

Compliance Simplification

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Let us do this by establishing a core Principle...

- Core principle of any indirect taxation model has to be...

***Input Tax Credit will be provided only on
“matched” invoices***

- By “matched” we mean legitimate invoices where the supplier has admitted tax liability by uploading the invoice on the portal
- This means either deny or automatically reverse credit on unmatched invoices

Failure Criteria : There are some models that are doomed to fail

1. Any solution that **increases the burden on the taxpayer** to correct mismatches is guaranteed to fail
 - There will be severe resistance from the taxpayers to bear the additional burden
2. Any solution that **relies on tax official's intervention** to reduce the mismatch is also doomed to fail
 - Especially in the GST regime where there will division of administrative authority b/w Center & State
 - Introduces subjectivity of assessments & audits and potentially perceived as tools of harassment
3. Any solution that **permits higher levels of mismatch** in the first place will also fail
 - High levels of mismatch means there can be no automatic reversal. Paves way for failure causes 1 & 2 i.e. greater burden of correction and Tax official intervention

Let us take a look at the GSTR – 1-2A-2-1A model

- The model “attempted” to solve the some of the failure scenarios by introducing an acceptance workflow for invoice matching. As a principle – a step in the right direction.
- While GSTR-1 was reasonably successful, GSTR-2A and & 2 did not work as planned
- *It has been presumed that comparing Supplier provided invoice with Purchase books was too much a burden. But is it?*

Comparing Supplier provided Invoice with own purchase books

- Let's not forget...

Every business large or small, automated or manual routinely compares Supplier invoice with the purchase books!

- It is a necessary step **before releasing payment**. No business says – comparing is hard – so let me pay whatever supplier claims!

But then why was GSTR2 perceived as a burden?

- Comparing Supplier invoice with Purchase books all over again for tax credit claim purposes is a burden
- Comparing Supplier invoice that is not at the same granularity as their books is a burden
- Comparing & correcting Supplier invoice 2 months after the transaction is a burden
- Comparing all Supplier invoices in a span of 5 days that too by a professional is a burden

In summary, GSTR-2 model was burdensome because...

- By modeling “Invoice Upload” and “Acceptance” as Tax “Returns” (GSTR-1 & GSTR-2), the model created a perception that there are 3 returns per month.
 - People perceived them as a tax function creating a dependence on a tax professional when upload & acceptance is patently a business reporting function
- Structure of forms was also too complex which required a tax professionals help
 - Concepts like Tax on Advance, its utilization to offset liability, separate reporting of different type of invoices made GSTR-1 & 2 look more like a return form than a statement
- Reporting of invoices at rate-level instead of line-item level created more work to the supplier
 - It also made matching and acceptance unacceptably tedious

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What then is a Successful Model

- A successful model is one which achieves the agreed goal without the failure characteristics of increased tax payer burden or intervention of tax official.
- In other words one which...

...aligns with the natural business cycle of verification & payment of supplier invoices

Highlights of the proposed solution – Invoice Upload

- Suppliers “upload” sales invoices on the GST System which automatically calculates his/her liability. Invoice is also made available to Buyer for acceptance
- Key Contrasts from GSTR-1
 - It is simply an Invoice **“Upload”** - not **“filing”** of return
 - Invoice format and data granularity to exactly match the actual invoice submitted by supplier for payment viz. **Invoice Item Level** right from day one – not rolled up at tax rate or commodity levels
 - Upload happens on a **continuous basis**. It means the verification and acceptance coincides with the actual business transaction. Invoices uploaded after the 10th is automatically included in next return
 - Market forces will evolve a model where invoice is paid only after upload on GST System

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Highlights of the proposed solution – Invoice Acceptance

- Buyer “accepts” supplier invoices on the GST System which automatically determines the input tax credit (ITC)
- Key Contrasts from GSTR-2 and pure System Matching Model
 - It is simply an Invoice **“acceptance” - not “filing”** of return. **Acceptance** can happen on **continuous basis** – not waiting for all the GSTR-1 to be filed.
 - In the case of pure System matching model the correction and acceptance will be at least **20-50 days after the transaction**
 - Invoice once accepted is “locked” cannot be modified by the supplier. Brings finality to the transaction
 - System to **provide robust tools** to facilitate smooth acceptance – including offline matching of supplier invoices with purchase books, auto-acceptance capabilities and improved support to GSP/ASPs for tighter integration with accounting packages.

