

Seminar on Tax Audit

Organised by
NAGPUR BRANCH
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PRESENTATION BY
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FEW ISSUES ON TAX AUDIT IN INCOME TAX

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11/09/2014

(2)

Tax Audit Issues :

1. Whether print out of books of account is necessary ?
2. Whether section 44AD is qua assessee or qua business ?
3. Whether threshold limit of Rs. 25 lacs is applicable to all professions ?
4. Whether tax audit is not compulsory in marginal cases even if the profit is below 8% of turnover ?
5. Whether tax audit is not required in case of 'agency business', even if it earns less than 8% on turnover below Rs. 100 lacs. Sec. 44AD vis-à-vis Sec. 44AB?.
6. Whether the partner of a firm receiving salary, interest, bonus, commission or remuneration is subject to audit u/s. 44AB ?
7. Whether Interest is to be disallowed u/s. 14A when investment yields both taxable and exempt income ?
8. Whether loss from share derivatives is business loss or speculation loss? Section 43(5) vis-à-vis Section 73.
9. Controversy revolving around Sec. 40a(ia) ?
10. Whether Sec. 269SS and 269T applies to non cheque/non draft loan/deposit transactions ?.
11. Whether delayed payments of Employee's PF Contribution is allowable u/s. 43B ?

Should we file the Return of Income on 30-09-2014 ?

- Notification S.O. 1902 dt. 25-07-2014- Income Tax (7th Amendment) Rules, 2014.
- F.No.133/24/2014-TPL – dt. 20-08-2014 -Order Under Section 119 of the Income-tax Act, 1961.

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Various issues in New Form requiring guidance from ICAI :

- Importance of Guidance Note of ICAI :
- Supreme Court in the case of CIT v. Punjab Stainless steel Industries (Appeal No. 5592 of 2008) , Order dated 5-5-2014:

“In our opinion, when a recognized body of Accountants, after due deliberation and consideration publishes certain material for its members, one can rely upon the same.”

1. Whether print out of books of account is necessary ?

- **Sec. 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”.

- **Section 4 of the Information Technology Act, 2000:**

“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 – rendered or made available in an electronic form; and – accessible so as to be usable for a subsequent reference.”

2. Whether the section 44AD is qua assessee or qua business ?

- Section 44AD : Deletion of subsection (5) from earlier section
- Where the assessee is proprietor of more than one concern, aggregate of all the businesses to be taken into consideration for the purposes of compliance with the provisions of sec. 44AB. *Asst. CIT & Anr. V. Dr. K. Satish Shetty [2009] 310 ITR 366 (Kar.)*
- Guidance Note of ICAI on this point.

3. Whether the threshold limit of Rs. 25 lacs is applicable to all professions ?

- Professions specified under section 44AA are legal, medical, engineering, architectural, technical consultancy, accountancy, interior decoration. Notified professions are company secretary (Not. 9102 dt.25-9-92), authorized representative before any law and film artists (Not. SO 17(E) dt.12-1-77) and information technology (Not.116 dt. 4-5-01).
- Subsection (5) of Section 44AD provides exception to Professions covered u/s. 44AA.

4. Whether tax audit is not compulsory in marginal cases even if the profit is below 8% of turnover ?

- Section 44AB : Every person,-
(d) carrying on the business shall, if the profits and gains from 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.....
- The subsection 5 of section 44AD states that an eligible assessee **who claims** that his profits and gains from the eligible business are lower than the profits and gains specified in subsection (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 Sec. 44AA(2) and get them audited and furnish a report of such audit as required u/s. 44AB.

5. Whether tax audit is not required in case of 'agency business', even if it earns less than 8% on turnover below Rs. 100 lacs. Sec. 44AD vis-à-vis Sec. 44AB.

- Section 44AD provides exceptions to agency business.
 - Agency business not defined.
 - The term 'agent' is defined in **Section 182** of The Indian Contract Act as "a person employed to do any act for another, or to represent another in dealing with third persons".
 - Test provided by CBDT in its circular No. 452 dt. 17-3-86 while clarifying the applicability of section 44AD in case of commission agents stated that :
 - A person who:
 - i) does not act as a principal
 - ii) is indemnified by the principal, in the event of any loss
 - iii) do not have dominion over the goods of the principal , and
 - iv) do not have interest in the profits and losses of the principal.
- Would be called as carrying on agency business or pure commission agent.

6. Whether the partner of a firm receiving salary, interest, bonus, commission or remuneration is subject to audit u/s. 44AB ?

- Partners liable for audit since what he gets is business income assessable u/s. 28(v).
- Amal Ganguly (ITA No. 2135/Kol./2008, Assessment Year 2003-04) dt....
- Usha A Narayanan v. DCIT (ITA No. 703/Kol/2012 A.Y. 2006-07) dt. 25-3-2013
- Sagar Dutta v. DCIT (ITA no. 692/Kol/2012 AY 2006-07) dt. 3-5-2013
- Guidance Note of the ICAI.

