'Tax Audit u/s 44 AB'
AY 2015-16

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Disqualification for Appointment of Tax Auditors

Budget 2015-16-Disqualification of Auditors Appointment as per Section 288 for Carrying out Income Tax Audit or Certification Work -

The Income Tax Act, 1961 (the Act) contains several provisions (e.g. section 44AB, section 80-IA, section 92E, section 115JB, etc.) which requires the assessee taxpayers to furnish audit reports and certificates issued by an 'accountant' for ensuring correct reporting/computation of taxable income by the tax payers.

Explanation to section 288(2) of the Act defines an 'accountant' as a chartered accountant within the meaning of Chartered Accountants Act, 1949 (including a person eligible to be appointed as auditor under section 141 of the Companies Act, 2013, of the companies registered under any State).

The Comptroller and Auditor General of India (C&AG) published its report on "Appreciation of Third Party (Chartered Accountant) Certification in Assessment Proceedings" (No.32 of 2014). In Para 3.9 of the Report, it has been stated that the Chartered Accountant Act, 1949 debars an auditor to express his opinion on the financial statement of any business or any enterprise in which he, his relative, his firm or partner in the firm, has substantial interest.

However, during the course of audit, it has been noticed that an auditor has furnished his report in Form 56F in respect of a closely held company in which the auditor's brother was the managing director. To ensure the independence of auditor, sub-section (3) of section 141 of the Companies Act, 2013 contains a list of certain persons who are not eligible for appointment as auditor.

The audit/certification function under the Income-tax Act is mainly provided for protecting the interests of revenue. An auditor who is not independent cannot meaningfully discharge his function of protecting the interests of revenue.

Therefore, it is proposed to amend section 288 with effect from 1st June, 2015 to provide that an auditor who is not eligible to be appointed as auditor of a company as per the provisions of sub-section (3) of section 141 of the Companies Act, 2013 shall not be eligible for carrying out any audit or furnishing of any report/certificate under any provisions of the Act in respect of that company

On similar lines, ineligibility for carrying out any audit or furnishing of any report/certificate under any provisions of the Act in respect of non-company is also proposed to be provided.

However, it is proposed to provide that the ineligibility for carrying out any audit or furnishing of any report/certificate in respect of an assessee shall not make an accountant ineligible for attending income-tax proceeding referred to in sub-section (1) of section 288 of the Act as authorized representative on behalf of that assessee.

It is further proposed to provide that the person convicted by a court of an offence involving fraud shall not be eligible to act as authorized representative for a period of 10 years from the date of such conviction. (It is also proposed to revise the definition of 'accountant' in Explanation below section 288(2) of the Act on the lines of definition of 'chartered accountant' in the Companies Act, 2013).

The existing Explanation to subsection (2) of Section 288 shall be replaced by the following new comprehensive explanation:

*'**Explanation***: In this section, "accountant" means a chartered accountant as defined in clause (*b*) of sub-section (*1*) of section 2 of the Chartered Accountants Act, 1949 who holds a valid certificate of practice under sub-section (*1*) of section 6 of that Act, but does not include the person listed Annexure attached [except for the purposes of representing the assessee under sub-section (*1*)]-

An overview of section 44AB of Income Tax Act

A: - Applicability-

Every person-

a) **Carrying on business shall, if his total sales, turnover or gross receipts, as the case may be, in business exceed or exceeds one crore rupees in any previous year; or**

b) **Carrying on profession shall, if his gross receipts in profession exceeds twenty-five lakh rupees in any previous year; or**

c) **Carrying on the business shall, if the profits and gains from the business are deemed to be profits and gains of such person under section 44AE or Section 44BB or Section 44BBB as case May be and he has claimed such income to be lower than the profits or gains so deemed to the profit and gains of his business, as the case May be in any previous year or**

d) **Carrying on the business shall, if the profits and gains from the business are deemed to be the profits and gains of such person under section 44AD and he has claimed such income to be lower than the profits and gains so deemed to be the profits and gains of his business and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year.**

Get his accounts of such previous year audited by an accountant before the specified date and furnish by that date the report of such audit in the prescribed form duly signed and verified by such accountant as defined under section 288 of the Act and setting forth such particulars as may be prescribed, provided that this Section shall not apply to the person, who derive the income of the nature referred to section 44B and Section 44BBA on and from the date as notified.

Explanations:- Section Business Covered 44AD Eligible Business, 44AE Transport Business, 44B Shipping Business of a non-resident, 44BB Providing service or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils 44BBA Operation of aircraft by non-resident and 44BBB Civil construction etc. in certain turnkey power project by non-residents Any Other Relevant Section This refers to the sections not listed above under which income may be assessable on presumptive basis like section 44D and section 115A(1)(b) and will include any other section that may be enacted in future for presumptive taxation.

Tax Audit Report where Accounts are audited under any other law: -

Provided further that Provided further that in a case where such person is required by or under any other law to get his accounts audited, it shall be sufficient compliance with the provisions of this section if such person gets the accounts of such business or profession audited under such law before the specified date and furnishes by that date the report of the audit as required under such other law and a further report by an accountant in the form prescribed under this section.

Responsibility of the Tax Auditor

Considering the above provisions, it is clear that responsibility of the tax auditor is much higher in the cases where the account are not audited under other law i.e. Proprietary or Partnership firms and he has to carry out the entire audits of the books of accounts maintained and also has to report that the said accounts read with the notes thereon gives true and fair view as far as Balance Sheet and P & l Account/Income & Expenditure Account are concerned. Which means that tax auditor has to spent more time over and above the provisions specified in the form 3CD.

The revision in new the reporting requirement has significantly increased the responsibility of the tax auditors (Chartered Accountants). As per section 44AB only chartered accountants can perform tax audits.

If on scrutiny the particulars as furnished in Form 3CD are found to be inaccurate or false, the tax auditors might face strict action. **Attention is invited to section 276C related to prosecution for willful attempt to evade tax, etc.**

Tax auditors must be very careful in discharging their responsibility while reporting all forty-one clauses. They should preserve their working notes and make suitable observations/qualifications in clause (3) of Form No. 3CA or Clause (5) of Form No. 3CB as the case may be. The Revised (2014) Guidance Note on Tax Audit issued by ICAI gives vital guidance which must be adhered to.

Materiality and Audit Engagement

The tax auditor will also have to keep in mind the concept of materiality depending upon the circumstances of each case. He would be well advised to refer to the Standards on Auditing (SAs) issued by ICAI, as well as the "Guidance Note on Audit Reports and Certificates for Special Purposes". If the statutory auditor of a person is also appointed to undertake tax audit, it is advisable to carry out both the audits concurrently. Section 143 of the Companies Act 2013 gives certain powers to the auditors to call for the books of account, information, documents, explanations, etc. and to have access to all books and records. **No such powers are given to the tax auditor appointed under section 44AB. Attention is invited to SA 210- Agreeing the Terms of Audit Engagements.**

In other words, where an audit has already been conducted and the opinion of the auditor has been expressed on the accounts, it would not be necessary to repeat the entire exercise to express similar opinion all over again. The tax auditor has only to annex a copy of the audited accounts and the auditor's report and other documents forming part of these accounts to his report and verify the particulars in the prescribed form for expressing his opinion as to whether these are true and correct.

While test checks may suffice in the conduct of a statutory audit for the expression of the auditor's opinion as to whether the accounts depict a „true and fair‟ view, the tax auditor may be required to apply reasonable tests on the total information to be prepared by the assessee in respect of certain items in the prescribed form, e.g., in verification of payments for purchases/expenses exceeding Rs. 20,000/- in cash.

Test Check of Data: *“While test checks may suffice in the conduct of a statutory audit for the expression of the auditor's opinion as to whether the accounts depict a ‘true and fair’ view, the tax auditor may be required to apply* ***reasonable tests*** *on the total information to be prepared by the assessee in respect of certain items in the prescribed form, e.g., in verification of payments for purchases/expenses exceeding Rs. 20,000/- in cash. While the entity may have to prepare the details for the entire year,* ***the tax auditor may have to ensure that no items have been omitted in the information furnished and a reasonable test check would reveal whether or not the information furnished is correct.*** *The extent of check undertaken would have to be indicated by the tax auditor in his working papers and audit notes. The tax auditor would be well advised to so design his tax audit programme as would reveal the extent of checking and to ensure adequate documentation in support of the information being certified.”*

While the entity may have to prepare the details for the entire year, the tax auditor may have to ensure that no items have been omitted in the information furnished and a reasonable test check would reveal whether or not the information furnished is correct. The extent of check undertaken would have to be indicated by the tax auditor in his working papers and audit notes.

The tax auditor would be well advised to so design his tax audit programme as would reveal the extent of checking and to ensure adequate documentation in support of the information being certified. The tax auditor may rely upon the audit conducted by an internal auditor or by an outside professional firm appointed as internal auditor, by using his own judgment as to the degree of reliance which he wishes to place on the work of the internal auditor relevant to tax audit. The degree of reliance would depend on the areas of work covered by the internal auditor and relevant for purposes of tax audit, particularly by reference to working papers/documents of the internal auditor and ensuring that reasonable checks/tests have been applied to transactions covered by the internal auditor, to satisfy himself about the authenticity of the ultimate information.

It would be in the interest of the tax auditor to obtain and scrutinize the programme of work and procedures adopted and the relevant working papers and documents obtained by the internal auditor in evidence of the work carried out by him. Reference may be made to the SA 610 - Using the Work of Internal Auditors. Primarily, however, it would, be necessary for the tax auditor to ensure that in expressing his opinion, he has adequately satisfied himself as to the authenticity of the information contained in the relevant form and that, his working papers and documents are adequate to enable him to certify the particulars. Reference may be made to Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its‟ Environment (SA-315), The Auditors‟ Responses to Assessed Risks (SA-330) and Analytical Procedures (SA-520).

Audit procedures applicable to a person whose accounts of the business or profession have been audited under any other law will apply as well to a person who carries on business or profession but who is not required by or under any other law to get his accounts audited. In order to express his opinion on the accounts of a person belonging to the latter category the tax auditor should apply the same tests and checks as he would have applied in the conduct of audit of the former category.

In case the relevant vouchers for the expenditure and payments made by a non- corporate entity are not available, it will be necessary for the tax auditor to call for any other evidence in support of such expenditure and payments. The entity should be advised to maintain vouchers/records in evidence of transactions to avoid a qualification in the matter by the tax auditors. The qualification in respect of this matter would, in the normal course, be necessary in case the vouchers or other evidence required to be maintained are not produced in evidence of the income/expenditure or assets/liabilities.

The entity should be encouraged to maintain office vouchers with the recipient's signatures for the amounts reimbursed on account of expenditure like local conveyance etc., for which other supporting evidence is not possible to obtain.

It would also be advisable to give appropriate notes on accounts in the case of a person who carries on business or profession but who is not required by or under any other law to get his accounts audited. These may include disclosure regarding method of accounting and practices consistently and regularly followed, and whether a change in such matters or practice has been made during the year, notwithstanding the fact that such disclosures are required to be made in Form No.3CD.

Reporting

In case of 3CD the tax auditor has to report that particulars given in the said form 3CD and annexure thereto are **true and correct**.

In the case of an audit of Firms and Individuals, the tax auditor is required to express his opinion as to whether the financial statements give a true and fair view of the state of affairs of the assessee in the case of the balance sheet and in the case of the profit and loss account/ income and expenditure account, of the profit/loss or income/expenditure.

As regards the statement of particulars to be annexed to the audit report, he is required to give his opinion as to whether the particulars are true and correct. In giving his report the tax auditor will have to use his professional skill and expertise and apply such audit tests as the circumstances of the case may require, considering the contents of the audit report.

He will have to conduct the audit by applying the generally accepted auditing procedures which are applicable for any other audit. He can apply the technique of test audit depending on the type of internal control procedures followed by the assessee.

Audit Report and Qualifications

1. Compliance with Audit Report format SA 700 and SA 705 on qualifications in auditor's report is not possible as per the prescribed format
2. Qualifications' and 'Observations' used interchangeably in the format
3. In Form 3CB, qualifications / emphasis of matter on financial statements referred to as observations/ comments/discrepancies/inconsistencies – though auditor is opining on '**true and fair view**'
4. At the end of the Form 3CA and 3CB, auditor to certify the particulars to be given in Form 3CD as '**true and correct**' – subject to observations/qualifications.
5. The well understood distinction between observations/ qualifications/ discrepancies/ inconsistencies, etc. are blurred in the prescribed format

Standard matters of qualification in the software utility

Following 20 examples of qualification to Tax Audit

1. **Proper books of account, to enable reporting in form 3CD, have not been maintained by the assessee.**
2. **All the information and explanations which to the best of my/our knowledge and belief were necessary for the purpose of my/our audit has not been provided by the assessee.**
3. **Documents necessary to verify the reportable transaction were not made available.**
4. **Proper stock records are not maintained by the assessee.**
5. **Valuation of closing stock is not possible.**
6. **Yield/percentage of wastage is not ascertainable.**
7. **Records necessary to verify personal nature of expenses not maintained by the assessee.**
8. **TDS returns could not be verified with the books of account**
9. **Records produced for verification of payments through account payee cheque not sufficient.**
10. **Amount of expense related to exempt income u/s 14A of Income Tax Act, 1961 could not be ascertained.**
11. **Creditors under Micro, Small and Medium Enterprises Development Act, 2006 are not ascertainable.**
12. **Prior period expenses are not ascertainable from books of account.**
13. **Fair market value of shares u/s 56(2)(viia)/(viib) is not ascertainable.**
14. **Reports of audits carried by Excise/Service Tax Department were not made available.**
15. **GP ratio is not ascertainable from the financial statements prepared by the assessee.**
16. **Information regarding demand raised or refund issued during the P.Y. under any tax laws other than Income Tax Act or Wealth Tax Act was not made available.**
17. **The conceptual difference between 'true and fair view' and 'true and correct' to be taken into account.**
18. **Opinion on "True and Fair View" Auditor to be guided by Accounting Standards and not necessarily by the provisions of Income Tax Act.**
19. **Applicability of Accounting Standards of ICAI to Non Corporate Assessee.**
20. **Accounting standards prescribed under Income Tax Act.**

RSRV & Associates, Chartered Accountants

Certification of prescribed particulars in Form No. 3CD

General Issues

1. **Information to be compiled and authenticated by the assessee** - Auditor's duty to check the details, applying the auditing standards and techniques.
2. **In the case of conflicting Judicial precedents, Auditor should state the Judgment relied upon.**
3. **In the case of conflicting views with the assessee, the Auditor may state both the views and leave it to the Tax Department to decide the matter.**
4. **The Auditor will be primarily guided by the Income Tax Act while reporting the particulars in Form 3CD unless the matter involves purely accounting aspects such as Accounting Ratios.**

Increased focus on Tax Auditors and CAs

- Increased focus on role of tax auditors due to:
  - Reports signed under dummy or non-existent names
  - Reports signed exceeding permissible limits
  - Reports issued without undertaking an 'audit'
  - Reports issued by charging very low fees
- Mandatory e-filing of TAR mainly due to overcome above concerns
- **Serious doubts cast on conduct of concerned CA firm**

ITAT decision – Vijay V Meghani vs DCIT (Mum) 20/8/2014:- *ITAT held in its order that ICAI CPE programmes might have failed to achieve the desired objectives with some of the Chartered Accountants. It further said that it is high time that the ICAI should take note of these practicalities and should take corrective steps in order to maintain/restore the high standards and quality expected from a C.A. professional. -*

- ForAY2015-16: There are several instances in IT Act1961,where auditor attestation is necessary
- Audit required vide section 44AB of IT Act as under:

Sales/Gross Turnover or Gross Receipts exceed	AY1985-86 to AY2010-11	AY2011-12 to AY2012-13	AY2013-14 onwards
In case of Business	40lakhs	60lakhs	1crore
In case of Profession	10lakhs	15lakhs	25lakhs

- From AY 2011-12 onwards, auditu/s 44AB also necessary where assessee claims non-applicability of sec 44AD.
- ICAI has issued revised 'GN on Audit u/s 44AB'in 2014.

Procedure and Compliance

Audit in case of non-corporate entities

- Entire audit to be conducted.
- True and Fair view of Financial Statement is to be ascertained.

