



CA. Rakesh Chhabra

Member of the Institute

Legal Framework for Post-Supply Adjustments under the GST Regime

This article discusses the complications of post-supply adjustments under the GST regime in India. The focus is on post-sale discounts, the issuance of credit notes and the reversals of corresponding input tax credits. It highlights the legal requirements under Sections 15(3)(b) and 34 of the CGST Act, emphasizing that the taxable value would be reduced only if terms are pre-agreed at the time of sale and the incidence of tax has not been passed to another person, and further, the corresponding ITC has been reversed by

the recipient. In this article, we also distinguish commercial and non-commercial credit notes. Recent amendments in Budget 2025 and CBIC Circular No. 212/6/2024 mandate documentary proof of ITC reversal.

The Goods and Services Tax (GST) in India has now been in place for eight years. GST has brought many significant structural reforms and uniformity in indirect tax across the country. However, there are several interpretational and operational issues in the various provisions. One of the most concerning issues is the GST Implications on post-sale discounts, including cash discounts, cashback schemes, rate reductions upon achieving the sales targets, promotional incentives and other performance-based discounts. These commercial arrangements are common in business practice and raise complex questions with respect to deduction from the value of supply and output tax liability, as well as corresponding reversal of Input Tax Credit (ITC) by the recipient.

This is further made more difficult to understand industry-specific variations in the structuring of such incentives, such as buy more save more, free samples and gifts, buy one get one offer, etc. In the absence of proper legal guidance and divergent advance rulings, businesses are often left navigating a grey area, resulting in various litigation and compliance disputes.

In this article, our aim is to discuss the legal principle that governs the post-supply adjustments under the GST regime, analyse the prevailing challenges or difficulties and recent judicial pronouncements and clarifications.

Understanding Post-Supply Discounts/ Adjustments

Under the GST regime, post-supply discounts or adjustments refer to any rate reduction or any downward revision in the consideration of supply after the supply of goods/services has been affected. These adjustments may arise due to pre-agreed commercial terms, performance-based incentives, or discretionary business decisions made post-supply of goods or services. While such practices are deeply entrenched in trade and commerce, however, their treatment under GST remains nuanced and often contentious.

The following are the main post-supply discounts:

i) Cash Discounts: These are savings given to customers for early payment or settlement of invoices.

ii) Cashback Schemes: These are given after a sale based on promotional campaigns or consumer behaviour.

iii) Target-Based Discounts: Reductions in rate upon achieving pre-established purchase volumes or sales targets.

iv) Promotional Discounts: These are linked to marketing campaigns, including freebies, sponsored trips or tours and price reductions on future purchases.

Legal framework under GST

The treatment of post-supply adjustments or discounts is governed by provisions under the **Central Goods and Services Tax Act, 2017** ("CGST Act"), read with the **Central Goods and Services Tax Rules, 2017** ("CGST Rules"), and various notifications issued by the tax authorities. Two critical aspects that govern these adjustments are:

- i) the valuation of supply under *Section 15(3)(b) of the CGST Act*,
- ii) the reversal of Input Tax Credit (ITC) obligations.

a. Conditions under Section 15(3)(b) of CGST Act

Section 15 of the CGST Act governs the provisions with respect to the value of taxable supply. As per the provisions of Section 15 (1) of the CGST Act, the value of a supply of goods or services or both shall be the transaction value which is the price actually paid or payable for the said supply of goods or services or both where the supplier and the recipient of the supply are not related and the price is the sole consideration for the supply.

Further, Section 15(3)(b) of the CGST Act provides that the value of a supply shall not include any discount which is given after the supply has been affected, if:

- it is established in terms of the agreement entered into at or before the time of supply and linked to relevant invoices,
- input tax credit attributable to the discount, as evidenced by a document, has been duly reversed by the recipient of the supply.

This provision is important in determining whether a post-supply discount would be excluded from the transaction value, resulting in a reduction in the taxable value and consequently the GST liability. If the discount does not satisfy these criteria, it must be included in the value of supply, and GST must be paid. It means there is no need to issue credit notes using GST implications, *i.e.*, the supplier would not reduce its output liability, and the recipient would not reverse the proportionate ITC. Only if it is predetermined at the time of sale/supply of goods/services and the recipient has reversed the proportionate ITC, then it should be reduced from the output tax liability of the supplier/seller.

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b. Input Tax Credit (ITC) Reversal Requirement

Section 34 of the CGST Act governs the provisions with respect to the issuance of credit and debit notes, which are the instruments typically used to make adjustments after a supply. Where a credit note is issued by the supplier to reflect a reduction in the value of supply due to discounts or other adjustments, on the other hand, the recipient is required to reverse the proportionate ITC availed on the original transaction.

