

Handbook on Finalisation of Accounts with GST Perspective



GST & Indirect Taxes Committee
The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

**Handbook on
Finalisation of Accounts
with
GST Perspective**



The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

© The Institute of Chartered Accountants of India

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form, or by any means, electronic, mechanical, photocopying, recording, or otherwise without prior permission, in writing, from the publisher.

DISCLAIMER:

The views expressed in this book are of the author(s). The Institute of Chartered Accountants of India may not necessary subscribe to the views expressed by the author(s).

The information contained in this book has been drawn primarily from the www.cbic.gov.in and other sources. While every effort has been made to keep the information in this book error free, the Institute or any office of the same does not take the responsibility for any typographical or clerical error which may have crept in while compiling the information.

First Edition : November, 2020

Authors Name : CA. S Ramesh and CA. K Arun Kumar

Committee/Department : GST & Indirect Taxes Committee

E-mail : gst@icai.in

Website : <http://www.icai.org>; <https://idtc.icai.org>

Price : ₹ 80/-

ISBN : 978-81-8441-

Published by : The Publication Department on behalf of the Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi - 110 002.

Printed by : Sahitya Bhawan Publications, Hospital Road, Agra - 282 003.

Foreword

The introduction of Goods & Services Tax (GST) in India is one of the most significant indirect tax reforms since Independence. The reform that took more than a decade of mutual co-operation, continuous discussion and intense debate between Central and State Governments about implementation methodology, was finally implemented with effect from 1st July 2017, subsuming almost all indirect taxes at the Central and State levels. As the journey of GST implementation progressed in India, the authorities have been quick to address the various challenges faced by the Industry and public concerns by issuing a series of notifications, clarifications, press releases and FAQs, to resolve a wide range of concerns.

The GST along with its challenges have brought in various benefits also like creation of National market by bringing down fiscal barriers amongst the States and has mitigated the cascading effect of taxes by allowing seamless credit of input tax across goods and services. The Institute of Chartered Accountants of India (ICAI) through its GST & Indirect Taxes Committee has been playing a vital role in the implementation of GST in India by providing suggestions to the Government at each stage of development of GST. Further, the Institute has been playing proactive role and is a catalyst in dissemination of knowledge and awareness through technical publications, news letters, e-learning and organizing various programmes, certificate courses, webcasts etc. for all stakeholders.

I am happy to note that the GST & Indirect Taxes Committee of ICAI has now taken an initiative to issue a series of Handbooks covering various procedural aspects of GST and in that series is bringing out this **Handbook on Finalisation of Accounts with GST perspective** with an objective to provide guidance to the readers on this subject matter. The Handbook explains the various precautions to be taken with GST perspective while finalising of accounts in a simple and easy to understand language and is aimed at updating the knowledge base of members in a lucid and concise manner.

I congratulate CA. Rajendra Kumar P, Chairman, CA. Sushil Kumar Goyal, Vice-Chairman and other members of GST & Indirect Taxes Committee for coming out with this Handbook and for taking active steps in providing regular guidance to the members and other stakeholders at large.

I am sure that Members will find this publication very useful in discharging the statutory functions and responsibilities under the GST laws in an efficient and effective manner.

Place: New Delhi

Date: 10th November, 2020

CA. Atul Kumar Gupta

President, ICAI

Preface

Goods and Services Tax (GST) was introduced in India from 1st July, 2017. It is one of the major tax reforms since independence in the area of indirect taxation. It was introduced with the objective to mitigate the cascading effect of taxes by allowing seamless credit across goods and services, facilitate free flow of goods and services across India and boosting tax revenue from better compliance and widening the tax base. A remarkable feature of GST implementation is that all the States in India came together with the Centre to form a unique federal body called GST Council, which is entrusted with the objective of recommending policies and procedural matters in the formation and implementation of GST legislation. The spirit of co-operative federalism took deep roots thereby ensuring that large federal countries like India can implement the GST Law.

In order to facilitate an understanding of the various compliances under GST, the GST & Indirect Taxes Committee of ICAI has taken an initiative to prepare a handbook on procedural aspects like registration, refund, return, invoice etc. One of the results of such initiative is this **Handbook on Finalisation of Accounts with GST perspective**. An attempt has been made here to cover all aspects related to finalisation of accounts at one place and is intended to give general guidance to all stakeholders and also help them in resolving issues that they may face during the course of their compliances under the GST. This Handbook on Finalisation of Accounts with GST perspective is comprehensive containing an analysis of the entire provisions under the law including notifications, circulars or orders upto 31st October, 2020 issued by the Government from time to time along with FAQ's, MCQ's, Flowcharts, Diagrams, Illustrations etc. to make the reading interesting and understanding easier.

We stand by the Government in our role as “Partners in GST Knowledge Dissemination” and have always been supporting the Government with our intellectual resources, expertise and efforts to make GST error-free.

We sincerely thank CA. Atul Kumar Gupta, President and CA. Nihar Niranjana Jambusaria, Vice-President, ICAI for their encouragement to the initiatives of the GST & Indirect Taxes Committee. We express our gratitude for the untiring effort of CA. S Ramesh and CA. K Arun Kumar for sharing their

intellectual expertise and CA. Virender Chauhan for reviewing this publication. We place on record the services and unstinted support provided by the Secretariat of the Committee.

We record here the dedicated and devoted work done by the Secretary of the Committee, CA. Sharad Singhal who passed away at a very young age of 36 on 26th September 2020. The World of GST in general and our Committee in particular will miss his intellectual expertise. The will of the Almighty prevails over everything and all of us have to accept His decision with a bow.

We trust this Handbook will be of practical use to all the members of the Institute and other stakeholders. We also welcome suggestions at gst@icai.in and request you to visit our website <https://idtc.icai.org> and provide valuable inputs in our journey to make GST truly a good and simple tax.

CA. Rajendra Kumar P
Chairman
GST & Indirect Taxes Committee

CA. Sushil Kumar Goyal
Vice- Chairman
GST & Indirect Taxes Committee

Place: New Delhi
Date: 10th November, 2020

Contents

Chapter 1 – Introduction.....	1
Chapter 2 – Audit approach to GST compliances	6
Chapter 3 – Review of Balance Sheet	9
Chapter 4 – Statement of Profit & Loss	19
Chapter 5 – CARO & Tax Audit.....	35
Chapter 6 – FAQs	38

Chapter 1

Introduction

1.0 Finalisation of Accounts

The term 'Finalisation of Accounts' refers to the process of planning and control of activities relating to the preparation of the Financial Statements of a business entity.

There must exist a well-defined system to ensure, (a) timely preparation of the Financial Statements, (b) compliance with the various statutes applicable to the entity, and (c) that the Financial Statements represent a true & fair view of the financial status of the entity.

The procedure must encompass all the financial activities conducted or entered into, during the financial year of the business entity.

1.1 Financial Statements

Financial Statements are formal written records of the financial activities and position of a business entity. These statements are the main source of information for various stakeholders regarding the profitability and financial position of a business. As major decisions by stakeholders having a financial impact are taken based on the Financial Statements, it is imperative that they must present a true and fair view of the financial position. To ensure the same, auditing of these Financial Statements has been largely mandated by various statutes.

Financial Statements normally comprise of-

- (a) The statement of financial position (also known as the Balance Sheet) presents the financial position of the entity as on a given date.
- (b) The income statement (also known as the Profit & Loss Account) discloses the entity's financial performance over a specified period.
- (c) The Cash Flow Statement depicts the movement of cash and bank balances over a specified period.

- (d) Statement of Changes in Equity (also known as the statement of retained earnings) depicts the movement of owners' equity over a period of time.

While the statements mentioned in (a) & (b) above are to be prepared by all business entities, the Cash Flow Statement and Statement of Changes in Equity are mandated only for specified organisations.

1.2 Notes to Financial Statements

Any explanatory note annexed to, or forming part of, any document referred to in (a) to (d) above will also form part of Financial Statements as per section 2(40) of the Companies Act, 2013.

Reference is invited to Paragraph 8 of SA 700 (Revised) – “Forming an Opinion and Reporting on Financial Statements”, set out below:

“Reference to “financial statements” in this SA means “a complete set of general purpose financial statements, including the related notes.” The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information and any other information required to be included as part of the financial statements by the laws and regulations governing the entity.”