Moreover, since the appointment of the tax auditor is made by assessee, it will be in the interest of the assessee to furnish all the information and explanations and produce books of account and records required by the tax auditor. If, however, after agreeing to the terms of the engagement, the assessee subsequently refuses to produce any particular record or to give any specific information or explanation, **the tax auditor will be required to issue a qualified opinion if the effect is material but not pervasive and a disclaimer of opinion if the effect is material and pervasive, in accordance with SA 705-Modifications to the Opinion in the Independent Auditors" Report.**

The audit report given under section 44AB is to assist the income-tax department to assess the correct income of the assessee. In order that the tax auditor may be in a position to explain any question which may arise later on, it is necessary that he should keep detailed notes about the evidence on which he has relied upon while conducting the audit and also maintain all his working papers.

Such working papers should include his notes on the following, amongst other matters: -

1. Work done while conducting the audit and by whom.
2. Explanations and information given to him during the course of the audit and by whom.
3. Decision on the various points taken.
4. The judicial pronouncements relied upon by him while making the audit report.
5. Certificates issued by the client/management letters. The requirements of documentation and peer review concepts are applicable in respect of tax audit conducted by chartered accountants.

Tax Audit in case of Companies

For this purpose, attention is also invited to SA 230 - Audit Documentation, which provides that the tax auditor should document matters which are important in providing evidence that the audit was carried out in accordance with the basic principles. If the accounts of the business or profession of a person have been audited under any other law by the statutory auditor(s), **it is not necessary for the tax auditor appointed under section 44AB to conduct the audit once again in the matter of expression of "true and fair view" of the state of affairs of the entity and of its profit/loss** for the period covered by the audit. However, the said section envisages the certification of the particulars in the prescribed form on which the tax auditor has to express his opinion as to whether these are `true and correct'.

- **Only particulars in Form 3CD to be certified.**
- **Reliance to be placed on report of Statutory Auditor.**
- **SA 600 "Using the work of another auditor"**
- **Some additional verification may be necessary**
- **Co-relation of particulars given inform 3CD with disclosures in FS (e.g. AS 18, CARO report, etc.)**

- **Format for FS (non-corporate Entities)**
  - Recommended by ICAI–
    - BS in horizontal format– PL in vertical format
    - For firms to also state whether registered or not
    - Format also mentions Previous Years figures

- **Format for FS (Corporate Entities)**
  - In **Revised Schedule III**

Compliance with ICAI Code of Ethics

- Appointment and NOC procedures.
- Same person cannot conduct Internal Audit & Tax Audit.
- The auditor should not be indebted for more than Rs. 10,000
- **Ceiling on number of Tax Audit assignments**
  - 60 per partner (for audits during AY 2014-15 onwards) (earlier45)
  - HO and Branch considered as 1 assignment.
  - Audits conducted under section 44AD, 44AE and 44AF or under state VAT laws not to be included in the limits
- Minimum Fees to be charged:
  - Council decision for minimum fees (notified in 2009) repealed with effect from 7th June 2011
  - preferable to follow ICAI recommended scale of fees
- Record of Tax Audit assignments in prescribed format.

Applicability of Accounting Standards

- **Corporate entities**
  - Mandatory as per Companies (AS) Rules, 2006 as also sec 133 of Companies Act, 2013
  - Concessions to SMCs from some AS
- **Non-corporate entities**
  - Compliance not given by any statute (except for IT-AS 1 & IT-AS 2 issued under section 145 of Income Tax Act)
  - As per ICAI guidelines – mandatory for auditors while reporting – exemptions for SMEs from some AS.
  - **AS 1, AS 2, AS 7, AS 9, AS 10, AS 11, etc. need to be followed as otherwise the FS may not give "True and Fair" view**
  - **Consider implications u/s 145 if AS not followed**

Method of accounting.

145. (1) Income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" shall, subject to the provisions of sub-section (2), be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

(2) The Central Government may notify in the Official Gazette from time to time accounting standards] to be followed by any class of assessee or in respect of any class of income.

(3) Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1) [or accounting standards as notified under sub-section (2), have not been regularly followed by the assessee], the Assessing Officer may make an assessment in the manner provided in section144.

Business or Profession

B: - EXPLANATION of term PROFESSION & BUSINESS

- **Whether a particular activity can be classified as 'businesses' or 'profession' will depend on the facts and circumstances of each case.**

The term "business" is defined in section 2(13) of the Act, as under: **"Business" includes any trade, commerce, or manufacture or any adventure or concern in the nature of trade, commerce or manufacture. The word `business' is one of wide import and it means activity carried on continuously and systematically by a person by the application of his labour or skill with a view to earning an income.** The expression "business" does not necessarily mean trade or manufacture only. Whether a particular activity can be classified as "business" or "profession" will depend on the facts and circumstances of each case. **Barendra Prasad Roy v ITO[1981]129ITR295(SC)**

- Sec2(36) defines profession to include vocation.

The profession is not defined under the Act except in section 44AA (1) for maintenance of Books of account which are listed as under: -

The expression "profession" involves the idea of an occupation requiring purely intellectual skill or manual skill controlled by the intellectual skill of the operator, as distinguished from an operation which is substantially the production or sale or arrangement for the production or sale, of commodities.

- SC has stated "The expression 'profession' involves the idea of an occupation requiring purely intellectual skill or manual skill controlled by the intellectual skill of the operator, as distinguished from an operation which is substantially the production or sale or arrangement for the production or sale, of commodities."
  - CIT Vs. Manmohan Das (Deceased)[1966]59ITR699(SC),
  - CIT Vs. Ram Kripal Tripathi [1980]125ITR408(All).

Business or Profession

- CBDT has vide Notification No. SO-18(E)dated12.1.77,No.SO 2675dated25.9.1992 and No. SO385(E), dated4.5.2001 notified professions u/s 44AA.Theseare:
  - Accountancy
  - Architectural, Interior Decoration
  - Authorized Representative
  - Company Secretary
  - Engineering
  - Film Artists/Actors, Cameraman, Director, Singer, Story-writer, editor, Singer, lyricist ,dress designer etc.
  - Legal, Medical
  - Technical Consultancy
  - Information Technology

Followings are classified as Businesses: -

- Insurance Agent
- Nursing home
- Management consultants
- Coaching classes
- Stock broking
- Dealer in shares/securities
- Gain on sale on investments
- Clearing, forwarding and shipping agents
- Financial Planning Advisors,
- Dentist having individual practicing
- Group of Dentists practicing jointly as partners of a partnership firm.

What is Turnover?

- **Sec 2(91) of Companies Act, 2013 defines Turnover as:**
  - "turnover" means the aggregate value of the realization of amount made from the sale, supply or distribution of goods or on account of services rendered, or both, by the company during a financial year; (w. e. f. 12-9-2013)

- **CST Act, 1956 defines Turnover as:**
  - "turnover" used in relation to any dealer liable to tax under this Act means the aggregate of the sale prices received and receivable by him in respect of sales of any goods in the course of inter-State trade or commerce made during any prescribed period and determined in accordance with the provisions of the Act and rules made there under.
  - Sec 8A (1) of the said Act provides that in determining turnover, deduction of sales tax should be made from the aggregate of sales price.

- **Turnover also defined by ICAI in:**
  - Guide to Company Audit
  - Statement on CARO

  - **ICAI GN on sec 44AB defines in para 5.8 'turnover' as under**:
  - "the aggregate amount for which sales are effected or services rendered by an enterprise".

- **As per the GN:**
  - If sales tax and excise duty are included in the sale price, no adjustment in respect thereof should be made for considering the quantum of turnover. Trade discounts can be deducted from sales but not the commission allowed to third parties.
  - If, however, the Excise duty and/or sales tax recovered are credited separately to Excise duty or Sales Tax Account (being separate accounts) and payments to the authority are debited in the same account, they would be excluded from turnover.
- For Companies, in view of definition in sec2 (91) of the Companies Act,2013, may be difficult to follow above GN.

Turnover and Gross Receipts

The term “turnover” is a commercial term and it should be construed in accordance with the method of accounting regularly employed by the company. **The term “turnover” for the purposes of this clause may be interpreted to mean the aggregate amount for which sales are effected or services rendered by an enterprise.** If sales tax and excise duty are included in the sale price, no adjustment in respect thereof should be made for considering the quantum of turnover. Trade discounts can be deducted from sales but not the commission allowed to third parties. If, however, the Excise duty and / or sales tax recovered are credited separately to Excise duty or Sales tax Account (being separate accounts) and payments to the authority are debited in the same account, they would not be included in the turnover. However, sales of scrap shown separately under the heading, miscellaneous income will have to be included in turnover.

Considering that the words "Sales", "Turnover" and "Gross receipts" are commercial terms, they should be construed in accordance with the method of accounting regularly employed by the assessee. Section 145(1) provides that income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" should be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. The method of accounting followed by the assessee is also relevant for the determination of sales, turnover or gross receipts in the light of the above discussion. The total value of the sales less sales return is to be considered as turnover Net of trade discount including Turnover Discount (no cash discount). In normal situation sale off fixed assets, investments and commission on sales will not be part of the Turnover.

The term "gross receipts" is also not defined in the Act. It will include all receipts whether in cash or in kind arising from carrying on of the business which will normally be assessable as business income under the Act.

Whether the following is part of turnover?

- Trade discount.
- Cash discount.
- Sale proceeds of fixed assets.
- Sale of scrap (included in ‘Other Income’).
- Sale proceeds of shares/property held as ‘Investments’.
- Sale proceeds of shares/property held as ‘Stock-in-trade’.
- Sales by commission agent’s/share brokers.
- Rent received.
- Dividend received.

Shares & Securities

The turnover or gross receipts in respect of transactions in shares, securities and derivatives may be determined in the following manner.

(a) **Speculative transaction**: A speculative transaction means a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scripts. Thus, in a speculative transaction, the contract for sale or purchase which is entered into is not completed by giving or receiving delivery so as to result in the sale as per value of contract note. The contract is settled otherwise and squared up by paying out the difference which may be positive or negative. As such, in such transaction the difference amount is 'turnover'. In the case of an assessee undertaking speculative transactions there can be both positive and negative differences arising by settlement of various such contracts during the year. Each transaction resulting into whether a positive or negative difference is an independent transaction. Further, amount paid on account of negative difference paid is not related to the amount received on account of positive difference. In such transactions though the contract notes are issued for full value of the purchased or sold asset the entries in the books of account are made only for the differences. **Accordingly, the aggregate of both positive and negative differences is to be considered as the turnover of such transactions for determining the liability to audit vide section 44AB.**

(b) **Derivatives, futures and options**: Such transactions are completed without the delivery of shares or securities. These are also squared up by payment of differences. The contract notes are issued for the full value of the asset purchased or sold but entries in the books of account are made only for the differences. The transactions may be squared up any time on or before the striking date. The buyer of the option pays the premium. **The turnover in such types of transactions is to be determined as follows:**

(i) The total of favorable and unfavorable differences shall be taken as turnover.

(ii) Premium received on sale of options is also to be included in turnover.

(iii) In respect of any reverse trades entered, the difference thereon, should also form part of the turnover.

(c) **Delivery based transactions**: Where the transaction for the purchase or sale of any commodity including stocks and shares is delivery based whether intended or by default.

Income is Exempt from Tax

Exempted Turnover Requires Tax Audit

Such cases may cover those assessee who are wholly outside the purview of income-tax law as well as those whose income is otherwise exempt under the Act. It is felt that neither section 44AB nor any other provisions of the Act stipulate exemption from the compulsory tax audit to any person whose income is exempt from tax.

This section makes it mandatory for every person carrying on any business or profession to get his accounts audited where conditions laid down in the section are satisfied and to furnish the report of such audit in the prescribed form. A trust/association/institution carrying on business may enjoy exemptions as the case may be under sections 10(21), 10(23A), 10(23B) or section 10(23BB) or section 10(23C) or section 11. A co- operative society carrying on business may enjoy deduction under section 80P. Such institutions/associations of persons will have to get their accounts audited and to furnish such audit report for purposes of section 44AB if their turnover in business exceeds the prescribed limit (Presently Rs.100 lakhs w.e.f. A.Y. 2013-14).

Only Agriculture Income (Tax Audit Not Applicable)

But an agriculturist, who does not have any income under the head "Profits and gains of business or profession" chargeable to tax under the Act and who is not required to file any return under the said Act, need not get his accounts audited for purposes of section 44AB even though his total sales of agricultural products may exceed the prescribed limit (Presently Rs.100 lakhs w. e. f. A.Y. 2013-14)

Non-Residents: - The case of non-residents may be considered separately. **Section 44AB does not make any distinction between a resident or non-resident.** Therefore, a non-resident assessee is also required to get his accounts audited and to furnish such report under section 44AB if his turnover/sales/gross receipts exceed the prescribed limits. This audit, however, would be confined only to the Indian operations carried out by the non-resident assessee since he is chargeable to income-tax in India only in respect of income accruing or arising or received in India. Income below Taxable **Limit: -** It may be appreciated that the object of audit under section 44AB is only to assist the Assessing Officer in computing the total income of an assessee in accordance with different provisions of the Act. Therefore, even if the income of a person is below the taxable limit laid down in the relevant Finance Act of a particular year, he will have to get his accounts audited and to furnish such report under section 44AB, if his turnover in business exceeds the prescribed limit (Presently Rs.100 lakhs w. e. f. A.Y. 2013-14).

- Para 5.9 of the GN further states considering that the words "Sales", "Turnover" and "Gross receipts" "are commercial terms, they should be construed in accordance with the method of accounting regularly employed by the assessee".
- As per sec 145(1) income chargeable under "Profits and gains of business or profession" or "Income from other sources" is to be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. This method of accounting followed would also be relevant to determine sales, turnover or gross receipts.
- Whether the transaction is made on "principal to principal" basis of "principal to agent" basis is also relevant.

What are Gross Receipts?

Para 5.14 of GN states:

- **Gross Receipts** includes all receipts whether in cash or in kind arising from carrying on of the business which will normally be assessable as business income under the Act.
- Are the following included in **"Gross Receipts"**?
    - Export benefits received.
    - Interest received by money lender.
    - Exchange difference (net)
    - Insurance claims (other than fixed assets)
    - Package Tour charges recovered by a travel agent
    - Share of profit of a partner from a firm.
    - Write back of amounts payable to creditors (GN says 'no')

- In case of Reimbursements, the GN states that:
    - If the assessee is merely reimbursed for certain expenses incurred, the same will not form part of his gross receipts.
    - But in the case of charges recovered, which are not by way of reimbursement of the actual expenses incurred, they will form part of his gross receipts.
    - In case of professionals, may also depend on whether 'service tax' is recovered on such reimbursements.

Audit Procedures

- **Letter of appointment (by management)**
- **SA 210 – Agreeing to the terms of Audit Engagement**
  - **Engagement letter to be issued**
- **SA 230 – Audit Documentation**
- **SA 610 – relying on work of Internal Auditors**
- **SA 315 – Identifying and Assessing risk of material misstatement through understanding the entity.**
- **SA 330 – Auditors' responses to assessed risks**
- **SA 520 – Analytical Procedures**

Applicability of SA 700 while issuing Form 3CB

- SA 700(R) is applicable for all reports on audits of General Purpose Financial Statements (GPFS) in view of Footnote 9 to SA 800 states that "In India, financial statement prepared for filing with income tax authorities are considered to be general purpose financial statements."

- Clarification issued by ICAI on July 5, 2013:
  Considering the fact that all tax audit reports are now mandatorily required to be filed online and that the format of the report is prescribed by the CG, it is decided to defer the applicability of SA-700 (Revised) on the tax audit report under section 44AB of the IT Act by one year i.e. the requirements of SA-700(Revised) are not applicable for tax audit reports filed up to 31st March, 2014

ICAI Announcement – Council meeting 326 of 27-29 July 2013

- The Council noted that in many cases such prescribed auditor's report were required to be filed online in a preset form and, hence, it was not possible for the auditors to make necessary changes in these reports to bring them in line with the SA 700. …

- On a perusal of a cross section of the formats of the auditor's report prescribed under various laws, specially, the Income-tax Act, 1961 and the Value Added Tax Acts of various States, it is clear that these prescribed formats do not contain all the elements of the auditor's report as required in paragraph 43 of SA 700.

- Accordingly, it would not per se be possible for the auditors to state in their audit reports that the audit has been carried out in accordance with the Standards on Auditing. However, the auditors would be required to carry out the audits in accordance with the Standards on Auditing issued by the ICAI.

