

Issues in clauses of Tax Audit

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Applicability of Tax Audit: Sec. 44AB

Applicable:

- **Business:** Gross Turnover, Receipts Or Total Sales > **Rs.1 Crore**
- **Profession:** Gross Receipts > **Rs.50 Lakhs**
- Where profits & gains from business are taxable on presumptive basis u/s. **44ADA, 44AE, 44BB or 44BBB** & such person claims his income to be lower than profits & gains so estimated.
- Assessee covered u/s 44AD(4) and income exceeds basic Exemption limit.

Not Applicable:

- Person is covered u/s 44AD(1) & Turnover, Receipts Or Total Sales < 2cr.

- **Part A:** Clause 1 to clause 8
- **Part B:** Clause 9 to 41
- **Amendments in Part B:**
 - i. Insertion of new clause 13(d),13(e) and 13(f)- Disclosure requirements in ICDS.
 - ii. Insertion of new clause 31- Details of loans/ deposits taken and repaid.

Clause 1: Name of Assessee

- Name of the assessee whose accounts are being audited under section 44AB.
- As mentioned in the PAN.
- Proprietary concern: Name of the Firm and proprietor.
- **Change in the name of the assessee between the last day of the previous year and the date of tax audit report:** Name as on the last date of the previous year and also on the tax audit report date be stated.

Clause 2: Address

- Address should correspond to the address which the assessee is using while making communication with the Income Tax Department for assessment purposes.
- Audit of a branch-Address of the branch should be stated.
- Change in address after the end of the financial year and before the date of tax audit, the fact may be brought on form 3CD.
- In case of a company - Address of the registered office be stated along with the principle place of business, if any.

Clause 3: Permanent Account Number

- State here the PAN of the assessee.
- In case of a new Tax Audit, it is advisable to procure copy of the PAN card of the assessee.
- If PAN is not allotted as on the date of signing of audit report, the fact should be stated and in such case one should seek copy of pan application acknowledgment .

Clause 4: Details of registration no. under Indirect tax Law

In case the assessee is liable to pay indirect tax like excise duty, service tax, sales tax, customs duty, etc, please furnish the registration number or any other identification number allotted for the same.

To Disclose:

- i. List of all indirect tax registrations to be obtained
- ii. If the assessee is liable but is not registered- The auditor will report the same

Clause 5: Status

- The status does not refer to the residential status.
- Status of the person - Defined as per section 2(31)
- If there is any dispute with respect to status - Full facts relating to the same should be mentioned.

Clause 6 : Previous year

- Presently the previous year u/s 3 of The Income Tax Act are uniform and ends on 31st March, the relevant previous year should be mentioned.

Clause 7: Assessment year

- The assessment year relevant to the previous year whose accounts are being audited should be stated.

The relevant clause of section 44AB under which the audit has been conducted.

- Auditor has to report the clause of the section under which the Audit is been conducted, along with the description.

Clause 9 : Names of members/partners in case of AOP/ Firm

(a) Firm/ AOP: Name of partners/members and their profit sharing ratios.

(b) Particulars of any change in the partners/ members or their profit sharing ratio:

- Applicable to partnership firm & associations of persons.
- If a partner of a firm/AOP acts in a representative capacity, the name of beneficial partner/member should be stated along with such fact.
- If the loss sharing ratio is different of PSR, it should also be stated.
- Detail of all changes in partners/members & also there profit sharing ratio during the previous year should be stated.
- There is no need to state the change in remuneration (partner's salary) and interest to partners or members.

Clause 10: Nature of business/profession & changes if any

- (a) Nature of business or profession.
- (b) Particulars of any change in the nature of business/ profession.
 - The principal to find out whether or not the transaction in question is an **Adventure in the nature of trade**
 - **Trade** means a business which a person has learnt or carries on for procuring subsistence or profit, occupation or employment
 - The Income Tax Act defines the term **Business** only inclusively.

Two essential requirements for an activity to be considered as business:

- (i) it must be a continuous course of activity; and
- (ii) it must be carried on with a profit motive

Clause 11: Details of Books of accounts

a. Whether books of accounts are prescribed u/s 44AA?

if yes list of books so prescribed.

b. List of BOA maintained and the address at which they are maintained.

(i) In case of computerized system of accounting , mention BOA generated by such system.

(ii) If the BOA are not kept at one location, furnish the addresses of locations along with the details of BOA maintained at each location

c. List of BOA and nature of relevant documents examined.

- Disclose only those books that are verified for the purpose of expressing true and fair view on financial statements.
- MIS and other reports generated by the computer system should not be included.

Clause 12: Presumptive income and relevant section

“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, 44BBB or any other relevant section).”

- The amount of any presumptive profit which is credited to/included in the P&L A/c. need be stated along with the relevant section.
- Special care to be taken in case of composite accounts for presumptive business and other business.
- Tax Auditor is not expected to verify calculations under presumptive Method, if any, included in the profit.

Clause 13: Method of Accounting

a) Method of accounting employed in the previous year

Mercantile **or** Cash System

b) Whether there has been any change in the method of accounting employed

vis-a-vis the method employed in the immediately preceding previous year.

Clause 13: Method of Accounting

- c) If answer to (b) above is in the affirmative, give details of such changes ,and the effect thereof on the profit or loss.

Sr. No.	Particulars	Increase in Profit	Decrease in Profit

- (d) Whether any adjustment is required to whether any adjustment is required to be made to the profits or loss for complying with the ICDS notified u/s 145(2)

- (e) If, yes, give details of such adjustments

Clause 13: Method of Accounting (contd..)