The rationale for ITC reversal is to maintain parity between the supplier's reduction in output tax liability and the recipient's entitlement to claim credit, thereby preventing undue tax benefits. Failure by the recipient to reverse ITC can lead to adverse tax consequences, including demands for differential tax and interest.

The timing of ITC reversal is also significant as it generally needs to be affected in the tax period in which the credit note is received. This aligns the supplier's and recipient's tax positions and ensures proper reconciliation in GST returns.

Roles and Treatment of Credit Notes under GST

Under the GST regime, credit notes serve as a key instrument for post-supply adjustments, which enables

the suppliers to rectify mistakes in the original tax invoices or respond to changes in the nature of the supply after the issuance of a tax invoice.

As per Section 34(1) of the CGST Act, a registered supplier is empowered to issue a credit note where the taxable value or tax charged in the original invoice exceeds the actual amount payable or where a recipient returns defective goods due to quality issues. A supplier can lawfully reduce their output tax liability by issuing a credit note, provided the corresponding ITC has been reversed by the recipient. The supplier must disclose the credit note details in Form GSTR-1 for the relevant tax period and make the necessary adjustment in Form GSTR-3B, which records the net tax payable. However, the CGST Act places a time limitation on such adjustments. The credit note must be declared on or before 30th November of the following financial year or before the date of filing of the relevant annual return, whichever is earlier.

Importantly, Section 34(2) of the CGST Act, as amended in the Budget 2025, imposes certain restrictions on the issuance of credit notes. A credit note cannot be issued to reduce tax liability if the input tax credit has not been reversed by the recipient and the incidence of tax has already been passed on to another person, ensuring adherence to the principle of unjust enrichment.



Commercial vs Non-Commercial Credit Notes

In practical business scenarios, credit notes issued post-supply can broadly be categorized into two types:

- a) commercial credit notes (also referred to as financial credit notes)
- b) non-commercial credit notes (also referred to as tax credit notes)

This distinction has not been defined under the GST law, it has emerged from various departmental circulars, interpretational guidance and industry practice.

Generally, non-commercial credit notes are issued where there is a direct impact on the taxable value of the supply and GST discharged on the same, such as in cases of goods return, rate difference, etc. These are issued in accordance with the provisions of Section 34 of the Act, which allow the supplier to reduce their output tax liability subject to the recipient reversing the corresponding ITC. These credit notes are declared in GSTR-1 and reflected in GSTR-3B to adjust the tax liability.

On the other hand, commercial credit notes are issued where there is no impact on the taxable value of the supply and no requirement to reduce the output tax liability, as per the provisions of the



“Section 34 of the CGST Act governs the provisions with respect to the issuance of credit and debit notes, which are the instruments typically used to make adjustments after a supply.”

Act supported by various circulars and judicial pronouncements, such as in cases of cash discounts or incentives for early payments, etc. These discounts are generally not agreed upon at the time of supply; therefore, they do not meet the conditions laid down under Section 15(3) of the CGST Act. As a result, the supplier may issue a commercial credit note to reflect a commercial understanding; in this scenario, neither the supplier would reduce their original tax liability, nor the recipient would reverse their ITC. This position has been clarified by the Central Board of Indirect Taxes and Customs (CBIC) in *Circular No. 92/11/2019-GST dated 07th March 2019* and *105/24/2019-GST dated 28th June 2019*, which clearly states that in such cases, the credit note is merely a financial document and does not impact GST returns or tax computations. Hence, commercial credit notes serve a purely accounting or contractual function without invoking any post-supply tax adjustments under GST.

Judicial Pronouncements and Departmental Clarifications

- a) **Circular No. 92/11/2019 GST dated 7th March 2019**

“It is hereby clarified that financial/commercial credit note(s) can be issued by the supplier even if the conditions mentioned in clause (b) of sub-section (3) of section 15 of the said Act are not satisfied. In other words, credit note(s) can be issued as a commercial transaction between the two contracting parties.”

It is further clarified that such secondary discounts shall not be excluded while determining the value of supply as such discounts are not known at the time of supply and the conditions laid down in clause (b) of sub-section (3) of section 15 of the said Act are not satisfied”

- b) **Circular No. 105/24/2019 GST dated 28th June 2019**

“It is clarified that the dealer will not be required to reverse ITC attributable to the tax already paid on such post-sale discount received by him through issuance of financial / commercial credit notes by the supplier of goods in view of the provisions contained in second proviso to sub-rule (1) of rule 37 of the CGST Rules read with second proviso to sub-section (2) of section 16 of the CGST Act as long as the dealer pays the value of the supply as reduced after adjusting the amount of post-sale discount in terms of financial/commercial credit notes received by him from the supplier of goods plus the amount of original tax charged by the supplier.”