7. Whether Interest is to be disallowed u/s. 14A when investment yields both taxable and exempt income:

- Investment in shares yielding dividend and capital gains or business profits or investment in partnership firm yielding share in profits and remuneration or interest on capital.
- Guidance Note of ICAI
- Cheminvest Ltd.-v-ITO 121 ITD 318
CIT v. Winsome Textile Industries Ltd. [2009] 319 ITR 204 (PH)
CIT-vs- Corrtch Energy (P.) Ltd. [2014] 45 taxmann.com 116 (Gujarat)
CIT-vs-Shivam Motors--judgment dated 5.5.2014 of ALL high court
*CIT-vs-Lakhani Marketing Incl---*Judgment dated 02.04.14 of Pb & Hr HC
- CBDT circular no. 5/2014 dated 11-2-2014 has clarified that : In exercise of its powers u/s. 119 of the Act, hereby clarifies that Rule 8D read with section 14A of the Act provides for disallowance of the expenditure even where taxpayer in a particular year has not earned any exempt income.

8. Whether loss from share derivatives is business loss or speculation loss. Section 43(5) vis-à-vis Section 73:

- New clause 33(e) is inserted in the Form No. 3CD, which requires reporting of speculation losses in terms of Explanation to Section 73.
- Section 43(5) defines what is speculative transaction. As per proviso, Trading in shares derivatives (AY 2006-07) and trading in commodity derivatives (AY 2014-15) are not considered to be speculative transactions.
- Explanation to Section 73 creates a deeming fiction by treating the purchase and sale of shares by companies (other than few exceptions) would be considered as speculation business.
- Considering the fact that as per the Securities Contract Regulation Act, the definition of shares include 'derivative' also, the share derivative losses would be considered as speculation losses. And such losses will have to be reported under Clause 32(e) newly inserted recently.
- However, transactions of commodities derivatives by Companies would still not be considered as speculative transactions.

9. Controversy revolving around section 40a(ia) :

- a. Whether the tax has to be deducted **at source**?
- b. Whether disallowance is restricted to “payable” amount only?
- c. Impact of changes by Finance Act 2014 in section 40a(ia).

a. Whether Tax has to be deducted at Source.

- a. Rajkot Tribunal held expenditure disallowed unless the tax is deducted at source.
- b. The literal interpretation of wording of Section 40a(ia)
- c. Gujarat High Court in Patel Ramniklal Hirji's case held rejecting Revenue's appeal, that there is no substantial question of law involved.
- d. Mumbai ITAT in Nanasaheb Dhumal's case held role of Chapter XVII-B is only to verify the nature of payments whether attract TDS or not.
- e. Proviso to section 40a(ia) itself supports the view that tax need not be deducted at source.
- f. Section 195A also offers scope for symbolic deduction.
- g. **Hon'ble Rajasthan High Court** in ACIT v. Farasol Ltd (1987) (163 ITR 364 RAJ).

b. Whether disallowance is restricted to “payable” amount only :

- a. Hon. Allahabad High Court held it applies only to “payable” amount in CIT vs. Vector Shipping Services Pvt. Ltd. 357 ITR 642.
- b. Department’s SLP recently dismissed by the Supreme Court *in limine*.
- c. Mumbai ITAT in ACIT v. Rishti Stock and Shares Pvt. Ltd. (ITA No. 112/Mum./2012 dt. 2-8-2013) held the decisions of Hon. Allahabad High Court was ‘obiter dicta’, and not ‘ratio decidendi’.
- d. CBDT issued a circular (No. F 279/Misc/M-61/2012-ITJ(vol-II)dt. 16-12-2013 - Departmental View).
- e. Except Uttar Pradesh, the CBDT circular shall rule.

C. Impact of changes in Finance Act 2014.

- a. The entire chapter XVII-B is now subjected to disallowance test of sec. 40a(ia).
- b. Allow ability of payments between April 2014 to 10th July, 2014.
- c. Issues as to applicability of new section 194IA (payment for transfer of immovable property).

10. Whether Sec. 269SS and 269T applies to non cheque/draft loan/deposit transactions:

- Explanation to section 269SS clarifies “loan or deposit” means loan or deposit of money.
- Finance Act 2014 has excluded loan or deposit by using electronic online clearing systems.

What about :

➤ **Share application Money accepted in cash:**

- Bhalotia Engineering Works (P) Ltd. vs. CIT (2005) 275 ITR 399 (Jharkhand)
- CIT vs. I.P. India (P) Ltd. (2012) 343 ITR 353 (Delhi)

➤ **Cash Transaction between firms within family and with partners :**

- CIT vs. V. Sivkumar (2013) 354 ITR 9 (Mad)

Whether Sec. 269SS and 269T applies to non cheque/draft loan/deposit transactions. (contd.)

