



GUIDELINES TO FILL FORM 3CD AY 2014-15

Clause 1: Name of Assessee

1. Give name of the assessee whose accounts are being audited under section 44AB.
2. Incase of audit of a branch, the name of the branch should be stated alongwith the name of the assessee.
3. Incase of proprietary concern, Furnish name of the proprietary firm along with the name of the proprietor.
4. Incase of change in name of the company, eg, conversion into public Ltd co or vice versa, state both names and also state the fact of the change by way of a note.
5. In case of any change in the name of the assessee between the last day of the previous year and the date of tax audit report, the name as on the last date of the previous year and also on the tax audit report date be stated.

Clause 2: Address

1. As far as possible the address should correspond to the address which the assessee is using while making communication with the Income Tax Department for assessment purposes (i.e the address where any communication/notice etc send by the department may be taken as effective service), address as appearing on Tax Challans, PAN, etc.
2. Incase of audit of a branch, the address of the branch should be stated.
3. Incase of change in address after the end of the financial year and before the date of tax audit, the fact may be brought on form 3CD.
4. Incase of a company, the address of the registered office be stated alongwith the principle place of business, if any.

Clause 3: Permanent Account Number

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

Clause 4: Status

1. The status does not refers to the residential status.

2. It means status of the person who is defined as per section 2(31) [i.e Individual, HUF, Company, Firm, etc.].3. In case there is any dispute with respect to status of the assessee, full facts relating to the same should be mentioned.(dispute may arise for e.g. w.r.t treatment of a partnership firm 'As Such' or as 'AOP')Co-operative societies and co-operative banks are artificial juridical persons – **M.V Rajendra vs. ITO 260 ITR 422 (Ker)**Joint venture set up by two registered firms is not a joint venture by AOP or BOI and is not a person within meaning of clause (v) of Section 2(31)-**Gouranga Lal Chatterjee vs. ITO 247 ITR 737 (Cal)**. The income was held to be assessable in the hands of individual partners.Person in section 2(31) includes institutions-**CIT vs. Gujarat Maritime Board**

289 ITR 0139 (Guj) Affirmed in 295 ITR 561 (SC)

Distinction between AOP and BOI

Meera and Company vs. Commissioner of Income-tax 224 ITR 635 [SC]

Sub-clause (v) of clause (31) of section 2 of the Income-tax Act, 1961, speaks of “an association of persons or a body of individuals”. This implies that an “association of persons” is not something distinct and separate from a “body of individuals”. The latter expression has been added to obviate any controversy as to whether only combinations of human beings are to be treated as a unit of assessment. When several individuals are found to have joined together for the purpose of making profit, the group of individuals may be conveniently described as a “body of individuals”. “An association of persons or a body of individuals, whether incorporated or not”, has been brought within the net of taxation with the intention clearly to hit combinations of individuals or other persons who were engaged together in some joint enterprise. The combinations may or may not be incorporated. A profit-yielding joint venture has to be taxed as a single unit.

G.N Sunanda vs. CIT 174 ITR 0664 (KAR)

In order to constitute an association of persons, there must be joining together in a common venture the object of which is to produce income, profits or gains. Though a body of individuals is not identical with an association of persons, they have similarities; an association of persons may consist of non-individuals, but a body of individuals consists of only human beings. “Body” in “body of individuals” would mean association for some common purpose or object and there must be unity under some common tie or occupation. A mere collection of individuals without a common tie or aim will not constitute a body of individuals under section 2(31) of the Income-tax Act, 1961, and under section 47(ii) of the Act. A “body of individuals” must be capable of holding income producing assets or assets that produce income.

Clause 5: Previous year ended

Here the date of which the previous year ended has to be stated. Since presently the previous year u/s 3 of The Income Tax Act are uniform and ends on 31st march, being a financial year, the relevant previous year should be mentioned.

Clause 6: Assessment year ended

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

Clause 7: Particulars of Partners/members of firm or AOP, their P.S.R and changes

(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.

1. This clause is applicable only to partnership firm & associations of persons. Firm Includes a LLP. However, LLP's registered outside India are not Firms or AOP.

