

# The Hidden Liability Machine

Why India's Tax System forces innocent businesses to pay for their vendors' non-compliance.

A Deep Dive into GST Input Tax Credit (ITC) Risks

# Part 1: How GST is *Supposed* to Work

Imagine you are a business owner (Buyer).



Let's say you buy raw materials for ₹100.

- Step 1: The Tax is **18%**.
- Step 2: You pay the Vendor **₹118** (₹100 Cost + ₹18 Tax).
- Step 3: The Vendor is *supposed* to pay that ₹18 to the Government.

## The "Input Tax Credit" (ITC):

Because you already paid ₹18 to the vendor, the government says:  
"You don't need to pay tax on your own sales until you've used up this ₹18 credit."

This ₹18 is like **cash in your digital wallet**.

# Part 2: The Trap

What happens if the Vendor takes your ₹118 and runs away? Or simply forgets to file their tax return?

## Common Logic says:

"I paid the tax to the vendor. I have the invoice. Start an investigation against the vendor!"

## Indian Law says:

"We don't care. Since the vendor didn't pay us, **YOU** must reverse the credit."

## The Consequence:

- You lose the ₹18 credit (it vanishes).
- You must pay **Interest** (18-24%).
- You face a **Penalty**.

**Key Insight:** You effectively pay the tax **TWICE** because you trusted the wrong vendor.

# Part 3: The Weapon (Rule 37A)

The government recently introduced **Rule 37A** to automate this punishment.

## Section 16(2)(c) & Rule 37A

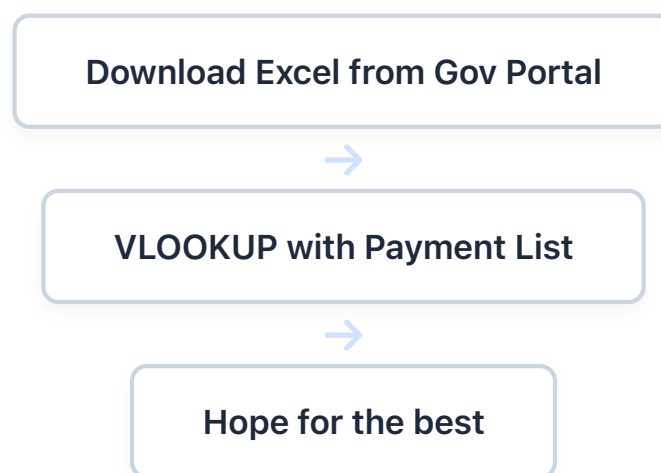
*"ITC cannot be claimed unless the tax charged has been actually paid to the Government."*

This shifted the burden of proof entirely onto the Buyer.

- **Observation:** The Government has outsourced audit to the Buyer.
- **Result:** CFOs are terrified. A single "Red Flag" vendor can contaminate their balance sheet for years.

# Part 4: How Companies Cope Today

Current State: "The Spreadsheet Chaos"



## Why this fails:

1. • **No Timestamp:** If a vendor was "Green" today but turns "Red" next year, how do you prove you checked?
2. • **Human Error:** Accounts Payable teams process thousands of invoices. They miss things.
3. • **Legally Defenseless:** A screenshot or Excel sheet is not strong evidence in court.

# Part 5: Our Solution

## ITC Protection & Vendor Due Diligence System

We don't just "check" status. We build a **Legal Defense Shield**.

### 1. The Gatekeeper

We sit **before** the payment run. If a vendor is risky, the money doesn't leave the bank.

### 2. The Auditor Artifact

We generate a signed, timestamped PDF Certificate for every check.  
*"This file is your shield."*

# Part 6: How It Works (V0)

Simple, operational workflow for Finance Teams.

- 1 **Upload:** AP Clerk uploads the "Proposed Payment Batch" (Excel).
- 2 **Analyze:** System checks Public GST Data + Rule 37A Triggers.
- 3 **Action:** Dashboard shows **STOP PAY (Risky)** or **RELEASE (Safe)**.
- 4 **Evidence:** System emails a "Due Diligence Certificate" PDF to the CFO.

