

# GUIDANCE NOTE ON TAX AUDIT UNDER SECTION 44AB OF THE INCOME-TAX ACT, 1961

(Revised 2014 Edition)



**The Institute of Chartered Accountants of India**

*(Set up by an Act of Parliament)*

New Delhi

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## Foreword to the Seventh Edition

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The "Guidance Note on Tax Audit u/s 44AB of the Income Tax Act, 1961" is amongst one of the important guidance issued by ICAI and is referred not only by our Chartered Accountants but also by assessing officers and in various judicial forums. It was brought out in the year 1985 immediately after the introduction of tax audit provisions and has been revised regularly to guide members in discharging their obligations in a timely and effective manner.

Since the publication of the last issue in the year 2013, the formats of tax audit reports have undergone significant changes, thereby expanding the scope of reporting and verification by our chartered accountants. Considering the need of updating the knowledge and enhancing the professional competencies of the members of our fraternity, the Direct Taxes Committee of the Institute of Chartered Accountants of India has come out with the Seventh edition of Guidance Note.

I congratulate, the Direct Taxes Committee, particularly CA. G. Sekar, Chairman and CA. Sanjiv Kumar Chaudhary, Vice-Chairman, for responsibly undertaking this revision and fulfilling this arduous task within limited time frame.

I am confident that this guidance note will be of great significance and will also provide assistance to our members on the critical issues arising out of the amendments.

**Date: 9<sup>th</sup> September, 2014**

**Place: New Delhi**

**CA. K. Raghu**

**President, ICAI**



## Preface to the Seventh Edition

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The year 1984 witnessed an important entrant to the Income tax Act, 1961 i.e. the provisions relating to tax audit. Since the main purpose of introduction of this provision was to ensure the accuracy of books of accounts maintained, which forms the basis of computation of income of the assessee, the onerous responsibility was casted on chartered accountants.

Time and again changes were made in the reporting requirements of tax audit report which not only widened the scope of audit to an incredible scale but has also indicated the trust banked upon the Chartered Accountancy Profession by the Government. The authorities also seek the suggestions of ICAI for changes to be made in the reporting requirements, which are submitted to them from time to time. In fact it was the recommendation of ICAI and persistent follow up thereof, due to which the system of e-filing of tax audit reports became a reality in the year 2013. That was the time when ICAI came out with the sixth issue of this Guidance Note.

Recently in July, 2014 the CBDT amended the formats of tax audit reports, thereby expanding the scope of audit tremendously. Majority of the changes made by the Department find its source either in the Guidance Note or recommendations made by ICAI in past few years. Since significant changes have been made in the format of tax audit reports for which members are to be guided, the Direct Taxes Committee of ICAI decided to revise the Guidance Note. Through this seventh edition of the guidance note, an effort has been made to equip our members so that they are able to effectively discharge their responsibilities with regard to the additional requirements. Although, very limited time was available for revision of the entire Guidance Note, the Direct Taxes Committee left no stone unturned to bring out this guidance at the earliest.

I am extremely thankful to CA. K. Raghu, President and CA. Manoj Fadnis, Vice President of the Institute of Chartered Accountants of India who have been the guiding force behind the revision of the Guidance Note.

Also, I wish to acknowledge the sincere contribution of all the members of the Direct Taxes Committee particularly, the members of the Delhi based study group formed under the convenorship of CA. Sanjiv Chaudhary, Vice Chairman and my following Central Council Colleagues, who spared their valuable time for providing significant inputs based upon which the revised draft of the Guidance Note has been prepared:

*Northern Region*

CA. Sanjay Agarwal

CA. Naveen N.D. Gupta

*Western Region*

CA. Dhinal Shah

CA. Tarun Ghia

I am also appreciative of the contribution made by the following co-opted members and special invitees of the Direct Taxes Committee:

CA. Manish Dafaria, Indore

CA. Ajay Wadhwa, Delhi

CA. Himanshu Goyal, Delhi

CA. Veera Babu CH, Guntur

Last but not the least, I appreciate the dedicated efforts of CA. Mukta Kathuria Verma, Secretary, Direct Taxes Committee, CA. Ravi Gupta, Executive Officer and the entire Secretariat of Direct Taxes Committee for their technical and administrative assistance in bringing out this seventh edition of the Guidance Note in limited available time.

Undoubtedly, this edition also would guide our members as the earlier edition and would be of great assistance to our members.

**Date: 9<sup>th</sup> September, 2014**

**Place: New Delhi**

**CA. G. Sekar**

**Chairman  
Direct taxes Committee**

## Foreword to the First Edition

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The introduction of the provisions regarding compulsory audit of accounts for tax purposes under Section 44AB of the Income Tax Act, 1961, signified a very healthy development in our tax laws. It fulfils a long felt need and seeks to rectify a weakness which was diagnosed long ago. The requirements of the provisions place a tremendous responsibility on the members of our profession in carrying out the audit and in furnishing the audit report setting forth the prescribed particulars.

I have no doubt that our profession would rise to the occasion, acquit itself well in discharging this responsibility and justify the confidence reposed by the Government in our profession.

I would like to compliment the Taxation Committee in bringing out this timely publication. I am sure this guide would be of help to our members and ensure their full contribution to the achievement of the objectives of this provision.

14-2-1985

New Delhi

**A. C. Chakrabortti**

*President*





## Preface to the First Edition

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Section 44AB has been introduced in the Income-tax Act, 1961, by the Finance Act, 1984. This section provides for audit of accounts of assesseees having total sales, turnover or gross receipts exceeding the specified limits of Rs.40 lakhs for business and Rs.10 lakhs for profession. New Rule 6G, inserted in the Income-tax Rules, prescribes the Forms of Audit report for the above purpose. The requirements for the above audit will apply to accounts relating to previous year relevant to assessment year 1985-86 and subsequent years.

Audit of accounts in the corporate sector has been made compulsory by legislation over a period of years. Realising the importance of audit, in recent years, this requirement is being extended to non-corporate sector also.

The Income-tax Act already provides for audit of accounts of Public Charitable Trusts and non-corporate assessee establishing new industrial undertakings. Section 142(2A) gave wide powers to the tax authorities to get the accounts in certain specified circumstances audited by a chartered accountant. The new provision introduced by section 44AB has considerably widened the scope of audit.

The Taxation Committee of the Institute has published (i) Guide for Audit of Public Trusts under section 12A(b) and (ii) Guide to Special Audit under section 142(2A). A monograph on compulsory maintenance of accounts has also been published and the same has been updated.

Considering the fact that the scope of audit under the tax laws has considerably widened after the introduction of section 44AB, the Taxation Committee has prepared this Guidance Note on Tax Audit for the use of our members. In this guidance note an attempt has been made to explain the scope of Tax Audit requirements. It has been emphasised that in any audit assignment the general principles of audit have to be followed. The members accepting these assignments will have to use their professional skill and expertise while expressing their opinion on the financial statements and other particulars required to be stated.

I am happy that with the active co-operation of the members of the Taxation Committee, it has been possible to finalise this Guidance Note soon after the final publication of the audit report forms by CBDT. In particular, I must express my gratitude to Shri P.N. Shah, our past President, Sarvashri N.K.

Poddar, M.G. Patel and A.H. Dalal, members of the Taxation Committee and the Secretary of the Committee for the efforts put in by them in the finalisation of the guidance note. I am confident that this guidance note will be of great assistance to our members in industry or in public practice.

13<sup>th</sup> February, 1985

**G. Narayanaswamy**  
**Chairman**  
*Taxation Committee*

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## Clarification regarding authority attached to the documents Issued by the Institute

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*"Guidance Notes' are primarily designed to provide guidance to members on matters which may arise in the course of their professional work and on which they may desire assistance in resolving issues which may pose difficulty. Guidance Notes are recommendatory in nature. A member should ordinarily follow recommendations in a guidance note relating to an auditing matter except where he is satisfied that in the circumstances of the case, it may not be necessary to do so. Similarly, while discharging his attest function, a member should examine whether the recommendations in a guidance note relating to an accounting matter have been followed or not. If the same have not been followed, the member should consider whether keeping in view the circumstances of the case, a disclosure in his report is necessary".*

*(Volume I.A of the Compendium of Engagement and Quality Control Standards (9<sup>th</sup> Edition, 2012), page 3, Para 5)*





# Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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## 1. Terms, abbreviations used in this Guidance Note.

In this Guidance Note the following terms and abbreviations occur often in the text. A brief explanation of such terms and abbreviations is given below. Further, reference to a section without reference to the relevant Act means that the section has reference to the Income-tax Act, 1961.

- |     |  |  |
|-----|--|--|
| (a) | <b>Act</b>                                 | The Income-tax Act, 1961.  |
| (b) | <b>AS</b>                                  | Accounting Standards prescribed under the Companies Act, 2013 for company assessees and prescribed by the Institute of Chartered Accountants of India for non company assessees. |
| (c) | <b>AS(IT)</b>                              | Accounting Standards notified by the Central Government under section 145(2).  |
| (d) | <b>Assessee</b>                            | As defined in section 2(7) of the Act.   |
| (e) | <b>Audit report</b>                        | Any report submitted in Form No. 3CA/3CB along with the statement of particulars in Form No. 3CD.  |
| (f) | <b>Board</b>                               | The Central Board of Direct Taxes constituted under the Central Boards of Revenue Act, 1963.   |
| (g) | <b>Circular</b>                            | A circular or instructions issued by the Board under section 119(1) of the Act.  |
| (h) | <b>Form or Forms</b>                       | Collectively refer to Forms 3CA, 3CB and 3CD.  |
| (i) | <b>ICAI/Institute</b>                      | The Institute of Chartered Accountants of India.   |
| (j) | <b>Limited Liability Partnership (LLP)</b> | As defined in the Limited Liability Partnership Act, 2008  |

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**


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- (k) **Person** As defined in section 2(31) of the Act.
- (l) **Previous year** As defined in section 3 of the Act.
- (m) **Rules** The Income-tax Rules, 1962.
- (n) **Specified date** "Specified date", in relation to the accounts of the assessee of the previous year relevant to an assessment year, means the due date for furnishing the return of income under sub-section (1) of section 139 of the Act.
- (o) **SA** Standards on Auditing
- (p) **STT** Securities transactions tax leviable under Chapter VII of the Finance (No.2) Act, 2004.
- (q) **Tax audit** The audit carried out under the provisions of section 44AB.
- (r) **Tax auditor** Auditor appointed by an assessee to carry out tax audit.

## 2. Introduction

2.1 The Act provides for audit of accounts and/or report/certificate of a chartered accountant in the following cases in respect of AY 2014-15:

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
1.	Assessees carrying on the business of growing and manufacturing tea/coffee/rubber claiming deduction under section 33AB.	33AB (2)	5AC	3AC
2.	Assessees carrying on business consisting of the prospecting for, or	33ABA (2)	5AD	3AD

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	extraction or production of, petroleum or natural gas or both in India and in relation to which the Central Government has entered into an agreement for the purpose of deposit in Special Account/ Site Restoration Account under section 33ABA.			
3.	Assesseees other than companies or co-operative societies claiming amortisation of certain preliminary expenses under section 35D and assessee being Indian company or a non-corporate resident claiming deduction for expenditure on prospecting etc. for certain minerals under section 35E.	35D (4) and 35E (6)	6AB	3AE
4.	Assesseees carrying on business or profession whose sales, turnover or gross receipts exceed Rs.1 Crore (Rs.25 lakhs in the case of	44AB	6G	3CA/ 3CB/ and 3CD

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	profession) as per the provisions of section 44AB, and assessee who claim their income to be lower than the profits or gains deemed to be the profits and gains of their business under sections 44AD, 44AE, 44BB or 44BBB.			
5.	Assessee being a non-resident (not being a company) or a foreign company receiving income by way of royalty or fees for technical services from Government or India concern as per the provisions of section 44DA.	44DA (2)	6GA	3CE
6.	Every assessee who has effected slump sale in the previous year as per the provisions of section 50B.	50B (3)	6H	3CEA
7.	Every person who has entered into an 'International transaction or specified domestic transaction' as per the	92E	10E	3CEB

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	requirement of section 92E of the Act.			
8.	Assessees who have been ordered by the Assessing Officer with the previous approval of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner under section 142(2A) to get their books of account audited having regard to the nature and complexity of the accounts, volume of accounts, doubts about the correctness of the accounts, multiplicity of transactions in the accounts or specialized nature of business activity of the assessee and the interests of the revenue.	142(2A)	14A	6B
9.	Assessee being a trust or institution claiming deduction u/s 11 & 12 as per the requirement of section 12A(b).	12A(1)(b)	17B	10B

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
10.	Assessee being any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of section 10(23C) claiming exemption under section 10(23C).	10(23C)(iv)/(v)/(vi)/(via)	16CC	10BB
11.	Assessee being electoral trust receiving voluntary contributions	13B	17CA(12)	10BC
12.	Assessee claiming deduction in respect of eligible businesses under sections 80 – IA or 80 – IB (except Multiplex Theatres/ Convention Centres/ hospitals in rural areas) and eligible undertakings/enterprises claiming deduction under section 80 – IC.	80-IA (7)/80-IB/ 80-IC and 80-IE	18BBB (1)	10CCB
13.	Assessee claiming deduction under section 80-ID in respect of the profits	80-ID (3)(iv)	18DE(3)	10CCBBA

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	and gains derived from the business of hotels and convention centres in specified areas.			
14.	Assessee claiming deduction under section 80-IB (11C) in respect of the profits and gains from the business of operating and maintaining a hospital located anywhere in India other than the excluded area.	80-IB(11C)	18DDA	10CCBD
15.	Assessee claiming deduction under section 80-IA (6) in respect of profits and gains of business of housing or other activities which are an integral part of a highway project.	80-IA (6)	18BBE (3)	10CCC
16.	Assessee, being scheduled banks owning an offshore banking unit in a Special Economic Zone and International financial services centre, for claiming deduction under Section 80LA in	80LA (3)	19AE	10CCF

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S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	respect of specified incomes.			
17.	Assessee, being Indian companies, claiming deduction under section 80JJAA, in respect of employment of new workmen.	80JJAA(2)(b)	19AB	10DA
18.	Assessee responsible for making the payment to a non resident	195(6)	37BB(1)(ii)(a)	15CB
19.	Assessee who has failed to deduct tax at source in accordance with the provisions of the Act, not be deemed as an assessee in default provided certain conditions are fulfilled and a certificate from an accountant to this effect is furnished in the format prescribed under section 201(1) of the Act.	201(1)	31ACB (1)	26A
20.	Assessee who has failed to collect tax at source in accordance with the provisions of the Act, not be deemed as an assessee in default	206C (6A)	37J (1)	27BA



## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	provided certain conditions are fulfilled and a certificate from an accountant to this effect is furnished in the format prescribed under section 206C(6A) of the Act.			
21.	Corporate assessee liable to pay Minimum Alternate tax under section 115JB of the Act, to furnish a report from an accountant certifying the computation of book profits.	115JB (4)	40B	29B
22.	Non-corporate assessee liable to pay Alternate Minimum tax under section 115JC of the Act, to furnish a report from an accountant certifying the computation of adjusted book profits.	115JC (3)	40BA	29C
23.	Assessee being a non-resident having a liaison office in India prepare and deliver a statement containing such particulars as may be prescribed.	285	114DA	49C
24.	Manufacturer assessee deriving	10A(5)	16D	56F

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	Profits and gains from an undertaking by the export of articles or things or computer software			
25.	Corporate assessee being an amalgamated company to furnish certificate from the principal officer, duly verified by an accountant regarding achievement of the prescribed level of production and continuance of such level of production in subsequent years.	72A(2)(b)(iii)	9C(b)	62
26.	Assessee being Unit Trust of India, distributing income to its unit holders to furnish a statement giving details of amount so distributed to be verified by an accountant as required by section 115R(3A).	115R(3A)	12B(2)	63
27.	Assessee being a mutual fund, distributing income to its unit holders to furnish a statement	115R(3A)	12B(3)	63A

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

S. No.	Particulars of Report/ statement/ Certificates	Applicable Section of the Income-tax Act, 1961	Applicable Rule of Income-tax Rules, 1962	Form No.
	giving details of amount so distributed to be verified by an accountant as required by section 115R(3A).			
28.	Assessee being a venture capital company or a venture capital fund to furnish a statement giving details of the nature of income paid or credited during the previous year and other relevant details to be verified by an accountant as per section 115U.	115U (2)	12C (2)	64
29.	Assessees engaged in the business of operating qualifying ships having opted for computation of income from such business under the tonnage tax scheme contained in chapter XII G of the Act to furnish a report under section 115VW of the Act.	115VW(ii)	11T	66

2.2 The first edition of this Guidance Note was published in the year 1985 immediately after the introduction of tax audit provision to help members in discharging their responsibility in an efficient manner. In order to incorporate

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changes made by the amendments to the Finance Act, as well as judicial pronouncements, circulars etc., the said Guidance Note has been revised in the years 1989, 1998, 1999, 2005 and 2013. The sequence of certain significant events is as follows:

- (a) The Government had substituted revised Rule 6G and Forms 3CA, 3CB and 3CD in the Official Gazette on June 4, 1999, vide Notification No 10950/F.No. 153/74/98/TPL and omitted Forms No.3CC and 3CE.
- (b) These forms have been subsequently revised vide CBDT's Notification No. 280/2004 dated 16th November 2004.
- (c) Significant changes in the Form No.3CD were made in the year 2006 through a Notification No. 208/2006 dated 10th August, 2006 which notified the Income tax (Ninth Amendment) Rules, 2006.
- (d) Significant changes in the Form No.3CD were again made in the year 2014 through the Notification No. 33/2014 dated 25.07.2014 which notified the Income-tax (7<sup>th</sup> Amendment) Rules, 2014.

2.3 Form No. 3CD is quite comprehensive and covers generally all the items included in Form No. 6B prescribed for reporting under section 142(2A) and hence this Guidance Note would meet almost all the reporting requirements of audit under section 142(2A) also. However, if under section 142(2A), the Assessing Officer requires specific information, the same has to be given separately along with Form No. 6B. The Institute has published separate Guidance Notes for audit of Public Charitable Institutions under section 12A(b), Report under section 92E of the Act, Report under section 115JB of the Act and Report under section 115JC of the Act .

2.4 The tax audit was introduced by section 11 of the Finance Act, 1984, which inserted a new section 44AB with effect from 1st April, 1985 [Assessment Year 1985-86]. This section makes it obligatory for a person carrying on business to get his accounts audited by a chartered accountant, and to furnish by the 'specified date', the report in the prescribed form of such audit, if the total sales, turnover or gross receipts in business in the relevant previous year exceed or exceeds the prescribed limit (Rs. One Crore w.e.f. A.Y. 2013-14). For a professional, the provisions of tax audit become applicable, if his gross receipts in profession exceed the prescribed limit (Rs. Twenty five Lakhs w.e.f. A.Y. 2013-14) in the relevant previous year. As observed by the Finance Minister, while presenting the Union Budget for 1984-85, and as stated in the Memorandum explaining the

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

provisions of the Finance Bill, 1984, the compulsory audit is intended to ensure proper maintenance of books of account and other records, in order to reflect the true income of the tax payer and to facilitate the administration of tax laws by a proper presentation of the accounts before the tax authorities. This would also save the time of the Assessing Officers considerably in carrying out the verification. The scope of section 44AB was enlarged to provide that audit under the section would be required in case of a person carrying on the business of the nature referred to in section 44AD or 44AE or 44AF (by the Finance Act 1997 w.e.f. assessment year 1998-99) or 44BB or 44BBB (by the Finance Act 2003 w.e.f. assessment year 2004-05), if such person claims that his income is lower than the amount of income deemed under these sections as presumptive income. Thereafter, Finance (No.2) Act, 2009 (w.e.f. AY 2011-12) enlarged the scope of section 44AD to encompass within its ambit the assessee covered by the provision of erstwhile section 44AF and hence, section 44AF has been omitted. While section 44AF dealt with assessee carrying on retail trade, the amended section 44AD covers all assessee carrying on eligible business except professionals as referred to in section 44AA(1), a person earning income in the nature of commission or brokerage, a person carrying on any agency business.

2.5 The *vires* of section 44AB has been upheld by Hon'ble Supreme Court in *T.D. Venkata Rao v. Union of India* [1999] 237 ITR 315 (SC). The Apex Court has made the following significant observations:

*"Chartered Accountants, by reason of their training have special aptitude in the matter of audits. It is reasonable that they, who form a class by themselves, should be required to audit the accounts of businesses whose income (sic: turnover) exceeds Rs.40 lakhs\* and professionals whose income (sic: gross receipts) exceeds Rs.10 lakhs\*\* in any given year. There is no material on record and indeed in our view, there cannot be that an income-tax practitioner has the same expertise as chartered accountants in the matter of accounts. For the same reasons the challenge under article 19 must fail, and it must be pointed out that these income-tax practitioners are still entitled to be authorised representatives of assesseees."*

*\*(increased to Rs. One Crore w.e.f. A.Y. 2013-14)*

*\*\* (increased to Rs. Twenty Five Lakhs w.e.f. A.Y. 2013-14)*

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

### 3. Provisions of section 44AB

3.1 Section 44AB reads as under:

**"Audit of accounts of certain persons carrying on business or profession".**

44AB. *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 exceed 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 the profits and gains of such person under section 44AE or section 44BB or section 44BBB, as the case may be, and he has claimed his income to be lower than the profits or gains so deemed to be the profits 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 and setting forth such particulars as may be prescribed.*

*Provided that this section shall not apply to the person, who derives income of the nature referred to in section 44B or section 44BBA, on and from the 1st day of April, 1985 or, as the case may be, the date on which the relevant section came into force, whichever is later.*

*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*

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

*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.*

*Explanation - For the purposes of this section, -*

- (i) "accountant" shall have the same meaning as in the Explanation below sub-section (2) of section 288;*
- (ii) "specified date", in relation to the accounts of the assessee of the previous year relevant to an assessment year, means the due date for furnishing the return of income under sub-section (1) of section 139*

\* w.e.f. A.Y. 2013-14

3.2 The Explanation below sub-section (2) of section 288 defines "accountant". Accordingly, "accountant" means a chartered accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949), and includes, in relation to any State, any person who by virtue of the provisions of sub-section (2) of section 226 of the Companies Act, 1956 (1 of 1956), is entitled to be appointed to act as an auditor of companies registered in that State. Section 226 of the Companies Act, 1956 has been replaced by section 141 in the Companies Act, 2013 w.e.f 1.4.2014.

3.3 The above section stipulates that every person carrying on business or profession is required to get his accounts audited by a chartered accountant before the "specified date" and furnish by that date the report of such audit, if the total sales, turnover or gross receipts exceed the prescribed limit (Presently Rs.1 crore w.e.f. A.Y. 2013-14) in the case of business and gross receipts exceed the prescribed limit (Presently Rs.25 lakhs w.e.f. A.Y. 2013-14) in the case of profession - vide clauses (a) and (b) of section 44AB.

3.4 Clause (c) of section 44AB, inserted by the Finance Act, 1997 and subsequently amended by the Finance Act, 2003 and Finance (No. 2) Act, 2009, provides that in the case of an assessee carrying on a business of the nature specified in sections 44AE, 44BB or 44BBB tax audit will be required, if he claims his income to be lower than the presumptive income deemed under the said sections even if his sales, turnover, or gross receipts does not exceed the prescribed limit (Presently Rs.1 crore w.e.f A.Y. 2013-14).

3.5 (1) Clause (d) of section 44AB, inserted by the Finance Act, 2009 w.e.f 1-4-2011 provides that in the case of an assessee carrying on a business of the nature specified in section 44AD, tax audit will be required, if he claims

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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his income to be lower than the presumptive income deemed under the said section and such income exceeds the maximum amount not chargeable to income-tax (i.e. basic exemption limit). Section 44AD as amended by Finance Act, 2009 provides that notwithstanding anything to the contrary contained in sections 28 to 43C, in the case of an eligible assessee engaged in an eligible business, a sum equal to eight per cent of the total turnover or gross receipts of the assessee in the previous year on account of such business or, as the case may be, a sum higher than the aforesaid sum claimed to have been earned by the eligible assessee, shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession".

(2) Any deduction allowable under the provisions of sections 30 to 38 shall, for the purposes of sub-section (1), be deemed to have been already given full effect to and no further deduction under those sections shall be allowed :

Provided that where the eligible assessee is a firm, the salary and interest paid to its partners shall be deducted from the income computed under sub-section (1) subject to the conditions and limits specified in clause (b) of section 40.

(3) The written down value of any asset of an eligible business shall be deemed to have been calculated as if the eligible assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.

(4) The provisions of Chapter XVII-C shall not apply to an eligible assessee in so far as they relate to the eligible business.

(5) Notwithstanding anything contained in the foregoing provisions of this section, an eligible assessee who claims that his profits and gains from the eligible business are lower than the profits and gains specified in sub-section (1) and whose total income exceeds the maximum amount which is not chargeable to income-tax, shall be required to keep and maintain such books of account and other documents as required under sub-section (2) of section 44AA and get them audited and furnish a report of such audit as required under section 44AB.

(6) The provisions of this section, notwithstanding anything contained in the foregoing provisions, shall not apply to—

- (i) a person carrying on profession as referred to in sub-section (1) of section 44AA;
- (ii) a person earning income in the nature of commission or brokerage; or



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(iii) a person carrying on any agency business.

*Explanation.*—For the purposes of this section,—

(a) "eligible assessee" means,—

- (i) an individual, Hindu undivided family or a partnership firm, who is a resident, but not a limited liability partnership firm as defined under clause (n) of sub-section (1) of section 2 of the Limited Liability Partnership Act, 2008 (6 of 2009); and
- (ii) who has not claimed deduction under any of the sections 10A, 10AA, 10B, 10BA or deduction under any provisions of Chapter VIA under the heading "C. - Deductions in respect of certain incomes" in the relevant assessment year.

(b) "eligible business" means,—

- (i) any business except the business of plying, hiring or leasing goods carriages referred to in section 44AE; and
- (ii) whose total turnover or gross receipts in the previous year does not exceed an amount of one crore rupees.

3.6 Under the provisions of section 44AD, an eligible assessee can opt to be assessed on presumptive basis, so long as the sales, turnover or gross receipts from an eligible business do not exceed Rs.1 crore. Once the sales, turnover or gross receipts from any such eligible business(es) exceed the prescribed limit (Presently Rs.1 crore w.e.f A.Y. 2013-14), a tax audit will be required under clause (a) of section 44AB. The provisions of sections 44AA and 44AB shall not apply insofar as they relate to an eligible business as referred to in section 44AD and , the business of plying, hiring or leasing goods carriages as referred to in section 44AE. In computing the monetary limits under sections 44AA and 44AB, the sales, turnover or gross receipts, from the business in the said sections is to be excluded.

3.7 If a person is carrying on business(es), coming within the scope of sections 44AD, 44AE, 44BB or 44BBB but he exercises his option given under these sections to get his accounts audited under section 44AB, tax audit requirements would apply, in respect of such business(es) even if the turnover of such business(es) does not exceed the prescribed limit (Presently Rs.1 crore w.e.f A.Y. 2013-14). In the case of a person carrying on businesses covered by sections 44AD, 44AE, 44BB or 44BBB and opting for presumptive taxation, tax audit requirement would not apply in respect of such businesses. If such person is carrying on other business(es) not

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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covered by presumptive taxation, tax audit requirements would apply in respect thereof, if the turnover of such business(es), other than the business(es) covered by presumptive taxation thereof, exceed the prescribed limit (Presently Rs.1 crore w.e.f. A.Y. 2013-14).

3.8 The first proviso to section 44AB stipulates that this section will not be applicable to a person who derives income of the nature referred to in sections 44B or 44BBA. Accordingly, where the assessee is carrying on any one or more of the businesses specified in section 44B or 44BBA referred to in the first proviso to section 44AB, the sales/turnover/gross receipts from such businesses shall not be included in the total sales/turnover/gross receipts for determining the applicability of section 44AB.

3.9 The report of such audit, duly signed and verified by the chartered accountant is required to be given in such form and setting forth such particulars as prescribed by the Board. Rule 6G provides that such audit report and particulars should be given in Forms No. 3CA/3CB as may be applicable and the statement of particulars should be given in Form No.3CD.

3.10 A question may arise in the case of an assessee who is eligible to claim deductions under various sections like sections 80-IA, 80-IB or 80-IC etc., as to whether it will be necessary for him to get separate audit reports/certificates under these sections in addition to an audit report under section 44AB. The requirement of section 44AB is a general requirement covering the overall position of the accounts of the assessee. This applies to the consolidated accounts of the assessee for the relevant previous year covering the results of all the units owned by the assessee whether situated at one place or at different places. Therefore, when the turnover of all the units put together exceed the prescribed limits, the assessee will have to get the audit report under section 44AB in the prescribed form and separate audit reports in the forms prescribed for different purposes like sections 80-IA, 80-IB or 80-IC etc. will have to be further obtained by the assessee to meet the specific requirements of the relevant sections.

## **4. 'Profession' and 'business' explained**

4.1. 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.

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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 - *Barendra Prasad Ray v ITO [1981] 129 ITR 295 (SC)*.

4.2 Section 2(36) of the Act defines profession to include vocation. Profession is a word of wide import and includes "vocation" which is only a way of living. – Additional *CIT v. Ram Kripal Tripathi [1980] 125 ITR 408 (All)*.

4.3 Whether a particular activity can be classified as 'business' or 'profession' will depend on the facts and circumstances of each case. 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] 59 ITR 699 (SC)*, *CIT v. Ram Kripal Tripathi [1980] 125 ITR 408 (All)*.

4.4 The following have been listed out as professions in section 44AA read with Rule 6F and other professions notified thereunder (Notifications No. 1620 SO-18(E) dated 12.1.77, No. 9102SO 2675 dated 25.09.1992 and No.116 SO 385(E), dated 4.5.2001):

- (i) Accountancy
- (ii) Architectural
- (iii) Authorised Representative
- (iv) Company Secretary
- (v) Engineering
- (vi) Film Artists/Actors, Cameraman, Director including an assistant director; a music director, including an assistant music director, an art director, including an assistant art director; a dance director, including an assistant dance director; Singer, Story-writer, a screen-play writer, a dialogue writer; editor, , lyricist and dress designer .
- (vii) Interior Decoration
- (viii) Legal
- (ix) Medical
- (x) Technical Consultancy

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(xi) Information Technology. Attention is invited to *Notification No. 890(E)/2000* dated 26-9-2000.

4.5. The following activities have been held to be business :

- (i) Advertising agent
- (ii) Clearing, forwarding and shipping agents - *CIT v. Jeevanlal Lalloobhai & Co. [1994] 206 ITR 548 (Bom)*.
- (iii) Couriers
- (iv) Insurance agent
- (v) Nursing home
- (vi) Stock and share broking and dealing in shares and securities - *CIT v. Lallubhai Nagardas & Sons [1993] 204 ITR 93 (Bom)*.
- (vii) Travel agent.

## 5. Sales, turnover, gross receipts

5.1 It will be noted that the provision relating to tax audit applies to every person carrying on business, if his total sales, turnover or gross receipts in business exceed the prescribed limit (Rs.1 crore w.e.f. A.Y. 2013-14) and to a person carrying on a profession, if his gross receipts from profession exceed the prescribed limit (Rs.25 lakhs w.e.f A.Y. 2013-14) in any previous year. However, the term "sales", "turnover" or "gross receipts" are not defined in the Act, and therefore the meaning of the aforesaid terms has to be considered for the applicability of the section.

5.2 The Central Sales Tax Act, 1956 defines "Turnover" as follows:

*"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.*

Further, section 8A(1) of the said Act provides that in determining turnover, deduction of sales tax should be made from the aggregate of sales price.

5.3 The term "Turnover" has been defined under Section 2(91) of the Companies Act, 2013 as follows:

*"2(91) "turnover" means the aggregate value of the realisation of amount made from the sale, supply or distribution of goods or on*

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*account of services rendered, or both, by the company during a financial year;"*

5.4 In the "Guidance Note on Terms Used in Financial Statements" published by the Institute, the expression "Sales Turnover" (Item 15.01) has been defined as under:-

*"The aggregate amount for which sales are effected or services rendered by an enterprise. The term 'gross turnover' and 'net turnover' (or 'gross sales' and 'net sales') are sometimes used to distinguish the sales aggregate before and after deduction of returns and trade discounts".*

5.5 The Guide to Company Audit issued by the Institute in the year 1980, while discussing "sales", stated as follows:

*"Total turnover, that is, the aggregate amount for which sales are effected by the company, giving the amount of sales in respect of each class of goods dealt with by the company and indicating the quantities of such sales for each class separately.*

*Note (i) The term 'turnover' would mean the total sales after deducting therefrom goods returned, price adjustments, trade discount and cancellation of bills for the period of audit, if any. Adjustments which do not relate to turnover should not be made e.g. writing off bad debts, royalty etc. Where excise duty is included in turnover, the corresponding amount should be distinctly shown as a debit item in the profit and loss account."*

5.6 The "Statement on the Amendments to Schedule VI to the Companies Act, 1956" issued by the Institute (Page 14, 1976 edition)( replaced with Guidance Note on Revised Schedule VI of the Companies Act, 1956) while discussing the disclosure requirements relating to 'turnover' stated as follows:-

*"As regards the value of turnover, a question which may arise is with reference to various extra and ancillary charges. The invoices may involve various extra and ancillary charges such as those relating to packing, freight, forwarding, interest, commission, etc. It is suggested that ordinarily the value of turnover should be disclosed exclusive of such ancillary and extra charges, except in those cases where because of the accounting system followed by the company, separate demarcation of such charges is not possible from the accounts or where the company's billing procedure involves a composite charge*

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*inclusive of various services rather than a separate charge for each service.*

*In the case of invoices containing composite charges, it would not ordinarily be proper to attempt a demarcation of ancillary charges on a proportionate or estimated basis. For example, if a company makes a composite charge to its customer, inclusive of freight and despatch, the charge so made should accordingly be treated as part of the turnover for purpose of this section. It would not be proper to reduce the value of the turnover with reference to the approximate value of the service relating to freight and despatch. On the other hand, if the company makes a separate charge for freight and despatch and for other similar services, it would be quite proper to ignore such charges when computing the value of the turnover to be disclosed in the Profit and Loss Account. In other words, the disclosure may well be determined by reference to the company's invoicing and accounting policy and may thereby vary from company to company. For reasons of consistency as far as possible, a company should adhere to the same basic policy from year to year and if there is any change in the policy the effect of that change may need to be disclosed if it is material, so that a comparison of the turnover figures from year to year does not become misleading."*

5.7 The Statement on the Companies (Auditors' Report) Order, 2003 issued by the Institute in April 2004, while discussing the term 'turnover' in paragraph 23 states `as follows:

The term, "turnover", has not been defined by the Order. Part II of Schedule VI to the Act, however, defines the term "turnover" as the aggregate amount for which sales are effected by the company. It may be noted that the "sales effected" would include sale of goods as well as services rendered by the company. In an agency relationship, turnover is the amount of commission earned by the agent and not the aggregate amount for which sales are effected or services are rendered. The term "turnover" is a commercial term and it should be construed in accordance with the method of accounting regularly employed by the company.

5.8 Although, Schedule III of the Companies Act, 2013 has replaced the Revised Schedule VI of the Companies Act, 1956 in the year 2014, guidance given herein above with respect to meaning of the term "turnover" is still relevant.

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5.9 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.

5.10 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.

5.11 Applying the above generally accepted accounting principles, a few typical cases may be considered:

- (i) Discount allowed in the sales invoice will reduce the sale price and, therefore, the same can be deducted from the turnover.
- (ii) Cash discount otherwise than that allowed in a cash memo/sales invoice is in the nature of a financing charge and is not related to turnover. The same should not be deducted from the figure of turnover.
- (iii) Turnover discount is normally allowed to a customer if the sales made to him exceed a particular quantity. This being dependent on the turnover, as per trade practice, it is in the nature of trade discount and should be deducted from the figure of turnover even if the same is allowed at periodical intervals by separate credit notes.
- (iv) Special rebate allowed to a customer can be deducted from the sales if it is in the nature of trade discount. If it is in the nature of commission on sales, the same cannot be deducted from the figure of turnover.

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- (v) Price of goods returned should be deducted from the figure of turnover even if the returns are from the sales made in the earlier year/s.
- (vi) Sale proceeds of fixed assets would not form part of turnover since these are not held for resale.
- (vii) Sale proceeds of property held as investment property will not form part of turnover.
- (viii) Sale proceeds of any shares, securities, debentures, etc., held as investment will not form part of turnover. However if the shares, securities, debentures etc., are held as stock-in-trade, the sale proceeds thereof will form part of turnover.

5.12 (a) A question may also arise as to whether the sales by a commission agent or by a person on consignment basis forms part of the turnover of the commission agent and/or consignee as the case may be. In such cases, it will be necessary to find out, whether the property in the goods or all significant risks, reward of ownership of goods belongs to the commission agent or the consignee immediately before the transfer by him to third person. If the property in the goods or all significant risks and rewards of ownership of goods continue to belong to the principal, the relevant sale price shall not form part of the sales/turnover of the commission agent and/or the consignee as the case may be. If, however, the property in the goods, significant risks and reward of ownership belongs to the commission agent and/or the consignee, as the case may be, the sale price received/receivable by him shall form part of his sales/turnover.

(b) In this context, it would be useful to refer to the CBDT Circular No.452 dated 17<sup>th</sup> March, 1986, where the Board has clarified the question of applicability of section 44AB in the cases of Commission Agents, Arhatias, etc. The Circular is published in **Appendix I (Page no. 213)**.

5.13 Share brokers, on purchasing securities on behalf of their customers, do not get them transferred in their names but deliver them to the customers who get them transferred in their names. The same is true in case of sales also. The share broker holds the delivery merely on behalf of his customer. The property in goods does not get transferred to the share brokers. Only brokerage which is being accounted for in the books of account of share brokers should be taken into account for considering the limits for the purpose of section 44AB. However, in case of transactions entered into by share broker on his personal account, the sale value should also be taken into account for considering the limit for the purpose of section 44AB. The case of a sub-broker is not different from that of a share broker.



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5.14 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 scrips. 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 premia. The turnover in such types of transactions is to be determined as follows:
  - (i) The total of favourable and unfavourable 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.

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- (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, the total value of the sales is to be considered as turnover.

5.15 (a) Further, an issue may arise whether such transactions of purchase or sale of stocks and shares undertaken by the assessee are in the course of business or as investment. The answer to this issue will depend on the facts and circumstances of each case taking into consideration the nature of the transaction, frequency and volume of transactions etc. For this, attention is invited to the following judgments where this issue has been considered.

- (i) *CIT v. P.K.N. and Co Ltd (1966) 60 ITR 65 (SC)*
- (ii) *Saroj Kumar Mazumdar v. CIT (1959) 37 ITR 242 (SC)*
- (iii) *CIT v. Suttlej Cotton Mills Supply Agency Ltd. (1975) 100 ITR 706 (SC)*
- (iv) *G. Venkataswami Naidu & Co. v. CIT (1959) 35 ITR 594 (SC)*

Further, CBDT Circular No.4/2007, dated: 15-6-2007-**Appendix II (Page no. 217)** may also be referred to.

(b) In case such transactions are for the purposes of investment and income/loss arising therefrom is to be computed under the head 'Capital Gains', then the value of such transaction is not to be included in sales or turnover for deciding the applicability of audit under section 44AB. However, in case such transactions are in the course of business, then the total of such sales are to be included in the sale, turnover or gross receipts as the case may be, of the assessee for determining the applicability of audit under section 44AB.

5.16 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. Broadly speaking, the following items of income and/or receipts would be covered by the term "gross receipts in business":

- (i) Cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India;
- (ii) Any duty of customs or excise or service tax re-paid or repayable as drawback to any person against exports under the Customs and Central Excise Duties and Service tax Drawback Rules, 1995;
- (iii) The aggregate of gross income by way of interest received by the money lender;

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- (iv) Commission, brokerage, service and other incidental charges received in the business of chit funds;
- (v) Reimbursement of expenses incurred (e.g. packing, forwarding, freight, insurance, travelling etc.) and if the same is credited to a separate account in the books, only the net surplus on this account should be added to the turnover for the purposes of Section 44AB;
- (vi) The net exchange rate difference on export sales during the year on the basis of the principle explained in (v) above will have to be added;
- (vii) Hire charges of cold storage;
- (viii) Liquidated damages;
- (ix) Insurance claims - except for fixed assets;
- (x) Sale proceeds of scrap, wastage etc. unless treated as part of sale or turnover, whether or not credited to miscellaneous income account;
- (xi) Gross receipts including lease rent in the business of operating lease;
- (xii) Finance income to reimburse and reward the lessor for his investment and services;
- (xiii) Hire charges and instalments received in the course of hire purchase;
- (xiv) Advance received and forfeited from customers.
- (xv) the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession

5.17 The following items would not form part of "gross receipts in business" for purposes of section 44AB.

- (i) Sale proceeds of fixed assets including advance forfeited, if any;
- (ii) Sale proceeds of assets held as investments;
- (iii) Rental income unless the same is assessable as business income;
- (iv) Dividends on shares except in the case of an assessee dealing in shares;
- (v) Income by way of interest unless assessable as business income;
- (vi) Reimbursement of customs duty and other charges collected by a clearing agent;
- (vii) In the case of a recruiting agent, the advertisement charges received by him by way of reimbursement of expenses incurred by him;
- (viii) In the case of a travelling agent, the amount received from the clients

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for payment to the airlines, railways etc. where such amounts are received by way of reimbursement of expenses incurred on behalf of the client. If, however, the travel agent is conducting a package tour and charges a consolidated sum for transportation, boarding and lodging and other facilities, then the amount received from the members of group tour should form part of gross receipts;

- (ix) In the case of an advertising agent, the amount of advertising charges recovered by him from his clients provided these are by way of reimbursement. But if the advertising agent books the advertisement space in bulk and recovers the charges from different clients, the amount received by him from the clients will not be the same as the charges paid by him and in such a case the amount recovered by him will form part of his gross receipts;
- (x) Share of profit of a partner of a firm in the total income of the firm excluded from his total income under section 10(2A) of the Income-tax Act;
- (xi) Write back of amounts payable to creditors and/or provisions for expenses or taxes no longer required.

5.18 Thus, the principle to be applied is 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.

5.19 In the case of a professional, the expression "gross receipts" in profession would include all receipts arising from carrying on of the profession. A question may, however, arise as to whether the out of pocket expenses received by him should form part of his gross receipts for purposes of this section. Normally, in the case of solicitors, advocates or chartered accountants, such out of pocket expenses received in advance are credited in a separate client's account and utilised for making payments for stamp duties, registration fees, counsel's fees, travelling expenses etc. on behalf of the clients. These amounts, if collected separately either in advance or otherwise, should not form part of the "gross receipts". If, however, such out of pocket expenses are not specifically collected but are included/collected by way of a consolidated fee, the whole of the amount so collected shall form part of gross receipts and no adjustment should be made in respect of actual expenses paid by the professional person for and/or on behalf of his clients out of the gross fees so collected. However, the amount received by way of

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advance for which services are yet to be rendered will not form part of the receipts, as such advances are the liabilities of the assessee and cannot be treated as his receipts till the services are rendered.

5.20 A question may arise in the case of an assessee carrying on business and at the same time engaged in a profession as to what are the limits applicable to him under section 44AB for getting the accounts audited. In such a case if his professional receipts are, say, rupees twenty seven lakhs but his total sales, turnover or gross receipts in business are, say, rupees seventy two lakhs, it will be necessary for him to get his accounts of the profession and also the accounts of the business audited because the gross receipts from the profession exceed the limit of rupees twenty five lakhs. If however, the professional receipts are, say, rupees twenty one lakhs and total sales turnover or gross receipts from business are, say, rupees eighty six lakhs it will not be necessary for him to get his accounts audited under the above section, because his gross receipts from the profession as well as total sales, turnover or gross receipts from the business are below the prescribed limits.

5.21 It may, however, be noted that in cases where the assessee carries on more than one business activity, the results of all business activities should be clubbed together. In other words, the aggregate sales, turnover and/or gross receipts of all businesses carried on by an assessee would be taken into consideration in determining whether the prescribed limit (Presently Rs. 1 crore w.e.f. A.Y. 2013-14) as laid down in section 44AB has been exceeded or not. However, where the business is covered by section 44B or 44BBA turnover of such business shall be excluded. Similarly, where the business is covered by section 44AD or 44AE and the assessee opts to be assessed under the respective sections on presumptive basis, the turnover thereof shall be excluded. So far as a partnership firm is concerned, each firm is an independent assessee for purposes of Income-tax Act. Therefore, the figures of sales of each firm will have to be considered separately for purposes of determining whether or not the accounts of such firm are required to be audited for purposes of section 44AB.

5.22 It must also be understood that the issue whether the turnover exceeds the prescribed limit (Presently Rs.1 crore w.e.f A.Y. 2013-14) in the case of business or the gross receipts exceed the prescribed limit (Presently Rs.25 lakhs w.e.f. A.Y. 2013-14) in the case of profession is to be determined in each year independent of the results obtained in the preceding year or years. Further, this section applies only if the turnover exceeds the prescribed limit according to the accounts maintained by the assessee. If the

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Assessing Officer wants the assessee to get his accounts audited in cases where the figures of turnover as appearing in the books of account of the assessee do not exceed the prescribed limits, he has no option but to pass an order under section 142(2A) directing the assessee to get his accounts audited from a chartered accountant as may be nominated by the Commissioner of Income-tax or the Chief Commissioner of Income-tax.

## **6. Liability to tax audit - Special cases**

6.1 A question may arise in the case of an assessee whose income is not chargeable to income-tax by reason of a specific exemption contained in the law or otherwise, as to whether he is required to get his accounts audited and to furnish such report under section 44AB. 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.1 crore w.e.f. A.Y. 2013-14). 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.1 crore w.e.f. A.Y. 2013-14).

6.2 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 exceed the prescribed limit (Presently Rs.1 crore w.e.f. A.Y. 2013-14).

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6.3 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.

## 7. Specified date and tax audit

7.1 As per the recent developments, the tax audit report is required to be uploaded using digital signature of the tax auditor. A question may arise whether a tax auditor appointed under section 44AB can be held responsible if he does not complete the audit and if the tax audit report is not uploaded before the specified date. Answer to this question will depend on the facts and circumstances of the case. Normally, it is the professional duty of the chartered accountant to ensure that the audit accepted by him is completed before the due date. If there is any unreasonable delay on his part, he is answerable to the Institute if a complaint is made by the client. However, if the delay in the completion of audit is attributable to his client, the tax auditor cannot be held responsible. It is, therefore, necessary that no chartered accountant should accept audit assignments which he cannot complete within the above time frame. In this regard, reference may also be made to paragraph 12 of this Guidance Note.

## 8. Penalty

8.1. In order to ensure proper compliance with section 44AB, section 271B has been enacted which reads as under:-

### ***"Failure to get accounts audited***

***271B.*** *If any person fails to get his accounts audited in respect of any previous year or years relevant to an assessment year or furnish a report of such audit as required under section 44AB, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum equal to one-half per cent of the total sales, turnover or gross receipts, as the case may be, in business, or of the gross receipts in profession, in such previous year or years or a sum of one hundred fifty thousand rupees, whichever is less."*

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8.2. As such, the failure of a person, to get his accounts audited in respect of any previous year or furnish a copy of such report as required under section 44AB may attract a penalty equal to 0.5% of the total sales, turnover or gross receipts, or Rs.1.5 lakh whichever is less. However, in view of the specific provisions contained in section 273B, no penalty is imposable under section 271B on the assessee for the above failure if he proves that there was reasonable cause for the said failure. The onus of proving reasonable cause is on the assessee.

8.3. Some of the instances where Tribunals/Courts have accepted as "reasonable cause" are as follows:

- (a) Resignation of the tax auditor and consequent delay;
- (b) *Bona fide* interpretation of the term 'turnover' based on expert advice;
- (c) Death or physical inability of the partner in charge of the accounts;
- (d) Labour problems such as strike, lock out for a long period, etc.;
- (e) Loss of accounts because of fire, theft, etc. beyond the control of the assessee;
- (f) Non-availability of accounts on account of seizure;
- (g) Natural calamities, commotion, etc.

## 9. Tax auditor

9.1 The tax audit is to be carried out by an "accountant". The term "accountant" has been defined in sub-clause (i) of Explanation to section 44AB as under:

For the purposes of this section, -

- (i) "accountant" shall have the same meaning as in the Explanation below sub-section (2) of section 288".

The above-mentioned Explanation reads as under:

"Accountant" means a chartered accountant within the meaning of Chartered Accountants Act, 1949 (38 of 1949) and includes, in relation to any State, any person, who by virtue of the provisions of sub-section (2) of section 226 of the Companies Act, 1956 (1 of 1956), is entitled to be appointed to act as an auditor of companies registered in that State."

As stated earlier, section 226 of the Companies Act, 1956 has been replaced with section 141 in the Companies Act, 2013 with effect from 1.04.2014.



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9.2 The proviso to section 44AB lays down that where the accounts of an assessee are required to be audited by or under any other law, 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 other law before the specified date and furnishes by that date the report by an 'accountant' as required under section 44AB. It may be noted that after amendment by the Finance Act, 2001, tax audit can be carried out by an accountant only. Accordingly, in case of any assessee like a co-operative society where the accounts under the relevant law have been audited by a person other than a chartered accountant, the tax audit will have to be conducted by the 'accountant' as defined under section 44AB.

9.3. Though the section refers to the accounts being audited by an accountant which means a chartered accountant as defined above, the audit can also be done by a firm of chartered accountants. This has been a recognised practice under the Act. In such a case, it would be necessary to state the name of the partner who has signed the audit report on behalf of the firm. The member signing the report as a partner of a firm or in his individual capacity should give his membership number while registering himself in the e-filing portal.

9.4. Section 44AB stipulates that only Chartered Accountants should perform the tax audit. This section does not stipulate that only the statutory auditor appointed under the Companies Act or other similar Statute should perform the tax audit. As such the tax audit can be conducted either by the statutory auditor or by any other chartered accountant in full time practice.

9.5 It may be noted that the Council at its 242<sup>nd</sup> meeting has passed a resolution effective from 1st April 2005, that any member in part-time practice (namely, holding a certificate of practice and also engaging himself in any other business and/or occupation) is not entitled to perform attest functions including tax audit.

9.6 A question may arise in the case of a public sector company or any other company where the statutory auditor has not been appointed by the authorities concerned as to whether the tax auditor appointed under section 44AB can complete his audit without waiting for statutory audit report on the accounts audited by the statutory auditors. It may be noted that Form No. 3CA requires the tax auditor to enclose a copy of the audit report conducted by the statutory auditor or the auditor of the financial statements as the case may be. Where a statutory auditor has not been appointed by the authorities concerned or where the report of the statutory auditor is not available for whatever reasons, it will be possible for the tax auditor to give his report in Form No. 3CB and to certify the relevant particulars in Form No.3CD. This is

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particularly important in those cases where the assessee concerned has suffered losses in the relevant accounting year. It may, however, be noted that the tax auditor in such cases will have to conduct the financial audit as well in order to enable him to certify whether or not the accounts reported upon by him give a true and fair view of the state of affairs of the assessee whose accounts are audited by him under section 44AB.

9.7 Tax audit under section 44AB being a recurring audit assignment, for expressing professional opinion on the financial statements and the particulars, the member accepting the assignment should communicate with the member who had done tax audit in the earlier year as provided in the Chartered Accountants Act. When making the enquiry from the retiring auditor, the member accepting the assignment should find out whether there is any professional or other reasons why he should not accept the appointment. The professional reasons for not accepting the appointment include:

- ◆ Non-compliance of the provisions of sections 224 and 225 of the Companies Act as mentioned in \*Code of Ethics issued by ICAI under Clause (9) of Part I of First Schedule to Chartered Accountants Act, 1949. Sections 224 and 225 have been replaced with section 139/142 and section 140 respectively in Companies Act, 2013.
- ◆ Non-payment of undisputed audit fees by auditees other than in case of sick units for carrying out the statutory audit under the Companies Act, 1956/2013 or various other statutes.
- ◆ Issuance of qualified report

9.8 In the case of a person whose accounts of the business or profession have been audited under any other law (i.e. a company, a co-operative society, etc. which is required to get the accounts audited under a Statute) it is not necessary to communicate with the statutory auditor if he had not done tax audit in the earlier year. Attention of the members is invited to the detailed discussion in the publication of ICAI, \*"Code of Ethics" – **Appendix III (Page no. 220)**. Further, attention of members is invited to the Chapter-VII "Appointment of an Auditor in case of non-payment of undisputed fees" of the Council Guidelines No.1-CA(7)/02/2008, dated 8<sup>th</sup> August, 2008- **Appendix IV (Page no. 226)**

*\*In view of the fact that with effect from 01.04.2014, the Companies Act, 1956 has been replaced with Companies Act, 2013, the "Code of Ethics" issued by ICAI is under revision. The members may refer the revised "Code of Ethics" as and when published for the above mentioned provisions.*

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9.9 A chartered accountant should not accept the tax audit of a person to whom he is indebted for more than rupees ten thousand. Reference should be made to Chapter- X "Appointment of an auditor when he is indebted to a concern" of the Council Guidelines No.1-CA(7)/02/2008, dated 8<sup>th</sup> August, 2008- **Appendix IV (Page no. 226)** whereby a member of the Institute shall be deemed to be guilty of professional misconduct if he accepts appointment as an auditor of a concern while he is indebted to the concern or has given any guarantee or provided any security in connection with the indebtedness of any third person to the concern, for limits fixed in the statute and in other cases for amount exceeding rupees ten thousand. For this purpose, the limit of Rs. 10,000/- shall be the aggregate amount in respect of the proprietor and/or the partner/s of the firm of chartered accountants.

9.10 The Council has issued a Guideline No.1-CA(7)/02/2008, dated 8<sup>th</sup> August, 2008 given in **Appendix IV (Page no. 226) Chapter- IX "Appointment as Statutory auditor"** states that a member of the Institute in practice shall be deemed to be guilty of professional misconduct, if he accepts the appointment as statutory auditor of Public Sector Undertaking/ Government Company /Listed Company and other Public Company having turnover of Rs. 50 crores or more in a year and accepts any other work or assignment or service in regard to the same undertaking/company on a remuneration which in total exceeds the fee payable for carrying out the statutory audit of the same undertaking/company.

9.11 The above restrictions shall apply in respect of fees for other work or service or assignment payable to the statutory auditors and their associate concerns put together.

9.12 As per the said notification, the term "other work(s)" or "service(s)" or "assignment(s)" shall include Management Consultancy and all other professional services permitted by the Council pursuant to Section 2(2)(iv) of the Chartered Accountants Act, 1949 but shall not include: -

- (i) audit under any other statute;
- (ii) certification work required to be done by the statutory auditors; and
- (iii) any representation before an authority.

9.13 Since the obligation for tax audit has been specified in section 44AB of the Income-tax Act, 1961, it will be considered as an audit under any other statute for the purpose of this notification and thus the above restriction shall not apply in respect of tax audit fees.

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9.14 The tax auditor should obtain from the assessee a letter of appointment for conducting the audit as mentioned in section 44AB. It is advisable that such an appointment letter should be signed by the person competent to sign the return of income in terms of the provisions of section 140 of the Act. It would also be useful if the letter affirms that no other auditor was appointed to conduct the tax audit for the year for which the appointment is being made. The letter may also give the name and address of the tax auditor for the previous year, wherever relevant. This would give the necessary information to the incoming tax auditor to enable him to communicate with the previous auditor. The letter of appointment should also specify the remuneration of the tax auditor. SA-210, *Agreeing the Terms of Audit Engagement* issued by the ICAI requires that the auditor to agree with the terms of audit engagement with management or those charged with governance as appropriate. The agreed terms would need to be recorded in an audit engagement letter or other suitable form of written agreement and shall include (a) The objective and scope of the audit of the financial statements; It should be specifically mentioned that the scope of audit is restricted to the provisions contained in section 44AB of the Income tax Act, 1961 and the Income-tax Rules, 1962. (b) The responsibilities of the auditor; (c) The responsibilities of management; (d) Identification of the applicable financial reporting framework for the preparation of the financial statements; and (e) Reference to the expected form and content of any reports to be issued by the auditor as per the provisions of Income-tax Act, 1961 and Income-tax Rule, 1962 along with a statement that there may be circumstances in which a report may differ from its expected form and content. In the interest of both client and auditor, the auditor should send an engagement letter, preferably before the commencement of the engagement, to help avoid any misunderstandings with respect to the engagement. The engagement letter documents and confirms the auditor's acceptance of the appointment, the objective and scope of the audit and the extent of the auditor's responsibilities to the client. However, it may be noted that wherever an audit is to be conducted under a Statute, acknowledgement of the letter of the auditor by the client is considered to be sufficient compliance of SA-210. The tax auditor should get the statement of particulars, as required in the annexure to the audit report, authenticated by the assessee before he does the same.

9.15 The tax auditor is required to upload the tax audit report directly in the e-filing portal.

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9.16 The appointment of the auditor for tax audit in the case of a company need not be made at the general meeting of the members. It can be made by the Board of Directors or even by any officer, if so authorised by the Board in this behalf. The appointment in the case of a firm or a proprietary concern can be made by a partner or the proprietor or a person authorised by the assessee. It is possible for the assessee to appoint two or more chartered accountants as joint auditors for carrying out the tax audit, in which case, the audit report will have to be signed by all the chartered accountants. In case of disagreement, they can give their reports separately. In this regard, attention is invited to Para 12 of the SA 299, *Responsibility of Joint Auditors* issued by ICAI reproduced below:

*"Normally, the joint auditors are able to arrive at an agreed report. However, where the joint auditors are in disagreement with regard to any matters to be covered by the report, each one of them should express his own opinion through a separate report. A joint auditor is not bound by the views of the majority of the joint auditors regarding matters to be covered in the report and should express his opinion in a separate report in case of a disagreement."*

The responsibility of joint tax auditors will be the same as in the case of other audits e.g. audit under the Companies Act. For details relating to such responsibility, in the case of joint tax audit, reference may be made to SA 299, *Responsibility of Joint Auditors*.