However, this circular has been withdrawn by the CBDT vide *Circular No. 112/31/2019 – GST dated 03rd October 2019*

- c) **Circular No. 212/6/2024-GST dated 26th June 2024**

In practice, a key challenge under the GST framework has been the verification of ITC reversal by the recipient in cases where the supplier issues a credit note under Section 15(3)(b)(ii) of the CGST Act for post-sale discounts. The law permits the exclusion of such discounts from the taxable value only when certain conditions are met, particularly that the recipient reverses proportionate ITC. To address this issue, the government has issued Circular No. 212/6/2024-GST dated 26th June 2024, providing a procedural framework for substantiating the reversal of ITC in such cases. As per the circular, where the aggregate value of credit notes

issued by a supplier exceeds ₹5,00,000 in a financial year, the supplier shall obtain a certificate from a Chartered Accountant (CA) or Cost Accountant (CMA) certifying that the recipient has duly reversed the corresponding input tax credit. In cases where the total value of such credit notes is ₹5,00,000 or less, a self-declaration or undertaking from the recipient of the supply will suffice.

The supplier is required to maintain such certificates or undertakings and furnish them before the tax authorities if called upon during proceedings such as audit, investigation, scrutiny, or adjudication. Notably, this requirement also applies to past periods, where the supplier has issued credit notes for post-supply discounts and wishes to substantiate the reduction in taxable value. In such instances, the taxpayer may procure and furnish the relevant CA/CMA certificates or recipient undertakings, as applicable, to the concerned adjudicating, audit, or investigative authority to evidence the reversal of ITC in compliance with Section 15(3)(b)(ii).

- d) There is no requirement to reverse ITC with respect to commercial credit notes issued by suppliers towards cash discounts for early payment and incentives/



“The supplier must disclose the credit note details in Form GSTR-I for the relevant tax period and make the necessary adjustment in Form GSTR-3B, which records the net tax payable.”

schemes provided without GST adjustment. Furthermore, such transactions do not fall under the purview of supply by the recipient to the supplier. [Advance Ruling in the case of Mr. Rajesh Kumar Gupta Prop. M/s Mahaveer Prasad Mohanlal, Authority for Advance Ruling-MP]

- e) Where a commercial credit note is issued by the supplier to the recipient and the recipient's account is duly adjusted in the supplier's books of accounts, such adjustment shall be treated as 'payment' made by the recipient. It is ruled out in the advance ruling in the case of M/s Senco Gold Ltd [case No. 08 of 2019, West Bengal Authority for Advance Ruling]:

“The Applicant can pay the consideration for inward supplies by way of setting off book debt. The GST Act and rules made there under does not restrict the recipient from claiming the input tax credit when consideration is paid through book adjustment, subject to the conditions and restrictions as may be prescribed and, in the manner, specified in Sections 16 and 49 of the CGST Act.”

Conclusion

There is still a lot of ambiguity and interpretational uncertainty about how post-supply adjustments are handled under the GST framework. The law provides a framework through Sections 15(3) and 34 of the CGST Act and associated rules for recognizing valid post-supply discounts and credit notes; however, its practical application

remains a challenge due to different business practices. The key takeaway is that for any post-supply discount to result in a reduction of taxable value and output tax liability, strict adherence to the statutory conditions is required.

The government's focus is on plugging revenue leakages and ensuring proper credit matching through the introduction of an amendment in the recent budget and introducing a circular with respect to obtaining a certificate/undertaking from the recipient regarding the reversal of ITC.

In light of these complications, businesses must exercise due diligence when structuring post-supply incentive schemes, establish strong documentation and adopt consistent tax treatment backed by legal advice. A proactive compliance approach is necessary to reduce litigation risk and guarantee conformity with the purpose and changing interpretation of the GST law, given the disparity in advance decisions and the recurring modifications in CBIC circulars.

Furthermore, the recipient of the supply is required to evaluate the nature of the discount, like an advertisement campaign, display discount, etc. Such discounts would be a separate transaction; the discount amount would be the consideration for the supply of service by the recipient to the supplier of goods. The recipient would be required to charge GST on such an amount, and the supplier would be entitled to claim ITC of the same.

Author may be reached at
rakeshchhabra20@live.com
and eboard@icai.in