Attention is also invited to the following paragraphs of the Preface to the Statements of Accounting Standards-

“Para 3.4 The term ‘General Purpose Financial Statements’ includes balance sheet, statement of profit and loss, a cash flow statement (wherever applicable) and statements and explanatory notes which form part thereof, issued for the use of various stakeholders, Governments and their agencies and the public. References to financial statements in this Preface and in the Standards issued from time to time will be construed to refer to General Purpose Financial Statements.”

“Para 6.1 The Accounting Standards will be mandatory from the respective date(s) mentioned in the Accounting Standard(s). The mandatory status of an Accounting Standard implies that while discharging their attest functions, it will be the duty of the members of the Institute to examine whether the Accounting Standard is complied with in the presentation of financial statements covered by their audit.

In the event of any deviation from the Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviation”.

From a reading of the above-mentioned Paragraphs, it is clear that a complete set of Financial Statements should include related notes even in the case of non-corporates. It is imperative that an auditor engaged in attesting Financial Statements must ensure that explanatory notes are available and made an integral part of the same. Preparation of the notes is the responsibility of the auditee.

1.3 Audit of Financial Statements

Audit is mandatory for all entities registered under the Companies Act, 2013. In the case of non-corporate entities, even if audit of their accounts has not been mandated by the statutes governing them, the taxation Acts such as the Income Tax Act, 1961 and the Central Goods and Services Tax Act, 2017 have made audit mandatory for business entities having gross turnover/ receipts beyond a specified limit. Thus, Financial Statements are invariably audited by public accountants and or Government Regulators to ensure accuracy and for tax, financing, or investment purposes.

1.4 Impact of GST law on finalisation of Financial Statements

The primary objectives of an auditor is to (a) obtain reasonable assurance as to whether the Financial Statements, as a whole are free from material misstatement, whether due to fraud or error; and (b) to ensure that the Financial Statements give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the entity as at the date of closing of accounts, of its profit/ loss and other comprehensive income, consolidated changes in equity (if applicable) and cash flows for the year/ period then ended.

To achieve the above stated objective, it is imperative that an auditor should check for compliance with GST law and regulations.

Section 35(5) of CGST Act, 2017 states that every registered person whose turnover during a financial year exceeds the prescribed limit, shall get his accounts audited by a Chartered Accountant or a Cost Accountant and shall submit a copy of the audited annual accounts, the reconciliation statement

Handbook on Finalisation of Accounts with GST Perspective

under sub-section (2) of section 44 and such other documents in such form and manner as may be prescribed. The Proviso to this sub-section excludes from the purview of audit, any Department of the Central Government or a State Government or a local authority, whose books of accounts are subject to audit by the C&AG of India or by an auditor appointed for auditing the accounts of local authorities under any law for the time being in force.

Section 44(1) of CGST Act, 2017 states that every registered person, other than an Input Service Distributor, a person paying tax under section 51 or section 52, a casual taxable person and a non-resident taxable person, shall furnish an annual return for every financial year electronically in such form and manner as may be prescribed on or before the thirty-first day of December following the end of such financial year.

Section 44(2) of CGST Act, 2017 states that every registered person who is required to get his accounts audited in accordance with the provisions of sub-section (5) of section 35 shall, furnish electronically, the annual return under sub-section (1) along with a copy of the audited annual accounts and a reconciliation statement, reconciling the value of supplies declared in the return furnished for the financial year with the audited annual Financial Statement, and such other particulars as may be prescribed.

The prescribed forms for Annual Return and the Reconciliation Statement to be attested by the auditor (where applicable) are FORM GSTR-9 and FORM GSTR-9C, respectively.

It is evident from the above, that the due date for filing of FORM GSTR-9 & FORM GSTR-9C is 31st of December, following the end of the financial year. The due date prescribed for submission of audited accounts under various other Acts such as Companies Act, 2013 and the Income Tax Act, 1961 is earlier to the date prescribed under the GST Act. Consequently, the business entities and the auditors generally finalise the Financial Statements and file the same with the Registrar of Companies (in the case of corporates) and the Income Tax authorities and then commence the process of preparing the Annual Return prescribed under the GST Act. This process may not be the right approach as errors of omission and commission noticed during the GST audit process may result in material misstatement of the Financial Statements affecting the 'True & Fair' view of the same.

To ensure that there are no major/ material misstatements, it is imperative that an auditor checks compliance with GST laws and rules even during the

finalisation and audit of the Financial Statement under other statutes. It will not be out of place to state that the auditor should broadly review the reconciliation items for differences between books of accounts and GST returns before issuing his audit report to ensure that there are no major surprises during GST audit.

An illustrative list of reconciliations is set out below:

- Balance of Electronic Credit ledger with ITC in books
- Balance of Electronic Cash ledger with excess cash paid in books
- GST paid in cash in March return, with payables as per books
- Refund claimed in GST portal with GST ITC refund receivable in books
- Refund rejected in GST portal with Rates and taxes in books
- Turnover and output liability in GST returns and books
- ITC claimed in GST returns and books
- ITC reversed in GST returns and books
- Ineligible ITC in GST returns and books
- SCN/ ASMT 10/ Demand order with contingent liability/ liabilities
- Adjustments of previous year, done in subsequent GST returns
- Observations of internal auditors relating to GST matters
- Ratio analysis across branches like GP/ NP rates (on quarterly basis)
- RCM, TDS and TCS compliances
- Reconciliation of GTO in books v. in FORM GSTR-1
- Reconciliation of GTO in books v. in e-Way Bills
- Reconciliation of GTO in Form GSTR-3B v. in FORM GSTR-1
- ITC Reconciliation in FORM GSTR-2A v. FORM GSTR-3B
- ITC Reconciliation in FORM GSTR-2A v. in Books
- Reconciliation of accounts of the suppliers and vendors
- Issuance of proper CN/ DN and their treatment in the Books and Returns
- Whether cross-charge of certain incomes and expenditures are made.

Chapter 2

Audit Approach to GST Compliances

The GST law is a combination of various erstwhile tax regimes such as Excise Duty, State Value Added Tax, Service Tax, etc. As the GST law has evolved on the underlying principle of self-assessment, it is the responsibility of every registered person to self-evaluate and self-comply with the various requirements of the said law.

2.1 Taxpayer's Responsibility

The major requirements of the GST law, post registration can be summarised as follows:

Outward supply of goods and services

- Test of scope of supply
- Applicable exemptions
- Determining the point of taxation in terms of the 'time of supply' provisions laid down by law
- Determining the liability to tax in terms of the 'value of supply' provisions laid down by law
- Determining the place of supply of goods and services to pay the tax correctly to either the Central or State Government
- Correct classification of the goods & services as per HSN/ SAC
- Applying the correct rate of tax
- Accounting for TDS/ TCS
- Complying with the various due dates for paying tax, filing returns, appeals, etc.

Inward supply of goods and services

- Test eligibility for claiming ITC and reverse if found ineligible
- Discharge GST liability on certain goods and services under reverse charge mechanism
- Reverse ITC for non-payment to vendors within the stipulated time

Set off and pay tax

- Set off ITC against liability and pay the balance by cash
- GST paid under RCM can be used for set off
- GST under RCM to be discharged only by cash
- GST TDS/ TCS is part of cash and can be utilised to discharge liability under forward supply and RCM
- Payments of interest, late fees and penalty in certain cases

2.2 Audit under GST Act

The GST law mandates filing of an Annual Return by every registered tax payer (with a few exceptions) in such form as may be prescribed, before the thirty-first day of December, following the end of the financial year.

An audit of the accounts has also been mandated for registered taxpayers whose turnover exceeds the prescribed limit. Such registered taxpayers should file along with the Annual Return, a Reconciliation Statement duly certified by the auditor.

The audit mandated by GST law requires the examination of records, returns and other documents maintained or furnished by the registered person under the GST Act or the rules made thereunder or under any other law for the time being in force to verify the correctness of turnover declared, taxes paid, refund claimed and input tax credit availed, and to assess his compliance with the provisions of the GST Act or the rules made thereunder.

A Reconciliation Statement is one which reconciles the value of supplies declared in the Annual Return furnished for the financial year with the audited annual Financial Statement. It sets out the following:

- Reconciliation of turnover declared in audited annual Financial Statement with turnover declared in Annual Return
- Reconciliation of tax paid
- Reconciliation of Input Tax Credit (ITC) claimed

The auditor certifies, that to the best of his knowledge and belief, the information given in the Reconciliation Statement is true and correct and that nothing has been concealed therein.