9.17 The position of a tax auditor for conducting audit under section 44AB will be considered as an office of profit. Therefore, the provisions of section 314 of the Companies Act, 1956 will be attracted when a relative of a director is appointed as a tax auditor of the company, if the remuneration thereof exceeds the limits prescribed in the aforesaid section. The necessary formalities will be required to be complied with as required under section 314. It may be noted Section 314 of the Companies Act, 1956 has been replaced with section 188 of the Companies Act, 2013, w.e.f. 1.4.2014.

9.18 The Act does not prohibit a relative or an employee of the assessee being appointed as a tax auditor under section 44AB. It may, however, be noted that as per the decision of the Council (reported in the Code of Ethics under clause (4) of Part I of Second Schedule), a chartered accountant should not express his opinion on financial statements of any business or enterprise in which he, his firm or a partner in his firm has a substantial interest. It may be noted that the Council has decided not to permit a Chartered Accountant in employment to certify the financial statements of the

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concern in which he is employed, or of a concern under the same management as the concern in which he is employed, even though he holds certificate of practice and that such certification can be done by any Chartered Accountant in practice. This restriction would not however apply where the certification is permitted by any law, e.g. Section 228(4) of the Companies Act, 1956 and the Companies (Branch Audit Exemption) Rules, 1961 made thereunder. Therefore, an employee of an assessee or an employee of a concern under the same management cannot audit the accounts of an assessee under section 44AB. Relevant extracts from the \*Code of Ethics published by ICAI are given in **Appendix V (Page no. 237)**

*\*In view of the fact that with effect from 01.04.2014 the Companies Act, 1956 has been replaced with Companies Act, 2013, the "Code of Ethics" issued by ICAI is under revision. The members may refer the revised "Code of Ethics" as and when published for the above mentioned provisions.*

9.19 A chartered accountant who is responsible for writing or maintenance of the books of account of the assessee should not audit such accounts. This principle will apply to the partner of such a member as well as to the firm in which he is a partner. In view of this, a chartered accountant who is responsible for writing or maintenance of the books of account or his partner or the firm in which he is a partner should not accept tax audit assignment under section 44AB in the case of such an assessee.

9.20 The audit of accounts of a professional firm of chartered accountants, under section 44AB cannot be conducted by any partner or employee of such firm.

9.21 A chartered accountant/firm of chartered accountants, who is appointed as tax consultant of the assessee, can conduct tax audit under section 44AB. But an internal auditor of the assessee cannot conduct tax audit if he is an employee of the assessee. The Council of ICAI in its 281st meeting held from 3rd to 5th October, 2008 decided that an internal auditor of an assessee, whether working with the organisation or independently practicing chartered accountant or a firm of chartered accountants, cannot be appointed as his tax auditor. The decision was made effective from 12-12-2008.

9.22 A question may arise whether an assessee can remove a tax auditor appointed under section 44AB. The answer depends upon the facts and circumstances of the case. It is, however, possible for the management to remove a tax auditor where there are valid grounds for such removal. This

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may arise where the tax auditor has delayed the submission of audit report under section 44AB for an unreasonable period and if it is found that there is no possibility of getting the audit report uploaded before the specified date. In such cases, the management may be justified in removing the tax auditor. However, the tax auditor cannot be removed on the ground that he has given an adverse audit report or the assessee has an apprehension that the tax auditor is likely to give an adverse audit report. If there is any unjustified removal of tax auditors, the Ethical Standards Board constituted by the Institute can intervene in such cases. No other chartered accountant should accept the audit assignment if the removal of his predecessor is not on valid grounds.

9.23 Before accepting a tax audit, the chartered accountant should take into consideration the ceiling on tax audit assignments fixed under the Chapter VI- Tax Audit assignments under Section 44AB of the Income-tax Act, 1961 of the Council Guidelines No.1-CA(7)/02/2008, dated 8<sup>th</sup> August, 2008 as amended by a decision of the Council taken in its 331<sup>st</sup> meeting held from 10.02.2014 to 12.02.2014 and its 333<sup>rd</sup> meeting held from 14.05.2014 to 16.05.2014.- **Appendix-IV (Page no. 226)** .

9.24 In view of the said Guidelines a member of the Institute in practice, shall be deemed to be guilty of professional misconduct if, he accepts more than 60 tax audit assignments relating to an assessment year or such other limit as may be prescribed by ICAI from time to time under section 44AB, whether in respect of a person whose accounts have been audited under any other law or a person who carries on business or profession but who is not required by or under any other law to get his accounts audited.

9.25 (a) As per the Council Guidelines No.1-CA(7)/02/2008, dated 8<sup>th</sup> August, 2008, audit of books of account of persons carrying on businesses covered by sections 44AD and 44AE, is not included in the aforesaid limit. The auditor is advised to maintain the details of the audits conducted by virtue of the provisions of section 44AD and 44AE separately in the format mentioned in Para 9.26.

(b) Furthermore, a clarification was issued for reckoning the "specified number of tax audit assignments" conducted under section 44AB of the Income-tax Act, 1961, the text of the clarification is reproduced below:

*"Various statutes prevailing in India like DVAT, 2004 requires the assessee to furnish an audit report in a form duly signed and verified by such particulars as may be prescribed under section 44AB of the Income-tax Act, 1961 i.e. Form 3CB/3CD. This had lead to the doubts*

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*as to whether such audits would be included in the ceiling of "specified number of tax audit assignments".*

*Considering the same, the Council at its 311th meeting held on 8<sup>th</sup> and 9<sup>th</sup> November, 2011 clarified that audit prescribed under any statute which requires the audit report in the form as prescribed under section 44AB of the Income-tax Act, shall not be considered for the purpose of reckoning the specified number of tax audit assignments if the turnover of the auditee is below the turnover limit specified in section 44AB of the Income-tax Act, 1961. For instance audit under section 44AD, audit under DVAT, 2004 (for turnover between 40 to 60 Lakhs) etc. will not be considered for inclusion in the present limit of 60\* audits"*

*\*w.e.f 1.04.2014*

9.26 In case the member is a partner of a firm of chartered accountants in practice, the ceiling of 60 tax audit assignments shall be computed with reference to each of the partner in the said firm. Where any partner of the firm of chartered accountants in practice is also a partner of any other firm or firms of chartered accountants in practice, the ceiling limit of 60 shall apply with reference to all the firms together in relation to such partner. Similarly, where any partner accepts one or more tax audit assignments in his individual capacity, the total number of such assignments under section 44AB which may be accepted by him whether directly in his individual capacity or as partner of the firm of chartered accountants in practice shall not exceed 45 tax audit assignments. If two members or firms of chartered accountants are appointed as joint tax auditors, then the assignment will have to be included in the case of both the members or firms separately. It has, however, been clarified that the audit of the head office and branch offices concerned shall be regarded as one tax audit assignment. Similarly, the audit of one or more branches of the same concern by one chartered accountant in practice shall be construed as only one tax audit assignment. In computing the specified number of tax audit assignments each year's audit would be taken as a separate assignment. Every chartered accountant in practice shall maintain a record of the tax audit assignments accepted by him in each financial year in the format prescribed by the Council. This format is reproduced in **Appendix VI (Page no. 242)**.

9.27 The Institute has recommended fees for professional services on the basis of time devoted by a chartered accountant and his assistants. The fees for tax audit assignment can be charged by a chartered accountant on the



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basis of the work involved in the assignment. It may be appreciated that no uniform fees can be recommended on the basis of turnover because an assessee having turnover of Rs.1 crore in a trading activity may have less transactions as compared to an assessee having the same turnover in a manufacturing activity. Similarly the transactions in a wholesale business will be less than the transactions in a retail business. The revised minimum recommended scale of fees recommended by the Committee of Capacity Building of CA Firms and small and medium Practitioners as on date is given in **Appendix VII (Page No. 243)**.

9.28 The chartered accountants should charge reasonable fees depending upon the responsibility involved under the revised forms and taking into consideration the work involved in tax audit assignment which has increased considerably consequent to the revision of the forms. It is necessary that members of the profession should also maintain reasonable standards of professional fees.

9.29 As mentioned in Paragraph 9.26 above, the audit of the head office and branch offices of an assessee shall be regarded as one tax audit assignment.

## **10. Accounting Standards**

10.1. Recognizing the need to harmonize the diverse accounting policies and practices in use in India and keeping in view the International developments in the field of accounting, the Council of the Institute has issued Accounting Standards.

10.2. The legal recognition to the Accounting Standards formulated by the ICAI was granted in October 1998 with insertion of Section 211(3A), (3B), and (3C) in the Companies Act, 1956. As per Section 211(3C) of the Act, Accounting Standards issued by the ICAI may be prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standards (NACAS). As per the proviso to the section, till the notification of the Accounting Standards by the Government, the Accounting Standards issued by the ICAI are required to be followed by companies. In the year 2006, Accounting Standards 1 to 7 and 9 to 29 were notified by the Ministry of Corporate Affairs, Government of India, under the Companies (Accounting Standards) Rules, 2006 vide its notification dated December 7, 2006 in the Gazette of India. These were made effective in respect of accounting periods commencing on or after the publication of these Accounting Standards (i.e., December 7, 2006). As per the Companies

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(Accounting Standards) Rules, 2006, Companies are classified into two categories, i.e., Small and Medium Companies (SMCs) and Non-SMCs. The Companies Act, 2013 has replaced Companies Act, 1956. Section 133 of the Companies Act, 2013 provides for compliance to Accounting Standards. The existing Accounting Standards notified under Companies (Accounting Standards) Rules, 2006 would continue to be followed.

10.3 ICAI, keeping in view the fact that the Accounting Standards notified under Companies (Accounting Standards) Rules, 2006, will be applicable to the companies, announced the scheme for applicability of accounting standards issued by ICAI to non-companies. The criteria for classification non-corporate entities as decided by ICAI and companies under the Companies (Accounting Standards) Rules, 2006 is given in ***Appendix-VIII (Page no. 254)***.

10.4 The Accounting Standards, issued by ICAI/notified under Companies (Accounting Standards) Rules, 2006 are for use in the presentation of general purpose financial statements which are issued to the public by such commercial, industrial or business enterprises as may be specified by the Institute from time to time and subject to the attest function of its members. The term 'General Purpose Financial Statements' includes balance sheet, statement of profit and loss, a cash flow statement (wherever applicable) and other statements and explanatory notes which form part thereof, issued for the use of various stakeholders, Governments and their agencies and the public at large.

10.5. The Institute has so far issued thirty two definitive standards as follows:

- AS 1 Disclosure of Accounting Policies
- AS 2 Valuation of Inventories
- AS 3 Cash Flow Statements
- AS 4 Contingencies and Events Occurring After the Balance Sheet Date.
- AS 5 Net Profit or Loss for the period, Prior Period items and changes in Accounting policies
- AS-6 Depreciation Accounting
- AS 7 Construction Contracts
- AS 8 (Withdrawn pursuant to AS 26 becoming mandatory)  
Accounting for Research and Development

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- AS 9 Revenue Recognition
- AS10 Accounting for Fixed Assets
- AS11 The Effects of Changes in Foreign Exchange Rates
- AS12 Accounting for Government Grants
- AS13 Accounting for Investments
- AS14 Accounting for Amalgamations
- AS15 Employee Benefits
- AS16 Borrowing Costs
- AS 17 Segment Reporting
- AS 18 Related Party Disclosures
- AS 19 Leases
- AS 20 Earnings Per Share
- AS 21 Consolidated Financial Statements
- AS 22 Accounting for Taxes on Income
- AS 23 Accounting for Investments in Associates in Consolidated Financial Statements
- AS 24 Discontinuing Operations
- AS 25 Interim Financial Reporting
- AS 26 Intangible Assets
- AS 27 Financial Reporting of Interests in Joint Ventures
- AS 28 Impairment of Assets
- AS 29 Provisions, Contingent Liabilities and Contingent Assets
- AS 30 Financial Instruments: Recognition and Measurement
- AS 31 Financial Instruments: Presentation
- AS 32 Financial Instruments: Disclosures

10.6 AS 30, AS 31 and AS 32 issued by the Institute of Chartered Accountants of India (ICAI) in 2007 have not yet been notified by the Government under Section 211(3C)/133 of the Companies Act, 1956/2013 respectively. In respect of the financial statements or other financial information the status of AS 30 as announced by the Council of the ICAI is as follows:

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- (i) To the extent of accounting treatments covered by any of the existing notified accounting standards (for eg. AS 11, AS 13 etc) the existing accounting standards would continue to prevail over AS 30.
- (ii) In cases where a relevant regulatory authority has prescribed specific regulatory requirements (eg. Loan impairment, investment classification or accounting for securitizations by the RBI, etc), the prescribed regulatory requirements would continue to prevail over AS 30.
- (iii) The preparers of the financial statements are encouraged to follow the principles enunciated in the accounting treatments contained in AS 30. The aforesaid is, however, subject to (i) and (ii) above.

10.7 The abovementioned clarifications would also be relevant to the existing AS 31, *Financial Instruments: Presentation* and AS 32, *Financial Instruments: Disclosures*

#### 10.8 **Applicability of Accounting Standards and exemptions/relaxations for Small and Medium Sized Enterprises**

It may be noted that certain exemptions/relaxations from the applicability of accounting standards have been given to Small and Medium Size Enterprise (SMEs). Accordingly, the Council has decided upon the following scheme which has come into effect in respect of accounting periods commencing on or after 1.4.2004.

- (1) For the purpose of applicability of Accounting Standards, enterprises are classified into three categories, viz., Level I, Level II and Level III. Level II and Level III enterprises are considered as SMEs.
- (2) Level I enterprises are required to comply fully with all the accounting standards.
- (3) It has been decided that no relaxation should be given to Level II and Level III enterprises in respect of recognition and measurement principles. Relaxations are provided with regard to disclosure requirements. Accordingly, Level II and Level III enterprises are fully exempted from certain accounting standards which primarily lay down disclosure requirements. In respect of certain other accounting standards, which lay down recognition, measurement and disclosure requirements, relaxations from certain disclosure requirements are given. The exemptions/relaxations are decided to be provided by modifying the applicability portion of the relevant accounting standards. The applicability of AS and exemptions/relaxations thereof for SMEs are given in **Appendix VIII (Page no. 254)**.

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10.9 AS also apply in respect of financial statements audited under section 44AB of the Income-tax Act, 1961. Accordingly, members should examine compliance with the mandatory accounting standards when conducting such audit.

10.10 AS apply in respect of commercial, industrial or business activities of an enterprise. In the case of charitable or religious organisations, AS will not apply if all activities of such organisations are not of commercial, industrial or business nature (e.g. an activity of collecting donations and giving them to flood affected people). In other words, exclusion of an entity from the applicability of the AS would be permissible only if no part of the activity of such entity is commercial, industrial or business in nature. Even if a very small portion of the activities of an entity is considered to be commercial, industrial or business in nature, then it cannot claim exemption from the application of AS. The AS would apply to all its activities including those which are not commercial, industrial or business in nature.

10.11 The Companies Act, 2013, as well as many other statutes require that the financial statements of an enterprise should give a true and fair view of its financial position and working results. This requirement is implicit even in the absence of a specific statutory provision to this effect. However, what constitutes 'true and fair' view has not been defined either in the Companies Act, 2013, or in any other statute. The Accounting Standards (as well as other pronouncements of the Institute on accounting matters) seek to describe the accounting principles and the methods of applying these principles in preparation and presentation of financial statements so that they give a true and fair view.

10.12 In this connection, it may be noted that sub-section (1) of section 129 of the Companies Act, 2013, provides that the financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under section 133 and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III thereof. It also provides that items contained in such financial statements shall be in accordance with the accounting standards. Sub-section (5) of section 129 provides that without prejudice to sub-section (1), where the financial statements of a company do not comply with the accounting standards referred to in sub-section (1), the company shall disclose in its financial statements, the deviation from the accounting standards, the reasons for such deviation and the financial effects, if any, arising out of such deviation.

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10.13 Section 2(2) of Companies Act, 2013 provides that accounting standards" means the standards of accounting or any addendum thereto for companies or class of companies referred to in section 133.

10.14 The 'Preface to the Statements of Accounting Standards', issued by the Institute, *inter alia*, states:

*The Accounting Standards will be mandatory from the respective date(s) mentioned in the Accounting Standard(s). The mandatory status of an Accounting Standard implies that while discharging their attest functions, it will be the duty of the members of the Institute to examine whether the Accounting Standard is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from the Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviation.*

*Ensuring compliance with the Accounting Standards while preparing the financial statements is the responsibility of the management of the enterprise. Statutes governing certain enterprises require of the enterprises that the financial statements should be prepared in compliance with the Accounting Standards, e.g., the Companies Act, 2013 (section 129), and the Insurance Regulatory and Development Authority (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2000.'*

10.15 While discharging their attest function, the members of the Institute may keep the following in mind with regard to the mandatory AS.

### **AS 1 Disclosure of Accounting Policies<sup>1</sup>**

In the case of a company, members should qualify their audit reports in case:

- (a) accounting policies required to be disclosed under Schedule VI or any other provisions of the Companies Act, 1956, have not been disclosed, or
- (b) accounts have not been prepared on accrual basis, or
- (c) the fundamental accounting assumptions of going concern and consistency have not been followed and this fact has not been disclosed in the financial statements, or

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<sup>1</sup> As per the announcement of the Council 'accounting Standards 1,7,8,9 and 10 made mandatory' published in July 1990 issue of 'The Chartered Accountants'

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- (d) proper disclosures regarding changes in the accounting policies have not been made.
- (e) Accounting Standards referred to in section 211(3C) of the Companies Act, 1956 have not been followed.

10.16 Where a company has been given a specific exemption regarding any of the matters stated above, but the fact of such exemption has not been adequately disclosed in the accounts, the member should mention the fact of exemption in his audit report without necessarily making it a subject matter of audit qualification.

10.17 In the case of an enterprise other than a company, members should qualify their audit reports in case AS issued, prescribed and made mandatory by the ICAI have not been followed.

#### **10.18 Financial statements prepared on a basis other than accrual**

With regard to the fundamental accounting assumption of accrual, the Council has made a specific announcement that in respect of (a) Sole proprietary concerns/individuals, (b) Partnership firms, (c) Societies registered under the Societies Registration Act, (d) Trusts, (e) Hindu undivided families and (f) Association of persons, the auditor should examine whether the financial statements have been prepared on accrual basis. In case where the statute governing the enterprise requires the preparation and presentation of financial statements on accrual basis but the financial statements have not been so prepared, the auditor should qualify his report. On the other hand where there is no statutory requirement for preparation and presentation of financial statements on accrual basis, and the financial statements have been prepared on a basis other than 'accrual', the auditor should describe in his audit report, the basis of accounting followed, without necessarily making it a subject matter of a qualification. In such a case the auditor should also examine whether those provisions of the AS which are applicable in the context of the basis of accounting followed by the enterprise have been complied with or not and consider making suitable qualifications in his audit report accordingly.

#### **10.19 Accounting Standards under taxation law**

The Finance Act, 1995 substituted a new section 145 w.e.f. A.Y. 1997-98. The section deals with method of accounting and is reproduced below :-

*"145. (1) Income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" shall, subject*

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*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 assesseees 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 section 144."*

### 10.20 Standards notified by Government - AS (IT)

In exercise of the powers conferred by section 145(2), the Central Government has by Notification No. S.O.69 (E), dated 25th January, 1996 notified two AS (IT). This notification came into force with effect from 1st day of April, 1996, and is accordingly applicable from assessment year 1997-98 and subsequent assessment years.

10.21 These AS (IT) are given below:

***Accounting Standards to be followed by all assesseees following mercantile system of accounting:***

#### ***A. Accounting Standard I relating to disclosure of accounting policies***

*1. All significant accounting policies adopted in the preparation and presentation of financial statements shall be disclosed.*

*2. The disclosure of the significant accounting policies shall form part of the financial statements and the significant accounting policies shall normally be disclosed in one place.*

*3. Any change in an accounting policy which has a material effect in the previous year or in the years subsequent to the previous years shall be disclosed. The impact of, and the adjustments resulting from such change, if material, shall be shown in the financial statements of the period in which such change is made to reflect the effect of such change. Where the effect of such change is not ascertainable, wholly or in part, the fact shall be indicated. If a change is made in the accounting policies which has no material effect on the financial statements for the previous year but which is reasonably expected to*



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*have a material effect in any year subsequent to the previous year, the fact of such change shall be appropriately disclosed in the previous year in which the change is adopted.*

4. *Accounting policies adopted by an assessee should be such so as to represent a true and fair view of the state of affairs of the business, profession or vocation in the financial statements prepared and presented on the basis of such accounting policies. For this purpose, the major considerations governing the selection and application of accounting policies are the following, namely:*

- (i) Prudence - Provisions should be made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of available information;*
- (ii) Substance over form - The accounting treatment and presentation in financial statements of transactions and events should be governed by their substance and not merely by the legal form;*
- (iii) Materiality - Financial statements should disclose all material items, the knowledge of which might influence the decisions of the user of the financial statements.*

5. *If the fundamental accounting assumptions relating to going concern, Consistency and Accrual are followed in financial statements, specific disclosure in respect of such assumptions is not required. If a fundamental accounting assumption is not followed, such fact shall be disclosed.*

6. *For the purposes of paragraphs (1) to (5), the expressions, -*

- (a) "Accounting policies" means the specific accounting principles and the methods of applying those principles adopted by the assessee in the preparation and presentation of financial statements;*
- (b) "Accrual" refers to the assumption that revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate;*
- (c) "Consistency" refers to the assumption that accounting policies are consistent from one period to another;*

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- (d) *"Financial statements" means any statement to provide information about the financial position, performance and changes in the financial position of an assessee and includes balance sheet, profit and loss account and other statements and explanatory notes forming part thereof;*
- (e) *"Going concern" refers to the assumption that the assessee has neither the intention nor the necessity of liquidation or of curtailing materially the scale of the business, profession or vocation and intends to continue his business, profession or vocation for the foreseeable future.*

### **B. Accounting Standard II relating to disclosure of prior period and extraordinary items and changes in accounting policies:**

1. *Prior period items shall be separately disclosed in the profit and loss account in the previous year together with their nature and amount in a manner so that their impact on profit or loss in the previous year can be perceived.*
2. *Extraordinary items of the enterprise during the previous year shall be disclosed in the profit and loss account as part of taxable income. The nature and amount of each such item shall be separately disclosed in a manner so that their relative significance and effect on the operating results of the previous year can be perceived.*
3. *A change in an accounting policy shall be made only if the adoption of a different accounting policy is required by statute or if it is considered that the change would result in a more appropriate preparation or presentation of the financial statements by an assessee.*
4. *Any change in an accounting policy which has a material effect shall be disclosed. The impact of, and the adjustments resulting from such change, if material, shall be shown in the financial statements of the period in which such change is made to reflect the effect of such change. Where the effect of such change is not ascertainable, wholly or in part, the fact shall be indicated. If a change is made in the accounting policies which has no material effect on the financial statements for the previous year but which is reasonably expected to have a material effect in years subsequent to the previous years, the fact of such change shall be appropriately disclosed in the previous year in which the change is adopted.*

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5. *A change in an accounting estimate that has a material effect in the previous year shall be disclosed and quantified. Any change in an accounting estimate which is reasonably expected to have a material effect in years subsequent to the previous year shall also be disclosed.*

6. *If a question arises as to whether a change is a change in accounting policy or a change in an accounting estimate, such a question shall be referred to the Board for decision.*

7. *For the purposes of paragraphs (1) to (6), the expressions:*

(a) *"Accounting estimate" means an estimate made for the purpose of preparation of financial statements which is based on the circumstances existing at the time when the financial statements are prepared;*

(b) *"Accounting policies" means the specific accounting principles and the method of applying those principles adopted by the assessee in the preparation and presentation of financial statements;*

(c) *"Extraordinary items" means gains or losses which arise from events or transactions which are distinct from the ordinary activities of the business and which are both material and expected not to recur frequently or regularly. Extraordinary items include material adjustments necessitated by circumstances which though related to the years preceding the previous years are determined in the previous year;*

*Provided that income or expenses arising from the ordinary activities of the business or profession or vocation of an assessee, though abnormal in amount or infrequent in occurrence, shall not qualify as extraordinary items;*

(d) *"Financial statements" means any statement to provide information about the financial position, performance and changes in the financial position of an assessee and includes balance sheet, profit and loss account and other statements and explanatory notes forming part thereof;*

(e) *"Prior period items" means material charges or credits which arise in the previous year as a result of errors or*

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*omissions in the preparation of the financial statements of one or more previous years.*

*Provided that the charge or credit arising on the outcome of a contingency, which at the time of occurrence could not be estimated accurately shall not constitute the correction of an error but a change in estimate and such an item shall not be treated as a prior period item.*

10.22 The above Accounting Standards are to be followed by all assessees following mercantile system of accounting. Therefore, it is clear that those assessees who are following cash system of accounting need not follow the Accounting Standards notified above.

### 10.23 Implications of non-compliance with the AS and AS (IT)

As mentioned earlier, AS are applicable to tax audit also when the tax auditor performs the attest function, i.e., report on whether the accounts are true and fair. Therefore, in case of non-compliance with the AS, the chartered accountant should make appropriate qualifications/ disclosures in the audit report. However, such qualifications/disclosures may or may not have any impact on the computation of total income for the purpose of the Act. Similarly, section 145 provides that the AS (IT) notified under that section should be followed by the assessees to whom they are made applicable. It should be noted that the tax auditor auditing accounts under section 44AB is not computing the income but is - (a) reporting on accounts, and (b) reporting on the relevant information furnished in Form No. 3CD. Form No. 3CD vide clause 11(d) requires reporting of the details of deviation, if any, in the method of accounting employed in the previous year from accounting standards prescribed under section 145 and the effect thereof on the profit or loss. Further, it may be noted that there is no material difference between AS (IT)-1 and AS (IT)-2 notified by the Government and the corresponding AS-1 and AS-5 of the ICAI respectively.

## 11. Audit Procedures

11.1 In the case of an audit, 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

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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 should use his professional judgment to apply the technique of audit sampling in accordance with the principles enunciated in SA 530 (Revised) *"Audit Sampling"* depending on the nature and volume of transactions, the materiality involved and the internal control procedures followed by the assessee. He would also be well advised to refer to the other Standards on Auditing (SAs) as may be relevant, 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.

11.2 Section 227/143 of the Companies Act 1956/2013 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*. The Standard requires an auditor to establish whether the pre-conditions for an audit are present so as to accept or continue an audit engagement. As per para 6(b) (iii) the auditor is required to obtain agreement of management that it acknowledges and understands its responsibilities to provide the auditor with (a) access to all information of which the management is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters, (b) additional information that the auditor may request the management for the purpose of the audit and (c) unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence. 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 in relation to the reporting requirement under section 44AB, the tax auditor should see the impact thereof from the perspective of "management integrity" vis-a-vis overall assessment of risk of misstatements in accordance with under SA 315, *Identifying and Assessing the risks of material misstatement through understanding the entity and its environment* and consequently on his/her opinion for reporting in clause (3) of Form No.3CA or Clause (5) of Form No. 3CB as the case may be.

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11.3 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 necessary working papers about the evidence on which he has relied upon while conducting the audit and also maintain all his necessary working papers. Such working papers should include his notes on the following, amongst other matters:

- (a) work done while conducting the audit and by whom;
- (b) explanations and information given to him during the course of the audit and by whom;
- (c) decision on the various points taken;
- (d) the judicial pronouncements relied upon by him while making the audit report; and
- (e) certificates issued by the client/management letters.

11.4 The requirements of documentation are applicable in respect of tax audit conducted by chartered accountants. For this purpose attention is also invited to SA 230, *Audit Documentation*, which provides that the tax auditor should prepare documentation that provides a sufficient and appropriate record of the basis for the auditor's report and evidence that the audit was planned and performed in accordance with SA's and applicable legal and regulatory requirements..

11.5 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'. 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.

11.6 Just in case of the conduct of a statutory audit for the purpose of expression of the auditor's opinion as to whether the financial statements

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depict a 'true and fair' view, the statutory auditor applies audit sampling, in case of tax audits also the tax auditor may apply audit sampling techniques as prescribed in SA 530, *Audit Sampling* on the information provided by the assessee to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion.. 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.

11.7 Where the assessee has been subjected to an internal audit and the tax auditor decides to use the work of the internal auditor for the purpose of the tax audit under section 44AB, the latter's procedures would be guided by the principles laid down in Standard on Auditing (SA) 610, *Using the Work of Internal Auditors*.

11.8 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/observation\* 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,

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notwithstanding the fact that such disclosures are required to be made in Form No.3CD.

\* Attention of the members is invited to the principles laid out in SA 705, *Modifications to the Opinion in the Independent Auditor's Report*.

11.9 The ICAI had pursuant to the issuance of the Revised SA 700, *Forming an Opinion and Reporting on Financial Statements*, prescribed a revised format of the auditor's report on financial statements, which has been made effective in respect of audits of financial statements for periods beginning on or after 1st April 2012. Since Form No. 3CA and Form No. 3CB are required to be filed online in a preset form and the same are not in line with the requirements of SA 700, there is no specifically allocated field for providing information relating to the respective responsibilities of the assessee and the tax auditor as required in terms of the principles laid out in SA 700. However, having regard to the importance of these respective responsibility paragraphs from the perspective of the readers of the tax audit report, it is suggested that these respective responsibility paragraphs relating can be provided in the space provided for giving observations, etc., under clause (3) of Form No.3CA or Clause (5) of Form No.3CB as the case may be.

11.10 The illustrative Assessee's responsibility paragraph and Tax Auditor's responsibility paragraphs in respect of Form No.3CB are given hereunder. The same may be suitably reworded to meet the situation envisaged in Form No.3CA.

#### ***"Assessee's Responsibility for the Financial Statements and the Statement of Particulars in Form 3CD***

1. *The assessee is responsible for the preparation of the aforesaid financial statements that give a true and fair view of the financial position and financial performance (if applicable) in accordance with the applicable Accounting Standards issued by the Institute of Chartered Accountants of India<sup>2</sup>. This responsibility includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of the financial statements that give a true and fair view and are free from material misstatement, whether due to fraud or error.*
2. *The assessee is also responsible for the preparation of the statement of particulars required to be furnished under section 44AB of the*

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<sup>2</sup> (in case of the assessee being a Company, the reference would be to the Accounting Standards referred to in sub-section (3C) of section 211 of the Companies Act, 1956/ section 133 of the Companies Act, 2013)



### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

*Income-tax Act, 1961 annexed herewith in Form No. 3CD read with Rule 6G(1)(b) of Income Tax Rules, 1962 that give true and correct particulars as per the provisions of the Income-tax Act, 1961 read with Rules, Notifications, circulars etc that are to be included in the Statement.*

#### **Tax Auditor's Responsibility**

3. *My/ Our responsibility is to express an opinion on these financial statements based on my/our audit. I/We have conducted this audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.*
4. *An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances but not for the purposes of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.*
5. *I/We believe that the audit evidence I/we have obtained is sufficient and appropriate to provide a basis for my/our audit opinion.*
6. *I/We are also responsible for verifying the statement of particulars required to be furnished under section 44AB of the Income-tax Act, 1961 annexed herewith in Form No. 3CD read with Rule 6G (1) (b) of Income-tax Rules, 1962. I/ We have conducted my/our verification of the statement in accordance with Guidance Note on Tax Audit under section 44AB of the Income-tax Act, 1961, issued by the Institute of Chartered Accountants of India."*

11.11 In this regard, attention of the members is also invited to the Announcement regarding "Applicability of SA 700, forming an opinion and

## **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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reporting on financial statements, to formats of auditor's reports prescribed under various laws and/ or regulations" (22.08.2013), issued by ICAI, given in *Appendix IX (Page No. 266)*.

### **12. Professional misconduct**

12.1 It may be noted that when any question relating to professional misconduct in connection with tax audit arises, the tax auditor would be liable under the Chartered Accountants Act and the ICAI's disciplinary jurisdiction will prevail in this regard.

### **13. Audit Report**

13.1 Section 44AB requires the tax auditor to submit the audit report in the prescribed form and setting forth the prescribed particulars. Sub-rule (1) of Rule 6G provides that the report of audit of accounts of a person required to be furnished under section 44AB shall -

- (a) in the case of a person who carries on business or profession and who is required by or under any other law to get his accounts audited, be in Form No. 3CA;
- (b) in the case of a person who carries on business or profession, but not being a person referred to in clause (a), in Form No. 3CB.

13.2 Sub-rule (2) of Rule 6G further provides that the particulars which are required to be furnished under section 44AB shall be in Form No. 3CD.

13.3 It may be noted that the audit report in Form No.3CB is in two parts. The first part requires the tax auditor to give his opinion as to whether or not the accounts audited by him give a true and fair view:

- (i) in the case of the balance sheet, of the state of affairs as at the last date of the accounting year.
- (ii) in the case of the profit and loss account, of the profit or loss of the assessee for the relevant accounting year.

13.4 The second part of the report states that the statement of particulars required to be furnished under section 44AB is annexed to the audit report in Form No. 3CD. The tax auditor is required to give his opinion whether the prescribed particulars furnished by the assessee are true and correct, subject to observations and qualifications, if any.

13.5 In paragraph 3 of Form No. 3CB the auditor has to report that the financial statements audited by him give a 'true and fair' view. With regard to the term "true and fair view" the auditor is advised to consider in the

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Framework for Preparation and Presentation of Financial Statements as also paragraph 12, 13, 14 and 27 of SA 700 (Revised), *Forming an opinion and reporting on Financial Statements*. Attention of the members is drawn to Para 5 of SA 200, *Overall Objectives of the Independent Auditor* reproduced below:

*"5. As the basis for the auditor's opinion, SAs require the auditor to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. Reasonable assurance is a high level of assurance. It is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (i.e., the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive."*

13.6 The requirement in paragraph 3 of Form No.3CA and paragraph 5 of Form No.3CB relating to particulars in Form No.3CD is that the auditor should report that these particulars in Form No.3CD are "true and correct". The terminology "true and fair" is widely understood though not defined even under the Companies Act, 1956/2013. On the other hand, the words "true and correct" lay emphasis on factual accuracy of the information. In this context reference is invited to AS-1 and AS(IT)-I relating to disclosure of accounting policies. These standards recognise that the major considerations governing the selection and application of accounting policies are (i) prudence, (ii) substance over form and (iii) materiality. Therefore, while giving particulars in Form No.3CD these aspects should be kept in view. In particular, considering the nature of particulars to be given in Form No.3CD, the aspect of materiality should be considered. In other words, particulars should be given in the respect of material items and the auditors should assess factual correctness relating to these particulars. Attention of the members, in this context is, however, also drawn to Para 51 of "Framework for Assurance Engagements" reproduced below:

*"51. "Reasonable assurance" is less than absolute assurance. Reducing assurance engagement risk to zero is very rarely attainable or cost beneficial as a result of factors such as the following:*

➤ *The use of selective testing.*

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- *The inherent limitations of internal control.*
- *The fact that much of the evidence available to the practitioner is persuasive rather than conclusive.*
- *The use of judgment in gathering and evaluating evidence and forming conclusions based on that evidence.*
- *In some cases, the characteristics of the subject matter when evaluated or measured against the identified criteria."*

13.7 In the case of a person whose accounts of the business or profession have been audited under any other law, it is not required for the tax auditor appointed under section 44AB to give his opinion, as to whether or not the accounts give a true and fair view as indicated herein above. It would only be necessary for him to annex a copy of the audited accounts as well as a copy of the audit report given by the statutory auditor with his report in Form No. 3CA along with Form No.3CD.

13.8 In the case of a person who carries on business and also renders professional services but who is not required by or under any other law to get his accounts audited, report should be given in Form No. 3CB. The statement of particulars should be given in Form No. 3CD.

13.9 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 expression "proper books of account" should mean, the books of original entry and other books of account required to be maintained to record all the transactions of the assessee in the same manner, as in the case of a person whose accounts of the business or profession have been audited under any other law. Although, books of account have not yet been prescribed for a person who carries on business or profession (except under Section 44AA for certain categories of profession), the tax auditor should examine whether such books are maintained by the assessee to provide the information and the basis required to prepare the balance sheet and the profit and loss account correctly in the formats recommended in **Appendices XV (Page no. 278) and XVI (Page no. 286)** of this Guidance Note.

13.10 In case the accounts of a person who carries on business or profession are being audited for the first time, the tax auditor should ensure compliance with SA 510 (Revised), *Initial Audit Engagements- Opening Balance*.

13.11 In certain cases, members are called upon to report on the accounts reopened and revised by the board of directors. The accounts of a company once adopted at its annual general meeting should not normally be re-

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opened and revised. The Institute and the Ministry of Corporate Affairs have affirmed this position. In case of revision, the audit report should be given in the manner as required by the Institute in SA-560 (Revised), *Subsequent Events*. The Ministry of Corporate Affairs had also clarified that accounts can be revised to comply with technical requirements. It may be pointed out that report under section 44AB should not normally be revised. However, sometimes a member may be required to revise his tax audit report on grounds such as:

- (i) revision of accounts of a company after its adoption in annual general meeting.
- (ii) change of law e.g., retrospective amendment.
- (iii) change in interpretation, e.g. CBDT Circular, judgements, etc.

13.12 In case where a member is called upon to report on the revised accounts, then he must mention in the revised report that the said report is a revised report and a reference should be made to the earlier report also. In the revised report, reasons for revising the report should also be mentioned.

13.13 In the case of companies having their accounting year which is different from the financial year, accounts of the financial year are required to be prepared and audited. The audit report shall be in Form 3CB. The above position has also been clarified by the CBDT in its Circular No, 561 dated 22.5.1990. The Circular is reproduced in **Appendix X (Page no 268)**.

## 14. Form No. 3CA

14.1 This form is to be used in a case where the accounts of the business or profession of a person have been audited under any other law. The first part of the report refers to the fact that the statutory audit of the assessee was conducted by a chartered accountant or any other auditor in pursuance of the provisions of the relevant Act, and the copy of the audit report along with the audited profit and loss account and balance sheet and the documents declared by the relevant Act to be part of or annexed to the profit and loss account and balance sheet, are annexed to the report in Form No. 3CA. In a case where the tax auditor carrying out the audit under section 44AB is different from the statutory auditor, a reference should be made to the name of such statutory auditor. In case the statutory auditor is carrying out the audit under section 44AB, the fact that he has carried out the statutory audit under the relevant Act should be stated. Attention of the members in this context is invited to SA 600 *Using the work of Another Auditor*.

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14.2 The next paragraph states that the statement of particulars required to be furnished under section 44AB is annexed with the particulars in Form No. 3CD. The tax auditor has to further state that, in his opinion and to the best of his information and according to examination of books of account including other relevant documents and explanations given to him, the particulars given in the said Form No.3CD and the annexure thereto are true and correct subject to the observations/qualifications, if any.

14.3 The auditor is required to examine not only the books of accounts but also other relevant documents directly related to transactions reflected in the books of accounts like original purchase invoice, copy of bank statements, bills, vouchers, various agreements/ contracts or any other document on the basis of which preliminary entries are passed in the books of accounts.

14.4 Attention is also drawn to the definition of 'document' as per section 2(22AA) of the Act which is as under:

*"document" includes an electronic record as defined in clause (t) of sub-section (1) of section 2 of the Information Technology Act, 2000 (21 of 2000).*

Section 2(1)(t) of the Information Technology Act, 2000 as referred above is reproduced below:

*"electronic record" means data, record or data generated, image or sound stored, received or sent in an electronic form or micro film or computer generated micro fiche.*

The definition of term "document" is an inclusive definition and includes within its ambit documents other than those considered as electronic record as per section 2(1)(t) of the Information Technology Act, 2000. The above definition can also be relied when reporting under clause 11(c) of Form No. 3CD discussed later in this Guidance Note.

14.5 Where any of the requirements in this form is answered in negative or with qualification, the report shall state the reasons thereof. The tax auditor should state this qualification in the audit report so that the same becomes a comprehensive report and the user of the audited statement of particulars can realize the impact of such qualifications.

14.6 It is possible that in the case of a person whose accounts of the business or profession have been audited under any other law, which has branches at various places, the branch accounts might have been audited by branch auditors under the statute. If the audit under section 44AB is also carried out by the same branch auditors or other chartered accountants, they

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should submit the report in Form No. 3CA to the management or the principal tax auditor appointed for the head office under Section 44AB. Attention in this regard is drawn to SA 600, *Using the Work of Another Auditor* which discusses the procedures in this regard as well as the principal tax auditor's responsibility in relation to his use of the work of the branch auditor. The principal tax auditor should submit his consolidated report on the registered office/head office and branch accounts and report in his tax audit report as his observation in paragraph 3 of Form No. 3CA as under:

*"I/We have taken into consideration the audit report and the audited statements of accounts, and particulars received from the auditors, duly appointed under the relevant law, of the branches not audited by me/us".*

14.7 Item No. 4 of the notes to Form No. 3CA requires that the person, who signs this audit report, shall indicate reference of his membership No./certificate of practice number/authority under which he is entitled to sign this report. No separate certificate of practice number is allotted by ICAI. As such, where a chartered accountant acts as a tax auditor he should give his membership number with ICAI while registering himself in the e-filing portal. In case, the e-filing utility of Form No. 3CA requires the mention of the Firm Registration number and the name of the firm on whose behalf the member has conducted audit, the same should invariably be provided by the tax auditor.

14.8 An assessee may have one or more branches outside India. The accounts of such branches are normally audited by the professional accountants overseas. The results of such branches are also incorporated in the consolidated accounts prepared in this country. In the case of foreign branches, the relevant information in respect of such branches as is required by Form No. 3CD, may be obtained by the tax auditor in India from the assessee who should obtain the same from the overseas auditor who had audited the accounts of such foreign branches. The tax auditor in India while certifying the information in Form No. 3CD may rely upon the information obtained by him from the overseas auditor and while submitting his consolidated report in Form No. 3CD, he should specifically point out the following in his audit report in paragraph 3 of Form No. 3CA as his observation:-

*"I/We have taken into consideration the audit report and the audited statements of accounts, and particulars received from the auditors, appointed under the relevant law, of the overseas branches not audited by me/us".*

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If the assessee is unable to obtain relevant information in respect of the overseas branches duly certified by the overseas auditor, the relevant facts should be suitably disclosed and reported upon.

14.9 Where the tax auditor is unable to obtain the required information in respect of branches situated in India or outside India then the fact should be suitably disclosed along with its impact on the Auditor's opinion on the particulars furnished in Form No.3CD, as an observation in clause (3) of Form No. 3CA. Reference is drawn to SA 705, *Modifications to the opinion in the Independent Auditor's report*.

## 15. Form No. 3CB

15.1 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 audit report has to be given in Form No. 3CB. Form No. 3CB consists of five paragraphs.

15.2 The tax auditor has to state whether he has examined the balance sheet as on a particular relevant date and the profit and loss account/income and expenditure account for that period. Further, such a balance sheet and the profit and loss account must be attached with the audit report.

15.3 The tax auditor has to certify that the balance sheet and the profit and loss account/income and expenditure account are in agreement with the books of account maintained at the head office and branches. Also, he has to mention the total number of branches.

15.4 He has to report his observations, comments, discrepancies or inconsistencies, if any. Subject to the above observations, comments, discrepancies, inconsistencies he has to state whether:

- (a) he has obtained all the information and explanations which, to the best of his knowledge and belief, were necessary for the purposes of the audit;
- (b) in his opinion proper books of account have been kept by the head office and branches of the assessee so far as appears from his examination of the books;
- (c) in his opinion and to the best of his information and according to the explanations given to him the said accounts, read with notes thereon, if any, give a true and fair view;
  - (i) in the case of the balance sheet of the state of the affairs of the assessee as at 31st March, \_\_\_\_\_ and



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- (ii) in the case of the profit and loss account/income and expenditure account of the profit/loss or surplus/deficit of the assessee for the year ended on that date.

15.5 Under clause (a) of paragraph 3 of Form No.3CB, the tax auditor has to report his "observations/comments/ discrepancies/inconsistencies," if any. The expression "Subject to above" appearing in clause (b) makes it clear that such observations/comments/ discrepancies/ inconsistencies which are of qualificatory nature relate to necessary information and explanations for the purposes of the audit or the keeping of proper books of accounts or the true and fair view of the financial statements, respectively to be reported on in paragraphs (A), (B) and (C) under clause (b) of paragraph 3. While reporting on clause (a) of paragraph 3 of Form No. 3CB the tax auditor should report only such of those observations/comments/ discrepancies/ inconsistencies which are of qualificatory nature which affect his reporting about obtaining all the information and explanations which were necessary for the purposes of the audit, about the keeping of proper books of account by the head office and branches of the assessee and about the true and fair view of the financial statements. Further, only such observations/comments/ discrepancies/inconsistencies which are of a qualificatory nature should be mentioned under clause (a). Any other observations/comments/ discrepancies/inconsistencies, which do not affect the reporting on the matters specified above may form part of the notes to accounts forming part of the accounts. In case the tax auditor has no observations/comments/ discrepancies/inconsistencies to report which are of qualificatory nature, "NIL" should be reported in this part of paragraph 3. The tax auditor may then give his report as required by sub-paragraphs (A), (B), and (C) of paragraph 3 and paragraph 4.

15.6 Paragraph 4 of Form No.3CB provides that the prescribed particulars are furnished in Form No.3CD annexed to the report. Paragraph 5 of Form No.3CB requires the auditor to report whether in his opinion and to the best of his information and according to the explanations given to him, the particulars given in Form No.3CD are true and correct subject to observations/qualifications, if any. The auditor may have a difference of opinion with regard to the particulars furnished by the assessee and he has to bring these differences under various clauses in Form No.3CD. The auditor should make a specific reference to those clauses in Form No.3CD in which he has expressed his reservations, difference of opinion, disclaimer etc. in this paragraph.

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15.7 If a person who carries on business or profession but who is not required by or under any other law to get his accounts audited, has branches and separate accounts are maintained at the branches, the assessee can request the tax auditor appointed under section 44AB to audit the head office and branch accounts. In the alternative, the assessee can appoint separate tax auditors for branches. The branch tax auditor in such a case will have to give an audit report in Form No. 3CB to the management or the tax auditor appointed for the audit of head office accounts. The tax auditor appointed for the audit of head office can rely on the report of branch tax auditors subject to such checks and verifications as he may choose to make and shall submit his consolidated report on the head office and branch accounts. He should make suitable reference to the audit conducted by separate branch tax auditors in the same manner as stated in para 14.6 above.

15.8 If the tax auditor is called upon to give his report only in respect of one or more businesses carried on by the assessee and the books of accounts of the other businesses are not produced as the same are not required to be audited under the Act, the tax auditor should mention the fact that audit has not been conducted of those businesses whose books of account had not been produced. However, if the financial statements include, *inter alia*, the results of such business for which books of account have not been produced, the auditor should qualify his report in Form No. 3CB.

## 16. Form No. 3CD

16.1 The statement of particulars given in Form No. 3CD as annexure to the audit report contains forty one clauses. The tax auditor has to report whether the particulars are true and correct. This Form is a statement of particulars required to be furnished under section 44AB. The same is to be annexed to the reports in Forms No. 3CA and 3CB in respect of a person who carries on business or profession and whose accounts have been audited under any other law and in respect of person who carries on business or profession but who is not required by or under any other law to get his accounts audited respectively.

16.2 As stated earlier, the tax auditor should obtain from the assessee, the statement of particulars in Form No. 3CD duly authenticated by him. It would be advisable for the assessee to take into consideration the following general principles while preparing the statement of particulars:

- (a) He can rely upon the judicial pronouncements while taking any particular view about inclusion or exclusion of any items in the particulars to be furnished under any of the clauses specified in Form No.3CD.

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- (b) If there is a conflict of judicial opinion on any particular issue, he may refer to the view which has been followed while giving the particulars under any specified clause.
- (c) The AS, Guidance Notes, SA issued by the Institute from time to time should be followed.

16.3 While furnishing the particulars in Form No.3CD it would be advisable for the tax auditor to consider the following:

- (a) If a particular item of income/expenditure is covered in more than one of the specified clauses in the statement of particulars, care should be taken to make a suitable cross reference to such items at the appropriate places.
- (b) If there is any difference in the opinion of the tax auditor and that of the assessee in respect of any information furnished in Form No. 3CD, the tax auditor should state both the view points and also the relevant information in order to enable the tax authority to take a decision in the matter.
- (c) If any particular clause in Form No.3CD is not applicable, he should state that the same is not applicable.
- (d) In computing the allowance or disallowance, he should keep in view the law applicable in the relevant year, even though the form of audit report may not have been amended to bring it in conformity with the amended law.
- (e) In case the prescribed particulars are given in part or piecemeal to the tax auditor or relevant form is incomplete and the assessee does not give the information against all or any of the clauses, the auditor should not withhold the entire audit report. In such a case, he can qualify his report on matters in respect of which information is not furnished to him. In the absence of relevant information, the tax auditor would have no option but to state in his report that the relevant information has not been furnished by the assessee.
- (f) The information in Form No.3CD should be based on the books of accounts, records, documents, information and explanations made available to the tax auditor for his examination.
- (g) In case the auditor relies on a judicial pronouncement, he may mention the fact as his observations in clause (3) of Form No.3CA or clause (5) provided in Form No.3CB, as the case may be

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**17. Particulars to be furnished in Form No.3CD.****PART – A**

1. Name of the assessee : \_\_\_\_\_
2. Address : \_\_\_\_\_
3. Permanent Account Number : \_\_\_\_\_
4. 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 : \_\_\_\_\_
5. Status : \_\_\_\_\_
6. Previous year : from .....to ....
7. Assessment year : \_\_\_\_\_
8. Indicate the relevant clause of section 44AB under which the audit has been Conducted : \_\_\_\_\_

**[Clauses 1 to 8]**

The requirements of clauses 1 to 8 of Part-A are discussed as follows:

17.1 Under clause (1) the name of the assessee whose accounts are being audited under section 44AB should be given. However, if the tax audit is in respect of a branch, name of such branch should be mentioned along with the name of the assessee.

17.2 The address to be mentioned under clause (2) should be the same as has been communicated by the assessee to the Income-tax Department for assessment purposes as on the date of signing of the audit report. If the tax audit is in respect of a branch or a unit, the address of the branch or the unit should be given. In the case of a company, the address of the registered office should also be stated. In the case of a new assessee, the address should be that of the principal place of business.

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17.3 Under clause (3) the permanent account number (PAN) allotted to the assessee should be indicated. It may be noted that in the e-filing format PAN is a mandatory field.

17.4 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.

17.5 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.

17.6 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.

17.7 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.

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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17.8 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.

17.9 Under clause (5) the status of the assessee is to be mentioned. Obviously this refers to the different classes of assessee included in the definition of "person" in section 2 (31) of the Act, namely, individual, Hindu undivided family, company, firm, an association of persons or a body of individuals whether incorporated or not, a local authority or artificial juridical person.

17.10 Under clause (6) the period of the previous year has to be stated. Since the previous year under the Act now uniformly begins on 1<sup>st</sup> April and ends on 31<sup>st</sup> 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 judgement depending on the facts and circumstances of the same.

17.11 Under clause (7) the assessment year relevant to the previous year for which the accounts are being audited should be mentioned.

17.12 Under clause (8) the auditor is required to mention the relevant clause of section 44AB under which the audit has been conducted. In case the assessee is carrying on business and his total sales, turnover or gross receipts as the case may be, exceeds one crore in the relevant previous year, the auditor is required to mention clause (a) under this head. If the assessee is carrying on profession and his gross receipts exceed twenty five lakh rupees in the relevant previous year, the auditor is required to mention clause (b) under this head. Likewise, if the audit under section 44AB is being conducted by virtue of provisions of section 44AE, 44BB and 44BBB, the auditor is required to mention clause (c). For audit being conducted by virtue of provisions of section 44AD, clause (d) is to be mentioned under this head.

18. (a) If firm or Association of Persons, indicate names of partners/members and their profit sharing ratios.
- (b) If there is any change in the partners or members or in their profit sharing ratio since the last date of the preceding year, the particulars of such change

[Clause 9(a) and (b)]

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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18.1 Where the assessee is a firm or association of persons (AOP) or body of individuals, the names of partners of the firm or members of the association of persons or body of individuals and their profit sharing ratios (%) have to be stated. In case where the partner of a firm or the member of AOP/ BOI acts in a representative capacity, the name of the beneficial partner/member should be stated. Thus, the details of partners or members during the entire previous year will have to be furnished. The term "profit sharing ratios" would include loss-sharing ratio also since loss is nothing but negative profits. This would not cover any specific ratio or understanding in relation to payment of remuneration or interest to partners or members. In this connection, reference may be made to Circular No.739 dated 25.3.1996 issued by the Board reproduced in *Appendix XI (Page no. 269)*.

18.2 If there is any change in the partners of the firm or members of the association of persons/ body of individuals or their profit or loss sharing ratio since the last date of the preceding year, the particulars of such change must be stated. All the changes occurring during the entire previous year must be stated.

18.3 The particulars in this clause should be verified from the instrument or agreement or any other document evidencing partnership or association of persons including any supplementary documents or other documents effecting such changes. For this purpose, the tax auditor may also verify:

- (i) in case of registered firms (including Indian LLPs), whether the relevant documents have been filed with the concerned authorities,
- (ii) whether notice of changes, if required, has been given to the registrar of firms, and
- (iii) any minutes or any other understanding recording any changes in the partners/members or their profit sharing ratios.

18.4 The tax auditor should obtain certified copies of the deeds, documents, understanding, notice of changes etc. including certified copies of the acknowledgment, if any, evidencing filing of documents with the concerned authorities, if registered.

18.5 In certain cases of association of persons or body of individuals, it may be possible that the shares of the members are not precisely ascertainable during the previous year resulting in a situation whereby the shares of the members are indeterminate or unknown. In such circumstances, the relevant fact should be stated.

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18.6 As per section 2(23) of the Income-tax Act, 1961 the term "Firm" shall have the meaning assigned to it in the Indian Partnership Act, 1932, and shall include a Limited Liability partnership firm as defined in Limited Liability Partnership Act, 2008.

19. (a) **Nature of business or profession (if more than one business or profession is carried on during the previous year, nature of every business or profession)**
- (b) **If there is any change in the nature of business or profession, the particulars of such change.**

**[Clause 10 (a) and (b)]**

19.1 In regard to the nature of business, the principal line of each business is to be determined and stated in this clause, i.e. the sector in which the business or profession falls such as manufacturing, trading, commission agent, builder, contractor, professionals, service sector, financial service sector or entertainment industry. In case of a person belongs to service sector the nature of each type of service should be broadly stated. Thereafter, the auditor is required to mention the sub-sector pertaining to the sector selected.

19.2 . Information has to be furnished in respect of each business. The code to be mentioned against the nature of business pertains to the main area of business activity.

19.3 Any material change in the nature of business should be precisely set out. The change will include change from manufacturer to trader as well as change in the principal line of business. For example, an assessee switching over from wholesale business to retail business or an assessee switching over from manufacturing his own commodities to manufacturing goods on job basis for others. Likewise, any addition to or permanent discontinuance of, a particular line of business may also amount to change requiring reporting. However, temporary suspension of the business may not amount to change and therefore need not be reported.

19.4 A review of business report or the minutes of meetings would enable the tax auditor to note the changes, if any. Based thereon, he may make necessary enquiries and seek information and determine whether any change has occurred or not. If need be, the tax auditor should get a declaration from the assessee regarding change in the nature of business, if any.



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19.5 In the case of business reorganization/ reconstruction if there is a similar line of activity, no reference needs to be made. However, if a new line of activity emerges because of business reorganization/ reconstruction, the same may be stated. In the case of restructuring, if any line of activity is being hived off, the same may also be reported.

19.6 The auditor should keep in mind the above guidance while furnishing information under this clause in the format provided for in the e-filing utility

**20. (a) Whether books of account are prescribed under section 44AA, if yes, list of books so prescribed.**

**(b) List of books of account maintained and the address at which the books of account are kept .**

(In case books of account are maintained in a computer system, mention the books of account generated by such computer system. If the books of accounts are not kept at one location, please furnish the addresses of locations along with the details of books of accounts maintained at each location.)

**(c) List of books of account and nature of relevant documents examined.**

**[Clause 11 (a) to (c)]**

20.1 The list of books of accounts prescribed, maintained and examined has to be stated under this clause. There may be difference between the three lists. For example, books of accounts may have been prescribed but all the prescribed books might not have been maintained or the entire books of accounts maintained might not have been produced for examination. The tax auditor should exercise his professional judgment in order to arrive at the conclusion whether such a situation warrants any disclosure or qualifications while forming his opinion on the matters covered by reporting requirements in Form No.3CB.

20.2 The CBDT under Rule 6F has prescribed the books of account and other documents to be kept and maintained by a person carrying on certain professions specified in sub-section (1) of section 44AA. As such, every person carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or authorised representative or film artist and whose total gross receipts exceed one lakh fifty thousand rupees in all the three years immediately preceding the previous year, or where the profession has been newly set up in the previous year, his total gross receipts in the profession for that year

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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are likely to exceed the said amount, is required to maintain the following books of account:

1. Cash book.
2. Journal, if the accounts are maintained according to the mercantile system of accounting.
3. Ledger.

Apart from the aforesaid books of account, a person carrying on medical profession is required to keep the following:

- (a) daily case register in Form No.3C showing data, patient's name, nature of professional services rendered, fees received and date of receipt; and
- (b) an inventory under broad heads, as on the first and the last days of the previous year, of the stock of drugs, medicines and other consumable accessories used for the purpose of his profession.

