

Special Audit in GST – Rule of CMAs- Part I

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Preamble – Audit under GST

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- ▶ 1. Audit Report by Tax Payer – The Registered Dealer – Sec.35 of CGST Act 2017
 - ▶ In the Form of Reconciliation Statement
 - ▶ Annually
 - ▶ GSTR-9 and GSTR-9C
 - ▶ Criteria – Turnover Above Rs.2 Crores
 - ▶ *Removed from the year 2020-21*

- ▶ 2. Audit by Tax Authorities – Sec.65 of CGST Act 2017
 - ▶ The Commissioner of CGST/SGST (or any officer authorized by him) may conduct an audit of a taxpayer. The frequency and manner of an audit will be prescribed later.
 - ▶ A notice will be sent to the auditee at least 15 days before.
 - ▶ The audit will be completed within 3 months from the date of commencement of the audit.
 - ▶ The Commissioner can extend the audit period for a further six months with reasons recorded in writing.

Obligation of the auditee and report

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- ▶ The taxable person will be required to:
 - ▶ provide the necessary facility to verify the books of account/other documents as required
 - ▶ to give information and assistance for timely completion of the audit.
- ▶ Findings
 - ▶ On conclusion of an audit, the officer will inform the taxable person within 30 days of: the findings, their reasons, and the taxable person's rights and obligations
 - ▶ If the audit results in detection of unpaid/short paid tax or wrong refund or wrong input tax credit availed, then demand and recovery actions will be initiated.

Special Audit

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- ▶ Sec.66 of CGST Act 2017
 - ▶ The Assistant Commissioner can order a special audit if the regular audit reveals inconsistencies in the taxpayer's records.
 - ▶ These inconsistencies could either include
 - ▶ **inaccurate tax declarations** or
 - ▶ **incorrect credits availed.**
 - ▶ A **Chartered Accountant or Cost Accountant** will conduct the special audit process.
 - ▶ the **Commissioner will nominate** the Auditor

Approval and Procedure

- ▶ Here, the **Rule 102(1) of CGST Rules, 2017** comes in to role which prescribed that a direction required u/s 66(1) of CGST Act, 2017, shall be issued in **FORM GST ADT-03**.
- ▶ So, to get the special audit under GST of any registered person prior approval of Commissioner is necessary, any audit without approval of Commissioner is void ab initio.

Why Special Audit

- ▶ 1. It can be conducted at any stage of scrutiny, inquiry, investigation or any other proceedings before the Officer not below the rank of Assistant Commissioner.
- ▶ 2. If he thinks fit or if he has an opinion that the value has not been correctly declared or the credit availed is not within the normal limits, he may direct special Audit by a chartered accountant or a cost accountant by getting prior approval of Commissioner.

Time Limit

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- ▶ 1. That as per **Section 66(2) of the CGST Act, 2017**, the law prescribed the time limit to complete the Audit and to submit a report duly signed and certified by a chartered accountant or a cost accountant *within the period of ninety days* to the Assistant Commissioner.
- ▶ 2. Further, it is provided in law that the Assistant Commissioner is vested with power to *extend the limit for a period of further ninety days*, on an application of registered person or by a chartered accountant or a cost accountant or having sufficient reason to extend the same.

Opportunity of Hearing

- ▶ As per **Section 66(4) of the CGST Act, 2017**, the law states that any material which is gathered for special audit u/s 66(1) of CGST Act, 2017, which is proposed to be used against assessee in any proceeding against him, an opportunity of being heard to be given to assessee in respect of that material.

Expenses

- ▶ As per **Section 66(5) of the CGST Act, 2017**, the law states that all the expenses including remuneration due to a chartered accountant or a cost accountant shall be determined;
- ▶ Paid by the Commissioner; and
- ▶ The decision of Commissioner is final.

Why Special Audit

- ▶ Special audit provides a lawful and legal way for the GST officers to take the assistance of a chartered accountant or cost accountant to determine tax liabilities in complex cases.
- ▶ The professional expertise of a chartered accountant or cost accountant will be of great significance in ensuring that the interest of revenue is safeguarded at all times.

Findings

- ▶ As per **Section 66(6) of the CGST Act, 2017**, the proper officer on completion of audit u/s 66 of CGST Act, 2017 shall give his finding of audit and if he finds that tax was not paid or short paid or erroneously refunded, or input tax credit wrongly availed or utilized, than the proper officer may invoke the provisions of Section 73 or Section 74 of CGST Act, 2017.
- ▶ Here, the **Rule 102(2) of CGST Rules, 2017** comes in to role which prescribed that on completion of audit the registered person shall be informed in **FORM GST ADT-04**.

