RSM Astute Consulting

GST Implementation By Business Organizations - Managing Change

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Reference: RSM Astute/NEW/0110 January 2010

1.0 Background

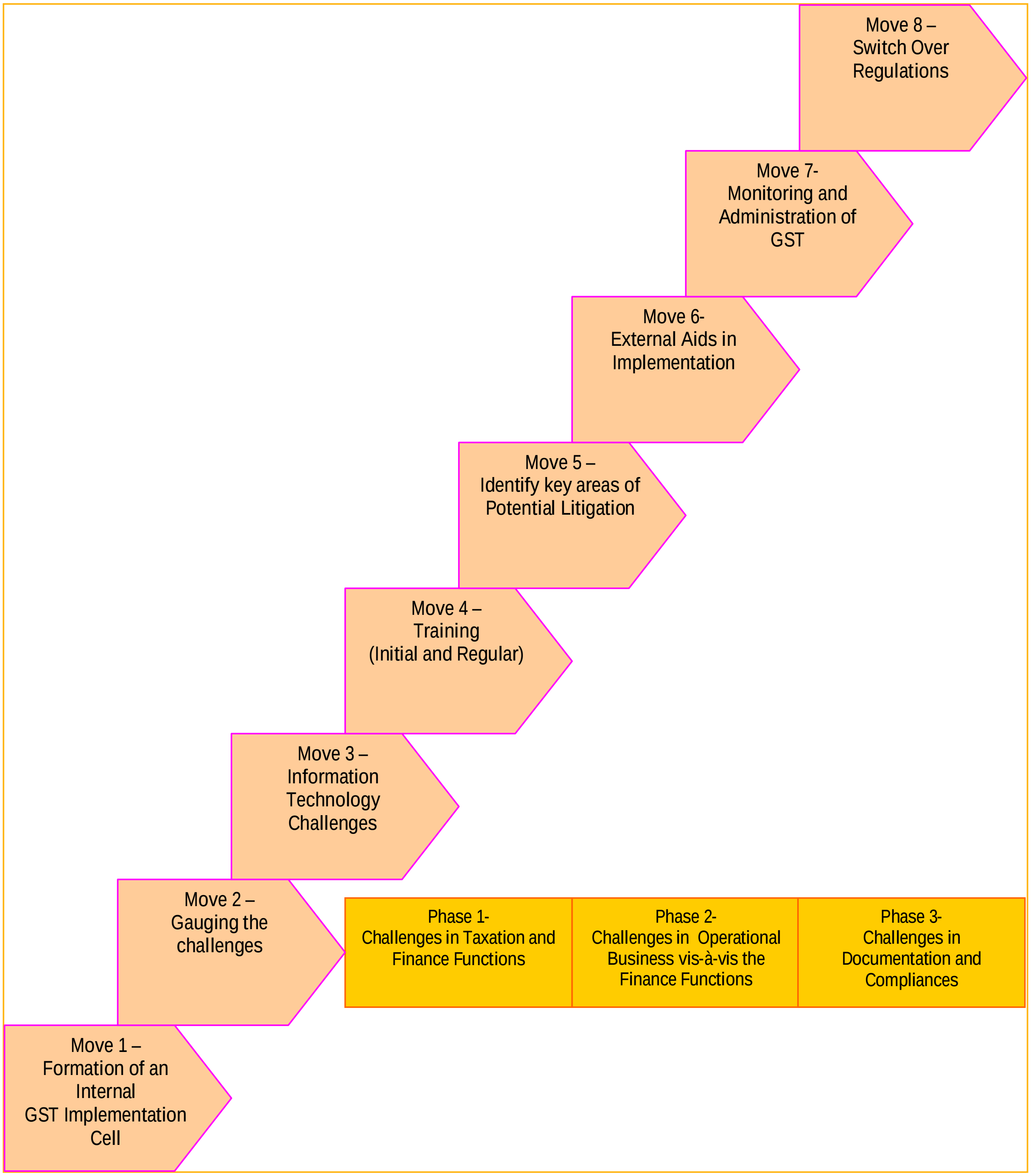
The Empowered Committee of the State Finance Ministers had released the First Discussion Paper on Goods and Services Tax ('GST') in India on 10 November 2009. Thereafter the 13th Finance Commission has published the "Report of the Task Force on GST" on 15 December 2009.

The preparation of a road map towards implementation of GST has already posed a major hurdle before the Government (Central and State) which is evident from the fact that the announcement for the implementation of GST from 1 April 2010 was made by the then Hon'ble Union Finance Minister Shri P. Chidambaram in the Central Budget (2007-2008) whereas the First Discussion Paper is released in November 2009. The very fact that the implementation of GST involves a general consensus of the Central Government and the State Government and at the same time subsumes various Central and State levies which were hitherto levied and administered independently by the Central Government and State Government has resulted in a need of gearing up the various revenue administering authorities.

