

Special Audit – Desk Review - Rule of CMAs -Part II

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Preparing for Special Audit

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- ▶ Audit Working Papers
 - ▶ Scope of Special Audit
 - ▶ Value of Outward Supply
 - ▶ HSN Classification of Goods
 - ▶ SAC Classification of Services
 - ▶ Value of Inward Supply
 - ▶ List of Major Raw Materials
 - ▶ Expenses
 - ▶ Business Operations of the Taxable Person
 - ▶ Industry Sector
 - ▶ Market Share
 - ▶ Value Addition
 - ▶ Profitability
 - ▶ Management

Synopsis

- ▶ Part A – Supply of Goods
 - ▶ Desk Review and Audit Plan
 - ▶ Procedure/Formats
- ▶ Part B – Supply of Services
 - ▶ Based on Available Records
 - ▶ Analysis

Source of Information

- ▶ Cost Audit Reports, if Cost Audit is Applicable
 - ▶ *Otherwise*
- ▶ Cost Accounting Records and Systems
- ▶ Cost Accounting Standards in vogue

Cost Audit Report

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- ▶ Cost Audit Report provides
 - ▶ quantitative and financial details regarding production, clearance, capacity utilization, input-output ratio, related party transaction, valuation of production along with reconciliation of annual turnover with taxable value of Goods produced as per the GST returns.
- ▶ The report gives the information/details on the cost data for the company as a whole as well as in the respect of each plant/unit of the company located at different locations, thus study of the report helps the comparison of various information/details across the plants and units.

Extracting Data required for Desk Review

- ▶ CRA-3 and Annexures
- ▶ Total available quantity
 - ▶ Samples/ Quantity Captively consumed.
 - ▶ Outward supplies - with break-up of Export & domestic clearance
- ▶ Should reconcile this data with GST Return and major variation (if noticed) should be looked into.

Statements

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- ▶ Cost of Production
- ▶ Separate cost statements would be available in respect of each product/ activity group. Auditors may utilise the same for valuation aspects. It also helps to compute taxable value under cost Construction method under Rule 30 of CGST Rules, 2017
- ▶ Ratio Analysis
- ▶ Use the same for comparison of operating costs of each group, over a period of time.
- ▶ Related Party Transactions – Distinct Persons in GST
- ▶ Use this information with regard to valuation of related party transactions under Rule 28 of CGST Rules, 2017
- ▶ Productwise Profitability Statement – Analysis of Value Addition

Reconciliation Statement

- ▶ Information on other than sale of goods or services
- ▶ Where it forms part of taxable supply
- ▶ Information from Non Cost Items of Income

Extracting Information if Cost Audit is not applicable

- ▶ Apply the Principles of CAS
- ▶ Use Guidance Notes
- ▶ Apply your Cost Accounting Knowledge
- ▶ Obtain the relevant records
- ▶ Do Home Work (Desk Review) before starting physical audit

Information from Tax Audit Report

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- ▶ i. Clause 18 of the Tax Audit Report provides information about amount of depreciation under Section 32 of the Income Tax Act, 1961 and that of ITC availed on capital goods.
- ▶ ii. Clause 27(a) of the Tax Audit report gives the details of ITC claimed. It also provides the details of credit available and carried forward to the next year. Hence, the Auditor can authenticate the amount of credit carried forward in the GST returns with the information provided in terms of this clause



- ▶ iii. Clause 21 (b) of the Tax Audit Report also gives information regarding prior period incomes and expenses booked in the year under Tax audit. The Auditor shall ensure that GST on such supplies is paid on these amounts as per the provisions of Time of supply under CGST Act.
- ▶ iv. Clause 38 of the Tax Audit Report provides the information relating to Cost Audit. If such an audit has been carried out, the Auditor should examine the Cost Audit Report.
- ▶ v. Clause 40 of the Tax Audit Report provides the important accounting ratios.
- ▶

Desk Review for Services-Steps

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- ▶ Records Examination
- ▶ Make Ratio Analysis
- ▶ Make Trend Analysis
- ▶ Analysis of ITC (Based on Returns)
- ▶ Annual Turnover vis-à-vis GST Paid
- ▶ Annual expenditure of foreign currency vis-a-vis GST paid under reverse charge
- ▶ VIII. Brief details of service wise exports (zero-rated), turnover of non-taxable services and exempted services for the last three years
- ▶ IX. Brief details of service wise pure agent benefit claimed for the last three years
- ▶ X. In case the unit is registered as ISD, give the details of ITC availed and distributed
- ▶ XI. Analysis of data of GST returns filed
- ▶ XII. Prepare Audit plan