20.3 In the case of a person for whom the books of account have been prescribed under rule 6F, the list of books so prescribed have to be stated under clause 11(a). It may be noted that the daily case register and the inventory under broad heads do not constitute books of account and hence the same need not be mentioned under clause 11(a). Sometimes an assessee may carry on multiple activities. Books of account might have been prescribed for one of the activities. In that case, mention may be made of the activity for which books have been prescribed.

20.4 The tax auditor should obtain from the assessee a complete list of books of account and other documents maintained by him (both financial and non-financial records) and make appropriate marks of identification to ensure the identification of the books and records produced before him for audit. The list of books of account maintained by the assessee should be given under clause 11(b).

20.5 Section 44AA(2) provides that persons carrying on business or profession, other than those specified in sub-section (1), shall keep and maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act, if his income from business or profession exceeds the monetary limits prescribed under section 44AA(2) or his total sales, turnover or gross receipts in business or profession exceed the monetary limits prescribed under section 44AA(2) in any one of the three years immediately preceding the previous year. The tax auditor will,

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therefore, have to verify that the assessee has maintained such books of accounts and documents as may enable the Assessing Officer to compute the total income of the assessee in accordance with the provisions of the Act. It may be noted that though the Central Board of Direct Taxes has been empowered under sub-section (3) of section 44AA to prescribe books of account to be maintained under sub-section (2), so far no books of accounts have been prescribed.

20.6 For a person whose accounts of the business or profession have been audited under any other law, the requirement for maintenance of books of account is contained in the relevant statutes. In the case of other assessee, normal books of account to be maintained will be cash book/bank book, sales/purchase journal or register and ledger. Assessee engaged in trading/manufacturing activities should also maintain quantitative details of principal items of stores, raw materials and finished goods. While giving his report in Form No. 3CB about maintenance of proper books of account, the tax auditor should ensure that they are maintained in accordance with the above requirements. In case where stock records are not properly maintained by the assessee due to the nature, level, volume and variety of items/ transactions, the tax auditor will have to consider the concept of materiality and practicality while giving particulars in Form No. 3CD.

20.7 (a) As per section 2(12A) of the Income-tax Act, 1961, "books or books of account" includes ledgers, day-books, cash books, account-books and other books, whether kept in the written form or as print-outs of data stored in a floppy, disc, tape or any other form of electro-magnetic data storage device. As to the requirement regarding the mentioning of the books of accounts generated by the computer system, the tax auditor should obtain a list of books of account which are generated by the computer system. The list given by the assessee can be verified from the printout of such books obtained from the assessee. Only such books of account and other records which properly come within the scope of the expression "proper books of account" should be mentioned.

(b) It may be noted that section 4 of the Information Technology Act, 2000 states that "Where any law provides that information or any other matter shall be in writing or in the typewritten or printed form, then, notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied if such information or matter is-

- (i) rendered or made available in an electronic form; and
- (ii) accessible so as to be usable for a subsequent reference."

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20.8 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. The auditor is advised to obtain from the assessee a list in the following format and accordingly report the same in clause 11(b). In case of a company assessee auditor should also verify as to whether any forms are filed under the Companies Act for maintenance of books of accounts at a place other than the registered office:

Sr No.	Principal place of maintenance of books of accounts	Details of books maintained
1	2	3

20.9 In case, where books of accounts are maintained and generated through computer system, the auditor should obtain from the assessee the details of address of the place where the server is located or the principal place of business/Head office or registered office by whatever name called and mention the same accordingly in clause 11(b).

20.10 Books of account examined would constitute the books of original entry and the other books of account. In addition to the list of books of accounts examined, the auditor is required to mention the nature of relevant documents examined also. Since the assessee is required to maintain evidence such as bills, vouchers, receipts, debit note, credit note, inventory register, agreements, orders etc., the auditor generally examines these documents while conducting audit. The underlying documents would differ from assessee to assessee depending on the nature of activity carried on by the assessee. Reference to such supporting evidence/ relevant documents is also required to be made under this clause. Attention is drawn to Para 14.3 and 14.4 for guidance with regard to the term "relevant documents".

**21. 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 Chapter XII-G, First Schedule or any other relevant section).**

[Clause 12]

21.1 Where the profits and gains of the business are assessable to tax under presumptive basis under any of the sections mentioned below, the amount of such profits and gains credited/debited to the profit and loss account should be indicated under this clause:

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S. No.	Section	Business covered
1	44AD	Eligible business
2	44AE	Transport business
3	44B	Shipping business of a non-resident
4	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
5	44BBA	Operation of aircraft by non-resident
6	44BBB	Civil construction etc. in certain turnkey power project by non-residents
7	Chapter XII-G	Special provisions relating to Shipping Companies (Section 115V to 115VT)
8	First Schedule	Insurance Business
9	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

If the profit and loss account does not include profit assessable on presumptive basis, then, there is no requirement to furnish the particulars under this clause.

21.2 The amount to be mentioned under this clause means the amount included in the profit and loss account. The tax auditor is not required to indicate as to whether such amount corresponds to the amount assessable under the relevant section relating to presumptive taxation. As such, the reporting requirement gets satisfied if the amount as per profit and loss account is reported.

21.3 The tax auditor may come across three different situations as follows:

- (a) Where the assessee, maintaining regular books of account has more than one business which include business of the nature assessable on presumptive basis under any of the said sections and the profit and loss account prepared from such books of account, *inter alia*, includes the income of the business assessable under the scheme of presumptive taxation.
- (b) Where the assessee has more than one business including some business(es) falling under any of the aforesaid sections, but maintains

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separate sets of accounts for each such business and opts for getting the accounts of all such businesses audited under section 44AB.

- (c) Where the assessee, having regular books of account for his main business, has some additional business of the nature described in any of the aforesaid sections and no books of account whatsoever is maintained for such additional business but the net income is credited to the main profit & loss account of the assessee.

21.4 Under each of the aforesaid three situations, the tax auditor may proceed as follows:

- (a) This situation may give rise to the problem of apportionment of common expenditure in order to arrive at the correct amount of profit credited to profit and loss account and assessable on a presumptive basis. In such a situation, the endeavour of the tax auditor should be to arrive at a fair and reasonable estimate of such expenditure on the basis of evidence in possession of the assessee or by asking the assessee to prepare such estimate which should be checked by him. It is also necessary to mention the basis of apportionment of common expenditure. However, if the tax auditor is not satisfied with the reasonableness of such apportionment, he should indicate such fact under this clause by a suitable note.
- (b) In this case, since a separate set of accounts are maintained for respective businesses, it poses no problem for the tax auditor in ascertaining the amount of profit to be disclosed.
- (c) Here, the tax auditor is unable to satisfy himself about the correctness of the net income from the presumptive business credited to the profit and loss account. He should, therefore, state the amount of income as appearing in the profit and loss account, with a suitable note expressing his inability to verify the said figure. In the absence of books of account, the tax auditor would be unable to form an opinion about the true and fair view of the profit and loss account or balance sheet of the assessee and therefore, it would become necessary for him to qualify his report in Form No. 3CB.

21.5 In the case of an assessee opting against presumptive taxation, the provisions of section 44AB (c) requires such an assessee to get his accounts audited irrespective of the fact that his turnover has not exceeded the prescribed limit (presently Rs. 1 crore w.e.f A.Y. 2013-14) . There may be another circumstance where an assessee has mixed nature of business amenable to taxation on presumptive basis and under normal provisions of law – turnover of which does not exceed the prescribed limit (presently Rs. 1

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crore w.e.f. A.Y. 2013-14). In such a case, the tax auditor auditing the books of account etc. relating to business covered by the provisions relating to presumptive taxation should sufficiently indicate in his report that his audit report in Form No. 3CB and particulars in Form No.3 CD only relate to the business covered by the provisions relating to presumptive taxation and his audit report does not relate to business assessable under the normal provisions of the Act.

21.6 Even where the assessee opts for presumptive taxation, the tax auditor should impress upon the assessee that it would be advisable to maintain some basic records to support the turnover/gross receipts declared for presumptive taxation.

21.7 Where the profit and loss account includes any profits and gains assessable by virtue of provisions of section 44AE, the auditor should obtain and verify the following information from the assessee:

Sr No.	Nature of vehicle	No. of Vehicles	Month of acquisition in case of vehicle purchased during the relevant previous year	Presumptive income per month	Number of months Owned during the previous year (Part of the month to be rounded off)	Presumptive income for the previous year
1	2	3	4	5	6	7

21.8 In respect of provisions relating to Chapter XII-G, the auditor should obtain and verify the following information from the assessee being a qualifying shipping company:

Sr No.	Name of the Ship	Net tonnage capacity as per DGS certificate	Net tonnage capacity rounded off to nearest 100	Tonnage income per day	No of days operated during the previous year as per DGS Certificate	Tonnage income per year
1	2	3	4	5	6	7

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21.9 The auditor should keep in mind the above guidance while furnishing information under this clause in the format provided in the e-filing utility.

22. (a) **Method of accounting employed in the previous year.**
- (b) **Whether there had been any change in the method of accounting employed vis-a-vis the method employed in the immediately preceding previous year.**
- (c) **If answer to (b) above is in the affirmative, give details of such change, and the effect thereof on the profit or loss.**

Serial number	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)
1	2	3	4

- (d) **Details of deviation, if any, in the method of accounting employed in the previous year from accounting standards prescribed under section 145 and the effect thereof on the profit or loss.**

[Clause 13 (a) to (d)]

22.1 The Finance Act, 1995 amended section 145 with effect from assessment year 1997-98 to provide that the income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" must be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. It has also been provided that the Central Government may notify in the Official Gazette from time to time the accounting standards to be followed by any class of assessee or in respect of any class of income. The hybrid system of accounting viz. mixture of cash and mercantile hitherto allowed to be followed by the assessee was not permitted from assessment year 1997-98 & onwards. However, the assessee may adopt cash system of accounting for one business and mercantile system of accounting for other business. Once the choice of method of accounting is decided, the assessee must follow consistently the method of accounting employed. If he employs different methods for different businesses regularly and consistently, the profits would have to be computed in accordance with the respective methods, provided the result is a proper determination of profits. As regards the accrual system of accounting, the Institute has published a "Guidance Note on Accrual Basis of Accounting" which may be referred to.

22.2 It may be noted that in view of amendment made by the Companies (Amendment) Act, 1988 in section 209 of the Companies Act, 1956 every



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company is required to keep books of account on accrual basis. In other words, a company governed by the Companies Act, 1956 cannot follow cash system of accounting unless exempted under the Companies Act, 1956/2013. The provisions of section 209 (3) of the Companies Act, 1956 are, however, not applicable to entities other than companies. Section 209 has been replaced with the section 128/129 in the Companies Act, 2013 w.e.f.1.4.2014.

22.3 Under sub-clause (b), whether there has been any change in the method of accounting employed vis-à-vis the method employed in the immediately preceding previous year is to be stated. As already noted, an assessee can follow either cash or mercantile system of accounting.

22.4 If there is any change, the effect thereof i.e. increase or decrease in profits has to be stated under this clause. So far as the question of effect of such change on the profit or loss is concerned, the concept of materiality is the basic governing factor. If it is not possible to quantify the effect of the change in the method of accounting, appropriate disclosure should be made under this clause.

22.5 An assessee can follow a number of accounting policies for the purpose of maintaining his books of account. As per AS-1 all significant accounting policies adopted in the preparation and presentation of financial statements shall be disclosed. The disclosure of the significant accounting policies shall form part of the financial statements and the significant accounting policies shall normally be disclosed in one place. Any change in an accounting policy which has a material effect in the previous year or in the years subsequent to the previous year shall be disclosed. The impact of, and the adjustments resulting from such change, if material, shall be shown in the financial statement of the period in which such change is made to reflect the effect of such change.

22.6 As per paragraph 9 under AS(IT) relating to disclosure of prior period and extraordinary items and changes in accounting policies, a change in an accounting policy can be made only if:

- (a) adoption of different policy is required by the statute; or
- (b) the change would result in a more appropriate presentation of the financial statements.

22.7 A change in an accounting policy will not amount to a change in the method of accounting and hence such change in the accounting policy need not be mentioned under sub-clause (b). This is due to the fact that as per the

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requirements of AS-1 and AS (IT)-1 such changes and the impact of such changes will be disclosed in the financial statements. It may be noted that a change in the method of valuation of stock will amount only to a change in an accounting policy and hence such a change need not be mentioned under sub-clause 13(b) but should be mentioned in the financial statements.

22.8 The tax auditor should apply reasonable checks to the earlier year's accounts to ascertain whether there is any change in the method of accounting as compared to that of the year under audit, after obtaining a written confirmation from the assessee as to the method of accounting followed.

22.9 It must also be ascertained as to whether the AS (IT) as may be applicable to the assessee or to the class of income, have been followed. Presently, only two AS (IT) have been prescribed. – AS (IT)-I relating to disclosure of accounting policies and AS (IT)-II relating to disclosure of prior period and extraordinary items and changes in profit and loss account. The tax auditor has to report the details of the deviations in the method of accounting in the previous year from the AS(IT) and the effect thereon on the profit or loss. The tax auditor, while reporting on prior period and extraordinary items should report only such items which fall within the meaning of prior period items and extraordinary items in the relevant AS (IT). Attention is invited to AS (IT)-II, paragraph 10, according to which any change in an accounting policy which has a material effect is required to be disclosed. As stated above, a change in the method of valuation of closing stock would amount to a change in an accounting policy and has to be stated in the financial statements. The tax auditor should ensure that in case the same is not stated in the financial statements, the fact should suitably be stated under clause 13(d). He may rely on the various pronouncements and clarifications made by the ICAI.

22.10 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.

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23. (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, please furnish:

Serial number	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)
1	2	3	4

[Clause 14 (a) and (b)]

23.1 The method of valuation of closing stock is to be stated under this clause. AS-2 "Valuation of Inventories" issued by ICAI requires disclosure of significant accounting policies. Accordingly, a reference may be invited to the same or the method of valuation may be again described in Form No.3CD.

23.2 The method of valuation followed by the assessee having regard to the articles or goods dealt in or manufactured by the assessee, should be clearly indicated. Some examples are given below:

- (i) raw material at cost or net realisable value whichever is lower,
- (ii) finished goods at cost or net realizable value whichever is lower.

23.3 In sub-clause (a) of clause 14 of Form No.3CD, the reference is made to "closing stock". The expression "stock-in-trade" means finished goods and raw materials. Since sub-clause (b) refers to section 145A where the term "inventories" is used, the term "closing stock" will include all items of inventories. AS-2 defines the term "inventories" to include finished goods, raw materials, work-in-progress, materials, maintenance supplies, consumables and loose tools. Therefore, method of valuation of items of inventories will have to be given under sub-clause (a).

23.4 The tax auditor should study the procedure followed by the assessee in taking the inventory of closing stock at the end of the year and the valuation thereof. He should obtain the inventory of closing stock, indicating the basis of valuation thereof, for reporting on the method of valuation of closing stock under this clause.

23.5 The method of stock valuation must be consistently followed from year to year and the method followed must be brought out clearly. The tax auditor should examine the basis adopted for ascertaining the cost and this basis should be consistently followed. It is necessary to ensure that the method followed for valuation of stock results in disclosure of correct profit and gains. The Supreme Court in case of *CIT v. British Paints Ltd. [1991] 188 ITR 44*

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(SC) has held that the method of valuation of stock at actual cost of raw materials and not taking into account overhead charges was not the correct method of valuation even though the said method has been consistently followed. As per AS-2 - Valuation of inventories (Revised) (from accounting year starting from 1.4.1999), historical cost of manufactured inventories can be arrived at on the basis of absorption costing alone and the allocation of fixed costs of inventories should be based on the normal level of production only. It is further provided that overheads should be included as part of the inventory cost only to the extent that they clearly relate to putting the inventories in their present location and condition.

23.6 It is not necessary to indicate any change in the method of valuation of closing stock under this clause. However, as stated earlier in paragraph 22.6, any such change in the method of valuation of closing stock would amount to change in an accounting policy and needs to be disclosed in the financial statements as required by AS-1 and AS(IT).

23.7 The details of deviation, if any, from the method of valuation prescribed under section 145A, and the effect thereof on the profit or loss have to be stated under clause 14(b).

23.8 Section 145A was enacted by the Finance (No.2) Act, 1998 and came into force from A.Y. 1999-2000. This section provides that the valuation of purchase and sale of goods and inventory for the purpose of computation of income from business or profession shall be made on the basis of the method of accounting regularly employed by the assessee but this shall be subject to certain adjustments. Therefore, it is not necessary to change the method of valuation of purchase, sale and inventory regularly employed in the books of account. The adjustments provided in this section can be made while computing the income for the purpose of preparing the return of income. These adjustments are as follows:

- (a) Any tax, duty, cess or fee actually paid or incurred on inputs should be added to the cost of inputs (raw materials, stores etc.) if not already added in the books of account.
- (b) Any tax, duty, cess or fee actually paid or incurred on sale of goods should be added to the sales, if not already added in the books of account.
- (c) Any tax, duty, cess or fee actually paid or incurred on the inventory (finished goods, work-in-progress, raw materials etc.) should be added to the inventories, if not already added while valuing the inventory in the accounts.

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23.9 The statutory adjustments required under section 145A can be explained by the following example.

Particulars	Qty	Rate excluding excise duty	Rate of excise duty
Opening stock	10	10	2
Raw material purchased	90	10	2
Other manufacturing cost	80	10	-
Finished goods manufactured	80	-	-
Sales of finished goods	60	25	3
Closing stock of raw material	20	10	2
Closing stock of finished goods	20	20	3

The input output ratio of raw material to finished goods is 1: 1

23.10 It may be stated that the CENVAT is a procedure whereby manufacturer can utilise credit for input duty against duty payable on final products. Duty credit taken on input is of the nature of set off available against the excise duty payable on the final products. For the accounting periods ending on or before 31<sup>st</sup> March, 1999, the following two alternative methods of treatment of CENVAT credit in the accounts are permissible.

- I. Duty paid on inputs may be debited to a separate account, e.g. CENVAT credit receivable account. As and when the CENVAT credit is actually utilised against payment of excise duty on final products appropriate accounting entries will be required to adjust the excise duty paid out of "CENVAT credit receivable account" to the account maintained for payment/provision for excise duty on final product. In this case, the purchase cost of the inputs would be net of input duty. Therefore, the inputs consumed and the inventory of inputs would be valued on the basis of purchase cost net of input duty. This method is hereinafter referred to as "exclusive method".
- II. In the second alternative, the cost of inputs may be recorded at the total amount paid to the supplier inclusive of input duty. To the extent the CENVAT credit is utilised for payment of excise duty on final products, the amount could be credited to a separate account, i.e. CENVAT credit availed account. Out of the CENVAT credit availed

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account, the amount of CENVAT credit availed in respect of consumption of inputs would be reduced from the total cost of inputs consumed. This method is hereinafter referred to as "inclusive method".

The effect of section 145A is to reflect the figures on "inclusive method".

Following two illustrations explain the above propositions.

The profit & loss account on "exclusive method" would be as under:

Item	Particulars	Unit	Rate	Amount	Amount	Item	Particulars	Unit	Rate	Amount
(a)	Opening Stock	10	10	100		(h)	By sales	60	25	1,500
(b)	Purchase of raw material	90	10	900		(i)	By closing stock of finished goods	20	20	400
	Total	100	10	1000						
(c)	Less closing stock of raw Material	20	10	200						
(d)	Raw material consumed	80	10		800					
(e)	To manufacturing Cost	80	10		800					
(f)	To excise duty on finished goods sold				0					
(g)	To gross Profit				300					
	<b>TOTAL</b>				<b>1900</b>		<b>TOTAL</b>			<b>1900</b>

The profit & loss account on "inclusive method" which is also in accordance with the provisions of section 145A would be as under:

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Item	Particulars	Unit	Rate	Amount	Amount	Item	Particulars	Unit	Rate	Amount
(j)	Opening stock	10	12	120		(s)	By sales	60	28	1680
(k)	Purchase of raw material	90	12	1080		(t)	By closing stock of finished goods	20	23	460
	Total	100	12	1200						
(l)	Less closing stock	20	12	240						
(m)	Less CENVAT credit	80	2	160						
(n)	Raw material Consumed	80	10		800					
(o)	To manufacturing cost	80	10		800					
(p)	To excise duty on finished goods	60	3		180					
(q)	To excise duty on closing stock of finished goods	20	3		60					
(r)	To gross profit				300					
	<b>TOTAL</b>				<b>2140</b>		<b>TOTAL</b>			<b>2140</b>

23.11 It may be pointed out that the "inclusive method" is not permitted by AS-2 which is made mandatory from accounting year beginning on or after 01.04.1999. Further, in the Guidance Note on Accounting for CENVAT the second method (inclusive method) has been withdrawn with effect from accounting year commencing from 1.4.1999. In view of the above, the adjustments under section 145A will have to be made in all cases where 'exclusive method' is followed.

23.12 In this connection, it is worthwhile to note that the Memorandum explaining the provisions of section 145A inserted by the Finance (No.2) Bill, 1998 states as follows:

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### *"Computation of value of inventory.*

*The issue relating to whether the value of closing stock of the inputs, work-in-progress and finished goods must necessarily include the element for which MODVAT\* credit is available has been the matter of considerable litigation.*

*In order to ensure that the value of opening and closing stock (bold for emphasis) reflect the correct value, it is proposed to insert a new section to clarify that while computing the value of the inventory as per the method of accounting regularly employed by the assessee, the same shall include the amount of any tax, duty, cess or fees paid or liability incurred for the same under any law in force.*

*The proposed amendment which is clarificatory in nature shall take effect retrospectively from the 1st day of April, 1986 and will accordingly apply in relation to assessment year 1986-87 and subsequent years.*

*[Clause 45]"*

\*Now CENVAT.

(Section 145A was initially proposed to be applicable in relation to assessment year 1986-87 and subsequent years. However, later on, when the Finance (No.2) Bill, 1998 was enacted into law the provision was made applicable from 1.4.1999 i.e. assessment year 1999-2000)

23.13 It may be noted that when the adjustments are made in the valuation of inventories, this will affect both the opening as well as closing stock. Whatever adjustment is made in the valuation of closing stock, the same will be reflected in the opening stock also. Question for consideration is whether the opening stock as on 1.4.1998 should be adjusted as required under section 145A. It is now well settled that if any adjustment is required to be made by a statute, effect to the same should be given irrespective of any consequences on the computation of income for tax purposes. Section 145A starts with the *non obstante* clause "Notwithstanding anything to the contrary contained in section 145". Therefore, to give effect to section 145A, the opening stock as on 1.4.98 will have to be increased by any tax, duty, cess or fee actually paid or incurred with reference to such stock if the same has not been added for the purpose of valuation in the accounts.

23.14 It may be noted that while making the adjustments stated in Para 23.8 and 23.13 above, the tax auditor should ensure that if any deduction is claimed for any tax, duty, cess or fee on the items covered by these two



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paragraphs by way of debit in the profit and loss account, either in the earlier year or in the year under report, adjustment for the same should be made in such a manner that no double deduction is claimed for the same expenditure. Similarly, adjustment should be made for any item of income to ensure that the same item is not treated as income twice.

23.15 When the exclusive method is followed in the accounts, the adjustments to be made under section 145A can be explained by the following illustrations which are required to be reported under clause 14(b).

Sl. No.	Particulars	(Rupees) Increase in Profit	(Rupees) Decrease in Profit
1.	Increase in cost of opening stock on inclusion of excise duty on which CENVAT credit is available/availed (j - a)		20
2.	Increase in purchase cost of raw material on inclusion of excise duty on which CENVAT credit is available/availed (k - b)		180
3.	Increase in sales of finished goods on inclusion of excise duty (s - h)	180	
4.	Excise duty paid on sale of finished goods as a result of its inclusion in sales (p-f)	-	180
5.	Increase in closing stock of raw material on inclusion of excise duty (l - c)	40	-
6.	Increase in closing stock of finished goods on inclusion of excise duty (t - i)	60	-
7.	Increase in excise duty on closing stock of finished goods as a result of its inclusion in closing stock of finished goods (q)	-	60
8.	Accounting of CENVAT credit availed and utilised on raw materials consumed in payment of excise duty on finished goods accounted on the basis of raw material consumed (m)	160	-
	<b>TOTAL</b>	<b>440</b>	<b>440</b>

It may be noted that the net impact on the profit or loss will be nil.

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**Note 1:** The reference in brackets is to items in the illustration given in paragraphs 23.10 above.

**Note 2:** The CENVAT credit in the "inclusive method" has been worked out on the basis of quantity of raw material consumed multiplied by excise duty paid on purchase of such raw material (Rs.160) (item m), though the CENVAT credit set off availed and utilized by the assessee against payment of excise duty on finished goods is Rs.180. This is so because the raw material consumed during the year under both the methods is Rs.800. The CENVAT credit in the inclusive method would have to be deducted from purchase of raw material on the basis of consumption of raw material and not on the basis of set off availed in excise law to arrive at correct cost of consumption. In the illustration if CENVAT credit of Rs.180 is accounted, then the raw material consumed would be Rs.780. This figure would not be the correct figure of consumption, since 80 units have been consumed and the net cost of each raw material is Rs.10 (12-2). In other words, the consumption of raw material to be debited during the year should be Rs.800 i.e. 80 units multiplied by 10. So also the figure of excise duty on finished goods sold of Rs.180 is correctly debited because the same represents excise duty on finished goods sold and the same cannot be changed on account of CENVAT credit set off availed.

In the inclusive method the cost of the finished goods have been taken at Rs.20 plus Rs.3 excise duty. The raw material component included in the finished goods has been taken at Rs.10 since CENVAT credit have been accounted at the rate of Rs.2 in arriving at consumption of raw material.

**Note 3:** Similar treatment should be given for other tax, duty, cess, or fee paid by the assessee i.e. sales tax etc.

**Note 4:** It may be noted that liability for sales tax arises on sale as against liability for excise duty which arises on manufacture. As such the liability for sales tax need not be adjusted in the closing stock of finished goods before the same are sold.

23.16 It may be noted that after making the above addition to the closing stock under section 145A, it will be possible to claim a separate deduction for excise duty actually paid after the year end but before the due date for filing the return of income on production of evidence as provided under section 43B. Therefore, in the above illustration if the assessee has paid Rs.60 added in the valuation of closing stock of finished goods before the due date for filing the return, deduction for the same can be separately claimed in the computation of income under section 43B, if other conditions of those sections are satisfied.

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23.17 The computation of total income would appear as under :

	Rs.	Rs.	Rs.
Profit as per Profit and Loss account on the basis of exclusive method (see paragraph 23.10)			300
<i>Add:</i> Adjustments required under section 145A:			
1) Excise duty on sales (Rs.3/ per unit for 60 units)	180		
2) Excise duty on closing stock of raw materials (Rs. 2/- per unit for 20 units)	40		
3) Excise duty on closing stock of finished goods (Rs.3/ per unit for 20 units)	60		
4) CENVAT credit utilized on consumption of raw materials (Rs.2/- per unit for 80 units)	160	440	
		-----	
<i>Less:</i>			
1) Excise duty on opening stock of raw material (Rs.2/- per unit for 10 units)	20		
2) Excise duty on purchase of raw materials (Rs.2/- per unit on 90 units)	180		
3) Excise duty on sales (paid or incurred as per section 145A)	180	380	60
	-----	-----	-----
			360
<i>* Less:</i> Deduction under section 43B on the assumption that the amount is paid on or before due date of filing return of income in respect of excise duty payable on finished goods			60
			-----
Profit			300
			-----

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23.18 The input State-Level Value Added Tax (VAT) paid on purchases cannot be included in the cost of purchases where the tax paid on inputs is available for set-off against the tax payable on sales or is refundable, it is in the nature of taxes recoverable from taxing authorities. The Accounting Standard (AS) 2 "Valuation of Inventories" deals with "cost of inventories" and "cost of purchases". As per para 6 and 7 of the said AS-2, the cost of purchases cannot include duties and the taxes which are subsequently recoverable from the taxing authorities. Hence the input tax which is refundable, should not be included in the cost of purchases.

23.19 The Input State-Level VAT, to the extent it is refundable, will not form part of the cost of the inventory. The inventory of inputs is to be valued at net of the input tax which is refundable. If the inputs are obtained from the dealers who are exempt from the VAT, the actual cost of purchase should be considered as a part of cost of inventory.

23.20 A dealer may purchase certain common inputs which can be used for manufacturing goods which are declared tax free as well as taxable goods. In such case, the dealer should estimate inputs expected to be used for making tax free goods and for making taxable goods. The dealer should recognize VAT credit only in respect of those inputs which are used for making taxable goods and no VAT credit should be recognized in respect of inputs used for making tax free goods. Similar accounting treatment should be given in the case of stock transfer/ consignment sale of goods out of the State where VAT credit is available only to the extent of a certain portion of input tax paid.

23.21 VAT is collected from the customers on behalf of the VAT authorities and, therefore, its collection from the customers is not an economic benefit for the enterprise. It does not result in any increase in the equity of the enterprise. Accordingly, it should not be recognized as an income of the enterprise. Similarly, the payment of VAT should not be treated as an expense in the financial statements of the enterprise. Therefore, it should be credited to an appropriate account, say, 'VAT Payable Account'. In case the VAT has not been charged separately but has made a composite charge, it should segregate the portion of sales which is attributable to tax and should credit the same to 'VAT Payable Account' at periodic intervals. The amount of VAT payable adjusted against the VAT Credit Receivable (Capital Goods) Account and amounts paid in cash will be debited to this account. The credit balance in VAT Payable Account at the year-end should be shown on the 'Liabilities' side of the balance sheet under the head 'Current Liabilities'. It is

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important to note that where the assessee is enjoying tax holiday under the relevant state law as a result of which the liability to pay is deferred for a period of more than one year then it should be reflected as a long term liability.

23.22 Section 145A of the Income-tax Act provides that the valuation of purchase and sales of goods and inventory for the purpose of computation of income from business or profession shall be made on the basis of method of accounting regularly employed by the assessee but this shall be subject to certain adjustments. Therefore, it is not necessary to change the method of valuation of purchase, sale and inventory regularly employed in the books of account. The adjustment provided for in this section should be made while computing the income for the purpose of preparing the return of income. Therefore, the recommended method for accounting of VAT will not result in non-compliance of section 145A of the Income-tax Act.

23.23 The adjustments envisaged by section 145A will not have any impact on the trading account of the assessee. In other words both under exclusive method of accounting and inclusive method of accounting, the gross profit in the trading account will remain the same. The same is illustrated for a trading concern and a manufacturing concern as follows:

#### (I) Trading Concern

*Assuming that the assessee has opening stock of Rs.3,30,000/- on which input tax rebate of Rs.30,000/- is available. During the year three items purchased @ Rs.3,00,000/- per item. VAT on purchase @ 10%. There is no opening stock. Two items are sold @ Rs.4,50,000/- per item. VAT on sales @ 10%*

#### The Trading Account on "EXCLUSIVE METHOD"

Particulars	Qty.	Rate	Amount	Particulars	Qty.	Rate	Amount
To Opening Stock	1	3,30,000	3,30,000	By Sales	2	4,50,000	9,00,000
Less Input tax rebate			30,000				
			3,00,000				
To Purchases	3	3,00,000	9,00,000	By Closing Stock	2	3,00,000	6,00,000
To Gross Profit			<u>3,00,000</u>				
<b>Total</b>			<b><u>15,00,000</u></b>				<b>15,00,000</b>

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#### The Trading Account on "INCLUSIVE METHOD"

Particulars	Qty	Rate	Amount	Particulars	Qty	Rate	Amount
To Opening Stock	1	3,30,000	3,30,000	By Sales	2	4,95,000	9,90,000
To Purchases	3	3,30,000	9,90,000	By Closing Stock	2	3,30,000	6,60,000
			<u>13,20,000</u>				
Less: VAT credit availed on cost of goods sold			60,000				
			12,60,000				
VAT paid on sales			90,000				
Gross Profit			3,00,000				
			<b>16,50,000</b>				<b>16,50,000</b>

The statutory adjustments required under section 145A can be explained by the following example:

Sl. No.	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)
1.	Increase in Opening Stock on inclusion of VAT		30,000
2.	Increase in Purchases on inclusion of VAT		90,000
3.	Increase in Sales on inclusion of VAT	90,000	
4.	Increase in Closing Stock on inclusion of VAT	60,000	
5.	VAT paid on sales		90,000
6.	VAT credit availed on cost of goods sold	60,000	
		<b>2,10,000</b>	<b>2,10,000</b>

The net impact on Profit & Loss Account is NIL.

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The computation of total income would appear as under:-

Profit as per Profit & Loss account on the basis of exclusive method	Rs.3,00,000
Add: Adjustments required under section 145A	
1. Increase in Sales on inclusion of VAT	Rs. 90,000
2. Increase in Closing Stock on inclusion of VAT	Rs. 60,000
<b>Total</b>	<b>Rs. 4,50,000</b>
Less:	
1. Increase in Opening Stock on inclusion of VAT	Rs. 30,000
2. VAT Credit Receivables (Input) A/c	Rs. 90,000
3. VAT Paid on sales 90,000	
Less: VAT Credit availed on Cost of Goods Sold 60,000	
Net VAT Paid	<u>Rs.30,000</u>
<b>Profit</b>	<b>Rs. <u>3,00,000</u></b>

#### (II) Manufacturing concern

The following information is considered in the case of a manufacturing concern:-

Opening Stock of Raw Material 50 units	@ Rs.100 per unit
Purchases of Raw Material 300 units	@ Rs.100 per unit
Sales 250 units	@ Rs.150 per unit
Manufacturing Expenses	Rs.3,000
Closing Stock of Raw Material	50 units
Closing Stock of Finished Goods	50 units
Rate of VAT on purchases and sales	4%

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**Manufacturing Account on “EXCLUSIVE METHOD”**

Particulars	Qty	Rate	Amount	Amount	Particulars	Qty	Rate	Amount
Opening Stock	50	100	5,000		By Sales	250	150	37,500
Purchase of raw materials	300	100	30,000		By closing stock of finished goods	50	110	5,500
<b>Total</b>	<b>350</b>	<b>100</b>	<b>35,000</b>					
Less: Closing Stock of raw material	50	100	5,000					
Raw material Consumed (C) = (A) – (B)	300			30,000				
To manufacturing Expenses	300	10		3,000				
To VAT on finished goods sold				0				
To gross profit				10,000				
<b>Total</b>				<b>43,000</b>	<b>Total</b>			<b>43,000</b>

**Manufacturing Account on “INCLUSIVE METHOD”**

Particulars	Qty	Rate	Amount	Amount	Particulars	Qty	Rate	Amount
Opening Stock	50	104	5,200		By Sales	250	156	39,000
Purchase of raw materials	300	104	31,200		By closing stock of finished goods	50	114	5,700
<b>Total</b>	<b>350</b>	<b>104</b>	<b>36,400</b>					
Less: Closing Stock of raw material	50	104	5,200					
Less: VAT on Raw Material Consumed	300	4	1,200					



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Particulars	Qty	Rate	Amount	Amount	Particulars	Qty	Rate	Amount
Raw material Consumed (C) = (A) - (B)	300	100		30,000				
To manufacturing expenses	300	100		3,000				
To VAT on finished goods sold	250	6		1,500				
To VAT included in finished goods on account of inclusion of VAT in the raw material value	50	4		200				
To gross profit				10,000				
<b>Total</b>				<b>44,700</b>	<b>Total</b>			<b>44,700</b>

The valuation of finished goods includes the raw material cost and the manufacturing expenses. The raw material costs is taken at Rs.100 per unit in the exclusive method and Rs.104 in the inclusive method. The overhead cost is Rs.10 per unit.

23.24 It will be seen from the above that the gross profit is the same both under the inclusive and the exclusive method. Further, the closing stock of raw materials includes the appropriate VAT. But the VAT is not includible in the closing stock of finished goods since the incidence of VAT arises only on sale. However, VAT on raw material included in the finished goods has also been included in the value of closing stock of finished goods.

The statutory adjustments required under section 145A can be explained by the following example:

Sl. No.	Particulars	Increase in Profit (Rupees)	Decrease in Profit (Rupees)
1.	Increase in cost of opening stock of raw material on inclusion of VAT		200

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Sl. No.	Particulars	Increase in Profit (Rupees)	Decrease in Profit (Rupees)
2.	Increase in purchase on account of inclusion of VAT.		1,200
3.	Increase in sales of finished goods on inclusion of VAT.	1,500	
4.	VAT paid on sale of finished goods as a result of its inclusion in sales		1,500
5.	Increase in closing stock of raw material on inclusion of VAT	200	
6.	Accounting of VAT credit availed and utilized on raw material consumed in payment of VAT on finished goods, accounted on the basis of raw material consumed.	1,200	
7.	Increase on account of VAT included in finished goods on account of inclusion of VAT in the raw material value	200	
8.	Increase in VAT on closing stock of finished goods on account of inclusion of VAT in the raw material value		200
<b>Total</b>		<b>3,100</b>	<b>3,100</b>

The net impact on the Profit & Loss Account is NIL.

The computation of total income total income would appear as under:-

Profit as per Profit & Loss account on the basis of exclusive method	Rs.10,000
Add: Adjustments required under section 145A	
1. Increase in Sales on inclusion of VAT	Rs. 1,500
2. Increase in Closing Stock of Raw Material on inclusion of VAT	Rs. 200
3. Increase in Stock of finished goods on account of inclusion of VAT in the raw material value	<u>Rs. 200</u>
	Rs.1,900
<b>Total</b>	<b>Rs.11,900</b>

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Less:

1.	VAT on Opening Stock of Raw Material		Rs.200
2.	VAT included in Purchases		Rs.1200
3.	VAT Paid on Sales	Rs.1500	
	Less: Input Tax Credit on Raw		
	Material Consumed	Rs.1200	
	Add: VAT included in Closing Stock		
	Of Finished Goods	Rs.200	Rs.500
	<b>Profit</b>		<b>Rs 10,000</b>

**24. Give the following particulars of the capital asset converted into stock-in-trade:-**

- (a) Description of capital asset;
- (b) Date of acquisition;
- (c) Cost of acquisition;
- (d) Amount at which the asset is converted into stock-in-trade.

**[Clause 15]**

24.1 For furnishing the particulars required by clause 15, the provisions of section 2(47), 45(2), 47(iv), (v) and 47A have to be kept in mind.

24.2 From the A.Y. 1985-86 onwards the conversion by the owner of an asset into or treatment of such asset as stock-in-trade of a business carried on by him is treated as a 'transfer' within the meaning of section 2(47). Under section 45(2) such a conversion or treatment of capital asset into stock-in-trade will be deemed to be a transfer of the previous year in which the asset is so converted or treated as stock-in-trade. However, the capital gains arising from such a transfer will become chargeable in the previous year in which such converted asset is sold or otherwise transferred. In the case of long-term capital asset, indexation of cost of acquisition and cost of improvement, if any, will be with respect to the previous year in which such conversion took place. The fair market value of the asset, as on the date of such conversion or treatment as stock-in trade, shall be deemed to be the full value of the consideration of the asset. The excess of the sale price over the fair market value as on the date of conversion would be treated as business income and taxed under the head 'profits and gains of business or profession'. The capital gains being the difference between the cost of acquisition and the fair market value on the date of the conversion or

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treatment as stock-in-trade will be chargeable to tax in the year in which the asset is sold.

24.3 Section 47 of the Act enumerates the transactions which will not be regarded as transfer. Under clause (iv) any transfer of a capital asset by a company to its subsidiary company if the parent company or its nominees hold the whole of the share capital of the subsidiary company and the subsidiary company is an Indian company will not be treated as a transfer. Under clause (v) any transfer of a capital asset by a subsidiary company to the holding company if the whole of the share capital of the subsidiary company is held by the holding company and the holding company is an Indian company will not be considered as a transfer.

24.4 The capital gains exempted by virtue of clause (iv) or clause (v) of section 47 may become chargeable under certain circumstances. The provisions of section 47A are relevant here. Accordingly, where at any time before the expiry of a period of 8 years from the date of transfer of a capital asset referred to in clause (iv) or clause (v) of section 47, such capital asset is converted by the transferee company into, or is treated by it as, stock-in-trade of its business or the parent company or its nominees or, as the case may be, the holding company ceases to hold the whole of the share capital of the subsidiary company, the amount of profits or gains arising from the transfer of such capital assets not charged under section 45 by virtue of the provisions contained in clause (iv) or clause (v) of section 47 shall be deemed to be income chargeable under the head "capital gains" of the previous year in which such transfer took place.

24.5 The particulars to be stated under new clause 15 should be furnished with respect to the previous year in which the asset has been converted into stock-in-trade. The clause does not require details regarding the taxability of capital gains or business income arising from such deemed transfer.

24.6 Under clause (a) description of the capital asset is required to be mentioned for example shares, security, land, building, plant, machinery etc.

24.7 Under Clause (b) the date of acquisition is to be reported. For ascertaining the correct date the tax auditor will have to refer the accounts of the financial year in which such capital asset is acquired. The date assumes importance for the purpose of determining whether the asset is long-term or short-term in nature.

24.8 Under clause (c) the cost of acquisition is required to be reported. Here the cost of acquisition as per the books of account is to be mentioned. In case of depreciable assets, the carrying cost appearing in the books will be the written down value. But the value to be reported will be the original

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cost of acquisition. Even in case of an asset acquired prior to the 1<sup>st</sup> day of April, 1981 the value to be reported will be the original cost of acquisition. The assessee may exercise the option of considering the fair market value of the asset as on 1<sup>st</sup> April, 1981 for assets acquired prior to that date for the purpose of computation of capital gains as provided under section 55(2)(b)(i). Further, in case of block of assets a particular asset loses its identity and therefore to report the original cost of acquisition may not be possible in all cases. In case of corporate entities where the requirements of CARO are applicable the cost may be available from the fixed asset register. However, in case of companies where CARO is not applicable and other partnership concerns, the reporting requirements as to the original cost of acquisition may not be practically possible.

24.9 Under clause (d) the amount recorded in the books of account at which the asset is converted into stock-in-trade should be stated. Such an amount may not be the fair market value as on the date of conversion or treatment as stock-in-trade. If a value other than carrying cost is recorded then the auditor has to examine the basis of arriving at such a value. The valuation of stock-in-trade is to be examined with reference to AS-2 – Valuation of Inventories. Non-compliance with AS-2 is to be suitably qualified in the main audit report.

24.10 It is desirable that necessary accounting entry is passed in the books of account at the time of conversion of the asset into or treatment of the same as stock-in-trade.

24.11 In the case of assessee like a proprietorship concern, prior to the conversion of the asset into stock-in-trade, the details regarding the date of acquisition and cost of acquisition may not be recorded in the books of account. It is also possible that the year in which the capital asset is acquired, the accounts of the assessee may not have been subjected to audit. Also an assessee can acquire a capital asset through various modes such as discussed under section 49 of the Act. Under such circumstances the auditor may have to verify the cost and the date of acquisition. The following broad principles need to be kept in mind.

24.12 While verifying the cost of acquisition of the fixed asset, the auditor should bear in mind the principles enunciated in Accounting Standard (AS) 10, Accounting for Fixed Assets. As per paragraph 20 of the said Accounting Standard, the cost of a fixed asset comprises of its purchase price and any attributable cost of bringing the asset to its working condition for its intended use. Thus, in case of capital assets purchased by the assessee, it would relatively be easy for the auditor to verify the cost of acquisition, the evidence being provided by the supporting purchase invoices from the

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supplier, entries appearing in the bank statements in respect of payment to the supplier, entries appearing in the cash book/ bank statement for payment of cartage installment etc. In case of self-constructed capital assets, the cost would comprise those costs that relate directly to the specific capital asset and those that are attributable to the construction activity in general and can be allocated to the specific asset. In case of Capital assets acquired in exchange or in part exchange for another asset, the cost of the asset acquired is either the fair market value or the net book value of the asset given up, whichever is more clearly evident, adjusted for any balancing payment or receipt of cash or other consideration. In case the capital asset is recorded at the net book value of the asset, the fixed asset register would provide the prime evidence of the value. If, however the capital asset so acquired is recorded at the market value the auditor would need to examine the basis for arriving at the fair market value, for example, the valuer's report, market quotes (in case of listed securities). Where the valuer is the tax auditor's internal/ external, the tax auditor should have regard to the principles laid down in SA 620, *Using the Work of An Auditor's Expert*. In any case the auditor would also need to look into how the assessee has decided the value at which the asset is recorded in the books of account is more clearly evident than the other value. In case of a capital asset acquired by way of inheritance, the auditor may find it difficult to verify the cost of acquisition to the original owner. In case there does not exist any documentary evidence as to the cost of acquisition of the asset to the original owner, say the sale/purchase agreement the auditor may need to rely upon the reports of the experts such as valuers. In addition to the above, the auditor should also refer to the guidance contained in the Guidance Note on Audit of Property, Plant and Equipment issued by the Institute.

**25. Amounts not credited to the profit and loss account, being,-**

- (a) the items falling within the scope of section 28;
- (b) the proforma credits, drawbacks, refund of duty of customs or excise or service tax, or refund of sales tax or value added tax, where such credits, drawbacks or refunds are admitted as due by the authorities concerned;
- (c) escalation claims accepted during the previous year;
- (d) any other item of income;
- (e) capital receipt, if any.

[Clause 16 (a) to (e)]

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25.1 Under this clause various amounts falling within the scope of section 28 which are not credited to the profit and loss account are to be stated. The information under sub-clauses (a), (d) and (e) of clause (16) is to be given with reference to the entries in the books of account and records made available to the tax auditor for the purpose of tax audit under section 44AB. Sub-clauses 16 (b), (c) & (d) require information in respect of items which may also be covered under section 28 and as such will also fall in clause 16 (a). However, those items which are reported in clauses 16(b), (c) and (d) need not be reported in clause 16 (a). The tax auditor may obtain a management representation in writing from the assessee in respect of all items falling under this clause.

25.2 Section 28 refers to

- (i) the profits and gains of any business or profession,
- (ii) any compensation received on termination of employment, agency etc.
- (iii) income derived by a trade, professional or similar association from specific services performed for its members,
- (iiia) profits on sale of a licence granted under the Imports Control Order, 1955,
- (iiib) cash assistance against exports
- (iiic) customs duty or excise repaid or repayable as drawback against exports,
- (iiid) profit on the transfer of DEPB Scheme being the Duty Remission Scheme,
- (iiie) profit on the transfer of DFRC being the Duty Remission Scheme
- (iv) the value of any benefit or perquisite arising from business or the exercise of a profession
- (v) any interest, salary, bonus, commission or remuneration, by whatever name called, received by a partner of the firm from such firm,
- (va) any sum, whether received for (a) not carrying out any activity in relation to any business (b) not sharing any know how, patent, copyright, trade mark, licence, franchise or any other business or commercial right of similar nature or information or technique

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likely to assist in the manufacture or processing of goods or provision for services

- (vi) any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy
- (vii) any sum received on account of any capital assets (other than land or goodwill or financial instrument) being demolished, destroyed, discarded or transferred if the whole of the expenditure on such capital assets has been allowed under Section 35AD.

25.3 As per Explanation 2, where speculative transactions constitute a business, such speculation business is deemed to be distinct and separate business from any other business.

25.4 The details of the following claims, if admitted as due by the concerned authorities but not credited to the profit and loss account, are to be stated under sub-clause (b).

- (i) Pro forma credits
- (ii) Drawback
- (iii) Refund of duty of customs
- (iv) Refund of excise duty
- (v) Refund of service tax
- (vi) Refund of sales tax or value added tax

In respect of items falling under sub-clause (b) the tax auditor should examine all relevant correspondence, records and evidence in order to determine whether any particular refund/claim has been admitted as due and accepted during the relevant financial year.

25.5 There may be practical difficulties in verifying the information in regard to such refunds and credits. It may, therefore, be necessary for the tax auditor to scrutinise the relevant files or subsequent records relating to such refunds while verifying the particulars and also obtain an appropriate management representation.

25.6 The words 'admitted by the concerned authorities' would mean 'admitted by the authorities within the relevant previous year'.

25.7 The system of accounting followed in respect of these particular items may also be brought out in appropriate cases. If the assessee is following



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cash basis of accounting, it should be clearly brought out, since the admittance of claims during the relevant previous year without actual receipt has no significance in cases where cash method of accounting is followed. Credits/claims which have been admitted as due after the relevant previous year need not be reported here.

Where such amounts have not been credited in the profit and loss account but netted against the relevant expenditure/income heads, such fact should be clearly brought out.

25.8 Under sub-clause (c), the escalation claims accepted during the previous year but not credited to the profit and loss account are to be stated. The escalation claims accepted during the year would normally mean "accepted during the relevant previous year". If such amount has not been credited to the profit and loss account the fact should be brought out. The system of accounting followed in respect of this particular item may also be brought out in appropriate cases. If the assessee is following cash basis of accounting with reference to this item, it should be clearly brought out since acceptance of claims during the relevant previous year without actual receipt has no significance in cases where cash method of accounting is followed.

25.9 Escalation claims would normally arise pursuant to a contract (including contracts entered into in earlier years), if so permitted by the contract. Only those claims to which the other party has signified unconditional acceptance could constitute accepted claims. Mere making of claims by the assessee or claims under negotiations or claims which are sub-judice [*CIT v. Hindustan Housing & Land Development Trust Ltd. [1986] 161 ITR 524 (SC)*] cannot constitute claims accepted. The Auditor should take a professional judgment about acceptance of claim based on facts and circumstances of each case.

25.10 Sub-clause (d) covers any other items which the tax auditor considers as an income of the assessee based on his verification of records and other documents and information gathered, but which has not been credited to the profit and loss account. In giving the details under sub-clauses (c) and (d), due regard should be given to AS-9 - Revenue Recognition.

25.11 The tax auditor should scrutinise all the items including casual and nonrecurring items appearing in the books of account, particularly the credit items, and ensure himself whether any such credit which is in the nature of income has been credited to the profit and loss account or not.

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25.12 Under sub-clause (e), capital receipt, if any, which has not been credited to the profit and loss account has to be stated. The tax auditor should use his professional expertise and judgement in determining whether the receipt is capital or revenue. The tax auditor may record various judicial pronouncements on which he has relied in his working papers.

25.13 The following is an illustrative list of capital receipts which, if not credited to the profit and loss account, are to be stated under this sub-clause.

- (a) Capital subsidy received in the form of Government grants which are in the nature of promoters' contribution i.e., they are given with reference to the total investment of the undertaking or by way of contribution to its total capital outlay. For e.g. Capital Investment Subsidy Scheme.
- (b) Government grant in relation to a specific fixed asset where such grant is shown as a deduction from the gross value of the asset by the concern in arriving at its book value.
- (c) Compensation for surrendering certain rights.
- (d) Profit on sale of fixed assets/investments to the extent not credited to the profit and loss account.

25.14 Loans and borrowings are not required to be stated under this sub-clause.

25.15 If during the course of audit auditor finds that certain income (e.g. income referred to in section 41(1)) are not credited to profit and loss account, the particulars of the same along with the amount is required to be reported under this clause.

**26. 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, please furnish:**

Details of property	Consideration received or accrued	Value adopted or assessed or assessable
1	2	3

(Clause 17)

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26.1 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 & gains from such transfer, the value so adopted or assessed or assessable shall be deemed to be the full value of consideration.

26.2 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.

26.3 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

26.4 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.

26.5 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.

26.6 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

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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.

26.7 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 this provisions or not, would require to be evaluated based on facts & circumstances of transactions.

**27. Particulars of depreciation allowable as per the Income-tax Act, 1961 in respect of each asset or block of assets, as the case may be, in the following form:-**

- (a) Description of asset/block of assets.
- (b) Rate of depreciation.
- (c) Actual cost or written down value, as the case may be.
- (d) Additions/deductions during the year with dates; in the case of any addition of an asset, date put to use; including adjustments on account of –
  - (i) Central Value Added Tax credits claimed and allowed under the Central Excise Rules, 1944, in respect of assets acquired on or after 1st March, 1994,
  - (ii) change in rate of exchange of currency, and
  - (iii) subsidy or grant or reimbursement, by whatever name called.
- (e) Depreciation allowable.
- (f) Written down value at the end of the year.

[Clause 18 (a) to (f)]

27.1 Having regard to the nature of requirements prescribed, it may be necessary for the tax auditor to examine:

- (a) Classification of the asset
- (b) Classification thereof to a block
- (c) The working of actual cost or written down value
- (d) The date of acquisition and the date on which it is put to use

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- (e) The applicable rate of depreciation
- (f) The additions / deductions and dates thereof
- (g) Adjustments required – specified as well as on account of sale, etc.

27.2 The word “allowable” implies that depreciation should be permissible as a deduction, as per the provisions of the Act and the Rules. This would require exercise of judgement having regard to the facts and circumstances of the case, developments in law from time to time, etc.

27.3 For the purpose of determining the rate of depreciation, the tax auditor has to examine the classification of the assets into various blocks. For example, a particular asset may be classified as plant or machinery from the viewpoint of one class of assessee, yet it may not be plant or machinery from the viewpoint of another class of assessee. The purpose for which the asset is used is also very material in this regard. Hence, the tax auditor should ensure that the classification as made by the assessee is in consonance with legal principles. In this connection, he should traverse through judicial pronouncements as well as through the past assessment history of the assessee, and upon an analysis thereof, if he comes to the conclusion that the matter is not free from doubt or controversy, he has to indicate the fact in his report by way of suitable qualification. It may also be necessary to rely upon technical data for determining the proper classification of the block. Since the tax auditor is not a technical expert, he has to obtain suitable certificate from concerned experts.

27.4 Once the classification has been ascertained and checked properly, the rates applicable as per the Income-tax Rules, 1962 follow as a natural corollary. The tax auditor must have due regard to the Income-tax Rules, 1962, relevant clarifications from the Department and judicial decisions.

27.5 Under sub-clauses (a) to (b), information in respect of description of assets, block of assets under which the concerned asset is classifiable and the rate of depreciation are to be stated. This will include information about the existing assets. In respect of the existing assets, the computation of depreciation would involve stating the opening written down value of the block of assets which should be taken from the relevant income-tax records. The tax auditor will be conducting the audit in the current year only. As such the tax auditor can rely upon the classification of assets and written down value stated in the income tax records available with the assessee. The tax auditor should mention the fact that he has relied upon the income tax records of the assessee in respect of the information regarding the classification of assets and written down value of the existing assets.

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27.6 If there is any dispute with regard to the classification of an asset in a particular block or the rate of depreciation applied, the tax auditor must give his working with suitable reasons. Further, there may be disputes in the earlier years between the assessee and the Department regarding classification, rate of depreciation etc. in respect of which the tax auditor should give suitable disclosure depending upon the facts and circumstances of the case. Alternatively, where the tax auditor adopts a system of classification different from the one adopted by the assessee, suitable disclosure should be made regarding the effect thereof.

27.7 It will, therefore, be advisable to put a suitable note with regard to those items in respect of which disputes for the earlier years are not resolved up to the date of giving the audit report and it should be clarified that the amount of depreciation allowable may change as a result of any decision which may be received after the audit report is given. This note can be in the following manner:

"NOTE: Certain disputes about

- (a) the rate of depreciation on \_\_\_\_\_
- (b) determination of WDV of block of assets relating to \_\_\_\_\_ and
- (c) ownership of \_\_\_\_\_ have arisen in the assessment years \_\_\_\_\_ for which assessments are pending/appeals are pending. The figures of WDV and/or rate of depreciation mentioned in the above statement may require modification when these disputes are resolved. Therefore, the amount of depreciation allowable as stated in the above statement will have to be accordingly modified."

27.8 For the purpose of determination of actual cost, the tax auditor has to be guided by the relevant legal provisions. Since determination of actual cost has got accounting implications, he can rely on the relevant Accounting Standards and Guidance Notes. Due to the amendments made by the Finance (No.2) Act, 1998, depreciation is allowable on intangible assets like know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of similar nature. There may be intangible assets like patents invented by the company, brand names, etc. for which the assessee might have incurred costs. The tax auditor should examine the basis on which the cost of such intangible assets has been arrived at.

27.9 The additions/deductions during the year have to be reported, with dates. The tax auditor is advised to get the details of each asset or block of asset added during the year or disposed of during the year with the dates of

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acquisition/disposal. Where any addition was made, the date on which the asset was put to use is to be reported. In respect of deductions, the sale value of the assets disposed of along with dates should be mentioned. The provisions of Section 36(1)(iii) and Explanation 8 to section 43(1) of the Act, should be kept in mind for capitalization of interest to the cost of assets. The tax auditor should check the working regarding the calculation of depreciation allowable under the Act. To ascertain when the asset has been put to use, the tax auditor could call for basic records like production records/installation details/excise records/service tax records/records relating to power connection for operating the machine and any other relevant evidence. In the absence of any specific documentation with regard to the effective date from which the asset is put to use, he could get a representation letter from the management, in respect of the assets acquired. He should examine whether the apportionment of depreciation in cases like succession, amalgamation, demerger etc. has been properly made.

27.10 Section 43(1) of the Act defines actual cost as under :

“Actual Cost” means the actual cost of the assets to the assessee, reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority.

Further section 43(1) has explanation from 1 to 13 which provides for different situations for the purpose of calculating the actual cost.

Section 43(2) defines the word “Paid” and Section 43(3) defines the word “Plant”.