Particulars	Increase in Profit (Rs.)	Decrease in Profit (Rs.)	Net Effect (Rs.)
ICDS-I Accounting Policies			
ICDS-II valuation of Inventories			
ICDS-III Construction Contracts			
ICDS-IV Revenue Recognition			
ICDS-V Tangible Fixed Assets			
ICDS-VI Changes in Foreign Exchange Rates			
ICDS-VII Government Grants			
ICDS-VIII Securities			
ICDS-IX Borrowing Costs			
ICDS-X Provisions, Contingent Liabilities & Contingent Assets			
Total	-	-	-

Clause 13: Method of Accounting

(f) Disclosure as per ICDS

Sr. No.	Particulars
(i)	ICDS-I Accounting Policies
(ii)	ICDS-II valuation of Inventories
(iii)	ICDS-III Construction Contracts
(iv)	ICDS-IV Revenue Recognition
(v)	ICDS-V Tangible Fixed Assets
(vi)	ICDS-VII Government Grants
(vii)	ICDS-IX Borrowing Costs
(viii)	ICDS-X Provisions, Contingent Liabilities & Contingent Assets

(a) Method of valuation of closing stock employed in the previous year.

(b) Details of deviation, if any, from the method of valuation prescribed under section 145A, and the effect thereof on the profit or loss.

- Here the method employed for valuation of closing stock having regard to the articles or goods dealt in or manufactured by the assessee is to be stated.
- For ascertainment of the same, reference may be made to the annual financial statements (significant accounting policies) or a management representation may be obtained after duly satisfying himself regarding the method of valuation of closing stock.
- To report effect of changes in profit & loss due to tax & duty paid.
- Section 145A v/s AS-2 v/s ICDS-II

Clause 15 : Particulars of capital asset converted into stock in trade

Clause 15

Give the following particulars of Capital Asset converted into Stock in trade –

- Description of Capital Asset [Sub clause (a)]
- Date of Acquisition [Sub clause (b)]
- Cost of Acquisition [Sub clause (c)]
- Amount at which asset is converted into stock in trade. [Sub clause (d)]

Clause 15: Particulars of capital asset converted into stock in trade

For reporting under Clause 15, the following provisions need to be considered:

1) Section 2(14) - Definition of capital asset:

- Capital asset means property of **any kind** held by an assessee whether or not connected with his business or profession but **does not include** ;
 - i. **Stock in trade, raw materials or consumable stores.**
 - ii. Personal effects of movable nature.
 - iii. Rural agricultural land.
 - iv. Gold deposit bonds.

2) Section 2(47) - Definition of transfer:

- Transfer, in relation to capital asset, includes, inter alia, - conversion of capital asset into stock in trade of a business carried on by the assessee

For reporting under Clause 15, the following provisions need to be considered:

3) Section 45 – Capital Gains:

- Under sec 45(2) the capital gains arising from such conversion a capital asset into, or its treatment as stock-in-trade of a business shall be chargeable to income-tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred
- Further, the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of the consideration

Clause 15: Particulars of capital asset converted into stock in trade

Matters to be considered:

- 1) Under sub-clause (c) the cost of acquisition is required to be reported. The cost of acquisition as per books of account is to be mentioned. While verifying the cost of acquisition, principles enunciated in AS 10 should be borne in mind.
- 2) Under sub-clause (d) the amount recorded in the books of account at which asset is converted into stock-in-trade should be stated. The valuation is stock-in-trade is to be examined with reference to AS 2.
- 3) Non-compliance with AS 10 or As 2 is to be suitably reported in main audit report.

Clause 15: Particulars of capital asset converted into stock in trade

Matters to be considered:

- 4) To **verify the basis of arriving the FMV and a suitable disclosure to be made,**
like –

“During the year under consideration, a land admeasuring ___ is converted into stock-in-trade and the fair market value of the same as on date of conversion is based on the valuation report obtained from ____”

In such a case, compliance with SA 500 – Audit Evidence should be ensured.

Clause 16: Amounts not credited to Profit & Loss Account

Amounts not credited to profit and loss account being;

- Items falling within the scope of Section 28. [Sub clause (a)]
- Pro forma credits, drawbacks, refund of customs or excise duties or service tax, sales tax or VAT, where the same are admitted as due by concerned authorities. [Sub clause(b)]
- Escalation claimed during the previous year [Sub clause (c)]
- Any other items of income. [Sub clause (d)]
- Capital Receipt [Sub clause (e)]

Clause 16 : Amounts not credited to Profit & Loss Account

Illustrative list of capital receipts not credited to Profit & Loss Account

- Capital subsidy received in the form of government grants which are in the nature of promoters' contribution.
- Government grants related to specific fixed asset.
- Compensation for surrender of rights.
- Profit/loss on sale of fixed assets/investments to the extent not credited in the profit and loss account.

Clause 16 : Amounts not credited to Profit & Loss Account

Matters to be considered:

- **Sub-clause (a):**

Section 28 shall also include any sum received for not carrying on any activity under an agreement in relation to any business or profession. (w.e.f. 01/04/2017)

- **Sub-clause (b):**

The words 'admitted by the concerned authorities' would mean '**admitted within the relevant previous year**'. However, if the assessee follows cash basis of accounting the admittance of claim without actual receipt will have no significance.