Considering that the implementation of GST would cover some of the major indirect tax regulations such as Central Excise, Customs Countervailing Duty, Special Additional Duty, State Level Value Added Tax, Central Sales Tax, Service Tax etc, which have different taxable events, different point of time for arising of liability and payment of taxes etc the need to gear up is not only restricted to the Revenue Authorities but more importantly to Business Organizations across the Country who are expected to understand the regulations, modify / integrate the same with the organizational systems to ensure an effective implementation of the same as also develop and sustain a working level knowledge orientation on GST principles / procedures across the organization. Thus the challenges are equally high for the business organizations to ensure an effective implementation of GST in their businesses.

We have made an attempt to bring out some of the aspects which every business organization may have to address before the effective date of implementation of GST so as to ensure that the Organization is fully geared to face the challenges which may be imposed in the initial stages.

2.0 GST Implementation – Pictorial Representation



3.0 Move 1 - Formation Of An Internal GST Implementation Cell ('GIC')

3.1 A GST Implementation Cell (GIC) needs to be formed, who shall be entrusted with the key responsibility of ensuring a smooth transition from the existing regulations to the new GST Regime. The GIC should be ideally headed by the Chief Financial Officer or Head of Taxation with full support from the Head of Indirect Taxation.

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3.3 Considering the GST regime shall have a significant impact on the various business functions, it is essential that the GIC comprises of team members from various departments including:

- Finance
- Taxation
- Accounts
- Procurement
- Production / Manufacturing and Servicing
- Logistics
- Warehousing
- Sales & Marketing
- Information Technology

4.0 Move 2 – Gauging The Challenges

4.1 The first and foremost responsibility of the GIC should be to identify the various business functions and team members who would be affected in the new GST Regime. After the above analysis, each of the business functions would need to be studied in depth to gauge the challenges which the organization shall face. The above analysis can be undertaken either parallelly or in a phased manner.

4.2 Phase 1 - Challenges In Taxation And Finance Functions

GST being a major indirect reform is bound to have a significant impact on the Taxation and Finance Functions of any organization. Some of the initial significant challenges would include:

- Determining whether the existing goods / services fall under taxable / exempt category in GST Regime
- Determining the rate of GST applicable
- Impact of Composition / concession Schemes
- Impact of withdrawals of concessions to SEZ, EOU, EHTP, etc.
- Impact of withdrawals of exemptions and deferral schemes
- Determination of Taxable Events for sale of goods and provision of services.
- Determination of Input Tax Credit ('ITC') on State Goods and Services Tax ('SGST'), Central Goods and Services Tax ('CGST'), Integrated Goods and Services Tax ('IGST').
- Determination of event on which Input Tax Credit ('ITC') shall be eligible and disallowed / reduced.

- Impact of Central and State taxes not subsumed in GST Regime such as Purchase Tax and ITC of the same
- Impact on Cash Flow, working capital and Profitability
- Review of existing sales and servicing contracts from a change in the pricing and tax rates perspective.
- Impact on existing contracts, tax benefits.
- Impact of certain transaction models such as sales in transit, high sea sales, penultimate sales for exports
- Impact on existing ITC (under Excise, Service Tax, VAT etc).
- Impact on Inventory (at factory, depot)
- Tax Impact on supply of goods / provision of services to offshore locations such as Mumbai High
- Impact on supply of goods / provision of services to SEZ, EOU, EHTP, etc. locations
- Impact on of inter-State, inter-unit transfers, consignment transfers, etc
- Impact of GST on cost associated with packing, labeling, etc.
- Impact on Work in Progress – Goods, Long Term Contracts for construction, lease, etc, provision of services already under progress.

4.3 Phase 2 - Challenges In Operational Business Vis-À-Vis The Finance Functions

Across the world, it is generally seen that the introduction of GST reduces the tax burden on the ultimate consumer and hence reduction in general prices of goods. Accordingly, it is imperative that operational business functions such as procurement, sales and marketing etc shall be impacted under the GST Regime.

- Procurement of Goods and Services – Domestic (local vis-à-vis inter-State) and Imports, centralized and decentralized
- Remodeling of the Product Costing
- Determination of pricing of the Finished Goods
- Need to develop new Sales Model - ITC impact on account of Inter State Sales / Transfer to Depots.
- Planning for Capital expenditures during cut-off stage

4.4 Phase 3 - Challenges In Documentation And Compliances

As the GST would replace Excise, Service Tax and Value Added Tax, the same shall have a significant impact on the documentation being used in commercial, accounting and compliances functions. Accordingly, the GIC will have to revamp the documentation, accounting and compliances related function. The same would include:

- Format of Purchase Orders and Contracts
- Format of Register for Raw Materials, Finished Goods,
- Format of Register for allocation of inputs and ITC to taxable Goods/Services and exempt Goods/Services
- Formats for input and output register (taxable / exempt)
- Format of Price Lists
- Format of Invoices
- Format of delivery challans
- Policies for approving input documents
- Accounting for GST Charged (i.e. SGST,and CGST/ IGST)