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Highlights of the proposed solution – Handling Missed Invoices

- We propose to eliminate concept of “Provisional Credit” – However Buyers can “notify” supplier through the system to upload any missed invoice – but cannot upload or modify it themselves
- Key Contrasts from GSTR-2
 - Buyer is simply declaring the invoices missed by his/her supplier
 - System will notify the supplier – reminding them to upload the same
 - When supplier uploads such invoice, System will match and remove it from the missed invoice list
 - Missed invoice statistics will be retained and used to compute performance scores of the tax payers

Highlights of the proposed solution – Handling non-Payment

- In the proposed model, there will be no “Mismatch” in the traditional sense – hence no question of reversal. But there is still the possibility of non-payment of taxes by the supplier
- The current law penalizes the buyer by denying or reversing credit – but this is widely perceived as unfair to buyer. We understand courts have also ruled against it
- It is therefore recommended that the new law...
 - Re-Define the criteria of a legitimate invoice as one where Supplier has admitted liability by uploading into the portal
 - Makes provisions to recover dues from the Supplier rather than penalizing buyer

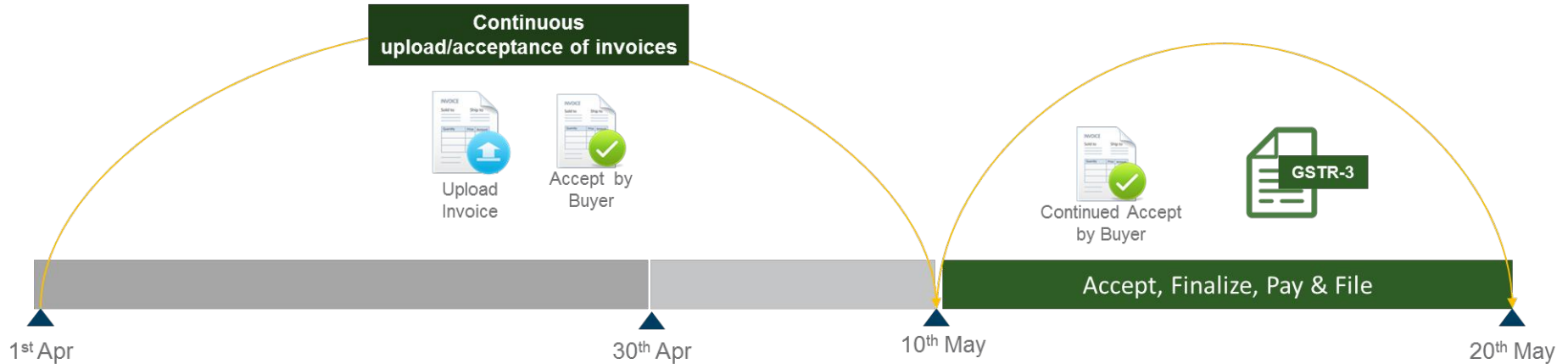
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Highlights of the proposed solution – Channels of reporting

- GST System will offer multiple channels for upload and acceptance of invoices and filing of returns
 - Small taxpayers with no automated accounting systems can view and accept pending invoices **directly on the portal**
 - Small-Medium Taxpayers with some level of automation can use **Excel based offline tool** to download, compare and accept pending invoices
 - Large tax payers with fully automated accounting will do the reconciliation and acceptance directly in their accounting system and upload results directly **through APIs**

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Proposed Solution



- Continuous invoice upload/acceptance with counter parties – No cut-offs
- Remove concept of provisional ITC
 - No uploading of missed invoice or modify supplier invoice.
 - Consequently, no mismatch or ITC reversals