Clause 16 : Amounts not credited to Profit & Loss Account

Matters to be considered:

- **Sub-clause (c): Escalation Claims -**

- i. Where assessee follows cash basis of accounting, whether details of escalation claims accepted without actual receipt is to be reported?
- ii. Whether the following escalation claims constitute claims accepted?
 - Claims merely made by the assessee
 - Claims under negotiations
 - Claims which are sub-judice

(Ref: CIT v. Hindustan Housing & Land Development Trust Ltd.)

Clause 16 : Amounts not credited to Profit & Loss Account

- **Sub-clause (d): Any Other Income -**

- i. Does 'any other income' include even 'income from other sources'?
- ii. In case of incomes exempt for individuals, should the same be disclosed under 'any other income'?

- **Sub-clause (e): Capital Receipt**

- i. Does the phrase 'Capital Receipts, if any' includes capital contribution like gifts, share capital etc?
- ii. Should interest on Fixed Deposits or Other Incomes (like rentals) which are reduced from cost of fixed assets / Capital WIP be mentioned?

Clause 17 : Transfer of Land & Building at a value lesser than Stamp duty value

“Where any land and building or both is transferred during the previous year for a consideration less than the value adopted or assessed or assessable by any authority of a State government referred to in Section 43CA or 50C.”

Details of Property	Consideration received or accrued	Value adopted or assessed/assessable

Clause 17 : Transfer of Land & Building at a value lesser than Stamp duty value

For reporting under Clause 17, the following provisions need to be considered:

- 1) Section 43CA - Special provision for full value of consideration for transfer of assets other than capital assets in certain cases:

It is applicable where an **asset (other than capital asset) being land or building or both** has been transferred and the value of such an asset is **less than** the value adopted for the purpose of payment of stamp duty. The value so adopted shall be deemed to be the full value of consideration and the gain arising therefrom is taxable as **business income**.

Clause 17 : Transfer of Land & Building at a value lesser than Stamp duty value

For reporting under Clause 17, the following provisions need to be considered:

2) Section 50C - Special provision for full value of consideration in certain cases:

It is applicable where a **capital asset being land or building or both** has been transferred and the value of such an asset is **less than** the value adopted for the purpose of payment of stamp duty. The value so adopted shall be deemed to be the full value of consideration and the gain arising therefrom is taxable as **capital gain**.

Clause 17 : Transfer of Land & Building at a value lesser than Stamp duty value

Audit Considerations:

- The auditor should obtain a list of all properties held and transferred during the year. The same should be verified from statement of profit and loss or Balance Sheet.
- Amount of consideration received or accrued should be as disclosed in the books of account.
- The auditor should also obtain a copy of registered sale deed for reporting the value adopted or assessed or assessable.
- Where the property is not registered, the auditor may have to rely on third party experts like lawyer or solicitor representation. In such cases, compliance with SA 620 – Using the Work of an Auditor's Expert needs to be kept in mind.

Clause 17 : Transfer of Land & Building at a value lesser than Stamp duty value

Matters to be considered:

- What should be the manner in which provisions of Section 43CA is to be applied in case of builder adopting Percentage completion method for recognition of revenue?
- Whether the comparison of Stamp duty Value with Actual consideration for revenue recognition based on percentage completion method should be at each stage and for each year as on date of transfer or any other date ?
- Whether leasehold right / development rights / TDR / FSI etc would be covered under this clause?

Relevant issues

1. Determine Rate of depreciation as per Appendix I of Income Tax Rules
2. Obtain a depreciation schedule from the client showing opening block, additions and deletions to fixed assets, depreciation rate applied, amount of depreciation claimed, etc.
3. Verify the opening written down value from the computation enclosed with the previous year's return and the Form 3CD of the previous year. Enquire if there are disputes with respect to classification or rate of depreciation for the assessee raised by the Income tax authorities.
4. In cases where additional depreciation is being claimed, ensure that the conditions specified in the section have been complied with for the assets in respect of which such additional depreciation is being claimed.

Clause 19 : Amounts admissible as deductions from 32AC to 35E

Amounts admissible under sections:

Section	Amount debited to profit and loss Account	Amounts admissible as per the provisions of the income-tax Act, 1961 and also fulfils the conditions, if any specified under the relevant 14 provisions of Income-tax Act, 1961 or Income-tax Rules, 1962 or any other guidelines, circular, etc., issued in this behalf.
32AC		
33AB		
33ABA		
35		
35AC		
35AD		
35CCA		
35CCB		
35CCC		
35CCD		
35D		
35DD		
35DDA		
35E		

Clause 19 : Amounts admissible as deductions from 32AC to 35E

Audit Considerations:

- The Tax Auditor should indicate the amount debited to the Profit & Loss Account and the amount actually admissible in accordance with the said sections.
- The Tax Auditor should ensure eligibility of the expenditure/payment for deduction and compliance of conditions prescribed in the said sections.
- The Amounts not debited to Profit & Loss Account but admissible under any sections mentioned in the clause have to be stated. [Example : Section 33AB and Section 33ABA –Depositing amounts in designated accounts]

Clause 19 : Amounts admissible as deductions from 32AC to 35E

Relevant Issues:

- In case where audit is required under certain sections to claim deduction and separate auditor is appointed for this purpose, is it enough to rely on such auditor's report ?
- How will the auditor rely on the work done by such other auditors / experts for the work done by them? What should be the extent of reliance to be placed?
- What would be the stand of a Tax Auditor in case such report is unavailable?
- Where auditors have changed, can the auditor rely on previous year's computation and audit report with respect to sec 35D, 35DD, 35DDA etc or should scrutinize expenses incurred in earlier years?

