

Enhancing GST Compliance: Navigating the New Automated Return Scrutiny System



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The Central Board of Indirect Taxes and Customs (CBIC) aims to streamline compliances in the Goods and Services Tax (GST) regime, given the fact that most cases pending in the legal forums are related to data mismatches with a very few arising from the interpretation of law. Due to technological advancements, CBIC has been using advanced artificial intelligence and analytics to monitor mismatches. This is part of the CBIC's plans to use more data analytics to improve compliance.

Additionally, CBIC has taken a significant leap towards ensuring tax compliance with the introduction of an automated return scrutiny system. This system is designed to meticulously monitor discrepancies in tax liabilities and input tax credits (ITC), mirroring the precision of the Income Tax Department's Computer Assisted Scrutiny Selection (CASS). By leveraging artificial intelligence and analytics, CBIC aims to flag inconsistencies and streamline the process of tax collection.

The focus of the automated scrutiny system is to reconcile differences between the details reported in GSTR-1 (monthly statement of outward supplies) and GSTR-3B (monthly summary of outward supplies and input tax credit). Additionally, the system compares the ITC available as per GSTR-2B (auto-drafted ITC statement) with the ITC claimed in GSTR-3B. Discrepancies in these forms can trigger automated notices, prompting taxpayers to provide corrections or explanations within a stipulated time frame.

In any self-assessment-based regime of taxation, tax returns are the first line of verification

and scrutiny for tax authorities. Accordingly, tax liability mismatches between GSTR-1 and GSTR-3B and ITC mismatches between GSTR-2B and GSTR-3B are one of the indicative parameters for identifying GSTINs by the GST authorities for the purpose of scrutiny of returns.

Accordingly, two pivotal rules have been instituted to bolster this scrutiny mechanism, i.e., Rule 88C and Rule 88D in the CGST ("Central Goods and Services Tax") Rules, 2017 as amended from time to time.

Rule 88C addresses the variances in self-assessed tax liabilities between GSTR-1 and GSTR-3B. Let us read on to understand this.....



Rule 88C

Section 75(12) of the CGST Act, 2017 permits the recovery of self-assessed tax without issuance of show cause notice under section 73 or 74 of CGST Act, 2017. Accordingly, CBIC vide Notification No. 26/2022-Central Tax dated 26.12.2022 inserted rule 88C in the CGST Rules, 2017 to prescribe the manner of dealing with **difference in self-assessed tax liability declared in GSTR-1 and tax liability paid in GSTR-3B**.

As per rule 88C, if the tax liability declared in GSTR-1 is more than tax liability paid in GSTR-3B by such amount and such percentage, then Form DRC-01B will be issued to taxpayer to either pay the differential tax or explain the difference within the time limit of 7 days.

In view of the above, GSTN developed a functionality in Form DRC-01B to enable the taxpayer to pay the differential tax liability or explain the difference in GSTR-1/IFF & 3B returns electronically on the common portal. The salient features of the functionality are as below:

- Form DRC-01B is applicable to various types of taxpayers, including regular taxpayers (including SEZ units and SEZ developers), casual taxpayers, and taxpayers who have opted composition scheme.
- The functionality compares the liability declared in GSTR-1/IFF with the liability paid in GSTR-3B for each return **period. If the declared liability exceeds the paid liability by a predefined limit or the percentage difference exceeds the configurable threshold**, taxpayer will receive an intimation in the form of DRC-01B.
- Form DRC-01B is divided into two parts – Part A and Part B. Part A is the system generated intimation from GSTN which details out the difference in liability under each head of GST and Part B is for taxpayer to provide reply against the intimation.

- Once DRC-01B is issued, the taxpayer will have two options in Form DRC-01B Part B - either pay differential tax along with interest under Section 50 of the CGST Act, 2017 through DRC-03 (Part B part 1) and/or provide reason for mismatch in liability reported and paid (Part B part 2).
- Part B part 2 contains list of 4 pre-set reasons for explanation of difference and there is an option for selecting 'Any other reason'. Detailed explanation must be provided for the selected option.
- DRC-01B will be issued after GSTR-1 and 3B are filed. If a satisfactory explanation has not been provided and if the differential tax has not paid off then taxpayers will not be able to file GSTR-1 for subsequent tax periods as per rule 59(6)(d) of the CGST Rules, 2017.
- Pursuant to rule 88C of CGST Rules, 2017, the taxpayer will have 7 days to provide an explanation or pay differential tax, failing which recovery of tax will be initiated against taxpayer under Section 79 of the CGST Act, 2017.

Now, let us look at rule 88D and understand....

Rule 88D

CBIC vide Notification No. 38/2023-Central Tax dated 04.08.2023 has inserted rule 88D in the CGST Rules, 2017 to prescribe the manner of **dealing with difference in ITC available in GSTR-2B and that availed in GSTR-3B**. As per section 73 of the CGST Act, 2017 read with rule 88D, if the ITC availed in GSTR-3B is more than ITC available in GSTR-2B by a **pre-defined limit or a percentage difference**, then Form DRC-01C will be issued to taxpayer to either pay the differential ITC availed or explain the difference within the time limit of 7 days.

In view of the above, GSTN has issued an advisory – "Online Compliance Pertaining to ITC mismatch -GST DRC-01C" dated 14th November 2023 in





complete alignment with the objective of the CBIC to allow availment of ITC in accordance with 'matching concept' i.e., ITC claimed by the recipient of supply is matched with the GST paid by the supplier in relation to that supply.