Handbook on Finalisation of Accounts with GST Perspective

It is clear from the reading of the above that the objective of the audit under GST law is to reconcile the figures disclosed in the returns filed with those in the Financial Statements and in case of discrepancies, list out the reasons for the same. In the event the discrepancies result in additional liability, the same must be quantified along with interest and disclosed in the Reconciliation Statement. The liability must be provided for in the books and disclosed in the Financial Statements of the entity. Failure to do so will affect the 'True & Fair' view of the Financial Statements.

Often, the Financial Statements are audited and certified as 'True & Fair', well in advance of the time stipulated for filing of Annual Returns and the Reconciliation Statements and without carrying out the audit prescribed under the GST law. This may result in understatement of liability or overstatement of assets due to various reasons such as liability not discharged under RCM, ineligible ITC not reversed, etc. There may also be instances where the revenue and expenses may be under or overstated.

To avoid such mistakes creeping into the audited Financial Statements, it is imperative that the auditor carries out the GST audit simultaneously with the audit of the Financial Statements. In case the same is not practically possible, due to time constraint and professional work pressure, the auditor must ensure compliance with GST law and regulations have been adhered to and chances of misstatements in the Financial Statements are not likely to be material.

This booklet sets out in the subsequent Chapters some common non-compliance with GST law and how to spot and rectify the same. The approach is to review the various line items in the asset and liabilities in the balance sheet and the likely impact that GST law has on them. Similarly the revenue and expense line items in the profit and loss account is to be reviewed for compliances such as, right rate of tax charged on outward supply, discharge of tax on advance received for services to be rendered and for receipt of certain services under RCM, reversal of ineligible credits, reversal of even eligible credits due to non-fulfilment of conditions stipulated, etc.

Chapter 3

Review of Balance Sheet

ASSETS

3.1.0 Property, Plant and Equipment (commonly known as Fixed/ Tangible Assets)

Property, plant and equipment are commonly classified as land, land and building, plant and machinery, furniture and fixtures, office equipment, computers and related equipments and vehicles, etc.

During finalisation of accounts, the following points are to be considered while auditing such assets-

- (i) In general, all assets purchased will have a GST component which can be taken as input tax credit.
- (ii) There are certain categories of assets for which input tax credit is not available and in certain cases input tax credit is available with restrictions, more commonly known as blocked/ ineligible credits.
- (iii) Ineligible credits, if any, as stated in point (b) above are to be considered as part of cost of an asset and cannot be treated as input tax credit.
- (iv) Assets in the custody of third parties.
- (v) Reverse charge mechanism on certain items of capital goods, like-plant and machinery.
- (vi) Impact of GST on disposal of assets on which input tax credit may or may not be already taken.
- (vii) Transfer of assets to related parties/ distinct persons.
- (viii) Impact on GST on retention of assets at the time of closure of units.

3.1.1 Blocked/ Ineligible credits

As per section 17(5) of CGST Act, input tax credit is not available in respect of the following categories of assets-

(a) Motor vehicles

Input tax credit shall not be available in respect of motor vehicles for transportation of persons having approved seating capacity of not more than 13 persons (including the driver) including leasing, renting or hiring thereof, except when they are used for making the following taxable supplies-

- (i) Further supply of such vehicles; or
- (ii) Transportation of passengers; or
- (iii) Imparting training on driving such motor vehicles.

(b) Vessels and aircraft

Input tax credit shall not be available on vessels and aircraft except when they are used-

- (i) For making the following taxable supplies-
 - (a) Further supply of such vessels or aircraft; or
 - (b) Transportation of passengers; or
 - (c) Imparting training on navigating such vessels; or
 - (d) Imparting training on flying such aircraft;
- (ii) For transportation of goods.

It may also be noted that input tax credit shall not be allowed in respect of services of general insurance, servicing, repairs and maintenance in so far as they relate to motor vehicles, vessels or aircraft referred to above, except when such services are used for specified purposes stated above.

(c) Construction of immovable property

Input tax credit shall not be available in respect to goods or services or both received by a taxable person for construction of an immovable property i.e. building, other than plant and machinery.

Action Points

The auditor should verify the correctness of the amount capitalized in the books of accounts to ensure that the GST on ineligible items are not taken as input tax credit.

3.1.2 Assets in the custody of third parties

Capital assets like moulds, dies, jigs, fixtures and tools can be held by third parties (job workers) for an indefinite period of time as may be decided by the principal. This will not have any impact under GST law. However, the auditor should ensure that the principal maintains all relevant data in terms of location of the third party, nature of asset held etc.

Capital assets other than moulds, dies etc. with a job worker are to be returned within a period of 3 years or as extended from time to time by the appropriate authority. This must be reviewed on a regular basis to avoid any legal consequences.

Action Points

The auditor should verify whether the capital assets sent to job workers, if any, have been returned within the specified timeline. If the same is not returned the auditor has to ensure that the same has been declared as deemed supply and relevant tax discharged on the said assets.

3.1.3 RCM on import of services

There are several services such as erection and commissioning, technical consulting services, architect's services, etc. which are capitalized as part of cost of asset as per AS-10/ IND AS-16. These services will be treated as import of services when they are rendered by persons outside India and the recipient is liable to discharge GST on reverse charge basis.

Action Points

The auditor should verify whether there are import of services in case of assets purchased. For the import of services, the auditor should verify whether liability has been discharged as per the relevant provisions. The auditor must ensure that the tax paid under RCM is not claimed as ITC, if the same has been paid for construction of building.

3.1.4 Disposal of assets on which input tax credit taken

As per section 18(6) of CGST Act, in case of disposal of capital goods or plant and machinery, on which input tax credit has been availed, the registered person shall pay an amount equal to the input tax credit availed on the said capital goods or plant and machinery reduced by such percentage points as may be prescribed or the tax on the transaction value of such

Handbook on Finalisation of Accounts with GST Perspective

capital goods or plant and machinery determined under section 15, whichever is higher.

Example

Cost of capital asset Rs. 10,00,000

ITC claimed Rs. 1,80,000

Max life of asset as per GST rules: 5 years

Asset sold after 3 years of use for Rs. 3,25,000

(A) ITC to be reversed (ITC availed/ Max life of the asset in months) x
Remaining useful life of the asset in months

= Rs. 1,80,000 x 24/60 = Rs. 72,000

(B) GST payable on sale value = Rs. 3,25,000 x 18% = Rs. 58,500

Higher of (A) & (B) will be the GST liability.

In cases where refractory bricks, moulds and dies, jigs and fixtures are disposed of as scrap, the registered taxpayer shall pay tax on the transaction value of such goods determined under section 15.

Action Points

The auditor should identify the impact on the said transaction with relevance to Rule 44(6) of CGST rules.

3.1.5 Right of Use of Assets under IND AS

In the case of companies where IND AS is followed, right to use of assets would be created in the books of accounts. There will not be any impact in relation to GST as the ITC can be taken only on the basis of actual invoices without considering any factors like time value, discounting etc.

Action Points

The auditor, in those cases, should take additional care if any input tax credit has been availed by the entity.

3.2.0 Inventories

Inventories consist of raw materials, work-in-progress, finished goods and stock-in-trade.

In terms of the finalisation of accounts with reference to GST, following points are to be considered:

- (a) In general, all inventories purchased will have a GST component which can be taken as input tax credit.
- (b) Caution needs to be taken in case of goods-in-transit, goods sent to job workers and goods sent to agents.

3.2.1 Goods in Transit

In case of goods-in-transit, the input tax credit shall be available on the invoices from the suppliers only when the goods are received by the entity. This will cause a timing difference in terms of input tax credit available *vis-a-vis* availed.

Action Points

The auditor should verify the goods-in-transit to ensure that the input tax credit is availed in the books only when the goods are received by the business entity, as this is one of the primary conditions to be satisfied for availing credit under section 16.

3.2.2 Goods at third party site – Job worker

A job worker is a person who carries out a process or a treatment on goods belonging to another registered person. A job worker need not be a registered person.

A registered person (principal) sends goods to a job worker/ sub-contractor for say, finishing or polishing related activities. In this case the entity should maintain a record of inventories sent and should have proper documentation in terms of delivery challan.

Similarly, there can be cases where the raw materials are directly sent to job workers premises from the vendors' location, without passing through the principal. In this situation the principal can claim ITC only when the goods are physically received by the job worker. There can also be cases where the goods move to multiple job workers e.g. textile industry for various stages of production.