Section 2(11) defines “Block of assets” and section 43(6) read with explanations 1 to 7 defines “Written Down Value”.

27.11 The Guidance Note on Accounting for State-level Value Added Tax issued by ICAI has suggested the following treatment in respect of VAT Credit on Capital Goods.

*“24. The accounting treatment recommended in the following paragraphs applies only to those capital goods which are eligible for the credit.*

*25. Paragraph 9.1 of Accounting Standard (AS) 10, Accounting for Fixed Assets, issued by the Institute of Chartered Accountants of India, inter-alia, provides as below:*

*“9.1 The cost of an item of fixed asset comprises its purchase*

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*price, including import duties and other nonrefundable taxes or levies and any directly attributable cost of bringing the asset to its working condition for its intended use; any trade discounts and rebates are deducted in arriving at the purchase price. ..."*

*VAT credit is considered to be of the nature of a refundable tax. Therefore, the tax paid on purchase of capital goods should not be included in the cost of such capital goods."*

In view of above, the VAT Credit eligible on capital goods should be reduced from the cost of the assets for the purpose of claim of depreciation.

27.12 Details have to be given in respect of adjustments on account of three factors. The first adjustment relates to CENVAT claimed and allowed under the Central Excise Rules, 1944 in respect of assets acquired on or after 1st March, 1994. Explanation 9 to section 43(1) of the Act provides that where an asset is or has been acquired on or after the 1st day of March, 1994 by an assessee, the actual cost of asset shall be reduced by the amount of duty of excise or the additional duty leviable under section 3 of the Customs Tariff Act, 1974 (51 of 1975) or Service Tax in respect of which a claim of credit has been made and allowed under the Central Excise Rules, 1944 and Finance Act 1994 (relating to Service Tax) read with CENVAT Credit Rules 2004. It is necessary, therefore, for the tax auditor to examine the details of assets acquired on or after 1st March, 1994 and the details of CENVAT credit claimed and allowed in respect of those assets

27.13 In Clause 18(d)(i) the amount of CENVAT credit claimed and allowed on capital goods and deducted from the cost of the asset has to be mentioned. Under the CENVAT Credit Rules, 2004, the assessee is entitled to avail credit of duty paid on capital goods and utilise the same, in payment of excise duty leviable on final products, or in payment of service tax on taxable output services. However the CENVAT credit of duty paid on capital goods is not allowed if the assessee claims depreciation under the Act on an amount including the amount of CENVAT credit [Rule 4 (4) of the CENVAT credit rules, 2004].

27.14 As such the assessee should not include duty paid on capital goods eligible for CENVAT credit as part of the cost of fixed assets, otherwise he will not eligible to claim the CENVAT credit. Whenever, CENVAT credit is rejected in the subsequent year, the auditor should make separate disclosure for the amount of CENVAT credit adjusted during the year which pertains to earlier years. Similarly, if the CENVAT credit is claimed and allowed but which has not been deducted from the cost of the asset, such credit should



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be deducted from the cost and the appropriate disclosure should be made separately for such adjustment.

27.15 The tax auditor should also verify that the amount of CENVAT credit deducted from cost of capital goods tallies with the credit availed on this account.

27.16 The second adjustment relates to the change in the rate of exchange of currency. Section 43A deals with the adjustment on account of change in the rate of exchange of currency. The Finance Act, 2002 has substituted a new section 43A w.e.f. A.Y. 2002-03. As per this amendment,

- (i) where an assessee has acquired any asset in any previous year from a country outside India for the purposes of his business or profession and,
- (ii) in consequence of a change in the rate of the exchange during any previous year after the acquisition of such asset,
- (iii) there is an increase or reduction in the liability of the assessee as expressed in Indian currency (as compared to the liability existing at the time of acquisition of the asset) at the time of making the payment towards the whole or part of the cost of the asset or towards repayment of the whole or a part of the monies borrowed by him from any person,
- (iv) directly, or indirectly in any foreign currency specifically for the purpose of acquiring the asset along with the interest, if any,
- (v) the increase or reduction in the liability during the previous year which is taken into account at the time of making the payment,
- (vi) irrespective of the method of accounting followed by the assessee, is to be added to, or as the case may be, deducted from the cost of the asset as defined in clause (1) of section 43.

27.17 In other words the extent of addition or reduction will be limited to the exchange difference actually paid during the previous year. The tax auditor is required to verify that the adjustments in the cost of fixed assets on account of changes in the rate of exchange of currency in the schedule of fixed assets prepared for computation of depreciation as per Income-tax Rules are in accordance with the provisions of section 43A and information about such adjustment is provided under sub-clause (ii) of clause 18(d). The Tax Auditor may also prepare a reconciliation statement for his own records for any different treatment followed for the purpose of books of accounts as per

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applicable accounting treatment under Accounting Standards. The auditor should also refer the explanations to section 43A.

27.18 The third adjustment relates to the subsidy or grant or reimbursement, by whatever name called. Explanation 10 to section 43(1) provides that where a portion of the cost of an asset acquired by the assessee has been met directly or indirectly by the Central Government or a State Government or any authority established under any law or by any other person, in the form of a subsidy or grant or reimbursement (by whatever name called), then, so much of the cost as is relatable to such subsidy or grant or reimbursement shall not be included in the actual cost of the asset to the assessee. As per the proviso to the above Explanation, where such subsidy or grant or reimbursement is of such nature that it cannot be directly relatable to the asset acquired, such of the amount which bears to the total subsidy or reimbursement or grant the same proportion as such asset bears to all the assets in respect of or with reference to which the subsidy or grant or reimbursement is so received, shall not be included in the actual cost of the asset to the assessee. Subsidy coming within the scope of Explanation 10 to section 43(1) in respect of asset acquired in any earlier year(s) and received during the year has to be deducted from the written down value of such assets in the year of receipt.

27.19 Finally, the amount of depreciation allowable and the WDV at the year end have to be stated. Wherever a claim for depreciation involves any reliance on any judgement or opinion or other contentions (as to its classification, rate applicable, cost, date on which put to use etc.), it may be advisable for tax auditor to disclose full particulars thereof and the basis on which the depreciation allowable has been determined and vouched by him.

27.20 The Finance Act, 2001 had inserted Explanation 5 below sub-section (1) of section 32, to the effect that the provisions of section 32(1) regarding allowing of depreciation shall apply whether or not the assessee has claimed the deduction in respect of depreciation in computing his total income. Thus, the claim for depreciation is now mandatory and the written down value of each asset every year has to be reduced by the amount of depreciation allowable under the Income-tax Rules and the details required under the relevant sub-clauses need to be stated.

27.21 Section 32(1)(ia) effective from Financial year 2002-03 provide for additional depreciation to a concern engaged in the business of manufacturing or production of an article or thing or installation of a new machinery on fulfillment of the prescribed conditions like specified

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percentage of increase in installed capacity. Additional depreciation shall be allowable in respect of new machinery or plant installed on or after 31<sup>st</sup> day of March, 2005, which is

- (i) engaged in the business of manufacture or production of any article or thing or
- (ii) In the business of generation or generation or distribution of power

except those machinery or plant which before installation by the assessee was used by any other person, machinery or plant installed in office premises or residential accommodation, office appliances, road transport vehicles and that machinery or plant the actual cost of which is allowed in computing the income. The tax auditor will need to verify the claim of additional depreciation under this clause as well.

27.22 Wherever, the full deduction of the cost of capital goods is allowed (e.g. expenditure on Scientific Research u/s. 35) the auditor should verify that the cost of such asset is not included in the block of assets for the purpose of depreciation.

27.23 The tax auditor has to keep in mind the above guidance while furnishing details in respect of this clause in the format provided in the e-filing utility.

#### 28. (a) 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 fulfills 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.
32AC		
33AB		
33ABA		
35(1)(i)		
35(1)(ii)		
35(1)(ia)		

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35(1)(iii)		
35(1)(iv)		
35(2AA)		
35(2AB)		
35ABB		
35AC		
35AD		
35CCA		
35CCB		
35CCC		
35CCD		
35D		
35DD		
35DDA		
35E		

**[Clause 19]**

28.1 The assessee can claim deduction under the sections 32AC, 33AB, 33ABA, 35, 35ABB, 35AC, 35AD, 35CCA, 35CCB, 35CCC, 35CCD, 35D, 35DD, 35DDA and 35E subject to the terms and conditions mentioned in these Sections.

28.2 In case the assessee has obtained a separate Audit Report for claiming deductions under any of these sections, he must make a reference to that report while giving the details under this clause.

28.3 The Tax Auditor should indicate the amount debited to the Profit & Loss Account and the amount actually admissible in accordance with the applicable provisions of law.

28.4 The amount not debited to the Profit & Loss Account but admissible under any of the Sections mentioned in the clause have to be stated. For example sections 33AB and 33ABA allow deduction in respect of amount deposited in designated account for specified purposes which, as per accounting principles, are not to be debited to the Profit & Loss Account. In this connection, the Tax Auditor has to work out, on the basis of the conditions prescribed in the concerned Section, the amount admissible there under and report the same.

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28.5 An assessee may be eligible for deduction under one or more sub-sections of section 35. In such case, the Tax Auditor should state the deduction allowable under each sub-section separately under applicable part, i.e. the amount deductible in respect of the amount debited in Profit & Loss Account and the amount not debited to the Profit & Loss Account.

28.6 The Tax Auditor should also ensure the eligibility of the expenditure/payment for deduction and compliance of the conditions prescribed in the sub-section including approval from the relevant/prescribed authority, notification issued by the Central Government, any other guideline circular etc issued in this behalf. Tax auditor should also refer Rule 6 of Income-tax Rules, 1962.

28.7 In case the auditor relies on a judicial pronouncement, he may mention the fact in his observations para provided in Form No.3CA or Form No.3CB, as the case may be.

28.8 The following Table summarizes Sub-section-wise eligibility, requirement of compliance of the conditions and the amount of deductions required to be mentioned under this clause (The summary is only illustrative and Tax Auditor is advised to refer actual provision of the Act):

**Table showing deductions applicable from A.Y. 2014-15 onwards (as per law prevailing on 1-4-2014)**

Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
32AC	Investment in New Plant & Machinery	15% of the actual cost of such new assets.
33AB	Amount deposited in Tea/Coffee/Rubber Development Account	Deduction is allowed for the least of the following: (a) Sum equal to the amount or the aggregate of the amounts so deposited.(b) Sum equal to 40% of the profits of such business.

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
33ABA	Where an amount is being deposited by an assessee in a scheme approved by the Government of India in the Ministry of Petroleum and Natural Gas for the purpose of prospecting or extraction etc. of petroleum or natural gas.	Deduction is allowed for the least of the following: (a) Sum equal to the amount or the aggregate of the amounts so deposited. (b) Sum equal to 20% of the profits of such business
35(1)(i)	Any Expenditure other than Capital Expenditure incurred by the assessee for scientific research related to its own business.	100% of the expenditure
35(1)(ii)	Amount paid to Research association which has as its object the undertaking of scientific research  Or amount paid to a University, college or other institutions to be used for scientific research. Provided that, such association, university, college or other institution is approved and is specified as such, by notification in the official gazette, by Central Govt.	175% of amount paid/contributed from A.Y. 2011-12 and onwards  125% of amount paid/contributed till A.Y 2010-11.
35(1)(ia)	Amount paid to a Company which is registered in India, having its main object of carrying out of scientific research and development and is approved by the jurisdictional Chief Commissioner of Income Tax in the prescribed manner.	125% of amount paid from A.Y. 2009-10

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
35(1)(iii)	<p>Amount paid to a research association which has as its main object the undertaking of research in social science or statistical research</p> <p>Or</p> <p>Amount paid to a university, college or other institutions to be used for research in social science or statistical research.</p> <p>Provided that, such association, university, college or other institution is approved and is specified as such, by notification in the official gazette, by Central Govt.</p>	125% of amount paid.
35(1)(iv)	Expenditure of capital nature on scientific research, other than expenditure on acquisition of any land, incurred related to the business carried on by the assessee.	100% of the capital expenditure incurred
35(2AA)	Any amount paid to National Laboratory; or a University; or Indian Institute of Technology or specified person as defined in the explanation 2 to the section with a specific direction that the said sum shall be used for scientific research undertaken under a programme approved by the prescribed authority.	<p>200% of amount paid from A.Y. 12-13 and onwards.</p> <p>175% for A.Y.2011-12</p> <p>125% till A.Y.2010-11</p>
35(2AB)	Deduction is available only to company (refer section 2 (17) of Income Tax Act, 1961)	200% of Expenditure incurred from A.Y. 2011-12 and onwards.

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Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
	<p>(Applicable from 01/04/2009 i.e. A.Y 2010-11 &amp; onwards)</p> <p><b>From A.Y. 2012-13 and onwards:</b> Company engaged in the business of Bio Technology or in any business of manufacture or production of any article or thing, not being an article or thing specified in the list of the Eleventh Schedule.</p> <p><b>Upto A.Y. 2011-12:</b> Finance Act, 2009, i.e. from A.Y. 2010-11 provides that, company engaged in the business of business of manufacture or production of any drugs, pharmaceuticals, electronic equipments, computers, telecommunication equipments, chemicals or any other article or thing notified by the Board. Expenditure incurred both revenue and capital, not being expenditure in the nature of cost of any land or building; on in house research and development facility as approved by the prescribed authority. Expenditure incurred in relation to drugs and pharmaceuticals shall include expenditure on clinical drug trial, for regulatory approvals and filling an application for patent. Prescribed authority is Secretary, Department of Scientific and Industrial Research.</p>	<p>150% of Expenditure incurred from A.Y. 2001-02 to A.Y. 2011-12</p> <p>125% till A.Y. 2000-01.</p>



## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
35ABB	Any expenditure, being in the nature of capital expenditure incurred for acquiring any right to operate telecommunication services[either before the commencement of the business to operate telecommunication services or thereafter at any time during any previous year]	Deduction equal to the appropriate fraction of the amount of such expenditure.  Where "appropriate fraction" means the fraction the numerator of which is one and the denominator of which is the total number of the relevant previous years;
35AC	Expenditure by way of payment of any sum to a public sector company or a local authority or to an association or institution approved by the National Committee for carrying out any eligible project or scheme	100% of such expenditure
35AD	Deduction in respect of any expenditure of capital nature incurred wholly & exclusively for any specified business.	Setting up and Operating cold chain facility-150% of expenditure  Setting up and Operating warehousing facility for storage of Agriculture produce-150% of expenditure  Laying and operating a cross country natural gas pipeline network for

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
		<p>distribution-100% of expenditure</p> <p>Building and operating a new Hotel in India, of two star or above category- 100% of such expenditure</p> <p>Building and operating a new Hospital in India, with at least one hundred beds for patients- 150% of expenditure</p> <p>Developing and building a housing project under a scheme for slum rehabilitation-100% of expenditure</p> <p>Developing and building a housing project under a scheme for affordable housing- 150% of expenditure</p> <p>Production of fertilizer in India- 150% of expenditure</p> <p>Setting up and operating an inland container depot or a container freight station-100% of expenditure</p>

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
		<p>Bee-keeping and production of honey and beeswax-100% of expenditure</p> <p>Setting up and operating a warehousing facility for storage of sugar-100% of expenditure</p> <p>Laying and operating a slurry pipeline for the transportation of iron ore – 100% of expenditure w.e.f AY 2015-16</p> <p>Setting and operating a semi-conductor wafer fabrication manufacturing unit – 100% of expenditure wef AY 2015-16</p>
35CCA	Expenditure by way of payment to association and institutions for carrying out rural development programmes	100% of expenditure
35CCB	Expenditure by way of payment to associations and institutions for carrying out programmes of conservation of natural resources	100% of expenditure
35CCC	Expenditure on agricultural extension project notified by the Board	150% of expenditure
35CCD	Expenditure incurred by a company on any skill development project notified by the Board	150% of expenditure

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Section & Sub-section	Eligible expenditure/payment	Amount/Quantum of Deduction
35D	Expenditure incurred by an Indian Company or a person who is resident in India on amortization of certain preliminary expenses.	One tenth of such expenditure for each of the ten successive previous years beginning with the previous year in which business commences or as the case may be.
35DD	Amortisation of Expenditure incurred by an Indian Company for the purpose of amalgamation or demerger	One fifth of such expenditure for each of the five successive previous years beginning with the previous year in which amalgamation or demerger takes place.
35DDA	Expenditure incurred by way of payment of any sum to an employee in connection with his voluntary retirement, in accordance with any scheme or scheme of voluntary retirement.	One-fifth of the amount so paid shall be deducted in computing the profits and gains of the business for that previous year, and the balance shall be deducted in equal installments for each of the four immediately succeeding previous years.
35E	Deduction for expenditure on prospecting or extraction or production of certain minerals.	One tenth of amount of such expenditure for each of ten successive previous years.

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Members are advised to refer the Income-tax Act, 1961 for any change in the provisions of Act at the time of signing the audit report.

28.8 Where under any section an assessee is eligible for deduction under one or more of the sub-sections of the said section, the Tax Auditor should certify the amount of deduction available under each sub-section separately in the applicable part, i.e. the amount deductible in respect of the amount debited to Profit & Loss Account and the amount not debited to the Profit & Loss Account.

29. (a) Any sum paid to an employee as bonus or commission for services rendered, where such sum was otherwise payable to him as profits or dividend. [Section 36(1)(ii)].

(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 for payment	The actual amount paid	The actual date of payment to the concerned authorities
1	2	3	4	5	6

[Clause 20 (a) and (b)]

29.1 Section 36(1)(ii) provides for deduction of any sum paid to an employee as bonus or commission for services rendered where such sum would not have been payable to him as profit or dividend, if it had not been paid as bonus or commission. In other words, if bonus or commission is in the nature of profit or dividend, it may not be normally allowable as a deduction unless such payment is wholly and exclusively made to the employee. [*Shahzada Nand & Sons v. CIT* [1977]] 108 ITR 358 (SC).

29.2 Under Clause 20(b), the requirement is only in respect of the disclosure of the amount and the tax auditor is not expected to express his opinion about its allowability or otherwise. The tax auditor should verify the employment/ contract details of the employees so as to ascertain the nature of payments.

29.3 Section 36(i)(va) of the Act permits deduction of any sum received by the assessee from any of his employees to which the provisions of section

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

2(24)(x) are applicable, if it is credited by the assessee to the account of the employees in the relevant statutory fund on or before the due date.

29.4 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 ESI Fund or any other Fund for employees' welfare (hereafter referred to as "Welfare Fund").

29.5 As per the explanation provided in section 36(1)(va), "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 there under or under any standing order, award, contract of service or otherwise, i.e., the date by which it is required to be credited as per the provisions of the applicable law etc. It may be noted that Employees' P.F. manual provides for 5 days of grace period for payment of contribution. This can be taken into consideration for determining the due date of payment.

29.6 The tax auditor should get a list of various contributions recovered from the employees which come within the scope of this clause and the date on which it is deposited. He should also verify the documents relating to provident funds and other welfare funds. He should verify the agreement under which employees have to make contributions to provident fund and other welfare funds. The ledger account of contributions from employees should be reviewed; the due dates of payments and the actual dates of payment should be verified with the evidence available. In view of the voluminous nature of the information, the tax auditor can apply test checks and compliance tests to satisfy himself that the system of recovery and remittance is proper. Under this clause, details regarding the nature of fund, details of the amount deducted, due date for payment, actual amount paid and actual date of payment to the concerned authorities in respect of provident fund, ESI fund or other staff welfare fund have to be stated.

29.7 The tax auditor should maintain the following information in his working papers for the purpose of reporting in the format provided in the e-filing utility:

(a)

Description	Amount
1	2

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(b)

Serial number	Nature of fund	Sum received from employees	Due date for payment	The actual amount paid	The actual date of payment to the concerned authorities
1	2	3	4	5	6

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

[Clause 21(a)]

Nature	Serial number	Particulars	Amount in Rs.
Capital Expenditure			
Personal Expenditure			
Advertisement expenditure in any souvenir, brochure, tract, pamphlet or the like published by a political party			
Expenditure incurred at clubs being entrance fees and subscriptions			

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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			

31. (b) Amounts inadmissible under section 40(a):
- (i) as payment to non-resident referred to in sub-clause (i)
- (A) Details of payment on which tax is not deducted:
- (I) date of payment
  - (II) amount of payment
  - (III) nature of payment
  - (IV) name and address of the 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)



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- (I) date of payment
  - (II) amount of payment
  - (III) nature of payment
  - (IV) name and address of the payer\*
  - (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 and 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 and address of the payee
    - (V) Amount of tax deducted
    - (VI) Amount out of (V) deposited, if any
- (iii) Under sub-clause (ic) [wherever applicable]
- (iv) Under sub-clause (ia)
- (v) Under sub-clause (iib)
- (vi) Under sub-clause (iii)
  - (A) Date of payment
  - (B) Amount of payment
  - (C) Name and address of the payee
- (vii) Under sub-clause (iv)
- (viii) Under sub-clause (v)

\* should be read as "payee" for proper reporting

[Clause 21(b)]

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32. (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;

[Clause 21(c)]

33. (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:

Serial number	Date of payment	Nature of payment	Amount	Name and Permanent Account Number of the payee, if available
1.	2.	3.	4.	5.

- (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);

Serial number	Date of payment	Nature of payment	Amount	Name and Permanent Account Number of the payee, if available
1.	2.	3.	4.	5.

[Clause 21(d)]

34. (e) provision for payment of gratuity not allowable under section 40A(7);

[Clause 21(e)]

35. (f) any sum paid by the assessee as an employer not allowable under section 40A(9);

[Clause 21(f)]

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- 36. (g) particulars of any liability of a contingent nature;  
[Clause 21(g)]
- 37. (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  
[Clause 21(h)]
- 38. (i) amount inadmissible under the proviso to section 36(1)(iii)  
[Clause 21(i)]

**30. Clause 21**

This clause requires the tax auditor to state the amount of expenditure incurred by the assessee in respect of various items listed above. These expenses may be allowable or may not be allowable or may be allowable subject to certain limits. It is important to note that the amount of expenditure in respect of each of the items is required to be stated. Accordingly, tax auditor will have to obtain the information and make necessary enquiries in that behalf. It will necessitate verification of books of account and other relevant documents, basis of classification, groups under which such expenses have been debited, and so on.

**30.1 Clause 21(a) - Expenditure in the nature of capital, personal, advertisement expenditure etc.**

**Expenditure of Capital nature:**

Capital expenditure is not allowable in computing business income unless specifically provided in any sections of the Act. The word "capital expenditure" is not defined in the Act and no conclusive test or rules can be laid down to determine whether a particular expenditure is capital or revenue in the nature. Different tests have been applied by the courts in different cases depending upon the facts and circumstances of each case and the case law on the subject, as evolved over a period of years, gives guidance for determining the nature of expenditure.

30.2 Some tests which, however, are generally applied to determine whether a particular item of expenditure is of capital nature, are set out hereunder:

- (i) Whether it brings into existence an asset or advantage of enduring benefit. The question whether a particular benefit is of an enduring or permanent nature will depend upon the facts and circumstances of each case, the concept of permanency being relative.

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- (ii) Whether it is referable to fixed capital or fixed assets in contrast to circulating capital or current assets.
- (iii) Whether it relates to the basic framework of the assessee's business.
- (iv) Whether it is an expenditure to acquire an intangible asset.

30.3 The above factors are not exhaustive and the tax auditor is required to verify the expenditure based on facts of the case after considering the applicable provisions of the Act.

30.4 The nature of receipt in the hands of the recipient is not a determining factor to decide the nature of payment in the hands of payer. If the amount is in the nature of capital receipt in the hands of the payee, it does not necessarily imply that it is a capital expenditure for the payer and vice versa. The case of the payer has to be considered independently based on the facts concerning him.

30.5 Under the Act, capital expenditure of certain types e.g., on scientific research referred to in section 35, is deductible in computing the income. Similarly depreciation at 100% is allowed in respect of certain assets as prescribed in New Appendix I of the Income-tax Rules, 1962. Ordinarily the capital expenditure should not be debited to profit and loss account. The tax auditor needs to keep in mind that the accounting standards also apply in respect of financial statements audited under section 44AB of the Act. Therefore, besides disclosing the amount of such capital expenditure debited to profit and loss account under this clause, the tax auditor should give suitable disclosure/ qualifications in para 3(a) of Form No. 3CB, depending on the facts of the case.

30.6 The details of capital expenditure, if any, debited to the profit and loss account should be maintained in a classified manner stating the amount under various heads separately. Since part of this capital expenditure may be allowable as deduction in the computation of total income, it is advisable to maintain particulars regarding the nature of expenditure, the amount of expenditure incurred, and the relevant provision under which the expenditure is admissible. However, the total amount of capital expenditure debited to the profit and loss account is to be reported under this clause in the e-filing portal.

#### **Expenditure of personal nature:**

30.7 Personal expenses debited to the profit and loss account are to be specified under this sub-clause as they are not deductible in the computation of total income under section 37. It may be noted that the word "personal" is

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confined to and attached with the “assessee” and not necessarily to and with persons other than the assessee.

30.8 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.

30.9 The tax auditor is advised to maintain the following details as part of his working papers for the purpose of reporting in the format provided in the e-filing utility:

Sl. No.	Nature and particulars of expenditure	Account head under which debited	Amount of expenditure	Remarks
1	2	3	4	5

#### **Expenditure on advertisement in any souvenir, brochure, tract, pamphlet or the like, published by a political party:**

30.10 Section 37(2B) provides that no allowance shall be made in respect of expenditure incurred by an assessee on advertisement in any souvenir, brochure, tract, pamphlet or the like published by a political party. Therefore, the expenditure of this nature should be segregated and reported under this clause.

30.11 The tax auditor may come across advertising expenditure incurred on advertising in a souvenir, brochure, tract, pamphlet or journal published by a trade union or a labour union formed by a political party. The trade union or labour union though promoted or formed by a political party may have a distinct legal entity. In that event, expenditure incurred by the assessee by way of advertisement given in the souvenir, brochure, tract, pamphlet or journal published by the trade union or the labour union is not required to be indicated against clause 21(a) in Form No. 3CD. If the trade union or labour union formed by the political party does not have a separate and distinct

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legal entity, then the expenditure incurred on such an advertisement will have to be indicated against this clause.

30.12 The auditor may also keep in mind the provisions of section 80GGB and 80GGC which allow deduction in respect of contribution made by corporate and non-corporate assesseees respectively to political parties and electoral trust, as required to be reported by him in clause 33 of Form no. 3CD.

#### **Expenditure incurred at clubs being cost for club services and facilities used, entrance fees and subscriptions:**

30.13 The amount of payments made to clubs by the assessee during the year being cost for club services and facilities used should be indicated under this clause. The payments may be for entrance fees as well as membership subscription and for catering and other services by the club, both in respect of directors and other employees in case of companies and for partners or proprietors in other cases. The fact whether such expenses are incurred in the course of business or whether they are of personal nature should be ascertained. If they are personal in nature, they are to be shown separately under Clause 21(a) referred to earlier.

30.14 Details of payments made to clubs are also required by tax authorities for the purpose of determining whether any portion of club expenses could be treated as perquisite in the hands of the person concerned. All payments made to credit card agencies should be carefully scrutinised. Credit card agency is nothing but credit/collecting agency. In order to determine whether the payments have been made to a club, one has to look into the substantive activity of the institution concerned.

30.15 This clause requires reporting of particulars and the amount of such expenses incurred in the respective fields. However, the following particulars may be maintained as working papers by the auditor for the purpose of reporting in the format provided in the e-filing utility:

Sr. No.	Name of the Club	Nature of Amount paid			Remarks
		Entrance/admission Fees	Subscription expenses	Cost of Club Services and facilities used	
(1)	(2)	(3)	(4)	(5)	(6)

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**Expenditure by way of penalty or fine for violation of any law for the time being in force; Expenditure by way of penalty or fine not covered above; Expenditure incurred for any other purpose which is an offence or is prohibited by law:**

30.16 This clause requires separate reporting of penalty or fine for violation of any law for the time being in force, and any other penalty or fine. The tax auditor should obtain in writing from the assessee the details of all payments by way of penalty or fine for violation of any laws have been made and paid or incurred during the relevant previous year and how such amounts have been dealt with in the books of accounts produced for audit.

30.17 The tax auditor may not be an expert to decide the nature of payment (as to whether it is prohibited by law or not) and may not be aware of the intricacies of all the laws of the land. He can rely on the expert opinion. It must be borne in mind that the tax auditor while reporting under this clause is not required to express any opinion as to the allowability or otherwise of the amount of penalty or fine for violation of law. He is only required to give the details of such items as have been charged in the books of accounts. This clause covers only penalty or fine for violation of law and not the payment for contractual breach or liquidator damages. The tax auditor should keep in mind the difference between the amount prohibited by law and the amount paid which is compulsory in nature under the relevant statute. While stating the particulars under this clause, the tax auditor should also take into consideration the concept of materiality.

30.18 In order to ascertain the facts whether the sum debited in the profit and loss account is by way of penalty or fine for any violation of law, the tax auditor will have to refer to the relevant law under which the amount has been paid or incurred and ascertain whether such amount is in the nature of penalty or fine. He should also ascertain all the facts by having recourse to the order of the jurisdictional authority which has levied the penalty or fine. Even if the assessee is contesting against such order before higher authorities, the same will not be relevant and the mere point for ascertaining is whether such sum is debited to the profit and loss account and if yes, the same has to be disclosed.

30.19 The courts have laid down that any penalty or fine for violation of law is not admissible as expenditure. It is in this context the requirement stipulated by clause 21(a) is to be answered.

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30.20 The following Explanation to section 37(1) of the Act has been inserted by Finance Act (No.2) Act, 1998 with effect from assessment year 1962-63.

*"For the removal of doubts, it is hereby declared that any expenditure incurred by an assessee for any purpose which is offence or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure".*

30.21 Under this sub-clause, any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law is to be stated.

30.22 Any expenditure in consequence of violation of law like penalty or fine levied for evading provisions of the Act, FEMA, Excise and Customs law etc., cannot be claimed as deduction under the Act. A penalty imposed for violation of any law during the course of trade cannot be described as a commercial loss. Even if the need for making payments has arisen out of trading operations, the payments are not wholly and exclusively for the purpose of the trade. Violation of law is not a normal incidence of business. This principle was laid down by Hon'ble Supreme Court in case of *CIT v. Maddi Venkataratnam & Co. (P) Ltd* [1998] 96 Taxman 643 and in the case of *Hazi Aziz Shekoo Bros v. CIT* [1961] 41 ITR 350. In both the cases it was held that one can carry business or his trade without violating the law.

30.23 In *Prakash Cotton Mills (P) Ltd. v CIT* [1993] 201 ITR 684 (SC) it has been held that whenever any statutory impost paid by an assessee by way of damages or penalty or interest is claimed as an allowable expenditure under section 37(1) of the Act, the assessing authority is required to examine the scheme of the provisions of the relevant statute providing for payment of such impost notwithstanding the nomenclature of the impost as given by the statute, to find whether it is compensatory or penal in nature.

30.24 The authority has to allow deduction under section 37(1) wherever such examination reveals the concerned impost to be purely compensatory in nature. Wherever such impost is found to be of a composite nature, that is, partly of compensatory nature and partly of penal nature, the authority would have to bifurcate the two components of the impost and give deduction of that component which is compensatory in nature and refuse to give deduction of that component which is penal in nature. The above principle was reiterated in the case of *Swadeshi Cotton Mills* (1998) 233 ITR 199.



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30.25 Further, in *CIT v Ahmedabad Cotton Mfg. Co. Ltd. [1993] 205 ITR 163(SC)*, the Supreme Court held that what needs to be done by an Assessing Authority under the Act, in examining the claim of an assessee that the payment made by such assessee was a deductible expenditure under section 37 although called a penalty, is to see whether the law or scheme under which the amount was paid, required such payment to be made, as penalty or as something akin to penalty, that is, imposed by way of punishment for breach for infraction of the law or the statutory scheme. If the amount so paid is found to be not a penalty or something akin to penalty due to the fact that the amount paid by the assessee was in exercise of the option conferred upon him under the levy, law or scheme concerned, then one has to regard such payment as business expenditure of the assessee, allowable under section 37 as incidental to business laid out and expended wholly and exclusively for the purposes of the business.

30.26 In case of *Malwa Vanaspati & Chemical Co. v. CIT [1997] 225 ITR 383(SC)*, it was held that where the assessee is required to pay an amount comprising both the elements of compensation and penalty, the compensation is allowable as business expenditure, but not the penalty.

30.27 Where the penalty or fine is in the nature of penalty or fine only, the entire amount thereof will have to be stated. As discussed above, with reference to certain penalty/penal interest courts have held that it is partially compensatory payment and partially in the nature of penalty. In such a case, on the basis of appropriate criteria, the amount charged will have to be bifurcated and only the amount relating to penalty may be stated.

### 31. Clause 21(b) - amounts inadmissible under section 40(a)

31.1 This clause is substantially expanded to furnish detailed information for deduction and deposit of TDS. Section 40(a) specifies certain amounts which shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession". The relevant provisions for A.Y. 2014-15 are as under:

- (i) **Non-Resident Payments:** Any interest, royalty, fees for technical services or other sum chargeable under the Income-tax Act which is payable outside India or in India to a non-resident or a foreign company 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 during the previous year or in the subsequent year before the expiry of the time prescribed under sub section (1) of section 200.

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Provided that where in respect of any such sum, tax has been deducted in any subsequent year or, has been deducted in the previous year but paid in any subsequent year after the expiry of the time prescribed under sub-section (1) of section 200, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Finance Act, 2014 has amended section 40(a)(i) to provide that if the tax deducted is paid during the previous year or in the subsequent year before the expiry of time prescribed for filling the tax return u/s. 139(1), the same shall be allowed as deduction in the previous year in which the tax is deducted.

- (ii) **Resident Payments:** 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 or 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 section 139(1).

As per first proviso to Section 40(a)(ia), where tax is deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in section 139(1), the expenditure is allowable as a deduction in the year in which such tax has been paid. The Finance Act 2012, inserted second proviso in section 40(a)(ia) with effect from 01-04-2013 (A.Y.2013-14) as a consequence to amendment in Section 201. The second proviso provides 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 clause (ia) of section 40(a), 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.

- (iii) Any sum paid on account of wealth tax.
- (iv) The Finance Act, 2013 inserted a sub-clause (iib) in section 40(a) with effect from A.Y. 2014-15. Accordingly, any amount paid by way of a Royalty, License Fees, Service Fees, Privilege Fees, Service Charges or any other fees or charge by whatever name called, which is levied

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exclusively on or which is appropriated directly or indirectly from a State Government undertaking by the State Government shall not be allowed as a deduction from the income under the head "profit and gains from business or profession".

- (v) Any payment which is chargeable under the head "salaries", if it is payable outside India or to a non-resident and if the tax has not been paid thereon nor deducted therefrom under Chapter XVII-B.
- (vi) Any payment to a provident or other fund established for the benefit of employees of the assessee, unless the assessee has made effective arrangement to secure that tax shall be deducted at source from any payment made from the fund which are chargeable to tax under the head "Salaries".
- (vii) Any tax actually paid by an employer referred to in clause (10CC) of section 10.

31.2 The Finance (No.2) Act, 2014 has amended the provisions of section 40(a)(ia) w.e.f. AY 2015-16 to disallow only 30% of any sum payable to a resident 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 under section 139(1). The first proviso to section 40(a)(ia) has also been amended to provide that where any sum on which 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 percent of such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

31.3 In respect of item (i) and (vi) above, the tax auditor should obtain in writing from the assessee the details of all payments debited to the profit and loss account. Where an actual remittance overseas has been made by the assessee during the relevant previous year without deducting any tax at source, the tax auditor may rely upon the legal opinion and/or certificates from chartered accountants based upon which remittances have been made without deduction of tax at source.. The tax auditor may refer SA 620, *Using the work of an auditor's expert* issued by ICAI for reliance on certificates / legal opinion. In this connection the tax auditor is advised to refer the applicable Double Taxation Avoidance Agreement (DTAA). Where no remittances have been made during the relevant year, the tax auditor may examine the relevant provisions vis-à-vis the agreement or correspondence in pursuant to which the liability is provided by the assessee in his books of account in order to determine whether any amount so provided is at all

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chargeable to tax under the Act. The tax auditor may use his professional judgement in these matters based upon decided cases and he may rely upon a legal opinion obtained by the assessee where no tax is required to be deducted in respect of the amount so provided. In case he disagrees with the stand taken by the assessee, he should give both the views in his report.

31.4 Under clause 21(b)(i)(A), the auditor is required to report payments to non residents on which tax is required to be deducted but not deducted in respect of interest, royalty, fees for technical services and other such chargeable amount under the Income tax Act. The Auditor is advised to give details under this clause for each individual payee.

31.5 Similarly under clause 21(b)(i)(B), the auditor is required to report payments on which tax is deducted but is not deposited within the time prescribed during the previous year or in subsequent year. Such details are also required to be given for each individual payee prescribed under Section 40(a)(i).

31.6 Under this sub-clause the tax auditor is required to report the details of payment on which tax is not deducted at source and also the details of payment on which tax has been deducted but not paid during the previous year or in the subsequent year before the expiry of time prescribed under section 200(1)/139(1). The tax auditor should maintain the following data in his working papers for the purpose of reporting under this sub-clause:

(a) Details of payment on which tax was not deducted:

Sr. No	Date of payment	Amount of payment	Nature of payment	Name and address of the payee	PAN of the payee, if available
1	2	3	4	5	6

(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)/139(1):

Sr. No.	Date of payment	Amount of payment	Nature of payment	Name and address of the payee	PAN of the payee, if available	Amount of tax deducted
1	2	3	4	5	6	7

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31.7 With the introduction of clause (ia) in section 40(a), the scope of disallowance of the expenditure has been widened to include interest, commission, brokerage, rent, royalty, fees for professional services or fees for technical services payable to a resident or amounts payable to a contractor or subcontractor, being resident for carrying out any work including supply of labour for carrying out any work. Under this sub-clause any payment of the expenses, specified therein on which tax is deductible under Chapter XVIIIB and such tax has not been deducted or after deduction has not been paid on or before the date of filing of return specified under section 139(1), is not eligible for deduction while computing income chargeable under the head "profits and gains of business or profession". Accordingly, such amount will be inadmissible and will be required to be disclosed under this clause. For this purpose the tax auditor will be required to examine whether the provisions relating to tax deduction at source have been complied with in respect of payments specified under the clause. For this purpose the tax auditor may examine the books of accounts and tax deduction returns pertaining to these payments.

31.8 Where the auditee claims deduction under the second proviso to sub-section (ia) it is deemed that he has deducted and paid the tax and hence such sum on which tax is so deemed to be deducted and paid is not inadmissible, the tax auditor should verify compliance with the requirements of section 201. He should also obtain and keep in his record a copy of certificate in Form 26A as required by section 201 read with section 40(a)(ia).

31.9 Under clause 21(b)(ii)(A), auditor is required to report payments to residents on which tax is required to be deducted but not deducted in respect of interest, royalty, fees for technical services and other such chargeable under Chapter XVII-B of the Income Tax Act. The auditor is advised to give details under this clause for each individual payee.

31.10 Similarly under clause 21(b)(ii)(B), auditor is required to report payments on which tax is deducted but is not deposited within the time prescribed during the previous year or in subsequent year. Such details are also required to be given for each individual payee prescribed under section 40(a)(ia).

31.11 Tax auditor should also verify that the particulars given under this clause do not differ from the particulars given under clause 34 of Form no. 3CD to the extent applicable. Under this sub-clause, the tax auditor is required to report the details of payment on which tax is not deducted at

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source and also the details of payment on which tax has been deducted but not paid on or before the due date specified in section 139(1). The tax auditor should maintain the following data in his working papers for the purpose of reporting under this sub-clause:

(a) Details of payment on which tax was not deducted:

Sr. No	Date of payment	Amount of payment	Nature of payment	Name and address of the payee	PAN of the payee, if available
1	2	3	4	5	6

(b) Details of payment on which tax has been deducted but has not been paid on or before the due date specified under section 139(1):

Sr. No.	Date of payment	Amount of payment	Nature of payment	Name and address of the payee	PAN of the payee, if available	Amount of tax deducted	Amount out of (5) deposited, if any
1	2	3	4	5	6	7	8

31.12 The Item no. (iii) of clause 21(b) requires reporting of any sum paid on account of fringe benefit tax under Chapter XIIH, wherever applicable. Since Fringe benefit tax was abolished by the Finance (No.2) Act, 2009 with effect from 1-04-2009, the tax auditor will be required to furnish information under this item only if the audit report relates to an assessment year to which the provisions of chapter XII H were applicable. For all other cases, the tax auditor may report "NIL" or "Not Applicable" as per the requirement of the format of e-filing utility. The provision relating to Fringe Benefit Tax (FBT) has been omitted from A.Y. 2010-11. If any such tax is paid during the year, the same is not allowed as deduction u/s. 40(a)(i)(c). The auditor is required to report such amount of tax paid under clause 21(b)(iii), if any liability has been incurred due to any order of any authority up to AY 2010-11 .

31.13 The amount of Wealth Tax paid is not allowed as a deduction u/s. 40(a)(ia) and thus is required to be reported under clause 21(b)(iv).

31.14 Finance Act, 2013 inserted new sub clause 40(a)(iib) w.e.f. A.Y. 2014-15 to provide that (a) any amount paid by way of a royalty, license fees, service fees, privilege fees, service charge or any other fees or charge by

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whatever name called, which is levied exclusively on; or (b) which is appropriated, directly or indirectly from, a State Government undertaking by the State Government is inadmissible expenditure. The explanation to this sub clause (iib) also defines a State Government undertaking. The Tax auditor should verify any such payment made by State Government undertaking to the State Government and should report under clause 21(b)(v).

31.15 The amount of salary which is paid outside India or to a non-resident in respect of which tax has not been deducted but which is required to be deducted under the applicable provisions of the Income Tax Act or tax has not been paid after deduction, the same is not allowed as a deduction u/s. 40(a)(iii) and the same is required to be reported under clause 21(b)(vi). This information is required to be given for each individual payee. The tax auditor should also furnish the date of payment along with the name and address of the payee. The tax auditor should maintain the following information in his working papers for the purpose of reporting in the format provided in the e-filing utility:

Sr No.	Date of payment	Amount of payment	Name of payee	PAN of the payee, if available	Address
1	2	3	4	5	6

31.16 Section 40(a)(iv) provides that any payment to a provident or other fund established for the benefit of employees of the assessee shall be disallowed, 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". The auditor is also required to report the same under item (vii) of this sub-clause.

31.17 Any tax paid by an employer on non-monetary perquisites is exempt in the hands of the employee as per section 10(10CC). Further, as per section 40(a)(v) the tax paid by the employer on non-monetary perquisites provided to employees shall not be deductible in computing profits and gains from business or profession. The tax auditor is required to report the amount of such tax paid by the employer, in case it is debited to the profit and loss account under clause 21(b)(viii).

31.18 In case where the assessee submits that any sum debited to profit and loss account is not inadmissible under the provisions of sub-section (a) of

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section 40, the tax auditor may exercise his judgement in the light of the applicable laws and report accordingly about the compliance of this provision. The tax auditor may rely upon the judicial pronouncements while taking any particular view. In case of difference of opinion between the tax auditor and the assessee, the tax auditor should state both the view points. In case of voluminous nature of the information, the tax auditor can apply materiality principles, tests checks and compliance tests for verifying the information required to be provided under this clause.

#### **32. Clause 21(c)- Amount debited to profit and loss account being, interest, salary, bonus, commission or remuneration inadmissible under section 40(b)/40(ba) and computation thereof;**

32.1 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.

32.2 Salary, bonus, commission or remuneration or interest are 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.

32.3 The inadmissible remuneration, salary, bonus or commission under section 40(b) has to be determined on the basis of the provisions of sub-clause (v) thereof read with the limits laid down therein. Such limits are laid down as a percentage of book profits. Explanation 3 to section 40(b) provides that "book profits" means the net profit, as shown in the profit and loss account for the relevant previous year, computed in the manner laid down in Chapter IV-D as increased by the aggregate amount of the remuneration paid or payable to all the partners of the firm if such amount has been deducted while computing the net profit. The inadmissible amount of salary, bonus, commission or remuneration is to be worked out after



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deducting interest allowable to partners as per the provisions of section 40(b). According to Explanation 4, "working partner" means an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner. It is advisable for the auditor to obtain from the assessee a detailed working of the inadmissible remuneration, salary, bonus or commission under section 40(b). He has to verify the computation from the instrument or agreement or any other document evidencing partnership including any supplementary documents or other documents effecting changes which would affect the computation of the inadmissible amounts under section 40(b).

32.4 Under section 40(b)(iv), any payment of interest to any partner which is authorised by, and is in accordance with, the terms of the partnership deed and relates to any period falling after the date of such partnership deed in so far as such amount exceeds the amount calculated at the rate specified under the Income-tax Act from time to time will not be admissible as a deduction.

32.5 Section 40(ba) lays down that any interest or remuneration paid by an AOP to its member shall not be allowed as a deduction to the AOP. It may also be noted that in computing such disallowance:

- (a) where interest is paid by AOP / BOI to a member who has also paid interest to AOP/ BOI, only net amount of interest, if any, shall be disallowed;
- (b) where a member is in a representative capacity, the disallowance of net interest paid by AOP/BOI shall be the amount of net interest received by the member in a representative capacity or by the person who is so represented by the member;
- (c) where a person who is a member in his individual capacity receives the interest for the benefit of or on behalf of any other person, then, interest so paid by AOP/ BOI shall not be disallowed;

32.6 In order to determine the amounts inadmissible under section 40(b), the tax auditor should obtain the computation of total income from the assessee.

32.7 In working out the inadmissible amount the tax auditor must have due regard to the Circular No.739 dated 25.3.1996 issued by the Board reproduced in **Appendix XI (Page no. 269)**.

32.8 The tax auditor should maintain the information in the following format as a part of his working papers and report appropriately in the format provided in the e-filing utility:

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Sr. No.	Nature of payments made to partner/member	Section 40(b)/40(ba)	Amount debited to profit and loss account	Amount admissible u/s 40(b)/40(ba)	Amount inadmissible u/s 40(b)/40(ba) [difference between (c) and (d)]	Remarks, if any
(a)	(b)	(c)	(d)	(e)	(f)	(g)

32.9 The tax auditor may note that the information required to be reported is the amount of inadmissible expenditure as per section 40(b) or 40(ba) and not the total amount debited to profit and loss account.

**33. Clause 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:

Serial Number	Date of Payment	Nature of Payment	Amount	Name and Permanent Account Number of the payee, if available
1	2	3	4	5

(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);

Serial Number	Date of Payment	Nature of Payment	Amount	Name and Permanent Account Number of the payee, if available
1	2	3	4	5

[Clause 21(d)]

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33.1 (a) As per the provisions of the sub-section (3) of section 40A where the assessee incurs any expenditure in respect of 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, exceeding rupees twenty thousand, no deduction would be allowed in respect of such expenditure. In case of payment made for plying, hiring or leasing of goods carriage, limit is Rs.35,000/- instead of Rs.20,000/-.

(b) Further, as per the provisions of section 40A(3A) where any allowance has been made in the assessment for any year in respect of any liability incurred by the assessee for any expenditure and subsequently during the previous year the assessee makes payment in respect thereof, otherwise than an account payee cheque drawn on a bank or account payee bank draft exceeding Rs.20,000, the payment so made shall be deemed to be the profits and gains of business or profession and accordingly chargeable to income tax with respect to that previous year. In case of payment made for plying, hiring or leasing of goods carriage, limit is Rs.35,000/- instead of Rs.20,000/-.

(c) Further, no disallowance would be made if the payment or aggregate of payments, exceeding Rs. 20,000 (Rs. 35000 in case of plying, hiring or leasing of goods carriage) is made to a person in a day otherwise than by an account payee cheque drawn on a bank or account payee bank draft in respect of cases and circumstances prescribed under Rule 6DD having regard to the nature and extent of banking facilities available, considerations of business expediency and other relevant factors. Notification No.97/2008 dated 10.10.2008 has amended Rule 6DD w.e.f. A.Y. 2008-09

33.2 For the purpose of furnishing the above particulars, the tax auditor should obtain a list of all cash payments in respect of expenditure exceeding Rs.20,000 (Rs.35000/- in case of plying, hiring or leasing goods carriages w.e.f. 1.10.2009) made by the assessee during the relevant year which should include the list of payments exempted in terms of Rule 6DD with reasons. This list should be verified by the tax auditor with the books of account in order to ascertain whether the conditions for specific exemption granted under clauses (a) to (i) of Rule 6DD are satisfied. Details of payments which do not satisfy the above conditions should be stated under this clause.

33.3 The tax auditor has to take into account the technological advancements in the field of banking and information technology where payments have been taken other than through an account payee cheque or

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bank draft. Rule 6DD of the Rule specifically exempts the cases where the payment is made by any letter of credit arrangements through a bank; a mail or telegraphic transfer through a bank; a book adjustment from any account in a bank to any other account in that or any other bank; a bill of exchange made payable only to a bank; the use of electronic clearing system through a bank account; a credit card; a debit card. 33.4 Practically, it may not be possible to verify each payment, reflected in the bank statement, as to whether the payment 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 for expenditure referred to in section 40A(3) and section 40A(3A) 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 fact 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.

33.4 The tax auditor should maintain the following particulars in his audit working papers file for the purpose of reporting in the format provided in the e-filing utility:

Sl. No.	Nature and particulars of expenditure	Date of payment	Payment or aggregate payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft	Total amount of expenditure	Name and Permanent Account number of the payee, if available	Remarks
1	2	3	4	5	6	7

33.5 Wherever possible individual items of inadmissible expenses may be given. However, where, in view of the large volume of transactions it is not

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possible to give individual items of inadmissible amounts, the tax auditor may furnish such details under broad heads of accounts.

33.6 Items of expenditure in respect of which specific exemption has been given under Clauses (a) to (l) of Rule 6DD are not required to be stated under this clause.

#### **34. Clause 21(e) - provision for payment of gratuity not allowable under section 40A(7);**

34.1 As per section 40A(7), the deduction shall be allowed in relation to any provision made by the assessee for the purpose of payment of a sum by way of any contribution towards an approved gratuity fund, or for the purpose of payment of any gratuity, that has become payable during the previous year.

34.2 The tax auditor should call for the order of the Commissioner of Income-tax granting approval to the gratuity fund, verify the date from which it is effective and also verify whether the provision has been made as provided in the trust deed.

34.3 In case the provision made for payment of gratuity is not allowable under section 40A(7), the same is to be stated under this sub-clause.

#### **35. Clause 21(f) - any sum paid by the assessee as an employer not allowable under section 40A(9);**

35.1 Under section 40A(9) any payment made by an employer towards the setting up or formation of or as contribution to any fund, trust, company, association of persons, body of individuals, society registered under the Societies Registration Act, 1860, or other institutions (other than contributions to recognised provident fund or approved superannuation fund or notified pension scheme or approved gratuity fund) is not allowable. The tax auditor should furnish the details of payments which are not allowable under this section.

35.2 It may be noted that section 40A(9) allows deduction of any contributions made as an employer towards recognized provident fund or approved superannuation fund or notified pension scheme or approved gratuity fund or as required by or under any other law for the time being in force. Thus, any contribution made to Employees' Welfare Co-op Society will not be allowed as a deduction in the case of the employer company under section 40A(9), unless such contribution is required by or under any other law for the time being in force. *Instruction: No. 1799, dated 3-10-1988.*

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#### 36. Clause 21(g) - particulars of any liability of a contingent nature:

36.1 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.

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

36.3 The tax auditor should maintain the following information in his working papers for the purpose of reporting in the format provided in the e-filing utility

Nature of liability	Amount
1	2

#### 37. Clause 21(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;

37.1 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.

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37.2 As per sub-section (2), the Assessing Officer shall determine the amount of expenditure incurred in relation to such income, which does not form part of the total income under the Act. Such determination should be in accordance with the method as may be prescribed. Such power of the Assessing Officer can be exercised only when he, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee.

37.3 Sub-section (3) provides that the provisions of subsection (2) shall also apply in relation to a case where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under this Act.

37.4 The expenditure which is relatable to the income which does not form part of the total income is not allowed as a deduction in terms of section 14A of the Act. Such income are dealt with in Part III- Incomes Which Do Not Form Part Of Total Income. Section 10 deals with Incomes not included in total income. Sections 10A to 10C deals with the special provisions in respect of the specified undertakings. In general, an assessee may have besides his business income, income from agriculture which is exempt under sub-section (1), share of profit in a partnership firm which is exempt under sub-section (2A), income from dividends referred to in section 115-O which is exempt under sub-section (34), long term capital gains on the transfer of equity shares which is exempt under sub-section (38) etc. In all such cases, the expenditure relating to the income which is not included in total income is inadmissible under section 14A. In case of an investment in a partnership firm, while the interest and the salary received by the partner are taxable, the share of profit is exempt. The amount of inadmissible expenditure depends on the facts and circumstances of each case.

37.5 The Central Board of Direct Taxes, had through Income-tax (Fifth Amendment) Rules, 2008 inserted a new Rule 8D which lays down the method for determining the amount of expenditure in relation to income not includible in total income. Sub-rule (1) of Rule 8D provides that having regard to the accounts of the assessee of a previous year, if the Assessing Officer is not satisfied with the correctness of the claim of expenditure made by the assessee or with the claim made by the assessee that no expenditure has been incurred, in relation to income which does not form part of the total income under the Act for such previous year, he shall determine the amount of such inadmissible expenditure in accordance with the method of computation laid down in sub-rule (2) of Rule 8D.

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37.6 Sub-rule (2) of Rule 8D provides for the method of computation of the expenditure in relation to income not forming part of the total income. The disallowance shall be the aggregate of the following:

- (i) the amount of expenditure directly relating to income which does not form part of total income;
- (ii) in a case where the assessee has incurred expenditure by way of interest during the previous year which is not directly attributable to any particular income or receipt, an amount computed in accordance with the following formula, namely :

$$A \times \frac{B}{C}$$

Where A = amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year;

B = the average of value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

C = the average of total assets as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year.

- (iii) an amount equal to one-half per cent of the average of the value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year.

"Total Assets" for the purpose of Rule 8D shall mean, total assets as appearing in the balance sheet excluding the increase on account of revaluation of assets but including the decrease on account of revaluation of assets.

37.7 The method prescribed under sub-rule (2) of Rule 8D is applicable when the Assessing Officer is not satisfied with the correctness of the claim of expenditure made by the assessee or with the claim made by the assessee that no expenditure has been incurred. Normally this situation would arise at the time of assessment i.e. after the tax audit has been completed and the return has been filed. Therefore, at the time of tax audit the tax auditor will have to verify the amount of inadmissible expenditure as



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determined by the assessee. The method under sub-rule (2) of Rule 8D is to be adopted by the Assessing Officer when he is not satisfied with the amount as determined by the assessee. Rule 8D does not mandate that the assessee should necessarily compute the disallowance as per the method prescribed under sub rule (2). Therefore, the assessee may or may not adopt the same.

37.8 It is primarily the responsibility of the assessee to furnish the details of amount of deduction inadmissible in terms of section 14A i.e. in respect of the expenditure incurred in relation to income, which does not form part of the total income. The tax auditor shall examine the details of amount of inadmissible expenditure as furnished by the assessee. While carrying out such examination the tax auditor is entitled to rely on the management representation. However, Standard on Auditing (SA) 580, *Written representations* may be referred to.

37.9 The tax auditor will verify the amount of inadmissible expenditure as estimated by the assessee with reference to established principles of allocation of expenditure based on logical parameters like proportion of exempt and taxable income recorded, turnover, man hours spent to earn the relevant income etc. For allocation of interest between taxable and non-taxable income, the quantum of investment, the period and the rate of interest are generally the relevant factors to be considered. This requires proper estimates to be made by the assessee. The tax auditor is required to audit such estimates. Attention is invited to Standard on Auditing - 540 "Audit of Accounting Estimates".

37.10 An assessee may claim that no expenditure has been incurred by him in relation to income which does not form part of the total income under the Act. Even in such a case the provisions of section 14A will apply. Accordingly, the tax auditor is required to verify such contention of the assessee.

37.11 As stated before the method prescribed under sub-rule (2) of Rule 8D is to be adopted by the Assessing Officer when he is not satisfied with the correctness of claim made by the assessee. As per clause (i) of sub-rule (2) the expenditure which is directly relatable to income which does not form part of total income is inadmissible expenditure. Besides such expenditure there may be expenditure such as interest, which is relatable to both taxable and non-taxable income which needs to be properly allocated while calculating the inadmissible amount. Interest which, can be directly attributable to any particular income or receipt chargeable to tax needs to be excluded while

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determining the inadmissible amount. Clause (ii) of sub-rule (2) of rule 8D deals with allocation of interest which, is not directly attributable to any particular income or receipt. However the variable A used in the formula in clause (ii) of sub- rule (2) is said to be equal to the amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year. It may be seen that what is proposed to be allocated as per clause (ii) is interest which is not directly attributable to any particular income or receipt. Therefore, variable A is the amount of expenditure by way of interest other than the amount of interest directly attributable to any non taxable income as per clause (i) and also interest which may be directly attributable to any taxable income. Interest on term loan may be an example of such interest which is generally related to taxable income and is therefore excluded.

37.12 The broad principles enunciated in para 16.3 may be kept in mind while verifying the amount of inadmissible expenditure. After verifying the amount of inadmissible expenditure, if the tax auditor:

- (a) is in agreement with the assessee, he should report the amount with suitable disclosures of material assumptions, if any.
- (b) is not in agreement with the assessee with regard to the amount of expenditure determined, he may give:

**- A qualified opinion:**

A qualified opinion can be given when the auditor is of the opinion that the effect of any disagreement with the assessee is not so material and pervasive as to require an adverse opinion or limitation on scope is not so material and pervasive as to require a disclaimer of opinion.