Form 3CA, 3CB & 3CD

- When to use 3CA and 3CB?
- Form 3CA is applicable to persons specified in section 44AB, who carry on business or profession, and who are required by or under any other law to get their accounts audited.

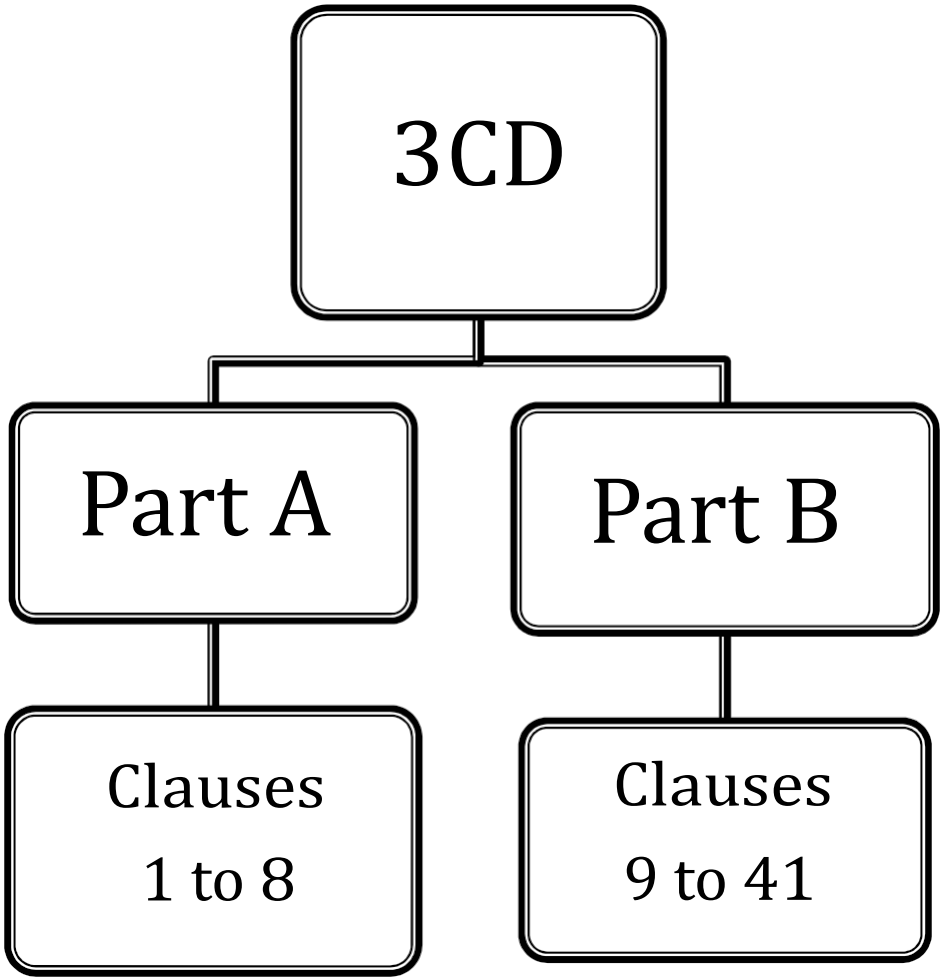
  Form 3CB is applicable to per sons applicable to persons specified insection44AB, who carry on business or profession, other than those who are required by or under any other law to get their accounts audited.
- Notes to Accounts to normally specify:
- Method of accounting followed – accrual or cash
- Revenue Recognition
- Inventory valuation
- Fixed Assets and Depreciation
- Investments
- Accounting of Forex fluctuations
- Items that may require qualification:
- Mandatory AS not followed (esp. for Companies)
- Non provision of Income Tax
- Non provision of Employee bonus and retirement benefits

- Confirmations for balances
- Inventory valuation on estimated basis
- For a proprietor having 2-3 different business – whether same or different Form 3CD?
- Primary responsibility of management
- To be certified by management

Signatures

- Form 3CA / 3CB to be signed by Chartered Accountant
- Mention of Firm Registration Number (FRN)
- Mention of membership number
- Form 3CD also to be signed by Assessee?
- Preferable for CA to put initials/stamp on each page/annexure of 3CD.

Form 3CD



Form 3CD–Whether Comments Necessary in Following Cases?

- **No interest charged on loans to relatives**
- **Insufficient household withdrawals**
- **Books not closed**
- **Investments, assets (like car, flat) held in names of partners and not name of firm.**
- **No quantity records are maintained**
- **Stocks not tallying with bank**

Clause 1, 2 , 3 & 5 are for Name, Address, PAN of the Assessee.

Clause 4 Regarding Indirect Taxes

Clause 4 of 3CD Whether the Assessee is liable to pay Indirect Tax Like Excise Duty, Service Tax, Sales Tax, Customs Duty, etc. if yes, please furnish the registration number or any other identification number allotted for the same.

Under clause (4), the auditor is required to mention the registration number or any other identification number, if any, allotted, in case the assessee is liable to pay indirect taxes like excise duty, service tax, sales tax, customs duty, etc.

Part A of Form No. 3CD generally requires the auditor to give the factual details of the Assessee. Thus, the auditor is primarily required to furnish the details of registration numbers as provided to him by the Assessee.

The reporting is however, to be done in the manner or format specified by the e-filing utility in this context

The term “Indirect taxes” is neither defined in the Income-tax Act, 1961 nor under any other law.

The levy of different types of indirect taxes on various transactions may differ from State to State.

Thus, it is recommended that the auditor should obtain from the Assessee the list of indirect taxes applicable to him.

Once the auditor obtains this management representation, he is required to obtain a copy of the registration certificate clearly mentioning the registration number under that relevant law. For example, Service tax registration number, Excise registration number, VAT registration number/ Central Sales Tax Registration number etc.

The Assessee may have multiple registrations for various manufacturing units, service units, godowns etc. under the same law.

In such circumstances also, a copy of all registration certificates is to be obtained from the Assessee for appropriate disclosure under this clause.

Where the indirect tax law does not require any registration, appropriate identification number may be reported in this clause.

For example, in Customs Act, 1962, since there is no registration number, a copy of Export Import Code (IEC) may be obtained and information be accordingly furnished.

The auditor has to keep in mind the provisions of Standard on Auditing 580 “Written Representation”.

In case the auditor prima facie is of the opinion that any indirect taxes laws is applicable on the business or profession of the assessee but the assessee is not registered under the said law, he should report the same appropriately.

The information may be obtained and maintained in the following format: -

Sr. No	Relevant Indirect tax Law which requires registration	Place of Business/ profession/service unit for which registration is in place/ or has been applied for:-	Registration/ Identification number
1.	2.	3.	4.

Clause 6 of 3CD regarding Previous Years

Under clause (6) the period of the previous year has to be stated. Since the previous year under the Act now uniformly begins on 1st April and ends on 31st March, the relevant previous year should be mentioned.

In case of amalgamations, demergers, reconstitution, new business, closure of existing business etc. the date of beginning/ ending of the previous year may be different, the auditor may accordingly, mention the relevant date of beginning and ending of the previous year in this clause.

Hence, the tax auditor has to apply his professional judgment depending on the facts and circumstances of the same.

Clause 7 is for Assessment Year only.

Clause 8 Indicate the relevant clause of Section 44AB under which the audit.

Relevant clause of section 44AB under which the tax audit has been conducted

1. 44AB(a)carrying on business if total sales, turnover or gross receipts, exceeds One crore rupees.
2. 44AB(b)carrying on profession if gross receipts exceed Twenty- five lakh rupees.
3. 44AB(c) Carrying on the business referred to in sections 44AE or 44BB or 44BBB and claiming his income from any such business to be lower than the income prescribed under the relevant section; or
4. 44AB(d) Where the profits and gains from the business are deemed to be the profits and gains of the assessee U/s 44AD and the assessee has claimed his income lower than the income prescribed U/s 44AD and during such previous year his income exceeds the basic exemption limit.

The Auditor has to report under which clause of Tax Audit, the Audit has been conducted.

The Auditor has to report if the Audit is of Business or Profession or under Presumptive taxation scheme. (Clause 8)

Clause 9 is only for the firm or Association of persons for their Name and Profit sharing Ratio.

Clause 10(a) & (b): Nature of Business or Profession

- **To give broad nature of each business/profession.**
- **To give principal line of each business/profession.**
    - **Main sector to be given with sub-sector**
    - **e. g. Manufacturing– aromatic chemicals.**

•Details as per Part B of annexure to Form 3CD.

- **E-filing portal requires details as:**

•Sector, sub-sector, code

- **Mention of any material change like:**

•New business started

•Some business discontinued– (if only temporary not to mention)

- **In practice, activities that constitute>10% are given.**

Clause 11(a), 11(b), 11(c): Whether books prescribed u/s 44 AA

- To give list of books prescribed, maintained and address of each location where books are maintained.
- Booksforcertainprofessionalsmentionedinsec44AA (1)
- Books constitute books of original entry and maybe prescribed under some other statute.
- Sec2 (12A) of the Act defines "books or books of account"–can be in Written form or print-outs or other form of electromagnetic data.
- Though books not prescribed in sec44AA (2), such books are required to be maintained to enable the AO to compute the income as per the IT Act.
- To give the list for allocations (including stock registers)
- If maintained in a computer system–to mention so.
- List of books of account and nature of relevant documents examined.

AS PER REVISED GUIDANCE NOTE 2014

From AY 2014-15, the address at which the books so maintained are kept is also required to be mentioned under clause (b).

In case the books of accounts are kept at more than one location then the auditor is required to mention the details of address of each such location along with the detail of books of account maintained thereof.

Clause 12 on Presumptive Income

Whether the profit and loss account includes any profits and gains assessable on presumptive basis, if yes, indicate the amount and the relevant sections (44AD, 44AE, 44AF, 44B, 44BB, 44BBA and 44BBB, **ChapterXII-G, First Schedule** or any other relevant section).

A. Section 44AD – Presumptive computation of profits for taxation for business

Any eligible Assessee engaged in an eligible business. Eligible Assessee is defined as an individual, HUF, resident partnership firm**, but excludes an LLP under the LLP Act, 2008 and any Assessee who has claimed a deduction under sections 10A, 10AA, 10B, 10BA or heading C of Chapter VIA (sections 80I-A, 80-IB,** etc.). An eligible business means any business other than the business of plying, hiring, or leasing of goods carriage as given in section 44AE and whose turnover/gross receipt in the previous year does not exceed Rs. 60,00,000 in A.Y. 2011-12 and 2012-13 and Rs. 1,00,00,000 in AY 2013-14 or in Year Succeeding the AY 2013-14.

Deemed Income:
8% of the total turnover or gross receipts of the Assessee on account of such business or any higher amount voluntarily declared by him shall be deemed to be his income chargeable to tax.
Provisions of Chapter XVII C relating to Advance Payment of taxes will not apply to the eligible Assessee in respect of eligible business only.

B. Section 44AE – Business of plying, leasing or hiring trucks *(Applicable till A.Y. 2010-11, this section is amended from A.Y. 2011-12)*

Any person engaged in the business of plying, leasing or hiring of trucks if he owns not more than 10 goods carriages at any time during the previous year including those taken on hire purchase or on installments. This scheme does not apply to those who operate trucks on hire without owning them (Circular 684, dated 10-6-1994)

Deemed Income:

1. **Heavy Goods Vehicle**- **Higher of Rs. 5,000** for every month (or part of a month) during which the goods carriage is owned by the tax-payer or an amount actually earned from such vehicle.
2. **Other than Heavy goods vehicle**- **Higher of Rs. 4,500** for every month (or part of a month) during which the goods carriage is owned by the tax-payer or an amount actually earned from such vehicle.

C. Section 44AF – Business of retail trading of goods
(Applicable till A.Y. 2010-11, this section will become inoperative from AY 2011-12 and the retail traders can choose to be governed by section 44AD from A.Y. 2011-12 which requires presumptive income at 8% of gross receipts/turnover)

Clause13 (a), (b), (c), (d): Method of Accounting

- Method of accounting followed
  - Accrual vs. Cash method (mixed or hybrid method not allowed)
  - Method to be consistently followed
  - Allow ability of remuneration in case of professional firm following Cash basis
  - Cash basis not possible for companies (in view of sec 209 of Cos Act 1956 / sec 128 of Companies Act 2013
- Deviation from accounting standards prescribed u/s 145 – sec 145 has notified 2 AS:
  - AS 1 (IT) – similar to AS 1 of ICAI / notified AS for Cos
  - AS 2(IT) – similar to AS 5 of ICAI / notified AS for Cos
- AS 1(IT) requires disclosure of all significant accounting policies
- Change in method of accounting
- Allowed as per Para 9 of AS 2(IT) in 2 cases
- Adoption required by statute
- Change would result in more appropriate presentation of FS
- Materiality to be considered
- Effect on profit/loss to be stated (in columnar format)
- Changed policy to be followed consistently
- Change in policy is not to be reported as 'change of method of accounting' – impact thereof is however disclosed in FS.

The Finance (No. 2) Act, 2014 has amended section 145 w. e. f. AY 2015-16 to the effect that the words 'accounting standards' be replaced with the words 'income computation and disclosure standards'.

As per the memorandum explaining the Finance (No. 2) Bill 2014, such an amendment has been made in order to clarify that the standards notified under section 145(2) are only meant for computation of income and disclosure of information and the Assessee need not maintain books of account on the basis of AS notified under the Income-tax Act, 1961.

The Accounting Standards issued by ICAI/ Companies Accounting Standard Rule, 2006 would still be required to be followed by the assessee, for preparation of financial statements.

Clause 14(a), (b): Method of Valuation of closing stock

- **Closing stock consists of RM, WIP, FG, Stores, etc.**
- **Normal valuation principles to be followed:**
  - At lower of Cost or NRV;
  - To follow Absorption Costing;
  - To include all costs incl. **excise duty (sec 145A)**
  - To mention how cost is determined
  - **If cost arrived at as SP less GP margin – whether ok?**
  - **Allowed at SP in certain cases [SC decision of British Paints (188 ITR 44)]**
- To also value stores, packing items
- **Change in method of valuation covered in Clause 13**
  - To mention effect of 145A on
  - Any tax, duty, cess, etc. paid/incurred on inputs to be added to the cost of the inputs, if not already added;
  - Any tax, duty, cess, etc. paid/incurred on sale of goods to be added in sales, if not already added;
  - Any tax, duty, cess, etc. paid/incurred on inventory to be added to inventory valuation, if not already added;
  - Section 145A thus requires "Inclusive method" as against "Exclusive method" mandated by AS 2.
  - ICAI GN on "Tax Audit u/s44AB" mentions (with an illustration) that in both methods, impact on profit/loss is Nil.
  - **For an entity following "Exclusive method" ICAI GN has suggested disclosure in the following table.**
  - **Get list of Closing Inventory;**
  - **Confirm whether all items like RM, WIP, FG, Stores, packing materials, consumables, etc. are valued**
  - **Confirm method of valuation (incl. determination of cost, etc.)**
  - **Tally inventory list with that submitted to the bank –**
  - **Quantity should match–value may differ due to different valuation method applied.**

	Particulars	Increase in Profit(Rs.)	Decrease in Profit(Rs.)
1	Increase in cost of opening stock on inclusion of excise duty on which CENVAT available/availed	Xxx	Xxx
2	Increase in purchase cost of RM on inclusion of excise duty on which CENVAT available/availed	Xxx	Xxx
3	Increase in sales of finished goods on inclusion of ED	Xxx	Xxx
4	ED paid on Sale of FG due to inclusion in Sales	Xxx	Xxx
5	Increase in closing stock of RM on inclusion of ED	Xxx	Xxx
6	Increase in closing stock of FG on inclusion of ED	xxx	Xxx
7	Increase in ED on closing stock of FG as a result of its inclusion in closing stock of FG	xxx	Xxx
8	Accounting of CENVAT credit availed and utilized on RM consumed in payment of ED on FG accounted on basis of RM consumed	Xxx	Xxx

- **Disclosure as per ICAI GN, if 145A not followed**

Section 145A of the Income Tax laid that the valuation of purchase, sale of goods and inventory for the purposes of determining the income chargeable under the head "Profits and gains of business or profession" shall be adjusted to include the amount of any tax, duty, cess or fee (by whatever name called) actually paid or incurred by the Assessee to bring the goods to the place of its location and condition as on the date of valuation.