It must be noted that the goods sent to the job worker, must be returned to the principal within a period of twelve months which may be extended to 24 months with the prior approval of the appropriate authority.

Action Points

The auditor, while finalizing the accounts of an entity, should verify whether the goods lying at third party are returned within the prescribed time limits. If the same is not returned within the prescribed time limits, the same will be treated as deemed supply and creation of liability and payment of tax would be warranted on the said goods.

3.2.3 Goods at third party site – Sale on Approval Basis

In the case of goods sent on sale or approval basis, the supply shall be deemed, either at the time of supply or six months from the date of removal, whichever is earlier.

Action Points

In case goods are sent on “Sale on approval basis”, the auditor should verify the compliance in terms of GST provisions. If the goods are not returned within 6 months, it should be treated as deemed supply and creation of liability and payment of tax would be warranted on the said goods.

3.2.4 Adjustments to inventory on account of physical verification

Discrepancies noticed on physical verification of inventory between book stock and physical stock must be examined and suitable action taken. These differences may arise due to expired goods (beyond shelf life), theft, damage, distribution of free samples, return to vendors and non-accounting of purchases in the financial records, etc. Some of these differences must be written off or written back.

Action Points

The auditor must ensure that ITC must be reversed when goods are written off.

3.3 Trade Receivables

In case of export of services, the GST mandates various conditions like location of recipient of services outside India, place of supply outside India, the receipt of sale proceeds should be in convertible foreign exchange or Indian rupees wherever permitted by RBI etc. Further, if the exports are made under Letter of Undertaking (LUT) without payment of any duty under

GST, rule 96A stipulates that convertible foreign currency or Indian rupees are to be received before the expiry of one year, or such further period as may be allowed by the Commissioner, from the date of issue of the invoice for export. In the event of non-realization of the proceeds from export of services within the stipulated time as mentioned above, GST is payable on the same.

In export of services, there can be sub-contracting of some services outside India. In cases where such sub-contracting is involved to any other person outside India, then the impact of sub-contracting will lead to import of services in India and accordingly liability is to be discharged by the Indian entity.

Action Points

An auditor before finalizing the audit, must look into various aspects in relation to exports of services or goods from the perspective of GST and should ensure whether the liability and input credits are properly accounted for.

From a finalisation perspective, the auditor is expected to verify whether the export of services criteria is met in terms of receivables in foreign currency and whether the same is received within the stipulated period. In case the same is not done and if the tax payable is material, it may affect the 'True & Fair View' of the Financial Statements. Due care must be exercised during finalisation and audit of the Financial Statements.

3.4 Other Current Assets

During the course of verification of the current assets balances in the balance sheet, the auditor should necessarily map the input tax credit ledgers as per books with the GST credit ledgers. The input tax credit ledgers disclosed in the financial statements should normally tally with the GST credit ledgers as per the portal. However, invariably there will be differences and it is incumbent for an auditor to reconcile the differences as per GST return with the books of accounts and ensure there are no material or unexplained differences.

The following items would generally form part of reconciliation between books and GST returns:

Handbook on Finalisation of Accounts with GST Perspective

- (a) Input tax credits taken in a subsequent period in the GST returns whereas the same is accounted in a different accounting period.
- (b) Input tax credits disclosed in books not available in the GST portal on account of (a) non-filing of forms in cases of merger/ acquisition of companies and (b) transitional input credit taken before registration etc.
- (c) Reversal of ITC made in the portal not reversed in the books of accounts.
- (d) Refunds rejected/ short received not adjusted in the books of accounts.
- (e) Refunds filed without transferring ITC to 'Refund receivable account' in the books, which are pending for approval.
- (f) ITC availed in the portal shall be subject to rules like 10% of available credit in FORM GSTR-2A, etc. However, ITC would have been accounted in full in the books of accounts.

Further, the auditor should also reconcile FORM GSTR-2A balances with the input credit taken as per returns. Material differences may affect the availability of input credit and consequently increasing the GST payable.

The following items would generally form part of reconciliation between FORM GSTR-2A and GST returns:

- (a) Non-filing/ late filing of FORM GSTR-1 by the vendors for the supplies made by them.
- (b) Supplies filed in FORM GSTR-1 by the vendors not related to the entity.
- (c) Ineligible ITC.
- (d) Reversal of ITC on account of non-payment to vendors.
- (e) Goods-in-transit at the end of the period.
- (f) ITC taken in subsequent periods.

Action Points

The auditor should verify the two-way reconciliation i.e. books v. GST returns and FORM GSTR-3B returns v. FORM GSTR-2A to ensure completeness of the credits availed. The auditor should ensure that the balances of the input

tax credit as per the Financial Statements comprise of eligible credits as per the relevant provisions of the CGST Act. Ineligible credits, if any, must be either capitalized or expensed off depending on the nature of the ITC. The differences in the reconciling of items or in case of ineligible credits, if material, will affect the true and fair view of the Financial Statements.

3.5 GST Cash Balances

GST cash balances as provided in the books of accounts are to be reconciled with the electronic cash balances before finalisation of accounts.

Differences arise between GST cash ledger and the books of accounts in the following cases:

- (a) TDS/ TCS credits received from customers not accounted properly in the books of accounts.
- (b) Cash paid on account of any demand of self-assessment during annual return filing, but payment not properly dealt with in the books of accounts.
- (c) Amount paid on account of any demand which has been properly dealt with in the books of accounts (debited to rates and taxes) but relevant form has not been filed in the GST portal to offset the liability.

3.6 Disclosure of GST liability/ GST asset in the Financial Statements

The GST input credit balances and output liability shall be allowed to be off-set when the entity has legally enforceable right to set-off the recognized amounts. The excess of input credit over output payables shall be disclosed as part of other current assets and excess of output liability over input credits shall be disclosed as other current liabilities. If the right to off-set is not statutorily available, then the same shall be disclosed as gross numbers i.e. output liabilities will be shown as current liabilities and input credit shall be shown as other current assets.

Example: If a company has CGST input credit and SGST payable then the same are to be disclosed separately as they are not allowed to be set-off under GST laws.

LIABILITIES

3.7 Trade Payables

During verification of trade payables, balances in the balance sheet, the auditor should necessarily verify the GST provisions for the purpose of allowability of input tax credit. The auditor should verify the following from GST perspective for finalisation of accounts.

- (a) In case of foreign creditors, particularly service vendors, the auditor should verify the impact of import of services and where applicable should review whether RCM has been properly discharged.
- (b) For domestic creditors, review of payment is *sine qua non* as ITC claimed must be reversed in case payment to the creditor is not made within a period of 180 days from the date of invoice and necessary interest to be provided on such reversal. Auditor must also ensure that ITC so reversed is reclaimed when the payment is made to the creditor.
- (c) In case of e-commerce companies, provisions relating to TCS have to closely monitored and discharging of liability should be done on a periodic basis as envisaged by the GST Act read along with relevant rules.

Chapter 4

Statement of Profit and Loss

REVENUE

4.1 Revenue

During the course of verification of the credit items in the statement of profit and loss, the auditor should necessarily map the revenue as per books with the GST returns. The turnover or outward supply disclosed in the statement of profit and loss should normally tally with the turnover reported in FORM GSTR-3B and FORM GSTR-1. However, invariably there will be differences and it is incumbent for an auditor to reconcile the differences as per GST returns with the books of accounts and ensure that there are no material or unexplained differences.

The following items would generally form part of reconciliation between books and GST returns:

- (a) Turnover of each registration in case of multiple registrations.
- (b) Supply between GSTIN under same PAN (stock transfers).
- (c) Activities treated as supply even if made without consideration (deemed supplies).
- (d) Classification of supply under various Chapters (HSN Classification).
- (e) Impact of discounts on GST.
- (f) Impact of GST on advance received.
- (g) Exchange rate impact on turnover.
- (h) Non-GST supplies (e.g. High sea sales) – [Refer Schedule III of CGST Act.]
- (i) Sales promotion schemes: Free supplies (FOC) and buy one get one offer.
- (j) Recovery/ reimbursements of expenses incurred.
- (k) Adjustments required as per Accounting Standards.
- (l) Adjustments required as per Indian Accounting Standards.

4.1.1 Turnover of each registration in case of multi-location/ multi-registration

Financial Statements are prepared on a consolidated basis for an entity as a whole. From the perspective of GST, an entity can have multiple GSTINs on account of following reasons:

- (a) Operations in multiple States.
- (b) Multiple registrations within the same State.
- (c) Registrations mandated within the same State i.e. SEZ/ DTA locations etc.