**- An adverse opinion:**

The auditor in rare circumstances may come across a situation where the impact of his disagreement about the computation of such inadmissible expenditure is so material and pervasive that it affects the overall opinion. In such a case the tax auditor may give an adverse opinion.

**-The disclaimer of opinion:**

When the assessee has neither provided the basis nor the supporting documents, for the claim of such inadmissible expenditure, then due to limitation on the scope of auditors work, the auditor can give disclaimer of opinion.

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**38. Clause 21(i)- amount inadmissible under the proviso to section 36(1)(iii).**

38.1 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.

38.2 The proviso thereunder (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.

38.3 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 proviso. 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.

38.4 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.

38.5 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".

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

38.7 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.

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### 39. Clause 22- Amount inadmissible under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006

#### [Clause (22)]

39.1 This clause was 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.

39.2 The tax auditor is required to state the amount of interest inadmissible under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006. The Micro, Small and Medium Enterprises Development Act, 2006 (MSME Act) is an Act to provide for facilitating the promotion and development and enhancing the competitiveness of micro, small and medium enterprises and for matters connected therewith or incidental thereto.

39.3 Section 23 of the MSME Act lays down that an interest payable or paid by the buyer, under or in accordance with the provisions of this Act, shall not for the purposes of the computation of income under the Income-tax Act, 1961 be allowed as a deduction.

39.4 The inadmissible interest has to be determined on the basis of the provisions of the MSME Act. Section 16 of the MSME Act provides for the date from which and the rate at which the interest is payable. Accordingly, where a buyer fails to make payment of the amount to the supplier, as required under section 15, the buyer shall, notwithstanding anything contained in any agreement between the buyer and the supplier or any law for the time being in force, be liable to pay compound interest with monthly rests to the supplier on that amount from the appointed date or, as the case may be, from the date immediately following the date agreed upon, at three times of the bank rate notified by the Reserve Bank.

39.5 Section 15 of the MSME Act, requires the buyer to make payment on or before the date agreed upon in writing, or where there is no agreement in this behalf, before the appointed day. It also provides that the period agreed upon in writing shall not exceed forty five days from the day of acceptance or the day of deemed acceptance.

39.6 Section 22 of the MSME Act provides that where any buyer is required to get his annual accounts audited under any law for the time being in force, such buyer shall furnish the following additional information in his annual statement of accounts, namely:-

- (i) The principal amount and interest due thereon (to be shown separately) remaining unpaid to any supplier as at the end of each accounting year;

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- (ii) The amount of interest paid by the buyer in terms of Section 16, along with the amount of payment made to supplier beyond the appointed date during each accounting year;
- (iii) The amount of interest due and payable for the delay in making payment (which have been paid but beyond the appointed day during the year) but without adding the interest specified under this Act;
- (iv) The amount of interest accrued and remaining unpaid at the end of each accounting year; and
- (v) The amount of further interest remaining due and payable even in the succeeding years, until such date when the interest dues as above are actually paid to the small enterprise, for the purpose of disallowance as a deductible expenditure under section 23.

39.7 Where the tax auditor is issuing his report in Form No.3CB, he should verify that the financial statements audited by him contain the information as prescribed under section 22 of the MSME Act. If no disclosure is made by the auditee in the financial statements he should give an appropriate qualification in Form No.3CB, in addition to the reporting requirement in clause 22 of Form No. 3CD.

39.8 The tax auditor while reporting in respect of clause 22 should take the following steps:

- (a) The auditor should seek information regarding status of the enterprise i.e. whether the same is covered under the Micro, Small and Medium Enterprises Development Act, 2006. Where the information is available and has been disclosed the same should be reported as such in Form No. 3CD. Where the information is not available the auditor should also mention the same in the Form No.3CD.
- (b) Since Section 22 of the Micro, Small and Medium Enterprises Development Act, 2006 requires disclosure of information, the tax auditor should cross check the disclosure made in the financial statements.
- (c) Obtain a full list of suppliers of the assessee which fall within the purview of the definition of "Supplier" under section 2(n) of the Micro, Small and Medium Enterprises Development Act, 2006. It is the responsibility of the auditee to classify and identify those suppliers who are covered by this Act.

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- (d) Review the list so obtained.
- (e) Verify from the books of account whether any interest payable or paid to the buyer in terms of section 16 of the MSME Act has been debited or provided for in the books of account.
- (f) Verify the interest payable or paid as mentioned above on test check basis.
- (g) Verify the additional information provided by the auditee relating to interest under section 16 in his financial statement.
- (h) If on test check basis, the auditor is satisfied, then the amount so debited to the profit and loss account should be reported under clause 22.

39.9 Where the tax auditor, upon due verification, finds that the auditee has neither provided for nor paid any interest payable under the MSME Act, the no amount is inadmissible under section 23 of MSME Act. In such a case, appropriate reporting should be made against this clause in the format provided in the e-filing utility.

39.10 A question may come up, as to what would be disallowance, in case the auditee is liable to pay any interest under MSME Act, but he has not provided the interest in his accounts. In such a case, there can be no disallowance, as he has not claimed the same in his accounts. But whenever he pays and claim such interest, the same will be disallowable in year of payment. In case the auditee has adopted mercantile system of accounting, the non-provision may affect true and fair view and the auditor should give suitable qualification.

39.11 The relevant extracts of the MSME Act are given in *Appendix XII (Page no 271)*.

### **40. Particulars of payments made to persons specified under section 40A(2)(b). [Clause 23]**

40.1 Section 40(A)(2) provides that expenditure for which payment has been or is to be made to certain specified persons listed in the section- Refer *Appendix XIII (Page no. 273)* may be disallowed if, in the opinion of the Assessing Officer, such expenditure is excessive or unreasonable having regard to:

- (i) the fair market value of the goods, services or facilities for which the payment is made; or
- (ii) for the legitimate needs of business or profession of the assessee; or

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- (iii) the benefit derived by or accruing to the assessee from such expenditure.

Further, proviso to section 40A(2)(a) provides that no disallowance on account of any expenditure being excessive or unreasonable having regard to the fair market value, shall be made in respect of a specified domestic transaction referred to in section 92BA, if such transaction is at arm's length price as defined in clause (ii) of section 92F.

40.2 The section enjoins on the Assessing Officer the power to fix the quantum of disallowance. Under this clause, the particulars of payments coming under this sub-section are to be stated. The following steps may be taken by the tax auditor in this connection:

- (a) Obtain full list of specified persons as contemplated in this section.
- (b) Obtain details of expenditure/payments made to the specified persons.
- (c) Scrutinise all items of expenditure/payments to the above persons.
- (d) It may be difficult to locate all such payments and it may also involve a time consuming effort. It is, however, possible to localise the area of enquiry by ascertaining the following:
  - (i) Call for all contracts or agreements entered into by the assessee and list out the contracts or agreements entered into with the specified persons and segregate the items of payments made to them under these agreements.
  - (ii) In case of payments for purchases and expenses on credit basis, the appropriate ledger accounts can be scrutinised to identify the dealings with the specified persons.
  - (iii) In case of cash purchases and expenses, the purchase or expense account should be scrutinised. It may be difficult to identify such payments in each and every case where the volume of transactions is rather huge and voluminous. Therefore, it may be necessary to restrict the scrutiny only to such payments in excess of certain monetary limits depending upon the size of the concern and the volume of business of the assessee.
  - (iv) In case of a large company, it may not be possible to verify the list of all persons covered by this section and, therefore, the information supplied by the assessee can be relied upon. In this context, a reference may be made to Circular No.143 dated 20.8.1974, issued by the Board, in which it is clarified that an

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tax auditor can rely upon the list of persons covered under Section 13(3) as given by the managing trustee of a Public Trust. (Refer Appendix 'B' of "A Guide to Audit of Public Trusts under the Income-tax Act" published by the Institute). Where the tax auditor relies upon the information in this regard furnished to him by the assessee it would be advisable to make an appropriate disclosure.

40.3 The tax auditor should maintain the following information in his working papers for the purpose of reporting in the format provided in the e-filing utility: :

Name of the related party	PAN of related person	Relation	Date	Payment made (Amount)
1	2	3	4	5

40.4 The Finance Act, 2012 had amended Section 40A(2)(a) to provide that the transactions referred to in Section 92BA (called Specified Domestic Transactions) with persons referred to in 40A(2)(b) shall be at Arm's Length Price. The tax auditor is advised to refer the "Guidance Note on Report under section 92E of the Income tax Act, 1961" issued by ICAI for compliance of these provisions.

### 41. Amounts deemed to be profits and gains under section 32AC, 33AB or 33ABA or 33AC.

[Clause 24]

41.1 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 31<sup>st</sup> day of March, 2013 but before the 1<sup>st</sup> 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



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

41.2 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.

41.3 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.

41.4 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 31<sup>st</sup> 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 1<sup>st</sup> day of April, 2005.

41.5 The tax auditor should maintain the following information in his working papers for the purpose of reporting in the format provided in the e-filing utility:

Section	Description	Amount
1	2	3

**42. Any amount of profit chargeable to tax under section 41 and computation thereof.**

**[Clause 25]**

42.1 (i) 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

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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.

(ii) 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 is 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.

(iii) *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.

(iv) 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.]

42.2 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

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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 scrap 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.

42.3 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.

42.4 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.

42.5 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.

42.6 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.

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42.7 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.

42.8 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.

42.9 The tax auditor should maintain the following in his working papers for the purpose of furnishing details required in the format provided in the e-filing utility:

Sr. No.	Name of person	Amount of income	Section	Description of transaction	Computation if any
1	2	3	4	5	6

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

- (A) pre-existed on the first day of the previous year but was not allowed in the assessment of any preceding 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);

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**(b) not paid on or before the aforesaid date.**

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

**[Clause 26]**

43.1 In the case of an assessee maintaining its accounts on the mercantile system, the tax auditor should verify the aforesaid particulars of section 43B from the books of account for the year under audit as well as from the books of account, vouchers and documents of the immediately succeeding assessment year as well as return of income for the earlier assessment years so that the information about the aforesaid payments made in the subsequent year can be furnished.

43.2 Section 43B provides that notwithstanding anything contained in any other provisions of the Act, the following amounts shall be allowed as deduction in computing the business income of an assessee in the previous year in which such amounts are actually paid:

- (a) any tax, duty (sales tax, value added tax, service tax, excise duty, municipal/property tax, etc.), cess or fee, by whatever name called, payable by the assessee under any law for the time being in force.
- (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.
- (c) any bonus or commission payable by the assessee to its employees for services rendered, where such sum would not have been payable to him as profits or dividend, if it had not been paid as bonus or commission.
- (d) interest on any loan or borrowing from any public financial institution, a state financial corporation or a state industrial investment corporation payable in accordance with the terms and conditions of the agreement governing such loan or borrowing.
- (e) 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.
- (f) any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee.

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43.3 All the payments referred in clause (a) to (f) above whether pre-existed on the first day of previous year but not allowed in assessment of any preceding previous years or incurred in the previous year are to be reckoned. In respect of the liability which pre-existed on the first day of the previous year is allowable as deduction if paid during the previous year. This is required to be reported in clause 26(A)(a). In respect of the liability which is incurred in the previous year is allowable to the extent it is paid on or before the due date for furnishing the return of the income under section 139(1). Such items are to be disclosed in clause 26(B)(a).

43.4 The tax auditor, in his tax audit report, should, therefore, clearly distinguish the liability incurred during the previous year in respect of all the specified sums referred to in clauses (a) to (f) from the liability that pre-existed on the first day of the relevant previous year.

43.5 If the assessee is following the cash basis of accounting, sums referred to in clause (a), (b), (c), (d), (e) and (f) of section 43B which are debited to the profit and loss account will be allowable as they would have been actually paid during the year.

43.6 Under the first proviso to section 43B, deduction is available in respect of any sum which is actually paid by the assessee on or before the due date applicable in his case for furnishing the return of income under sub-section (1) of section 139. Since the due date of filing of the return would usually be subsequent to the signing of the tax audit report the tax auditor would be able to give information in respect of matters only upto the date of signing of the tax audit report. The payment made subsequent to that date but before the date of filing of the return, will still be eligible for deduction under section 43B. Where due date for filing of return of income is extended, payments made upto the extended due date also qualify for deduction.

43.7 The provision made in the accounts for excise duty payable on finished goods in the bonded warehouse will also have to be disclosed under this clause. For enabling the assessee to claim this amount as a deduction the tax auditor may have to verify that the said goods have been cleared and that excise duty thereon has been paid or adjusted against CENVAT credits before the due date applicable in his case for furnishing the return of income under section 139 (1).

43.8 Under section 43B(a), sales-tax when paid is allowed as a deduction. Although under clause (a) of section 43B items that have been debited to the profit and loss account but not paid during the previous year, are to be specified, where it is the practice of the company to maintain a separate

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sales-tax/service tax/excise duty account and treat the sales tax/excise duty collected as a liability, it would be necessary to show by way of note under this clause, the amount of sales tax/excise duty collected but not paid. In case, any sum has been paid before the due date of filing the return, the date and the amount of payment along with the amount paid should also be disclosed.

43.9 There are different legal decisions with respect to allowability of employees contribution towards PF, EPF, etc not paid within due date. Bombay High Court in the case *CIT vs Pamwi Tissues Ltd (2008)215 CTR (Bom)150* and Gujarat High Court in the case of *CIT vs. Gujarat State Road Transport Corp. (2014) 223 taxmann 398 (Guj.)* held that employees contribution not paid within the due dates prescribed in Explanation to section 36(1)(va) was disallowable under section 43B. On the other hand Delhi High Court in the following cases has held in the favour of assesseees.

*CIT vs Dharmendra Sharma 297 ITR 320*

*CIT vs P.M. Electronics Ltd 313 ITR 161*

*CIT vs AIMIL Ltd and others 321 ITR 508*

43.10 It may be noted that emoluments in the nature of good work reward, incentives or ex-gratia are not bonus or commission as contemplated under section 36(1)(ii) but are deductible under section 37 of the Act as held by *Delhi High Court in Shri Ram Pistons and Rings Ltd. 307 ITR 363 and Autopins (India) Ltd. 192ITR161*.

43.11 The Explanations 3C and 3D to section 43B clarify that a deduction of any sum being interest payable under clause (d) and clause (e) of section 43B shall be allowed, if such interest has been actually paid and any interest referred to in that clause which has been converted into a loan or advance shall not be deemed to have been actually paid. Circular No.7/2006 dated 17<sup>th</sup> July, 2006 observes that the clarificatory Explanations only reiterate the rationale that conversion of interest into a loan or borrowing or advance does not amount to "actual payment". The circular clarifies that the unpaid interest whenever actually paid to the bank or financial institution will be in the nature of revenue expenditure deserving deduction in the computation of income. Therefore, the converted interest, by whatever name called, in the wake of its conversion into a loan or borrowing or advance, will be eligible for deduction in the computation of income of the previous year in which the converted interest is 'actually paid'. In other words, nomenclature of the sum of converted interest will make no difference as the sum of converted interest

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whenever is actually paid will not represent repayment of the principal. The circular clarifies that the fundamental principle remains that once an amount has been determined as interest payable to the banks or financial institutions, any subsequent change of nomenclature of interest will not affect its allowability and deduction in terms of section 43B will have to be allowed on its actual payment. The Assessing Officer would therefore be justified in seeking a certificate from the assessee to be obtained by the assessee from the lender bank or financial institution etc. as evidence of "actual payment" of interest to banks or financial institutions.

43.12 As per clause (f) sum payable by the assessee as an employer in lieu of any leave at the credit of his employees will be disallowed if not paid before the due date of filing of the return under section 139 (1).

43.13 The above particulars are required to be given irrespective of the fact whether they have been debited to profit and loss account or not and such a fact should be stated under this clause. For example, where excise, sales tax, etc. collected is accounted for as a Balance Sheet item.

43.14 In some cases the tax auditor may find amounts of the nature referred to in section 43B being credited to the profit and loss account although the relevant provisions for such liability had not been allowed as a deduction in any previous year in view of the specific provisions of section 43B requiring actual payment as a condition precedent to allowance. The amounts so credited to the profit and loss account are not chargeable to tax since the conditions referred to in section 41(1) have not been satisfied. The tax auditor should identify such items and maintain the same in his working papers.

43.15 The tax auditor should maintain the following information in his working papers for the purpose of reporting in the format provided in the e-filing utility;

S No	Section	Nature of liability	Amount
1	2	3	4

44. (a) Amount of Central Value Added Tax credits availed of or utilized during the previous year and its treatment in the profit and loss account and treatment of outstanding Central Value Added Tax credits in the accounts.



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**45. (b) Particulars of income or expenditure of prior period credited or debited to the profit and loss account.**

**[Clause 27 (a) and (b)]**

44.1 Sub-clause (a) requires the factual reporting about the amount of CENVAT credits availed of or utilised during the year as well as its treatment in profit and loss account and treatment of outstanding CENVAT credits in the accounts. CENVAT credit Rules, 2002 were first introduced in place of MODVAT credit and thereafter, effective 10 September 2004, CENVAT Credit Rules, 2004 have now become applicable. CENVAT credit is available on eligible inputs, input services and capital goods. Such credits are utilized for the payment of the excise duty and service tax liability. Accordingly the tax auditor should check relevant statutory records maintained under the Central Excise Rules, 2002 and the records maintained under CENVAT Credit Rules, 2004 and ascertain therefrom the amount of credit on eligible inputs, input services and the capital goods and the amount utilised during the previous year. Records maintained in RG-23, wherever available should also be verified.

44.2. The tax auditor should verify that there is a proper reconciliation between balance of CENVAT credit in the accounts and relevant excise and service tax records. The tax auditor should report the amount of CENVAT availed and utilised under this sub-clause. In a given case CENVAT availed may be lesser than the CENVAT credit utilised during the year on account of opening balance in CENVAT account or vice-versa and as such it would be advisable, in order to avoid any misleading conclusion and inferences, to report the opening and closing balances of CENVAT. Further the sub-clause requires reporting of the credits availed of or utilized during the previous year, it is desirable to report both the credits availed and the credits utilized.

44.3 In so far as the reporting of accounting treatment of CENVAT credit is concerned the clause requires that its treatment in profit and loss account and the treatment of outstanding CENVAT credit in the account have to be reported upon.

44.4 Where the assessee follows exclusive method of accounting, the excise duty paid on purchase of raw material, capital goods and service tax paid on input services is debited to the CENVAT/ Service Tax Credit Receivable Account and not as part of the purchase cost of raw material, capital goods or cost of input services. The credit utilized is debited to the Excise Duty/ Service Tax Payable A/c and credited to CENVAT/ Service Tax

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Credit Receivable Account. Thus, the credit availed and utilized will not have any impact on the profit and loss account.

44.5 The reporting requirement under clause 14(b) of Form No.3CD is a requirement distinct and separate from the reporting requirement under this clause. The tax auditor should verify that information furnished under this sub-clause is compatible with the information furnished under clause 14(b).

44.6 The tax auditor should consider the above guidance while reporting in the format provided in the e-filing utility with respect of this clause.

44.7 With regard to reporting of the amount of CENVAT credits availed or utilized during the previous year and its treatment in the profit and loss account wherever possible, it is advisable to give the details of the credit availed and utilized as separate line items.

44.8 With regard to reporting of the treatment of outstanding CENVAT Credits in the account, it is desirable to mention the opening and the closing outstanding balances in the CENVAT Credits accounts as separate line items. The account in which the outstanding amount is appearing should also be mentioned appropriately..

44.9 The tax auditor should maintain the following information in his working papers for the purpose of reporting in the format provided in the e-filing utility:

CENVAT	Amount	Treatment in Profit & Loss /Accounts
Opening balance		
CENVAT Availed		
CENVAT utilized		
Closing/outstanding Balance		

#### 45. Clause 27(b)

45.1 It may be noted that information under this clause would be relevant only in those cases where the assessee follows mercantile system of accounting. Under cash system of accounting, expenses debited/ income credited to the profit and loss account would be current *year's* expenses/income even though they may relate to earlier years. The tax auditor should obtain the particulars of expenditure or income of any earlier year debited or credited to the profit and loss account of the relevant

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previous year when mercantile system of accounting is followed. In the case of a person whose accounts of the business or profession have been audited under any other law, the information may be available from annual 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, however, a close scrutiny of the ledger in regard to the period for which expenditure or income is entered in the account books may be necessary.

45.2 It may be noted that there is a difference between expenditure of any earlier year debited to the profit and loss account and the expenditure relating to any earlier year, which has crystallised during the relevant year. Material adjustments necessitated by circumstances which though related to previous periods but determined in the current period, will not be considered as prior period items.

45.3 In such cases, though the expenditure may relate to the earlier year, it can be considered as arising during the year on the basis that the liability materialised or crystallised during the year and such cases will not be reported under this clause. Similar consideration will apply in relation to income also.

45.4 In AS - 5 as also in AS II notified by the Government under section 145, it has been explained that material charges (expenses) or credits (income) which arise in the current year as a result of errors or omissions in the accounts of the earlier years will be considered as prior period items. In view of this, the statutory auditor would normally take into consideration all items of prior period income and expenditure while giving his report on the financial statements. It would, therefore, be advisable for the tax auditor to ascertain the circumstances under which a particular expenditure has not been considered as a prior period expenditure. If, on making the enquiries he comes to the conclusion that a particular item has to be treated as prior period expenditure, he should disclose the same against this sub-clause.

45.5 The tax auditor should maintain the following information in his working papers file for the purpose of reporting in the format provided in the e-filing utility:

Sr. No.	Type	Particulars	Amount	Prior Period to which it relates (Year in yyyy-yy format)
1	2	3	4	5

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**46. 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.**

**[Clause 28]**

46.1 Section 56(2)(viiia) provides that where a firm or a company not being a company in which the public are substantially interested, receives, in any previous year any property being shares of a company (not being a company in which the public is substantially interested,

- (i) without consideration, the aggregate fair value of which exceeds rupees fifty thousand, the whole of the aggregate fair market value of such property
- (ii) for a consideration which is less than the aggregate fair market value of the property by an amount exceeding fifty thousand rupees, the aggregate fair market value of such property as exceeds such consideration

shall be chargeable to income-tax under the head "Income from other sources"

46.2 Section 56(2)(viiia) does not apply to the property received by way of a transaction not regarded as transfer under section 47(via), 47(vic), 47(vicb), 47(vid) and 47(vii). The fair market value of shares means the value determined in accordance with the method prescribed in rule 11UA of the Income-tax Rules, 1962.

46.3 Since section 56(2)(viiia) is applicable to firms and companies in which public is not substantially interested, reporting under this clause is required only for them and not for other assesseees. The auditor should obtain from the auditee, a list containing the details of shares received, if any, by him from any other company and verify the same from the books of accounts and other relevant documents. Such shares, if received will be reflected in the books of accounts either as investments or as stock in trade. In case such shares are received without consideration, the same may not be reflected in the books of accounts. Such shares may be verified from the relevant documents such as share certificates issued, if any, demat account statement etc. In either case, the same have to be reported under this clause. Attention is invited to the provisions of section 2(18) which defines the company in which public are substantially interested.

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46.4 For reporting under this clause, the auditor has to consider the provisions of Rule 11UA(1)(c) 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
- (c) fair market value of unquoted equity shares
- (d) fair market value of unquoted shares and securities other than equity shares in a company which are not listed in any recognized stock exchange

46.5 Where for determining the fair market value of unquoted shares and securities other than equity shares in a company which are not listed in any recognized stock exchange, 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".

46.6 The auditor should maintain the following information in his working paper file for the purpose of reporting in the format provided in the e-filing utility:-

Sr. No.	Name of the person from whom shares have been received	PAN of the person, if available	Nature of shares (Quoted in RSE/ Quoted in URSE/ unquoted shares etc)	Name of the Company whose shares received	CIN of the company	No. of Shares Received	Fair Market value as per Rule 11UA(1)(c)	Consideration paid	Amount taxable under section 56(2)(vii a) (if the difference (e)-(f) exceeds Rs.50,000)	Remarks, if any
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)	(k)

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**47. 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.**

**[Clause 29]**

47.1 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".

47.2 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.

47.3 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, licences, franchises or any other business or commercial rights of similar nature, whichever is higher.

47.4 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 assessee. 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.

47.5 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:

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- (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

47.6 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.

47.7 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".

47.8 The auditor should maintain the following information in his working paper file for the purpose of reporting in the format provided in the e-filing utility:-

Sr. No.	Name and status of the person to whom shares have been issued	PAN of person, if available	Nature of shares (Quoted in RSE/Quoted in URSE/unquoted equity shares etc.)	No. of Shares issued	Consideration received	Fair Market value as per Rule 11UA(1) (c)/11UA (2)	Face value of shares issued	Amount taxable under section 56(2)(viib) (Report the difference (e)-(f), ONLY if (e) is greater than (g), else report "Not Applicable")
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)

48. 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].

[Clause 30]

48.1 Details of the amount borrowed on hundi (including interest on such amount borrowed) and details of repayment otherwise than by an account

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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 6<sup>th</sup> June,1977 issued by Board explaining the provisions of section 69D - vide **Appendix XIV (Page no. 275)**.

48.2 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.

48.3 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.

48.4 The tax auditor should maintain the following information in his working papers for the purpose of reporting against the said clause in the format provided in the e-filing utility:

Sr. No.	Name of the concerned person	PAN of (b) , if available	Address of (b)	Amount borrowed	Date of borrowing	Amount due including interest	Amount repaid	Date of repayment
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)

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

- (i) name, address and permanent account number (if available with the assessee) of the lender or depositor;
- (ii) amount of loan or deposit taken or accepted;
- (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 otherwise than by an account payee cheque or an account payee bank draft.



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\*(These particulars need not be given in the case of a Government company, a banking company or a corporation established by a Central, State or Provincial Act.)

50. (b) Particulars of each repayment of loan or deposit in an amount exceeding the limit specified in section 269T made during the previous year:-
  - (i) name, address and permanent account number (if available with the assessee) of the payee;
  - (ii) amount of the repayment;
  - (iii) maximum amount outstanding in the account at any time during the previous year;
  - (iv) whether the repayment was made otherwise than by account payee cheque or account payee bank draft.
51. (c) Whether the taking or accepting loan or deposit, or repayment of the same were made by account payee cheque drawn on a bank or account payee bank draft based on the examination of books of account and other relevant documents

(The particulars (i) to (iv) at (b) and comment at (c) above need not be given in the case of a repayment of any loan or deposit taken or accepted from Government, Government company, banking company or a corporation established by a Central, State or Provincial Act.)

[Clause 31 (a), (b) and (c)]

**49. Clause 31(a)**

49.1 Section 269SS prescribes the mode of taking or accepting certain loans and deposits. As per this section, no person shall take or accept from any other person any loan or deposit otherwise than by an account payee cheque or account payee bank draft if,-

- (a) the amount of such loan or deposit or the aggregate amount of such loan and deposit; or
- (b) on the date of taking or accepting such loan or deposit, any loan or deposit taken or accepted earlier by such person from the depositor is remaining unpaid (whether repayment has fallen due or not), the amount or the aggregate amount remaining unpaid; or

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- (c) the amount or the aggregate amount referred to in clause (a) together with the amount or the aggregate amount referred to in clause (b),  
is twenty thousand rupees or more.

49.2 For the purposes of section 269SS "loan or deposit" means loan or deposit of money.

49.3 Particulars of each loan or deposit falling within the scope of this section as mentioned above taken or accepted during the previous year have to be stated under this sub-clause. This sub-clause requires five specific particulars in respect of each loan or deposit including the permanent account number of the lender, if available.

49.4 The tax auditor should obtain the above details from the assessee in respect of each loan or deposit and verify the same from the records maintained by him.

49.5 If the total of all loans/deposits from a person exceed Rs.20,000/- but each individual item is less than Rs.20,000/-, the information will still be required to be given in respect of all such entries starting from the entry when the balance reaches Rs.20,000/- or more and until the balance goes down below Rs.20,000/-. As such the tax auditor should verify all loans/deposits taken or accepted where balance has reached Rs.20,000 or more during the year for the purpose of reporting under this clause.

49.6 There will be practical difficulties in verifying the loan or deposit taken or accepted by account payee cheque or an account payee bank draft. In such cases, the tax auditor should verify the transactions with reference to such evidence which may be available. In the absence of satisfactory evidence, the guidance given by the Council of the Institute of Chartered Accountants of India to the tax auditors has been to make a suitable comment in his report as suggested below.

*"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".*

49.7 The tax auditor has to take into account the technological advancements in the field of banking and information technology where loans have been taken other than through an account payee cheque or 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

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cheques in the conventional manner are capable of being tracked. In order to judicially apply the provisions of section 269SS, 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 269SS .

49.8 For the purposes of this clause, the tax auditor may keep in mind the following typical situations:

- (i) Sale proceeds collected by the selling agent will not be considered as loan or deposit.
- (ii) A current account is not excluded from the definition of the term "deposit". Therefore, if the transactions in a current account exceed the amount of Rs.20,000/-, it will be necessary to give the information against this sub-clause. This is the position even if no interest is paid on current account.
- (iii) When there is a mixed account, the transactions relating to loans and deposits (temporary advances) should be segregated from other accounts and the transactions relating to loans and deposits (including temporary advances) should be stated under this clause.
- (iv) Advance received against agreement of sale of goods is not a loan or deposit.
- (v) Opening credit balance of loan taken in earlier years is not specifically required to be disclosed. However, while giving figures of maximum amount outstanding at any time during the year or while giving information about acceptance and repayment of loan/deposit, the opening balances in the loan accounts will have to be taken into consideration.
- (vi) Even if the loans are taken free of interest the information will still have to be given.
- (vii) Security deposits against contracts, etc. will be covered by the definition of 'deposit' and therefore, such information will have to be given. However, the amount retained by the contractee against performance of contract will not be covered as loans/deposits for reporting as amount is not received.
- (viii) Loans and deposits taken or accepted by means of transfer entries in the books of account constitute acceptance of deposits or loans

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otherwise than by account payee cheques. Hence, such entries have to be reported under this clause. 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 accepted.

- (ix) Share application money advance supported by appropriate documentation is neither deposit nor loan and subsequent allotment of shares or repayment of application money as a part of allotment process does not alter the character of application money and provision of Section 269SS/T are not attracted in such a case. *Rugmini Ram Ragav Spinners P. Ltd. 304 ITR 417 Madras High Court and IP India P. Ltd. 343 ITR 353 and Numero Uno Financial Services P. Ltd. 345 ITR 84 Delhi High Court* However, contrary view has been taken in *Bhalotia Engineering Works (P) Ltd. 275 ITR 399*

49.9 As per the proviso to section 269SS, the provisions of section 269SS shall not apply to any loan or deposit taken or accepted from, or any loan or deposit taken or accepted by,-

- (a) Government;
- (b) any banking company, post office savings bank or co-operative bank;
- (c) any corporation established by a Central, State or Provincial Act;
- (d) any Government company as defined in section 2(45) of the Companies Act, 2013; Section 617 of the Companies Act, 1956 has been replaced with section 2(45) in the Companies Act, 2013 with effect from 1.4.2014.
- (e) such other institution, association or body or class of institutions, associations or bodies which the Central Government may, for reasons to be recorded in writing, notify in this behalf in the Official Gazette.

49.10 The footnote in clause 31(a) states that the particulars required under this sub-clause need not be given in the case of a Government company, a banking company or a corporation established by a Central, State or Provincial Act. This is in accordance with the proviso to section 269SS mentioned above. As such, information about loans or deposits taken or accepted from or any loan or deposit taken or accepted by Government, banking company, etc. need not be reported under this sub-clause.

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49.11 The auditor should maintain the following information in his working papers for the purpose of reporting against this clause in the format provided in the e-filing utility:

Sr. No.	Name of the lender or depositor	Address of the lender or depositor	PAN of the lender or depositor, if available	Amount of loan or deposit taken or accepted	Whether the loan/deposit was squared up during the previous year	Maximum amount outstanding in the account at any time during the Previous year	Whether the loan/deposit was taken or accepted otherwise than by an account payee bank cheque or account bank draft
1	2	3	4	5	6	7	8

These particulars need not be given in case of a Government Company, a banking company or a corporation established by a Central, State or Provincial Act.

#### 50. Clause 31(b)

50.1 This sub-clause requires particulars of each repayment of loan or deposit in an amount exceeding the limits specified in section 269T made during the previous year. Section 269T after amendment by the Finance Act, 2002 w.e.f. 1.6.2002 is now applicable to repayment of both loans and deposits. Section 269T is attracted where repayment of the loan or deposit is made to a person, where the aggregate amount of loans or deposits held by such person either in his own name or jointly with any other person on the date of such repayment together with interest, if any, payable on such deposit is Rs.20,000 or more. Explanation (iii) contains a definition of the term "loan or deposit" for the purposes of section 269T. Accordingly, "loan or deposit" means any deposit of money which is repayable after notice or repayable after a period and, in the case of a person other than a company, includes loan or deposit of any nature. As such, all repayments made to any

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person where the loan or deposit along with interest is Rs.20,000 or more are to be reported under this sub-clause, even though the amount of repayment may be less than Rs.20,000. The tax auditor should verify such repayments and report accordingly.

50.2 The second proviso to section 269T inserted by the Finance Act, 2003 w.e.f. 1.6.2002 excludes repayments of loans taken from Government, Government company, Banking company, Corporation established by a Central, State or Provincial Act etc from the scope of the above section and therefore the tax auditor need not report such repayments in his report. However, section 269T does not exclude Government companies, banking companies from the scope of its applicability. As such, details of repayment are to be shown in the case of these entities also.

50.3 In the case of company assessee loan or deposit is defined to mean deposit repayable after notice or loan or deposit repayable after a period. Therefore, in case of a company loan or deposit repayable on demand will not be considered for the purpose of this section as loan or deposit.

50.4 However, in the case of non-company assessee loan or deposit is defined to mean loan or deposit of any nature. This distinction will have to be kept in mind while giving information under this sub-clause.

50.5 Loan or deposits discharged by means of transfer entries in the books of account constitute repayment of loan or deposits otherwise than by account payee cheques or account payee bank drafts. Hence, such entries have to be reported under this clause.

50.6 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 or 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. 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.

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50.7 The monetary limit of Rs. 20,000 or more is applicable in respect of a banking company or a cooperative bank with reference to each branch and in all other cases assessee as a whole.

50.8 The auditor should maintain the following information in his working papers for the purpose of reporting against this clause in the format provided in the e-filing utility:

Sr. No.	Name of the payee	Address of the payee	PAN of the payee, if available	Amount of loan or deposit taken or accepted	Amount of the repayment	Maximum amount outstanding in the account at any time during the Previous year	Whether the repayment was made otherwise than by an account payee bank cheque or account bank draft
1	2	3	4	5	6	7	8

#### 51 Clause 31(c)

51.1 Under this sub clause the tax auditor has to comment as to whether the taking or accepting loan or deposit, or repayment of the same through an account payee cheque or an account payee bank draft based on the examination of books of accounts & other relevant documents. .

51.2 In the case of a repayment of any loan or deposit taken or accepted from Government, Government company, banking company or a corporation established by a Central, State or Provincial Act, the particulars (i) to (iv) mentioned in sub-clause (b) of clause 31 and also the comment mentioned above need not be given.

51.3 However, section 269T does not exclude loans repaid by Government companies, banking companies, corporation established by a Central, State or Provincial Act from the scope of its applicability. As such, details of repayment made by such entities are to be shown.

51.4 It may be noted that the new requirement should be made applicable for the loans and the advances which are in excess of Rs 20,000/-. This is

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evident from a harmonious reading of the clause (c) with the clauses (a) and (b).

51.5 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.

51.6 The tax auditor has to consider the above guidance while reporting against this clause in the format provided in the e-filing utility.

**52. (a) Details of brought forward loss or depreciation allowance, in the following manner, to the extent available:**

Sl No.	Assessment year	Nature of loss / allowance (in rupees)	Amount as returned (in rupees)	Amount as assessed (give reference to relevant order)	Remarks
1	2	3	4	5	6

53. (b) 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.

54. (c) 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.

55.(d) 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.

56.(e) 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.

[Clause 32(a) to (e)]



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### **52. Clause 32(a)- Details of brought forward loss or depreciation allowance**

52.1 The amount of brought forward loss or depreciation allowance is required to be quantified as per return and assessment orders.

52.2 A reporting format is prescribed for the sake of standardization.

52.3 At times while the particular claim for loss/allowance pertains to a particular assessment year as per the return of income, the same may relate to another assessment year as per the assessment order, e.g, Depreciation claim in respect of assets capitalized at the end of the financial year. In those cases, once the assessment order is received, the particulars have to be re-stated with reference to the assessment year to which they relate as per the assessment order. This should be accompanied by suitable explanation in the remarks column.

52.4 Brought forward losses may relate to different heads of income such as property income, profits and gains of business or profession, speculation business or capital gains. Different provisions are contained in sections 32 and 70 to 79 of the Income-tax Act with regard to loss/depreciation under different heads. In the remarks column information about the pending assessment or appellate proceedings or about delay in filing loss returns should be given. For giving the above information, the auditors should study the assessment records i.e. income-tax returns filed, assessment orders, appellate orders and rectification/ revisional orders for the earlier years and ascertain if the figures given in the above clause are correct. Attention of the members is invited to provisions of section 80 read with section 139(3) of the Income-tax Act, 1961. Section 80 provides that notwithstanding anything contained in Chapter VI of the Act, no loss which has not been determined in pursuance of a return filed in accordance with the provisions of sub-section (3) of section 139 shall be carried forward and set off under sub-section (1) of section 72 or sub-section (2) of section 73 or sub-sections (1) or (3) of section 74 or sub-section (3) of section 74A. Besides these, the tax auditor should keep in mind the provisions of section 71B regarding Carry Forward and Set Off of Loss From House Property, section 73A regarding Carry Forward and Set Off of Losses by Specified Business and also section 78 regarding Carry Forward and Set Off of Losses in case of Change in Constitution of Firm or on Succession.

52.5 Any assessment, rectification, revision or appeal proceedings pending at the time of tax audit have to be disclosed in the remarks column by way of

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information. If consequential orders for any revision/appellate order is yet to be passed, the same can be disclosed along with the impact thereof if material.

52.6 The e filing utility may require additional information regarding the relevant order. The information is required to be disclosed to the extent available. The tax auditor should consider the above guidance for the purpose of reporting under this clause in the format provided in the e-filing utility.

### **53. Clause 32(b)- Details of change in shareholding, if any**

53.1 Section 79 of the Act provides that, notwithstanding anything contained in Chapter VI of the Act, in the case of a company, not being a company in which the public are substantially interested, where a change in shareholding has taken place in a previous year, then no loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year unless on the last day of that previous year and on the last day of the previous year in which the loss was incurred, the shares of the company carrying not less than 51% of the voting power were beneficially held by the same persons.

53.2 This provision shall not apply to a change in the voting power consequent upon:

- (a) the death of a shareholder, or
- (b) on account of transfer of shares by way of gifts to any relative of the shareholder making such gift.
- (c) any change in the shareholding of an Indian company which is subsidiary of a foreign company arising as a result of amalgamation or demerger of a foreign company subject to the condition that 51 per cent of the shareholders of the amalgamating or demerged foreign company continue to remain the shareholders of the amalgamated or the resulting foreign company.

53.3 However, the overriding provisions of section 79 do not affect the set off of unabsorbed depreciation which is governed by section 32(2). [*CIT v Concord Industries Ltd. (1979) 119 ITR 458 (Mad)*], *CIT v. Shri Subbulaxmi Mills Ltd. 249 ITR 795 (SC)*.

53.4 Sub-clause 32(b) requires a statement whether a change in shareholding of the company has taken place in the previous year due to

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which the losses incurred prior to the previous year cannot be allowed to be carried forward in terms of section 79.

53.5 The comparison of the composition of the shareholding is to be done with reference to the last day of the current previous year and the last day of every previous year in which the loss was incurred. The carry forward of the loss incurred in respect of different previous years is to be determined with respect to the individual previous years. Such comparison of the shareholding can be done by referring to the Register of Members.

#### **54. Clause 32(c) – Speculation Loss under section 73 of the Income Tax Act:**

54.1 Section 73 of the Act provides for the treatment of losses in speculation business. Section 73(1) provides that any loss, computed in respect of a speculation business carried on by the assessee, shall not be set off except against profits and gains, if any, of another speculation business.

54.2 Section 73(2) further provides that where for any assessment year any loss computed in respect of a speculation business has not been wholly set off under section 73(1), so much of the loss as is not so set off or the whole loss where the assessee had no income from any other speculation business, shall, subject to the other provisions of Chapter VI, be carried forward to the following assessment year, and-

- (i) it shall be set off against the profits and gains, if any, of any speculation business carried on by him assessable for that assessment year; and
- (ii) if the loss cannot be wholly so set off, the amount of loss not so set off shall be carried forward to the following assessment year and so on.

54.3 Section 73(3) provides that in respect of allowance on account of depreciation or capital expenditure on scientific research, the provisions of sub-section (2) of section 72 shall apply in relation to speculation business as they apply in relation to any other business.

54.4 Furthermore, section 73(4) provides that no loss shall be carried forward under this section for more than four assessment years immediately succeeding the assessment year for which the loss was first computed.

54.5 *As per Explanation 2 to section 28.*—Where speculative transactions carried on by an assessee are of such a nature as to constitute a business,

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the business (hereinafter referred to as "speculation business") shall be deemed to be distinct and separate from any other business.

54.6 As per section 43(5) "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 scrips :

Provided that for the purposes of this clause—

- (a) a contract in respect of raw materials or merchandise entered into by a person in the course of his manufacturing or merchanting business to guard against loss through future price fluctuations in respect of his contracts for actual delivery of goods manufactured by him or merchandise sold by him; or
- (b) a contract in respect of stocks and shares entered into by a dealer or investor therein to guard against loss in his holdings of stocks and shares through price fluctuations; or
- (c) a contract entered into by a member of a forward market or a stock exchange in the course of any transaction in the nature of jobbing or arbitrage to guard against loss which may arise in the ordinary course of his business as such member; or
- (d) an eligible transaction in respect of trading in derivatives referred to in clause (ac) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956) carried out in a recognised stock exchange; or
- (e) an eligible transaction in respect of trading in commodity derivatives carried out in a recognised association, which is chargeable to commodities transaction tax under Chapter VII of the Finance Act, 2013 ,

shall not be deemed to be a speculative transaction.

54.7 Having regard to the definition of "speculative Business", the tax auditor has to verify from the books of account and other relevant documents as to whether the assessee is carrying on any speculation business. On verification if the auditor is of the opinion that the auditee is carrying on speculation business, under this clause, the tax auditor has to furnish the details regarding speculation loss referred to in section 73, if any incurred by the assessee during the previous year. Attention is invited to Para 16.3(b) of this Guidance Note.

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54.8 The tax auditor should maintain the following information in his working papers for the purpose of reporting against this clause in the format provided in the e-filing utility:

S. No.	Nature of loss	Amount of loss for the current year	Brought forward loss of the earlier year(s)	Total loss to be carried forward to the subsequent year	Break- up of the speculation loss in terms of the number of years for which it has been carried forward	Whether the speculation loss has been set off against any other income other than profit & loss, if any, of speculation business
1	2	3	4	5	6	7

### 55. Clause 32(d) – Details of Losses incurred in respect of a Specified business as referred to under section 73A

55.1 Section 73A provides for provisions relating to carry forward and set off of losses by specified business. It 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.

55.2 Section 73A(2) provides that where for any assessment year any loss computed in respect of the specified business referred to in sub-section (1) has not been wholly set off under sub-section (1), so much of the loss as is not so set off or the whole loss where the assessee has no income from any other specified business, shall, subject to the other provisions of this Chapter, be carried forward to the following assessment year, and—

- (i) it shall be set off against the profits and gains, if any, of any specified business carried on by him assessable for that assessment year; and
- (ii) if the loss cannot be wholly so set off, the amount of loss not so set off shall be carried forward to the following assessment year and so on.]

55.3 Under clause 32(d), the tax auditor has to verify from the books of accounts and other relevant documents as to whether the assessee is carrying on specified business as referred to under section 35AD. In case the

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auditor is of the opinion that the assessee is carrying on such specified business, he has to furnish the details of the loss incurred, if any, in respect of any specified business during the previous year. In case the assessee carries on more than one specified businesses and loss has been incurred in both the business, the details of the loss incurred with respect of each business is to be specified separately.

55.4 The tax auditor should maintain the following information in his working papers for the purpose of reporting against this clause in the format provided in the e-filing utility:

Sr. No.	Nature of specified business	Amount of loss incurred, if any, during the previous year, with regard to the specified business mentioned in (b)	Loss from specified business brought forward from the earlier year	Amount of loss being set off against other specified business	Year of loss	Amount of loss being carried forward to the next assessment year ((c) –(d))	Whether loss set off against any other income other than from specified business as per sec. 35AD of the Act.
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)

**56. Clause 32(e) – Details of speculation loss, if any, incurred from deemed Speculation business as referred to in Explanation to section 73:**

56.1 The Explanation to section 73 provides that where any part of the business of a company ( other than a company whose gross total income consists mainly of income which is chargeable under the heads " Interest on securities", " Income from house property", " Capital gains" and " Income from other sources" or a company the principal business of which is the business of trading in shares or banking or the granting of loans and advances) consists in the purchase and sale of shares of other companies, such company shall, for the purposes of this section, be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares. The Finance Act, 2014 has amended the explanation to section 73 by deleting the words "the principal business of which is the business of trading in shares" from financial year 2014-2015.

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56.2 Under this clause, the tax auditor has to furnish the details regarding the speculation losses incurred, if any, as referred in explanation to section 73. The auditor may obtain information in the following format from the assessee and verify the same from the books of account, income tax returns of earlier years and other relevant documents:

Sr No	Applicable section	Nature of loss	AY of incurring loss	Amount of Loss	Amount set off during current AY	Amount to be carried forward
1	2	3	4	5	6	7

56.3 The above information so maintained may be used by the tax auditor for the purpose of reporting against this clause in the format provided in the e-filing utility.

57. 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.
1	2

[Clause 33]

57.1 Chapter VIA of the Act deals with various deductions which have to be given effect to by way of allowance from gross total Income of the assessee and they have been categorised under the Act as follows:

- A. Deduction in respect of certain payments.
- B. Deduction in respect of certain incomes.
- C. Other Deductions.

While Chapter III relates to Income which do not form part of total income, the reporting under this clause is required only with respect to exemptions claimed under section 10A (Special provisions in respect of newly

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established undertakings in free trade Zone etc) and section 10AA (Special provisions in respect of newly established units in Special Economic Zones)

57.2 As stated earlier, the tax audit report in Form No.3CA/3CB relates to business or professional activity of the assessee covered by section 44AB. Form No.3CD is an annexure to this Form giving particulars relating to the business/profession covered by the tax audit report. Therefore, the requirement under clause 33 relating to the deductions admissible under Chapter VIA, section 10A and section 10AA will have to be with reference to the items appearing in the books of accounts audited by the tax auditor. If the tax auditor is issuing tax audit report in respect of the accounts of a specific branch or a specific unit he will have to examine the particulars relating to deduction admissible under Chapter VIA and exemption relating to section 10A/10AA, as the case may be, with reference to the books of account of that branch or that unit which is audited by him. Similarly when the tax auditor is issuing report regarding tax audit of the head office he will have to take into consideration the tax audit reports of the branches as well as other units of the assessee which may have been audited by the other tax auditors. He will have to consider the particulars of deductions admissible under Chapter VIA and exemption relating to section 10A/10AA, as the case may be with reference to the particulars given by the tax auditor of other branches/units and also particulars of such deductions from books of the head office.

57.3 In the case of a sole proprietor being an individual or HUF it may so happen that the tax auditor is auditing the accounts of the business/profession and the sole proprietor is having other activities and other sources of income in respect of which tax audit is not mandatory. In such cases the particulars of deductions admissible under Chapter VIA will have to be given with reference to the items appearing in the books of accounts of the business/profession which is subject to audit under section 44AB.

57.4 The admissibility of the aforesaid deductions/exemptions is dependent upon various conditions laid down in the section under which deduction/exemption is admissible. It is, therefore, advised that while working out the amount of admissible deduction the tax auditor has to ascertain that those condition stand fulfilled or not. For ascertaining this, the tax auditor has to obtain all necessary evidence which would enable him to express the opinion regarding the admissibility of deductions. For example, under section 80IA one of the conditions is that the new Industrial



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undertaking which qualifies for deduction thereunder should not have been formed by splitting up or by the reconstitution of a business already in existence or by transfer to a new business of machinery or plant previously used for any purpose. In order to ascertain the fulfillment of this condition the tax auditor may have to check all documentary evidence in respect of plant and machinery installed in the industrial undertaking to arrive at the conclusion that plant and machinery is new and has not been used previously for any other purpose. Likewise if there is any condition which qualifies the admissibility of the amount of deduction, the tax auditor has to see and ascertain that those qualifying conditions are fulfilled on the basis of documentary evidence available with the assessee. There may be cases where there is difference between the amount claimed by the assessee and the amount computed out by the tax auditor. In such cases it is quite possible that the client's claim is based on some judicial pronouncement on the subject. In such case it may be advisable for the tax auditor to report the amount admissible. The amount claimed and the background behind and the basis of the claim of the assessee may form part of the working papers. If the claim of the assessee is well-founded and settled by judicial pronouncement the tax auditor may accept the claim but he has to record in his working papers that admissible amount has been reported on the basis of such judicial pronouncement.

57.5 It may be noted that there are certain sections under Chapter VIA like section 80-IA, 80-IB, 80-JJA etc. where separate audit report or certificate is required to be issued. Under the said sections, a non-corporate assessee who has income from industrial undertaking covered under the above sections has also to obtain audit report with reference to the accounts of these undertakings. While giving information with regard to the deduction allowable under these sections the tax auditor should refer to separate audit reports/ certificates obtained by the assessee. These audit reports/ certificates may have been given by the tax auditor or by any other auditor. The figures given in this separate audit reports/certificates should be taken into consideration while giving information with regard to income covered by these sections.

57.6 Since the details of exemptions admissible under sections 10A and 10AA are also to be reported in the desired format, the said information can be verified from the certificate issued by the chartered accountant in this regard. In case, a report under section 10A and 10AA has been issued by any other chartered accountant, then the same may be taken into

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consideration while reporting under this clause. Here attention is invited to SA-600, *Using the work of another auditor*.

57.7 Some sections in Chapter VIA such as section 80-G (donations), Section 80-GGB/80-GGC (contributions to political parties), section 80-JJAA (wages of new workmen) etc. relate to the expenditure incurred by an assessee. There are other sections such as section 80-P (income of co-operative societies), 80-JJA (certain specified business relating treatment of biodegradable waste) etc. which relate to income of the assessee. In respect of all these sections the tax auditor should ascertain whether there is any expenditure or income covered by the above sections recorded in the books of accounts audited by him. Information with regard to such expenditure/income in respect of deduction allowable under Chapter VIA should be given on the basis of the examination of the books of account and other records under clause 33.

58. (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:**

Tax deduction and collection Account Number (TAN)	Section	Nature of payment	Total amount of payment or receipt of the nature specified in column (3)	Total amount on which tax was required to be deducted or collected out of (4)	Total amount on which tax was deducted or collected at specified rate out of (5)	Amount of tax deducted or collected out of (6)	Total amount on which tax was deducted or collected at less than specified rate out of (7)*	Amount of tax deducted or collected on (8)	Amount of tax deducted or collected not deposited to the credit of the Central Government out of ** (6) and *** (8)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)

[Clause 34(a)]

\*Should be read as (5) for proper reporting

\*\* Should be read as (7) for proper reporting

\*\*\* Should be read as (9) for proper reporting

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59. (b) Whether the assessee has furnished the statement of tax deducted or tax collected within the prescribed time. If not, please furnish the details:

Tax deduction and collection Account Number (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

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

Tax deduction and collection Account Number (TAN)	Amount of interest under section 201(1A)/206C(7) is payable	Amount paid out of column (2) along with date of payment.
1	2	3

[Clause 34(a), (b) and (c)]

**58. Clause 34(a)**

58.1 While reporting under this clause the tax auditor may exercise his judgement in the light of the applicable laws and report accordingly about the applicability of the provisions of Chapter XVII-B or XVII-BB with regard to the auditee. The tax auditor may rely upon the judicial pronouncements while taking any particular view. While answering the issue of applicability of the provisions of Chapter XVII-B and/or XVII-BB, a number of debatable issues may arise before the assessee as well as the tax auditor. Where it is not possible to say yes/no, the answer to the question may have to be qualified depending upon the facts and circumstances of each case. Having verified the applicability of the provisions of Chapter XVII-B and Chapter XVII-BB, the tax auditor should answer the question as "Yes" and thereafter provide further details. Where the tax auditor is of the opinion that provisions of

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Chapter XVII-B and Chapter XVII-BB are not applicable he should answer the question as "No".

58.2 Once the tax auditor gives his affirmation with regard to applicability of the provisions of Chapter XVII-B and/ or Chapter XVII-BB, he is required to furnish further details in Clause 34(a). The auditor should obtain a copy of the TDS/TCS returns filed by the assessee which shall form the basis of reporting under this clause, to the extent possible. Further, in view of the voluminous nature of the transactions, the tax auditor can apply test checks and compliance tests on the transactions reported in the TDS return by the assessee for verifying the information required to be provided under this clause.

58.3 Column (1) of Clause 34(a) requires reporting of each Tax deduction and collection Account number with regard to which tax has been deducted or collected at source.

58.4 In column (2), the tax auditor is required to furnish the details of the applicable section in respect to which tax has been deducted or collected at source

58.5 In column (3), the tax auditor is required to furnish the details regarding the nature of payment.

58.6 In column (4), the auditor is required to furnish the details of the total amount of payment or receipt of the nature specified in column (3). The details in the said column may be drawn from the TDS/TCS statements furnished by the assessee to the Department along with the books of accounts and other relevant documents which include aggregate of payments on which tax is liable to be deducted as well as not liable to be deducted. Auditor may maintain working paper giving reconciliation of amount as per books of accounts and amount on which is TDS/TCS is required to be deducted/collected.

58.7 Column (5) casts an onerous responsibility on the auditor, wherein he is required to furnish the details of total amount on which the tax was required to be deducted or collected out of the amount mentioned in column (4) having regard to the nature of payments/ receipts under the relevant sections of Chapter XVII-B / XVII-BB. Since the reporting under column (4) is required to be made with regard to the nature of payments made or amount received, there may be a difference in the amounts reported under column (4) and column (5). The reasons for difference may be applicability of certificates issued under section 195/197 or threshold limits provided in

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specific sections or difference of opinion with regard to applicability of a particular section and the like.

58.8 While answering the issue of applicability of the provisions of Chapter XVII-B and/or XVII-BB, a number of debatable issues may arise before the assessee as well as the tax auditor. The auditor may have a difference of opinion with regard to the applicability of the provisions of TDS/TCS on a particular payment. In such a case, the tax auditor has to bring the difference of opinion appropriately as an observation in the clause (3) of Form No. 3CA or clause (5) of Form No.3CB as the case may be.

58.9 It is essential to note that it is the primary responsibility of the assessee to prepare the information in such a manner that the tax auditor can verify the compliance as required in the new clause. The tax auditor is required to verify that no items have been omitted in the information furnished to him and reasonable test checks 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.

58.10 In column (6) the tax auditor is required to furnish the total amount out of the amount deductible or collectible as mentioned in column (5) at which the tax was deducted or collected at the specified rate. The auditor has to consider the rates of deduction as per the law relevant to the previous year. Further, as per the provisions of sections 195/ 197 certificate can be issued for no deduction or lower deduction of tax at source. The tax auditor should refer to the relevant provisions, rules, circulars, notifications and such certificates obtained from the auditee to verify the cases where tax has been short deducted at source. In case the payer deducts/recipient collects tax at source at a rate lower than the specified rate on the basis of certificate issued under section 195 or 197, the lower rate or nil rate, as the case may be will be considered as the specified rate for the purpose of reporting under this clause. In the case of payment to non-residents the applicable rate of tax deduction at source is to be read along with the Double Taxation Avoidance Agreement. Column (7) requires furnishing of total amount of tax deducted/collected out of the amount furnished in column (6).

58.11 Similarly, column (8) requires the tax auditor to furnish the total amount out of the amount deductible or collectible as mentioned in column (5) at which the tax was deducted or collected at the rate less than the

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specified rate. The lesser deduction is required to be reported in this clause. This will include deduction at a lower rate than what is prescribed, application of wrong section for deduction of tax at source, etc. For example section 194C requires deduction @2% in case payment is made to a person other than individual or HUF, but the deductor deducts only 1%, the same has to be reported under this clause. In case there is difference of opinion with regard to rate of deduction or applicability of a particular section, the auditor may appropriately report the difference of opinion in the clause (3) of Form No. 3CA or clause (5) of Form No.3CB as the case may be giving both the views. Further, column (9) requires furnishing of total amount of tax deducted/collected out of the amount furnished in column (8).

58.12 Column (10) requires the auditor to furnish the details of the amount of tax deducted or collected but not deposited to the credit of the Central Government. As such the tax auditor should verify the cases where the tax has been deducted at source but not paid to the credit of the Central Government till the date of the audit. It may be seen that tax deducted but deposited late will not be required to be reported in this clause.

58.13 The details in the column (6), (7), (8), (9) and (10) may be drawn from the TDS/TCS returns furnished by the assessee to the Department and be verified from the books of accounts and other relevant documents.