As per the guidance note issued by the ICAI "Guidance Note on Tax Audit u/s 44AB of The Income Tax Act, 1961" there will be no impact of the section 145A on the computation of total income. With due respect I am of the opinion that the example given in the Guidance Note is not fully correct and required to be further analysis. There is impact on the total income due to impact of credit of indirect taxes.
As per my analysis there are two issues which required further analysis:

Regarding increasing the value of closing stock of finished goods for the duty to be levied/collectable at the time of actual sale.

Regarding impact of section 145A of Income Tax Act on the computation of total income.
Further following are issues which are not considered in the Guidance Note but required to be considered for the proper working of impact of section 145A:

Regarding impact of VAT or any other tax [In the guidance note only the impact of Excise Duty is discussed]
Regarding impact of duty paid on the purchase of capital goods on which depreciation cannot be claimed due to Explanation 9 to section 43(1).

Regarding increasing the value of closing stock of finished goods for the duty to be levied /collectable at the time of actual sale.
In the example given in the Guidance Note excise duty to be collected on the closing stock of finished goods as and when sold is taken into consideration. In my opinion as the excise duty is levied / collectable at the time of clearance of goods, inclusion of the same in the closing stock, without incurring any expenditure of such nature is not correct.

The exact sale value of the finished goods cannot be ascertained and there need to be presumption of sale.
In such case whether the sale price as on balance sheet date or actual sale price of the goods, if sold prior to the date of finalization of financial statement should be taken into consideration. If actual sale value is to be taken into consideration and all the closing stock of finished goods not sold till the date of finalization, then how to value etc. question arises.

The necessity and impact of closing stock in the financial statement while computing the profit was discussed by the Supreme Court in the case of Chainrup Sampatram v. Commissioner of Income-tax [24 ITR 481 (SC) (1953)]. Hon'ble Supreme Court in the case of CIT vs Dynavision Ltd. [348 ITR 380 (2012) (SC)].

Clause 15 Conversion of Capital Assets in Stock

When a Capital asset is converted into stock in trade then it comes within the definition of transfer u/s. 2(47) of I T Act, 1961, therefore it comes within the ambit of Capital gain Provisions.

1. **In which year the capital gain on transfer of capital assets into stock in trade arises?**

   Capital gain arises in the year in which capital assets is converted into stock in trade.

2. **In which year the capital gain on transfer of capital assets into stock in trade is Taxable?**

   Capital gain is taxable in the year in which the stock in trade (converted from capital assets) is going to sale.

3. **How to calculate the capital gain on conversion of capital assets into stock in trade?**

   First find out the fair market value of capital assets on the date of conversion. This fair market value of assets is the full value of consideration of asset.

4. **Is any profit under the head Business or Profession also arises on sale of stock in trade (converted from capital assets)?**

   Yes, Profit under the head Business also arises on sale of stock in trade (converted from capital assets)

5. **How to calculate the profit under the head business on sale of converted stock in trade?**

Sale Consideration	xxxx
Less: Fair Market Value of Assets	xxxx
Business Income	xxxx

Clause 16 Amount Not Credited to Profit & Loss A/c

a) **the items falling within the scope of section 28;**

b) **the Performa credits, drawbacks, refunds of duty of custom**

c) **or excise, or service tax or refunds of sales tax or value**

d) **added tax, where such credits, drawbacks or refunds are**

e) **Admitted as due by the authorities concerned.**

f) **escalation claims accepted during the previous years;**

g) **any other item of income;**

h) **Capital receipt, if any.**

Clause 17 Details of the Property Covered Under 43CA or 50C

Where any land or building or both is transferred during the previous year for a consideration less than valueadoptedorassessed or assessable by any authority of a State Governmentreferredtoin section 43CA or 50C, pleasefurnish:(contd…)

Section 43CA is applicable where the Assessee has transferred an asset (other than a capital asset) being land or building or both and the value of such an asset is less than the value adopted or assessed or assessable by any State government authority for the purpose of payment of stamp duty. In such a case for purpose of computing profit & gain from such transfer, the value so adopted or assessed or assessable shall be deemed to be the full value of consideration.

Section 50C is applicable where the Assessee has transferred a capital asset being land or building or both and the value of such an asset is less than the value adopted or assessed or assessable by any State Government authority for the purpose of payment of stamp duty. In such a case, for purpose of section 48, the value so adopted or assessed or assessable by stamp duty authority shall be deemed to be the full value of consideration.

Where any land or building or both is transferred during the previous year for a consideration less than value adopted or assessed or assessable by any authority of a State Government referred to in section 43CA or 50C, the auditor is required to furnish the following details:

(a) Details of property

(b) Consideration received or accrued

(c) Value adopted or assessed or assessable

Clause 18 Fixed Assets & Depreciation

- **Particulars of Block of Assets and depreciation**
    a. Description
    b. Rate of depreciation
    c. Actual cost or WDV
    d. Additions/Deductions with dates of acquisition/put to use – whether net of CENVAT credit, Foreign exchange fluctuations, subsidies
    e. Depreciation allowable
    f. WDV at end of the year
- Additions normally bifurcated into:
    - Used for more than 180 days and others
    - Cut-off date would be 2nd October (not 30th Sept)
- If list of additions very voluminous, summary information may be given.
- Date when Asset put to use – can differ with date of start of commercial production
- Capital assets claimed as deduction
    - R & D assets (also refer clause 15)
    - Assets less than Rs. 5,000?
- Computer Software: whether asset?

Expenditure on computer software is capital expenditure. ***Refer, Avaya Global Connect Ltd. 122 TTJ 300.*** **Again, Whether the expenses made towards the development of computer software is a Revenue Expenditure – Held, yes. Any expenses made towards computer software are Revenue expenditures.** ***Refer Varinder Agro Chemicals Ltd. 224 CTR 326.*** **Expenditure incurred on computer software packages though gives an enduring benefit it does not result in acquisition of any capital asset and constitutes revenue expenditure.** ***Refer, Southern Roadways Ltd. 220 CTR 298.***

Expenditure incurred on purchase of anti–virus software is of revenue expenditure. ***Refer Chambal Fertilizers & Chemicals Ltd. vs. ACIT Tax World. December Vol. XLIV. Part 6. P. 195.***

Adjustments for currency fluctuations (as per sec 43A)

The provisions of section 43A of the Income Tax Act are summarized hereunder:

- Where the Assessee has acquired any assets from a country outside India.
- The assets are acquired for the purpose of business or profession.
- Consequent to change in rate of exchange, there is increase / decrease in the liability of the assessee expressed in Indian currency towards cost of the assets or repayment of money borrowed for acquiring capital asset along with interest in foreign currency.
- Such increase or reduction in the liability shall be added or deducted from the actual cost of assets as and when paid or received.
- Adjustments for subsidies received (as per explanation 10 to sec 43).
- Provisions of section 36(1)(iii) to be considered.
- In case of disputes (which are under litigation) regarding depreciation claim in earlier years – to clearly mention the same.

In the column requiring the details of property, the auditor has to furnish the details about the nature of property i.e. whether the property transferred by him is land or a building along with the address of such property. If the Assessee has transferred more than one property, the detail of all such properties is required to be mentioned. The auditor should obtain a list of all properties transferred by the Assessee during the previous year. He may also verify the same from the statement of profit and loss or balance sheet, as the case may be. Attention is invited to the meaning of the term "transfer" as defined in section 2(47) of the Act.
Under the heading "consideration received or accrued", the auditor has to furnish the amount of consideration received or accrued, during the relevant previous year of audit, in respect of land/building transferred during the year as disclosed in the books of account of the Assessee.

For reporting the value adopted or assessed or assessable, the auditor should obtain from the Assessee a copy of the registered sale deed in case, the property is registered. In case the property is not registered, the auditor may verify relevant documents from relevant authorities or obtain third party expert like lawyer, solicitor representation to satisfy the compliance of section 43CA/ section 50C of the Act. In exceptional cases where the auditor is not able to obtain relevant documents, he may state the same through an observation in his report 3CA/CB.

Auditor would have to apply professional judgment as to what constitutes land or building for e.g. whether leasehold right / development rights / TDR / FSI etc. would fall under these provisions or not, would require to be evaluated based on facts & circumstances of transactions.

Clause 19 Amount Admissible

Amounts admissible as per the provisions of the Income-tax Act, 1961 and also fulfils the conditions, if any specified under the relevant provisions of Income-tax Act, 1961 or Income-tax Rules, 1962 or any other guidelines, circular, etc., issued in this behalf.

a. 32AC Investment Allowance 15% of Investment
b. 33AB Tea Development Account
c. 33ABA Site Restoration
d. 33AC Reserves for Shipping Business
e. 35Expenditure on Scientific Research
f. 35ABB Expenditure for obtaining Telecom License
g. 35AC Expenditure on Eligible Project or Schemes
h. 35CCA Payments to organizations carrying out rural development programme.
i. 35CCB Payments to organizations carrying out program of conservation of natural resources
j. 35D Amortization of certain preliminary expenses.
k. 35DD Amortization of expenses in case of amalgamation and demerger
l. 35DDA Amortization of expenditure incurred under voluntary retirement scheme
m. 35E Deduction for expenditure on prospecting, etc., for certain minerals

- **In case the Assessee has obtained a separate audit report for claiming deduction under any of these sections, he must make a reference to that report while giving the details under this clause.**
- **The tax auditor should indicate the amount debited to profit & loss a/c & amount admissible as per applicable provisions.**
- **The amount not debited to profit & loss a/c but admissible under any of the section mentioned have to be stated.**
- **If the Assessee is eligible for deduction under one or more of the above section, the tax auditor has to state deduction allowable under each section separately.**
- **New form provides for reporting of deemed income which results from sale or transfer of new asset, (if asset was acquired and installed by the Assessee for the purpose of claiming deduction under Section 32AC) within a period of five years from the date of its installation in plant and machinery<100cr.**

Clause 20 for Deduction u/s 36(1)

20(a) According to section 36 (1) (va), any sum received by the Assessee from any of his employees to which the provisions of sub-clause (x) of clause (24) of section 2 apply, if such sum is credited by the Assessee to the employee's account in the relevant fund or funds on or before the due date:

Explanation: - For the purposes of this clause, "due date" means the date by which the assessee is required as an employer to credit an employee's contribution to the employee's account in the relevant fund under any Act, rule, order or notification issued thereunder or under any standing order, award, contract of service or otherwise.

20(b) Details of contributions received from employees for various funds as referred to in section 36(1) (va).

Serial Number	Nature of fund	Sum received from employees	Due date of payment	The actual amount paid	The actual date of payment to the concerned authorities

Clause 21 of Form 3CD

21. (a) Please furnish the details of amounts debited to the profit and loss account, being in the nature of capital, personal, advertisement expenditure

Nature	Sr. no.	Particulars	Amount
Capital expenditure			
Personal Expenditure			
Advertisement expenditure in any souvenir, brochure, tract, pamphlet or the like published by a political party			

Nature (New Clause)	Serial No.	Particulars	Amount Rs.
Expenditure incurred at clubs being cost for club services and facilities used.			
Expenditure by way of penalty or fine for violation of any law for the time being force			
Expenditure by way of any other penalty or fine not covered above			
Expenditure incurred for any purpose which Is an offence or which is prohibited by law			

Section 143(1)(e) of the Companies Act 2013 specifically requires the auditor to inquire whether personal expenses have been charged to revenue account.

In the case of a person whose accounts of the business or profession have been audited under any other law, the tax auditor will have to report in respect of personal expenses debited in the profit and loss account.

In the case of a person who carries on business or profession but who is not required by or under any other law to get his accounts audited, the tax auditor will have to verify the personal expenses if debited in the expenses account while conducting the audit and verify the amount of expenses mentioned under this clause.

A) Whether Capital or Revenue Expenditure

1. Replacement of Machinery: Expenditure on replacement of old machines is in the nature of accumulated repairs and not current repairs. Therefore , the High court allowed such deduction under section 37 in place of section 31. *Refer CIT v Gitanjali Mills Limited 265 ITR 681 (2004).* Further, where parts of larger machines are purchased by the assessee, expenditure on such parts is allowable as revenue expenditure. (A. Y. 2001-02 to 2004-05). *Refer CIT Mod Industries Limited 197 Taxmann76.* Again Replacement of moulds did not result in creation of new capital assetor benefit of enduring nature, mere fact that moulds were used in production process could not be conclusive as to the nature of expenditure, hence, expenditure on replacement of moulds was revenue expenditure. *Refer CIT vs. Malerkotla Steels & Alloys (P.) Ltd 237 CTR 201 / 49 DTR 1.* The assessee company was engaged in printing and publication of various periodicals. It got repaired an empty derelict hall which was converted into a recreation room and was used by assessee's staff. The aforesaid deduction was allowed to the assessee as the repairs did not constitute a capital expenditure and hence were allowable under section 37(1) of the Act. *Refer ACIT vs. MM Publication Ltd 43 SOT 59.* Again Expenditure on up gradation or improvement of an existing product , through which all in all a new product is not made, is allowable as revenue expenditure. *Refer Matrix Telecom (P) Limited v ACIT 8 taxmann.com 26.* Again assessee is entitled to deduction of expenditure incurred on repairs to roof of a building commensurate with area is occupied by assessee for the purpose of his business. *Refer Danesh A Irani v CIT 7 taxmann.com 62*. Similarly, Assessee is a cardiologist purchased the second hand machines for use as spare parts to existing equipments is allowable as revenue expenditure. *Refer Aswanth N.Rao v ACIT 326 ITR 188.* Repair expenses incurred by the assessee on the rented premises is allowable u/s. 37(1) of the Act. *Refer Alkem Laboratories (P) Ltd. 28 DTR 11.* Replacement of machinery in a textile mill neither amounts to a current repairs nor revenue expenditure as each separate machine is an independent entity which brings an enduring benefit to the assessee.. *Refer Sri Mangayarkarshi Mills (P) Ltd. 26 DTR 58.* Expenditure incurred in acquiring new technology to replace existing technology is allowable as revenue expenditure. *Refer, Unidyne Energy Env System Pvt. Ltd. ITA No. 4007/Mum /2005, Bench – G, A.Y. 2001-02, dt. 10-9-2008 BCAJ p. 796, Vol. 40-B, Part 6, March 2009.* Again, Expenditure on replacement of parts of machinery is allowable revenue expenditure. Refer, Comsat Max Ltd. 124 TTJ 86.

2. **Expenditure incurred for restoring roof to original condition is not a capital expenditure**. Expenditure on removal of defect in design of car, relates to stock in trade of assessee is not a capital expenditure. *Refer Honda Siel Cars India Ltd. 1 ITR 497.* Again, Change of sound system does not increase revenue hence not capital exp. *Refer, CIT v Sagar Talkies 325 ITR 133.* Similarly, Spares parts purchased to be treated as revenue expenditure. *Refer, Dr. Ashwath N Rao V ACIT 5 taxmamm.com 63.* Again, where assessee following cash system of accounting, the expenditure incurred for purchase of second hand machinery for using its spare parts is revenue expenditure and the same is deductible in the year in which the sale consideration was paid even though the machinery was received in India after the end of relevant year. *Refer, Aswath N. Rao (Dr) vs. ACIT 38 DTR 205.* Again, Amount paid to foreign Company, for improving performance of its existing utility vehicles, and for purpose of development of concept of clay model for its utility vehicles, since the expenditure was incurred for improving performance of existing product, same was allowable under section 37(1). *Refer, Mahindra & Mahindra Ltd. 36 SOT 348*

3. **Compensation to Tenant: Amount paid by the Assessee, who purchased the plot of land, to the tenant occupying the structure erected by the tenant on such land for getting vacant possession is a capital expenditure. Refer CIT v Lucky Bharat Garage 174 ITR 526 (1998) & Chloride India Limited v CIT 130 ITR 61 (1981). However, Assessee entered into an agreement for purchase of property for infrastructural facilities for business, Assessee terminated the agreement and paid compensation, payment to be treated as capital in nature and not allowable as revenue expenditure. Refer Sap Labs India Pvt. Ltd. vs. ACIT 6 ITR 8**1.