Clause 20 : Employee benefits

- a. Sum paid to employee as bonus or commission, where the same was payable as profits or dividend u/s. 36(1)(ii)
- b. Sums received from employees as contributions to any provident fund or superannuation or any fund u/s. 2(24)(x) ; due date for payment & actual date of payment to concerned authorities u/s. 36(1)(va)

Nature of Fund	Sum received from employees	Actual amount paid	Due date for payment	Actual date of payment to concerned authorities

For reporting under Clause 20, the following provisions need to be considered:

- 1) Section 36(1)(ii) – provides for deduction of any sum paid to an employee as **bonus / commission** for services rendered where such sum would not have been otherwise payable to him as profit / dividend.
- 2) If bonus / commission is in the nature of profit / dividend, the same would not be allowable as a deduction and therefore, requires reporting under this clause.

For reporting under Clause 20, the following provisions need to be considered:

- 3) Section 36(1)(va) – permits deduction of any sum received by the assessee from his employees to which provisions of sec 2(24)(x) are applicable, if it is credited to the account of employees **on or before the due date.**
- 4) Section 2(24)(x) includes within the scope of income 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 ESI Act, or any other fund for the welfare of such employees.

Case Laws:

In the case of **CIT vs Gujarat State Road Transport Corp.** , it was held by the Gujarat HC that the delayed remittance of employee's contribution beyond due date prescribed in section 36(1)(va), is **not deductible** while computing business income, even though such remittance is made before due date of filing of return.

In case of **ITO 4(3)(3) vs. LKP Securities** (ITA No. 638/Mum/2012) it was held that due date of payment of employees contribution to welfare funds was due date specified in respective Act governing the same and not due date of filing return.

Contrary View was taken in the following case laws :

Ghatge Patil Transports Ltd [(2014) 368 ITR 0749 (Bom)]

M/s Hindustan Organics Chemicals Ltd. [(2014) 107 DTR 0105 (Bom)]

Audit Considerations:

- The auditor should obtain a list of various contributions recovered from employees. The ledger account of contributions should also be reviewed.
- The documents relating to provident fund and other welfare funds as well as agreements under which employees have to make contributions should be verified.
- The auditor should maintain the details regarding nature of fund, amounts deducted, due date of payment, actual amount paid and actual date of payment in his working papers.

Matters to be considered:

- Is it mandatory to disclose that employers have not deducted/ collected Provident Funds from Employees ?
- In case of Non-Corporate assessee following cash system of accounting , if provident fund contributions are deposited before end of relevant Previous year but remitted within statutory due dates, will the same be allowed as deductions?
- How can a Tax Auditor verify the details of payments of Provident Fund etc. in Tax Audit of sub-contractor particularly when liability is on main employer?
- As mentioned in the previous slide, different views have been taken by various courts as to the meaning of 'due date'. A note specifying the reliance placed on any case law may be added to avoid ambiguity.

Clause 21 : Admissibility of certain deductions

- Expenditure in nature of capital, personal, advertisement expenditure etc. [Sub clause (a)]
- Amounts admissible under 40(a). [Sub clause (b)]
- Amounts debited to Profit & Loss Account being interest, salary, bonus, commission or remuneration inadmissible under 40(b)/40(ba) [Sub clause (c)]
- Disallowance under 40A(3). [Sub clause (d)]
- Provision for gratuity not allowed under 40A(7) . [Sub clause (e)]
- Sums paid by an assessee as an employer not allowed under 40A(9) . [Sub clause (f)]
- Particulars of contingent liability. [Sub clause (g)]
- Amounts of deductions inadmissible in terms of Section 14A [Sub clause (h)].
- Amounts inadmissible under proviso to 36(1)(iii) [Sub clause (i)]

Clause 21 : Admissibility of certain deductions

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

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

Clause 21 : Admissibility of certain deductions

Relevant Issues:

- Capital expenditure is not defined in the Act and no conclusive test or rules can be laid down to determine whether an expenditure is capital / revenue. However, different tests have been applied by courts to decide whether the nature of expenditure is capital or not.
- The Tax Auditor is not an expert to decide the nature of payment (as to whether it is prohibited by law or not) and may not be aware about the intricacies of all the laws of the land. The Tax auditor should distinguish between compensation and penalty.
- Compensation are allowable business expenditure, whereas penalty is not. [Malwa Vanaspati & Chemical Co. v CIT]
- Section 36(1)(iii): While determining the allowability of interest should keep in mind the requirements of Accounting Standard 16 of Indian GAAP : Borrowing costs.

Clause 21 : Admissibility of certain deductions

b) Amounts admissible under 40(a):

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

(A) Details of payment on which tax is not deducted -

(date of payment, amount of payment, nature of payment, name & address of payee)

(B) Details 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) - (date of payment, amount of payment, nature of payment, name & address of payee, amount of tax deducted)

Clause 21 : Admissibility of certain deductions

b) Amounts admissible under 40(a):

(ii) As payment to resident referred to in sub clause (ia)

(A) Details of payment on which tax is not deducted -

(date of payment, amount of payment, nature of payment, name & address of payee)

(B) Details 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 139(1)-

(date of payment, amount of payment, nature of payment, name & address of payee, amount of tax deducted, amount out of tax deducted, deposited, if any)

Clause 21 : Admissibility of certain deductions

b) Amounts admissible under 40(a):

(iii) under sub-clause (ic): sum paid on account of FBT

(iv) under sub-clause (iia): sum paid on account of Wealth tax

(v) under sub-clause (iib): 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 SG undertaking by the SG.