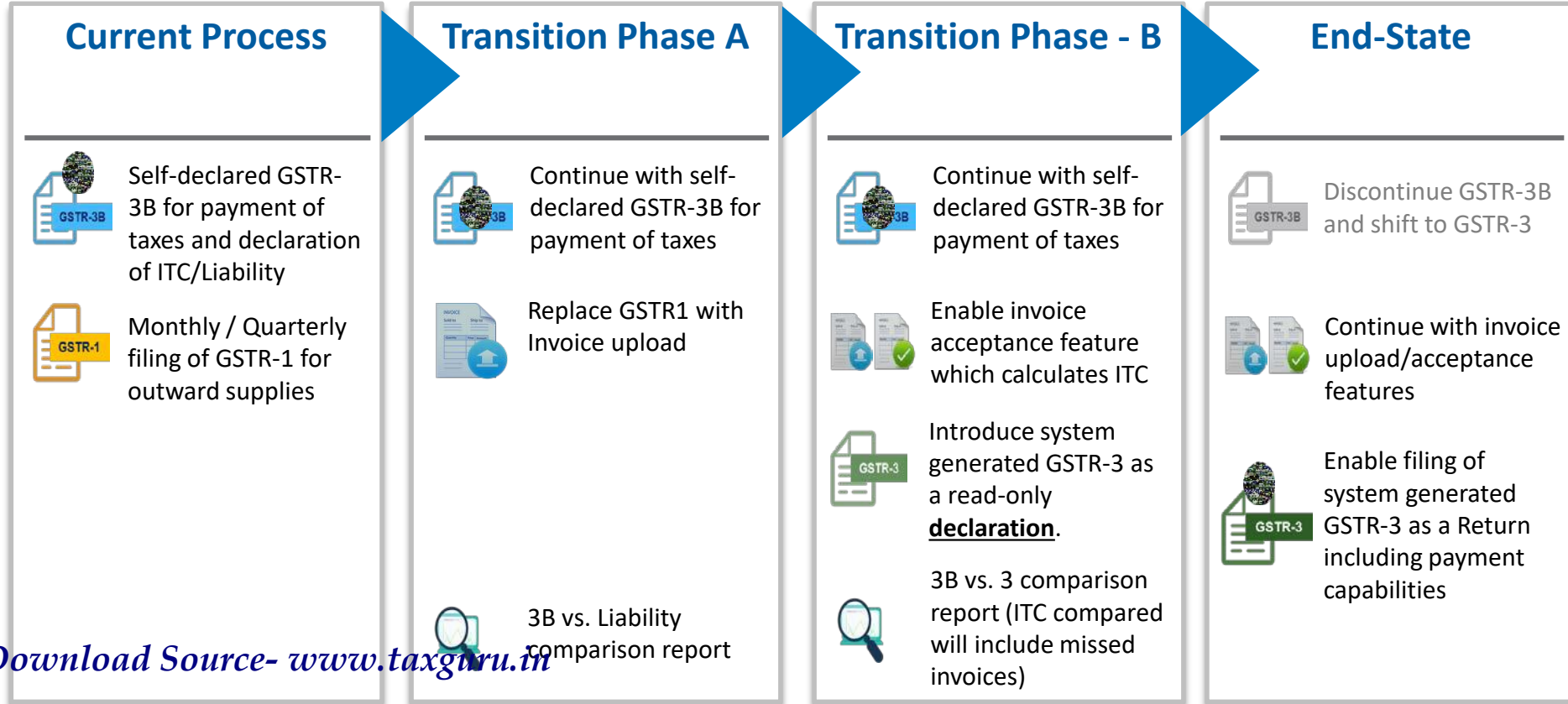
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We further propose a Gradual Transition so that it ...

- Eliminate risk of adoption issues impacting tax collection
- Provide sufficient time to stabilize the system including enhancements to improvements to user experience based on industry feedback
- Provide sufficient time to taxpayers to adapt to the new model – understand counter-party behavior & data quality and implement corrective measures as required
- Provide sufficient time to enable eco-system to develop tools/applications for automated upload of sales invoice and reconciliation of purchase invoice

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Gradual Transition to the New Model



Key Benefits of the proposed model

- **Simplicity:** Dramatically simplifies the process and reduces burden
 - As established earlier, every business routinely compares supplier invoices with their purchase books before release of payment. This model simply integrates with this natural business process
 - Compliance is as simple as “reporting” their business transaction regularly and making payment against a system generated return
 - In contrast, a pure System matching model with high levels of mismatch actually increases the burden – comparing & correcting **stale transactions** is **lot harder** than doing it as part of business cycle

Key Benefits of the proposed model

- **Incentive Aligned** : Natural alignment of incentives to both supplier and buyer
 - Supplier has to report invoices on-time – otherwise will not get paid or end-up paying interest
 - Buyer has to accept invoices on-time – otherwise will not get his/her input credit

Key Benefits of the proposed model

- **High Data Quality:** Cleaner data with low level of initial “mismatch”
 - As the model integrates with the natural business process between supplier and buyer, one can expect significant improvement in data quality
 - Experience from VAT shows that majority mismatch is due to difference in Invoice No. and Date. This happens due to dual version of same data flowing from both parties. Having a single version of data will reduce initial mismatch levels to a great extent
 - Since incentives are aligned to business interest, there will be greater focus to upload correct data

In conclusion...

- We must agree on the core principle of...

Input Tax Credit will be provided only on “matched” invoices

- Any model that increases tax payer burden, or relies on tax officer intervention is likely to fail.
- A successful model is one which aligns with the natural business process and not make Tax return preparation a separate function
- The proposed model will result in lower compliance burden to the tax payer, higher revenue collection and reduced administrative burden to the officials

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