- Accounting for ITC Paid (i.e. SGST and CGST / IGST)
- Accounting for SGST, CGST, IGST (charged or set-off) on account of purchase / sales returns, discounts etc.
- Systems of Determination of timely payment SGST, CGST and IGST Liability
- Filing of Returns.
- Filing of refund claims
- Amendment to the Standard Operating Manuals
- Re-vamping of existing accounting systems to suit the above GST requirements.
- Compliance Costs

5.0 Move 3 – Information Technology Challenges

Today most medium and large organizations operate on a real time virtual information technology network using ERP and its variants. Considering the far reaching implications the implementation of GST would have in a real time automated virtual information network there is a need to ascertain and strategize on –

- The areas where GST change over will impact the existing ERP system
- Identifying the impact areas and categorizing them based on criticality and functionality – strategic, compliance oriented, documentation oriented etc.
- Working on strategies on how to address these impact areas with minimal changes being done in the ERP network to keep the whole process cost effective
- Identifying the challenges of having a parallel system of legacy and current systems running (i.e. pre – GST and post – GST compliant systems)
- Rework on the IT strategy covering various related aspects to ensure that the organization as a whole from an IT perspective is geared up to migrate to the post GST era in a smooth and seamless manner
- Preparing required additional / new modules to comply with GST regulations with option for amendment

6.0 Move 4 –Training (Initial And Regular)

The GST Regime will need that every employee in the organization is well aware of the impact of GST on his day-to-day work. Accordingly, training would be an essentially ingredients in the initial stages of the GST Regime.

- In-depth training to the various functional heads who will monitor day to day work
- Initial training to all the employees whose routine day-to-day work shall be impacted with the introduction of GST
- Considering that GST shall be altogether a new regime for the Administrative Authorities, the regulations are bound to undergo various changes based on the practical experiences / difficulties faced during the implementation process. Accordingly, the GIC should ensure that there are systems of continuous training to the employees so as to enable to update their knowledge at regular intervals.

7.0 Move 5 – Identifying Key Areas Of Potential Litigation

Any migration will have its accompanying challenges. With GST encompassing a number of regulations covering both Central and State regulations, the challenges are also significant. Every challenge will bring with it financial and legal exposure and liabilities. Some of the key tasks in this area would be to –

- To ascertain some of the major and significant impact areas considering the specific requirements of the business organization where there is or can be subjectivity and lack of clarify which would result in potential litigations with the various stake holders, namely Vendors, Customers, Tax authorities etc.
- Categorize these impact areas based on criticality / possible financial impact.
- Work on addressing the issues bought out by a more focused study / interpretation of regulations and / or taking cues from how the industry in general is responding to the same.
- Where possible examine possibilities of getting expert views / opinions on the same to bring in the desired clarity.
- On issues which have high impact considering sensitivity explore the option of making a representation to the appropriate authorities to get the required feedback to suitably adopt appropriate strategies.

8.0 Move 6 – External Aids In Implementation

Considering the GST Regime to be something dynamic at least in the initial stages, it would be pertinent for the Organization to take assistance from external professional agencies to ensure that the GST implementation is in line with the Regulations.

- Get the GST implementation plan and strategy prepared by an External Professional Agency. If self done by the Organization, get it reviewed by a Professional Agency.
- Day to day advisory in respect of the GST so as to ensure that the GST team in the organization is updated with the latest changes which could have an impact on the organization.

9.0 Move 7 – Monitoring And Administration Of GST

Establishment of an internal control in line with the GST requirements

- Establish an internal control environment that effectively supports GST processing.
- Review of the effectiveness / deficiencies in the GST model implemented
- Regular Reporting of the transition to GST regulations
- Reporting of the impact of GST on the costing, pricing, profitability.
- Ensuring control and monitoring the regulatory changes undertaken having an impact on the business.

10.0 Move 8 - Switch Over Regulations

The switch over regulations needs to be carefully analyzed including the impact and the requirements for the transition. The same could include:

- Determination of Inventory – Raw Materials, Finished Goods, Work in Progress Consumables etc in the factory and the tax impact thereof.

- Determination of Inventory –Finished Goods, etc in the Depot and the tax impact thereof.
- Tax impacts on on-going contracts where work is undertaken prior to implementation and continued post implementation of GST.
- Change / Cancellation of Registration.
- Status of the existing ITC in Excise, Service Tax and Value Added Tax
- Impact on the various benefits available under the Foreign Trade Policy

11.0 Sign Off Comments

While GST is a welcome change which aims to simplify the regulations and making businesses more tax efficient and would be heralded as one of the significant Tax reforms happened in India in the recent times, the road ahead on implementation is a turbulent one. Business entities with professional help should target to address this challenge and effectively manage change.

“I can't change the direction of the wind, but I can adjust my sails to always reach my destination safe and sound” – Anonymous

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