4. **New Project Report: Expenditure incurred on project report for setting up a new unit is a capital expenditure. Refer CIT v J.K. Chemicals Limited 207 ITR 985 (1994)., However, Consultation charges paid by the Assessee in connection with the expansion of assessee's existing project were held to be allowable as revenue expenditure. Refer, Jyoti Ltd. 24 DTR 177. Similarly, Travelling and incidental expenditure in finalization of project for existing business allowable as revenue expenditure. Refer, Jt. CIT vs. Rallies India Ltd. 3 ITR 1 (Mum.) (Trib.) When no new asset created, then revenue expenditure Refer, CIT v DLF Commercial Developers Limited 323 ITR 321**.

5. **Expenses on Issue of Shares:** Expenditure incurred by a company in connection with issue of shares with a view to increase its share capital is directly related to the expansion of the capital base of the company, and is capital expenditure , even though, it may incidentally help in the business of the company and in profit making. Refer Brook Bond India Limited 225 ITR 798 (1997) & Kodak India Limited 229 ITR 445 (2002).

6. **Abandoned project.** ***Refer ONGC Videsh Ltd. 33 DTR 22.***
   Improvement of power line from Government Subsidy: Expenditure incurred by Assessee on rectification and improvement of power line was a revenue expenditure, even if ,it was spent out of subsidy amount received from Government.(Asst year 1987-88). *Refer Dy CIT v A.P.State Electricity Board 130 ITD*

7. **Website Development Expenses**: Expenditure on website would not change the fixed capital of an Assessee, even though website might provide enduring benefit to Assessee, expenditure incurred has to be regarded as revenue expenditure. Refer Indian Visit Com. (P) Limited) 176 Taxman 164. Similarly, Business expenses incurred for development of website to promote business activities, and display information and products is allowable as Revenue Expenditure. Refer, Polyplex Corp. Ltd. 176 Taxman 57.

8. **Computer Software**: Expenditure on computer software is capital expenditure. Refer, Avaya Global Connect Ltd. 122 TTJ 300.
   Again, whether the expenses made towards the development of computer software is a Revenue Expenditure – Held, yes. Any expenses made towards computer software are Revenue expenditures. Refer Varinder Agro Chemicals Ltd. 224 CTR 326.
   Expenditure incurred on computer software packages though gives an enduring benefit it does not result in acquisition of any capital asset and constitutes revenue expenditure. Refer, Southern Roadways Ltd. 220 CTR 298

9. **Mobile Handsets: The amount paid for handsets and for Talktime charges were not capital in nature. Refer, Radical Marketing Pvt. Ltd. vs. ITO ITAT 'SMC' Bench, Mumbai, ITA No. 3868/Mum/2008, decided on 19-5-2009 (BCAJ 42-A, May 2010 pg. 171)**.

B) Penalty:

1. **Compounding fees paid to RTO by a transporter for transporting over dimensional consignments is an allowable business expenditure u/s 37. Refer DCIT v Bharat C Gandhi 10 Taxmann.com 256.**

2. **However, Compounding fees being in nature of penalty & fine in terms of section 483 of Karnataka Municipal Corporation Act, 1976 is not allowable. Refer CIT vs. CB. K. R. Enterprises 219 Taxation 1.**

3. **In the case of Desiccant Rotors International (P) Ltd. vs. Dy. CIT47 DTR 193 it was decided that Payment made by the Assessee on settlement of dispute with a company of USA being neither a fine or a penalty for a proved offence nor an amount of Compensation of an offence but is merely a sum in settlement of an action charging the Assessee was denied and not proved the same cannot be rendered to be inadmissible deduction while determining the assessee's income from business.**

4. **Again Payments made towards luxury tax and not penalty is allowable as deduction. Refer RDB Industries Ltd. 120 TTJ 107.**

5. **Penalty, fines, etc paid by the Assessee to State Electricity Board for violating power regulation (drawing extra load in peak hours) was allowable deduction u/s. 37(1) of the Act. The Court further observed that if penalty is not for deliberate violation of law the same should be allowed as deduction. Refer Hero Cycles Ltd. 17 DTR 281.**

6. **Again, Payment, made under SEBI Regulation scheme, 2002 for failure to make disclosure as required under SEBI (Substantial Acquisition of shares and Takeovers) Regulations 1997 could not be treated as penalty as it is a payment for regularizing the default committed hence such payment cannot be disallowed by invoking explanation to s. 37(1). Refer, Kaira Can Company Ltd. 32 DTR 485**
7. **Penalty paid to NSE: Mumbai ITAT in another landmark case decided that fine or penalty imposed by NSE to its members is regulated by their in house laws and could not be termed as violation of statutory laws and hence cannot be disallowed. Refer Gold Crest Capital Markets Limited v ITO 36 ITR 177 (2010). Again, Penalty paid by Assessee a share broker, for excess utilization limits comparable to it for doing trade of its clients at a particular time was allowable u/s. 37(1) of the Income-tax Act. Refer VRM Share Broking (P) Ltd. 27 SOT 469**

8. **Regulation fees paid to Municipal Authority:** In this case High court of Karnataka decided that any regulation fees paid to municipal authority for compounding of offence is not available for deduction under section 37 **as the same was in the nature of penalty**. *Refer Millennia Developers (P) Limited v DCIT 37 DTR 19 (2010).*

9. **Payment of Protection Money to Rowdies & Police**: In the another landmark judgment decided by Karnataka High Court that any payment to **police or rowdies for getting protection from them is illegal** and should not be allowed. *Refer CIT v Neelavathi & Others 322 ITR 643 (2010)*.

10. **Fees paid to ROC:** It has been decided by the Rajasthan High Court that fees paid to the registrar of Companies for bringing about change in the memorandum and Articles should not be allowed. Refer CIT v Aditya Mills 181 ITR 195 (1990). Further, fees paid for increasing authorized capital is a capital expenditure. Refer CIT v Tungabhadra Industries Limited 207 ITR 553 (1994), CIT v Hindustan Insecticides Limited 250 ITR 228 (2001) & PSIDC v CIT 225 ITR 792 (1997).**Such expenditure also not eligible for deduction under section 35D of the act.**

11. **Bank Guarantee:** Gujarat High Court decided that any payment of bank charges related towards bank guarantee required for purchase of machinery should not be allowed as revenue expenditure. Refer CIT v Bharat Suryodaya Mills Co Limited 202 ITR 942 (1993).

C) Payment to Club

Club Membership: When membership of a club is taken in the name of director, it is for the Assessee-company to prove that membership was obtained solely for the purpose of business. Refer New India Extrusions (P) Limited v ACIT 10 Taxmann.com 165. Further Entrance fees paid towards corporate membership of the club is an expenditure incurred wholly and exclusively for the purpose of business and not towards capital account as it only facilitates smooth and efficient running of a business enterprise and does not add to the profit earning apparatus of a business enterprises and accordingly CIT (A) was justified in deleting the disallowances of entrances fee made by the Assessing Officer. Refer Dy. CIT vs. Bank of America Securities (India) (P) Ltd. 136 TTJ 441.

Again, Corporate membership fees payable to club is revenue exp. Refer CIT v Samtel Colour Limited 326 ITR 425

D) Donation to Political Parties: Sections 80GGB and 80GGC.

These two sections provide for deduction from gross total income of 100% of the amount donated by any company, individual, HUF, firm, LLP or other specified persons to recognized Political Parties or Electoral Trusts. Now, it is provided, by amendment of these sections, that no such deduction will be allowed if such donation is made in cash on or after 01-04-2013. It may be noted that in sections 80G and 80GGA donation to approved trusts can be made in cash up to Rs. 10,000/-. So far as Political Donations are concerned, it is now provided that no cash donations will be eligible for deduction under the above sections.

21(b) Amounts inadmissible under section 40(a): -

i. As payment to non- resident referred to in sub-clause (i)a

A) Details of payment on which tax is not deducted:

I. Date of payment
II. Amount of payment
III. Nature of payment
IV. Name of the payee
V. PAN of the payee, If available
VI. Address of the payee

B) Detail of payment on which tax has been deducted but has not been paid during the previous year or in the subsequent year before the expiry of time prescribed under section 200(1)

I. Date of payment
II. Amount of payment
III. Nature of payment
IV. Name and address of the payee
V. Amount of tax deducted

ii. As payment referred to in sub-clause (ia)

A) Details of payment on which tax is not deducted:

I. Date of payment
II. Amount of payment
III. Nature of payment
IV. Name of the payee
V. PAN of the payee If available
VI. Address of the payee

B) Details of payment on which tax has been deducted but has not been paid on or before the due date specified in sub-section (1) of section 139.

I. Date of payment
II. Amount of payment
III. Nature of payment
IV. Name & Address of the payee
V. Amount of Tax Deducted
VI. Amount out of (V) deposited, of any

This Revised Clause restricts the reporting only to sub-clause (i) and (ia).

a) Sub-Clause (i) deals with allow ability of payment made to non- resident Payees

b) Sub-Clause (ia) deals with payment to resident payees

It further requires Auditor to report the name and address of the payees in respect of whom default has been committed.

Sub-clause (ii & iia) – Income tax and Wealth tax are not deductible. Income tax also includes tax paid in any other country for which relief is available U/s 90, 90A, 91 of the Income Tax Act 1961. (Reporting not required in New Form 3CD

Sub-clause (iib) – any amount -

- paid by way of royalty, license fee, service fee, privilege fee, service charge or any other fee or charge, by whatever name called, which is levied exclusively on; or
- Which is appropriated, directly or indirectly, from, a state government undertaking by the state Government.

c) Sub-clause (iii) – Any salary payable outside India or to a non- resident shall be disallowed, if tax has not been deducted or paid.

d) Sub-Clause (iv) any payment to a provident or other fund for the benefit of the employees shall be disallowed unless the employer has made effective arrangements to secure that tax shall be deducted at source from any payments made from the fund which are chargeable to tax under the head "salaries".

e) Sub clause (v) any tax on non-monetary perquisites borne by the employer, on behalf of the employee which is exempt u/s 10(10CC) in the hands of the employee shall be disallowed.

Extract of Revised Section 40(a)(ia) of the Income Tax Act,1961 amended vide Finance Act, 2014 as applicable in relation to assessment year 2015-16 and subsequent years-

Section 40(a)(ia) [*any interest, commission or* brokerage, [*rent,*** *royalty,*] ***fees for*** *professional services* ***or fees for*** *technical services payable* ***to a resident, or amounts payable to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work*)]**, on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, [has not been paid on or before the due date specified in sub-section (1) of section 139 :]

[**Provided** that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in sub-section (1) of section 139, **[*thirty per cent of*]** such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid :]

[**Provided further** that where an assessee fails to deduct **the whole or any part of the tax** in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to sub-section (1) of section 201, then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the resident payee referred to in the said proviso.]

Disallowance for non-deduction or non-payment of TDS:

Under section 40(a)(ia) of the Act, in case of payments made to resident, the deductor is allowed to claim deduction for payments as expenditure in the previous year of payment, if tax is deducted during the previous year and the same is paid on or before the due date specified for filing of return of income under section 139(1) of the Act.

In case of non-deduction or non-payment of tax deducted at source (TDS) from certain payments made to residents, the entire amount of expenditure on which tax was deductible is disallowed under section 40(a)(ia) for the purposes of computing income under the head "Profits and gains of business or profession". The disallowance of whole of the amount of expenditure results into undue hardship.

In order to reduce the hardship, non-deduction or non-payment of TDS on payments made to residents as specified in section 40(a) (ia) of the Act, the **disallowance shall be restricted to 30% of the amount of expenditure on which TDS is not deducted**.

Earlier, 100% of such amount is disallowed.

Earlier, the non-deduction or non-payment of TDS on payments made to residents results in disallowance only with respect to certain specified categories of payments (viz. interest, commission, brokerage, rent, royalty, fee for technical services or fee for professional services).

NOW section 40(a) (ia) of the I-T Act to increase the scope of disallowance to **every category** of payment made to a resident on which tax is required to be deducted at source **under Chapter XVII-B** of the I-T Act.

Controversy:-

What amount to be disallowed us 40(a)(ia) on non deduction or short deduction?

Views:-

1) 30% of whole amount.

2) 30% of amount which TDS not deducted or short deducted (Proportional basis).

3) Disallowance under section 40(a)(ia) is only for non deduction of tax at source and not short-deduction of tax.

Analysis of views

1) First view is illogical as if person have deducted and paid tax on maximum amount but he didn't deducted and paid on minor amount.

2) Second view is true and fair view as 30% disallowance to be made on proportionally.

3) Third view is illogical because section 40(a) (ia) says that fails to deduct **the whole or any part of the tax.**

Let us understand it with some Examples:-

1) Tax to be deducted us 194J @10% is Rs 10,000/- on Rs 1,00,000/- and no deducted and paid. What will be amount of disallowance?

Answer:– No tax deducted and paid on Rs 1,00,000.

So Amount of disallowance will be Rs 30,000/- (30% of Rs 1,00,000/-) and if it is paid after due date then Rs 30,000/- will be allowed as deduction in next year.

2) Tax to be deducted us 194J @10% is Rs 10,000/- on Rs 1,00,000/- and actually deducted and paid Rs 1,000/-. What will be amount of disallowance?

Answer:- Tax deducted and paid is Rs 1,000/- means on Rs 10,000/- tax is deducted and on Rs 90,000/- tax is not deducted.

So Amount of disallowance will be Rs 27,000/- (30% of Rs 90,000/-) and if it is paid after due date then Rs 27,000/- will be allowed as deduction in next year. This is solved based on second view discussed above and if we take first view then disallowance will be Rs 30,000 which will be incorrect. To prove that first view is incorrect, let discuss example no 3.

3) Tax to be deducted us 194J @10% is Rs 10,000/- on Rs 1,00,000/- and actually deducted and paid Rs 9,000/-. What will be amount of disallowance?

Answer:- Tax deducted and paid is Rs 9,000/- means on Rs 90,000/- tax is deducted and on Rs 10,000/- tax is not deducted.

So Amount of disallowance will be Rs 3,000/- (30% of Rs 10,000/-) and if it is paid after due date then Rs 3,000/- will be allowed as deduction in next year. This is solved based on second view discussed above and if we take first view then disallowance will be Rs 30,000 which will be incorrect. Hence with this example it is proved that first view is incorrect.

Final Conclusion is that in case of non deduction and short deduction amount disallowed us 40(a)(ia) will be 30% of amount which TDS not deducted or short deducted (Proportional basis).

M/s Debdutta Construction Vs. ITO (ITAT Kolkata), Appeal Number-ITA 422& 423/Kol/2009, Date of pronouncement: 17.06.2015
In this case ITAT agreed with Assessee whereas Assessee relied on second provision to sec 40(a)(ia) which confirm that the expense will not be disallowed even if TDS had not been deducted on the expense debited to the profit & loss account provided Assessee proves that the amount on which TDS had not been deducted has been taken by deductee Assessee in his respective ITR and taxes on the same also been paid by them.

CIT vs. M/s Vector Shipping Services (P) Ltd., (2013) 262 CTR (All) 545 -

Hon'ble Allahabad High Court in case of CIT vs. M/s Vector Shipping Services (P) Ltd., (2013) 262 CTR (All) 545 held that for attracting disallowance under the said section, the amount should be payable and not which has been paid by the end of the year.

M/s. Mission vs. Income-tax Officer, (ITAT KOLKATTA), I.T.A No.1076/Kol/2014, Assessment year: 2009-10, Date of decision – 16th June 2015
After hearing the rival contentions, ITAT held that this is merely a case of short deduction of TDS. Admittedly, the Assessee has made labour payment or debited labour payment in the P&L Account at Rs.82,40,116/- and deducted TDS at Rs.87,490/- i.e. @ 1%. At best this can be a case for short deduction**. In the case of short deduction no disallowance can be made by invoking the provisions of section 40(a)(ia) of the Act**. ITAT stated that this view is fortified by the decision of Hon'ble Calcutta High Court in the case of CIT Vs. M/s. S. K. Tekriwal (2014) 361 ITR 432 (Cal)

TDS on transfer of immovable property:

(i) Section 194-1A – This new section is inserted in the Income-tax Act w.e.f. 01-06-2013. It provides that any person (transferee) who purchases any immovable property (whether residential or commercial) for a consideration, shall now deduct tax at source at the rate of 1% of the amount paid to a resident seller (transferor) if the said consideration exceeds Rs. 50 lakh. For this purpose, the term "Immovable Property", is defined to mean any land (other than Agricultural Land) or any building or part of a building. It may be noted that the section will apply in both cases i.e. when the purchaser is purchasing the property as a capital asset or as stock-in-trade.

