole consideration for the supply.

**1.2** The term 'value' does not include any discount which is given before or at the time of supply, if such discount is recorded in invoice. In case where the discount is given after supply, it will not be included if the discount is as per agreement at or before time of supply and ITC attributable to discount has been reversed.

**1.3** Further, under Section 34 of the CGST Act, 2017, credit note can be issued if the supply is returned, or where the supply is found deficient. In this regard, the government issued a circular in October 2018, wherein it was clarified that if credit note is issued within the applicable time limit, tax liability may be adjusted by supplier, subject to certain conditions.

**1.4** Further, another circular was issued in March 2019 to clarify many ambiguous issues on financial/ commercial credit note(s) and secondary discounts. Since this circular led to much confusion, the Department issued another circular in June 2019 to clarify various aspects on post-sale discounts and their valuation.

# Various schemes for marketing

## And impact of commercial credit notes under GST laws

**Various schemes are offered to suppliers by manufacturers to boost their supplies as part of their promotion drive. This section attempts to discuss all such schemes wherein commercial credit notes are issued to bring in the effect of various discount:**

### 2.1. Sell-in scheme (target based)

This scheme is offered by a supplier to a dealer wherein the supplier agrees to pay an amount by way of issuing credit notes, in respect of goods supplied to dealer, upon attainment/ achievement of mutually agreed target volume or value. Targets and rates/slabs are generally agreed/decided a priori but extended after supply.

In this case, discount is established as per an agreement entered at or before the supply. Based on above, it can be inferred that sell in scheme is a discount for achieving mutually agreed target volumes or value but not towards any act like undertaking special sales drive, advertisement campaign, exhibition, etc. **Therefore, the discount offered under this scheme may not attract GST**.

### 2.2. Sell-in scheme (fixed)

This scheme is offered by a supplier wherein the supplier pays out certain amounts by way of issuing credit notes, in respect of goods supplied to a dealer, without any obligation on the dealer to do any activity other than mere further supply. These credit notes reduce the actual price paid by the dealer to the supplier at the time of initial supply.

Based on Para 3 of circular dated 28 June 2019, it can be inferred that if such post-sale discount is given by supplier to dealer without any further obligation or action required at dealer's end, they will be related to original supply and would not be included in supply value. **Therefore, credit notes issued under this scheme may not attract GST**.

### 2.3. Sell-out scheme (go to market scheme)

A supplier agrees to pay an amount to the dealer and issues a credit note at a later date based on sales made by the dealer. This is based on attainment of mutually agreed targets value/ volume set by suppliers. Quantum of amount, targets, rates/ slabs, periodicity, etc., are generally agreed a priori, but extended after supply.

These discounts are generally based on products' final sale to consumers and offered by vendors to avoid excess stocking at dealer's end. This can be pre-agreed/fixed in amount or as percentage on dealer price or based upon different slabs for which different sell-out discount is provided.

This sell-out discount is a stand-alone discount given for achievement of sales volume and not towards any advertisement/exhibition/any activity or obligation. **Therefore, credit notes issued under this scheme may not attract GST**.

### 2.4. Sell-out scheme (non-target based)

A supplier agrees to pay a certain determined amount to a dealer, based on the sales made by them, irrespective of the targets. The essential condition is that these amounts are paid by the supplier to the dealer, on production of proof that these amounts are passed on as discounts in B2C transactions.

Based on the relevant provisions, we my infer that such post sales discount given by supplier will be related to original supply and GST may not be attracted on such amounts. **Therefore, credit notes issued under this scheme may not attract GST**.

### 2.5. Cash discount

Credit notes are issued by suppliers in the name of the dealer, when the dealer pays the full amount against the supplies received, either in advance or immediately after supply, without waiting for the generally agreed credit period.

Cash discounts refer to an incentive in return for paying a bill before the scheduled due date. These aim to motivate dealers to pay their bills within a certain time frame and give sellers an access to cash sooner than otherwise.

