NEW BUZZ IN THE WORLD OF COMPLIANCES: KYC

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The world has seen a lot of changes through centuries and business also. Today, we have grown from a localized world to a globalized world; it can be dubbed as e-village. The business can acquire any materials or components, or services from any corner of the globe and sell to any customer across the globe. This has brought in new markets and opportunities but at the same time has brought additional risks in way supply chain disruptions due to the pandemic or increased focus on localization and change in the consumer spending pattern.

The rollout of GST in India has made the whole country as One Market, thereby facilitating trade and commerce across the length and breadth of the country. This has also posed a new challenge as the supplier of goods or services will not have any personal relations as they are distinct places and know about his details completely; before the rollout of GST, the supplier of goods or services used to have personal rapport as they were close by and very few to deal. This has given an additional set of challenges.

In today's dynamic world, the need of the hour is to have complete knowledge of the customers and suppliers. To have this, many of the companies have already started the Customer/Supplier onboarding process. This process is expected to cover vital information like the Customer/Supplier's registration details across tax regimes or departments, the key contact person details and the bank details for remittance or funds transfer.

In the competitive, it has become mandatory and necessary to evaluate the supplier or customer before placing orders or making supplies. To date, we are aware of Know Your Customer's concept is the concept used predominantly in the BFSI sector, and now the same is being implemented in all the sectors. In today's world, KYC is being termed as Know Your Partner (KYP). If the taxpayers do not do their due diligence properly and start the suppliers, it can adversely impact their top line and bottom line.

Know Your Partner– Supplier

In the normal course of business, when a purchase order or work order or contract or tender is allotted, the following points are considered

i. Cost

ii. Consistency in Quality

iii. Capacity to Supply or Deliver

iv. Post Supply Service

v. Financial Strength

vi. Environmental, Social and Governance Score

The above is an exhaustive list and depends from taxpayer to taxpayer.

ESG Score is added off late, and in India, it is still in the infancy stages. Evaluating the ESG score helps to understand the company's culture, commitment towards the environment, long term strategy to meet the disruptions.

Now, GST is also required to be considered in the vendor evaluation framework. GST compliances need to be verified before having any transactions with supplier for the following reasons

a) Filing of Returns – need to verify if the supplier is filing the returns on time or not. If not, then there is a potential risk of defaulting the return filing.

b) Timely filing of Returns – filing of returns is important but what is more important is timely filing. This will indicate that the supplier has potential cash flow constraints. If such is the case, can the taxpayer make supplies as per the schedule? Or is it because of the lack of systems at the vendor's place? Does this have to be ascertained before taking the contract forward?

The above is quite a few aspects that are critical for the business and this vendor evaluation. There are multiple ways to do the same, like manually going to the GST Portal and verify it vendor-wise else do it bulk using a third-party application. The only challenge in both approaches is the users have to do this job religiously else it will backfire. The best is integrating the ERP/Accounting with a third-party solution or homegrown solution (not recommend as it is not of core competency and consumes a lot of time and effort for integration).

The major challenge is if the taxpayers do not do the due diligence at the time of issue of PO/Work order or contract, the delay in filing of returns by the suppliers will call for additional cash flows as the GST liability has to be discharged using cash rather than using the input tax credit. This will impact the working capital management as well increase the borrowing costs impacting the bottom line. Apart from this financial implication, the taxpayers have to follow up with the vendors for their filing, which involves intrinsic costs.

KnowYourPartner– Customer

Any organization has a process of onboarding customers for the first time, which is a normal process. The parameters normally considered while onboarding the customer or while determining the pricing subsequently are

i. Price

ii. Payment Terms

iii. Volume

iv. References

v. Compliance

vi. Financial strength

We used to hear in the olden days "Customer is King" in today's world of regulations; this is not much relevant. Before onboarding a customer, the taxpayers must take additional verification or due diligence to ensure that cash flows are not adversely impacted.

In the case of the banking industry, it the need of the hour. The lender can verify the GST Data for his purchases and sales of the borrower from the GST Returns and basis on that, compare with the CMA data being submitted from time to time. This will help the lender identify the risks early, take corrective steps, and ensure the account does not slip into the NPA category.

In the recent past, we have seen that the department is first suspending the registration at the first stage, in the second stage, it is canceling the registration, and, in some cases, even the bank accounts are attached. If such is the case, it will impact cash flows as the customer will not pay on time. This can hurt the organization very badly and can also impact the operations if the exposure is very high with the customer. It is not only for GST; even in MCA, if the returns and other compliances are not met properly, RoC is freezing the bank accounts. The taxpayers have to deal with multiple regulations to see their compliances and status.

To avoid getting into this trap, before the acceptance of the recipient/customer's purchase order, the return filing status and the timing of the returns have to be checked and verified.

Due to the pandemic, every organization has been impacted, and there is an impact on cash flow; this has resulted in a delay of returns. However, the Government has announced relaxation in the return filing dates, interest rates and penalties. From a statutory perspective,these measures give legroom for the taxpayers, but as a businessman, we need to evaluate on above lines before taking any future supplies.

Good Service Tax is one of the biggest tax reforms in India post-independence, but in reality, it is a business process reform. It has brought in One Nation One Tax which resulted in seamless input tax credit across the supply chain, same tax rates, same classification and common return filing. Though these are the major benefits, we had some teething trouble with the portal, and the same has been resolved to a larger extent. We could see improvements from time to time after the rollout of GST on the portal, and to provide better user experiences, new features are being added to the portal from time to time. Apart from these changes, the taxpayers are also required to make changes in their business after the rollout of GST, and for this reason, only it is also dubbed as Business Reform. After the GST rollout, the taxpayers had to revisit their contract terms or change the process of availing input tax credit, issuing various documents in GST from time to time to be tax compliant.

Apart from the above changes, the taxpayers have to be more focused on purchasing and whom to sell. This decision will play a key role in maintaining the bottom line as well as effective cash flow management. Taxpayer rating is already envisaged in the law under section 149 of the CGST Act, but it is not yet notified. The trade and industry need not wait for the same; the same can be adopted and implemented using various third-party tools (ComQuo or peridot). When you select a third-party site, ensure that they provide multiple services. With the recent changes in income tax, the amount of tax to be deducted is double the actual amount if the vendor has not filed two previous returns. Automation will help to maintain the compliances. The cost of compliance is very lesser compared to the cost of non-compliance. In case of non-compliance, there is a need to spend money and efforts to reply to notices and visit the department offices from time to time.

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