(ii) This section will apply to all assessees, whether resident or non-resident, who purchase any immovable property in India from a resident. In other words, the obligation for deduction of tax is on every purchaser of immovable property, whether he is required to get his books of accounts audited u/s. 44AB or not. It will not be necessary for the purchaser to obtain Tax Deduction Account Number (TAN) u/s. 203A. However, the purchaser will have to file TDS Return and deposit TDS amount with the Government as provided in Section 200. The seller of the property must provide his PAN to the purchaser. If this is not done, tax on the sale consideration will have to be deducted at 20% as provided in section 206AA. It may be noted that the option of obtaining certificate from the A.O. u/s. 197 prescribing NIL rate or lower rate of TDS is not available in the above case.

(iii) If the purchase of the immovable property is from a non-resident, the tax will be deductible by the purchaser at the applicable rate u/s. 195 as at present. This new section will not apply to such a purchase. Similarly, this new section will not apply to payment of compensation on acquisition of immovable property to which the provisions of TDS u/s. 194LA are applicable.

(iv) It may be noted that a similar provision for TDS was proposed to be introduced by the insertion of section 194LAA in the Income-tax Act by the Finance Bill, 2012. Under this provision, it was proposed that the purchaser of an immovable property for a consideration exceeding Rs. 50 lakh in the specified area and Rs. 20 lakh in other areas shall deduct tax at source @ 1% of the consideration. For this purpose, the consideration was to be considered as specified in the Sale Deed or stamp duty valuation u/s. 50C whichever was higher. The registering authority was directed not to register the document unless the evidence for payment of TDS amount was produced before him. There was a lot of protest against the introduction of such a provision last year. Therefore, this provision was dropped before passing the Finance Act, 2012. A similar provision is again introduced this year and in the absence of any serious debate the same has been now brought into force from 01-06-2013.

(v) This new provision is likely to raise some issues as under:

i. The definition of immovable property only covers land (other than agricultural land) or building or part of the building. This will mean that any right in a building such as tenancy right, leasehold right etc. will not be subject to this TDS provision. [Refer: *Atul G Puranik vs. ITO 132 ITD* 499 (Mum)]

ii. If a person has booked a flat in a building under construction, either the flat is booked before 01-06- 2013 or after that date, and makes payment for the same, a question will arise whether he is required to deduct tax at source under this section. It is possible to take the view that by the agreement with the builder the purchaser gets a right to get the flat when constructed. Therefore, when the instalment payments are made to the builder there is no transfer of immovable property. [Refer: *ITO vs. Yasin Moosa Godil* 147 TTJ 94 (Ahd)] The transfer of flat will take place only when possession is given. Therefore, the obligation to deduct tax will arise under this section only when the last instalment is paid against possession of the flat. However, TDS @ 1% will have to be deducted on the entire consideration for the flat at that time.

iii. Since there is no specific mention in this section that if the amount of stamp duty valuation u/s. 50C is more than the actual consideration, the stamp duty valuation will be considered as consideration for TDS purposes, it can be concluded that tax is to be deducted from the actual consideration payable as per the sale deed. As stated earlier, in the Finance Bill, 2012 the proposed section 194LAA specifically provided for considering stamp duty valuation if that was more than the consideration stated in the Sale Deed. There is no such provision in this new section 194-1A.

iv. Section 199 of the Income-tax Act provides that credit for TDS amount will be given against the income in respect of which such tax is deducted. In a transaction of sale of immovable property, the seller will be showing income from such sale under the head "Capital Gains" or "Income from Business or Profession". It may so happen that an individual selling his immovable property may claim exemption u/s. 54 or 54F due to reinvestment in another property or u/s. 54EC by reinvestment in Bonds. In all such cases, credit for TDS under this new section will be available even if the income computed under the head "Capital Gains" is NIL.

v. If the property is purchased by two or more persons as co-owners, the tax will be deductible by each co-owner in respect of his/her share of the consideration paid if the total consideration for the property exceeds Rs. 50 lakh. This section also applies in respect of purchase of property from a relative.

vi. It may be noted that there is no provision for disallowance of purchase price of the property u/s. 40(a)(ia) in the case of a purchaser who has purchased the property as stock-in-trade.

21(c) Amounts debited to Profit and Loss Account being interest, salary, bonus, commission or remuneration inadmissible, under section 40(b)/40(ba) and computation thereof: -

The tax auditor is required to state the inadmissible amount under section 40(b)/40(ba) and such information is also required to be given in respect of interest/ remuneration paid to a member of an Association of persons (AOP)/Body of individuals (BOI). By Finance Act (No.2) 2009, w.e.f. 1.4.2010, the term firm includes LLP (as registered under the provisions of LLP Act, 2008) The word "inadmissible" implies that the tax auditor will have to examine the facts, apply the conditions for allowance or disallowance and accordingly determine the prima facie inadmissibility of the deduction and also quantify the same.

Salary, bonus, commission or remuneration or interest is not admissible, unless the following conditions are satisfied:

a) Remuneration is paid to working partner(s).
b) Remuneration or interest is authorised by the partnership deed and is in accordance with the partnership deed.
c) Remuneration or interest does not pertain to a period prior to the date of partnership deed.
d) Amount paid within the Limit prescribed under the act.

21(d) Disallowance/deemed income under section 40A (3)

A) On the basis of the examination of books of account and other relevant documents/evidence, whether the expenditure covered under section 40A(3) read with rule 6DD were made by account payee cheque drawn on a bank or account payee bank draft. If not, please furnish the details:

I. Sr. No.
II. Date of Payment
III. Nature of Payment
IV. Amount
V. Name and PAN of Payee, if available

B) On the basis of the examination of books of account and other relevant documents/evidence, whether the payment referred to in section 40A (3A) read with rule 6DD were made by account payee cheque drawn on a bank or account payee bank draft. If not, please furnish the details of amount deemed to be the profits and gains of business or profession under section40A(3A):

I. Sr. No.
II. Date of Payment
III. Nature of Payment
IV. Amount
V. Name and PAN of Payee, if available

Payments Disallowed u/s 40A (3) & 40A (3A)

As per section 40A(3) w. e. f. 2009-10, where the assessee incurs any expenditure in respect of which a payment or aggregate of payments made to a person in a day, otherwise than account payee cheque or account payee bank draft, exceeds Rs 20000, no deduction shall be allowed in respect of such expenditure.

However such limit of Rs 20000 has been increased to Rs 35000 w. e. f. 01-10-2009 in case the payment is made for plying, hiring or leasing of goods carriage.

Section 40A(3A) further provides (w. e. f. asst. year 2009-10) that in case an allowance is made in the assessment for any year on the basis of incurred liability, but in the subsequent year or years, assessee makes a payment exceeding Rs 20000 in a day, otherwise than by an account payee cheque or account payee bank draft, in respect of such liability, then the payment so made shall be deemed to be the profit of the year in which such payment is made.[The limit of Rs 35000 in case of plying, hiring or leasing of goods carriage is also applicable to section 40A(3A)].

Thus payment in excess of Rs 20000 in a day in respect of any expenditure incurred in the current year or in the previous years otherwise than by an account payee cheque or account payee bank draft will be disallowed while calculating profits of an assessee.

Aggregate Payment has to be seen: **After the amendment w. e. f. 2009-10 if a person makes more than one different purchases for cash from same person in excess of Rs 20000 in a single day even though on separate cash memos, such aggregate payment will be disallowed u/s 40A(3). For example if A makes three purchases of Rs 8000 each from the same person during different time of the day and obtains three different cash memos, yet the transaction will be covered by section 40A(3) and such expenditure will be disallowed**.

Exceptions under Rule 6DD: Proviso to section 40A(3A) provides that no disallowance shall be made and no payment shall be deemed to be the profits and gains of business or profession under sub-section (3) and this subsection[Section 40A(3A)] where a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft, exceeds twenty thousand rupees, in such cases and under such circumstances as may be prescribed, having regard to the nature and extent of banking facilities available, considerations of business expediency and other relevant factors.

The cases and circumstances as mentioned in the above proviso are contained under Rule 6DD and have been added vide Notification No. S.O2431(E), dated 10-10-2008 and are applicable w. e. f. A.Y. 2009-10. These circumstances and cases as provided under Rule 6DD are as Listed in this Notification . we do not provide entire list as same can be read from notification itself

Earlier clause (j) to Rule 6DD provided that if the payment hit by section 40A (3) is made in exceptional and unavoidable circumstances then no disallowance would be made u/s 40A(3). But the said clause has been omitted w. e. f. A.Y. 1996-97.

Some case laws:

In CIT v K.K.S. K Leather Processor P. Ltd.[2007] 292 ITR 669(Mad.) it was held that payments made on a day on which the banks are closed either on account of holiday or strike, shall not come within the ambit of disallowance u/s 40A(3).

In The Commissioner of Income-tax versus Vijay Kumar Goel [2010] 324 ITR 376 (Chhattisgarh) it was held that From a reading of the definition of bill of exchange u/s 5 and cheque under section 6 of the Negotiable Instrument Act, 1881, it is clear the banker's cheques/pay orders/ call deposit receipts are instruments which fall within the definition of bill of exchange. Hence payment made by the same could not be disallowed u/s 40A(3).

Where Books of accounts have been rejected and profit has been estimated, it is deemed that all the expenses and disallowances have been considered. Hence no further disallowance u/s 40A (3) is permissible- CIT V. Smt Santosh Jain[2008] 296 ITR 324(P&H).

21(e) Provision for payment of gratuity not allowable under sec.40A (7).

Any provision for gratuity in the books of accounts shall not be allowed as a deduction unless-

1. The provision is made for any contribution towards an approved gratuity fund, or
2. The provision is for gratuity, which has become due and payable during the previous year.

21(f) any sum paid by the Assessee as an employer not allowable under section 40A (9):

Payment to any unrecognized welfare fund (Section 40A (9)):

- Any contribution made by the Assessee, as an employer to any unrecognized or non-statutory welfare fund is not allowable as deduction.

21(g) Particulars of any liability of a contingent nature.

As per accounting standards, there shall be disclosure for contingent liabilities too and any such contingent liability found during audit needs to be reported

The assessee is required to furnish particulars of any liability of a contingent nature debited to the profit and loss account. The tax auditor may not be able to immediately ascertain the details of contingent liabilities debited to the profit and loss account without a detailed scrutiny of various account heads e.g. outstanding liabilities, provision etc. Accounting policy followed and disclosed would be helpful in ascertaining and verifying details. The expenses relating to disputed claims will be revealed only on the basis of the scrutiny of records relating to contingent liabilities. The tax auditor may look into particular items of contingent liabilities of the earlier year in order to determine whether or not any items has been charged to the profit and loss account of the current year and if so, whether the liability continues to be contingent in nature.

Wherever necessary, a suitable note should be given by the tax auditor as to the non-availability of such particulars relating to the contingent liabilities.

Reference may be made to AS-29, 'Provisions, Contingent Liabilities and Contingent Assets' to determine what should normally be treated as a contingent liability**.**

21(h) Amount of deduction inadmissible in terms of sec. 14A in respect of the expenditure incurred in relation to income which does not form part of total income:

Section 14A was inserted in Chapter IV – Computation of total income by the Finance Act, 2001 with retrospective effect from 1.4.1962 i.e. A.Y. 1962-63. Accordingly, for the purposes of computing the total income under Chapter IV of the Act, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under the Act.

The Finance Act, 2002 added a proviso to section 14A to the effect that nothing contained in the section shall empower the Assessing Officer either to reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year beginning on or before the first day of April, 2001.

We state that the rule 8D is applied only by exercising the Provision of Section 14 A of the Income Tax Act 1961 which state that following Conditions should be satisfied for Attracting the disallowance provisions of section 14A

1. It is an Expenditure
2. Such Expenditure Is incurred
3. Such incurring of the said expenditures is in relation to Income Which Does not Form part of the Total Income Under the Income Tax Act 1961

If above all three conditions are satisfied, the quantum of Disallowance shall be determined in accordance with subjection (2) and (3). Section 14A has within its implicit notion of apportionment in the cases where the expenditure is incurred for composite / indivisible activities in respect of which taxable and non taxable Income is received.

But when it is possible to determine the actual expenditure in relation to the exempt income or when no expenditure in relation to exempt income, then Principal of apportionment embedded in section 14A has no implication.

In order to disallow expenditure under section 14A, there must be live Nexus being the expenditure incurred and the income not forming part of the Total income.

Notional Expenditure cannot be apportioned for the purpose of earning exempt income unless there is an actual expenditure in relation to earning the Income not forming part of the Total Income. From this Provisions of the Act it is clear that if the expenditure is incurred with an aim to earn taxable Income and there is apparent dominant and immediate connection between the expenditure incurred and Taxable Income, then no disallowance can be made under section 14A merely because some exempted Income is received by the assessee.

Provisions of the Section 14A is application only there is an expenses incurred for exempted income and if there is no expenses incurred in relation to said exempted income and Rule 8D is applied if the expenses incurred towards exempted is indivisible or there are common expenses which are incurred in relation to both the income.

The Case law of Justice Sam P. Bharucha V/S Additional CIT (2012) 25 Taxmann.com 381 (Mumbai Tribunal) where it was decided that if there is no direct nexus between expenditure incurred and exempted income then Provisions of Section 14A cannot be applied.

As per section 14A only Expenditure which has been proved to be incurred in relation to earning of tax free income only can be disallowed and section cannot extended to disallow even expenditure which is assumed to have been incurred for tax free Income . Therefore Common Expenditure incurred cannot be broken artificially to attribute for apportionment a part thereof to earning of tax free income on assumption that such part of common expenditure was incurred in relation to tax free Income. DLF Ltd v/s CIT (2009) 27 SOT 22 (Delhi Tribunal)

There should be direct Nexus Between Expenditure incurred and Exempted Income Asst. CIT V/S Jindal Saw Pipes Limited (2008) 118 TTJ 228 (Delhi Tribunal)

Expenditure must be incurred in relation to exempted income. The Corollary to this is that if no expenditure is incurred in relation to the exempt income, then no disallowance can be made u/s 14A . Maxopp Investment Ltd v/s CIT (2011) 15 Taxmann.com 390 Delhi)

Disallowances of Notional expenditure or presumptive expenditure cannot be made under section 14A in absence of Actual Expenditure . CIT V/S Metalman Auto Private Limited (2011) 11 taxmann.com 51 (Punjab & Haryana)

21(i) Amount inadmissible under the Provision to sec. 36(1)(iii)

The provisions of section 36(1)(iii) provide that the amount of the interest paid in respect of capital borrowed for the purposes of the business or profession would be allowed as a deduction in computing the income referred to in section 28 of the Act.

The proviso there under (inserted by the Finance Act, 2003 w. e. f. A.Y. 2004-05) provides that any amount of the interest paid, in respect of capital borrowed for acquisition of an asset for extension of existing business or profession (whether capitalized in the books or account or not) for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was put to use, shall not be allowed as a deduction.

The extension of an existing business or profession is a fact based exercise and the tax auditor should apply the professional judgment in determining the applicability of the provision. The tax auditor is also advised to verify the treatment given for such asset under other provision of the Act like Chapter VI A deductions or under other statutes.

The requirements of sub-clause (i) are applicable in respect of capital borrowed for acquisition of an asset for extension of the existing business or profession. The assessee has to furnish the details of amount inadmissible under the proviso to section 36(1) (iii). The tax auditor has to verify the correctness of the particulars furnished by the assessee with the documentary evidence.

The Tax Auditor while determining the admissible/inadmissible amount under section 36(1)(iii) should also keep in mind the requirements of Accounting Standards 16 of Indian GAAP – "Borrowing Cost".

The Explanation provides that recurring subscription paid periodically by shareholders or subscribers in Mutual Benefit Society which fulfil such conditions as may be prescribed, shall be deemed to be capital borrowed within the meaning of section 36(1)(iii).

The Explanation becomes applicable only where the computation of the income of such mutual benefit society is to be made under section 28 Read with section 44A.

Clause 22 Interest inadmissible

Amount of interest inadmissible under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006

This is a new clause inserted by the Central Board of Direct Taxes through its Notification No. 36/2009 dated 13-4-2009, in the Form No.3CD in Appendix II of the Income-tax Rules, 1962.