2. If a partner of a firm/AOP acts in a representative capacity, the name of beneficial partner/member should be stated along with such fact.

3. If the loss sharing ratio is different of PSR, it should also be stated.

4. The tax auditor should obtained relevant partnership deeds/ documents duly certified and get the changes verified.

5. Detail of all changes in partners/members & also there profit sharing ratio during the previous year should be stated.

6. There is no need to state the change in remuneration (partner's salary) and interest to partners or members generally. However, the Apex court in case of **CIT vs. R.M Chidambram Pillay [106 ITR 292]** has held that salary to partner is not a charge to profit but only an appropriation of profit. Accordingly change in salary during the year should be construed as change in PSR and thus be indicated.

Clause 8: Nature of business & profession & changes and its particular

(a) Nature of business or profession.

(b) If there is any change in the nature of business or profession, the particulars of such change.

a. The expression Business & Profession should be given their meaning as per the Income Tax Act.

b. Whether a particular activity can be classified as business or profession will depend upon facts of each case.

1. The principal to find out whether or not the transaction in question is an adventure in the nature of trade may be referred at **284 ITR 453 (BOM)- Deepak Tanna vs. CIT**
2. Trade means a business which a person has learnt or carries on for procuring subsistence or profit, occupation or employment- **224 ITR 318 (GAU)- CIT vs. Assam Hard Board Ltd.**
3. The Income Tax Act defines the term business only inclusively. The two essential requirements for an activity to be considered as business are (i) it must be a continuous course of activity, and (ii) it must be carried on with a profit motive. **221 ITR 018 (MAD)-CIT vs. Venkata Subbiah Reddiar (K.S)**
4. Difference between business and profession explained in **212 ITR 133 (RAJ)- CIT v/s Bhavgan Broker Agency**

The word “business” has been defined under clause (13) of section 2 of the Income-tax Act, 1961, to include any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture. The word “profession” has been defined in section 2(36) to include vocation, which refers to a way of living and not necessarily a course of activity indulged in, for earning one’s livelihood or making any income. “Business” is a term with a wider import than “profession”. All professions are businesses but all businesses are not professions. There should be some special qualification of a person apart from skill and ability, which is required in carrying on any activity which could be considered as profession. This could be by having education in a particular system either in a college or university or it may be even by experience.

Accordingly, the following have been held as business:-

- (i) Commission agent (**224 ITR 318 (Gau)**)
- (ii) Stock Brokers (**204 ITR 093 (Bom)**)
- (iii) C&F agents (**206 ITR 548 (Bom)**)
- (iv) Travel Agents
- (v) Courier Agents etc.

c. The expression profession has been specifically defined under the income tax act the specified profession have been referred u/s 44AA of the Act. These include legal, medical, engineering, accountancy, technical consultancy, authorized representative, film artists, company secretaries, information technology and until recently cricketers and umpires, etc.

d. The nature of business or profession should correspond to the relevant classification as per form ITR-4 (Heading nature of business).

e. In case any existing line of business is discontinued or a new line or facility is added due to business restructuring, amalgamation, demerger or any other reason, the fact relating to the same

may be stated. f. Any temporary suspension of business or cessation of the business may not amount to change and thus need not be reported.

An ongoing controversy is subsisting as to whether certain transactions in shares and securities would be business or investment. The CBDT has sought to clarify the issue by way of circular No. 4/2007, dated 15-6-2007 and had laid out certain parameters. The same may also be kept in mind by the Tax auditor while commenting upon nature of business or profession.

Clause 9: Books of account prescribed, maintained and examined

(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.

(c) List of books of account examined.

1. The limits as to mandatory maintenance of account books in case of specified profession are as stated in section 44AA (1) read with rule 6F. Thus under 9(a) the tax auditor is merely to comment whether any books of account are prescribed for assessee's line of business or not.

2. In case of specified professions, the tax auditor is to verify whether the books of account as prescribed are maintained or not & has to state the books of account maintained. i.e Cash book, ledger, journal (if mercantile system is being followed), Bills issued, etc.