#### **59. Clause 34(b)**

59.1 Under clause 34(b), the tax auditor has to ascertain and report as to whether the assessee has furnished the statement of tax deducted or tax collected at source within the prescribed time. If all the TDS/TCS statement(s) relating to the previous year have been filed within the prescribed time, the auditor has to mention "yes". In case the assessee has not filed any of the quarterly TDS/TCS statement(s) within the prescribed time, the auditor has to mention "No" in this clause. In such a case, the auditor shall provide further details in Clause 34(b) only with regard to the statement not filed within the prescribed time. Clause 34(b) requires the auditor to report the transactions with regard to each TAN for which tax has been deducted but the return has either not been filed or has been filed after the expiry of the prescribed time. With regard to each TAN, the auditor is required to mention the "Type of form" that was applicable like Form 24, 24G, 24Q, 26, 26A, 26B, 26Q etc, due date of furnishing such statement and the actual date of furnishing, if the statement(s) has been furnished. Lastly, the auditor is required to state as to whether the statement of tax deducted or collected, which has been furnished beyond prescribed time contains information about all the transactions which are required to be reported. As

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stated earlier, it is extremely difficult for the tax auditor to verify each and every transaction in this regard. Therefore, while verifying such transactions, the tax auditor can apply the concepts of materiality and audit sampling. The reporting requirement in clause (b) arises only where the assessee has either not furnished or furnished the statement of tax deducted or tax collected after the expiry of prescribed time.

59.2 In regard to clause 34(b), the tax auditor has to verify the particulars regarding tax deductible and tax collectible from the information furnished by the assessee. The various provisions of Chapter XVII-B and XVII-BB require different classes of assessee to deduct/collect tax at source on various nature of payments. The tax auditor should consider the applicability of the different provisions relating to tax deduction at source taking into consideration the status of the assessee and the applicability of the relevant provision. As regards the applicability of the provisions the tax auditor should take into consideration the relevant sections, rules, notifications, circulars and various judicial pronouncements in relation to transactions of relevant payments or collections. There may be occasions when the tax auditor may not agree with the interpretation/view taken by the auditee. In such cases the tax auditor may report both the views as an observation in clause (3) of Form No. 3CA or clause (5) of Form No. 3CB, as the case may be.

59.3 The information given in clause 34 should tally with the disallowances reported u/s 40(a) in clause 21(b) to the extent applicable.

#### **60. Clause 34(c)**

60.1 Under this clause, the auditor is required to furnish detailed information in case the assessee is liable to pay interest under section 201(1A) or section 206C(7) of the Act. Section 201(1A) provides for payment of interest at a specified rate in case the tax has not been deducted wholly or partly or after deducting has not been paid to the credit of Central Government as required by the Act. Similarly, section 206C(7) provides for payment of interest at a specified rate in case the tax is not collected wholly or partly or if collected not paid to the credit of the Central Government as required by the Act. The reporting as to whether the assessee is liable to pay such interest, should be in consonance with the reporting under clause 34(a) where the details of non-deduction are required to be reported by him.

60.2 Where the assessee is liable to pay interest u/s 201(1A) or 206C(7), the auditor should verify such amount from the books of account as on 31st March of the relevant previous year and also from PART G of the statement generated by the Department in Form No.26AS. In case the assessee had disputed the levy or calculation of interest under TRACES, in Form

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No.26AS, the auditor may re-calculate the amount of interest under section 201(1A) or section 206C(7) up to the date of audit report for reporting under this clause and also mention the fact in his observations paragraph provided in Form No.3CA or Form No.3CB, as the case may be.

61. (a) In the case of a trading concern, give quantitative details of the principal items of goods traded:
  - (i) Opening stock;
  - (ii) Purchases during the previous year;
  - (iii) Sales during the previous year;
  - (iv) Closing stock;
  - (v) shortage / excess, if any.
62. (b) In the case of a manufacturing concern, give quantitative details of the principal items of raw materials, finished products and by-products :
  - A. Raw materials:
    - (i) opening stock;
    - (ii) purchases during the previous year;
    - (iii) consumption during the previous year;
    - (iv) sales during the previous year;
    - (v) closing stock;
    - (vi) yield of finished products;
    - (vii) percentage of yield;
    - (viii) shortage/excess, if any.
  - B. Finished products/By-products:
    - (i) opening stock;
    - (ii) purchases during the previous year;
    - (iii) quantity manufactured during the previous year;
    - (iv) sales during the previous year;
    - (v) closing stock;
    - (vi) shortage/excess, if any.

[Clause 35 (a) and (b)]



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### **61. Clause 35(a)**

61.1 The tax auditor should obtain certificates from the assessee in respect of the principal items of goods traded, the balance of the opening stock, purchases, sales and closing stock and the extent of shortage/excess/damage and the reasons thereof.

### **62. Clause 35(b)**

62.1 This information should be given only in respect of those items where it is practicable to do so, having regard to the records maintained by the assessee.

62.2 In a large concern it may be difficult for tax auditor to verify each and every item of purchase, consumption and production. In such cases, he may verify the figures on a sampling method and satisfy himself as to the correctness of the figures furnished. This clause requires that quantitative details of "principal items" of raw materials and finished goods should be given. Therefore, information about petty items need not be given. What would constitute principal items will depend on the facts of each case. Normally, items which constitute more than 10% of the aggregate value of purchases, consumption or turnover may be classified as principal items.

62.3 The information about 'yield', 'percentage of yield', and 'shortages/excess' is also required to be given.

62.4 In respect of assessees other than companies and those whose accounts have not been audited under any other law, the tax auditor should obtain the following certified documents for the principal items of raw materials, finished goods and by-products:

- (a) Certificate from the assessee certifying the balance of the opening stock, purchases, sales and closing stock.
- (b) Certificate to the extent of shortage/excess/damage and the reasons thereof.

62.5 By-products represent products whose manufacture results incidentally from the manufacture of the main product or where the waste arising in the manufacture of main product is further processed to create a by-product. Where the by product so produced or is continuously generated it should be treated for the purpose of sale and disposal at par with at any other product produced by the company and similar records should be maintained. The quantitative details on the above lines are to be given in respect of by-product also.

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63. 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 tax paid thereon;
- (e) dates of payment with amounts.

[Clause 36]

63.1 Section 115-O provides for a special levy at the prescribed rate, on the amount of dividend declared, distributed or paid by such company whether such dividend is out of current profit or accumulated profits. Vide this clause the tax auditor has to report on profit distributed during the financial year and therefore, the amount of tax worked and paid out on such distributed profit at the prescribed rate plus surcharge at the applicable rate on the tax along with the education cess thereon has to be reported against this clause. The amount of the dividend referred to in sub-section (1) is to be reduced by the amount referred to in sub-section (1A). Since the tax is payable on such reduced amount, the gross amount may be reported in the sub-clause (a) and the amount of reduction as referred to in section 115-O(1A)(i) and 115-O(1A)(ii) shall be reported in sub-clause (b) and (c) separately. The tax auditor should keep the working papers to reveal how the net amount has been arrived at.

63.2 It may be noted that for the purposes of chapter XII-D containing special provisions relating to tax on distributed profits of domestic companies the expression "dividends" shall have the same meaning as is given to "dividend" in clause (22) of section 2 but shall not include sub-clause (e) thereof. However, the tax auditor need not go into the question of how the total amount of distributed profits has been arrived at.

63.3 The next requirement is to report the tax paid thereon and the date of payment. The date of payment of tax can be ascertained by the tax auditor from the duly received challan and books of account etc.

63.4 In this clause, the total amount of profits distributed in the previous year, tax paid thereon and the date of payment of tax is required to be given. Information about the date of declaration/distribution of dividend or payment of dividend is not required to be given.

63.5 The tax auditor should maintain the information in the following format for the purpose of reporting in the format provided in the e-filing utility:

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S. No.	Total Amount of distributed profits	Amount of reduction as referred to in section 115-O(1A)(i)	Amount of reduction as referred to in section 115-O(1A)(ii)	Total tax paid	Date of payments with Amount	
					Date of Payment	Amount
1	2	3	4	5	6	7

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

[Clause 37]

64.1 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 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 out.

64.2 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.

64.3 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 upto the date of tax audit report.

**65. Whether any audit was conducted under the Central Excise Act, 1944, if yes, give the details, if any, of disqualification or disagreement**

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**on any matter/item/value/quantity as may be reported/ identified by the auditor**

**[Clause 38]**

65.1 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.

65.2 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.

65.3 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 upto the date of tax audit report.

**66. 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/value/quantity as may be reported/ identified by the auditor.**

**[Clause 39]**

66.1 The tax auditor should ascertain from the management whether any audit was conducted under section 72A of the Finance Act, 1994 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 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.

66.2 In cases where service tax audit, which might have been ordered is not completed by the time the tax auditor gives his report, he has to report

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appropriately in this report stating that since service tax audit is not completed and the service tax audit report is not available with the assessee.

66.3 The tax auditor should examine the time period for which the service tax audit, if any, has been required to be carried out. Information is required to be given only in respect of such service tax 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 service tax audit report which is received upto the date of tax audit report.

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

Serial number	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)

[Clause 40]

67.1 These ratios have to be calculated only for assessees who are engaged in manufacturing or trading activities. Moreover, the ratios have to be given for the business as a whole and need not be given product wise. Further, the ratio mentioned in (5) need not be given for trading concern or service provider.

67.2 While calculating these ratios, the tax auditor should assign a meaning to the terms used in the above ratios having due regard to the generally accepted accounting principles. All the ratios mentioned in this clause are to be calculated in terms of value only.

67.3 The following definitions given by the ICAI in its Guidance Note on the Terms Used in Financial Statements may be noted.

- (a) **Gross Profit:** The excess of the proceeds of goods sold and services rendered during a period over their cost, before taking into account

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administration, selling, distribution and financing expenses. When the result of this computation is negative it is referred to as gross loss.

- (b) **Turnover:** The aggregate amount for which sales are effected or services rendered by an enterprise. The terms gross turnover and net turnover (or gross sales and net sales) are sometimes used to distinguish the sales aggregate before and after deduction of returns and trade discounts. Attention is also invited to Para 5 (Sales, Turnover, Gross receipts) of this Guidance Note.
- (c) **Net Profit:** The excess of revenue over expenses during a particular accounting period. When the result of this computation is negative, it is referred to as net loss. The net profit may be shown before or after tax.

It may be noted that the net profit to be shown here in this clause is net profit before tax.

67.4 For the purpose of calculating the ratio mentioned in (4), only closing stock is to be considered. The term 'stock-in-trade' used therein does not include stores and spare parts or loose tools. The term "stock-in-trade" would include only finished goods and would not include the stock of raw material and work-in-progress since the objective here is to compute the stock-turnover ratio.

67.5 Material consumed would, apart from raw material consumed, include stores, spare parts and loose tools.

67.6 The value of finished goods produced may be arrived at by using the following formula:

(a)	Raw material consumption	-
(b)	Stores and spare parts consumption	-
(c)	Wages	-
(d)	Other manufacturing expenses excluding depreciation.	-
	Sub total	-
	Add: Opening stock in process	-
	Deduct: Closing stocks in process - Value of finished goods produced	

67.7 Under this clause, calculation of the ratios are also to be stated. As such, computation of various components based upon which these ratios

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have been worked out is required to be stated under this clause. However, if any of the above component is stated in the financial statements themselves, a reference to the same may be made, to the extent possible.

67.8 There should be consistency between the numerator and the denominator while calculating the above ratios. Any significant deviation thereof should be pointed out.

67.9 The relevant previous year figures are to be taken from last previous year audit report. In case the preceding previous year is not subject to audit, nothing should be mentioned in the relevant column.

**68. 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.**

**[Clause 41]**

68.1 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.

68.2 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.

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68.3 The tax auditor should maintain the following information in his working papers for the purpose of reporting against this clause in the format provided in the e-filing utility.

S. No.	Name of the applicable Act	Demand/ Refund Order No., if any	Date of Demand raised/ refund issued	Financial Year to which the Demand / refund relates	Amount of demand raised/ refund issued	Adjustment of refund against demand, if any	Remarks
1	2	3	4	5	6	7	8

### 69. Signature and stamp/Seal of the signatory

69.1 Form 3CD has to be signed by the person competent to sign Form No. 3CA or Form No.3CB as the case may be. He has also to give his full name, address, membership number, firm registration number, wherever applicable, place and date. Further, the e-filing portal requires the tax auditor to affix his Digital Signature while registering himself. He is also required to put his stamp/Seal as well.

### 70. Code of Ethics and other matters

70.1 Some of the issues which are commonly raised in regard to different aspects of tax audit vis-à-vis the liability/ obligations of the tax auditor are considered hereunder.

70.2 The liability of the tax auditor in respect of tax audit will be the same as in any other audit assignment. It may be noted that when any question relating to the audit conducted by a tax auditor arises, he is answerable to the Council of the Institute under the Chartered Accountants Act. In all matters concerning tax audit, ICAI's disciplinary jurisdiction will prevail.

70.3 In case the assessee is found guilty of having concealed the particulars of his income it would not ipso facto mean that the tax auditor is also responsible. If the Assessing Officer comes to the conclusion that the tax auditor was grossly negligent in the performance of his duties, he can refer the matter to the ICAI so that appropriate action can be taken against the tax auditor under the Chartered Accountants Act.

70.4 The Assessing Officer or any other authority who is authorised to issue summons and to call for evidence or documents, can call upon the tax auditor who has audited the accounts to give any evidence or produce documents. For this purpose notice under section 131 can be issued by the Assessing Officer or other tax authority mentioned in the said section.



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70.5 If the actual work relating to examination of books and records is done by a qualified assistant in a firm of chartered accountants and the partner of the firm signing the audit report has relied upon this work, action, if any, for professional negligence can be initiated against the member who has signed the report and in such an event, it would be open for the member concerned to prove that he has taken due care and diligence in the performance of his duties and is not aware of any reason to believe that he should not have so relied.

70.6 If the qualified assistant (whether or not holding the certificate of practice) is found to be grossly negligent in the performance of his duties, the Council of the Institute can take disciplinary action against him.

70.7 A tax auditor can accept the assignment of tax representation.

70.8 Under the Code of Ethics, no tax auditor can charge professional fees by way of percentage of profits or which are contingent upon findings, or results of such employment, except as permitted under any regulation made under this Act. In this connection, reference is invited to Clause (10) of Part I of the First Schedule to the Chartered Accountants Act and the commentary on the subject at page 210 of the Code of Ethics (2009 Edition). Certain exceptions are made in Regulation 192, but these exceptions do not apply for charging of fees for tax audit.

70.9 Since the figures in Form No. 3CD are duly verified by a chartered accountant, they should normally be accepted by tax authorities. If, however, there is a specific reason for differing from the view taken by tax auditor, the Assessing Officer may compute the income of the assessee by adopting different figures.

70.10 The opinion expressed by the tax auditor is not binding on the assessee. If the tax auditor has qualified his report and expressed an opinion on a particular item, the assessee may take a different view while preparing his return of income. In such cases, it is advisable for the assessee to state his viewpoint and support the same by any judicial pronouncements on which he wants to rely.

### **71. Format of Financial Statements**

71.1 The tax auditor 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 has to give his report in Forms No. 3CB/3CD and will have to ensure that the financial statements i.e. balance sheet and profit and loss account/ income and expenditure statement, are prepared in such a manner that adequate information which is necessary to convey a true and fair view of the state of

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affairs of the assessee is given. So far as a person whose accounts of the business or profession have been audited under any other law is concerned, the information to be given in the financial statements is normally provided in the particular statute by which the assessee is governed. Since there is no such legislation in respect 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, it is necessary to achieve some uniformity in respect of information to be provided in the financial statements.

71.2 It should be noted that the responsibility for maintenance of books and records and that for preparation of financial statements is that of the assessee. It is, therefore, desirable that guidance is given 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 about the maintenance of books of accounts and records as well as about the requirements of auditing. Similarly, guidance is also required to be given about the preparation of financial statements and the information to be provided in such statements. (See "Monograph on Compulsory Maintenance of Accounts" published by ICAI)

71.3 Two separate sets of forms of balance sheet and profit and loss account have, therefore, been prepared and given as Appendices to this Guidance Note. **Appendix XV (Page no. 278)** gives the recommended format of the balance sheet and also the information to be provided in the profit and loss account, in case of an assessee engaged in trading business. This format can be used in the case of an assessee, who is engaged in profession and other service activities, by making such changes as may be considered to suit the circumstances. **Appendix XVI (Page no. 286)** gives the recommended format of the balance sheet and the requirements of the profit and loss account in the case of an assessee engaged in the manufacturing activities. It is suggested that the balance sheet and the profit and loss account can be prepared either in the vertical or in the horizontal form according to the circumstances of each case. If the information required to be given in any item or sub-item of the financial statements cannot conveniently be given on the face of the financial statements, the same may be given by way of footnotes/ annexures to and forming part of such financial statements. Since the formats are designed also for accounts of non-corporate borrowers from banks, they may be modified so as to exclude the information, which may not be relevant for accounts for tax audit. For presentation and disclosure requirements, applicable AS and AS (IT) should be kept in mind.

# APPENDICES

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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**NOTE**

- ◆ The appendices published hereinafter do not form part of the Statement. These are intended for the ease of reference to the readers.
- ◆ These appendices, among other things, also contain reproduction of texts of various sections of relevant statutes and notifications issued by the Government of India. While every effort has been made to avoid errors or omissions in reproduction, some errors are likely to creep in. It is, therefore, suggested that to avoid any doubt, the reader should cross-check all the facts, law and contents of the publication with original Government publication or notifications.

## APPENDIX I

### [PARA 5.12]

CIRCULAR NO. 452, DATED 17.3.1986

*Subject: Section 44AB of the Income-tax Act, 1961- Clarification regarding applicability in the cases of Commission Agents, arhatias etc. (Para 5.12).*

1. Section 44AB of the Income-tax Act, 1961, as inserted by the Finance Act, 1984, casts an obligation on every person carrying on business to get his accounts audited, if his total sales, turnover or gross receipts, as the case may be, exceed Rs.40 lakhs (substituted by Rs. 1 crore by Finance Act, 2012 w.e.f. A.Y. 2013-14) in any previous year relevant to the assessment year commencing on 1.4.1985 or any subsequent assessment year.
2. The Board have received representations from various persons, trade associations, etc., to clarify whether in cases where an agent effects sales/turnover on behalf of his principal, such sales/turnover have to be treated as the sales/turnover of the agent for the purpose of Section 44AB of the Income-tax Act, 1961.
3. The matter was examined in consultation with the Ministry of Law. There are various trade practices prevalent in the country in regard to agency business and no uniform pattern is followed by the commission agents, consignment agents, brokers, kachha arhatias and pacca arhatias dealing in different commodities in different parts of the country. The primary necessity in each instance is to ascertain with precision what are the express terms of the particular contract under consideration. Each transaction, therefore, requires to be examined with reference to its terms and conditions and no hard and fast rule can be laid down as to whether an agent is acting only as an agent or also as a principal.
4. Board are advised that so far as kachha arhatias are concerned, the turnover does not include the sales effected on behalf of the principals and only the gross commission has to be considered for the purpose of Section 44AB. But the position is different with regard to pacca arhatia. A pacca arhatia is not, in the proper sense of the word, an agent or even del credere agent. The relation between him and his

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constituent is substantially that between the two principals. On the basis of various Court pronouncements, following principles of distinction can be laid down between a kachha arhatia and a pacca arhatia:

- (1) A kachha arhatia acts only as an agent of his constituent and never acts as a principal. A pacca arhatia, on the other hand, is entitled to substitute his own goods towards the contract made for the constituent and buy the constituent's goods on his personal account and thus he acts as a principal as regards his constituent.
  - (2) A kachha arhatia brings a privity of contract between his constituent and the third party so that each becomes liable to the other. The pacca arhatia, on the other hand, makes himself liable upon the contract not only to the third party but also to his constituent.
  - (3) Though the kachha arhatia does not communicate the name of his constituent to the third party, he does communicate the name of the third party to the constituent. In other words, he is an agent for an unnamed principal. The pacca arhatia, on the other hand, does not inform his constituent as to the third party with whom he has entered into a contract on his behalf.
  - (4) The remuneration of kachha arhatia consists solely of commission and he is not interested in the profits and losses made by his constituent as is not the case with the pacca arhatia.
  - (5) The kaccha arhatia, unlike the pacca arhatia does not have any dominion over the goods.
  - (6) The kaccha arhatia has no personal interest of his own when he enters into a transaction and his interest is limited to the commission agent's charges and certain out of pocket expenses whereas a pacca arhatia has a personal interest of his own when he enters into a transaction.
  - (7) In the event of any loss, the kachha arhatia is entitled to be indemnified by his principal as is not the case with pacca arhatia.
5. The above distinction between a kachha arhatia and pacca arhatia may also be relevant for determining the applicability of Section 44AB

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in cases of other type of agents. In the case of agents whose position is similar to that of *kachha arhatia*, the turnover is only the commission and does not include the sales on behalf of the principals. In the case of agents of the type of *pacca arhatia*, on the other hand, the total sales/turnover of the business should be taken into consideration for determining the applicability of the provisions of Section 44AB of the Income-tax Act.

Circular No. 452 [F.No.201/3/85-IT(A-II)] dated 17th March 1986.

### JUDICIAL ANALYSIS

*EXPLAINED IN* - In *Jeyar Consultant & Investment (P.) Ltd. v. Assistant Commissioner [1993] 46 ITD 71 (Mad.-Trib.)*, it was observed that it is *ex facie* clear from the CBDT Circular No. 452 of 17-3-1986 which came to be issued in relation to *kacha* and *pacca arhatias*, who are an integral part of the trading sector, that instructions issued by the Board as respects *kacha* and *pacca arhatias* could not be applied to the case of the assessee who has arranged finances for other for a fee. The assessee may choose to label the fee as brokerage or even as commission. But the fee or to use a generic expression 'receipt' could not be regarded as turnover proper.

*RELIED ON IN* - The above circular was relied on in *ITO v. Shantilal Chunilal & Co. [1993] 45 ITD 581 (Pune - Trib.)*, with the following observations:

" . . . Further, reference was made by assessee to pages 52 to 54 which contains Board's Circular No. 452, dated 17-3-1986 which has been issued in connection with section 44AB of the Income-tax Act, 1961. Reliance was placed on para 4 of the said circular according to which the Board were advised that so far as *kachha arhatias* were concerned, the turnover did not include sales effected on behalf of the principals and only gross commission has to be considered for the purpose of section 44AB. The submission of the learned counsel for the assessee was that the case of the assessee is one of *kachha arhatia* and not a *pacca arhatia* and, therefore, only gross commission has to be considered for the purpose of section 44AB of the Income-tax Act, 1961. . . The CIT (Appeals) has excluded the adat receipt as well as interest receipt from the purview of turnover for the purpose of section 44AB. Relying on the clarifications given by the Board in its Circular No. 452, dated 17-3-1986, he has categorised the assessee as *kachha arhatia* and he has charged expenses incurred on such business which resulted in gross profit rate of 1.09 per cent.

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Therefore, it is very much relevant to clinch the issue whether the assessee is a *kachha arahatia* or not. Going by the clarification issued by the Board in the aforesaid Circular No. 452, dated 17-3-1986 the case of the assessee fits in with the *kachha arahatia vis-a-vis* case of *pucca arahatia*. . . ." (pp. 585-586).

*REFERRED TO IN- Manish Textiles v. ACIT [1991] 38 ITD 365 (Bom.).*



## APPENDIX II

### [PARA 5.15]

Circular No. 4/2007, dated 15<sup>th</sup> June, 2007

F.No.149/287/2005-TPL

#### **Distinction between shares held as stock-in-trade and shares held as investment - tests for such a distinction**

1. The Income-tax Act, 1961 makes a distinction between a "capital asset" and a "trading asset".
2. Capital asset is defined in Section 2(14) of the Act. Long-term capital assets and gains are dealt with under Section 2(29A) and Section 2(29B). Short-term capital assets and gains are dealt with under Section 2(42A) and Section 2(42B).
3. Trading asset is dealt with under Section 28 of the Act.
4. The Central Board of Direct Taxes (CBDT) through Instruction No.1827 dated August 31, 1989 had brought to the notice of the assessing officers that there is a distinction between shares held as investment (capital asset) and shares held as stock-in-trade (trading asset). In the light of a number of judicial decisions pronounced after the issue of the above instructions, it is proposed to update the above instructions for the information of assesseees as well as for guidance of the assessing officers.
5. In the case of *Commissioner of Income Tax (Central), Calcutta Vs Associated Industrial Development Company (P) Ltd (82 ITR 586)*, the Supreme Court observed that:  

"Whether a particular holding of shares is by way of investment or forms part of the stock-in-trade is a matter which is within the knowledge of the assessee who holds the shares and it should, in normal circumstances, be in a position to produce evidence from its records as to whether it has maintained any distinction between those shares which are its stock-in-trade and those which are held by way of investment."
6. In the case of *Commissioner of Income Tax, Bombay Vs H. Holck Larsen (160 ITR 67)*, the Supreme Court observed :

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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"The High Court, in our opinion, made a mistake in observing whether transactions of sale and purchase of shares were trading transactions or whether these were in the nature of investment was a question of law. This was a mixed question of law and fact."

7. The principles laid down by the Supreme Court in the above two cases afford adequate guidance to the assessing officers.

8. The Authority for Advance Rulings (AAR) (288 ITR 641), referring to the decisions of the Supreme Court in several cases, has culled out the following principles:

- "(i) Where a company purchases and sells shares, it must be shown that they were held as stock-in-trade and that existence of the power to purchase and sell shares in the memorandum of association is not decisive of the nature of transaction;
- (ii) the substantial nature of transactions, the manner of maintaining books of accounts, the magnitude of purchases and sales and the ratio between purchases and sales and the holding would furnish a good guide to determine the nature of transactions;
- (iii) ordinarily the purchase and sale of shares with the motive of earning a profit, would result in the transaction being in the nature of trade/adventure in the nature of trade; but where the object of the investment in shares of a company is to derive income by way of dividend etc. then the profits accruing by change in such investment (by sale of shares) will yield capital gain and not revenue receipt".

9. Dealing with the above three principles, the AAR has observed in the case of Fidelity group as under:-

"We shall revert to the aforementioned principles. The first principle requires us to ascertain whether the purchase of shares by a FII in exercise of the power in the memorandum of association/trust deed was as stock-in-trade as the mere existence of the power to purchase and sell shares will not by itself be decisive of the nature of transaction. We have to verify as to how the shares were valued/held in the books of account i.e. whether they were valued as stock-in-trade at the end of the financial year for the purpose of arriving at business income or held as investment in capital assets. The second principle furnishes a guide for determining the nature of transaction by verifying whether there are substantial transactions, their magnitude, etc., maintenance of books of account and finding the ratio between

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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purchases and sales. It will not be out of place to mention that regulation 18 of the SEBI Regulations enjoins upon every FII to keep and maintain books of account containing true and fair accounts relating to remittance of initial corpus of buying and selling and realizing capital gains on investments and accounts of remittance to India for investment in India and realizing capital gains on investment from such remittances. The third principle suggests that ordinarily purchases and sales of shares with the motive of realizing profit would lead to inference of trade/adventure in the nature of trade; where the object of the investment in shares of companies is to derive income by way of dividends etc., the transactions of purchases and sales of shares would yield capital gains and not business profits."

10. CBDT also wishes to emphasise that it is possible for a tax payer to have two portfolios, i.e., an investment portfolio comprising of securities which are to be treated as capital assets and a trading portfolio comprising of stock-in-trade which are to be treated as trading assets. Where an assessee has two portfolios, the assessee may have income under both heads i.e., capital gains as well as business income.

11. Assessing officers are advised that the above principles should guide them in determining whether, in a given case, the shares are held by the assessee as investment (and therefore giving rise to capital gains) or as stock-in-trade (and therefore giving rise to business profits). The assessing officers are further advised that no single principle would be decisive and the total effect of all the principles should be considered to determine whether, in a given case, the shares are held by the assessee as investment or stock-in-trade.

12. These instructions shall supplement the earlier Instruction no. 1827 dated August 31, 1989.

## APPENDIX III

### [PARA 9.8]

**Mandatory Communication - Relevant Extracts from the Code of Ethics**  
*(In view of the fact that with effect from 01.04.2014, the Companies Act, 1956 has been replaced with Companies Act, 2013, the "Code of Ethics" issued by ICAI is under revision. The members may refer the revised "Code of Ethics" as and when published.)*

(11<sup>th</sup> Edition - January, 2009)

(Pages 163 to 168)

**Clause (8):** *accepts a position as auditor previously held by another chartered accountant or a certified auditor who has been issued certificate under the Restricted Certificate Rules, 1932 without first communicating with him in writing;*

It must be pointed out that professional courtesy alone is not the major reason for requiring a member to communicate with the existing accountant who is a member of the Institute or a certified auditor. The underlying objective is that the member may have an opportunity to know the reasons for the change in order to be able to safeguard his own interest, the legitimate interest of the public and the independence of the existing accountant. It is not intended, in any way, to prevent or obstruct the change. When making the enquiry from the retiring auditor, the one proposed to be appointed or already appointed should primarily find out whether there are any professional or other reasons why he should not accept the appointment.

It is important to remember that every client has an inherent right to choose his accountant; also that he may, subject to compliance with the statutory requirements in the case of limited Companies, make a change whenever he chooses, whether or not the reasons which had impelled him to do so are good and valid. The change normally occurs where there has been a change of venue of business and a local accountant is preferred or where the partner who has been dealing with the clients affairs retires or dies; or where temperaments clash or the client has some good reasons to feel dissatisfied. In such cases, the retiring auditor should always accept the situation with good grace.

The existence of a dispute as regards the fees may be root cause of an auditor being changed. This would not constitute valid professional reasons

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on account of which an audit should not be accepted by the member to whom it is offered. However, in the case of an undisputed audit fees for carrying out the statutory audit under the Companies Act, 1956 or various other statutes having not been paid, the incoming auditor should not accept the appointment unless such fees are paid. In respect of other dues, the incoming auditor should in appropriate circumstances use his influence in favour of his predecessor to have the dispute as regards the fees settled. The professional reasons for not accepting an audit would be:

- (i) Non-compliance of the provisions of Sections 224 and 225 of the Companies Act as mentioned in Clause (9);
- (ii) Non-payment of undisputed audit fees by auditees other than in case of sick units for carrying out the statutory audit under the Companies Act, 1956 or various other statutes; and
- (iii) Issuance of a qualified report.

In the first two cases, an auditor who accepts the audit would be guilty of professional misconduct. In this connection, attention of members is invited to the Council Guidelines No. 1-CA/(7)/02/2008 dated 08.08.08 appearing in Chapter-3 of the book and also published at page 686 of October, 2008 issue of the Journal. In the said guidelines, Council has explained that the provision for audit fee in accounts signed by both the auditee or the auditor shall be considered as "undisputed" audit fee and "sick unit" shall mean where the net worth is negative.

In the last case, however, he may accept the audit if he is satisfied that the attitude of the retiring auditor was not proper and justified. If, on the other hand, he feels that the retiring auditor had qualified the report for good and valid reasons, he should refuse to accept the audit. There is no rule, written or unwritten, which would prevent an auditor from accepting the appointment offered to him in these circumstances. However, before accepting the audit, he should ascertain the full facts of the case. For nothing will bring the profession to disrepute so much as the knowledge amongst the public that if an auditor is found to be "inconvenient" by the client, he could readily be replaced by another who would not displease the client and this point cannot be too over-emphasised.

What should be the correct procedure to adopt when a prospective client tells you that he wants to change his auditor and wants you to take up his work? There being two persons involved, the Company and the old auditor, the former should be asked whether the retiring auditor had been informed of

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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the intention to change. If the answer is in the affirmative, then a communication should be addressed to the retiring auditor. If, however, it is learnt that the old auditor has not been informed, and the client is not willing to make the first move, it would be necessary to ask him the reason for the proposed change. If there is no valid reason for a change, it would be healthy practice not to accept the audit. If he decides to accept the audit he should address a communication to the retiring auditor.

As stated earlier, the object of the incoming auditor, in communicating with the retiring auditor is to ascertain from him whether there are any circumstances which warrant him not to accept the appointment. For example, whether the previous auditor has been changed on account of having qualified his report or he had expressed a wish not to continue on account of something inherently wrong with the administration of the business. The retiring auditor may even give out information regarding the condition of the accounts of the client or the reason that impelled him to qualify his report. In all these cases it would be essential for the incoming auditor to carefully consider the facts before deciding whether or not he should accept the audit, and should he do so, he must also take into account the information while discharging his duties and responsibilities.

Sometimes, the retiring auditor fails without justifiable cause except a feeling of hurt because of the change, to respond to the communication of the incoming auditor. So that it may not create a deadlock, the auditor appointed can act, after waiting for a reasonable time for a reply.

The Council has taken the view that a mere posting of a letter under certificate of posting is not sufficient to establish communication with the retiring auditor unless there is some evidence to show that the letter has in fact reached the person communicated with. A Chartered Accountant who relies solely upon a letter posted under certificate of posting therefore does so at his own risk.

The view taken by the Council has been confirmed in a decision by the *Rajasthan High Court in J.S. Bhati vs. The Council of the Institute of the Chartered Accountants of India* and another. (Pages 72-79 of Vol. V of Disciplinary Cases published by the Institute - Judgement delivered on 29th August, 1975). The following observations of the Court are relevant in this context:-

"Mere obtaining a certificate of posting in my opinion does not fulfill the requirements of clause (8) of Schedule I as the presumption under Section 114 of the Evidence Act that the letter in due course reached the addressee

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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cannot replace that positive degree of proof of the delivery of the letter to the addressee which the letters of the law in this case require. The expression 'in communication with' when read in the light of the instructions contained in the booklet 'Code of Conduct' cannot be interpreted in any other manner but to mean that there should be positive evidence of the fact that the communication addressed to the outgoing auditor by the incoming auditor reached his hands. Certificate of posting of a letter cannot, in the circumstances, be taken as positive evidence of its delivery to the addressee."

Members should therefore communicate with a retiring auditor in such a manner as to retain in their hands positive evidence of the delivery of the communication to the addressee. In the opinion of the Council, communication by a letter sent "Registered Acknowledgement due" or by hand against a written acknowledgement would in the normal course provide such evidence.

The Council is of the opinion that it would be a healthy practice to communicate with the member who had done the work previously in every case where a Chartered Accountant is required to give a certificate or in respect of a verification of the books of account for special purpose as well as in cases where he is appointed as a Liquidator, Trustee, or Receiver and his predecessor was a Chartered Accountant.

As a matter of professional courtesy and professional obligation it is necessary for the new auditor appointed to act jointly with the earlier auditor and to communicate with such earlier auditor.

It would also be a healthy practice if a tax auditor appointed for conducting special audit under the Income-tax Act, communicates with the member who has conducted the statutory audit.

It is desirable that a member, on receiving communication from the auditor who has been appointed in his place, should send a reply to him as soon as possible setting out in detail the reasons, which according to him had given rise to the change and other attendant circumstances but without disclosing any information as regards the affairs of the client which he is not competent to do.

The Council has taken the view that it is not obligatory for the auditor appointed to conduct a Special Audit under Section 233A of Companies Act, 1956 to communicate with the previous auditor who had conducted the regular audit for the period covered by the Special Audit.

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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The Council has also laid down the detailed guidelines on the subject as under:-

1. The requirement for communicating with the previous auditor being a Chartered Accountant in practice would apply to all types of audit viz., statutory audit, tax audit, internal audit, concurrent audit or any other kind of audit.
2. Various doubts have been raised by the members about the terms "audit", "previous auditor", "Certificate" and "report", normally while interpreting the aforesaid Clause (8). These terms need to be clarified.
3. As per para 2 of the Institute's publication viz. Standard on Auditing (SA) 200, *Overall Objectives of the Independent Auditor and Conduct of an Audit in Accordance with Standards on Auditing* an "audit" is the independent examination of financial information of any entity, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon.
4. The term "previous auditor" means the immediately preceding auditor who held same or similar assignment comprising same/similar scope of work. For example, a Chartered Accountant in practice appointed for an assignment of physical verification of inventory of raw materials, spares, stores and finished goods, before acceptance of appointment, must communicate with the previous auditor being a Chartered Accountant in practice who was holding the appointment of physical verification of inventory of raw materials, stores, finished goods and fixed assets. The mandatory communication with the previous auditor being a Chartered Accountant is required even in a case where the previous auditor happens to be an auditor for a year other than the immediately preceding year.
5. As explained in para 2.2 of the Institute's publication viz., 'Guidance Note on Audit Reports and Certificates for Special Purposes', a "certificate" is a written confirmation of the accuracy of the facts stated therein and does not involve any estimate or opinion. A "report", on the other hand, is a formal statement usually made after an enquiry, examination or review of specified matters under report and includes the reporting auditor's opinion thereon. Thus, when a reporting auditor issues a certificate, he is responsible for the factual accuracy of what is stated therein. On the other hand, when a reporting auditor gives a report, he is responsible for ensuring that the report is based on



### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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factual data, that his opinion is in due accordance with facts, and that it is arrived at by the application of due care and skill.

6. A communication is mandatorily required for all types of audit/report where the previous auditor is a Chartered Accountant. For certification, it would be healthy practice to communicate. In case of assignments done by other professionals not being Chartered Accountants, it would also be a healthy practice to communicate.
7. Although the mandatory requirement of communication with previous auditor being Chartered Accountant applies, in uniform manner, to audits of both government and non government entities, yet in the case of audit of government Companies/banks or their branches, if the appointment is made well in time to enable the obligation cast under this clause to be fulfilled, such obligation must be complied with before accepting the audit. However, in case the time schedule given for the assignment is such that there is no time to wait for the reply from the outgoing auditor, the incoming auditor may give a conditional acceptance of the appointment and commence the work which needs to be attended to immediately after he has sent the communication to the previous auditor in accordance with this clause. In his acceptance letter, he should make clear to the client that his acceptance of appointment is subject to professional objections, if any, from the previous auditors and that he will decide about his final acceptance after taking into account the information received from the previous auditor.

## **APPENDIX IV**

### **[PARA 9.8, 9.9, 9.10, 9.23]**

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Council Guidelines No.1-CA(7)/02/2008, dated 8<sup>th</sup> August,2008

#### **GUIDELINES FOR THE MEMBERS OF ICAI**

*(Issued under the provisions of The Chartered Accountants Act, 1949)*

#### **Chapter I**

#### **Preliminary**

##### **1.0 Short title, commencement, etc.**

- (a) These Guidelines have been issued by the Council of the Institute of Chartered Accountants of India under the provisions of The Chartered Accountants Act, 1949, as amended by The Chartered Accountants (Amendment) Act 2006, in supersession of the Notifications issued by the Council under erstwhile Clause (ii) of Part II of the Second Schedule to the Chartered Accountants Act, 1949.
- (b) These Guidelines be called the 'Council General Guidelines, 2008'.

##### **1.1 Definitions.**

###### **1.1.1 For the purpose of these Guidelines:**

- (a) 'Act' means the Chartered Accountants Act, 1949.
- (b) "Chartered accountant" means a person who is a member of the Institute.
- (c) "Council" means the Council of the Institute constituted under section 9 of the Act.
- (d) "Institute" means the Institute of Chartered Accountants of India constituted under the Act.

###### **1.1.2 All other words and expressions used but not defined herein have the same meaning as assigned to them within the Chartered Accountants Act, 1949 and the Rules, Regulations and Guidelines made there under.**

## **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

### **1.2 Applicability of the Guidelines**

These guidelines shall be applicable to all the Members of the Institute whether in practice or not wherever the context so requires.

### **Chapter II**

#### **Conduct of a Member being an employee**

2.0 A member of the Institute who is an employee shall exercise due diligence and shall not be grossly negligent in the conduct of his duties.

### **Chapter III**

#### **Appointment of a Member as Cost auditor**

#### **3.0 A member of the Institute shall not accept:**

- (i) The appointment as Cost auditor of a Company under Section 233B of the Companies Act, 1956 while he-
  - (a) is an auditor of the Company appointed under Section 224 of the Companies Act; or
  - (b) is an officer or employee of the Company; or
  - (c) is a partner, of any employee or officer of the Company; or
  - (d) is a partner or is in the employment of the Company's auditor appointed under Section 224 of the Companies Act, 1956; or
  - (e) is indebted to the Company for an amount exceeding one thousand rupees, or has given any guarantee or provided any security in connection with the indebtedness of any third person to the Company for an amount exceeding one thousand rupees;

**OR**

- (ii) After his appointment as Cost Auditor, he becomes subject to any of the disabilities stated in items (i) (a) to (e) above and continues to function as a cost auditor thereafter.

**3.1** A member of the Institute in practice shall not accept the appointment as auditor of a Company under Section 224 of the Companies Act, 1956, while he is an employee of the cost auditor of the Company appointed under Section 233B of the Companies Act, 1956.

## **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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### **Chapter IV**

#### **Opinion on financial statements when there is substantial interest**

**4.0** A member of the Institute shall not express his opinion on financial statements of any business or enterprise in which one or more persons who are his "relatives" within the meaning of Section 6 of the Companies Act, 1956 have, either by themselves or in conjunction with such member, a substantial interest in the said business or enterprise.

**Explanation:** For this purpose and for the purpose of compliance of Clause (4) of Part I of the Second Schedule to the Chartered Accountants Act, 1949, the expression "substantial interest" shall have the same meaning as is assigned thereto under Appendix (9) to the Chartered Accountants Regulations, 1988.

### **Chapter V**

#### **Maintenance of books of accounts**

**5.0** A member of the Institute in practice or the firm of Chartered Accountants of which he is a partner, shall maintain and keep in respect of his / its professional practice, proper books of account including the following:-

- (i) a Cash Book;
- (ii) a Ledger.

### **Chapter VI**

#### **Tax Audit assignments under Section 44 AB of the Income-tax Act, 1961**

**6.0** A member of the Institute in practice shall not accept, relating to an assessment year, more than the "specified number of tax audit assignments" under Section 44AB of the Income-tax Act, 1961.

Provided that in the case of a firm of Chartered Accountants in practice, the "specified number of tax audit assignments" shall be construed as the specified number of tax audit assignments for every partner of the firm.

Provided further that where any partner of the firm is also a partner of any other firm or firms of Chartered Accountants in practice, the number of tax audit assignments which may be taken for all the firms together in relation to such partner shall not exceed the "specified number of tax audit assignments" in the aggregate.

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

Provided further that where any partner of a firm of Chartered Accountants in practice accepts one or more tax audit assignments in his individual capacity, the total number of such assignments which may be accepted by him shall not exceed the "specified number of tax audit assignments" in the aggregate.

Provided also that the audits conducted under Section 44AD, 44AE and 44AF of the Income-tax Act, 1961 shall not be taken into account for the purpose of reckoning the "specified number of tax audit assignments".

#### **6.1 Explanation:**

For the above purpose, "the specified number of tax audit assignments" means -

- (a) in the case of a Chartered Accountant in practice or a proprietary firm of Chartered Accountant, 60 tax audit assignments, relating to an assessment year, whether in respect of corporate or non-corporate assesses.
- (b) in the case of firm of Chartered Accountants in practice, 60 tax audit assignments per partner in the firm, relating to an assessment year, whether in respect of corporate or non-corporate assesses.

**6.1.1** In computing the "specified number of tax audit assignments" each year's audit would be taken as a separate assignment.

**6.1.2** In computing the "specified number of tax audit assignments", the number of such assignments, which he or any partner of his firm has accepted whether singly or in combination with any other Chartered Accountant in practice or firm of such Chartered Accountants, shall be taken into account.

**6.1.3** The audit of the head office and branch offices of a concern shall be regarded as one tax audit assignment.

**6.1.4** The audit of one or more branches of the same concern by one Chartered Accountant in practice shall be construed as only one tax audit assignment.

**6.1.5** A Chartered Accountant being a part time practicing partner of a firm shall not be taken into account for the purpose of reckoning the tax audit assignments of the firm.

## **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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**6.1.6** A Chartered Accountant in practice shall maintain a record of the tax audit assignments accepted by him relating to each assessment year in the format as may be prescribed by the Council.

### **Chapter VII**

#### **Appointment of an Auditor in case of non-payment of undisputed fees**

**7.0** A member of the Institute in practice shall not accept the appointment as auditor of an entity in case the undisputed audit fee of another Chartered Accountant for carrying out the statutory audit under the Companies Act, 1956 or various other statutes has not been paid:

**Provided** that in the case of sick unit, the above prohibition of acceptance shall not apply.

#### **7.1 Explanation 1:**

For this purpose, the provision for audit fee in accounts signed by both - the auditee and the auditor shall be considered as "undisputed" audit fee.

#### **7.2 Explanation 2:**

For this purpose, "sick unit" shall mean where the net worth is negative.

### **Chapter VIII**

#### **Specified number of audit assignments**

**8.0** A member of the Institute in practice shall not hold at any time appointment of more than the "specified number of audit assignments" of Companies under Section 224 and/or Section 228 of the Companies Act, 1956.

**Provided** that in the case of a firm of Chartered Accountants in practice, the "specified number of audit assignments" shall be construed as the specific number of audit assignments for every partner of the firm.

**Provided** further that where any partner of the firm of Chartered Accountants in practice is also a partner of any other firm or firms of Chartered Accountants in practice, the number of audit assignments which may be taken for all the firms together in relation to such partner shall not exceed the "specified number of audit assignments" in the aggregate.

**Provided** further where any partner of a firm or firms of Chartered Accountants in practice accepts one or more audit of Companies in his individual capacity, or in the name of his proprietary firm, the total number of such assignments which may be accepted by all firms in relation to such

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

Chartered Accountant and by him shall not exceed the "specified number of audit assignments" in the aggregate.

#### **8.1 Explanation:**

For the above purpose, the "specified number of audit assignments" means –

- a. in the case of a Chartered Accountant in practice or a proprietary firm of Chartered Accountant, thirty audit assignments whether in respect of private Companies or other Companies.
- b. in the case of Chartered Accountants in practice, thirty audit assignments per partner in the firm, whether in respect of private Companies or other Companies.

**Provided** that out of such "specified number of audit assignments, the number of audit assignments of public Companies each of which has a paid-up share capital of rupees twenty-five lakhs or more, shall not exceed ten.

#### **8.2 In computing the "specified number of audit assignments"-**

- a. the number of audit of such Companies, which he or any partner of his firm has accepted whether singly or in combination with any other Chartered Accountant in practice or firm of such Chartered Accountants, shall be taken into account.
- b. the audit of the head office and branch offices of a Company by one Chartered Accountant or firm of such Chartered Accountants in practice shall be regarded as one audit assignment.
- c. the audit of one or more branches of the same Company by one Chartered Accountant in practice or by firm of Chartered Accountants in practice in which he is a partner shall be construed as one audit assignment only.
- d. the number of partners of a firm on the date of acceptance of audit assignment shall be taken into account.

**8.3** A Chartered Accountant in practice, whether in full-time or part-time employment elsewhere, shall not be counted for the purpose of determination of "specified number of audit of Companies" by firms of Chartered Accountants.

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

**8.4** A Chartered Accountant being a part time practicing partner of a firm shall not be taken into account for the purpose of reckoning the audit assignments of the firm.

**8.5** A Chartered Accountant in practice as well as firm of Chartered Accountants in practice shall maintain a record of the audit assignments accepted by him or by the firm of Chartered Accountants, or by any of the partners of the firm in his individual name or as a partner of any other firm, as far as possible, in the following format:

S. No	Name of the Company	Registration Number	Date of Appointment	Date of Acceptance	Date on which Form 23-B filed with the Registrar of Companies
1	2	3	4	5	6

## **Chapter IX**

### **Appointment as Statutory auditor**

**9.0** A member of the Institute in practice shall not accept the appointment as statutory auditor of Public Sector Undertaking(s)/ Government Company(ies)/ Listed Company(ies) and other Public Company(ies) having turnover of Rs. 50 crores or more in a year where he accepts any other work(s) or assignment(s) or service(s) in regard to the same Undertaking(s)/ Company(ies) on a remuneration which in total exceeds the fee payable for carrying out the statutory audit of the same Undertaking/company.

**Provided** that in case appointing authority(ies)/regulatory body(ies) specify(ies) more stringent condition(s)/ restriction(s), the same shall apply instead of the conditions/ restrictions specified under these Guidelines.

**9.1** The above restrictions shall apply in respect of fees for other work(s) or service(s) or assignment(s) payable to the statutory auditors and their associate concern(s) put together.

**9.2** For the above purpose,

- (i) the term "other work(s)" or "service(s)" or "assignment(s)" shall include Management Consultancy and all other professional services permitted by the Council pursuant to Section 2(2)(iv) of the Chartered Accountants Act, 1949 but shall not include: -



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- (a) audit under any other statute;
- (b) certification work required to be done by the statutory auditors; and
- (c) any representation before an authority;
- (ii) the term "associate concern" means any corporate body or partnership firm which renders the Management Consultancy and all other professional services permitted by the Council wherein the proprietor and/or partner(s) of the statutory auditor firm and/or their "relative(s)" is/are Director/s or partner/s and/or jointly or severally hold "substantial interest" in the said corporate body or partnership;
- (iii) the terms "relative" and "substantial interest" shall have the same meaning as are assigned thereto under Appendix (9) to the Chartered Accountants Regulations, 1988.

**9.3** In regard to taking up other work(s) or service(s) or assignment(s) of the undertaking/company referred to above, it shall be open to such associate concern or corporate body to render such work(s) or service(s) or assignment(s) so long as aggregate remuneration for such other work(s) or service(s) or assignment(s) payable to the statutory auditor/s together with fees payable to its associate concern(s) or corporate body(ies) do/does not exceed the aggregate of fee payable for carrying out the statutory audit.

### **Chapter X**

#### **Appointment of an auditor when he is indebted to a concern**

**10.0** A member of the Institute in practice or a partner of a firm in practice or a firm shall not accept appointment as auditor of a concern while indebted to the concern or given any guarantee or provided any security in connection with the indebtedness of any third person to the concern, for limits fixed in the statute and in other cases for amount exceeding Rs. 10,000/-

### **Chapter XI**

#### **Directions in case of unjustified removal of auditors**

**11.0** A member of the Institute in practice shall follow the direction given, by the Council or an appropriate Committee or on behalf of any of them, to him being the incoming auditor(s) not to accept the appointment as auditor(s), in the case of unjustified removal of the earlier auditor(s).

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### Chapter XII

#### Minimum Audit Fee in respect of Audit\*

**12.0** A member of the Institute in practice shall not, on behalf of the firm of chartered accountants in which he is a partner, accept or carry out any audit work involving receipt of audit fees (excluding reimbursement of expenses, if any) for such work of an amount less than what is specified hereunder:-

- (a) consisting of 5 or more partners but less than 10 partners with at least one partner holding a certificate of practice for five years or more; or
- (b) consisting of 10 or more partners with at least one partner holding a certificate of practice for five years or more.

		Practising firm having 5 or more partners but less than 10 partners	Practising firm having 10 or more partners
(i)	In cities with population of 3 million and above. (as per the last census)	Rs. 6000/-p.a.	Rs. 12000/-p.a.
(ii)	In cities/towns having population of less than 3 million. (as per the last census)	Rs. 3500/-p.a.	Rs. 8000/-p.a.

Provided that such restriction shall not apply in respect of the following: -

- (i) audit of accounts of charitable institutions clubs, provident funds, etc. where the appointment is honorary i.e. without any fees;
- (ii) statutory audit of branches of banks including regional rural banks;
- (iii) audit of newly formed concerns relating to two accounting years from the date of commencement of their operations;
- (iv) certification or audit under Income-tax Act or other attestation work carried out by the Statutory Auditor; and
- (v) Sales Tax Audit and VAT Audit.

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\* Chapter XII – 'Minimum Audit fee in respect of Audit' was repealed by the Council at its 306<sup>th</sup> meeting held on 7<sup>th</sup> & 8<sup>th</sup> June, 2011.

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

### 12.1 Explanation:

For the purpose of these Guidelines, the expression statutory auditor means and includes a chartered accountant appointed as an auditor under a Central/State or Provincial Act as well as an auditor appointed under any agreement.

The Council has clarified that for the above purpose the audit of Provident Fund Trust, Gratuity Fund etc. carried out by the statutory auditor are to be considered as separate and distinct audit so that the above restrictions are applicable to it.

### Chapter XIII

#### **Repeal and Saving**

**13.0** The Notifications as specified in the Schedule hereto, issued under erstwhile Clause (ii) of Part II of the Second Schedule to the Chartered Accountants Act, 1949 by the Council from time to time shall stand repealed from the date herein.

**13.1** Notwithstanding such repeal:-

- (a) Anything done or any action taken or purported to have been done or taken, any enquiry or investigation commenced or show cause notice issued in respect of the said notifications shall be deemed to have been done or taken under the corresponding provisions of these guidelines.
- (b) Any application made to the Council or Director (Discipline) under the said Notifications and pending before the Director (Discipline), Board of Discipline, Disciplinary Committee and the Council shall be deemed to have been made under the corresponding provisions of these Guidelines.

### SCHEDULE

#### **NOTIFICATIONS ISSUED BY THE COUNCIL UNDER ERSTWHILE CLAUSE (ii) OF PART II OF THE SECOND SCHEDULE TO THE CHARTERED ACCOUNTANTS ACT, 1949.**

1. No.1- CA(7)/65, dated 6<sup>th</sup> November, 1965.
2. No.1- CA (37)/70, Published in Part III Section 4 of the Gazette of India dated 30<sup>th</sup> May, 1970.
3. No.1- CA (39)/70, Published in Part III Section 4 of the Gazette of India dated 24<sup>th</sup> October, 1970.

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4. No.1-CA (44)/71, Published in Part III Section 4 of the Gazette of India dated 20th March, 1971.
5. No.1- CA (153)/86, Published in Part III Section 4 of the Gazette of India dated 30th August, 1986.
6. No.1- CA (7)/3/88, Published in Part III Section 4 of the Gazette of India dated 4th February, 1989.
7. No.1- CA (7)/9/89, Published in Part III Section 4 of the Gazette of India dated 19th August, 1989 (Since quashed by the Supreme Court vide Order dated 16<sup>th</sup> May, 2007).
8. No.1- CA (7)/43/99, Published in Part III Section 4 of the Gazette of India dated 31st July, 1999.
9. No.1- CA (7)/46/99, Published in Part III Section 4 of the Gazette of India dated 13th November, 1999.
10. No.1- CA (7)/53/2001, Published in Part III Section 4 of the Gazette of India dated 12<sup>th</sup> May, 2001.
11. No.1- CA (7)/60/2002, Published in Part III Section 4 of the Gazette of India dated 23<sup>rd</sup> March, 2002.
12. No.1- CA (7)/63/2002, Published in Part III Section 4 of the Gazette of India dated 7<sup>th</sup> September, 2002.
13. No.1- CA (7)/67/2002, Published in Part III Section 4 of the Gazette of India dated 19<sup>th</sup> October, 2002.
14. No.1- CA (7)/75/2004, Published in Part III Section 4 of the Gazette of India dated 22<sup>nd</sup> May, 2004.

## APPENDIX V

### [PARA 9.18]

Relevant extracts from the Code of Ethics, 11<sup>th</sup> Edition, January 2009 pages 239- 243 *(In view of the fact that with effect from 01.04.2014.the Companies Act, 1956 has been replaced with Companies Act, 2013, the "Code of Ethics" issued by ICAI is under revision. The members may refer the revised "Code of Ethics" as and when published.)*

**Clause (4):** expresses his opinion on financial statements of any business or any enterprise in which he, his firm or a partner in his firm has a substantial interest;

If the opinion of auditors are to command respect and the confidence of the public, it is essential that it must be free of any interest which is likely to affect their independence. Since financial interest in the business can be a substantial interest and one of the important factors which may disturb independence, the existence of such an interest direct or indirect affects the opinion of the auditors. As per this clause, an auditor should not express his opinion on financial statements of any business or enterprise wherein he has a substantial interest. This is intended to assure the public as regards the faith and confidences that could be reposed on the independent opinion expressed by the auditors.

In this connection attention of members is also invited to Chapter IV of Council Guidelines No. 1-CA(7)/02/2008 dated 8<sup>th</sup> August, 2008. The said guidelines state that a member of the Institute shall not express his opinion on financial statements of any business or enterprise in which one or more persons, who are his "relatives" within the meaning of AS-18, have either by themselves or in conjunction with such members, a substantial interest in the said business or enterprise. For the purpose of said guideline and aforesaid clause, the expression "substantial interest" shall have meaning as is assigned thereto, under Appendix (9) of the Chartered Accountants Regulations, 1988. (see **Appendix-'F'**).

The words "financial statements" used in this clause would cover both reports and certificates usually given after an examination of the accounts or the financial statement or any attest function under any statutory enactment or for purposes of income-tax assessments. This would not, however, apply to cases where such statements are prepared by members in employment

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purely for the information of their respective employers in the normal course of their duties and not meant to be submitted to any outside authority.

Public conscience is expected to be ahead of the law. Members, therefore, are expected to interpret the requirement as regards independence much more strictly than what the law requires and should not place themselves in positions which would either compromise or jeopardise their independence.

Member must take care to see that they do not land themselves in situations where there could be conflict of interest and duty. For example, where a Chartered Accountant is appointed the Liquidator of a Company, he should not qua a Chartered Accountant himself, audit the Statement of Accounts to be filed under Section 551(1) of the Companies Act, 1956. The audit in such circumstances should be done by a chartered Accountant other than the one who is the Liquidator of the Company.