The tax auditor is required to state the amount of interest inadmissible under section 23 of the Micro, Small and Medium Enterprises Development.

- Micro, Small and Medium Enterprises Development Act, 2006- "Implications for Annual Financial Statements" The Micro, Small and Medium Enterprises Development Act, 2006 ("the Act") has...
- Interest paid or payable to the micro, small and medium enterprises required to be reported in 3CD report Large companies may, henceforth, not find it easy to escape the taxman's...
- SEBI decided to facilitate setting up of Separate stock exchange for Small and Medium Enterprises (SMEs) Securities and Exchange Board of India (SEBI) which recognizes and regulates Stock.

Clause 23 Payment to Specified Persons

Sec. 40 A(2) provides that where the Assessee incurs any expenditure in respect of which a payment has been or is to be made to a relative or to an associate concern so much of the expenditure as is consider to be unreasonable or excessive shall be disallowed by A. O. And now the word "relative" has been defined in the sec.2 (41) of the Act.

In relation to a company (whether Private or Public), Relationship will have to be reckoned for the purpose, with reference to the directors or persons having substantial interest in the company.

Substantial interest in case of business carried on by a company, such person is, at any time during the previous year, the beneficial owner of equity shares carrying not less than 20% of voting power.

The decision of the ITAT, Ahmedabad 'A' Bench dated 09.07.10 in the case of Vipul Y. Mehta-vs- ACIT in ITA No. 869/Ahd/2010 for the assessment year 2007-08 wherein it was held that loan taken from the relatives cannot be compared with bank loan because loan from the relatives are without security, while loan from the bank is secured. In this decision, reliance was also placed in the decision of the Tribunal in the case of Omkarmal Gaurishanker –Vs- ITO reported in 92 TTJ (Ahd.) 223 wherein it was held that interest paid to relatives @24% is reasonable. It is also pertinent to note that interest paid by the Assessee before us is only 18%. Keeping in view the decision of the ITAT, Ahmedabad 'A" Bench in the case of Vipul Y. Mehta (supra), we are of the view that it is neither excessive nor unreasonable.

Income tax - Sec 40A(2)(b) - Whether when Assessee imports raw materials from non-resident promoter, it can be presumed that assessee pays an exclusive price, and hence, disallowance is warranted - NO, rules Delhi HC

NEW DELHI, MAY 25, 2011: The issues before the High Court are - Whether when Assessee imports raw materials from its non-resident promoter, it can be presumed that the Assessee pays exclusive price for the same; whether AO is right in doubting the ALP and making 2% disallowance without any evidence on record; Whether when Customs assessment order is produced to establish the ALP of imported goods, it can be said that the assessee has discharged its liability in this connection and whether onus to disprove it is cast on the AO in such a situation. And the verdict goes against the Revenue

Clause 24 Deemed to be Profit & Gains

Section 32AC allows deduction @ 15% in respect of Investment in new Plant & Machinery to a company who is engaged in the business of manufacture or production of any article or thing and who acquires and installs new asset after the 31st day of March,2013 but before the 1st day of April,2015 and the aggregate actual cost of such new assets exceeds one hundred crore rupees.

The Finance Act, 2014 has amended section 32AC w. e. f. financial year 2014-15. The investment limit in the plant and machinery has been reduced to Rs. 25 crores from Rs. 100 crores.

The auditor is required to report the deemed income chargeable as profits and gains of business under the circumstances specified in sub sections (2) of section 32AC. Only because section 32AC(2) provides for chargeability of deemed income under the head "profit and gains from business or profession" in addition to taxability of capital gains, the auditor is not required to report any capital gains/losses arising on transfer on the said asset.

The tax auditor will be required to verify the compliance to the conditions of the provisions of section 32AC and report the claim of deduction accordingly.

Section 33AB allows deduction in respect of Tea Development Account, Coffee Development Account and Rubber Development Account.

The auditor is required to report the deemed income chargeable as profits and gains of business under the circumstances specified in sub sections [4], [5], [7] and [8] of section 33AB.

Section 33ABA allows deduction in respect of Site Restoration Fund. The auditor is required to report the deemed income chargeable as profits and gains of business under the circumstances specified in sub sections [5], [7] and [8] of section 33ABA. Where deduction has been claimed with respect to interest credited in Special Account or the Site Restoration Account, utilization of withdrawal thereof for purposes other than those specified shall be deemed to be income from business.

Likewise, section 33AC allows deduction in respect of reserve created out of the profit of the assessee engaged in shipping business to be utilized in accordance with the provision of sub section (2) of section 33AC. The tax auditor is required to report the deemed income chargeable as profits and gains of business under the circumstances specified in sub-sections (3) and (4) of section 33AC for the amount of reserves created on or before 31st March, 2004.

However, consequent to the amendment made by the Finance (No.2) Act, 2004, no deduction shall be allowed under section 33AC for any assessment year commencing on or after 1st day of April, 2005.

Clause 25 Profit chargeable to tax under section 41

Section 41(1) provides that where any allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee and subsequently during any previous year the assessee obtains any amount, whether in cash or in any other manner whatsoever, in respect of such loss or expenditure or some benefits in respect of trading liability by way of remission or cessation thereof, the amount obtained by him or the value of benefit accruing to him is chargeable to tax as business income.

Where the assessee who has suffered loss or has incurred expenditure for which deduction has been allowed or by whom the trading liability has been incurred is succeeded in his business either because of amalgamation of companies or demerger or on account of the constitution of new firm or the business if continued by some other person when the assessee ceases to carry on the business, then the successor in the business will be chargeable to tax on any amount received in respect of such loss, expenditure or trading liability.

Explanation (1) to section 41(1) provides that the expression "loss or expenditure or some benefit in respect of any such trading liability by way of remission or cession thereof" shall include the remission or cession of any liability by a unilateral act of the assessee or successor in the business by way of writing off such liability in his accounts.

Liability of assessee does not cease merely because liability has become barred by limitation. Liability ceases when it has become barred by limitation and the assessee has unequivocally expressed its intention not to honour the liability, when demanded. This is a question of fact whether or not assessee has expressed unequivocally his intentions {CIT Vs Chase Bright. Steel Ltd 177 ITR 128 (BOM)}. When a liability is shown outstanding for more than 4 years, in case of an assessee company, this amounted to acknowledging the debt in favour of creditors for the purposes of section 18 of the Limitation Act, 1963.

The Assessee's liability to the creditors thus subsisted and did not cease nor was it remitted by the creditors. The liability was enforceable in the court of Law .The amount was not assessable under section 41(1).This was so held by Delhi High Court in the case of CIT V/s Shri Vardhman Overseas Ltd(2012) 343 ITR 408(Del). [SLP has been dismissed by the Supreme Court against this decision.]

Section 41(2) provides for chargeability to income-tax as income of the business of the previous year in which the moneys payable for the building, machinery, plant or furniture of an undertaking engaged in generation or generation and distribution of power is sold, discarded, demolished or destroyed. Such undertakings are allowed depreciation on such percentage on the actual cost as are prescribed. The depreciation rate are prescribed vide Rule 5(IA) in Appendix IA. Depreciation is to be calculated on Straight Line Method (SLM) on individual asset and not on block of assets, under clause (i) of sub-section (1) of section 32.

Where the moneys payable in respect of such building, machinery, plant or furniture, as the case may be, together with the amount of crap value, if any, exceeds the written down value, so much of the excess as does not exceed the difference between the actual cost and the written down value shall be chargeable to income-tax as income of the business of the previous year in which the moneys payable for the building, machinery, plant or furniture become due.
Where the moneys payable in respect of the building, machinery, plant or furniture become due in a previous year in which the business, for the purpose of which the building, machinery, plant or furniture was being used, is no longer in existence, the above provision shall apply as if the business is in existence in that previous year. To ascertain capital gain, if any, provisions of section 50A are relevant.

Section 41(3) provides that where any capital asset used in scientific research is sold without having been used for other purposes and the sale proceeds together with the amount of deduction allowed under section 35 exceeds the amount of capital expenditure, such surplus or the amount of deduction allowed, whichever is less, is chargeable to tax as business income in the year in which the sale took place. This is irrespective of whether the business of the assessee is in existence or not during the previous year in which the capital asset is sold.

It may be noted that section 41(3) is applicable only if an asset is sold without having been used for other purposes. In other words, if an asset which is initially purchased for the purpose of scientific research is utilised for business purposes on completion of scientific research and later on is sold or transferred, then section 41(3) is not applicable but in such case section 50 would apply.

Section 41(4) provides where any bad debt has been allowed as deduction under section 36(1) (vii) and the amount subsequently recovered on such debt is greater than the difference between the debt and the deduction so allowed, the excess realisation is chargeable to tax as business income of the year in which debt is recovered. For this purpose, it is immaterial whether the business of the assessee is in existence or not during the previous year in which recovery is made.

Section 41(4A) provides that if any amount is withdrawn from the special reserve created under section 36(1)(viii), then it will be chargeable to tax in the year in which the amount is withdrawn, regardless of the fact whether the business is in existence in that year or not.

Section 41(5) provides that where the business or profession referred to in section 41 is no longer in existence and there is income chargeable to tax under sub-section (1), sub-section (3), sub-section (4) or sub-section (4A) in respect of that business or profession, any loss, not being a loss sustained in speculation business which arose in that business or profession during the previous year in which it ceased to exist and which could not be set-off against any other income of that previous year shall, so far as may be, be set off against the income chargeable to tax under the sub-sections aforesaid. This is irrespective of the number of years that may have elapsed from the year in which the loss has been suffered.

The tax auditor should obtain a list containing all the amounts chargeable under section 41 with the accompanying evidence, correspondence, etc. He should in all relevant cases examine the past records to satisfy himself about the correctness of the information provided by the assessee. The tax auditor has to state the profit chargeable to tax under this section. This information has to be given irrespective of the fact whether the relevant amount has been credited to the profit and loss account or not. The computation of the profit chargeable under this clause is also to be stated.

Clause 26 (A)/(B): Disallowances u/s 43B (a) to (f)

- Disallowances for the following:
  - Any tax, duty, cess, fee, etc.;
  - Employers' contribution to Provident Fund or other funds;
  - Bonus of commission payable to employees;
  - Interest on loan from financial institutions or scheduled banks;
  - Leave encashment

The following sum are allowed in the year in which they are incurred, only if they are paid before the due date of furnishing the return of income under section 139(1) of that year.

1. Any sum payable by the Assessee by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force. (See Note 1)
2. any sum payable by the Assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees
3. any bonus or commission to employees
4. any sum payable by the Assessee as interest on any loan or borrowing from any public financial institution or a State financial corporation or a State industrial investment corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing (See Note 2)
5. any sum payable by the Assessee as interest on any loan or advances from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan or advances (See Note 2)
6. any sum payable by the Assessee as an employer in lieu of any leave at the credit of his employee (Leave Encashment)

It they are paid after due date of furnishing return of that year, then such expenditure is allowed in the year in which it is actually paid.

Note 1 – "Any sum payable" means a sum for which the Assessee incurred liability in the previous year even though such sum might not have been payable within that year under the relevant law. For e. g. Vat for the month of March is payable by 14th April. Since this liability is incurred in month of March only, this amount is covered under this section and will be disallowed if not paid till the due date of furnishing return.

Note 2 – In case of (d) & (e), if interest is not actually paid and converted into loan or advance, then it is not treated as actually paid and therefore not allowed as deduction in the year to which it relates. Such interest is allowed in the year in which such converted loan is actually paid. [Circular no. 7/2006] If sales tax payment is deferred under a scheme framed by the government, then it is considered that the amount of sales tax has been paid and therefore allowed in the year in which incurred.

The Supreme Court in the case CIT v. McDowell & Co. Ltd. [2009] 180 Taxman 514 (SC), has held, on the facts and circumstances of the case, that furnishing of bank guarantee cannot be equated with actual payment.

Furnishing of bank-guarantee does not amount to actual payment of a liability as envisaged under the Act. Also Rajasthan HC in CIT vs. Udaipur Distillery Co. Ltd. (2004) 180 Taxation 581 has held that payment by bank guarantee cannot be equated with actual payment.
However, the guarantee commission itself paid to the bank is a revenue & deductible expenditure [CIT vs. Sivakami Mills Ltd. (1997) 227 ITR 465 (SC).

Observation of Rajasthan High Court while delivering judgment in the case *Rajasthan Rajya Sahakari Spinning & Ginning Mills Federation Ltd. v. ITAT & Anr. (2003) 172 Taxation 92 (Raj) at page 99*

"It is true that while interpreting the provisions of the Act, meaning should not be given to the word which results in absurdity, hardship or injustice, but at the same time to infer the intention of the legislature, the plain language of the provision should not be ignored which born out from the plain language used in the provision".

M/s U.P. Co-operative Processing & Cold Storage Federation Ltd Vs A.C.I.T. (ITAT Lucknow), ITA No.280/LKW/2013,Assessment year: 2008-09, Date of decision – 16th June 2015

Brief Facts and Question of Law:
This is assessee's appeal directed against the order passed by learned CIT (A)-I, Lucknow dated 06/02/2013 for the assessment year 2008-09. learned CIT(A)-I, Lucknow has not given weightage to this fact and legal status that provision of audit fee does not come under the ambit of 43B of the I.T. Act 1961.

HELD BY ITAT, LUCKNOW There is clear finding of CIT(A) that since the Assessee is following mercantile system of accounting, the expenses of earlier year cannot be allowed in the present year because the Assessee had not been able to furnish any evidence to show that the above expenses have crystallized in the present year. Before us also, no such evidence has been brought on record by the Assessee that the expenses have crystallized during the present year. We, therefore, do not find any reason to interfere in the order of CIT (A). Accordingly, this ground is rejected.

Repayment of interest on loan by conversion does not amount to actual payment u/s 43B

CIT, Delhi vs. M. M. Aqua Technologies Ltd (Delhi High Court), Appeal No. ITA 110/2005, Date of Order: 18.05.2015 Issue is: - "Whether the funding of the interest amount by way of a term loan amounts to actual payment as contemplated by Section 43B of the Income-tax Act, 1961?" Fact of the case: - 1. Assessee was heavily indebted to its institutional creditors and ICICI was the lead manager of those creditors. 2. The accumulated interest on the overdue principal had mounted to Rs. 3,00,14,900 and The Assessee was unable to discharge this interest liability due to its financial hardship. 3. the ICICI, by a letter waived a part of the compound interest together with the commitment charges and agreed to accept 3,00,149 convertible debentures of Rs 100 each, amounting to Rs. 3,00,14,900 in lieu of the outstanding interest.

AS per ***section 2 (24) (x) of the Income Tax Act, 1961 any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, 1948 (34 of 1948), or any other fund for the welfare of such employees, is treated as Income in his hands.***

According to ***section 36 (1) (va), any sum received by the assessee from any of his employees to which the provisions of sub-clause (x) of clause (24) of section 2 apply, if such sum is credited by the assessee to the employee's account in the relevant fund or funds on or before the due date*****:**

Explanation: For the purposes of this clause, "due date" means the date by which the assessee is required as an employer to credit an employee's contribution to the employee's account in the relevant fund under any Act, rule, order or notification issued thereunder or under any standing order, award, contract of service or otherwise.

- Liability pre-existing as on 1st day of PY and not allowed in any preceding Year Paid / Unpaid during the PY
- Liability incurred in PY Paid / Unpaid before due date of filing return u/s 139(1)
- To also state whether Sales Tax, Excise, etc. passed through PL

Some typical reporting issues:

- Borrowings from NBFCs not covered
- Treatment of funded interest (to refer circular7/2006)
- Sales Tax Deferral Loans
- Provision for Excise Duty on closing stock of finished goods.
- Payments made after signing of Form3CD, but before filing of return–to attach proof or separate certificate
- Assumptions for making provision for taxation.
- List of items disallowed to be cross tallied with Deferred Tax calculations (which would qualify for DTA)
- If certain items disallowed in earlier year and now written back in books (since no longer payable), not to include the same for tax computation.