Information from Annual Reports for Desk Review

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- ▶ i) Director's Report (ii) Statutory Auditor's Report (iii) Balance sheet and Profit & Loss Account (iv) Financial statements of subsidiary companies, if any.
- ▶ Director's Report: Director's report may, inter alia, contain information about-
 - ▶ a) Foreign Exchange earned during the year.
 - ▶ b) Foreign Exchange paid during the year, e.g. may be on account of taxable services provided by the Registered person/Taxpayer where he is liable to pay GST under reverse charge mechanism.
 - ▶ c) Information on the operations carried out by the Registered person/Tax payer during the year under report. This may help in finding the exact nature of services provided by the Registered person/Tax payer.
 - ▶ d) The facts stated in Director's Report should be reconciled with the GST Returns.
- ▶ Auditor's Report: Statutory auditor certifies as to whether the books of account of the company are properly maintained or not and also whether internal control mechanism is commensurate with the size and extent of business of the company.
- ▶ Adverse noting of the Statutory Auditor Reply has to be obtained from the management

From P&L Account

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- ▶ Disputed tax liabilities separately for Customs, and Income Tax.
- ▶ Cases booked under Income Tax Act may be examined to find out any implication on the GST.
 - ▶ Available in CARO Report
- ▶ Check C& AG Report in case of Government Company/Entity
- ▶ Expenditure or income of the major heads should be compared with the previous year's amount in order to find out cases of major variations.

Analysis of Income Schedule

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- ▶ Profit and Loss Account would show a consolidated entry for business income from all sources.
- ▶ According to accounting standards, non-business income such as interest income or dividend income is required to be shown separately.
- ▶ The auditors should call for the groupings of business income shown in the Profit and Loss Account.
- ▶ The said groupings would show the different heads under which the incomes have been accounted for.
- ▶ They should carefully study the nature of business income – some of which may have accrued from the supply of taxable services and the balance from the supply of non-taxable services.
- ▶ This helps verification during Special Audit
 - ▶ The exact nature of these services may be determined from the supporting documents such as vouchers, bills or contracts.
 - ▶ Auditors need to be guided by the nomenclature (used for each service) in the Trial Balance or Annexures to the Profit and Loss Account.
 - ▶ It is possible that the true nature of the service may be Taxable or either non-taxable or exempted.
- ▶ ***Other incomes like insurance claims receipt, sale of capital goods, commission received, erection and commissioning income, freight and insurance recovered etc. may be examined in detail to find out the exact nature of such incomes and whether these are liable for GST and have any bearing on ITC utilisation.***

Fixed Asset Schedule

- ▶ Study of fixed assets schedule may show additions and deductions to the fixed assets during the year. For the deductions made during the year, verification may be made as to whether appropriate GST was paid, if the ITC was availed in the past.

Trial Balance

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- ▶ Familiarization with chart of accounts/account code and understand as to what extent the information is detailed and integrated with other subsystems;
 - ▶ Helps to check Vouchers during audit to understand the information mentioned therein.
- ▶ Understand the grouping of sub accounts under main accounts for the purposes of summarization into Profit and Loss account and the Balance Sheet.
- ▶ Identification of accounts, which have a prima facie relevance for GST payment.
- ▶ These accounts may have to be seen in detail at later stage of audit depending upon the result of subsequent audit processes;
- ▶ Understand the tax accounting system in so far as it pertains to Tax payment and treatment of credit of GST on input services;

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- ▶ ii. Clause 27(a) of the Tax Audit report gives the details of ITC claimed. It also provides the details of credit available and carried forward to the next year.
 - ▶ The Auditor can authenticate the amount of credit carried forward in the GST returns with the information provided in terms of this clause.
- ▶ iii. Clause 21(b) of the Tax Audit Report also gives information regarding prior period incomes and expenses booked in the year under Tax audit.
 - ▶ The Auditor shall ensure that GST is paid on these amounts in case they are subject to GST.

TDS Certificates

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- ▶ Information
- ▶ By deducting the amount of GST from the value on which tax has been deducted at source, the receipts appearing in the books of accounts can be reconciled.
- ▶ The nature of supplies can also be confirmed from these certificates and in case of any discrepancy in the categorization of services under proper head, elaborate checks need to be carried out by the Auditor.
- ▶ Details of TDS credit claimed in the Income Tax Return may also be examined