The turnover of each registration is to be consolidated and compared with the turnover disclosed in the Income Statement. The collation of data from the books of accounts maintained by the taxpayer in the case of pan India service contracts may be a complex exercise, if the percentage of completion method is applied to the contract as a whole and not to the services rendered by individual units with distinct GSTNs. The auditor should review the data provided for each registration to ensure proper disclosure in registration-wise returns as this may lead to penal consequences in case of any material discrepancies in the disclosures made.

Action Points

The auditor should review the GSTIN-wise returns filed with GST authorities in FORM GSTR-1 and ensure that the data presented are appropriate. The auditor should also understand the methods, processes and controls around preparation of data obtained for different registrations.

4.1.2 Supply between GSTIN of same PAN

The auditor should verify the supplies made between various registrations outside the State to evaluate, if the supplies made are subjected to GST and whether liability has been discharged for the same.

Action Points

Such supplies will not get reflected in the turnover as per financial statements. The auditor can verify the completeness of the same by cross verifying the supplies with the e-way bills generated by the entity. The auditor should also verify the sales/ stock transfer registers generated out of the ERP to review the completeness and to provide for the actual liability (if any) on these supplies.

4.1.3 Cross Utilization of services / Cross Charges

Like stock transfers, services between branches would also attract GST liability. Cross charge is for supply of services from one unit to another in terms of common functions undertaken by such branches. Thus, it is an allocation of common functions to different branches. Cross charge is a broader concept, where the location that received goods and services in its own capacity uses such resources for provision of common support functions of the entity and thus, supply support functions to other units.

Examples of cross charges would include:

- (a) Head Office could be providing support to branches, such as centralized accounting services, HR Services etc.
- (b) Cost incurred commonly at or by the Head Office, such as software maintenance charges, cloud computing & storage costs, marketing and brand building costs.
- (c) Billing of proportionate expenses incurred by branches engaged in serving other branches without billings third parties.

Action Points

An auditor at the time of finalisation, has to verify the impact of cross utilization of services, if any, for an entity registered in multiple States and should ensure that proper liability is accounted and discharged as per the provisions of the Act.

4.1.4 Activities treated as supply, even if, made without consideration

The auditor should verify whether GST liability has been discharged and proper disclosure been made in the books of accounts. Activities treated as supplies without consideration can be verified from the various Notes/ Schedules and also during the course of audit, which may not form part of financial statements. The following are generally considered as deemed supplies under GST Act.

(a) Supply of services between related persons

Import of services by a taxable person from a related person or from any of his other establishments outside India, for business purposes, without any consideration will be treated as supply and will attract GST liability under RCM.

Example: ABC Inc. incorporated in the US is the holding company of B Ltd. (subsidiary) in India. Services/ recharges (IT Implementation etc.) are imported by B Ltd. from ABC Inc. without any consideration. GST should be paid by B Ltd. on reverse charge basis.

(b) Permanent Transfer of Business Assets where ITC has been availed on such assets

Permanent transfer or sale of business assets on which input tax credit has been availed will also be treated as supply, even if, no consideration is received. GST is applicable on sale of business assets only. It does not apply to the sale of personal land/ building and other personal assets.

“Permanent transfer” means transfer without any intention of receiving the goods back.

Action Points

Generally, transactions between related persons without any considerations do not reflect in the Financial Statements of the entity. However, the auditor has to satisfy himself based on the discussion with management, understanding of the organisation during the course of audit that there are no transactions of such nature.

The auditor should verify the transactions during the year to understand, if any such deemed supplies have taken place during the year. The auditor may also consider the disclosure made under Accounting Standard 18 – “Related Party Disclosure” to cross check and to ensure that no transaction is missed out from verification for GST compliance. In case such supply had taken place, the auditor should ensure that the GST liability on the said transactions along with interest, if any, are accounted and discharged as per the provisions of the GST Act. In case the same is not done and if the tax payable is material, it may affect the ‘True & Fair’ view of the Financial Statements. Due care must be exercised during finalisation and audit of the Financial Statements.

4.1.5 Classification of Supply under various Chapters (HSN Classification)

In case of an entity operating in multiple products, the entity must discharge its tax liability based on the Chapter heading under which such goods are

classified. There can be cases where the goods can be defined under multiple Chapters. Similarly, there can be goods which can have different duty structure within the same Chapter. The entity may inadvertently choose a lower rate which will result in short recovery and payment of GST.

Example – All items under Chapter 64 (Footwear, gaiters and the like: parts of such articles) are taxed at 18% IGST or 9% CGST + 9% SGST, except,

Footwear with retail sale price not exceeding Rs.1000 per pair which is subject to 5% IGST or 2.5% CGST + 2.5% SGST, if such sale price is marked or embossed on the footwear itself.

This difference in rate must be properly captured in the stock item master and the auditor must ensure that footwear taxable at 18% have not been taxed at 5%.

Action Points

The auditor must satisfy himself that the entity has classified according to the relevant Chapter the goods dealt by it. In case there is a difference in the Chapter heading, GST liability may vary and, if material, would affect the true and fair view of the Financial Statements.

4.1.6 Impact of Discounts on GST

Discounts offered by an entity for supplies made are to be reviewed carefully as the impact of the same in GST will result in liability being overstated or understated, depending on the type of discounts offered. Discounts offered can be reduced from the value of supply only if the conditions stipulated in section 15(3) of the CGST Act, are complied with.

Section 15(3) states that the value of the supply shall not include any discount which is given—

- (a) before or at the time of the supply if such discount has been duly recorded in the invoice issued in respect of such supply; and
- (b) after supply if—
 - (i) such discount is established in terms of an agreement entered into at or before the time of such supply and specifically linked to relevant invoices; and

Handbook on Finalisation of Accounts with GST Perspective

- (ii) input tax credit as is attributable to the discount on the basis of document issued by the supplier has been reversed by the recipient of the supply.

The provisions of the GST Act with regard to reduction or otherwise from the taxable value of supply can be summarized as follows-

Discount offered	Whether discount can be reduced from taxable value of supply
At the time of or before the supply and the fact is recorded in the invoice.	Yes; S.15(3)(a)
After supply based on agreement entered into before the said supply and is linked to a specified invoice.	Yes; S.15(3)(b)
After the supply without an agreement entered into prior to the said supply.	No

Discount provided by the entity on its supplies are to be classified as to whether it was agreed or provided or traceable at the time of supply or not. The auditor should review the discounts provided and its impact on GST liability.

Action Points

The auditor must verify the nature of discounts provided by the entity to its customers and review the corresponding impact on the GST liability. In case, there are material discrepancies, then the auditor may have to record the same in his report, if the entity does not pass necessary rectification entries during finalisation of Financial Statements.

4.1.7 Impact of GST on Advances received

While finalizing the books of accounts, the auditor should review the impact of GST liability on advances received and whether the said liability has been discharged as per the provisions of the GST Act.

Generally, advances can be classified as set out below:

- (a) **Security Deposits:** These are utilised by the supplier only on occurrence of a contingent event. In case such even does not occur, then the security deposit will be refundable to the customer on

completion or according to the terms and conditions of contract agreement. Generally, such deposits are not taxed under GST. However, in case of happening of the contingent event and consequent adjustment of security deposits, the same shall be taxable under GST.

- (b) Retention Money:** Retention money is the sum of money (generally a percentage of the contract value) held back by the customer as a safeguard for any defective or non-conforming work by the contractor. As per the GST law, the contractor is required to discharge his GST liability on the whole invoice value, which also includes retention money kept by the customer.
- (c) Advances for materials to be supplied:** These are not subject to GST liability at the time of receipt of the advance.
- (d) Advances for services to be rendered in future:** Any advance received for services to be rendered in future, is liable to GST on the date of receipt of the same. Thus, the receiver of the advance has to discharge the GST liability on the advances received by him.

Action Points

The various types of advances listed above, will have different impact on GST. The auditor should carefully investigate every type of advance and review its standpoint from the perspective of GST and conclude before finalizing the financial statements.

4.1.8 Exchange rate impact on turnover

Supplies of goods and services invoiced in foreign currency are recorded in the books of accounts at the exchange rate prevailing on the date of supply. Accounting Standard 11 – “The Effects of Changes in Foreign Exchange Rates” also allows the use of an average rate (say for a week or month) that approximates the actual rate on the date of the transaction.

