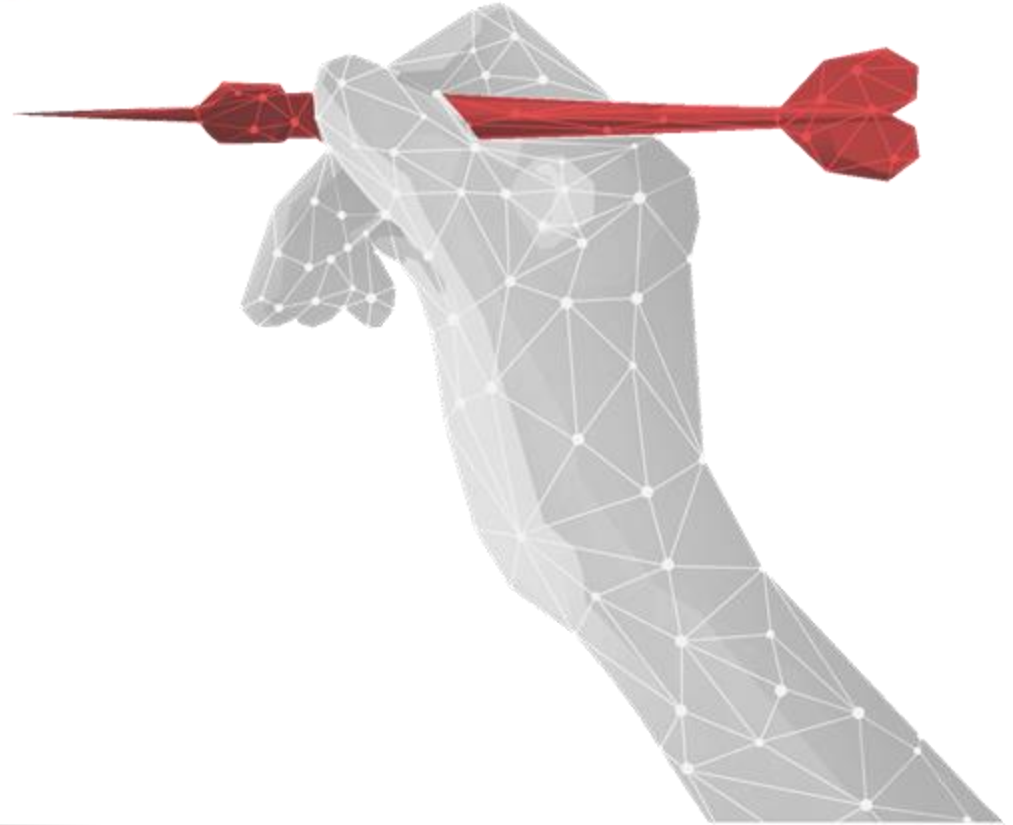


J A A & ASSOCIATES
CHARTERED ACCOUNTANTS



Newsletter

September- October 2021

GST curve balls – Why didn't my auditor point them out

The road of life twists and turns and
no two directions are ever the same.
Yet our lessons come from the
journey, not the destination.

— *Don Williams* —

GST Challenges

GST turned four this July.

As the department came out of the VAT/Service Tax hangover and Covid-19 revenue pressures – we are seeing a barrage of assessment / audit notices under GST laws.

Many of the observations are routine – input tax credit frauds ¹ or GSTR 2A reconciliations

Some are interesting new takes

Others are re-interpretations of settled positions – a sign of times to come as GST litigation picks up speed

Auditors dilemma

Auditors and Internal auditors face this question as the notices flow in – ***why didn't you forewarn us?***

We bring you 3 case studies - covering one example each relating to trading industry, export/imports and cost-plus back-offices.

If you have similar interesting issues, write to us at office@jaa-associates.com and let us know.

¹ https://www.business-standard.com/article/economy-policy/gst-officers-detect-rs-4-000-cr-of-input-tax-credit-fraud-in-apr-jun-121080901139_1.html

'Trading' barbs – a deep dive into your 4 year old records

While questions on input tax credits mostly relate to reconciliation with GSTR2A, a curious tax officer asked a trading company to match the closing stock value with the closing balance of input tax credits.

Argument of the tax officer was that a trading company making profits should generally not have accumulated input credits which are not commensurate with the tax component of the stock



Author's notes

While this is logically sound, maintenance of such reconciliations is not mandated under law

Such reconciliation would require a deep – dive on the entire tax filings and stock statements right from inception to ensure stock vs. input credit is matched for every line item

Imagine a company with products with varying rates of out put tax, exports, inputs of various kinds and the kind of analysis required to allow this conclusion

'Delivery' difficulties – *your forward cover may be taxable*

Tax officers question was that forward exchange contracts for foreign exchange receivables / payables are settled by delivery and hence taxable –

The officer has relied upon FAQs / instructions of CBIC to arrive at the conclusion that **derivatives which are settled by delivery are taxable**,

Author's notes

Even assuming that such forward exchange contracts are settled by 'delivery', the delivery is of foreign currency which is nothing but money

Further, what is taxable, the premium, the entire settlement or only the net difference?