# Part 7: The Opportunity

Why this is a venture-backable business.

## Target

### Exporters

They live and die by ITC refunds. A mapped solution is 'Must Have', not 'Nice to Have'.

## Model

### Subscription

Recurring Annual License.  
High switching cost  
(because we hold their compliance history).

*We are selling "Sleep" to CFOs in a highly regulated market.*



## Part 8: The Real Cost

This is not a theoretical problem. Here's what happens in reality:

# ₹12.4 Lakhs

**ITC Reversed + Interest + Penalty**

**Cause:** One vendor's GST registration was suspended.

**Buyer's fault:** None. They had a valid invoice.

**Outcome:** Buyer paid the tax twice.

**This happens every quarter to mid-sized exporters.**

Our tool costs **₹5L/year**. One prevented reversal = 2.5x ROI.


# Part 9: The Decision Engine

We use **rule-based logic**, not vague "AI risk scores".

## Three Decision States:



## Sample Rules:

| Condition                                 | Decision   |
|---|--|
| GST Status = Cancelled                    |  <b>PAYMENT HOLD</b> |
| GSTR-3B not filed for 2+ months           |  <b>PAYMENT HOLD</b> |
| Filing delayed by 30+ days                |  <b>HOLD</b>         |
| Active + On-time filings (last 3 periods) |  <b>RELEASE</b>      |

# Part 10: Who Uses It & How

This is not a "dashboard for everyone". It has **role-based access**.

## User Roles:

|                        |  |
|------------------------|--|
| <b>AP Clerk</b>        | Uploads payment batch (Excel)              |
| <b>Finance Manager</b> | Reviews flagged vendors, can override HOLD |
| <b>CFO</b>             | Final approval, audit trail access         |

## Usage Frequency:

- **Weekly:** Payment batch upload & review
- **Monthly:** Audit trail review by CFO
- **Quarterly:** Compliance report for statutory audit

# Part 11: The Trust Framework

We are **honest** about what we can and cannot guarantee.

## Data Freshness Policy:

### Every check displays:

*"This verification is based on publicly available GST data as of [DD-MMM-YYYY HH:MM IST]."*

## Staleness Warnings:

| Data Age    | Warning   |
|-------------|---|
| < 24 hours  | ✅ No warning                                    |
| 24-72 hours | ⚠️ "Data is 2 days old"                         |
| > 72 hours  | 🚫 "Data is stale. Manual verification required" |

### Liability Disclaimer (on every PDF):

"This certificate is a **decision support tool** based on publicly available data. It does not guarantee vendor behavior. The buyer retains full responsibility for ITC claims under Section 16(2)(c)."



# Part 12: What We Build First (V0)

We are **not** building everything at once.

## ✓ IN SCOPE (V0)

- • Upload Excel with GSTINs
- • Check GST status (Active/Cancelled/Suspended)
- • Check GSTR-3B filing history (last 3 periods)
- • Generate timestamped PDF certificate
- • Dashboard with STOP/HOLD/RELEASE flags

## ✗ OUT OF SCOPE (V0)

- • Penny drop / Bank verification (V1)
- • ERP integration (manual export for now)
- • Email alerts (manual download)
- • Historical trend analysis (V1)
- • ML-based risk scoring (rule-based only)

**V0 Goal: Validate the "Auditor Artifact" value with 5 friendly exporters.**

# Part 13: The Business Model

This is **not** a per-transaction SaaS. This is enterprise control software.

## Pricing Model:

### Annual License Fee

Recurring revenue. High retention.

## Positioning:

**"Cheaper than one bad vendor reversal."**

If a CFO pays ₹5L/year for this tool and it prevents even ONE ₹10L ITC reversal, the ROI is instant.

## Why High Retention?

- **Compliance History Lock-in:** We store their audit trail. Switching = losing evidence.
- **Statutory Requirement:** Rule 37A is not going away.
- **CFO Trust:** Once they trust the system, they won't risk going back to Excel.