As per GST, the exchange rate to be adopted is the rate notified under section 14 of the Customs Act. This will lead to difference between books and GST returns.

The auditor must reconcile the turnover as per books with the figures reported in FORM GSTR-1 and ensure that there are valid reasons/ explanations for the various line items in the Reconciliation Statement.

Handbook on Finalisation of Accounts with GST Perspective

It must be noted that as per GST Rules for export services, the rate to be adopted is as per generally accepted accounting principles (GAAP), which effectively means one can adopt the same rate as recorded in the books of accounts, provided there is no significant variation.

Action Points

An auditor must review the reconciliation for revenue as per the Financial Statements with that of the amounts declared in GST, on account of using different exchange rates before forming his opinion on the financial statements.

4.1.9 Non- GST supplies

An auditor while finalising the books of accounts of an entity, has to review if any supplies are made outside the purview of GST law and if so has to review the completeness of the said transactions by various auditing approaches to conclude on the Financial Statements.

Generally, the following items are considered to be out of the scope of GST:

- (a) Services by an employee to the employer in the course of or in relation to his employment.
- (b) Supply of goods from a place in the non-taxable territory to another place in the non-taxable territory without such goods entering India.
- (c) Supply of warehoused goods (warehoused goods as defined in the Customs Act) to any person before clearance for home-consumption.
- (d) Supply of goods by the consignee to any other person, by endorsement of documents of title to the goods, after the goods have been dispatched from the port of origin located outside India but before clearance for home consumption.

Although the above items do not have any impact on GST liabilities, input tax credit availed, if any, must be reviewed for allowability and if not allowable should be transferred to the profit and loss account.

Action Points

The auditor should conclude on the completeness of the above transactions by reviewing various agreements with the customers and related parties and significant transactions, if any. If any transactions are present, then the impact on the said transactions on input tax credit/ liability discharged are to be accounted appropriately.

4.1.10 Sales Promotion Schemes: Free supplies/ Samples (FOC) and Buy one get one offer

Promotional activities taken by the entity must be reviewed as part of finalisation of accounts. Following types of activities are covered under sales promotions schemes:

- (a) Free samples and gifts.
- (b) Buy one get one offer.

(a) Free samples and gifts:

It is a general practice in certain businesses to distribute free samples and gifts to customers as part of sales promotion activities. These free samples or gifts, which are supplied free of cost are not treated as supply under GST. However, the ITC availed on the inward supply of these items must be reversed.

Action Points

The auditor should review the nature of these transactions, the impact on the said transactions in terms of reversal of input tax credit and check whether it has been appropriately dealt with in the books of accounts.

(b) Buy one get one offer

Similar to free gifts, it is an accepted business practice in case of retail and whole-sale entities to offer marketing schemes – buy one get one free; buy a product “x” get product “y” for free. This must be distinguished from the free sample/ gifts mentioned above, since there is no GST impact on adoption of this marketing scheme, which is a subject matter of litigation.

4.1.11 Expenses reimbursement

Some entities seek reimbursement of expenses incurred (at actuals) for supply of services, by raising a debit note and not charging GST on the same. This is an incorrect practice. The logic that there is no element of profit and the expenses are backed by proper supporting documents, does not make the claim free from the applicability of GST. The auditor must exercise due caution while checking the same and ensure that a liability is created in case GST has not been charged on the amount claimed as reimbursement. However, when reimbursement is sought for payments mandated by law, the same will not be subject to GST. For instance in case

Handbook on Finalisation of Accounts with GST Perspective

of audit firms, out of pocket expenses like travelling/ conveyance incurred and claimed are liable to GST, whereas reimbursement sought for payment to MCA towards filing fees ,will not be subject to GST.

Action Points

The auditor should verify, if any transaction falls under reimbursement category and should review the GST implication on the same. Generally, all reimbursement will attract GST unless the reimbursement is on account of pure agents as defined in Rule 33 of CGST Rules.

4.1.12 Accounting Standard adjustments

Entities preparing their Financial Statements following Generally Accepted Accounting Principles as applicable under Companies Act, 2013 may adopt revenue recognition policy which may vary from the provisions of the GST Act and Rules prescribed thereunder.

Here are some examples of policies which can have impact on GST liability:

- (a) In case of supply of goods, transfer of risk and reward may not happen at the year end, However, the entity will raise a bill for the goods once the same is sent out of factory. The revenue will be accounted only in the subsequent year's income statement, when the risk and rewards pass to the buyer. For GST purpose, the same will form part of outward supply and liability to be discharged accordingly.
- (b) Revenue from rendering of services is recognised either on completion of services basis or on percentage of completion method. However, for discharging the liability under GST, the value of outward supply must be disclosed (i) in the return for the month in which an advance, if any, is received or (ii) in the return for the month in which an invoice/ progressive billing is raised as per the time frame stipulated in the Act. This will invariably lead to a difference between turnover as per books and the value of outward supply disclosed in the GST returns and will be a line item in the reconciliation statement.
- (c) Revenue from construction contracts are accounted in the Financial Statements based on percentage of completion whereas the same is not the case under GST Act and Rules.

Action Points

The auditor should review the accounting policies adopted by the entities. If

there are any adjustments on account of accounting policies/ Standards which are not directly relatable to the GST rules, then auditor should ensure that the adjustments are properly kept on record as part of reconciliation. Any liability on account of the said adjustments are to be discharged at the appropriate time as prescribed under the GST Act.

4.1.13 IND AS Adjustments

The company preparing its Financial Statements following IND AS principles as applicable under Companies Act, 2013 may adopt accounting policies which may not map with the provisions of the GST Act and Rules made thereunder.

Here are some examples of policies which can have impact on GST liability:

- (a) Recognizing revenue in a reporting currency having a functional currency other than Indian rupees. To elaborate, for the purpose of GST, sales will be accounted at the exchange rate prevailing on the date of transaction (notified under section 14 of the Customs Act), whereas in books it will generally be recorded at a prefixed average rate. This will result in differences, requiring reconciliation.
- (b) Revenue recognition as per IND AS-115 states that revenue shall be postponed to subsequent periods, if the stipulated conditions are not satisfied within the same year. Eg. If the goods are sold along with a warranty clause, then revenue in relation to the warranty period cannot be accounted immediately and has to be postponed to the subsequent period. However, as per the provisions of GST Act for goods sold, invoices are to be raised within the timeline prescribed by the Rules and tax discharged in the subsequent month.

Action Points

The auditor should review the accounting policy adopted by the entity. In cases where the accounting treatment mandated by the Accounting Standards is not in consonance with those dictated by the GST Act/ Rules, then the auditor should ensure that the adjustments are meticulously kept on record as part of reconciliation. Any liability on account of the said adjustments are to be discharged at the appropriate time as prescribed under the GST Act.

EXPENSES

4.2. Expenses

During verification of the debit items in the statement of profit and loss, the auditor should review the impact of GST on various expenses and ensure that the same have been properly accounted for. This will ensure that the Financial Statements are not materially misstated for ineligible or wrong credits availed. An entity should follow a robust system of maintaining the vendor masters along with the GSTIN of the vendor to ensure that the input tax credit is taken only on eligible items. The entities should also satisfy the following criteria to take input credits:

- (a) The entity should be in possession of the tax invoice or debit note, or any other document issued by the supplier.
- (b) It should have received the goods or services or both.
- (c) The tax charged in respect of supply has been paid to the Government by the vendor.
- (d) The entity should have furnished the returns under section 39.

Claim of ITC without fulfilling the above conditions can result in disputes and in turn lead to penalties and interest which may affect the Financial Statement at large.

The auditor needs to look into the following matters for the purpose of review of expenses with reference to GST Act and Rules made thereunder:

- (a) Blocked Credits.
- (b) Expenses on which GST is payable of reverse charge basis.
- (c) Import of Services.
- (d) Recoveries from employees.

4.2.1 Blocked Credits

Following are the list of blocked credits under section 17(5) of the GST Act in relation to statement of profit and loss:

- (a) Supply of food and beverages, outdoor catering, health services, life insurance and health insurance.

Statement of Profit and Loss

GST on supply of food and beverages is not allowed as input tax credit as the same is for personal consumption and not in furtherance of business or subsequent taxable supply.

Example: ABC Ltd. arranges refreshments/ tea/ coffee as part of staff welfare to its employees. It will not be able to claim ITC on the same.