This is a case of creativity which would escape every CFO, not to mention the auditors who may henceforth be expected to be as creative

'Intermediary' Troubles – *your back office export invoice may be taxable*

Cost plus back-office of foreign holding company is a typical structure – one of the backbones of the \$150 Bn Indian IT economy

The tax officer has analysed this structure in detail and arrived a conclusion that the subsidiary is nothing but an agent of the foreign holding company since they have equity control (which makes them deemed principals) and all the expenses are reimbursed with margin (such margin being deemed commission charged by agent).

Accordingly it was concluded that back-office cost-plus company is an intermediary and thereby the services exported should suffer GST since place of supply is within India.

Author's notes

The fact that the IT services provided by back offices are IT exports are corroborated under various regulations / Laws – FTP / STPI (Softex) and existing precedences

The tax officer seems to be trying to get cut the belly of the goose laying the golden egg

Such re-interpretations of well established business structures merely to collect taxes result in burdening the already over-worked judiciary (not to mention the overworked taxpayers) may not be desirable

Especially in a climate where the government wants to seem business friendly (remember Cairn Energy?)



**RBI, NFRA, ICAI –
Who's the boss**



Who's the boss

There is no doubt that any profession needs to be regulated to repose trust, acceptability and for public good

Chartered Accountants *aka* auditors have traditionally been governed by ICAI and its various committees.

ICAI council itself has elected members of the profession as well as government nominees

There is a system established over decades of jurisprudence



Recent 2 events have put the spotlight back on who is the auditor answerable to?

Can RBI unilaterally debar a firm, in effect take a disciplinary step on the auditors – erring or not? ¹

Does NFRA have powers over shadowing that of ICAI? ²

¹ <https://economictimes.indiatimes.com/industry/services/consultancy/-/audit/rbi-bans-haribhakti-co-for-two-years-from-undertaking-any-audit-assignments/articleshow/86959255.cms>

² <https://www.thehindubusinessline.com/economy/micro-small-and-medium-companies-nfra-floats-consultation-paper-on-statutory-audit/article36748848.ece>

JAA view

1. There is a need to ease business –

These can be achieved by

Reduce NCLT timelines – especially for liquidation or other corporate action that facilitate simplification

Allow easy conversion into LLP/partnership firm – ease tax laws to allow the same

Don't reduce credibility of a company form of organization by making it sans audit.

2. Don't do away with audit - harmonize–

Harmonise audit scopes of GST/IT/Statutory audits. Reduce data collection initiatives as part of audit – let data analysis take care of it

Don't reduce credibility of a company form of organization by making it sans audit.

Like earlier – allow conversion of entities that don't have significant public stakeholders into easier forms of organization

JAA view

3. Regulation

ICAI has handled professional regulation of Chartered Accountants for nearly a century

If the Government feels the need to regulate, create one regulator with clear standards, mandate and participation.

For example, PCAOB in the US only regulates audit profession for listed companies

4. Disciplining

Set up time bound and fair investigation of disciplinary complaints

Currently any fraud leads to a witch hunt of the auditors – be it IL&FS or SREI, the impact and public scrutiny of auditors is much higher than the directors and operational executives

What should we do?

We as CAs should look to the future

Develop multi-disciplines – data analytics, fraud, pattern analysis – move with the needs of the current trends

Create capabilities in Information Security, Cyber Security, General Computer Controls

Have capability assessment and enhancement for members – qualify the members

Instead of being wounded by continuous regulatory ‘set-backs’

Address each challenge:

1. Address questions on valuation that led to Income Tax Act changes removing ‘Accountants’ as one of the parties to issue report – investigate and take action quickly – Enhance valuation capabilities
 2. Audit quality – subscribe, set a methodology/framework, create qualification criterion within firms
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Some notes



While responses by industry for NFRAs consultation paper follow the red herring of ease of doing business, they ignore the implied credibility basis which Indian startups have been raising billions of capital, the basic trust in the business economy

CA firms have continuously been opposing any moves to regulate by the NFRA saying that the profession is capable of self regulation – has the profession lived up to this belief?

https://www.linkedin.com/posts/amarjit-chopra-91a7b530_debarring-of-haribhakti-company-llp-by-activity-6854295001237622784-a-mx

<https://taxguru.in/company-law/open-letter-chairman-nfra-opposing-consultation-paper-abolishing-statutory-audit.html>

<https://yourstory.com/smbstory/nfra-auditing-msmes-financial-statements-gst-small-business/amp>

Thank You