Audit as per Sec.2(13) of CGST Act 2017

- ▶ Verification of
 - ▶ Correctness of the Turnover Declared
 - ▶ Taxes Paid Correctly or Not
 - ▶ Availment of Input Tax Credit
 - ▶ Refund Claims
 - ▶ To check the compliances

Effect of other audit

- ▶ If an audit has been conducted by tax authorities under section 65 of The GST act, special audit under section 66 can still be directed irrespective of any Audit covered under any provisions of this Act or under any Act.
- ▶ The audit of accounts under any other provision or law will not have any relevance in conduct of special audit.

Demand – Sec.73 or Sec.74

- ▶ Where the special audit leads to detection of tax evasion not paid or short paid or erroneously refunded, or input tax credit (ITC) wrongly availed or utilised, the process of demand and recovery will be initiated against the GST registered person.

Issues

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- ▶ GSTR-1 and GSTR-3B
 - ▶ Outward supplies furnished in the annual return is a combination of all the monthly GSTR-1 returns filed for a tax period. There can be the difference between outward supplies show in GSTR-1 and turnover showed in GSTR-3B for which no action is taken.
- ▶ Reconciliation
 - ▶ State wise reconciliation between the audited financials and GST annual returns will be a major task for taxpayers. There are numerous transactions for reconciliation.
- ▶ Specific Areas
 - ▶ taxpayers like builders and developers who recognize the income based on percentage completion or project completion method as per Ind AS which is not in line with a time of supply as per GST. There are numerous taxpayers whose financial turnover is different from GST turnover.

Issues

- ▶ Could face presumptive taxpayers like Second-hand car dealers, Life insurance industries, Air travel agent industry etc. wherein turnover in financial is different from a turnover on which GST is applicable.
- ▶ Disclosure of HSN-wise details of Input Tax Credit where taxpayers don't have adequate IT system in place and data was not recorded as per the requirements.
- ▶ No apparent mechanism to correct the discrepancies/mistakes made in the annual return
- ▶ Reconciliation of GSTR-2A with ITC claimed as per GSTR-3B.

DESK REVIEW - Meaning

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- ▶ It is the first and foremost step taken by an Auditor to conduct an audit.
- ▶ Conduct audit procedures in the office itself without going to auditee's place of business.
- ▶ Desk Review involves collecting important information from the assessee to understand the operations prior to the conduct of field audit.
- ▶ Collecting the information that required by the Auditor for basic review.

Step 1

- ▶ The desk review lays emphasis on gathering data about the assessee/taxpayer,
- ▶ The operations, business practices and an understanding of the potential audit issues,
- ▶ understanding the financial and accounting system, studying the flow of materials, cash; and
- ▶ documentation and run tests to evaluate the vulnerable areas.
- ▶ The preliminary review assists in development of a logical audit plan and focus on potential issues.
- ▶ A good desk review is critical to the drawing up of good audit plan.

Assessee Master File (AMF)

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- ▶ An effective audit is to collect all relevant information about the assessee/taxpayer from various sources, arrange it in a systematic manner.
- ▶ The audit can be planned in a result-oriented manner. The AMF should contain all the useful information about an assessee/taxpayer, in the form of statistical data as well as in narrative form.
- ▶ This file should be useful as a ready reckoner.

General Information

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1. Name and Address of the Dealer
2. Principal Place of Business
3. Authorized Person –
Meet before starting the audit
4. GST Registration Detailers
5. Details of multiple registrations
6. Related Party Details – Distinct Person
7. Nature of Business
Supply of Goods or Supply of Services or both
Type of Products/Services

Tax Payer – Registered Taxable Person

- ▶ Status of the Tax Payer
 - ▶ Proprietorship
 - ▶ Partnership
 - ▶ Company
 - ▶ Any other body corporate
- ▶ Whether the Company has ISD

Step 2 – Accounts and Records

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- ▶ Latest Financial Accounts - B/S and P&L with schedules
- ▶ Tax Audit Reports under IT Act 1961
 - ▶ 44AB
 - ▶ 3CEB
- ▶ Cost Audit Report, if applicable
 - ▶ Important Role of CMA in GST Audit
- ▶ Any other statutory reports or compliances
- ▶ Accounting System Software

GST Records

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- ▶ Returns
 - ▶ GSTR-1, GSTR-3B, GSTR-2A and GSTR-2B
 - ▶ Ledgers
 - ▶ Electronic Liability Ledger
 - ▶ Electronic Ledger
 - ▶ Electronic Cash Ledger
- ▶ Other GST Records
- ▶ Stock Transfers, if any