Exception: ITC would be available when inward supply of goods or services or both of a particular category is used by a registered person for making an outward taxable supply of the same category of goods or services or both or as an element of a taxable composite or mixed supply.

- (b) Membership Fees of a club, health and fitness centre, travel benefits for employees.

GST on membership fees is not allowed as input tax credit as the same is in the nature of personal consumption and not in the furtherance of the business or subsequent taxable supply.

Example: Mr. A, a Managing Director has taken membership of a club and the company pays the membership fees, ITC will not be available to the company or Mr. A.

Example: A Ltd. offers a travel package to its employees for personal holidays. ITC on GST paid by A Ltd. for the holiday package will not be allowed.

- (c) ITC on personal use of assets/ goods/ services

ITC will not be available for the goods and services used for personal purposes.

- (d) Maintenance of vehicles used for transportation of passengers.

GST paid on servicing and maintenance of such motor vehicles and aircraft will not be allowed as input tax credit as the same are explicitly blocked under section 17(5) except in case of vehicles with a seating capacity of more than 13 persons (including driver) or in cases of exclusions provided in the said section.

Action Points

The auditor while reviewing the expenses must ensure that the entity has reversed the input credits taken, if any, on the above line items and expenses in its statement of profit and loss.

4.2.2 Expenses on which GST is payable on reverse charge basis

As per section 9(3) of CGST Act, the Government has provided a list of goods/ services on which GST has to be paid on a reverse charge basis. The following is an illustrative list of goods/ services on which GST is paid on reverse charge basis:

S No	Nature of Supply	Supplier	Recipient
1	Purchase of used vehicles, seized and confiscated goods, old and used goods, waste and scrap	Central Government, State Government, Union territory or a local authority	Any registered person
2	Purchase of Cement	Any person	Promoter in Real Estate
3	Services of Goods Transport Agency (GTA)	Goods Transport Agency (GTA)	Any factory, society, co-operative society, registered person, body corporate, partnership firm, casual taxable person located in the taxable territory
4	Legal Services of advocates	An individual advocate including a senior advocate or firm of advocates	Any business entity located in the taxable territory
5	Director's services (except remuneration)	A director of a company or a body corporate	The company or a body corporate located in the taxable territory

Statement of Profit and Loss

6	Services by way of transfer of development rights or Floor Space Index (FSI) (including additional FSI) for construction of a project	Any person	Promoter in real estate
7	Security services	Any person other than a body corporate	A registered person, being a body corporate located in the taxable territory

4.2.3 Import of Services

As per the GST provisions import of service in the course or furtherance of business will be subject to GST on reverse charge basis.

For a transaction to be considered as import of services, the following criteria have been prescribed by the IGST Act:

- (a) Supplier of service is located outside.
- (b) Recipient of service is located in India.
- (c) Place of supply of service is in India.

Example: ABC and Co. an architecture consultancy firm of USA provided its services to XYZ & Associates, a Chartered Accountant firm in India for designing its office at Bangalore for a consideration of Rs. 10,00,000.

Action Points

The auditor should verify the statement of profit and loss and review for any services which are liable to be paid as part of import of services under reverse charge mechanism. Further, the auditor should also review the reconciliation of the supplies made under RCM/ import of services disclosed in FORM GSTR-3B returns with the financial statements to ensure completeness of the data submitted.

4.2.4 Recoveries from employees and perquisites to employees – Free Gifts

It is a practice of trade and industry that certain recoveries are made by the entities from their employees for the benefits enjoyed by those employees. These are commonly in the nature of subsidised food, sponsorship fees or membership fees paid, medi-claim expenses, uniforms, shoes and equipment provided, subsidized cab, guest house expenses, etc.

Recoveries made from employees for provision of above services, are liable to GST. However, if the services are mandated by a statute and recoveries are made, then the same shall not attract GST.

Example: Recoveries for canteen facility provided by an entity in case of a factory will not be liable for GST under RCM as the same is mandated under Factories Act.

As per Schedule I of CGST Act, gifts and perquisites provided by business entities up to a value of Rs. 50,000/- per year to its employees are outside the ambit of GST. However, gifts of value more than Rs. 50,000/- are subject to GST, even when made in the course of furtherance of business.

Action Points

The auditor should verify the statement of profit and loss and review for the creation of GST liability on the recoveries made.

Chapter 5

Companies Auditor's Report Order (CARO) 2016 and Tax Audit Report

GST has a critical and far reaching impact on various items of Financial Statements as discussed in the earlier Chapters. In addition to the balance sheet and statement of profit and loss account, it has impact on CARO and tax audit reports.

5.1 Companies Auditor's Report Order

5.1.1 Inventory [Clause 3(ii)]

While reporting under this clause, the auditor should ensure that ITC availed on the inventory destroyed, damaged, lost, etc. have been reversed in the books of accounts.

5.1.2 Undisputed statutory dues [Clause 3(vii)(a)]

Whether the company is regular in depositing undisputed statutory dues including provident fund, Employees' State Insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated.

As per ICAI Guidance Note on Companies Auditor's Report Order (2016) the following are examples of the wordings which can be used in relevant situations:

- (i) "undisputed statutory dues including provident fund, or employees' state insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise, value added tax, goods and service tax cess have been regularly deposited by the company with the appropriate authorities in all cases during the year".
- (ii) "undisputed statutory dues including provident fund, employees' state insurance, income-tax, sales-tax, service tax, duty of customs, duty of

Handbook on Finalisation of Accounts with GST Perspective

excise, value added tax, goods and service tax, cess have generally been regularly deposited with the appropriate authorities though there has been a slight delay in a few cases”.

- (iii) “undisputed statutory dues including provident fund, employees’ state insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise, value added tax, goods and service tax, cess have not generally been regularly deposited with the appropriate authorities though the delays in deposit have not been serious”.
- (iv) “undisputed statutory dues including provident fund, employees’ state insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise , value added tax, goods and service tax, cess have not been regularly deposited with the appropriate authorities and there have been serious delays in a large number of cases”.

Action Points

The auditor must review whether the dues paid and returns filed by the entity are within the time limits prescribed.

5.1.3 Disputed Statutory Dues [Clause 3(vii)(b)]

Where dues of income tax or sales tax or service tax or duty of customs or duty of excise or value added tax, goods and service tax have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned.

This Clause requires that in case of disputed statutory dues, the amounts involved should be stated along with the forum where the dispute is pending. Therefore, even minor amounts would be required to be reported under this Clause. The amount should be reported in a manner so that the reader is able to understand the dispute and the amount involved therein.

Action Points

The auditor should review the status of past assessments. The auditor should obtain a confirmation and representation from management and review the probability of the issues being decided in favour of the entity depending on the facts of the case.

5.2 GST and Tax Audit Report

Tax audit report has a considerable amount of disclosure to be made in relation to GST.

Following disclosures are to be made under tax audit report:

- (a) GST registration details under Part A Clause 4.
- (b) Reconciliation of GST on opening stock, purchases, sales and closing stock as part of section 145A of Income Tax Act under Clause 14.
- (c) Particulars of depreciation allowable as per the Income Tax Act, in respect of each asset or block of assets as the case may be under Clause 18.
- (d) Any expenditure by way of penalty or fine for violation of any law for the time being force under Clause 21(a).
- (e) Details of GST paid on sales as part of section 43B under Clause 26.

Actions Points

- (a) The auditor should ensure proper disclosure of registrations under Part A clause 4 i.e. all registrations taken by an entity across all States including input service distributor registration.
- (b) The auditor should have a reconciliation of GST on the various items mentioned as part of inclusive accounting under Income Tax Act.
- (c) The auditor should verify whether the cost of addition to asset has been properly disclosed in the tax audit report. The cost of the asset disclosed in the tax audit report should be in line with the capitalisation policy followed for tangible and intangible assets, in the books.
- (d) Review FORM GST DRC-07, FORM GST PMT-06 and FORM GST DRC-03 forms/ chalans from the GST portal to ascertain if any penalties/ demands had been paid by the entity.
- (e) The auditor should review the payments made after the year end to ascertain if the liability at the end of the year is discharged completely.