(vi) under sub-clause (iii): amount chargeable under the head “Salaries” payable outside india or to a non-resident
(date of payment, amount of payment, name & address of the payee)

Clause 21 : Admissibility of certain deductions

b) Amounts admissible under 40(a):

(vii) under sub-clause (iv): payment to a provident or any other fund established for the benefit of employees of the assessee, unless the assessee 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"

(viii) under sub-clause (v): any tax actually paid by an employer referred to in clause (10CC) of Section 10.

Clause 21 : Admissibility of certain deductions

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;

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

(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 section 40A (3A);

Clause 21 : Admissibility of certain deductions

- e) provision for payment of gratuity not allowable under section 40A(7);
- f) any sum paid by the assessee as an employer not allowable under section 40A(9);
- g) particulars of any liability of a contingent nature;
- h) amount of deduction inadmissible in terms of section 14A in respect of the expenditure incurred in relation to income which does not form part of the total income;
- i) amount inadmissible under the proviso to section 36(1)(iii)

Clause 21 : Admissibility of certain deductions

- **Payments to non Residents Section 40(a)(ia)**: Can we rely on CA certificate for foreign remittances or should we decide for each and every foreign payment based on underlying documents/agreements ?
- **DCIT vs Chandabhoy & Jassabhoy**, wherein it was held that provisions of section 40(a)(ia) can be invoked only in the event of non-deduction of tax at source but not for lesser deduction
- **Disallowance under section 14A**: While carrying out the examination of the details furnished by the assessee the tax auditor can rely on management representation letter. SA 580 on 'Written representation' may be referred to.
- The Auditor should verify the list of cash payments. In respect of expenditure of more than Rs. 20,000/- and should include list of payments exempted under Rule 6DD.

Clause 22 : Amounts inadmissible under Section 23

Amount of interest inadmissible under Section 23 of Micro, Small & Medium Enterprise Development Act, 2006.

Micro Enterprise

- In case of enterprise engaged in manufacture or production of goods pertaining to any industry specified in SCH 1 (Development and Regulations) Act 1951. Investment in plant and machinery **does not exceed Rs.25 lacs.**
- Incase of service enterprise, investment in equipment **does not exceed Rs.10 lacs.**

Small Enterprise

- In case of enterprise engaged in manufacture or production of goods pertaining to any industry specified in SCH 1 (Development and Regulations) Act 1951. Investment in plant and machinery exceeds Rs. 25 lacs but does not exceed Rs. 5 cr
- In case of service enterprise, investment in equipment exceeds 10 lacs but does not exceed Rs. 2 cr.

Medium Enterprise

- In case of enterprise engaged in manufacture or production of goods pertaining to any industry specified in SCH 1 (Development and Regulations) Act 1951. Investment in plant and machinery exceeds Rs. 5 cr but does not exceed Rs. 10 cr
- In case of service enterprise, investment in equipment exceeds 2 cr but does not exceed Rs. 5 cr.

Clause 22 : Amounts inadmissible under Section 23

- As per **Section 23 of MSME Act** the interest payable or paid by the buyer, under or in accordance with provisions of Section 16 of the Act , shall not for the purpose of computation of income under Income Tax Act, 1961 be allowed as deduction.

Audit Considerations

- Where the auditor is issuing report in Form 3CB, if no disclosure is made by the auditee in financial statements about the information as prescribed u/s 22 of MSME Act, an appropriate qualification in Form 3CB should be given.
- The auditor should obtain full list of suppliers which fall within the definition of 'supplier'. It is the **responsibility of the auditee to classify and identify the suppliers who are covered by this Act**. The list so obtained shall be reviewed by the auditor.
- Verify the interest paid or payable under section 16 of MSME Act from books of account on test check basis and obtain reasonable assurance of compliance.

Matters to be considered

- What would be the disallowance in case the auditor is liable to pay any interest under MSME Act but he has not provided the interest in his accounts?
- In such a case, what would be the situation when he actually pays and claims such interest?
- Where the auditor has relied on the auditee for classifying and identifying the suppliers covered under the MSME Act, 2006 whether a note explaining the reliance placed on auditee is enough to discharge the onus?

Clause 23 : Payments to Related parties

Particulars of payments made to persons specified u/s. 40A(2)(b)

40A(2)(b)	Where the assessee is	Persons referred to in clause (b)
(i)	Individual	any relative of the assessee;
(ii)	Company, firm, AOP, HUF	any director, partner, or member or any relative of such director, partner or member;
(iii)	Carrying on business or profession	any individual who has a substantial interest in the business or profession of the assessee, or any relative of such individual;
(iv)	Carrying on business or profession	a company, firm, AOP or HUF having a substantial interest* in the business or profession of the assessee
		or any director, partner or member of such company, firm, AOP or HUF
		or any relative of such director, partner or member or any other company carrying on business or profession in which the first mentioned company has substantial interest*;
(v)	Carrying on business or profession	a company, firm, AOP or HUF of which a director/ partner / member, has a substantial interest* in the business or profession of the assessee; or any director/ partner / member of such company, firm, AOP or HUF or any relative of such director, partner or member;
(vi)	Any person who carries on a business or profession	All of the above

*Substantial Interest : 20% or more voting power or share of profit of such business or profession.