➤ **Cash received as Trade Advance:**

- CIT & ANR. vs. Kailash Chandra Deepak Kumar (2009) 317 ITR 351.
- CIT v. Madhav Enterprises (356 ITR 588)(2013- Guj. HC)

➤ **Acceptance or Repayment of loan by Journal Entries:**

- CIT v. Triumph International 345 ITR 270
- Sunflower Builders v. DCIT 61 ITD 227
- Lodha Builders Pvt. Ltd vs. ACIT (ITAT Mumbai) I.T.A. No.476/M/2014
- CIT vs. WorldWide Township Projects Ltd (Delhi High Court) (ITA 232/2014)

11. Whether delayed payments of Employee's PF Contribution is allowable u/s. 43B:

- a. Section 2(24)(x) and Section 36(1)(va) were inserted by Finance Act, 1987 whereby the employee contribution to PF which is deducted from employees salary was deemed to be income of the assessee and an expenditure for corresponding amount was allowed if it was deposited with Govt. Treasury within the due date prescribed under the PF Act.
- b. Section 43B was introduced by Finance Act 1983. Clause (b) thereof reads as:
- c. “any sum payable by the assessee **as an employer** by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees”

Whether delayed payments of Employee's PF Contribution is allowable u/s. 43B: (contd.)

➤ **High Court Decisions not in favour of time limit mentioned in proviso to 43B(b)**

- CIT v. Bengal Chemicals & Pharmaceuticals Ltd. (2011) 11 Taxmann.com 328 (Kol.)
- CIT v. Pawmi Tissues Ltd. (2008) 215 CTR 150 (Bom.)
- ITO vs. LKP Securities Ltd. ITA No 638/Mum/2012 dated 17th May 2013.
- CIT v. Gujarat State Road Development Corporation Ltd.in Tax Appeal No. 637 of 2013

Whether delayed payments of Employee's PF Contribution is allowable u/s. 43B: (contd.)

➤ **Reasons putforth by the Courts:**

1. Sec. 43B refers only to Employer's PF contribution and not employees PF
2. Specific provision in respect of employee PF exists in section 36(1)(va).
3. There is no amendment in section 36(1)(va) since its introduction in 1987, in case it be so intended there would have been amendment to it.
4. Prior to Finance Act, 2003, second proviso in Sec. 43B specifically stated the due date for employer PF. However, thereafter the proviso was deleted granting extended time to employer PF.
5. Retrospective deletion of proviso in Sec. 43B does not mean there is automatic extension of due date for employee PF.
6. The decision of Supreme Court in Alom Extrusions Ltd is distinguishable on facts.

Whether delayed payments of Employee's PF Contribution is allowable u/s. 43B: (contd.)

➤ **High Court decisions in favour of time limit mentioned in proviso to Sec. 43B(b).**

- CIT v. Kichha Sugar Company Ltd. (ITA no. 50 of 2009) (Uttarakhand)
- CIT v. Aimil Limited (2010) 321 ITR 508 (Del.)
- CIT v. Nipso Polyfabriks Ltd. (2013) 350 ITR 327 (HP)
- CIT v. Sabari Enterprises (2008) 298 ITR 141 (Kar.)
- CIT v. Udaipur Dugdh Sah. Utpadak Sangh Ltd. (2013) 35 Taxmann.com 616 (Raj.)
- CIT v. Hemala Embroidery Mills P. Ltd. (2013) 37 Taxmann.com 160 (P&H)
- CIT v. P.M. Electronics Ltd., 313 ITR 161 (Del.)
- CIT v. Jaipur VidyutVitran Nigam Ltd: ITA No. 278/2011 (Raj.)
- Spectrum Consultants India (P.) Ltd. v. CIT (2013) 34 taxmann.com 20 (Kar);

Whether delayed payments of Employee's PF Contribution is allowable u/s. 43B: (contd.)

➤ **Reasons put forth by Courts :**

1. The PF Act does not distinguish between employer and employee contribution for payment due dates, then why to distinguish for the purposes of income tax.
2. There is a separate specific provision for allowing deduction for payment of employee contribution in section 36(1)(va) since the amount collected is considered as income under section 2(24)(x) of the Act.
3. The introduction of section 43B was with a view to discourage the assessee in delaying the payment of PF contributions, however, with a view to avoid hardships, time limit was extended later.

Whether delayed payments of Employee's PF Contribution is allowable u/s. 43B: (contd.)

➤ **Latest Bombay High Court Judgment:**

- CIT v. Hindustan Organic Chemicals Ltd.
(Appeal No. 399 of 2012) Order pronounced on 11th July, 2014.

Questions ?

THANK YOU