GST Implementation - Impact on Accounting System

With the introduction of GST from 1st July 2017, India has moved towards a single indirect tax regime for goods & services for the entire country with uniform law. In view of the majority of taxes getting subsumed, there are numerous impacts on various functional areas of a business. From accounting perspective, entities have to re-align their accounting systems in accordance with the provisions of the GST Law. The GST law which is considered as a progressive tax reform for the country is not limited to tax structure. It also encompasses the entire accounting and financial reporting structure. Few implications on accounting systems are discussed in this article. Read on to know more..

Impact areas:

a. State-wise Registration and Accounting:

Section 22 of CGST Act requires every supplier to be registered under GST in the state from where he makes a taxable supply of goods or services or both. Therefore, there is a requirement of taking registration in every state from where a taxpayer is making taxable supply. On the contrary, in the erstwhile service tax regime, a service provider had the option to take a centralised registration even if he was rendering services from multiple locations.

Having said that, the supplier is required to take registration in every state, requirement of filing GST returns and payment of tax in that state automatically arises. Therefore, taxpayer who has presence in multiple states has to take registration and maintain sufficient records in all the states from where he is making taxable supplies. Therefore, taxpayer has to maintain its books of accounts in accordance with Section 35 of CGST Act & Rules made thereunder in multiple states to comply with the law. Accordingly, burden of maintaining multiple books of accounts lies with the taxpayer under the GST law.

b. Supplies without Consideration:

Schedule I of CGST Act states certain activities to be treated as supply even if made without consideration. *Clause II of said schedule covers supply of goods or services or both between related persons or between distinct persons as specified in section 25, when made in the course or furtherance of business.*

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Further, *Section 25(4) of the CGST Act provides that every registration of a person will be treated as a separate taxable person or distinct person for the purposes of the Act.* Accordingly, all transactions involving supply of goods or services between inter-state branches of an organisation are considered as *supply*. Let us discuss implications on supply of goods & services separately.

Supply of Goods: The transaction of supply of goods from one state to another state within the same organisation will be considered as normal supply and implications like third party sales will follow. Say, Company A Limited has transferred its stock from factory to depot which are located in different states or from Depot A to Depot B located in different states. As per Schedule I, this activity shall be considered as supply even if without consideration and chargeable to GST. Now, company A has to raise tax invoice and show such stock transfer as its supply in the state where Factory is located. Further, Depot has to consider it as inward supply to avail Input tax credit and accordingly report it as its purchase in the books of accounts. Such transactions of supply will lead to multiplicity of revenue of company as a whole. However, these transactions have to be recorded in a manner that net impact at the time of preparing financials statements is nil.

Supply of Services:

Similarly, Clause II also covers supply of services between distinct persons as supply. Therefore, all transactions where one branch is engaged in providing support which may include but not limited to support related marketing, management, IT functions etc. to another branch/head office or vice-versa will be considered as supply of services.

Companies having presence in multiple states or Pan India has to map its process flows in a manner that there is clear distinction of role of each office so that flow of services is visible. Accordingly, company has to raise tax invoice from the branch providing support services on recipient unit/s and record & settle such transactions in the manner that books of accounts are compliant with the GST law and appropriate adjustments are also made in books of accounts.

c. **Outward and Inward Supplies: Input Tax Credit (ITC) and Revenue Recognition:**

Since, Ind AS are also in the process of implementation in India, companies are restructuring its books of accounts in accordance with the newly implemented Ind-AS which are designed on pattern of globally recognised IFRS. Currently, accounting treatment of various indirect taxes varies, based on their nature and point of levy.

Under Ind AS, excise duty is included in revenue, since it is a production-based tax. Sales tax and VAT is not included in revenue, since it is levied at the time of sales. GST is a destination-based tax, which is levied at the point of supply. Hence, it appears that revenue will not be presented including GST however certain clarity in Ind-AS is expected in this regard.

Further, there can be certain transactions where company is getting consideration for making supply but does not record it as its revenue from operations nor does it credit the amount in its profit & loss account. However, such activity shall be considered as supply for consideration within the purview of the GST Law. Such transactions have to be dealt carefully as they will form part of reconciliation item between supplies reported under GST return and amount of revenue recorded in the books of accounts.

For instance, in case company is recovering certain amount from employees for canteen services and deducting the same from salary expenses in P&L account but treating the same as supply under GST.

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Further, in case of real estate sector, companies may adopt different policy of recording revenue in its books of accounts due to Ind AS or RERA 2016 and different policy for raising demand notes to customers. Therefore, companies have to align their revenue recognition policies in accordance with the GST law while considering other regulatory statutes.

For the purpose of matching ITC availed in the books of accounts and ITC available on GSTN portal, company is required to make proper reconciliations.

Accordingly, companies will need to devise a proper system in place, for timely state-wise reconciliations of periodic GST filings in various states, with the amount recorded in the books of accounts.

d. Specific Provisions which have Direct Impact on Accounting such as Works Contract, Composite Supply etc.

There are certain specific implications on peculiar transactions due to concepts introduced in the GST Law.

Works contract

Schedule II of CGST Act *inter-alia* deems works contract under GST law to be treated as supply of services. Further, works contract as defined under Section 2(119) of CGST Act *means a contract for building, construction, fabrication, completion, erection, installation, fitting out, improvement, modification, repair, maintenance, renovation, alteration or commissioning of any immovable property wherein transfer of property in goods (whether as goods or in some other form) is involved in the execution of such contract.*

Therefore, an activity of works contract in relation to immovable property shall be considered as supply of services. Accordingly, company has to raise tax invoice considering such activity as supply of services. In such a case, it is pertinent to note that movement of goods for such activity of works contract would not be done on tax invoice as such activity is to be considered as supply of services as a whole but at the same time inventory of company has to be reduced with the quantity moving out. Company may find difficulty to execute such transactions in its systems as such without further modification.

Composite supplies

Composite supply as defined under section 2(30) of CGST Act *means a supply made by a taxable person to a recipient consisting of two or more taxable supplies of goods or services or both, or any combination thereof, which are naturally bundled and supplied in conjunction with each other in the ordinary course of business, one of which is a principal supply.*

Therefore, an activity of works contract in relation to immovable property shall be considered as supply of services. Accordingly, company has to raise tax invoice considering such activity as supply of services.

Now, say an assessee is engaged in activity of composite supply wherein he is supplying goods on FOR basis wherein the transaction includes supply of goods as well as supply of transportation services as it is the requirement of contract to deliver goods at customer premises.

Further as per Section 8 of CGST Act, the tax liability on a composite supply comprising two or more supplies, one of which is a principal supply, shall be treated as a supply of such principal supply. Accordingly, assesse has to raise tax invoice for supply of goods which will be treated as principal supply in the instant case. However, for the purpose of recording transaction in its books of accounts, sale of goods and transportation charges has to be recorded separately or it can be clubbed to be seen from Ind AS perspective.

Similarly, there are certain other transactions which *may have different* treatment under GST as compared to the treatment given in books of accounts. Such transactions have to be considered and dealt carefully.

Conclusion:

In the light of above challenges, it appears that there is a dire need of action in terms of resolving some accounting issues being faced by the members/industry. For instance, clarity is required on *supply* and to bring out a clear distinction between 'sale' and 'supply' for the purpose of recording revenue.

Further, to address the accounting concerns, which includes but is not limited to matters discussed above, Schedule III of the Companies Act, 2013 needs to be amended. ■