Matters to be considered

Whether payments made to related parties of capital nature are covered in reporting ?

How can a tax auditor ascertain details regarding persons covered in the said section and how can such transactions be verified ?

Transfer Pricing

Domestic Transfer Pricing

Matters to be disclosed

- Name of the related party
- PAN of the related assessee
- Relation with the assessee
- Nature of Payment
- Amount of payment made

Amounts deemed to be profits and gains u/s 32AC or 33AB or 33ABA or 33AC

- 32AC : Investment in new plant or machinery
- 33AB : Tea development account, coffee development account and rubber development account.
- 33ABA : Site Restoration fund
- 33AC : Reserves for shipping business

(only eligible assessee can claim the benefit under this section)

Any amount of profits chargeable to tax u/s 41 and computation thereof.

To Disclose:

- Name of the party
- Amount involved
- Section under which it is covered
- Details of transactions
- Computation of the same if any

Clause 26 : Disallowance under section 43B

In respect of any sum referred to in clause (a), (b), (c), (d), (e) or (f) of Section 43B, the liability of which :

- A) Pre-existed on the 1st day of the previous year but not allowed in the assessment of any previous year and was
 - a) paid during the previous year
 - b) not paid during the previous year.
- B) was incurred in the previous year and was
 - a) paid on or before the due date for furnishing the return of income of the previous year under section 139(1).
 - b) not paid on or before the aforesaid dates.

(State whether sales tax, customs duty, excise duty or any other indirect tax, levy , cess, impost etc. is passed through profit and loss account)

Section 43B - Certain deductions to be only on actual payment

The following amounts shall be allowed as deduction only in the previous year in which such amounts are actually paid:

- (a) any sum payable by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force, or
- (b) any sum payable 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, or
- (c) any sum referred to in section 36(1)(ii), or
- (d) & (e) any sum payable as interest on any loan or borrowing from any public financial institution or a State financial corporation or a State industrial investment corporation, or a scheduled bank
- (f) any sum payable as an employer in lieu of any leave at the credit of his employee, shall be allowed (irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him) only in computing the income referred to in section 28 of that previous year in which such sum is actually paid by him

Matters to be considered

- Is Profession tax liability required to be reported under section 43B ?
- Where taxes, duties etc. referred to in Section 43B are paid after tax audit is completed but before due date of filing returns, how should the same be dealt with by a Tax Auditor ?

(a) Value of CenVAT credits availed or utilized during the previous year of its treatment in the profit and loss account and treatment of outstanding CenVAT credits in accounts.

(b) Particulars of income or expenditure of prior period credited or debited to profit and loss account. *(In case of cash systems of accounting, there will not be any item appearing under this clause)*

Clause 28 : Purchase of shares of company for inadequate consideration

“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)(viiia), if yes, please furnish the details of the same.”

Section 56(2)(viiia) – provides that *“where a firm or a company in which the public is not substantially interested, receives from any person or persons, any property, being shares of a company not being a company in which the public are substantially interested,—*

- (i) without consideration, the aggregate **FMV of which exceeds Rs.50,000**, the whole of the aggregate FMV of such property;*
- (ii) for a consideration which is less than the aggregate FMV of the property by an amount exceeding Rs.50,000, the **aggregate FMV of such property as exceeds such consideration** shall be chargeable to tax under the head Income from Other Sources.*

Rule 11UA provides the methodology for computation of FMV. *The FMV of the shares has to be computed as per Rule 11UA , irrespective of the market value of the shares transferred.*

Clause 28 : Purchase of shares of company for inadequate consideration

Audit Considerations

- This clause may also attract Standard on Auditing – 620 “Using the work of an Auditor’s expert” in case a valuation report is obtained to determine the FMV of the shares in case of unquoted instruments.
- The Auditor should obtain a list containing the details of shares received and verify the same with the relevant documents and books of accounts. Such shares will be reflected in the books of accounts under “Investments” or “Stock in trade”.
- When the shares are issued for no consideration, then the Tax Auditor can verify the same by share certificates, demat account statements etc. as the same will not be reflected in the books of accounts.

Clause 28 : Purchase of shares of company for inadequate consideration

Audit Considerations:

- The Auditor should obtain a list containing the details of shares issued to any person being a resident and verify the same with the relevant documents and books of accounts.
- The following information should be maintained in the working papers:
 - i. Name and status of person to whom shares have been issued
 - ii. PAN of the person, if available
 - iii. Nature of shares (Quoted in RSE / URSE / unquoted)
 - iv. No. of shares issued
 - v. Consideration received
 - vi. Fair Market Value as per Rule 11UA(1)(c) / 11UA(2)
 - vii. Face value of shares
 - viii. Amount taxable u/s 56(2)(viib)

Clause 29 : Issue of shares at a price higher than the FMV

“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.”

- **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 tax under the head Income from Other Sources.
- Rule 11UA provides the methodology for computation of FMV.

Clause 29 : Issue of shares at a price higher than the FMV

Matters to be considered:

- What would be the consequences if the company has issued shares to residents and non-residents under private placement at a price which is higher than the FMV of the shares ?