Clause 27(a), (b): Treatment of CENVAT, Income/Exp. Of Prior period

- 27(a)–Reporting of CENVAT credits availed, treatment in PL and outstanding Balance.
- Ensure proper reconciliation of data as derived from excise and service tax records.
- Consider various circulars in regard to Excise/Service Tax for availment and utilization of CENVAT credit.
- Obtain details on SCN or other correspondence with the Excise/Service Tax department.
- In some industries (say. Textiles) claiming CENVAT credit is optional–in such cases consider whether o/s balance can be utilized in future.
- 27(b)–Reporting of income or expenditure of prior period included in PL.
- Definition of 'Prior Period Items' errors or omissions that arise due to errors or omissions in earlier periods.
- As per AS 5[and AS (IT) 2], revision of estimates does not result in a Prior Period Item.
- Materiality to be considered while reporting the same.
- Reporting not relevant in case 'Cash Basis' is being followed.

Clause 28 Provisions of 56(2) (viia)

Whether during the previous year the assessee has received any property, being share of a company not being a company in which the public are substantially interested, without consideration or for inadequate consideration as referred to in section 56(2) (viia), if yes, please furnish the details of the same:

Provision Contained in Sec-56(2)(Vii)-

Where an individual or HUF receives in any previous year, from any person or persons-

(a) Any sum of money, without consideration, the aggregate value of which exceeds Rs. 50,000/-, the whole of the aggregate value is taxable,

(b) Any immovable **property,-**

I. Without consideration, the stamp duty value of which exceeds Rs. 50,000/-, the stamp duty value of such property is taxable,

II. Received for a consideration which is less than the stamp duty value of the property and difference is more than Rs.50,000/- then such difference is taxable

(c) Any property other than immovable **property,-**

I. Without consideration, the aggregate fair market value of which exceeds Rs. 50,000/-, the whole of the aggregate fair market value is taxable,

II. Received for a consideration which is less than the aggregate fair market value of the property and difference is more than Rs.50,000/- then such difference is taxable

Analysis of Section- 56(2) (Vii) Read with section of Capital Gain Section 50C, Sec-47.

I. Any transfer of capital assets under gift, will or an irrevocable trust is not taxable under head Capital Gain. It is not regarded as transfer U/s 47.

II. Any distribution of capital assets on the partial or total partition of a Hindu Undivided Family is not taxable under head Capital Gain. Because it is not regarded as transfer U/s 47.

III. As per Sec-50C, where the consideration received or accruing as a result of the transfer by an assessee of a capital asset, being land or building or both, is less than the value adopted or assessed or assessable by any authority of State Government for the purpose of payment of stamp duty, such value deemed as full consideration.

Clause 29 of Form 3CD

Whether during the previous year the Assessee received any consideration for issue of shares which exceeds the fair market value of the shares as referred to in section 56(2) (viib), if yes, please furnish the details of the same. If yes, the auditor is required to furnish the details of the same.

This Clause applies to Companies in which Public are not substantially interested

Section 56(2)(viib) provides that where a company, not being a company in which the public are substantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares shall be chargeable to income-tax under the head "Income from other sources".

The provisions of this clause are not applicable where the consideration is received -

(a) By a venture capital undertaking from a venture capital company or a venture capital fund.
(b) By a company from a class or classes of persons as may be notified by the Central Government in this behalf.

As per the explanation to section 56(2)(viib), the fair market value shall be the value as may be determined in accordance with such method as prescribed under Rule 11UA or as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of issue of shares, of its assets, including intangible assets being goodwill, know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of similar nature, whichever is higher.

Since section 56(2) (viib) is applicable to companies in which public is not substantially interested, reporting under this clause is to be done only for corporate assessees.

The auditor should obtain from the auditee, a list containing the details of shares issued, if any, by him to any person being a resident and verify the same from the books of accounts and other relevant documents. Attention is invited to the provisions of section 2(18) which defines the company in which public are substantially interested.

For reporting under this clause with respect to quoted shares, the auditor has to consider the provisions of Rule 11UA (1)(c)(a) which provides for manner of determining:

a. Fair market value of quoted shares and securities received by way of transaction carried out through any recognized stock exchange.
b. Fair market value of quoted shares and securities received by way of transaction carried out OTHER THAN through any recognized stock exchange.

For reporting under this clause with respect to unquoted equity shares, the auditor has to consider the provisions of Rule 11UA (2) which provides for manner of determining the fair market value of unquoted equity shares.

Where for determining the fair market value of unquoted equity shares, a valuation report has been obtained by the Assessee from a Merchant banker or an accountant, the auditor should obtain a copy of the same. Here, attention is invited to the **Standard on Auditing-620 "Using the work of an Auditor's expert"**.

Clause 30: Amount Borrowed on Hundi

Details of the amount borrowed on Hundi (including interest on such amount borrowed) and details of repayment otherwise than by an account payee cheque, are required to be indicated under this clause. In this context, a reference may also be made to Circular No.208 dated 15th November, 1976 and Circular No. 221 dated 6th June,1977 issued by Board explaining the provisions of section 69D - vide ***Appendix XIV (Page no. 275).***

For this purpose, the tax auditor should obtain a complete list of borrowings and repayments of Hundi loans otherwise than by account payee cheques and verify the same with the books of account.

There will be practical difficulties in verifying the loan taken or repaid on Hundi by account payee cheque. In such cases, the tax auditor should verify the borrowing/repayments with reference to such evidence which may be available and in the absence of conclusive or satisfactory evidence or the auditor may obtain suitable certificate/ management representation in this regard.

Clause 31(a), 31(b), 31(c): Loans or Deposits accepted/repaid

Loans/deposits exceeding limits u/s269SS/269T:

- To give Name, Address, PAN, amount accepted, whether squared up during the year, maximum amount, whether taken otherwise than by A/c Payee cheque/draft.
- If total amount of loan/deposit exceeds Rs. 20,000, to reporteven if each transaction is less than Rs. 20,000.
- Though, applies only to amounts accepted/repaid during the year, preferable to disclose movement of even existing loans.

- If accounts are utilized as current accounts, to segregate loan and other transactions.
- Security Deposits, loans from NBFCs also to be reported.
- If data voluminous (say company accepting FDs), to test check and mention the fact.
- Repayments by book/transfer entries to be reported.
- Whether repayments by cheque on behalf of deposit or to be reported? (e. g. direct payments for PPF, tax, LIP, etc.)
- Share Application money advance supported by appropriate documentation not to be reported.
- Disclaimer Note normally given if evidence of paid cheques, etc. not available.
- NA for loans from banks, government companies.

31(c)–whether the accepting or repayment of loan / deposits was made by A/c payee cheque/draft based on examination of books of account and other relevant factors

The tax auditor has to take into account the technological advancements in the field of banking and information technology where loans have been repaid other than through an account payee cheque of bank draft which are capable of being tracked such as bank transactions made electronically through the internet or through mail transfer or telegraphic transfer.

These types of payments, though not made by account payee cheques in the conventional manner, are capable of being tracked. In order to judicially apply the provisions of section 269T, the tax auditor need not report such cases under this clause.

The Finance (No.2) Act, 2014 has acknowledged the fact and allowed the "use of electronic clearing system through a bank account" as a permissible mode for the purposes of section 269T.

Notification no. 208/2007 dated June 27, 2007

The entries that relate to transactions with a supplier and customer on account of purchase or sale of goods /services will not be treated as loans or deposits repaid.

Practically, it may not possible to verify each payment, reflected in the bank statement, as to whether the payment/ acceptance of deposits or loans has been made through account payee cheque, demand draft, pay order or not, it is thus desirable that the tax auditor should obtain suitable certificate from the Assessee to the effect that the payments/ receipts referred to in section 269SS and 269T were made by account payee cheque drawn on a bank or account payee bank draft as the case may be.

Where the reporting has been done on the basis of the certificate of the Assessee, the same shall be reported as an observation in clause (3) of Form No. 3CA and clause (5) of Form No.3CB, as the case may be.

Clause 32 Brought forward Losses & Depreciation

32(a) whether a change in shareholding of the company has taken place in the previous year due to which the losses incurred prior to the previous year cannot be allowed to be carried forward in terms of section 79.

32(b) whether the Assessee has incurred any speculation loss referred to in section 73 during the previous year, if yes, please furnish the details of the same.

32(c) whether the Assessee has incurred any loss referred to in section 73A in respect of any specified business during the previous year, if yes, please furnish details of the same.

32(d) In case of a company please state that whether the company is deemed to be carrying on a speculation business as referred in explanation to section 73, if yes, please furnish the details of speculation loss if any incurred during the previous year. –

32(e) Section-wise details of deductions, if any, admissible under Chapter VIA or Chapter III (Section 10A, Section 10AA).

Additional Reporting of Losses in speculation business (Section 73) and of carry forward and set-off of losses by specified business (Section 73(A) – Auditor has to furnish the following details.

(1) Details of speculation loss referred to in section 73 during the previous year.

(2) Details of loss referred to in section 73A in respect of any specified business.

(3) Auditor has to state whether the company is deemed to be carrying on a speculation business as referred in explanation to section 73 and details of speculation loss from such business. (Clause 32(c), 32(d) and 32(e)

Clause 33 Applicability of the TDS provisions only Yes or No

Clause 34 of Form 3CD

Clause 34(a)

Whether the Assessee is required to deduct or collect tax as per the provisions of Chapter XVII-B or Chapter XVII-BB. If Yes, please furnish: -

I. **TAN**
II. **Sec.**
III. **Nature of Payment**
IV. **Total amount of Payment or Receipt of the nature specified in Col. 3**
V. **Total amount on which tax was required to be deducted or collected out of (4)**
VI. **Total amount on which tax was deducted or collected at specified rate out of (5)**
VII. **Amount of tax deducted or collected Out of (6)**
VIII. **Total amount on which tax was deducted or collected at less than specified rate out of (7)**
IX. **Amount of tax deducted or collected on (8)**
X. **Amount of tax deducted or collected not deposited to the credit of the Central Government out of (6) and (8).**

Clause 34(b)

Whether the Assessee has furnished the statement of tax deducted and collected within the prescribed time. If not, Please Furnish the details: -

I. **TAN**
II. **Type of Form**
III. **Due Date of Furnishing**
IV. **Date of Furnishing, if furnished**
V. **Whether the statement of Tax deducted or collected contains information about all transactions which are required to be reported.**

Clause 34(c)

Whether Assessee liable to pay interest u/s 201(1A) 206C (7) ? If yes, the details thereof are to be furnished in the following format:

I. **TAN**
II. **Amount of Interest Payable**
III. **Amount Paid of (II)**
IV. **Date of Payment**

Clause 35: Quantitative Details

- Information to be given as per books of accounts.
- Details about trading as well as manufacturing activities for all principal items.
- Materiality can be kept in mind–

  Items constituting more than 10% of aggregate value of purchases/consumption/turnover (as per Revised Schedule VI).
- To reconcile with stock details given to banks.
- Reporting of Yield, Shortage/Excess–to compare the same with earlier years or with industry norms.

Clause 36: Dividend Distribution

In the case of a domestic company, details of tax on distributed profits under section 115-O in the following form: -

a. **Total amount of distributed profits**
b. **Amount of reduction as referred to in section 115-o(1A)(i)**
c. **Amount of reduction as referred to in section 115-o(1A)(ii)**
d. **Total taxes paid thereon**
e. **Dates of payment with amount**

Clause 37 Cost Audit

Whether any cost audit was carried out, if yes, give the details, if any, of disqualification or disagreement on any matter /item /quantity as may be reported / identified by the auditor.

The requirement of attachment of copy of cost audit report along with Form has been substituted with reporting of qualifications in cost audit report (clause 37).

The tax auditor should ascertain from the management whether cost audit was carried out and if yes, a copy of the same should be obtained from the Assessee.

Even though the tax auditor is not required to make any detailed study of such report, he has to take note of the details of disqualification or disagreement on any matter/ item/ value/ quantity as may be reported /identified by the cost auditor.

The tax auditor need not express any opinion in a case where such audit has been ordered but the same has not been carried.

In cases where cost audit which might have been ordered is not completed by the time the tax auditor issues his report, he has to report appropriately in this report stating that since cost audit is not completed and the cost audit report is not available with the Assessee.

The tax auditor should examine the time period for which the cost audit if any has been required to be carried out.

Information is required to be given only in respect of such cost audit report the time period of which falls within the relevant previous year.

In effect the information is required to be given in respect of that cost audit report which is received up to the date of tax audit report.

Clause 38 Excise Audit

Whether any audit was conducted under the Central Excise Act, 1944, if yes, give the details, if any, of disqualification or disagreement on any matter/item/quantity as may be reported /identified by the auditor.

The tax auditor should ascertain from the management whether any audit was conducted under the Central Excise Act, 1944 and if such audit was carried out, obtain a copy of the report.

Even though the tax auditor is not required to make any detailed study of such report, he has to take note of the details if any, of disqualification or disagreement on any matter/ item/ value/ quantity as may be reported /identified by the auditor.

The tax auditor need not express any opinion in a case where such audit has been ordered but the same has not been carried out.

In cases where excise audit which might have been ordered is not completed by the time the tax auditor gives his report, he has to report appropriately in this report stating that since excise audit is not completed and the excise audit report is not available with the Assessee.

The tax auditor should examine the time period for which the excise audit, if any, has been required to be carried out. Information is required to be given only in respect of such excise audit report the time period of which falls within the relevant previous year.

In effect the information is required to be given in respect of that excise audit report which is received up to the date of tax audit report.

Clause 39 Service Tax Audit

Whether any audit was conducted under section 72A of the Finance Act, 1994 in relation to valuation of taxable services, if yes, give the details, if any, of disqualification or disagreement on any matter/item/quantity as may be reported /identified by the auditor.

Audit under Service tax to be reported - Report on Audit conducted under section 72A.

Auditor has to report whether any audit was conducted under section 72A of the Finance Act and has to give details, if any, of disqualification or disagreement on any matter/item/value/quantity as may be reported/identified by the auditor. (Clause 39).

Clause 40 Ratio Analysis

Details regarding turnover, gross profit, etc., for the previous year and preceding previous year:

Serial No.	Particulars	Previous Year	Preceding Previous Year
1	Total turnover of the Assessee		
2	Gross profit/turnover		
3	Net profit/turnover		
4	Stock-in-trade/turnover		
5	Material consumed/finished goods produced		

(The details required to be furnished for principal items of goods traded or manufactured or services rendered)

Ratio Analysis of Two years

Up to last year Auditor was required to disclose Ratio of current year only but now auditor needs to disclose ratio of preceding financial year also.

In addition to this auditor, has also to report the total turnover for the previous year as well as for preceding financial year. (Clause 40)

Clause 41 Demand or Refund

Please furnish the details of demand raised or refund issued during the previous year under any tax laws other than Income Tax Act, 1961 and Wealth Tax Act, 1957 along with details of relevant proceedings.

Details of Demand and Refund under other laws

Auditor has to furnish the details of demand raised or refund issued during the previous year under any tax laws other than Income Tax Act, 1961 and Wealth Tax Act, 1957 along with details of relevant proceedings. (Clause 41) Example: Vat, Service tax, Excise, Customs, Municipal tax, Octroi, R M C, etc.,

The auditee may be assessed under various tax laws other than Income-tax Act, 1961 and Wealth-tax Act, 1956 resulting into a demand order or a refund order. The tax auditor should obtain a copy of all the demand/ refund orders issued by the governmental authorities during the previous year under any tax laws other than Income Tax Act and Wealth Tax Act.

Normally, the Indirect tax laws such as Central Excise Duty, Service Tax, Customs Duty, Value Added Tax, CST, Professional Tax etc.would be covered as other tax laws. Hence, the cess or duty like Marketing Cess, Cess on Royalty, Octroi Duty, Entry Tax etc. would not be covered as other tax laws.

However, the auditor should exercise his professional judgment in determining the applicability to relevant tax laws for reporting under this clause.

It may be noted that even though the demand/refund order is issued during the previous year, it may pertain to a period other than the relevant previous year.

In such cases also, reporting has to be done under this clause. The tax auditor should verify the books of account and the orders passed by the respective Department for ascertaining whether any such demand has been raised or refund order has been issued under any other tax law and accordingly report the same.

If there is any adjustment of refund against any demand, the auditor shall also report the same under this clause.

Documentation

- **Documentation for 3CD should be separate.**
- **Check list for 3CD.**
- **For debatable issues, separate management representations, if required.**
- **Important for Peer Review since Tax Audit is also an attest function.**
- **To follow SA 230-Golden principle for Documentation:**

WRITE what you DO and DO what you WRITE.

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