Chapter 6

FAQs

Q.1. *During GST Audit there were adjustments in relation to ITC, output tax, debit notes and credit notes. These adjustments were not part of the audited financial statements. Whether such adjustment can be taken in next year accounts?*

Ans. The finalisation of accounts with respect to GST perspective is to avoid/ reduce any material differences arising on account of GST audit/ adjustments. After finalizing Financial Statements, if material differences on account of GST audit are identified, then the same should be to properly adjusted or incorporated in the subsequent year's Financial Statements. The same would warrant a separate disclosure as prior period item, if considered material.

Q.2. *How are interests and penalty on late payment of GST treated in finalisation of accounts from a GST perspective?*

Ans. Penalty on late payment and interest are to be shown as part of rates and taxes in the other expenses and charged to statement of profit and loss.

Q.3. *If GST audit is finished after final audit of financial accounts is completed and audit report is received, should the audited accounts be revised?*

Ans. As of now there is no option to revise the accounts already finalized and adopted in case of companies and accounts filed under income tax law for non-corporates. Any adjustments on account of GST audit shall be adjusted in the subsequent period only.

Q.4. *How to compute GST liability on import of service and what exchange rate to consider? What is the due date to discharge GST liability?*

Ans. The rate of exchange for determination of value of taxable services shall be the applicable rate of exchange determined as per the generally accepted accounting principles for the date of time of supply of such services. The liability is to be disclosed in FORM GSTR-3B

and discharged with other liabilities. The due date for the same is 20th, 22nd or 24th of the subsequent month.

Q.5. *GST bills raised in one financial year and GST TDS made by the debtors in the next (another) financial year. When should the GST TDS be accounted?*

Ans. GST TDS must be accounted only when the same is received in the GST portal i.e. when the supplier files FORM GSTR-7. The due date for FORM GSTR-7 is generally 10th of the subsequent month of payments made to customers.

Q.6. *What kind of note or provision is required in case of export of services at zero rate GST?*

Ans. No note is required if Letter of Undertaking (LUT) has been filed prior to export of services. However, if export has taken place without filing LUT, the GST authorities may direct the entity to discharge GST liability on the same. The entity can claim back the same as refund by preferring an application in this regard. The auditor must ensure that a provision is made for the same along with interest. In case the entity fails to make a provision, the auditor must exercise professional judgement to modify his opinion.

Q.7. *Can a supplier of renting of motor vehicle service who is charging GST @ 12% avail ITC on purchase of motor vehicles? Whether ITC is available when the supplier purchases motor vehicles and uses it in his renting of motor vehicle business?*

Ans. Yes. In terms of section 17, as an exception to ineligible ITC, any GST paid on motor vehicles will be allowed as ITC, when the output tax charged is 12%, if the same is used for making further taxable supply i.e. for renting of motor vehicles. It may be noted that ITC cannot be claimed when the output tax charged is 5%.

Q.8. *Whether refund of input tax credit on capital goods is allowed in case of export of services without payment of tax?*

Ans. Input tax credit on capital goods is not allowed as a refund as per the GST provisions.

Q.9. *E-way bill was generated wrongly, and penalty has been paid through cash ledger to get the vehicle released from detention.*

However, FORM GST DRC-03 has not been filed due to dispute and the dealer has made an appeal against such penalty. Whether is it proper to show such disputed payments in current assets?

Ans. The penalty paid on account of dispute shall be shown separately as loans and advances or other current assets. This may also warrant a disclosure as part of contingent liability as the said amount is not provided in the books of accounts.

Q.10. *An entity has not received goods as on 31st March for which invoice from the vendors are dated before 31st March. Whether input tax can be taken in the present scenario?*

Ans. Section 16(2)(b) of the CGST Act, mandates that input tax credit in respect of any supply of goods/ services shall be available to the registered person, after he has received such goods/ services. Therefore, input tax credit cannot be taken in the present scenario.

Q.11. *What is the impact of discount provided after the sales are made?*

Ans. Discount offered can be reduced from the transaction value, if there is a written agreement entered into before or at the time of supply, mentioning the discount conditions and timeline and the discount offered can be linked to the supply invoice for which it is made.

Q.12. *If there is transfer of asset from one unit to another, i.e. within same company, then whether the period of 5 years will be counted from the date of original purchase or from the date of transfer?*

Ans. For the purpose of useful lives/ elapsed life, original date of purchase is to be considered and not any subsequent movement within an entity.

Q.13. *While concluding statutory and tax audit of corporate, is it the responsibility of statutory auditor to examine all direct and indirect tax related compliance including verification and reconciliation of GST input credit availed as per books and as per monthly FORM GSTR-1?*

Ans. As per Standards on Auditing (SA) – 315, the auditor should assess the risk of material misstatement through understanding the entity and its environment. The auditor should also investigate the compliance of other laws and regulations which impact the entity and should consider the impact in his audit report.

Q.14. Can an entity utilise the GST TDS to pay the RCM liability, late fees or interest?

Ans. GST (TDS) deducted at source by the recipient is credited into electronic cash ledger, which can be used for payment of liabilities on account of RCM, late fees or interest.

Q.15. The credit period agreed between parties is more than 180 days. Whether ITC must be reversed even in case of increased credit period, if not paid within 180 days?

Ans. An entity should reverse the input tax credit taken if the vendor is not paid within 180 days of invoice even if the credit period agreed between the parties are more than 180 days.

As per section 16 of the GST Act, where a recipient fails to pay to the supplier of goods or services or both, other than the supplies on which tax is payable on reverse charge basis, the amount towards the value of supply along with tax payable thereon within a period of 180 days from the date of issue of invoice by the supplier, an amount equal to the input tax credit availed by the recipient, shall be added to his output tax liability.

Hence, it is clear that even in cases where the agreed credit period is more than 180 days, the input credit availed should be reversed as per section 16 of GST Act.

Q.16. Whether deduction from employee's salary towards penalty for causing deliberate damages due to wrong handling of machinery, is liable for GST levy?

Ans. The recoveries on account of default by the employee shall not be considered as supplies under GST as the employer-employee relationship subsist and hence it will not attract GST levy.

Q.17. Whether ITC is available on repairs and maintenance of building?

Ans. As per section 17 of CGST Act, goods or services or both received by a taxable person for construction of an immovable property (other than plant or machinery) on his own account including when such goods or services or both are used in the course or furtherance of business is not allowed as part of input tax credit. As an exception to the above, construction including re-construction, renovation, additions or

Handbook on Finalisation of Accounts with GST Perspective

alterations or repairs to the extent not capitalised can be taken as input.

Q.18. *While accounting year end provisions for services like rent, audit fee, retainer fees, etc., should it be inclusive or exclusive of GST component?*

Ans. Section 16 of the GST Act, stipulates conditions for claiming input tax credit. As per the provisions unless the goods or services are received by the entity along with the tax invoice or any other tax documents input tax credit is not available to an entity.

Input tax credit should not be accounted in case of year end entries as there are no valid tax invoice / documents.

However, in case of services where RCM is attracted (eg import of services, legal fees, GTA, etc.,) the provision should include GST.

Q.19. *Whether ITC can be claimed on GST paid under RCM?*

Ans. Any tax paid under RCM can be taken as an input tax credit as long as the same is not explicitly blocked under section 17 of the GST Act.

Q.20. *Whether RCM is attracted on transactions of Cost Sharing (Reimbursement of Expenses) between HO foreign entity and subsidiary in India?*

Ans. RCM is payable on cost sharing transactions, as the same would be considered as import of services.

Q.21. *Whether GST is to be included in the calculation of closing stock?*

Ans. GST should not be included as part of closing stock as GST paid on purchases lying in closing inventory. The GST component is considered as input tax credit. As per AS-2: "Valuation of Inventories" any recovered/ recoverable duties will not be considered as part of cost of inventory.

Q.22. *What type of ledger should be maintained by the entity for the reversal of ITC?*

Ans. There is no specific ledger account for reversal of ITC. The reversal will either be classified as rates and taxes or in case of ineligible credits or it will be added as part of the expenses debited to the statement of profit and loss.

Q.23. *Whether audited Financial Statements are required for the purpose of doing GST audit? Whether there can be a case where audit under income tax would not be applicable, but GST audit would be applicable?*

Ans. Generally, this would not be a case as both tax audit limits and GST audit limits are on similar lines. However, there may be stray cases where GST may be applicable, e.g. an individual taxpayer receiving the rental income from commercial premises say Rs. 10 crores, such tax payer may not be subject to tax audit.

Q.24. *Is sittings fees paid to directors liable to GST?*

Ans. Yes; the company has to pay GST on reverse charge basis on sitting fees paid to directors.