Details of any amount borrowed on hundi or any amount due thereon (including interest on the amount borrowed) repaid, otherwise than through an account payee cheque

Section 69D- Amount borrowed or repaid by hundi

Note:

- It should be noted that hundi does not include bills of exchange but bills of exchange include hundi
- Where any amount is borrowed on hundi or repayment thereof (including Interest) is otherwise than through an account payee cheque drawn on a bank, the amount so borrowed or repaid shall be deemed to be the income of the person borrowing or repaying for the previous year in which the amount was borrowed or repaid

Clause 31 (a)

- Particulars of each loan or deposit in an amount exceeding the limit specified in section **269SS** taken or accepted during the previous year:-

What is to be disclosed:

- (i) name, address and PAN (if available with the assessee) of the lender/depositor;
- (ii) amount of loan/ deposit taken
- (iii) whether the loan or deposit was squared up during the previous year;
- (iv) maximum amount outstanding in the account at any time during the previous year;
- (v) whether the loan or deposit was taken or accepted by cheque or bank draft or ECS through a bank account
- (vi) Whether the loan or deposit was accepted by an account payee cheque or an account payee draft.

Clause 31 (b)

- Particulars of each specified sum in an amount exceeding the limit specified in section 269SS taken or accepted during the previous year
 - i. Name ,address and PAN (if available with the assessee assessee) of the person from whom specified sum is received;
 - ii. amount of specified sum taken or accepted;
 - iii. whether the specified sum was taken or accepted by cheque or bank draft or use of electronic clearing system through a bank account;
 - iv. in case the specified sum was taken or accepted by account payee cheque or bank draft

Clause 31 (c)

- Particulars of each payment of loan or specified advance in an amount exceeding the limit specified in **section 269T** made during the previous year.

(i) name, address and PAN (if available) of the lender/ depositor;

(ii) amount of repayment

(iv) maximum amount outstanding in the account at any time during the previous year;

(v) whether the repayment was made by cheque or bank draft or ECS through a bank account;

(vi) In case where repayment was made by bank/draft, whether the same was **accepted** by account payee cheque or account payee bank draft

Note: Particulars to be disclosed will be only if amount exceeds Rs.20,000/-

In case of company deposit repayable on demand will not be considered.

However, in case of others deposit of any nature are to be considered.

Clause 31 (d)

- Particulars of repayment of loan or deposit or Particulars of repayment of loan or deposit or any specified advance in an amount exceeding the limit specified in section **269T** received otherwise than by a cheque or bank draft or use of ECS through a bank account during the previous year

(i) Name, address and PAN of the Payer

(ii) amount of loan or deposit or any specified advance amount of loan or deposit or any specified advance received otherwise than by a cheque or bank draft or use of electronic clearing system through a bank account during the previous year.

Note: Particulars to be disclosed will be only if amount exceeds Rs.20,000/-

In case of company deposit repayable on demand will not be considered.

However, in case of others deposit of any nature are to be considered.

Clause 31 (e)

- Particulars of repayment of loan or deposit or any specified advance in an amount exceeding the limit specified in section **269T** received by a cheque/ bank draft which is not an account payee cheque/darft during the previous year :-

(i) Name, address and PAN of the Payer

(iv) amount of loan or deposit or any specified advance received by a cheque or a bank draft which is not an account payee cheque or account payee bank draft during the previous year.

Note: Particulars to be disclosed will be only if amount exceeds Rs.20,000/-

In case of company deposit repayable on demand will not be considered.

However, in case of others deposit of any nature are to be considered.

- Old acceptance/ repayment through an account payee cheque (note to be given)

“It is not possible for me/us to verify whether loans or deposits have been taken or accepted otherwise than by an account payee cheque or account payee bank draft, as the necessary evidence is not in the possession of the assessee.”

- All loans vis-à-vis loans covered in section 296SS and 269ST

Clause 32 : Details of brought forward loss or depreciation

- Details of brought forward loss or depreciation allowance, in following manner [Sub-Clause (a)]-

Serial No.	Assessment Year	Nature of Loss/ Allowance	Amount as per return	Amount as assessed	Remarks

- Where change in shareholding of company has taken place in P.Y due to which losses incurred in preceding P.Ys cannot be carried forward as per Section 79 [Sub-Clause (b)]
- Whether the assessee has incurred any speculation loss referred to in section 73 during the previous year [Sub-Clause (c)]

Clause 32 : Details of brought forward loss or depreciation

- Whether the assessee has incurred any loss referred to in section 73A in respect of any specified business during the previous year. [Sub-Clause (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. [Sub-Clause (e)]

Clause 32 : Details of brought forward loss or depreciation

For reporting under Clause 32, the following provisions need to be considered:

- Brought forward losses may pertain to different heads of income such as property income, profits and gains in business or profession, speculation business or capital gains, the provisions of which are contained in sections 32 and 70 to 79.
- Section 79 – provides that -
where a change in shareholding has taken place in a previous year in the case of a company, not being a company in which the public are substantially interested, no loss shall be carried forward and set off against the income of the previous year unless—
 - (a) on the last day of the previous year the shares of the company carrying not less than 51% of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less 51% of the voting power on the last day of the year or years in which the loss was incurred

Clause 32 : Details of brought forward loss or depreciation

For reporting under Clause 32, the following provisions need to be considered:

- Section 73 – provides that any loss in respect of speculation business shall not be set off except against profits or gains of another speculation business
- Section 73A – provides that Any loss, computed in respect of any specified business referred to in section 35AD shall not be set off except against profits and gains, if any, of any other specified business.

Clause 32 : Details of brought forward loss or depreciation

Matters to be considered:

- Where assessments are in various stages of litigation, is it correct to merely state ' information is not readily available and hence not furnished'?
- Any assessment, rectification, revision or appeal proceedings pending at the time of tax audit have to be disclosed under remarks column under sub-clause (a). If orders are yet to be passed, the same can be disclosed along with impact thereof, if material.