In this connection, the Council has decided not to permit a Chartered Accountant in employment to certify the financial statements of the concern in which he is employed, or of a concern under the same management as the concern in which he is employed, even though he holds certificate of practice and that such certification can be done by any Chartered Accountant in practice. This restriction would not however apply where the certification is permitted by any law, e.g. Section 228(iv) of the Companies Act, 1956 and the Companies (Branch Audit Exemption) Rules, 1961 made thereunder. The Council has also decided that a Chartered Accountant should not by himself or in his firm name:-

- (i) accept the auditorship of a college, if he is working as a part-time lecturer in the college.
- (ii) accept the auditorship of a trust where his partner is either an employee or a trustee of the trust.

The Council has, in this connection, issued the following guidelines:

Attention of the members is invited to the provisions of Clause (4) of Part I of the Second Schedule to the Chartered Accountants Act which provides that a Chartered Accountant in practice shall be deemed to be guilty of professional misconduct if he expresses his opinion on financial statements of any business or any enterprise in which he, his firm or a partner in his firm has a substantial interest.

Many new areas of professional work have been added, e.g., Tax Audit, Concurrent Audit of Banks, Concurrent Audit of Borrowers of Financial institutions, Audit of non-corporate borrowers of banks and financial

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institutions, audit of stock exchange, brokers etc. The Council wishes to emphasize that the aforesaid requirement of Clause (4) are equally applicable while performing all types of attest functions by the members. Some of the situations which may arise in the applicability of Clause (4) are discussed below for the guidance of members:-

**1. Where the member, his firm or his partner or his relative has substantial interest in the business or enterprise.**

The independence of mind is a fundamental concept of audit and/or expression of opinion on the financial statements in any form and, therefore, must always be maintained. Nothing can substitute for the essential and fundamental requirements of independence. Therefore, the Council's views are clarified in the following circumstances.

**(i) An enterprise/concern of which a member is either an owner or a partner**

The holding of interest in the business or enterprise by a member himself whether as sole-proprietor or partner in a firm, in the opinion of the Council, would affect his independence of mind in the performance of professional duties in conducting the audit and/or expressing an opinion on financial statements of such enterprise. Therefore, a member should not audit financial statements of such business or enterprise.

**(ii) Where the partner or relative of a member has substantial interest**

The holding of substantial interest by the partner or relative of the member in the business or enterprise of which the audit is to be carried out and opinion is to be expressed on the financial statement, may also affect the independence of mind of the member, in the opinion of Council, in the performance of professional duties. Therefore, the member may, for the same reasons as not to compromise his independence, desist from undertaking the audit of financial statements of such business or enterprise.

**2. Where the member or his partner or relative is a director or in the employment of an officer or an employee of the Company.**

Section 226 of the Companies Act specifically prohibits a member from auditing the accounts of a Company in which he is a director or in the employment of an officer or an employee of the Company. Although the provisions of the aforesaid section are not specifically applicable in the context of audits performed under other statutes, e.g. tax audit, yet the underlying principle of independence of mind is equally applicable in those situations also. Therefore, the Council's views are clarified in the following situations.

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#### **(i) Where a member is a director**

In cases where the member is a director of a Company the financial statements of which are to be audited and/or opinion is to be expressed, he should not undertake such job and/or express opinion on the financial statements of that Company.

#### **(ii) Where a partner or relative of the member is a director in the Company who has a substantial interest.**

In such cases for the reason as not to compromise with the independence of mind, the member may desist from undertaking the audit of financial statements and/or expression of opinion thereon. The meaning of the words "relative" and "substantial interest" shall be the same as are contained in the Resolution passed by the Council in pursuance to Regulation, 190A of Chartered Accountants Regulations, 1988 (see **Appendix-'F'**).

An accountant is expected to be no less independent in the discharge of his duties as a tax consultant or as a financial adviser than as auditor. In fact, it is necessary that he should bear the same degree of integrity and independence of mind in all spheres of his work. Unless this is done, the accounts of Companies audited by Chartered Accountants or statements made by them during the course of assessment proceedings would not be relied upon as correct by the authorities.

The Council has clarified that the members are not permitted to write the books of account of their auditee clients.

A statutory auditor of a Company cannot also be its internal auditor, as it will not be possible for him to give independent and objective report issued under sub-Section 4A of Section 227 of the Companies Act read with the Companies (Auditor's Report) Order, 2003.

A member should satisfy himself before accepting an appointment as an auditor of an entity that his appointment is in accordance with the statute governing the entity. In case the entity is constituted under a trust deed/instrument, the member should satisfy whether his appointment is valid according to the instrument constituting the entity and rules and regulations made thereunder. In case the appointment is to be authorised by the regulatory authorities such as in the case of cooperative societies, trusts etc. then the member must satisfy whether such regulatory authorities have authorised the managing committee of the society/trust for appointment of the auditors. In a case where any entity is being managed by a Managing Committee or Board of Trustees or Board of Governors by whatever name



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called he should ensure that his appointment is duly made by a resolution passed of such Managing Committee or Board of Trustees or Board of Governors. Even in case of partnership or sole proprietary concerns, the member must ensure that a letter of appointment/engagement is given by the firm/sole proprietor before he accepts the appointment/ engagement.

## APPENDIX VI

*[PARA 9.26]*

### FORM OF TAX AUDIT PARTICULARS TO BE FURNISHED BY MEMBERS/FIRM

#### Record of Tax Audit Assignments

1. Name of the Member accepting the assignment
2. Membership No.
3. Financial year of audit acceptance
4. Name and Registration No. of the firm/ firms of which the member is a proprietor or partner.

Sl.No.	Name of the auditee	Assessment year of the auditee	Date of appointment	Date of acceptance	Name of the firm on whose behalf the member has accepted the assignment	Date of communication with the previous auditor (applicable)
1	2	3	4	5	6	7

## APPENDIX VII

*[PARA 9.27]*

Revised Minimum recommended scale of fees chargeable for the professional assignments done by Chartered Accountants - *An announcement hosted by Committee for Capacity Building of CA Firms and Small and Medium Practitioners-Last updated on 18<sup>th</sup> July, 2014:*

PARTICULARS			Rates	
			For Class A Cities	For Class B Cities
			Revised Minimum Recommended scale of Fees	Revised Minimum Recommended scale of Fees
I)	ADVISING ON DRAFTING OF DEEDS/AGREEMENTS			
	(a)	i) Partnership Deed	Rs. 10,500/- & Above	Rs. 7,000/- & Above
		ii) Partnership Deed (With consultation & Tax Advisory)	Rs. 15,000/- & Above	Rs. 10,000/- & Above
	(b)	Filing of Forms with Registrar of Firms	Rs. 4,500/- & Above Per Form	Rs. 3,000/- & Above Per Form
	(c)	Supplementary / Modification in Partnership Deed	Rs. 9,000/- & Above	Rs. 6,000/- & Above
II)	INCOME TAX			
	A.	Filing of Return of Income		
	I)	For Individuals/ HUFs etc.		
		(a) Filing of Return of Income with Salary/Other Sources/Share of Profit	Rs. 6,000/- & Above	Rs. 4,000/- & Above
		(b) Filing of Return of Income with detailed Capital Gain working		

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		(i) Less than 10 Transactions (For Shares & Securities)	Rs. 9,000/- & Above	Rs. 6,000/- & Above
		(ii) More than 10 Transactions (For Shares & Securities)	Rs. 15,000/- & Above	Rs. 10,000/- & Above
		(c) Filing of Return of Income for Capital Gain on Immovable property	Rs. 30,000/- & Above	Rs. 20,000/- & Above
		(d) Filing of Return of Income with Preparation of Bank Summary, Capital A/c & Balance Sheet.	Rs. 10,500/- & Above	Rs. 7,000/- & Above
	II)	(a) Partnership Firms/Sole Proprietor with Advisory Services	Rs. 12,000/- & Above	Rs. 8,000/- & Above
		(b) Minor's I.T. Statement	Rs. 6,000/- & Above	Rs. 4,000/- & Above
		(c) Private Ltd. Company :		
		(i) Active	Rs. 22,500/- & Above	Rs. 15,000/- & Above
		(ii) Defunct	Rs. 10,500/- & Above	Rs. 7,000/- & Above
		(d) Public Ltd. Company		
		(i) Active	Rs. 60,000/- & Above	Rs. 40,000/- & Above
		(ii) Defunct	Rs. 22,500/- & Above	Rs. 15,000/- & Above
	B.	Filing of Forms Etc.	(Quarterly Fees)	(Quarterly Fees)
		(a) Filing of TDS/TCS Return (per Form)		
		(i) With 5 or less Entries	Rs. 3,000/- & Above	Rs. 2,000/- & Above
		(ii) With more than 5 Entries	Rs. 7,500/- & Above	Rs. 5,000/- & Above

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		(b) Filing of Form No. 15-H/G ( per Set)	Rs. 3,000/- & Above	Rs. 2,000/- & Above
		(c) Form No. 49-A/49-B	Rs. 3,000/- & Above	Rs. 2,000/- & Above
		(d) Any other Forms filed under the Income Tax Act	Rs. 3,000/- & Above	Rs. 2,000/- & Above
	C.	Certificate		
		Obtaining Certificate from Income Tax Department	Rs. 12,000/- & Above	Rs. 8,000/- & Above
	D.	Filing of Appeals Etc.		
		(a) First Appeal Preparation of Statement of Facts, Grounds of Appeal, Etc.	Rs. 30,000/- & Above	Rs. 20,000/- & Above
		(b) Second Appeal (Tribunal)	Rs. 60,000/- & Above	Rs. 40,000/- & Above
	E.	Assessments Etc.		
		(a) Attending Scrutiny Assessment/Appeal		
		(i) Corporate	See Note 1	See Note 1
		(ii) Non Corporate	Rs. 30,000/- & Above	Rs. 20,000/- & Above
		(b) Attending before Authorities	Rs. 9,000/- & Above Per Visit	Rs. 6,000/- & Above Per Visit
		(c) Attending for Rectifications/Refunds/Appeal effects Etc.	Rs. 6,000/- & Above Per Visit	Rs. 4,000/- & Above Per Visit
		(d) Income Tax Survey	Rs. 75,000/- & Above	Rs. 50,000/- & Above
		(e) T.D.S. Survey	Rs. 45,000/- & Above	Rs. 30,000/- & Above
		(f) Income Tax Search and Seizure	See Note 1	See Note 1

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		(g) Any other Consultancy	See Note 1	See Note 1
<b>III)</b>	<b>CHARITABLE TRUST</b>			
	(a)	(i) Registration Under Local Act	Rs. 22,500/- & Above	Rs. 15,000/- & Above
		(ii) Societies Registration Act	Rs. 30,000/- & Above	Rs. 20,000/- & Above
	(b)	Registration Under Income Tax Act	Rs. 22,500/- & Above	Rs. 15,000/- & Above
	(c)	Exemption Certificate U/s 80G of Income Tax Act	Rs. 18,000/- & Above	Rs. 12,000/- & Above
	(d)	Filing Objection Memo/other Replies	Rs. 9,000/- & Above	Rs. 6,000/- & Above
	(e)	Filing of Change Report	Rs. 9,000/- & Above	Rs. 6,000/- & Above
	(f)	Filing of Annual Budget	Rs. 9,000/- & Above	Rs. 6,000/- & Above
	(g)	Attending before Charity Commissioner including for Attending Objections	Rs. 7,500/- & Above per visit	Rs. 5,000/- & Above per visit
	(h)	(i) F.C.R.A. Registration	Rs. 30,000/- & Above	Rs. 20,000/- & Above
		(ii) F.C.R.A. Certification	Rs. 7,500/- & Above	Rs. 5,000/- & Above
<b>IV)</b>	<b>COMPANY LAW AND LLP WORK</b>			
	(a)	Filing Application for Name Approval	Rs. 6,000/- & Above	Rs. 4,000/- & Above
	(b)	Incorporation of a Private Limited Company/LLP	Rs. 30,000/- & Above	Rs. 20,000/- & Above
	(c)	Incorporation of a Public Limited Company	Rs. 60,000/- & Above	Rs. 40,000/- & Above
	(d)	(i) Company's/LLP ROC Work, Preparation of Minutes, Statutory Register & Other Secretarial Work	See Note 1	See Note 1

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		(ii) Certification (Per Certificate)	Rs. 9,000/- & Above	Rs. 6,000/- & Above
	(e)	Filing Annual Return Etc.	Rs. 9,000/- & Above per Form	Rs. 6,000/- & Above per Form
	(f)	Filing Other Forms Like : F-32, 18, 2 etc.	Rs. 3,000/- & Above per Form	Rs. 2,000/- & Above per Form
	(g)	Increase in Authorised Capital		
		Filing of F-5, F-23, preparation of Revised Memorandum of Association/Article of Association/LLP Agreement	Rs. 22,500/- & Above	Rs. 15,000/- & Above
	(h)	DPIN/DIN per Application	Rs. 3,000/- & Above	Rs. 2,000/- & Above
	(i)	Company Law Consultancy including Petition drafting	See Note 1	See Note 1
	(j)	Company Law representation including LLP before RD and CLB	See Note 1	See Note 1
	(k)	ROC Representation	See Note 1	See Note 1
<b>V)</b>	<b>V.A.T./ PROFESSIONAL TAX</b>			
	A.	Registration Work		
		(a) Registration Under V.A.T. & C.S.T. Corporate Non Corporate	See Note 1 Rs. 15,000/- & Above	See Note 1 Rs. 10,000/- & Above
		(b) Professional Tax Registration (PTR)	Rs. 6,000/- & Above	Rs. 4,000/- & Above
		(c) Professional Tax Enrollment (per Application)	Rs. 3,000/- & Above	Rs. 2,000/- & Above

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	B.	Filing of Return (V.A.T.)		
		(a) Monthly Challans with Annual Return	Rs. 3,000 + (Per Month)	Rs. 2,000/- + (Per Month)
		(b) Quarterly Challans with Annual Return	Rs. 4,500 + (Per Quarter)	Rs. 3,000/- + (Per Quarter)
		(c) Six Monthly Challans with Annual Return	Rs. 6,000 + (Per 6 Months)	Rs. 4,000/- + (Per 6 Months)
		(d) Yearly Composition Return	Rs. 9,000/- & Above	Rs. 6,000/- & Above
	C.	Assessments/Appeals		
		(a) Attending V.A.T./Commercial Tax Assessments	Rs. 15,000/- + 7,500/- (Per Visit)	Rs. 10,000/- + 5,000/- (Per Visit)
		(b) Attending V.A.T./Commercial Tax Appeals	Rs. 15,000/- + 9,000/- (Per Visit)	Rs. 10,000/- + 6,000/- (Per Visit)
	D.	Filing of Appeal/Appeals Drafting		
		(a) First Appeal (AC/DC)	Rs. 15,000/- & Above	Rs. 10,000/- & Above
		(b) Second Appeal	Rs. 22,500/- & Above	Rs. 15,000/- & Above
	E.	Miscellaneous Work		
		(a) Professional Tax Returns & Assessment	Rs. 7,500/- & Above	Rs. 5,000/- & Above
		(b) Obtaining C/F/H Forms under V.A.T./Commercial Tax	( Per Application)	( Per Application)
		(i) First Time	Rs. 6,000/- & Above	Rs. 4,000/- & Above
		(ii) Renewal	Rs. 3,000/- & Above	Rs. 2,000/- & Above



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VI)	AUDIT AND OTHER ASSIGNMENTS		
	Rate per day would depend on the complexity of the work and the number of days spent by each person		
	(i) Principal	Rs. 15,000/- & Above per day	Rs. 10,000/- & Above per day
	(ii) Qualified Assistants	Rs. 7,500/- & Above per day	Rs. 5,000/- & Above per day
	(iii) Semi Qualified Assistants	Rs. 3,000/- & Above per day	Rs. 2,000/- & Above per day
	(iv) Other Assistants	Rs. 1,500/- & Above per day	Rs. 1,000/- & Above per day
	Subject to minimum indicative Fees as under:		
	(i) Tax Audit	Rs. 37,500/- & Above	Rs. 25,000/- & Above
	(ii) Company Audit		
	(a) Small Pvt. Ltd. Co. (Turnover up to Rs. 2 Crore)	Rs. 45,000/- & Above	Rs. 30,000/- & Above
	(b) Medium Size Pvt. Ltd. Co./ Public Ltd. Co.	Rs. 75,000/- & Above	Rs. 50,000/- & Above
	(c) Large Size Pvt. Ltd. Co./Public Ltd. Co.	See Note 1	See Note 1
	(iii) V.A.T. Audit	Rs. 22,500/- & Above	Rs. 15,000/- & Above
	(iv) Review of TDS Compliance	Rs. 22,500/- & Above	Rs. 15,000/- & Above
	(v) Transfer Pricing Audit	See Note 1	See Note 1

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<b>VII)</b>	<b>INVESTIGATION, MANAGEMENT SERVICES OR SPECIAL ASSIGNMENTS</b>			
		Rate per day would depend on the complexity of the work and the number of days spent by each person		
		(a) Principal	Rs. 30,000/- & Above + per day charge	Rs. 20,000/- & Above + per day charge
		(b) Qualified Assistant	Rs. 15,000/- & Above + per day charge	Rs. 10,000/- & Above + per day charge
		(c) Semi Qualified Assistant	Rs. 7,500/- & Above + per day charge	Rs. 5,000/- & Above + per day charge
<b>VIII)</b>	<b>CERIFICATION WORK</b>			
	(a)	Issuing Certificates under the Income Tax Act i.e. U/s 80IA/80IB/10 A/10B & other Certificates	See Note 1	See Note 1
	(b)	Other Certificates		
		For LIC/Passport/Credit Card/Etc.	Rs. 7,500/- & Above	Rs. 5,000/- & Above
	(c)	Other Attestation (True Copy)	Rs. 1,500/- per form	Rs. 1,000/- per Form
	(d)	Net worth Certificate for person going abroad	Rs. 1,5000/- & Above	Rs. 10,000/- & Above
<b>IX)</b>	<b>WEALTH TAX</b>			
	(a)	Per statement	Rs. 15,000/- & Above	Rs. 10,000/- & Above
	(b)	Statement & Filing Return	Rs. 20,000/- & Above	Rs. 15,000/- & Above

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

<b>X)</b>	<b>CONSULTATION &amp; ARBITRATION</b>		
	Rate per hour would depend on the complexity of the work and the number of hours agent by each person.		
	(a) Principal	Rs. 30,000/- & Above(initial fees) + additional fees @ Rs. 7,500/- & Above per hour	Rs. 20,000/- & Above(initial fees) + additional fees @ Rs. 5,000/- & Above per hour
	(b) Qualified Assistant	Rs. 5,300/- & Above per hour	Rs. 3,500/- & Above per hour
	(c) Semi Qualified Assistant	Rs. 2,300/- & Above per hour	Rs. 1,500/- & Above per hour
<b>XI)</b>	<b>NBFC/RBI MATTERS</b>		
	(a) NBFC Registration with RBI	See Note 1	See Note 1
	(b) Other Returns	Rs. 15,000/- & Above	Rs. 10,000/- & Above
<b>XII)</b>	<b>SERVICE TAX</b>		
	(a) Registration	Rs. 15,000/- & Above	Rs. 10,000/- & Above
	(b) Registration with Consultation	See Note 1	See Note 1
	(c) Tax Advisory & Consultation i.e. about value, taxability, classification etc.	See Note 1	See Note 1
	(d) Monthly Challan with Half Yearly Return	Rs. 15,000/- & Above + (Rs.3,000/- Per Month)	Rs. 10,000/- & Above + (Rs.2,000/- Per Month)

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

	(e)	Quarterly Challan with Half Yearly Return	Rs. 15,000/- & Above + (Rs. 4,500/- Per Quarter)	Rs. 10,000/- & Above + (Rs. 3,000/- Per Quarter)
	(f)	Adjudication	Rs. 45,000/- & Above	Rs. 30,000/- & Above
	(g)	Appeal & show cause notice drafting/ reply	Rs. 30,000/- & Above	Rs. 20,000/- & Above
<b>XIII)</b>	<b>FEMA MATTERS</b>			
	1	Filing Declaration with RBI in relation to transaction by NRIs/OCBs	Rs. 30,000/- & Above	Rs. 20,000/- & Above
	2	Obtaining Prior Permissions from RBI for Transaction with NRIs/OCBs	Rs. 45,000/- & Above	Rs. 30,000/- & Above
	3	Technical Collaboration:		
		Advising, obtaining RBI permission, drafting and preparing technical collaboration agreement and incidental matters	See Note 1	See Note 1
	4	Foreign Collaboration:		
		Advising, obtaining RBI permission, drafting and preparing technical collaboration agreement and incidental matters (incl. Shareholders Agreement)	See Note 1	See Note 1
	5	Advising on non Resident Taxation Matters including Double Tax Avoidance Agreements including FEMA	See Note 1	See Note 1
<b>XIV)</b>	<b>PROJECT FINANCING</b>			
	(a)	Preparation of CMA Data	See Note 1	See Note 1
	(b)	Services relating to Financial sector	See Note 1	See Note 1

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

**Notes:**

- 1) Fees to be charged depending on the complexity and the time spent on the particular assignment.
- 2) The above recommended minimum scale of fees is as recommended by the Committee for Capacity Building of CA Firms & Small and Medium Practitioners (CCBCAF&SMP) of ICAI and duly considered by the council.
- 3) The aforesaid table states recommendatory minimum scale of fees works out by taking into account average time required to complete such assignments. However, members are free to charge varying rates depending upon the nature and complexity of assignment and time involved in completing the same.
- 4) Office time spent in travelling & out-of-pocket expenses would be chargeable. The Committee issues for general information the above recommended scale of fees which it considers reasonable under present conditions. It will be appreciated that the actual fees charged in individual cases will be matter of agreement between the member and the client.
- 5) Service Tax should be collected separately wherever applicable.
- 6) The Committee also recommends that the bill for each service should be raised separately and immediately after the services are rendered.
- 7) "Class A Cities here includes Delhi, Mumbai, Calcutta, Chennai, Pune, Hyderabad, Bangalore and Ahmedabad.  
Class B Cities includes all other cities not included in "Class A"."
- 8) The amount charged will be based on the location of the service provider.

Please note the above mentioned rates are as per the data available on ICAI website at below link:

[http://www.icai.org/new\\_post.html?post\\_id=7252](http://www.icai.org/new_post.html?post_id=7252)

## APPENDIX VIII

### *[PARA 10.3 & 10.8]*

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#### I. Harmonised Criteria for Classification of Entities

##### (1) Criteria for classification of non-corporate entities as decided by the Institute of Chartered Accountants of India

##### Level I Entities

Non-corporate entities which fall in any one or more of the following categories, at the end of the relevant accounting period, are classified as Level I entities:

- (i) Entities whose equity or debt securities are listed or are in the process of listing on any stock exchange, whether in India or outside India.
- (ii) Banks (including co-operative banks), financial institutions or entities carrying on insurance business.
- (iii) All commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees fifty crore in the immediately preceding accounting year.
- (iv) All commercial, industrial and business reporting entities having borrowings (including public deposits) in excess of rupees ten crore at any time during the immediately preceding accounting year.
- (v) Holding and subsidiary entities of any one of the above.

##### Level II Entities (SMEs)

Non-corporate entities which are not Level I entities but fall in any one or more of the following categories are classified as Level II entities:

- (i) All commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds 1 crore but does not exceed rupees fifty crore in the immediately preceding accounting year.
- (ii) All commercial, industrial and business reporting entities having borrowings (including public deposits) in excess of rupees one crore but not in excess of rupees ten crore at any time during the immediately preceding accounting year.
- (iii) Holding and subsidiary entities of any one of the above.

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**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**


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**Level III Entities (SMEs)**

Non-corporate entities which are not covered under Level I and Level II are considered as Level III entities.

**Additional requirements**

- (1) An SME which does not disclose certain information pursuant to the exemptions or relaxations given to it should disclose (by way of a note to its financial statements) the fact that it is an SME and has complied with the Accounting Standards insofar as they are applicable to entities falling in Level II or Level III, as the case may be.
- (2) Where an entity, being covered in Level II or Level III, had qualified for any exemption or relaxation previously but no longer qualifies for the relevant exemption or relaxation in the current accounting period, the relevant standards or requirements become applicable from the current period and the figures for the corresponding period of the previous accounting period need not be revised merely by reason of its having ceased to be covered in Level II or Level III, as the case may be. The fact that the entity was covered in Level II or Level III, as the case may be, in the previous period and it had availed of the exemptions or relaxations available to that Level of entities should be disclosed in the notes to the financial statements.
- (3) Where an entity has been covered in Level I and subsequently, ceases to be so covered, the entity will not qualify for exemption/relaxation available to Level II entities, until the entity ceases to be covered in Level I for two consecutive years. Similar is the case in respect of an entity, which has been covered in Level I or Level II and subsequently, gets covered under Level III.
- (4) If an entity covered in Level II or Level III opts not to avail of the exemptions or relaxations available to that Level of entities in respect of any but not all of the Accounting Standards, it should disclose the Standard(s) in respect of which it has availed the exemption or relaxation.
- (5) If an entity covered in Level II or Level III desires to disclose the information not required to be disclosed pursuant to the exemptions or relaxations available to that Level of entities, it should disclose that information in compliance with the relevant Accounting Standard.
- (6) An entity covered in Level II or Level III may opt for availing certain exemptions or relaxations from compliance with the requirements prescribed in an Accounting Standard:

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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Provided that such a partial exemption or relaxation and disclosure should not be permitted to mislead any person or public.

(7) In respect of Accounting Standard (AS) 15, *Employee Benefits*, exemptions/ relaxations are available to Level II and Level III entities, under two sub-classifications, viz., (i) entities whose average number of persons employed during the year is 50 or more, and (ii) entities whose average number of persons employed during the year is less than 50. The requirements stated in paragraphs (1) to (6) above, mutatis mutandis, apply to these sub-classifications.

### **(2) Criteria for classification of companies under the Companies (Accounting Standards) Rules, 2006**

**Small and Medium-Sized Company (SMC) as defined in Clause 2(f) of the Companies (Accounting Standards) Rules, 2006:**

- (f) "Small and Medium Sized Company" (SMC) means, a company-
- (i) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;
  - (ii) which is not a bank, financial institution or an insurance company;
  - (iii) whose turnover (excluding other income) does not exceed rupees fifty crore in the immediately preceding accounting year;
  - (iv) which does not have borrowings (including public deposits) in excess of rupees ten crore at any time during the immediately preceding accounting year; and
  - (v) which is not a holding or subsidiary company of a company which is not a small and medium-sized company.

**Explanation:** For the purposes of clause (f), a company shall qualify as a Small and Medium Sized Company, if the conditions mentioned therein are satisfied as at the end of the relevant accounting period.

### **Non-SMCs**

Companies not falling within the definition of SMC are considered as Non-SMCs.



## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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### Instructions

#### A. *General Instructions*

1. SMCs shall follow the following instructions while complying with Accounting Standards under these Rules:-
  - 1.1 the SMC which does not disclose certain information pursuant to the exemptions or relaxations given to it shall disclose (by way of a note to its financial statements) the fact that it is an SMC and has complied with the Accounting Standards insofar as they are applicable to an SMC on the following lines:  

“The Company is a Small and Medium Sized Company (SMC) as defined in the General Instructions in respect of Accounting Standards notified under the Companies Act, 1956. Accordingly, the Company has complied with the Accounting Standards as applicable to a Small and Medium Sized Company.”
  - 1.2 Where a company, being an SMC, has qualified for any exemption or relaxation previously but no longer qualifies for the relevant exemption or relaxation in the current accounting period, the relevant standards or requirements become applicable from the current period and the figures for the corresponding period of the previous accounting period need not be revised merely by reason of its having ceased to be an SMC. The fact that the company was an SMC in the previous period and it had availed of the exemptions or relaxations available to SMCs shall be disclosed in the notes to the financial statements.
  - 1.3 If an SMC opts not to avail of the exemptions or relaxations available to an SMC in respect of any but not all of the Accounting Standards, it shall disclose the standard(s) in respect of which it has availed the exemption or relaxation.
  - 1.4 If an SMC desires to disclose the information not required to be disclosed pursuant to the exemptions or relaxations available to the SMCs, it shall disclose that information in compliance with the relevant accounting standard.
  - 1.5 The SMC may opt for availing certain exemptions or relaxations from compliance with the requirements prescribed in an Accounting Standard:

## **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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Provided that such a partial exemption or relaxation and disclosure shall not be permitted to mislead any person or public.

### ***B. Other Instructions***

Rule 5 of the Companies (Accounting Standards) Rules, 2006, provides as below:

"5. An existing company, which was previously not a Small and Medium Sized Company (SMC) and subsequently becomes an SMC, shall not be qualified for exemption or relaxation in respect of Accounting Standards available to an SMC until the company remains an SMC for two consecutive accounting periods."

## **II Applicability of Accounting Standards to Companies**

### **(I) Accounting Standards applicable to all companies in their entirety for accounting periods commencing on or after 7<sup>th</sup> December, 2006**

- AS 1 Disclosures of Accounting Policies
- AS 2 Valuation of Inventories
- AS 4 Contingencies and Events Occurring After the Balance Sheet Date
- AS 5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
- AS 6 Depreciation Accounting
- AS 7 Construction Contracts (revised 2002)
- AS 9 Revenue Recognition
- AS 10 Accounting for Fixed Assets
- AS 11 The Effects of Changes in Foreign Exchange Rates (revised 2003)
- AS 12 Accounting for Government Grants
- AS 13 Accounting for Investments
- AS 14 Accounting for Amalgamations
- AS 16 Borrowing Costs
- AS 18 Related Party Disclosures
- AS 22 Accounting for Taxes on Income

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**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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AS 24 Discontinuing Operations

AS 26 Intangible Assets

**(II) Exemptions or Relaxations for SMCs as defined in the Notification**

*(A) Accounting Standards not applicable to SMCs in their entirety:*

AS 3 Cash Flow Statements.

AS 17 Segment Reporting

*(B) Accounting Standards not applicable to SMCs since the relevant Regulations require compliance with them only by certain Non-SMCs<sup>3</sup>:*

(i) AS 21, Consolidated Financial Statements

(ii) AS 23, Accounting for Investments in Associates in Consolidated Financial Statements

(iii) AS 27, Financial Reporting of Interests in Joint Ventures (to the extent of requirements relating to Consolidated Financial Statements)

*(C) Accounting Standards in respect of which relaxations from certain requirements have been given to SMCs:*

(i) Accounting Standard (AS)15, Employee Benefits (revised 2005)

(a) paragraphs 11 to 16 of the standard to the extent they deal with recognition and measurement of short-term accumulating compensated absences which are non-vesting (i.e., short-term accumulating compensated absences in respect of which employees are not entitled to cash payment for unused entitlement on leaving);

(b) paragraphs 46 and 139 of the Standard which deal with discounting of amounts that fall due

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<sup>3</sup> AS 21, AS 23 and AS 27 (relating to consolidated financial statements) are required to be complied with by a company if the company, pursuant to the requirements of a statute/regulator or voluntarily, prepares and presents consolidated financial statements.

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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- more than 12 months after the balance sheet date;
  - (c) recognition and measurement principles laid down in paragraphs 50 to 116 and presentation and disclosure requirements laid down in paragraphs 117 to 123 of the Standard in respect of accounting for defined benefit plans. However, such companies should actuarially determine and provide for the accrued liability in respect of defined benefit plans by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard. Such companies should disclose actuarial assumptions as per paragraph 120(l) of the Standard; and
  - (d) recognition and measurement principles laid down in paragraphs 129 to 131 of the Standard in respect of accounting for other long-term employee benefits. However, such companies should actuarially determine and provide for the accrued liability in respect of other long-term employee benefits by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard.
- (ii) AS 19, Leases
- Paragraphs 22 (c),(e) and (f); 25 (a), (b) and (e); 37 (a) and (f); and 46 (b) and (d) relating to disclosures are not applicable to SMCs.
- (iii) AS 20, Earnings Per Share
- Disclosure of diluted earnings per share (both including and excluding extraordinary items) is exempted for SMCs.

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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(iv) AS 28, Impairment of Assets

SMCs are allowed to measure the 'value in use' on the basis of reasonable estimate thereof instead of computing the value in use by present value technique. Consequently, if an SMC chooses to measure the 'value in use' by not using the present value technique, the relevant provisions of AS 28, such as discount rate etc., would not be applicable to such an SMC. Further, such an SMC need not disclose the information required by paragraph 121(g) of the Standard.

(v) AS 29, Provisions, Contingent Liabilities and Contingent Assets

Paragraphs 66 and 67 relating to disclosures are not applicable to SMCs.

*(D) AS 25, Interim Financial Reporting, does not require a company to present interim financial report. It is applicable only if a company is required or elects to prepare and present an interim financial report. Only certain Non-SMCs are required by the concerned regulators to present interim financial results, e.g, quarterly financial results required by the SEBI. Therefore, the recognition and measurement requirements contained in this Standard are applicable to those Non-SMCs for preparation of interim financial results.*

### III. Applicability of Accounting Standards to Non-corporate Entities (As on 1.4.2008)

(I) Accounting Standards applicable to all Non-corporate Entities in their entirety (Level I, Level II and Level III)

AS 1 Disclosures of Accounting Policies

AS 2 Valuation of Inventories

AS 4 Contingencies and Events Occurring After the Balance Sheet Date

AS 5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies

AS 6 Depreciation Accounting

AS 7 Construction Contracts (revised 2002)

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- AS 9 Revenue Recognition
- AS 10 Accounting for Fixed Assets
- AS 11 The Effects of Changes in Foreign Exchange Rates (revised 2003)
- AS 12 Accounting for Government Grants
- AS 13 Accounting for Investments
- AS 14 Accounting for Amalgamations
- AS 16 Borrowing Costs
- AS 22 Accounting for Taxes on Income
- AS 26 Intangible Assets
- (II) **Exemptions or Relaxations for Non-corporate Entities falling in Level II and Level III (SMEs)**
  - (A) *Accounting Standards not applicable to Non-corporate Entities falling in Level II in their entirety:*
    - AS 3 Cash Flow Statements
    - AS 17 Segment Reporting
  - (B) *Accounting Standards not applicable to Non-corporate Entities falling in Level III in their entirety:*
    - AS 3 Cash Flow Statements
    - AS 17 Segment Reporting
    - AS 18 Related Party Disclosures
    - AS 24 Discontinuing Operations
  - (C) *Accounting Standards not applicable to all Non-corporate Entities since the relevant Regulators require compliance with them only by certain Level I entities:<sup>4</sup>*
    - (i) AS 21, Consolidated Financial Statements

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<sup>4</sup> AS 21, AS 23 and AS 27 (to the extent these standards relate to preparation of consolidated financial statements) are required to be complied with by a non-corporate entity if the non-corporate entity, pursuant to the requirements of a statute/regulator or voluntarily, prepares and presents consolidated financial statements.

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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- (ii) AS 23, Accounting for Investments in Associates in Consolidated Financial Statements
  - (iii) AS 27, Financial Reporting of Interests in Joint Ventures (to the extent of requirements relating to Consolidated Financial Statements)
- (D) *Accounting Standards in respect of which relaxations from certain requirements have been given to Non-corporate Entities falling in Level II and Level III (SMEs):*
- (i) Accounting Standard (AS) 15, Employee Benefits (revised 2005)
- (1) Level II and Level III Non-corporate entities whose average number of persons employed during the year is 50 or more are exempted from the applicability of the following paragraphs:
- (a) paragraphs 11 to 16 of the standard to the extent they deal with recognition and measurement of short-term accumulating compensated absences which are non-vesting (i.e., short-term accumulating compensated absences in respect of which employees are not entitled to cash payment for unused entitlement on leaving);
  - (b) paragraphs 46 and 139 of the Standard which deal with discounting of amounts that fall due more than 12 months after the balance sheet date;
  - (c) recognition and measurement principles laid down in paragraphs 50 to 116 and presentation and disclosure requirements laid down in paragraphs 117 to 123 of the Standard in respect of accounting for defined benefit plans. However, such entities should actuarially determine and provide for the accrued liability in respect of defined benefit plans by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard. Such entities should disclose actuarial assumptions as per paragraph 120(l) of the Standard; and
  - (d) recognition and measurement principles laid down in paragraphs 129 to 131 of the Standard in respect of accounting for other long-term employee benefits.

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However, such entities should actuarially determine and provide for the accrued liability in respect of other long-term employee benefits by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard.

- (2) Level II and Level III Non-corporate entities whose average number of persons employed during the year is less than 50 are exempted from the applicability of the following paragraphs:
  - (a) paragraphs 11 to 16 of the standard to the extent they deal with recognition and measurement of short-term accumulating compensated absences which are non-vesting (i.e., short-term accumulating compensated absences in respect of which employees are not entitled to cash payment for unused entitlement on leaving);
  - (b) paragraphs 46 and 139 of the Standard which deal with discounting of amounts that fall due more than 12 months after the balance sheet date;
  - (c) recognition and measurement principles laid down in paragraphs 50 to 116 and presentation and disclosure requirements laid down in paragraphs 117 to 123 of the Standard in respect of accounting for defined benefit plans. However, such entities may calculate and account for the accrued liability under the defined benefit plans by reference to some other rational method, e.g., a method based on the assumption that such benefits are payable to all employees at the end of the accounting year; and
  - (d) recognition and measurement principles laid down in paragraphs 129 to 131 of the Standard in respect of accounting for other long-term employee benefits. Such entities may calculate and account for the accrued liability under the other long-term employee benefits by reference to some other rational method, e.g., a method based on the assumption that such benefits are payable to all employees at the end of the accounting year.



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- (ii) AS 19, Leases  

Paragraphs 22 (c),(e) and (f); 25 (a), (b) and (e); 37 (a) and (f); and 46 (b) and (d) relating to disclosures are not applicable to non-corporate entities falling in Level II .

Paragraphs 22 (c),(e) and (f); 25 (a), (b) and (e); 37 (a), (f) and (g); and 46 (b), (d) and (e) relating to disclosures are not applicable to Level III entities.
- (iii) AS 20, Earnings Per Share  

Diluted earnings per share (both including and excluding extraordinary items) is not required to be disclosed by non-corporate entities falling in Level II and Level III and information required by paragraph 48(ii) of AS 20 is not required to be disclosed by Level III entities if this standard is applicable to these entities.
- (iv) AS 28, Impairment of Assets  

Non-corporate entities falling in Level II and Level III are allowed to measure the 'value in use' on the basis of reasonable estimate thereof instead of computing the value in use by present value technique. Consequently, if a non-corporate entity falling in Level II or Level III chooses to measure the 'value in use' by not using the present value technique, the relevant provisions of AS 28, such as discount rate etc., would not be applicable to such an entity. Further, such an entity need not disclose the information required by paragraph 121(g) of the Standard.
- (v) AS 29, Provisions, Contingent Liabilities and Contingent Assets  

Paragraphs 66 and 67 relating to disclosures are not applicable to non-corporate entities falling in Level II and Level III.
- (E) *AS 25, Interim Financial Reporting, does not require a non-corporate entity to present interim financial report. It is applicable only if a non-corporate entity is required or elects to prepare and present an interim financial report. Only certain Level I non-corporate entities are required by the concerned regulators to present interim financial results, e.g., quarterly financial results required by the SEBI. Therefore, the recognition and measurement requirements contained in this Standard are applicable to those Level I non-corporate entities for preparation of interim financial results.*

## APPENDIX IX

### *[PARA 11.11]*

#### **APPLICABILITY OF SA 700, FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS, TO FORMATS OF AUDITOR'S REPORTS PRESCRIBED UNDER VARIOUS LAWS AND/ OR REGULATIONS (22.08.2013)**

1. The Council of ICAI, at its 326th meeting held from 27th to 29th July 2013 considered the issue relating to application of Standard on Auditing (SA) 700, Forming An Opinion And Reporting on Financial Statements to such cases where the format of the auditor's report is prescribed under the relevant law or the regulation thereunder and are per se not in line with the requirements of SA 700. 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. Similarly, many a times, even where the auditor's report were to be submitted in a physical form and not filed online, the concerned regulatory/ government agencies may not accept such audit reports which contained any changes made by the auditors to the prescribed formats to bring them in line with SA 700.

2. In view of the above, the Council decided that while the matter was being taken up by the Institute with the relevant regulatory authorities/ Government agencies, etc., to change the prescribed formats for bringing the same in line with the requirements of SA 700, the members may, in the situations described in paragraph 1 above, submit the auditor's report in the format/s prescribed under the relevant law or regulation until announcement of necessary change is made by the appropriate authority. In such cases the members would not be viewed as having not complied with the provisions of SA 700.

3. In this context, it may also be noted that paragraph A55 of the SA 200, Overall Objectives of the Independent Auditor and the Conduct of An Audit in Accordance With Standards on Auditing clearly states as follows:

"A55. In performing an audit, the auditor may be required to comply with legal or regulatory requirements in addition to the SAs. The SAs do not override laws and regulations that govern an audit of financial statements....."

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**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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4. Further, paragraph 43 of SA 700 requires that if the auditor is required by any law or regulation to use a specific layout or wording of the auditor's report, the auditor shall refer to Standards on Auditing only if the auditor's report includes, at minimum, each of the elements as prescribed in the said paragraph.

5. 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. In the background of the difficulties mentioned in paragraph 1 above, it may also not be possible for the auditors to suitably modify the prescribed format. 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 Institute of Chartered Accountants of India.

The same can also be downloaded from the link below:

[http://www.icai.org/new\\_post.html?post\\_id=9835](http://www.icai.org/new_post.html?post_id=9835)

## APPENDIX X

[*PARA 13.13*]

Circular No.561, dated 22nd May, 1990

**Subject: Tax audit under section 44AB of the Income-tax Act, 1961, in the case of companies having accounting year other than financial year - Regarding**

1. The Board have received representations regarding difficulties faced in complying with the provisions of section 44AB of the Income-tax Act, 1961, in the case of companies which follow an accounting period other than financial year.
2. Section 3 of the Income-tax Act, *inter alia*, provides that with effect from 1st April, 1989, "previous year" for the purposes of that Act means financial year immediately preceding the assessment year. In spite of the introduction of a uniform previous year for purposes of income-tax, some companies may adopt an accounting period other than the financial year, say the calendar year, under the Companies Act for other purposes.
3. In such cases, a question has arisen as to whether, under section 44AB of the Income-tax Act, the tax auditor can audit and certify the accounts for the period for which accounts have been maintained under the Companies Act (i.e., in this case the calendar year) or whether the tax auditor will have to certify the accounts for the relevant financial year which is the uniform accounting year for tax purposes.
4. The Board have considered the matter and are of opinion that as the income of the previous year is chargeable to tax and, for the purposes of Income-tax Act, the previous year is the financial year, the tax auditor would have to carry out the audit under section 44AB in respect of the period covered by the previous year, i.e., the relevant financial year. The proviso to the aforesaid section 44AB, therefore, covers only the cases where the accounts are audited under any other law in respect of the financial year. Where the accounting year is different from the financial year, the proviso to section 44AB will not apply. Consequently, the tax auditors would have to carry out the tax audit in respect of the period covered by the relevant financial year and submit his report in Form 3CB as required in rule 6G(1)(b) of the Income-tax Rules.

Sd/-

Nishi Nair

Under Secretary to the Government of India.

[F.No.205/4/90-ITA-II]

## APPENDIX XI

*[PARA 18.1, 32.7]*

### Circular No.739 dated 25-3-1996

**Whether for assessment years subsequent to assessment year 1996-97, no deduction under section 40(b)(v) will be admissible unless partnership deed either specifies amount of remuneration payable to each individual working partner or lays down manner of quantifying such remuneration**

1. The Board have received representations seeking clarification regarding disallowance of remuneration paid to the working partners as provided under section 40(b)(v) of the Income-tax Act. In particular, the representations have referred to two types of clauses which are generally incorporated in the partnership deeds.

These are:

- (i) The partners have agreed that the remuneration to a working partner will be the amount of remuneration allowable under the provisions of section 40(b)(v) of the Income-tax Act; and
- (ii) The amount of remuneration to working partner will be as may be mutually agreed upon between partners at the end of the year.

It has been represented that the Assessing Officers are not allowing deduction on the basis of these and similar clauses in the course of scrutiny assessments for the reason that they neither specify the amount of remuneration to each individual nor lay down the manner of quantifying such remuneration.

2. The Board have considered the representations. Since the amended provisions of section 40(b) have been introduced only with effect from the assessment year 1993-94 and these may not have been understood correctly, the Board are of the view that a liberal approach may be taken for the initial years. It has been decided that for the assessment years 1993-94 to 1996-97 deduction for remuneration to a working partner may be allowed on the basis of the clauses of the type mentioned at 1(i) above.

3. In cases where neither the amount has been quantified nor even the limit of total remuneration has been specified but the same has been left to be determined by the partners at the end of the accounting period, in such cases payment of remuneration to partners cannot be allowed as deduction in the computation of firm's income.

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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4. It is clarified that for the assessment years subsequent to the assessment year 1996-97, no deduction under section 40(b)(v) will be admissible unless the partnership deed either specifies the amount of remuneration payable to each individual working partner or lays down the manner of quantifying such remuneration.

## APPENDIX XII

*[PARA 39.11]*

### THE RELEVANT EXTRACTS OF THE MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT ACT, 2006

"Appointed day" means the day following immediately after the expiry of the period of fifteen days from the day of acceptance or the day of deemed acceptance of any goods or any services by a buyer from a supplier.

"Day of acceptance" means the day of actual delivery of the goods or the rendering of service or where any objection is made in writing by the buyer regarding the acceptance of goods or services within 15 days from the day of delivery of goods or rendering of services, the day on which the objection is removed by the supplier.

"Day of deemed acceptance" means , where no objection is made in writing by the buyer regarding acceptance of goods or services within fifteen days from the day of deliver of the goods or rendering of services, the day of the actual delivery of goods or the rendering of services.

"Buyer" means who so ever buys any goods or receives any services from the supplier for a consideration.

"Supplier" means a micro or small enterprise, which has filed a memorandum with the authority referred to in section 7(1)(a).

"Micro Enterprise" means:

- (a) In case of enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the first schedule to the Industries(Development and Regulation) Act, 1951 an enterprise, where the investment in plant and machinery does not exceed twenty five lakh rupees;
- (b) In case of enterprises engaged in providing or rendering services, an enterprise, where the investment in equipment does not exceed ten lakh rupees.

"Small enterprise" means:

- (a) In case of enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the first schedule to the Industries (Development and Regulation) Act, 1951 an enterprise,

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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where the investment in plant and machinery is more than twenty five lakh rupees but does not exceed five crore rupees;

- (b) In case of enterprises engaged in providing or rendering services, an enterprise, where the investment in equipment is more than ten lakh rupees but does not exceed two crore rupees.

"Medium enterprise" means

- (a) In case of enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the first schedule to the Industries (Development and Regulation) Act, 1951 an enterprise, where the investment in plant and machinery is more than five crore rupees but does not exceed ten crore rupees;
- (b) In case of enterprises engaged in providing or rendering services, an enterprise, where the investment in equipment is more than two crore rupees but does not exceed five crore rupees.



## Appendix XIII

[Para 40.1]

Chart of persons specified in Section 40A(2)(b)- (Refer Paragraph 40.1)

### Part-I

Individual	Firm	Association of persons	HUF	Company
<i>His relatives</i>	<i>Its partners</i>	<i>Its members</i>	<i>Its members</i>	<i>Its directors</i>
	Their relatives	Their relatives	Their relatives	Their relatives

### Part-II

<i>Where person having substantial interest in the business or profession of the assessee is</i>			
Individual	Association of persons	HUF	Company
His relatives	Its members	Its members	Its directors
	Their relatives	Their relatives	Their relatives
			any other company carrying on business or profession in which the first mentioned company has substantial interest

**Note:** Where one or more of the persons falling in any of the above categories (i.e. individual and his relatives, firm, its partners and their relatives, etc.) have substantial interest in the business or profession carried on by any person – that person is also covered under section 40A(2)(b).

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**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**


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**PART III**

<b>Director</b>	<b>Partner</b>	<b>Member of AOP</b>	<b>Member of HUF</b>
Companies in which he is a Director	Firms in which he is a partner	AOP of which he is a member	
All other Directors of such Companies	All other partners of such firms	All other members of such AOP	All other members of such HUF
Their relatives	Their relatives	Their relatives	Their relatives

**Notes:**

1. Relative is defined in section 2(41) as in relation to an individual including husband, wife, brother, sister or any lineal ascendant or descendent of that individual.
2. "Person having a substantial interest" is explained in section 40A as under:
  - i. In the case of company - the person concerned is, at any time, during the previous year the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) carrying not less than 20% of the voting power.
  - ii. In other cases - such person is at any time during the previous year, beneficially entitled to not less than 20% of the profits of such business or profession.

## APPENDIX XIV

*[PARA 48.1]*

Circular No. 208, dated 15th November, 1976

F.No. 208/7/76-ITA-II

### Section 69D of the Income-tax Act, 1961 - Clarification Regarding

**Whether payment on or after April 1, 1977 of amount borrowed on hundi is to comply with the section regardless of whether hundi was executed prior to the said date or on or after that date**

1. The Taxation Laws (Amendment) Act, 1975, has added a new section 69D in Income-tax Act, 1961, with effect from 1st April, 1977, which provides that if any amount is borrowed from any person on a hundi or any amount due on it is repaid to any person, otherwise than through an account-payee cheque drawn on a bank, the amount so borrowed or repaid shall be assessed as the income of the tax-payer borrowing or repaying the said amount, for the previous year in which the amount is borrowed or repaid. This will also apply to the amount of interest paid on the amount borrowed on hundies. This provision is applicable only in respect of hundies and does not cover other types of loans, such as, repayment of loan by employees to employers, repayment of loan to banks, co-operative societies etc.

2. The term "hundi" has not been defined in the Income-tax Act, 1961. In common commercial parlance, it denotes an indigenous instrument in vernacular language which can be used by the holder thereof to collect money due thereon without using the medium of currency. It may also be regarded as an indigenous form of a bill of exchange expressed in vernacular language which has been in use in the mercantile community in India for the purpose of collecting dues. There are numerous varieties of hundies, for example Darshani Hundi, Muddati Hundi, Shaha Jogi Hundi, Jokhmi Hundi, Nam Jog Hundi, Dhani Jog Hundi, Jawabi Hundi and Zickri chit. The characteristics of hundies differ according to the varieties of the same. The following characteristics are found in most of the hundies:

1. A hundi is payable to a specified person or order or negotiable without endorsement by the payee.
2. A holder is entitled to sue on a hundi without an endorsement in his favour.

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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3. A hundi accepted by the drawee could be negotiated without endorsement.
4. If a hundi is lost, the owner could claim a duplicate or triplicate from the drawer and present it to the drawee for payment. Interest can be charged where usage is established.
3. This provision will come into force with effect from 1st April, 1977. Accordingly, any payment on or after 1st April, 1977, in respect of an amount borrowed on a hundi will have to comply with the requirements of this provision regardless of whether the hundi was executed prior to the said date or on or after that date.

**Circular No. 221, dated 6-6-1977**

**[F. No. 208/25/76-IT(A-II)],**

#### **Whether provisions of the section are applicable to darshani hundi transactions**

1. Reference is invited to Board's Circular No. 208 [F. No. 208/7/76-IT(A-II)], dated 15-11-1976 [printed at Sl. No. 478] in which the provisions of section 69D were explained.
2. A "hundi" in common commercial parlance denotes an indigenous form of bill of exchange, by and large in vernacular language, which is being used by the mercantile community in India. The hundis can be broadly classified as (i) darshani hundis (sight or demand hundis), and (ii) muddati hundis (usance hundis payable after a stipulated period of time mentioned therein). Darshani hundis are of different varieties, viz, (i) shahjog hundis, (ii) dhanijog hundis, (iii) namjog hundis, (iv) dekharanarjog hundis, (v) farmanijog hundis, and (vi) jokhmi hundis.
3. It has been represented to the Board that a darshani hundi created solely for the purpose of remittances of funds or financing inland trade or for operating accounts through indigenous banking channels does not involve borrowing of amounts and as such does not fall within the scope of section 69D. There are more than two parties in a darshani hundi. Normally four parties are involved in the case of a darshani hundi, viz, (i) the rakhya (the holder or purchaser), (ii) the drawer (an indigenous banker or a vyapari), (iii) the drawee (normally an indigenous banker but can also be a vyapari), and (iv) the payee. If the payee is also the rakhya, the parties will be three. Darshani hundi is payable at sight, i.e., immediately on presentation. A muddati (usance) hundi generally involving two parties, is payable after a stipulated period of time mentioned in the hundi.

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

4. The matter has been considered by the Board. We have been advised that *the provisions of section 69D are not applicable to darshani hundi transactions mentioned hereinafter :*

- 1.(a) A, who is the rakhya obtains on payment from B, the drawer, a hundi drawn on C, the drawee, in favour of D, the payee.
- (b) A, the rakhya having a running account or an overdraft account with B, obtains from him a hundi drawn on C, the drawee, in favour of D, the payee.
- 2.(a) A, a purchaser of goods from B, draws a hundi on C, the drawee, in favour of B or a third party D for the purpose of payment of the price of goods purchased or for settling the account.
- (b) For such purposes B can also draw a hundi on A either in his own favour or in favour of a third party D.
3. A has an account with an indigenous banker C, who has granted a credit facility to A and handed over a hundi book to him. A draws amounts through such hundis payable either to self, or bearer or third party. Such an arrangement arises out of the credit facility already granted and, therefore, no debtor creditor relationship has arisen between the parties because of the drawal of a hundi.

5. Normally, borrowal on hundi arises when a person gets money by execution of a hundi but in the instances cited above the hundi is given in the nature of a security and there is no borrowal on such hundis. Thus in cases of transactions referred to at (1), (2) and (3) of para 4, section 69D is not applicable. The settlement of account between any of the parties to such a darshani hundi can, thus, be otherwise than through an account payee cheque within the meaning of section 69D.

6. This circular covers darshani hundi transactions of the types referred to at (1), (2) and (3) of para 4 above. However, it could not be said that there could be no borrowal on darshani hundi. The transactions not of the type referred to above, on darshani hundis have to be examined with reference to the facts and circumstances of such cases so as to determine whether or not there is a borrowal on such hundis.

## APPENDIX XV

### [PARA 13.9 & 71.3]

#### RECOMMENDED FORM OF FINANCIAL STATEMENTS FOR NON-CORPORATE ENTITIES

#### FORM OF BALANCE SHEET (FOR NON CORPORATE MANUFACTURING ENTITIES)

NAME OF ENTITY

BALANCE SHEET AS AT

<i>Figure s for Previo us year</i>	<i>Capital and Liabilities</i>	<i>Figur es for Curre nt year</i>	<i>Figure s for Previo us year</i>	<i>Properties and Assets</i>	<i>Figur es for Curre nt year</i>
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#### I. CAPITAL

(In case of partnership, these particulars to be given separately for each partner and if possible the fixed capital accounts may be segregated from the current accounts) as at the beginning of the year.

Add/Deduct Net Profit/Net Loss during the year

Interest on capital

Drawings

Any other items (give details)

#### II. RESERVES

(Give details under

#### I. FIXED ASSETS

1. Under each head the original cost, the additions thereto, the deductions therefrom during the year and the total depreciation written off or provided upto the end of the year to be stated.

2. Where the assets have been revalued, the revalued figures to be shown. Each balance sheet for the first five years subsequent to the date of revaluation to state the amount of revaluation.

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

each head)

1. Capital reserves (if any)

2. Other Reserves (including restrained profits to the extent not already added to the capital, give details)

3. Sinking Funds (if any)

### III. LOANS AND BORROWINGS

1. Interest accrued and due on each category to be shown separately.

2. In the case of secured loans the nature of security to be specified.

3. Amounts due for repayments within one year from the balance sheet date to be shown separately.

4. Loan from partners, relatives of the proprietors or partners to be shown separately,

### A. CURRENT LIABILITIES

1. Sundry creditors for goods supplied

2. Sundry creditors (Others)

3. Advances /

3. Distinguishing as far as possible between expenditure upon:

a) Goodwill

b) Land

c) Buildings

d) Leaseholds

e) Railway sidings

f) Plant and Machinery

g) Furniture & Fittings

h) Development of property

i) Patents, Trademarks and designs

j) Livestock

k) Vehicles etc.

1. Cost

2. Less: depreciation

### II. ADVANCES AND DEPOSITS ON CAPITAL ACCOUNT

### III. INVESTMENTS

(attach details of investment showing in each

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Progress Payments from customers /deposits from dealers, selling agents etc.

4. Interest and other charges accrued but not due for payment.

5. Bills Payable

6. Statutory liabilities (Overdue amounts to be shown separately)

7. Other current liabilities and provisions (Major items to be shown separately).

### B. PROVISIONS :

1. For taxation

*Less* advance tax paid

2. For Provident Fund

3. For Contingencies

4. Other provisions.

(A foot note to the balance sheet may be added to show separately)

1. Claims against the entity not acknowledged as debts.

2. Uncalled liability on shares partly paid

3. Estimated amount of contracts remaining to be executed to capital account and

case nature of investment and mode of valuation e.g. cost or market value)

1. Investment in shares, debentures or bonds (Note: Investments in concern wherein proprietor, partner or their relative are interested to be shown separately)

2. Immovable properties

3. Investments in the capital of partnership firms

4. Other investments.

### IV. LOANS

1. The nature of security (if any) and amount of each type of loan to be specified.

2. Amounts due within one year to be shown separately.

3. Loans to proprietors, partners or associated concern (to be shown separately)

4. Loans considered bad or doubtful to



## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

not provided for

4. Contingent liability for bills discounted.

5. Other money for which the entity is contingently liable (give details)

6. Aggregate amount of arrears of depreciation, if any.

be shown separately.