Discount is given by the supplier to the dealer without any further obligation or action required at the dealer's end. **Payment to goods received is a general business activity and such discount would be related to original supply and may not be subject to levy of GST**.

## 2.6. Price drop or tax rate cut

Price-drop discounts are given by way of commercial credit notes and are provided to maintain competitiveness of products against competing brand prices or to liquidate old stock when new or updated versions are launched. These discounts are given to revise prices of old models and are not in lieu of any activity/obligation from dealers.

Here, it can be inferred that price drop discount is a stand-alone discount given through entire supply chain on existing stock of old models based on sole discretion of the manufacturer and is not towards any advertisement/exhibition/any activity or obligation from the dealer.

**Therefore, as there is no supply per se by the dealer, we can infer that commercial credit notes in this scheme cannot be treated as consideration and therefore, credit notes issued under this scheme may not attract GST**.

## 2.7. Co-operative/marketing support scheme

Credit notes are received for certain payments from suppliers, in respect of supplier's share of expenses incurred by the dealer towards advertising in print and electronic media, marketing, etc. This scheme provides financial assistance on reimbursement basis for such expenses.

We understand that as a general industry practice, such amounts are not received in nature of mere reimbursement. Therefore, relying on clarification provided in Circular dated 28 June 2019, these transactions would be treated separately, and additional discount may be considered for undertaking advertisement campaign. **Therefore, credit notes issued under this scheme may attract GST**.

## 2.8. Space rental/display exhibition

As a general industry practice, FMCG dealers receive such payments from suppliers by way of credit notes where these amounts are paid as the dealer showcases specified goods in prominent spaces of the showroom, which is different from the general display to attract customer's attention.

Exhibiting at prominent spaces of a showroom brings benefits to business by way of raising brand awareness, meeting potential customer and for penetration of new product into the market.

In tune with the clarification provided by the Department, we understand that if additional discounts given by supplier are post-sale incentive which require dealers to do some act like undertaking special sales drive, exhibition etc., then such transaction would be a separate transaction. In such case, additional discount will be treated as a consideration for undertaking such activity. **In such cases, dealer will be required to charge GST on value of such additional discount and credit notes issued under this scheme may attract GST**.

## 2.9. Demo/defective piece discount scheme

In showrooms, many goods are put up for demonstration. During such time, wear and tear to goods is bound to take place, which impacts their value. However, as a general practice, dealers convince customer and supply such goods at a reduced price compared to the original price.

In such circumstances, credit notes are issued as compensation for wear and tear during exhibition but not directly for exhibition of products. Also, if there is no wear and tear during such exhibition, there would be no requirement for issuance of a credit note.

Based on the above discussion, it can be inferred that such additional discount may not be in the form of a post-sale incentive and is related to original supply. **Further, such an amount will not be included in value and where the suppliers are issuing credit notes in such circumstances, GST may not be required to be levied**.

# Conclusion

One of the key challenges faced by this sector is the volume of data involved in relation to the market which is required to analyse target markets and to increase customer base. The persistent market watch to keep an eye on the various schemes floated by competitors is also imperative. Each of those schemes/ incentives and discounts will trigger GST implications as well. The Government has taken positions relating to different types of marketing schemes and GST applicability on such schemes. However, a conclusive decision on the same is yet to be taken on the same. Otherwise, the Revenue authorities may continue questioning the non-levy of GST on such schemes until the issuance of any clear instructions from the Government.

It is important to understand the applicable legal provisions and analyse transactions on case-to-case basis to determine the taxability of such transactions. The analysis of secondary market schemes is required to confirm if they qualify as post-sale discounts eligible for deduction under section 15(3)(b) or be considered as a subsidy directly linked to price under Section 15(2)(e) of the CGST Act. If it qualifies as subsidy directly linked to price, it will attract GST in the hands of recipient.

# Acknowledgements


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