The advisory re-iterates the provision of rule 88D of the CGST Rules, 2017 and prescribes the manner of dealing with difference in ITC available in GSTR-2B and that availed in GSTR-3B. This functionality is live on the portal. The salient features of the functionality are as below:

- Form DRC-01C is applicable to various types of taxpayers, including regular taxpayers (including SEZ units and SEZ developers), casual taxpayers, and taxpayers who have opted composition scheme.
- The functionality compares the ITC available in GSTR-2B with the ITC availed in GSTR-3B for each return period. If the availed ITC exceeds the auto-populated ITC by a predefined limit or the percentage difference exceeds the configurable threshold, taxpayer will receive an intimation in Form DRC-01C.
- Form DRC-01C is divided into two parts – Part A and Part B. Part A is the system generated intimation from GSTN which details out the difference in ITC availed under each head of GST and Part B is for taxpayer to provide reply against the intimation;
- Once DRC-01C is issued, the taxpayer will have two options in Form DRC-01C Part B - either pay differential tax of excess ITC availed along with interest under section 50 of the CGST Act, 2017 through DRC-03 (Part B part 1) and/or provide reason for mismatch in ITC availed (Part B part 2).
- Part B part 2 contains list of 8 pre-set reasons for explanation of difference and there is an option for selecting 'Any other reason'. Detailed explanation must be provided for the selected option.

- Pursuant to rule 88D of CGST Rules, 2017, the taxpayer will have 7 days to provide a satisfactory explanation or pay differential tax, failing which recovery of tax will be initiated against taxpayer under section 73 or section 74 of the CGST Act, 2017.
- DRC-01C will be issued after GSTR-3B is filed. If a reply is not provided within 7 days, then taxpayers will not be able to file GSTR-1 for subsequent tax periods as per rule 59(6)(e) of the CGST Rules, 2017.

Although introduction of these functionalities by GSTN provides a standardised approach for taxpayers to explain the difference in liability between their GSTR-1 and GSTR-3B returns and difference in ITC as per GSTR-2B and GSTR-3B electronically on the common portal rather than correcting the same during the filing of Annual Return, but ever since the introduction of these online functionalities by GSTN, taxpayers have started obtaining notices in Form DRC-01B and DRC-01C to explain the difference in self-assessed tax liability declared in GSTR-1 and tax liability paid in GSTR-3B and difference in ITC availed in GSTR-3B and auto-populated in GSTR-2B respectively. GSTN has also proactively issued to detailed step-by-step instruction manual, FAQs and advisory for understanding these functionalities.

Predefined limit and the percentage difference

Based on research on the issue, an interesting piece of information has been observed, i.e., the predefined limit and the percentage difference between tax liability reported in GSTR-1 and tax paid in GSTR-3B finds a place in the agenda (Agenda Item 7(xi), Para 7) for 48th Council Meeting dated 17th December 2022 and has been placed in the meeting for GST council's approval. Basis perusal of minutes of the meeting (Point 8.11), it is observed that this limit and provision of rule 88C were discussed and approved by GST council to





issue notices where difference in tax liability reported in GSTR-1 and tax paid in GSTR-3B is more than 20% as well as more than Rs. 25 lakhs.

Similarly, the predefined limit and the percentage difference between GSTR-2B and GSTR-3B ITC amounts finds a place in the agenda (Agenda Item 3(viii), Para 4) for 50th Council Meeting dated 11th July 2023 and has been placed in the meeting for GST council's approval.

Basis perusal of minutes of the meeting (Point 4.36), it is observed that the predefined limit and the percentage difference between GSTR-2B and GSTR-3B ITC amounts has been discussed, recommended and approved by GST council to be 20% and Rs. 25 Lakh limit respectively.

However, the big question remains that the predefined limit and the percentage difference between GSTR-1 and GSTR-3B liability amounts and GSTR-2B and GSTR-3B ITC amounts limit has not prescribed anywhere under GST Act or Rules and even in the "Advisory" and "Comprehensive manual on Rule 88 C and Rule 88 D" and a question arises therefore if it is open to challenge by the taxpayers?

In this regard, it we have observed that the phrase used in the above mentioned Rules is **"by such amount and such percentage, as may be recommended by the Council"** unlike the words **"as may be notified by the Government, on the recommendations of the Council"** or **"Government may, by notification, on the recommendations of the Council"** used at various other places in the GST law which specifically requires CBIC to issue Notification on recommendation of the Council for various purposes.

Therefore, from the reading of the rule, it appears that CBIC may not be required to separately notify the above limits and instead, the same can be internally recommended and communicated by the Council. It may be akin to internal instructions.

Conclusion and implications

The automated return scrutiny system is likely to lead issuance of more notices and hence returns must be prepared with utmost care and diligence. Also, it is important to regularly check GST dashboard and update the e-mail IDs as the notices will be issued on GST portal.

Currently, all the taxpayers have an option to amend the auto-populated outward supplies or inward supplies in GSTR-3B. Additionally, Invoice Management system ("IMS") has been introduced to enable taxpayers to take actions for ensuring accurate ITC claims.

IMS functions as a mechanism that allows taxpayers to align their invoices with those provided by their suppliers, thereby verifying the correctness of their ITC claims. Initially introduced as an advisory practice, it appears that over time, the Government is inclined to make this procedure compulsory by introducing a feature that locks auto-populated data of ITC in GSTR-3B.

The 55th GST council meeting has also recommended to provide legal framework in respect of generation of Form GSTR-2B based on the action taken by the taxpayers on IMS to further streamline the compliance process.

GSTN portal has issued an advisory dated 17th October 2024 which states that values auto-populating in GSTR-3B will be hard locked (non-editable) as per auto-populated values from GSTR-1/1A and GSTR-2B. Tentative timeline provided was January 2025 tax period onwards. However, this seems to be a distant reality as GSTN portal vide advisory dated 27th January 2025 deferred the implementation of hard locking of figures citing various requests from the trade seeking time to adapt to this change. Nonetheless, Tax payers need to prepare for the same!!



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