*Less:* provision for bad and Doubtful loans.

### **V. CURRENT ASSETS A-INVENTORIES)**

(The mode of valuation to be shown separately)

1. Raw materials (including stores and other items used in the process of manufacture)

2. Work in process.

3. Finished goods.

4. Consumable stores and spare parts.

5. Loose Tools.

6. Others

### **B. RECEIVABLES**

1. Debts due and outstanding for a period exceeding six months (to be shown separately).

2. Instalments of deferred receivables due within one year to be shown separately.

3. Debts considered bad or doubtful to be shown

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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separately.

4. Amount due from proprietors, partners or associated concerns to be shown separately.

i) On account of sales on deferred payments basis.

ii) On account of exports

iii) Others

iv) Total receivables

v) *Less:* provision for bad and doubtful debts.

### **C. BILLS OF EXCHANGE**

(Same information to be given as for 'Receivables')

### **D. ADVANCE ON CURRENT ACCOUNT**

(Same information to be given as for loans).

1. Advance to suppliers of merchandise supplies and sundries etc. and stores /spares/consumables.

2. Advance payment of taxes (in excess

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

	of tax payable)
	3. Pre-paid expenses.
	4. Others
	<b>E. CASH AND BANK BALANCES</b>
	1. Fixed deposit account
	2. Current and savings account
	3. Cash on hand
	<b>VI. MISCELLANEOUS EXPENDITURE</b>
	To the extent not written off or adjusted (specify the nature and amount of each item).
	<b>VII. ACCUMULATED</b>
	<i>Losses:</i> if any
	i) before depreciation
	ii) depreciation.
<b>TOTAL RUPEES</b>	<b>TOTAL RUPEES</b>

**Notes on Balance Sheet**

1. In case of partnership firms, state whether it is registered with registrar of firms, registration number, date of registration and the State in which it is registered.
2. Unless otherwise indicated, the terms used herein have the same meaning as they have in Schedule VI to the Companies Act, 1956.

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

**PRO FORMA OF PROFIT AND LOSS ACCOUNT  
FOR A NON-CORPORATE MANUFACTURING ENTITY**

Name of the entity \_\_\_\_\_

Profit and Loss Account for the year ending \_\_\_\_\_ (000's  
omitted)

	Previous Year (actuals)	This Year
1. Sales		
(Income from services may be shown separately)		
2. Less: Excise Duty		
3. Net Sales		
(Item No.1 minus Item No.2)		
4. Add/Deduct/Increase /Decrease in Finished Goods Closing Stock Less: Opening Stock		
5. Cost of Production		
(a) Rawmaterial consumption.		
Add: Purchases		
Less: Closing Stock		
(b) Stores and spare consumption		
(c) Salaries and wages		
(d) Other manufacturing expenses, excluding depreciation		
Sub-total		
Add: Opening stocks-in-process		
Deduct: Closing stock-in-process		
Cost of production		
Gross profit/loss (Item No.3 minus Item No.4)		

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

6. Sales and administrative expenses
7. Interest and other overheads
8. Other income/expenses Net (+)
9. Profit /loss before depreciation and tax  
(Item No.5 minus item No.(6 + 7))
10. Depreciation
11. Profit after depreciation
12. Taxation
13. Profit after tax

**Note:**

1. Any item of expenditure which forms a significant proportion, say 5% or more of the total sales or has special significance otherwise, should be shown separately under appropriate heads for example (i) salary (ii) commission (iii) perquisites and money value thereof.
2. If audited accounts for the previous year are not available, the fact should be stated.

## APPENDIX XVI

### [PARA 13.9 & 71.3]

#### RECOMMENDED FORM OF FINANCIAL STATEMENTS FOR NON-CORPORATE TRADING ENTITIES

NAME OF ENTITY

#### BALANCE SHEET AS AT

<i>Figure s for Previo us year</i>	<i>Capital and Liabilities</i>	<i>Figur es for Curre nt year</i>	<i>Figure s for Previo us year</i>	<i>Properties and Assets</i>	<i>Figur es for Curre nt year</i>
	<b>I. CAPITAL</b>			<b>I. FIXED ASSETS</b>	
	(In case of partnership, these particulars to be given separately for each partner and if possible the fixed capital accounts may be segregated from the current accounts) as at the beginning of the year.			1. Under each head the original cost, the additions thereto, the deductions therefrom during the year and the total depreciation written off or provided upto the end of the year to be stated.	
	Add/Deduct Net Profit/Net Loss during the year			2. Where the assets have been revalued, the revalued figures to be shown. Each balance sheet for the first five years subsequent to the date of revaluation to state the amount of revaluation.	
	Interest on capital				
	Drawings				
	Any other items (give details)				
	<b>II. RESERVES</b>				
	(Give details under each head)				
	1. Capital reserves (if				

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

any)

2. Other Reserves (including restrained profits to the extent not already added to the capital, give details)

3. Sinking Funds (if any)

### III. LOANS AND BORROWINGS

1. Interest accrued and due on each category to be shown separately.

2. In the case of secured loans the nature of security to be specified.

3. Amounts due for repayments within one year from the balance sheet date to be shown separately.

4. Loan from partners, relatives of the proprietors or partners to be shown separately,

a) Loans from financial institutions.

b) Loans and borrowings from banks (Specify the name of the bank, the relevant amount and the nature of the borrowing e.g. cash credit, term-

3. Distinguishing as far as possible between expenditure upon:

a) Goodwill

b) Land

c) Buildings

d) Leaseholds

e) Railway sidings

f) Plant and Machinery

g) Furniture & Fittings

h) Development of property

i) Patents, Trademarks and designs

j) Livestock

k) Vehicles etc.

1. Cost

2. Less: depreciation

### II. ADVANCES AND DEPOSITS ON CAPITAL ACCOUNT

### III. INVESTMENTS

(attach details of investment showing in each case nature of investment and

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

loans, overdraft, packing credit etc. (separately)

c) Fixed deposits (from public and others)

d) Other (Give details)

### IV. CURRENT LIABILITIES AND PROVISIONS

(Amounts due for payment beyond one year from the date of the balance sheet (to be shown separately)

#### A. CURRENT LIABILITIES

1. Sundry creditors for goods supplied

2. Sundry creditors (Others)

3. Advances / Progress Payments from customers/ deposits from dealers, selling agents etc.

4. Interest and other charges accrued but not due for payment.

5. Bills Payable

6. Statutory liabilities

(Overdue amounts to be shown separately)

7. Other current liabilities and provisions (Major items to be shown

mode of valuation e.g. cost or market value)

1. Investment in shares, debentures or bonds (Note: Investments in concern wherein proprietor, partner or their relative are interested to be shown separately)

2. Immovable properties

3. Investments in the capital of partnership firms

4. Other investments.

### IV. LOANS

1. The nature, security (if any) and amount of each type of loan to be specified.

2. Amounts due within one year to be shown separately.

3. Loans to proprietors, partners or associated concern (to be shown separately)

4. Loans considered bad or doubtful to be stated



## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

separately).

### **B. PROVISIONS :**

1. For taxation

*Less* advance tax paid

2. For Provident Fund

3. For Contingencies

4. Other provisions.

(A foot note to the balance sheet may be added to show separately)

1. Claims against the entity not acknowledged as debts.

2. Uncalled liability on shares partly paid

3. Estimated amount of contracts remaining to be executed to capital account and not provided for

4. Contingent liability for bills discounted.

5. Other money for which the entity is contingently liable (give details)

6. Aggregate amount of arrears of depreciation, if any.

separately.

*Less:* provision for bad and Doubtful loans.

### **V. CURRENT ASSETS A-INVENTORIES**

(The mode of valuation to be shown separately)

1. Stock in Trade

2. Supplies and sundries (If the trading organization is also involved in any processing activity ties other categories of inventories, e.g., raw material, and work-in-progress, should be separately disclosed.

### **B. RECEIVABLES**

1. Debts due and outstanding for a period exceeding six

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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months (to be shown separately).

2. Instalments of deferred receivables due within one year to be shown separately.

3. Debts considered bad or doubtful to be shown separately.

4. Amount due from proprietors, partners or associated concerns to be shown separately.

i) On account of sales on deferred payments basis.

ii) On account of exports

iii) Others

iv) Total receivables

v) *Less:* provision for bad and doubtful debts.

### **C. BILLS OF EXCHANGE**

(Same information to be given as for 'Receivables')

### **D. ADVANCE ON CURRENT ACCOUNT**

(Same information to be given as for

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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loans).

1. rawmaterials and stores/  
spares/consumable.

2. Advance payment of taxes (in excess of tax payable)

3. Pre-paid expenses.

4. Others

**E. CASH AND BANK BALANCES**

1. Fixed deposit account

2. Current and savings account

3. Cash on hand

**VI. MISCELLANEOUS EXPENDITURE**

To the extent not written off or adjusted (specify the nature and amount of each item).

**VII. ACCUMULATED**

*Losses:* if any

i) before depreciation

ii) depreciation

**TOTAL RUPEES**

**TOTAL RUPEES**

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**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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**Notes on Balance Sheet**

1. In case of partnership firms, state whether it is registered with registrar of firms, registration number, date of registration and the State in which it is registered.
2. Unless otherwise indicated, the terms used herein have the same meaning as they have in Schedule VI to the Companies Act, 1956.

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**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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**PROFORMA OF PROFIT AND LOSS ACCOUNT  
FOR A TRADING ENTITY**

Name of the entity \_\_\_\_\_

Profit and Loss Account for the year ending \_\_\_\_\_

	<i>Last Year</i>	<i>This Year</i>
	<i>Rs.</i>	<i>Rs.</i>
1. Sales (Net of Sales Tax)		
(Income from services may be shown separately)		
2. Cost of goods sold		
a) Opening Stock		
<i>Add:</i> Purchases (Less returns)		
<i>Less:</i> Closing Stock		
b) Other direct expenses (if any)		
3. Gross Profit (1 - 2)		
4. Sales and administrative expenses		
5. Other income/expenses* Net		
6. Interest		
7. Profit before depreciation and tax		
[Item 3 minus item (4 + 5 + 6)]		
8. Depreciation		
9. Taxation (for example for registered firms)**		
10. Profit after depreciation & taxation		
item 7 minus item (8 + 9)		

**Note:**

\* Any item of expenditure which forms a significant proportion, say 5% or more of the total sales or has special significance otherwise, should be shown separately under appropriate heads for example (i) salary (ii) commission (iii) perquisites and money value thereof.

\*\* Registered firms are subject to tax, before the profit is apportioned amongst partners.

## APPENDIX XVII

### FORM NO.3CA

[See rule 6G(1)(a)]

**Audit report under section 44AB of the Income-tax Act, 1961,  
in a case where the accounts of the business or profession of a person  
have been audited under any other law**

\*I / we report that the statutory audit of M/s. \_\_\_\_\_ ( Name  
and address of the assessee with Permanent Account Number) was  
conducted by \*me / us / M/s. \_\_\_\_\_ in  
pursuance of the provisions of the \_\_\_\_\_ Act,  
and \*I/we annex hereto a copy of \*my / our / their audit report dated  
\_\_\_\_\_ along with a copy of each of :-

- (a) the audited \*profit and loss account / income and expenditure  
account for the period beginning from -----to ending  
on -----.
- (b) the audited balance sheet as at, \_\_\_\_\_; and
- (c) documents declared by the said Act to be part of, or annexed to,  
the \*profit and loss account / income and expenditure account  
and balance sheet.

2. The statement of particulars required to be furnished under section  
44AB is annexed herewith in Form No. 3CD.

3. In \*my / our opinion and to the best of \*my / our information and  
according to examination of books of account including other relevant  
documents and explanations given to \*me / us, the particulars given in the  
said Form No.3 CD are true and correct subject to the following  
observations/qualifications, if any:

- a.
- b.
- c.

.....  
\*\*(Signature and stamp/Seal of the signatory)

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Place : \_\_\_\_\_ Name of the signatory .....

Date : \_\_\_\_\_ Full address .....

#### **Notes :**

1. \* Delete whichever is not applicable
2. \*\*This report has to be signed by a person eligible to sign the report as per the provisions of section 44AB of the Income Tax Act, 1961.
3. Where any of the requirements in this Form is answered in the negative or with qualification, give reasons therefore.
4. The person who signs this audit report shall indicate reference of his membership number / certificate of practice / authority under which he is entitled to sign this report.

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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**FORM NO.3CB**

[See rule 6G(1)(b)]

**Audit report under section 44AB of the Income-tax Act, 1961, in the case of a person referred to in clause (b) of sub-rule (1) of rule 6G**

1. \*I / we have examined the balance sheet as on, \_\_\_\_\_, and the \*profit and loss account / income and expenditure account for the period beginning from -----to ending on -----, attached herewith, of \_\_\_\_\_ ( Name ), \_\_\_\_\_ (Address), \_\_\_\_\_ (Permanent Account Number).

2. \*I / we certify that the balance sheet and the \*profit and loss / income and expenditure account are in agreement with the books of account maintained at the head office at \_\_\_\_\_ and \*\* \_\_\_\_\_ branches.

3.(a) \*I / we report the following observations / comments / discrepancies / inconsistencies; if any:

(b) Subject to above, -

(A) \*I / we have obtained all the information and explanations which, to the best of \*my / our knowledge and belief, were necessary for the purpose of the audit.

(B) In \*my / our opinion, proper books of account have been kept by the head office and branches of the assessee so far as appears from \*my / our examination of the books.

(C) In \*my / our opinion and to the best of \*my / our information and according to the explanations given to \*me / us, the said accounts, read with notes thereon, if any, give a true and fair view :-

(i) in the case of the balance sheet, of the state of the affairs of the assessee as at 31st March, ;and

(ii) in the case of the \*profit and loss account / income and expenditure account of the \*profit / loss or \*surplus / deficit of the assessee for the year ended on that date.

4. The statement of particulars required to be furnished under section 44AB is annexed herewith in Form No.3CD.

5. In \*my/our opinion and to the best of \*my / our information and according to explanations given to \*me / us, the particulars given in the said



### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Form No.3 CD are true and correct subject to following observations/qualifications, if any:

- a.
- b.
- c.

.....  
 \*\*\* (Signature and stamp/seal of the signatory)

Place : \_\_\_\_\_ Name of the signatory .....

Date : \_\_\_\_\_ Full address .....

#### **Notes :**

1. \*Delete whichever is not applicable.
2. \*\*Mention the total number of branches.
3. \*\*\*This report has to be signed by person eligible to sign the report as per the provisions of section 44AB of the Income Tax Act, 1961.
4. The person, who signs this audit report, shall indicate reference of his membership number / certificate of practice number / authority under which he is entitled to sign this report.

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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**FORM NO.3CD**

[See rule 6G(2)]

**Statement of particulars required to be furnished under  
section 44AB of the Income-tax Act, 1961**

**PART - A**

1. Name of the assessee : \_\_\_\_\_
2. Address : \_\_\_\_\_
3. Permanent Account Number : \_\_\_\_\_
4. 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  
: \_\_\_\_\_
5. Status : \_\_\_\_\_
6. Previous year : from .....to ....
7. Assessment year : \_\_\_\_\_
8. Indicate the relevant clause  
of section 44AB under which  
the audit has been Conducted  
: \_\_\_\_\_

**PART - B**

- 9.(a) If firm or association of persons, indicate names of partners/members and their profit sharing ratios.
- (b) If there is any change in the partners or members or in their profit sharing ratio since the last date of the preceding year, the particulars of such change
- 10.(a) Nature of business or profession (if more than one business or profession is carried on during the previous year, nature of every business or profession)

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

(b) If there is any change in the nature of business or profession, the particulars of such change.

11.(a) Whether books of account are prescribed under section 44AA, if yes, list of books so prescribed.

(b) List of books of account maintained and the address at which the books of accounts are kept.

(In case books of account are maintained in a computer system, mention the books of account generated by such computer system. If the books of accounts are not kept at one location, please furnish the addresses of locations along with the details of books of accounts maintained at each location.)

(c) List of books of account and nature of relevant documents examined.

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

13.(a) Method of accounting employed in the previous year

(b) Whether there had been any change in the method of accounting employed vis-a-vis the method employed in the immediately preceding previous year.

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

Serial number	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)

(d) Details of deviation, if any, in the method of accounting employed in the previous year from accounting standards prescribed under section 145 and the effect thereof on the profit or loss.

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

(b) In case of deviation from the method of valuation prescribed under section 145A, and the effect thereof on the profit or loss, please furnish:

Serial number	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

15. Give the following particulars of the capital asset converted into stock-in trade: -

- (a) Description of capital asset;
- (b) Date of acquisition;
- (c) Cost of acquisition;
- (d) Amount at which the asset is converted into stock-in-trade.

16. Amounts not credited to the profit and loss account, being, -

- (a) the items falling within the scope of section 28;
- (b) the proforma credits, drawbacks, refund of duty of customs or excise or service tax, or refund of sales tax or value added tax where such credits, drawbacks or refunds are admitted as due by the authorities concerned;
- (c) escalation claims accepted during the previous year;
- (d) any other item of income;
- (e) capital receipt, if any.

17. 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, please furnish:

Details of property	Consideration received or accrued	Value adopted or assessed or assessable

18. Particulars of depreciation allowable as per the Income Tax Act, 1961 in respect of each asset or block of assets, as the case may be, in the following form :-

- (a) Description of asset/block of assets.
- (b) Rate of depreciation.
- (c) Actual cost of written down value, as the case may be.
- (d) Additions/deductions during the year with dates; in the case of any addition of an asset, date put to use; including adjustments on account of –
  - (i) Central Value Added Tax credits claimed and allowed under the Central Excise Rules, 1944, in respect of assets acquired on or after 1st March, 1994,

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

- (ii) change in rate of exchange of currency, and
  - (iii) subsidy or grant or reimbursement, by whatever name called.
  - (e) Depreciation allowable.
  - (f) Written down value at the end of the year
19. 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 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.
32AC		
33AB		
33ABA		
35(1)(i)		
35(1)(ii)		
35(1)(iia)		
35(1)(iii)		
35(1)(iv)		
35(2AA)		
35(2AB)		
35ABB		
35AC		
35AD		
35CCA		
35CCB		
35CCC		
35CCD		
35D		
35DD		
35DDA		
35E		

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

20.(a) Any sum paid to an employee as bonus or commission for services rendered, where such sum was otherwise payable to him as profits or dividend. [Section 36(1)(ii)]

(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 for payment	The actual amount paid	The actual date of payment to the concerned authorities

21.(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	Serial number	Particulars	Amount in Rs.
Capital expenditure			
Personal expenditure			
Advertisement expenditure in any souvenir, brochure, tract, pamphlet or the like published by a political party			
Expenditure incurred at clubs being entrance fees and subscriptions			

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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			

- (b) Amounts inadmissible under section 40(a):-
  - (i) as payment to non-resident referred to in sub-clause (i)
    - (A) Details of payment on which tax is not deducted:
      - (I) date of payment
      - (II) amount of payment
      - (III) nature of payment
      - (IV) name and address of the 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)
      - (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:

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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- (I) date of payment
  - (II) amount of payment
  - (III) nature of payment
  - (IV) name and 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 and address of the payer
  - (V) amount of tax deducted
  - (VI) amount out of (V) deposited, if any
- (iii) under sub-clause (ic) [Wherever applicable]
- (iv) under sub-clause (ia)
- (v) under sub-clause (iib)
- (vi) under sub-clause (iii)
  - (A) date of payment
  - (B) amount of payment
  - (C) name and address of the payee
- (vii) under sub-clause (iv)
- (viii) under sub-clause (v)
- (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:



**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

Serial number	Date of payment	Nature of payment	Amount	Name and Permanent Account Number of the 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 section 40A(3A);

Serial number	Date of payment	Nature of payment	Amount	Name and Permanent Account Number of the payee, if available

- (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).
22. Amount of interest inadmissible under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006.
23. Particulars of payments made to persons specified under section 40A(2)(b).
24. Amounts deemed to be profits and gains under section 32AC or 33AB or 33ABA or 33AC.
25. Any amount of profit chargeable to tax under section 41 and computation thereof.

### **Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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

- (A) pre-existed on the first day of the previous year but was not allowed in the assessment of any preceding 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 date.

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

27.(a) Amount of Central Value Added Tax credits availed of or utilised during the previous year and its treatment in the profit and loss account and treatment of outstanding Central Value Added Tax credits in the accounts.

(b) Particulars of income or expenditure of prior period credited or debited to the profit and loss account.

28. 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.

29. 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.

30. 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]

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 :-

- (i) name, address and Permanent Account Number (if available with the assessee) of the lender or depositor;

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

- (ii) amount of loan or deposit taken or accepted;
- (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 otherwise than by an account payee cheque or an account payee bank draft.

\*(These particulars needs not be given in the case of a Government company, a banking company or a corporation established by a Central, State or Provincial Act.)

(b) Particulars of each repayment of loan or deposit in an amount exceeding the limit specified in section 269T made during the previous year:-

- (i) name, address and Permanent Account Number (if available with the assessee) of the payee;
- (ii) amount of the repayment;
- (iii) maximum amount outstanding in the account at any time during the previous year;
- (iv) whether the repayment was made otherwise than by account payee cheque or account payee bank draft.

(c) Whether the taking or accepting loan or deposit, or repayment of the same were made by account payee cheque drawn on a bank or account payee bank draft based on the examination of books of account and other relevant documents

(The particulars (i) to (iv) at (b) and comment at (c) above need not be given in the case of a repayment of any loan or deposit taken or accepted from Government, Government company, banking company or a corporation established by a Central, State or Provincial Act)

32.(a) Details of brought forward loss or depreciation allowance, in the following manner, to the extent available :

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

Serial Number	Assessment Year	Nature of loss / allowance (in rupees)	Amount as returned (in rupees)	Amounts as assessed (give reference to relevant order)	Remarks

(b) 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.

(c) 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.

(d) 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.

(e) 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.

33. 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.

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:

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

Tax deduction and collection Account Number (TAN)	Section	Nature of payment	Total amount of payment or receipt of the nature specified in column (3)	Total amount on which tax was required to be deducted or collected out of (4)	Total amount on which tax was deducted or collected at specified rate out of (5)	Amount of tax deducted or collected out of (6)	Total amount on which tax was deducted or collected at less than specified rate out of (7)	Amount of tax deducted or collected on (8)	Amount of tax deducted or collected not deposited to the credit of the Central Government out of (6) and (8)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)

(b) whether the assessee has furnished the statement of tax deducted or tax collected within the prescribed time. If not, please furnish the details:

Tax deduction and collection Account Number (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

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

Tax deduction and collection Account Number (TAN)	Amount of interest under section 201(1A)/206C(7) is payable	Amount paid out of column (2) along with date of payment.

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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35. (a) In the case of a trading concern, give quantitative details of principal items of goods traded :

- (i) Opening Stock;
- (ii) purchases during the previous year;
- (iii) sales during the previous year;
- (iv) closing stock;
- (v) shortage/excess, if any

(b) In the case of a manufacturing concern, give quantitative details of the principal items of raw materials, finished products and by-products :

A. Raw Materials :

- (i) opening stock;
- (ii) purchases during the previous year;
- (iii) consumption during the previous year;
- (iv) sales during the previous year;
- (v) closing stock;
- (vi) yield of finished products;
- (vii) percentage of yield;
- (viii) shortage/excess, if any.

B. Finished products/by- products :

- (i) opening stock;
- (ii) purchases during the previous year;
- (iii) quantity manufactured during the previous year;
- (iv) sales during the previous year;
- (v) closing stock;
- (vi) shortage/excess, if any.

36. 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);

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

- (c) amount of reduction as referred to in section 115-O(1A)(ii);
- (d) total tax paid thereon;
- (e) dates of payment with amounts.

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

38. 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/value/quantity as may be reported/identified by the auditor.

39. 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/value/quantity as may be reported/identified by the auditor.

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

S. 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)

41. 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 alongwith details of relevant proceedings.

.....  
 \*(Signature and stamp/Seal of the signatory)

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

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Place: \_\_\_\_\_ Name of the signatory .....

Date: \_\_\_\_\_ Full address.....

**Notes:**

1. \*This Form has to be signed by the person competent to sign Form No. 3CA or Form No. 3CB, as the case may be.



## APPENDIX XVIII

### COMPARATIVE STATEMENT – OLD AND NEW FORM Nos. 3CA/3CB/3CD

#### Comparative Statement of Old and New Form No. 3CA

Old Form No. 3CA	New Form No. 3CA
FORM NO. 3CA	FORM NO. 3CA
[See rule 6G(1)(a)]	[See rule 6G(1)(a)]
Audit report under section 44AB of the Income - tax Act, 1961, in a case where the accounts of the business or profession of a person have been audited under any other law	Audit report under section 44AB of the Income - tax Act, 1961, in a case where the accounts of the business or profession of a person have been audited under any other law
* I/We report that the statutory audit of .... [mention name and address of the assessee with permanent account number] was conducted by * me/us/M/s. .... in pursuance of the provisions of the....Act, and *I/we annex hereto a copy of * my/our/their audit report dated ....along with a copy each of –	*I / we report that the statutory audit of M/s..... (Name and address of the assessee with Permanent Account Number) was conducted by *me / us / M/s.....in pursuance of the provisions of the.... Act, and *I/we annex hereto a copy of * my / our / their audit report dated ....along with a copy of each of :-
(a) the audited * profit and loss account/income and expenditure account for the year ended on 31st March,....;	(a) the audited *profit and loss account / income and expenditure account for the <i>period beginning from ....to ending on ....</i>

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CA	New Form No. 3CA
(b) the audited balance sheet as at 31st March,...; and	(b) the audited balance sheet as at, ....;and
(c) documents declared by the said Act to be part of, or annexed to, the * profit and loss account/income and expenditure account and balance sheet.	(c) documents declared by the said Act to be part of, or annexed to, the * profit and loss account / income and expenditure account and balance sheet.
2. The statement of particulars required to be furnished under section 44AB is annexed herewith in Form No. 3CD.	2. The statement of particulars required to be furnished under section 44AB is annexed herewith in Form No. 3CD.
3. In * my/our opinion and to the best of * my/our information and according to explanations given to * me/us, the particulars given in the said Form No. 3CD and the Annexure thereto are true and correct.	3. In *my / our opinion and to the best of * my / our information and <i>according to examination of books of account including other relevant documents</i> and explanations given to *me / us, the particulars given in the said Form No.3 CD are true and correct <i>subject to the following observations/qualifications, if any:</i> <i>a.</i> <i>b.</i> <i>c.</i>
** <i>Signed</i>	** <i>(Signature and stamp/Seal of the signatory)</i>
Place.... Name :....	Place.... Name of the Signatory:....
Date.... Address....	Date.... Full Address....
Notes:	Notes:

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CA	New Form No. 3CA
1. *Delete whichever is not applicable.	1. * Delete whichever is not applicable
2. **This report has to be signed by- (i) a chartered accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949); or (ii) any person who, in relation to any State, is, by virtue of the provisions of sub-section (2) of section 226 of the Companies Act, 1956 (1 of 1956), entitled to be appointed to act as an auditor of companies registered in that State; or (iii) any person who is, by virtue of any other law, entitled to audit the accounts of the assessee for the relevant previous year.	2.**This report has to be signed <i>by a person eligible to sign the report as per the provisions of section 44AB of the Income Tax Act, 1961.</i>
3. Where any of the requirements in this Form is answered in the negative or with qualification, give reasons therefor.	3. Where any of the requirements in this Form is answered in the negative or with qualification, give reasons therefor.
4. The person, who signs this audit report, shall indicate reference of his membership number/certificate of practice number/ authority under which he is entitled to sign this report.	4. The person, who signs this audit report, shall indicate reference of his membership number/certificate of practice number/ authority under which he is entitled to sign this report.

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

#### Comparative Statement of Old and New Form No. 3CB

Old Form No. 3CB	New Form No. 3CB
FORM NO. 3CB	FORM NO. 3CB
[See rule 6G(1)(b)]	[See rule 6G(1)(b)]
Audit report under section 44AB of the Income - tax Act 1961, in the case of a person referred to in clause (b) of sub - rule (1) of rule 6G	Audit report under section 44AB of the Income - tax Act 1961, in the case of a person referred to in clause (b) of sub - rule (1) of rule 6G
*I / We have examined the Balance Sheet as at 31 <sup>st</sup> March...., and the *Profit and Loss Account / Income and Expenditure Account for the year ended on that date, attached herewith, of ..... [Mention Name and Address of the Assessee with permanent Account Number]	1. *I / we have examined the balance sheet as <i>on, .....</i> , and the *profit and loss account / income and expenditure account <i>for the period beginning from .... to ending on.....</i> , attached herewith, of .... (Name), .... (Address), .... (Permanent Account Number).
2. *I / we certify that the balance sheet and the *profit and loss / income and expenditure account are in agreement with the books of account maintained at the head office at .... and **.... branches.	2. *I / we certify that the balance sheet and the *profit and loss / income and expenditure account are in agreement with the books of account maintained at the head office at .... and **.... branches.
3.(a) *I / we report the following observations / comments / discrepancies / inconsistencies; if any:	3.(a) *I / we report the following observations / comments / discrepancies / inconsistencies; if any:
(b) Subject to above, -	(b) Subject to above, -

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CB	New Form No. 3CB
(A) *I / we have obtained all the information and explanations which, to the best of *my / our knowledge and belief, were necessary for the purposes of the audit.	(A) *I / we have obtained all the information and explanations which, to the best of *my / our knowledge and belief, were necessary for the <i>purpose</i> of the audit..
(B) In *my / our opinion, proper books of account have been kept by the head office and branches of the assessee so far as appears from *my / our examination of the books.	(B) In *my / our opinion, proper books of account have been kept by the head office and branches of the assessee so far as appears from *my / our examination of the books.
(C) In *my / our opinion and to the best of *my / our information and according to the explanations given to *me /us, the said accounts, read with notes thereon, if any, give a true and fair view:-	(C) In *my / our opinion and to the best of *my / our information and according to the explanations given to *me /us, the said accounts, read with notes thereon, if any, give a true and fair view:-
(i) in the case of the balance sheet, of the state of the affairs of the assessee as at 31 <sup>st</sup> March,... ;and  (ii) in the case of the *profit and loss account / income and expenditure account of the *profit / loss or *surplus / deficit of the assessee for the year ended on that date.	(i) in the case of the balance sheet, of the state of the affairs of the assessee as at 31 <sup>st</sup> March,... ;and  (ii) in the case of the *profit and loss account / income and expenditure account of the *profit / loss or *surplus / deficit of the assessee for the year ended on that date.
4. The statement of particulars required to be furnished under section 44AB is annexed herewith in Form No.3CD.	4. The statement of particulars required to be furnished under section 44AB is annexed herewith in Form No.3CD.

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CB	New Form No. 3CB
5. In *my/our opinion and to the best of *my / our information and according to explanations given to *me / us, the particulars given in the said Form No.3 CD <u>and the Annexures thereto</u> are true and correct.	5. In *my/our opinion and to the best of *my / our information and according to explanations given to *me / us, the particulars given in the said Form No.3 CD are true and correct <i>subject to following observations/qualifications, if any:</i>  <i>a.</i>  <i>b.</i>  <i>c.</i>
*** <i>Signed</i>	*** <i>(Signature and stamp/Seal of the signatory)</i>
Place.... Name :.... Date.... Address....	Place.... Name of the Signatory:.... Date.... Full Address....
<b>Notes:</b>	<b>Notes:</b>
1. *Delete whichever is not applicable.	1. * Delete whichever is not applicable
2. **Mention the total number of branches.	2. **Mention the total number of branches.
3. ***This report has to be signed by- (i) a chartered accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949); or (ii) any person who, in relation to any State, is, by virtue of the provisions of sub-section (2) of section 226 of the	3. ***This report has to be signed <i>by a person eligible to sign the report as per the provisions of section 44AB of the Income Tax Act, 1961.</i>

**Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961**

Old Form No. 3CB	New Form No. 3CB
Companies Act, 1956 (1 of 1956), entitled to be appointed to act as an auditor of companies registered in that State;	
4. The person, who signs this audit report, shall indicate reference of his membership number / certificate of practice number / authority under which he is entitled to sign this report.	4. The person, who signs this audit report, shall indicate reference of his membership number / certificate of practice number / authority under which he is entitled to sign this report.

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

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#### Comparative Statement of Old and New Form No. 3CD

Old Form No. 3CD	New From No. 3CD
1. Name of the Assessee	1. Name of the assessee
2. Address	2. Address
3. Permanent Account Number	3. Permanent Account Number (PAN)
	<i>4. 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</i>
4. Status	5. Status
5. Previous year ended: 31st March _____	6. Previous year <i>from.....to .....</i>
6. Assessment year	7. Assessment year
	<i>8. Indicate the relevant clause of section 44AB under which the audit has been conducted</i>



## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD
Part – B	Part – B
7. (a) If Firm or Association of Persons, indicate names of Partners/Members and their, Profit Sharing Ratios.	9. (a) If firm or association of persons, indicate names of partners/members and their profit sharing ratios.
(b) If there is any change in the Partners or Members or in their Profit Sharing Ratio since the last date of the preceding year, the particulars of such change.	(b) If there is any change in the partners or members or in their profit sharing ratio since the last date of the preceding year, the particulars of such change
8. (a) Nature of business or profession (if more than one business or profession is carried on during the previous year, nature of every business or profession).	10. (a) Nature of business or profession (if more than one business or profession is carried on during the previous year, nature of every business or profession)
(b) If there is any change in the nature of business or profession, the particulars of such change.	(b) If there is any change in the nature of business or profession, the particulars of such change.
9. (a) Whether Books of Account are prescribed under Section 44AA, if yes, list of books so prescribed.	11. (a) Whether books of account are prescribed under section 44AA, if yes, list of books so prescribed.
(b) Books of account maintained. (In case Books of Account are maintained in a computer system, mention the books of account generated by such computer system)	(b) <i>List of books of account maintained and the address at which the books of accounts are kept.</i> (In case books of account are maintained in a computer system, mention the books of account generated by such computer system. <i>If the books of accounts are not kept at one location, please furnish the addresses of</i>

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD			
	locations along with the details of books of accounts maintained at each location.)			
(c) List of books of account examined.	(c) List of books of account and nature of relevant documents examined.			
10. Whether the Profit and Loss Account includes any Profits and gains assessable on presumptive basis, if yes, indicate the amount and the relevant section (44AD, 44AE, 44AF, 44B, 44BB, 44BBA, 44BBB or any other relevant section).	12. Whether the profit and loss account includes any profits and gains assessable on presumptive basis, if yes, indicate the amount and the relevant section (44AD, 44AE, 44AF, 44B, 44BB, 44BBA, 44BBB, Chapter XII-G, First Schedule or any other relevant section.)			
11. (a) Method of accounting employed in the previous year.	13. (a) Method of accounting employed in the previous year			
(b) Whether there has been any change in the method of accounting employed vis-à-vis the method employed in the immediately preceding previous year.	(b) Whether there had been any change in the method of accounting employed vis-a-vis the method employed in the immediately preceding previous year			
(c) If answer to (b) above is in the affirmative, give details of such change, and the effect thereof on the Profit or Loss.	(c) If answer to (b) above is in the affirmative, give details of such change, and the effect thereof on the profit or loss.			
	Serial number	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)
(d) Details of deviation, if any, in the method of accounting employed in the previous year from Accounting Standards prescribed under Section 145 and the effect thereof on the Profit or Loss.	(d) Details of deviation, if any, in the method of accounting employed in the previous year from accounting standards prescribed under section 145 and the effect thereof on the profit or loss.			

## Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD			
12. (a) Method of Valuation of Closing Stock employed in the previous year.	14. (a) Method of valuation of closing stock employed in the previous year.			
	Serial number	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)
(b) Details of deviation, if any, from the method of valuation prescribed under Section 145A, and the effect thereof on the Profit or Loss.	(b) <i>In case of</i> deviation from the method of valuation prescribed under section 145A, and the effect thereof on the profit or loss, <i>please furnish</i> .			
(A) Give the following particulars of the Capital Asset converted into Stock in Trade:– (a)Description of Capital Asset (b)Date of Acquisition (c)Cost of Acquisition (d)Amount at which the Asset is converted into Stock in Trade.	15. Give the following particulars of the capital asset converted into stock-in-trade: - (a) Description of capital asset; (b) Date of acquisition; (c) Cost of acquisition; (d) Amount at which the asset is converted into stock-in-trade			
13. Amounts not credited to the Profit and Loss Account, being –	16. Amounts not credited to the profit and loss account, being, -			
(a) the items falling within the scope of Section 28;	(a) the items falling within the scope of section 28;			
(b) the proforma credits, drawbacks, refund of duty of customs or excise or service tax, or refunds of sales tax or value added tax, where such credits, drawbacks or refunds are admitted as due by the authorities concerned	(b) the pro forma credits, drawbacks, refund of duty of customs or excise or service tax, or refund of sales tax or value added tax where such credits, drawbacks or refunds are admitted as due by the authorities concerned;			

### Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD			
(c) Escalation Claims accepted during the previous year;	(c) escalation claims accepted during the previous year;			
(d) any other item of income;	(d) any other item of income;			
(e) capital receipt, if any.	(e) capital receipt, if any.			
	17. 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, please furnish:			
	Serial number	Particulars	Increase in profit (Rs.)	Decrease in profit (Rs.)
14. Particulars of depreciation allowable as per the Income–Tax Act, 1961 in respect of each asset or block of assets, as the case may be, in the following form :--	18. Particulars of depreciation allowable as per the Income Tax Act, 1961 in respect of each asset or block of assets, as the case may be, in the following form :-			
(a) Description of asset/block of assets.	(a) Description of asset/block of assets.			
(b) Rate of depreciation.	(b) Rate of depreciation.			
(c) Actual Cost or Written Down Value, as the case may be.	(c) Actual cost of written down value, as the case may be.			
(d) Additions/deductions during the year with dates; in	(d) Additions/deductions during the year with dates; in the case of any			

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD		
the case of any addition of an asset, date put to use; including adjustments on account of–	addition of an asset, date put to use; including adjustments on account of –		
(i) Modified Value Added Tax Credit claimed and allowed under the Central Excise Rules, 1944, in respect of assets acquired on or after 1st March 1994,	i) <i>Central</i> Value Added Tax credits claimed and allowed under the Central Excise Rules, 1944, in respect of assets acquired on or after 1st March, 1994,		
(ii) Change in Rate of Exchange of Currency, and	ii) change in rate of exchange of currency, and		
(iii) Subsidy or Grant or Reimbursement, by whatever name called.	iii) subsidy or grant or reimbursement, by whatever name called.		
(e) Depreciation allowable.	(e) Depreciation allowable.		
(f) Written down value at the end of the year.	(f) Written down value at the end of the year		
15. Amounts admissible under Sections-	19. Amounts admissible under sections:		
(a) 33AB	<i>Section</i>	<i>Amount debited to profit and loss account</i>	<i>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.</i>
(b) 33ABA			
(c) 33AC (wherever applicable)			
(d) 35			
(e) 35ABB			
(f) 35AC			
(g) 35CCA			
(h) 35CCB			

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD		
(i) 35D	32AC		
(j) 35DD	33AB		
(k) 35DDA	33ABA		
(l) 35E:-	35(1)(i)		
	35(1)(ii)		
(a) debited to the Profit and Loss Account	35(1)(ia)		
(showing the amount debited and deduction allowable	35(1)(iii)		
under each section separately);	35(1)(iv)		
(b) not debited to the Profit and Loss Account	35(2AA)		
	35(2AB)		
	35ABB		
	35AC		
	35AD		
	35CCA		
	35CCB		
	35CCC		
	35CCD		
	35D		
	35DD		
	35DDA		
	35E		

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD												
16. (a) Any sum paid to an Employee as Bonus or Commission for services rendered, where such sum was otherwise payable to him as Profits or Dividend. [Section 36(1)(ii)]	20. (a) Any sum paid to an employee as bonus or commission for services rendered, where such sum was otherwise payable to him as profits or dividend. [Section 36(1)(ii)]												
(b) Any sum received from Employees towards Contributions to any Provident Fund or Superannuation Fund or any other fund mentioned in Section 2(24)(x); and due date for payment and the actual date of payment to the concerned authorities under Section 36(1)(va).	(b) <i>Details of contributions</i> received from employees for various funds as referred to in section 36(1)(va): <table><tr><th><i>Serial number</i></th><th><i>Nature of fund</i></th><th><i>Sum received from employees</i></th><th><i>Due date for payment</i></th><th><i>The actual amount paid</i></th><th><i>The actual date of payment to the concerned authorities</i></th></tr><tr><td></td><td></td><td></td><td></td><td></td><td></td></tr></table>	<i>Serial number</i>	<i>Nature of fund</i>	<i>Sum received from employees</i>	<i>Due date for payment</i>	<i>The actual amount paid</i>	<i>The actual date of payment to the concerned authorities</i>						
<i>Serial number</i>	<i>Nature of fund</i>	<i>Sum received from employees</i>	<i>Due date for payment</i>	<i>The actual amount paid</i>	<i>The actual date of payment to the concerned authorities</i>								
17. Amounts debited to the Profit and Loss Account, being :- (a) expenditure of capital nature; (b) expenditure of personal nature; (c) expenditure on advertisement in any souvenir, brochure, tract, pamphlet or the like, published by a political party; (d) expenditure incurred at clubs, —	21. (a) <i>Please furnish the details of</i> amounts debited to the profit and loss account, being <i>in the nature of capital, personal, advertisement expenditure etc</i> <table><tr><th><i>Nature</i></th><th><i>Serial number</i></th><th><i>Particulars</i></th><th><i>Amount in Rs.</i></th></tr><tr><td rowspan="2">Capital expenditure</td><td></td><td></td><td></td></tr><tr><td></td><td></td><td></td></tr></table>	<i>Nature</i>	<i>Serial number</i>	<i>Particulars</i>	<i>Amount in Rs.</i>	Capital expenditure							
<i>Nature</i>	<i>Serial number</i>	<i>Particulars</i>	<i>Amount in Rs.</i>										
Capital expenditure													

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New Form No. 3CD			
(i) as entrance fees and subscriptions; (ii) as cost for club services and facilities used; (e) (i) expenditure by way of penalty or fine for violation of any law for the time being in force; (ii) any other penalty or fine; (iii) expenditure incurred for any purpose which is an offence or which is prohibited by law;				
	Personal expenditure			
	Advertisement expenditure in any souvenir, brochure, tract, pamphlet or the like published by a political party			
	Expenditure incurred at clubs being entrance fees and subscriptions			
	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			



Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New Form No. 3CD			
	force			
	Expenditure by way of any other penalty or fine <i>not covered above</i>			
	Expenditure incurred for any purpose which is an offence or which is prohibited by law			
(f) amounts inadmissible under Section 40(a);	<p>(b) <i>Amounts inadmissible under section 40(a):-</i></p> <p>(i) <i>as payment to non-resident referred to in sub-clause (i)</i></p> <p>(A) <i>Details of payment on which tax is not deducted:</i></p> <p>(I) <i>date of payment</i></p> <p>(II) <i>amount of payment</i></p> <p>(III) <i>nature of payment</i></p> <p>(IV) <i>name and address of the payee</i></p> <p>(B) <i>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)</i></p>			

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New Form No. 3CD
	<p>(I) <i>date of payment</i></p> <p>(II) <i>amount of payment</i></p> <p>(III) <i>nature of payment</i></p> <p>(IV) <i>name and address of the payee</i></p> <p>(V) <i>amount of tax deducted</i></p> <p>(ii) <i>as payment referred to in sub-clause (ia)</i></p> <p>(A) <i>Details of payment on which tax is not deducted:</i></p> <p>(I) <i>date of payment</i></p> <p>(II) <i>amount of payment</i></p> <p>(III) <i>nature of payment</i></p> <p>(IV) <i>name and address of the payee</i></p> <p>(B) <i>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></p> <p>(I) <i>date of payment</i></p> <p>(II) <i>amount of payment</i></p> <p>(III) <i>nature of payment</i></p> <p>(IV) <i>name and address of the payer</i></p>

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD
	<p>(V) amount of tax deducted</p> <p>(VI) amount out of (V) deposited, if any</p> <p>(iii) under sub-clause (ic) [Wherever applicable]</p> <p>(iv) under sub-clause (iia)</p> <p>(v) under sub-clause (iib)</p> <p>(vi) under sub-clause (iii)</p> <p>(A) date of payment</p> <p>(B) amount of payment</p> <p>(C) name and address of the payee</p> <p>(vii) under sub-clause (iv)</p> <p>(viii) under sub-clause (v)</p>
(g) Interest, Salary, Bonus, Commission or Remuneration inadmissible under Section 40(b)/40(ba) and computation thereof;	(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;
(h) (A) Whether a Certificate has been obtained from the Assessee regarding payments relating to any expenditure covered under Section 40A(3) that the payments were made by Account Payee Cheques	<p>(d) Disallowance/deemed income under section 40A(3):</p> <p>(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:</p>

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD				
<p>drawn on a Bank or Account Payee Bank Draft, as the case may be, [Yes/No]</p> <p>(B) amount inadmissible under Section 40A(3), read with Rule 6 DD [with break-up of inadmissible amounts];</p>	<i>Serial number</i>	<i>Date of payment</i>	<i>Nature of payment</i>	<i>Amount</i>	<i>Name and Permanent Account Number of the payee, if available</i>
	<p>(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);</p>				
	<i>Serial number</i>	<i>Date of payment</i>	<i>Nature of payment</i>	<i>Amount</i>	<i>Name and Permanent Account Number of the payee, if available</i>
<p>(i) provision for payment of gratuity not allowable under Section 40A(7);</p> <p>(j) any sum paid by the Assessee as an employer not allowable under section 40A(9);</p>	<p>(e) provision for payment of gratuity not allowable under section 40A(7);</p> <p>(f) any sum paid by the assessee as an employer not allowable under section 40A(9);</p> <p>(g) particulars of any liability of a contingent nature;</p>				

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New Form No. 3CD
(k) particulars of any liability of a contingent nature. (l) amount of deduction inadmissible in terms of section 14 A in respect of the expenditure incurred in relation to income which does not form part of the total income; (m) amount inadmissible under the proviso to section 36(1)(iii)	(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; (l) amount inadmissible under the proviso to section 36(1)(iii).
17A. Amount of interest inadmissible under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006.	22. Amount of interest inadmissible under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006.
18. Particulars of payments made to persons specified under Section 40A(2)(b).	23. Particulars of payments made to persons specified under section 40A(2)(b).
19. Amounts deemed to be Profits and Gains under Section 33AB or 33ABA or 33AC.	24. Amounts deemed to be profits and gains under section 32AC or 33AB or 33ABA or 33AC.
20. Any amount of Profit chargeable to tax under Section 41 and computation thereof.	25. Any amount of profit chargeable to tax under section 41 and computation thereof.
21.*(i) In respect of any sum referred to in clauses (a), (b), (c), (d), (e) or (f) of section 43B, the liability for	26. In respect of any sum referred to in clause (a),(b), (c), (d), (e) or (f) of section 43B, the liability for which:-

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD
which:–	
<p>(A) pre-existed on the first day of the previous year but was not allowed in the assessment of any preceding previous year and was –</p> <p>(a) paid during the previous year;</p> <p>(b) not paid during the previous year;</p> <p>(B) was incurred in the previous year and was</p> <p>(a) paid on or before the due date for furnishing the return of income of the previous year under section 139(1);</p> <p>(b) not paid on or before the aforesaid date.</p> <p>(ii) [***]</p> <p>* State whether Sales Tax, Customs Duty, Excise Duty or any other Indirect Tax, Cess, Import, etc. is passed through the Profit and Loss Account.</p>	<p>(A) pre-existed on the first day of the previous year but was not allowed in the assessment of any preceding previous year and was</p> <p>(a) paid during the previous year;</p> <p>(b) not paid during the previous year;</p> <p>(B) was incurred in the previous year and was</p> <p>(a) paid on or before the due date for furnishing the return of income of the previous year under section 139(1);</p> <p>(b) not paid on or before the aforesaid date.</p> <p>(State whether sales tax, customs duty, excise duty or any other indirect tax, levy, cess, impost, etc., is passed through the profit and loss account.)</p>
22. (a) Amount of Modified Value Added Tax credits availed of or utilised during the previous year and its treatment in the Profit and Loss Account and treatment of outstanding Modified Value Added Tax credits in the accounts.	<p>27. (a) Amount of <i>Central</i> Value Added Tax credits availed of or utilised during the previous year and its treatment in the profit and loss account and treatment of outstanding <i>Central</i>/Value Added Tax credits in the accounts.</p> <p>(b) Particulars of income or expenditure of prior period credited or debited to the profit and loss account.</p>

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD
(b) Particulars of income or expenditure of prior period credited or debited to the Profit and Loss Account.	
	28. <i>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.</i>
	29. <i>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.</i>
23. 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]	30. 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]
24. (a)* Particulars of each Loan or Deposit in an amount exceeding the limit specified in Section 269SS taken or accepted during the previous year:- (i) Name, Address and Permanent Account Number (if available with the Assessee) of the Lender or Depositor; (ii) Amount of Loan or Deposit taken or accepted;	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 :- (i) name, address and permanent account number (if available with the assessee) of the lender or depositor; (ii) amount of loan or deposit taken or accepted;

Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961

Old Form No. 3CD	New From No. 3CD
<p>(iii) Whether the Loan or Deposit was squared up during the previous year;</p> <p>(iv) Maximum Amount outstanding in the account at any time during the previous year;</p> <p>(v) Whether the Loan or Deposit was taken or accepted otherwise than by an Account Payee Cheque or an Account Payee Bank Draft.</p> <p>*(These particulars need not be given in the case of a Government company, a banking company or a corporation established by a Central, State or Provincial Act.)</p> <p>(b) Particulars of each repayment of Loan or Deposit in an amount exceeding the limit specified in Section 269T made during the previous year:—</p> <p>(i) Name, Address and Permanent Account Number (if available with the Assessee) of the payee;</p> <p>(ii) Amount of the repayment;</p> <p>(iii) Maximum Amount outstanding in the account at any time during the previous year;</p> <p>(iv) Whether the repayment was made otherwise than by Account Payee Cheque or Account Payee Bank Draft.</p>	<p>(iii) whether the loan or deposit was squared up during the previous year;</p> <p>(iv) maximum amount outstanding in the account at any time during the previous year;</p> <p>(v) whether the loan or deposit was taken or accepted otherwise than by an account payee cheque or an account payee bank draft.</p> <p>* (These particulars needs not be given in the case of a Government company, a banking company or a corporation established by a Central, State or Provincial Act.)</p> <p>(b) Particulars of each repayment of loan or deposit in an amount exceeding the limit specified in section 269T made during the previous year :-</p> <p>(i) name, address and Permanent Account Number (if available with the assessee) of the payee;</p> <p>(ii) amount of the repayment;</p> <p>(iii) maximum amount outstanding in the account at any time during the previous year;</p> <p>(iv) whether the repayment was made otherwise than by account payee cheque or account payee bank draft.</p> <p>(c) Whether the taking or accepting loan or deposit, or repayment of the same were made by account payee cheque <i>drawn on a bank</i> or account payee bank draft <i>based on the examination of books of account and other</i></p>



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<p>(c) Whether a Certificate has been obtained from the assessee regarding taking or accepting Loan or Deposit, or repayment of the same through an Account Payee Cheque or an Account Payee Bank Draft. [Yes/No]</p> <p>The particulars (i) to (iv) at (b) and the Certificate at (c) above need not be given in the case of a repayment of any loan or deposit taken or accepted from Government, Government Company, Banking Company or a Corporation established by a Central, State or Provincial Act.</p>						<p><i>relevant documents</i></p> <p>(The particulars (i) to (iv) at (b) and <i>comment at (c)</i> above need not be given in the case of a repayment of any loan or deposit taken or accepted from Government, Government company, banking company or a corporation established by a Central, State or Provincial Act)</p>					
<p>25. (a) Details of Brought Forward Loss or Depreciation Allowance, in the following manner, to the extent available:</p>						<p>32.(a) Details of brought forward loss or depreciation allowance, in the following manner, to the extent available :</p>					
S. No	Assessment year	Nature of loss/allowance (in rupees)	Amount as returned (in rupees)	Amount as assessed (give reference to relevant order)	Remarks	Serial Number	Assessment Year	Nature of loss / allowance (in rupees)	Amount as returned (in rupees)	Amounts as assessed (give reference to relevant order)	Remarks

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(b) 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.						(b) 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.					
						<p>(c) <i>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.</i></p> <p>(d) <i>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.</i></p> <p>(e) <i>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.</i></p>					
26. Section-wise details of deductions, if any, admissible under Chapter VIA.						33. 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			

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											of (6) and (8)
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
		(b)_whether the assessee has furnished the statement of tax deducted or tax collected within the prescribed time. If not, please furnish the details:									
		Tax deduction and collection Account Number (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	
		(c) whether the assessee is liable to pay interest under section 201(1A) or section 206C(7). If yes, please furnish:									
		Tax deduction and		Amount of interest			Amount paid out of				

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	<i>collection Account Number (TAN)</i>	<i>under section 201(1A)/206C(7) is payable</i>	<i>column (2) along with date of payment.</i>
<p>28. (a) In the case of a Trading Concern, give quantitative details of principal items of goods traded:</p> <p>(i) Opening Stock;</p> <p>(ii) Purchases during the previous year;</p> <p>(iii) Sales during the previous year</p> <p>(iv) Closing Stock;</p> <p>(v) Shortage/excess, if any</p> <p>(b) In the case of a Manufacturing Concern, give quantitative details of the principal items of Raw Materials, Finished Products and By-Products :</p> <p>A. Raw Materials:</p> <p>(i) Opening Stock;</p> <p>(ii) Purchases during the previous year;</p> <p>(iii) Consumption during the previous year;</p> <p>(iv) Sales during the previous year;</p> <p>(v) Closing stock;</p> <p>(vi) *Yield of Finished Products;</p>	<p>35. (a) In the case of a trading concern, give quantitative details of principal items of goods traded :</p> <p>(i) Opening Stock;</p> <p>(ii) Purchases during the previous year;</p> <p>(iii) Sales during the previous year</p> <p>(iv) Closing Stock;</p> <p>(v) Shortage/excess, if any</p> <p>(b) In the case of a Manufacturing Concern, give quantitative details of the principal items of Raw Materials, Finished Products and By-Products :</p> <p>A. Raw Materials:</p> <p>(i) Opening Stock;</p> <p>(ii) Purchases during the previous year;</p> <p>(iii) Consumption during the previous year;</p> <p>(iv) Sales during the previous year;</p> <p>(v) Closing stock;</p> <p>(vi) Yield of Finished Products;</p>		

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<p>(vii) *Percentage of yield; (viii) *Shortage/excess, if any.</p> <p>B. Finished products/by-products: (i) Opening Stock; (ii) Purchases during the previous year; (iii) Quantity manufactured during the previous year; (iv) Sales during the previous year; (v) Closing stock; (vi) Shortage/excess, if any. *Information may be given to the extent available.</p>	<p>(vii) Percentage of yield; (viii) Shortage/excess, if any.</p> <p>B. Finished products/by-products: (i) Opening Stock; (ii) Purchases during the previous year; (iii) Quantity manufactured during the previous year; (iv) Sales during the previous year; (v) Closing stock; (vi) Shortage/excess, if any.</p>
<p>29. In the case of a Domestic Company, details of Tax on Distributed Profits under Section 115O in the following form – (a) Total Amount of distributed profits; (b) Total Tax paid thereon; (c) Dates of Payment with amounts.</p>	<p>36. 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) <i>amount of reduction as referred to in section 115-O(1A)(i);</i> (c) <i>amount of reduction as referred to in section 115-O(1A)(ii);</i> (d) total tax paid thereon; (e) dates of payment with amounts.</p>
<p>30. Whether any Cost Audit was carried out, if yes, enclose a copy of the report of such audit [See section 139(9)].</p>	<p>37. Whether any cost audit was carried out, if yes, <i>give the details, if any, of disqualification or disagreement on any matter/item/value/quantity as may be reported/identified by the cost auditor.</i></p>

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31. Whether any audit was conducted under the Central Excise Act, 1944, if yes, enclose a copy of the report of such audit.	38. Whether any audit was conducted under the Central Excise Act, 1944, if yes, <i>give the details, if any, of disqualification or disagreement on any matter/item/value/quantity as may be reported /identified by the auditor.</i>			
	39. <i>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/value/quantity as may be reported/identified by the auditor.</i>			
32. Accounting ratios with calculations as follows: – (a) Gross Profit/Turnover; (b) Net Profit/Turnover; (c) Stock-in-Trade/Turnover; (d) Material Consumed / Finished Goods produced.	40. <i>Details regarding turnover, gross profit, etc., for the previous year and preceding previous year:</i>			
	<i>Serial number</i>	<i>Particulars</i>	<i>Previous year</i>	<i>Preceding previous year</i>
	1.	<i>Total turnover of the assessee</i>		
	2.	Gross profit/turnover		
	3.	Net profit/turnover		
	4.	Stock-in-trade/turnover		
	5.	Material consumed/finished goods produced		

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	<i>(The details required to be furnished for principal items of goods traded or manufactured or services rendered)</i>
	41. <i>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.</i>
*Signed  Place :..... Name:.. .....  Date:..... Address:.....	..... *(Signature and stamp/Seal of the signatory) Place: _____ Name of the signatory.....  Date: _____ Full address .....
Notes: 1. The Annexure to this Form must be filled up failing which the Form will be considered as incomplete. 2. This Form and the Annexure have to be signed by the person competent to sign Form No.3CA or Form No.3CB, as the case may be.	Notes: 1. *This Form has to be signed by the person competent to sign Form No. 3CA or Form No. 3CB, as the case may be.