Supply Details

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- ▶ Outward Supply during the year
- ▶ Inward Supply during the year
- ▶ Details of Depots/Warehouses
- ▶ Details with HSN Codes
- ▶ Customers – both domestic and exports
- ▶ Details of RCM Applicable
- ▶ Details of Advances Received
 - ▶ For Goods
 - ▶ For Services
- ▶ Details of important Contracts entered into with recipients of supply

Types of Supply

- ▶ Taxable Supply
- ▶ Zero Rated Supply
- ▶ Exempted Supply
- ▶ Invoicing Systems
- ▶ Output Tax

Step 3 - Financial Accounts - What to study

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- ▶ The Annual Report prepared by a company *inter alia* contains the following:
- ▶ 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: This gives information like overall financial results of the company, important happenings during the year and future plans of the company. Some of the important happenings like fire and loss of material in the company, details of new products launched, change in the marketing pattern etc. reported in the report may be useful to the auditor.
- ▶ Auditor's Report: These may be reports of Statutory auditor or Internal auditor or C & AG Audit. In the case of statutory audit, a separate report under CARO (Companies Auditor's Report Order, 2015) is required to be given.

Verification

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- ▶ (i) The Auditor's Report should be studied to find out any qualified/adverse opinion given by the auditors which may have impact on GST liability. For example, Auditor may report that goods meant for outward supply, available in stock were not reconciled or provision for obsolete items have not been made during the year. Tax auditor may like to examine such opinion in detail.
- ▶ ii) Company Auditor's Report Order (CARO) may be studied to find out whether the fixed assets records have been maintained properly or whether physical verification of inward supplies and goods meant for outward supply was undertaken and whether any discrepancies were noticed on such verification or whether the company has maintained proper records for unserviceable or damaged goods.

Contd..

- ▶ iii) CARO also shows disputed tax liabilities separately for Customs, Income Tax, GST etc. Cases booked under Income Tax may be examined to find out any implication on GST.
- ▶ iv) In the case of Public Sector unit, C & AG report and comment of the company available in the Annual Report should be examined

P&L Account

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- ▶ Nature of the Account: The Profit and Loss Account shows major items of expenditure and income.
- ▶ This is one of the important documents used during desk review to find out the overall working of the unit. In the main body of the Profit & Loss Account, only major heads of expenditure and income are given and the constituents of these headings are given in the annexure.
- ▶ Requires detailed study.

Study of Supply from P&L

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- ▶ Supplies may include inter-state supplies, intra-state supplies, Zero rated supplies including supplies to SEZ. Study of the pattern of supplies will give an idea about the volume of indigenous/ internal market for the registered person's supplies.
- ▶ (ii) Other incomes like scrap, insurance claims receipt, profit on sale of fixed assets, commission received, erection and commissioning, freight and insurance recovered etc. may be examined in detail to find out the exact nature of such incomes and whether these have any bearing on the valuation or whether these are liable for GST
- ▶ (iii) On the expenditure side, value of inward supplies on which GST is payable under Reverse Charge - Section 9(3) should be examined in detail. For this purpose, the relevant ledger account may be scrutinized as discussed under the head General Ledger. Ratios like i) inputs consumed to inputs purchased, ii) ITC availed on inputs to outward supplies, raw material purchased and ITC taken on inputs etc. may be worked out.
- ▶ (iv) Notes given along with the said schedule should be studied carefully to find out cases of use of material for non-production activities.
- ▶ (v) The 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

Notes

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- ▶ (i) Notes of Significant Accounting Policies may be studied to find out the accounting policy in the areas like revenue recognition or determination of obsolete stock.
- ▶ (ii) Notes on quantitative information on inward and outward supplies may reveal number of interesting aspects. Cases of use of inputs for other purposes (not in the course of business or furtherance of business) may also be noticed from the study of such information. Adjustment for shortages, losses etc. may also be reported in the said information.
- ▶ (iii) Any important transaction/happening during the year like non-reconciliation of accounts of inputs lying with job worker, major expenditure on research and development, destruction of record and reconstruction of duplicate records may also be noticed from the study of such notes.
- ▶ (iv) As per the Accounting Standard issued by the Institute of Chartered Accountant of India, the specified companies are required to disclose transactions with the related parties under the Companies Act as part of the Notes to the Accounts. The said information gives all types of transactions, payments made or payments received from various related parties.
- ▶ Such information is very useful to find out the details of the related parties and the type of transactions made by them.
- ▶ However, the related parties as per the Companies Act may not be considered as 'related person' under the GST Law.