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

Section under which deduction is claimed	Amounts admissible as per the provision of the Income-tax Act, 1961 and 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.

Relevant Issues

- Can TA rely on certificates issued by professionals other than CAs?
- Where payments qualifying for deduction u/s. 80D etc. might not have been paid out of business income but personal income, should same be disclosed?
- Where in preceding P.Y, admissibility of deductions claimed u/ss. 80-I, 80-IA, etc. are not questioned & allowed from return of income, is TA required to verify allowability of same?

Clause 34

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

TAN	Sec	Nature of Pymt	Total amnt of Pymnt or receipt of the nature specified in Col. 3	Total amnt on which tax was required to be deducted or collected out of (4)	Total amnt on which tax was deducted or collected at specified rate out of (5)	Amnt of tax ded. Or coll. Out of (6)	Total amnt on which tax was deducted or collected at less than specified rate out of (7)	Amnt of tax deducted or collected on (8)	Amnt of tax deducted or collected not deposited to the credit of the Central Govmnt out of (6) and (8)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)

Clause 34 (Contd.)

Whether the assessee has furnished the statement of tax deducted and collected within the prescribed time. **If not**, Please furnish the details :

TAN	Type of Form	Due Date for furnishing	Date of Furnishing, if furnished	Whether the statement of tax deducted or collected contains information about all transactions which are required to be reported
(1)	(2)	(3)	(4)	(5)

Clause 34 (Contd.)

(c) whether the assessee is liable to pay interest under section 201(1A) or section 206C(7). If Yes, please furnish

TAN	Amount of Interest Payable	Amount paid out of Col. (2)	Date of Payment
(1)	(2)	(3)	(4)

- Clause 34(a) : Compliance with TCS Provisions

Reporting on compliance with TCS provisions along with TDS provisions

- Clause 34(b) :filling of TDS and TCS returns

the tax auditor shall report on the compliance by the assessee with provisions of furnishing of TDS or TCS statements within prescribed time.

- Clause 34(c) : Assessee in default

if assessee is deemed as an assessee in default and he is liable to pay interest u/s 201(1A) or 206C(7), the tax auditor shall furnish the TAN of the assessee, interest payable and interest actually paid.

- In case of trading concern, quantitative details of principal goods traded-
 - Opening Stock
 - Purchases during P.Y
 - Sales during P.Y
 - Closing Stock
 - Short / Excess [**Sub-Clause (a)**]
- In case of manufacturing concern, quantitative details of raw materials, finished goods & / or by-products-
 - Opening Stock
 - Purchases during P.Y
 - Consumption / Production during P.Y
 - Closing Stock
 - Short / Excess

- Yield of finished products*
- Percentage of yield* [Sub-Clause (b)]

*Information may be given to the extent available; applies to raw materials only

Relevant Issues

- How much quantitative details be disclosed in case of retail traders where there are variety of items traded?
- Will TA be justified in conducting his audit in proper manner if he accepts MRs regarding quantitative details of items, in case there is no mechanism to record stock?
- How should TA report in case of civil contractor or construction company under this clause?
- Where assessee was not valuing WIP because processing time was minimal, how should TA report this issue under this clause?
- In case where units of raw materials & closing stock are not same, how should yield & shortage / excess of stock be measured?
- Are assessees rendering technical services required to maintain quantitative details of drawing materials like tracing papers, etc?

Clause 36 : Tax on distributed profits u/s 115-O

In the case of 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 tax paid thereon
- (e) Dates of payments with amounts

For reporting under Clause 36, the following provisions need to be considered:

- Section 115-O(1) – provides for levy of tax on dividends paid irrespective of whether dividend is paid out of current profits or accumulated profits in addition to the income-tax chargeable of a domestic company for any assessment year
- Section 115-O(1A) - The amount referred to in sub-section (1) shall be reduced by,—
 - (i) the amount of dividend received by the company from its subsidiary and,—
 - (a) where such subsidiary is a domestic company, the subsidiary has paid the tax which is payable under this section on such dividend; or
 - (b) where such subsidiary is a foreign company, the tax is payable by the domestic company under section 115BBD on such dividend:
 - (ii) the amount of dividend, if any, paid to any person for, or on behalf of, the New Pension System Trust referred to in clause (44) of section 10.

Clause 36 : Tax on distributed profits u/s 115-O

- Details of tax on dividend declared/ paid by domestic company during the Financial Year under audit should be reported.
- The gross amount of dividend is to be reported in sub-clause (a) and the reduced amount is to be reported in sub-clause (b) and (c)
- Auditor should keep working papers but , the tax auditor need not go into the question of how the total amount of distributed profits has been arrived at.
- Information about the date of declaration/distribution of dividend or payment of dividend is required to be given.

Clause 37

- Enclose a copy of Cost Audit Report, if any

Clause 38

- Enclose a copy of Excise Audit Report, if any

Clause 39

- Enclose a copy of Service Tax Audit, if any.

Clause 40: Accounting Ratios

Sr. No.	Particulars	Previous Year F.Y. 2016-17	Preceding previous year F.Y. 2015-16
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		

- Details of demand raised/ refund issued during the previous year under any tax laws other than Income Tax Act, 1961 and Wealth-tax Act, 1957
- Details of relevant proceedings to be furnished

THANK YOU



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