3. In case the books are maintained in computer system, the auditor's is to state the books of account maintained by the system, which he may do after obtaining a complete list of books & records and other documents (financial & non Financial) maintained by the assessee.

4. In case of assessee engaged in manufacturing/trading activities, the tax auditor should ensure that the inventory records are being kept which would facilitate him in procuring quantitative details of stores, raw material & finished goods

5. There might be cases where objectivity behind enactment of all three sub clauses of clause 9 comes into place for e.g. where the books of accounts have been prescribed but all have not been maintained or where books of accounts are maintained but all of them have not been referred to the tax auditor for examination. Under these circumstances the tax auditor is to ascertain as to how he would conclude whether such a situation warrants any disclosure or qualification.

Clause 10: Presumptive income and relevant section

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

1. The amount of any presumptive profit which is credited to/included in the profit and Loss A/c need be stated alongwith the relevant section.
2. The Section covered here are 44AD, 44AE, 44AF, 44B, 44BB, 44BBA, 44BBB or any other relevant section. The expression 'any other relevant section' means any section which deals with presumptive income and may be enacted in future by principle of ejusdem generis.
3. In case of composite books of account for presumptive income business and other business, expenses to be apportioned as per some reasonable basis on basis of some evidence in possession of the assessee. In case of separate books and non presumptive business turnover being less than specified limit, tax auditor should specify that the report is in respect of the business whose income is assessable on presumptive basis and that the report does not relate to the business assessable under the normal provisions of the Act.

Clause 11: Method of Accounting

- a) Method of accounting employed in the previous year.**
- b) Whether there has been any change in the method of accounting employed vis-a-vis the method employed in the immediately preceding previous year.**
- c) If answer to (b) above is in the affirmative, give details of such change, 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.**

1. The method of accounting employed in the previous year is to be stated. This varies upon the nature of business and profession and also the business organization of the assessee.
2. All companies are required as per section 209(3) of The Companies Act to follow mercantile system of accounting.
3. The hybrid system of accounting has been discontinued w.e.f. A/y 1997-98.
4. An assessee having different businesses may choose different method of accounting for them i.e. cash system for some and mercantile for others. As long as he is following the said different methods consistently and regularly and they result in proper determination of profits of the business, there is no need to change them.
5. The tax auditor is merely to state if there is any change in the method of accounting employed vis-a-vis the same method employed in the immediately preceding previous year or not.

6. In case there is any change in accounting policy, the tax auditor has to determine its materiality. Here also in case it is material, the fact relating to the change in accounting policy and also its effect on the profit and loss is to be stated in financial statements.

7. For the purposes of section 145, vis a vis method of accounting followed by the assessee, the department has notified **IT(AS)-I** relating to **Disclosure of accounting policies** : and **IT(AS)-II** relating to **Disclosure of prior period and extraordinary items and changes in accounting policies**. Accordingly, fundamental accounting assumptions of materiality, going concern, accrual, and substance over form, prudence etc are to be examined. If a fundamental accounting assumption is not followed, such fact shall be disclosed.

149 ITR 759[MAD] Commissioner of Income-tax Vs. Carborandum Universal Ltd.

That the adoption of the direct cost method was bona fide and was a permanent arrangement with the intention to follow the same method year after year, the change would have to be accepted notwithstanding the fact that during the assessment year in question, which was the first year when the change of method was brought about, a prejudice or detriment might be caused to the revenue. As the method of valuation adopted by the assessee had obtained recognition from practicing accountants and the commercial world for valuation of stock-in-trade, the adoption of that method could not be questioned by the Revenue unless the adoption of that method was found to be not bona fide or restricted to a particular year.

202 ITR 789 (BOM) Melmould Corporation v. Commissioner of Income-tax

Whenever there is a change in the method of valuation, there is bound to be some distortion in the calculation of profits in the year in which the change takes place. But, if the change is brought about bona fide and is in accordance with the normally accepted accounting practice, there is no reason why such a change should not be permitted.

Commissioner of Income-tax v. George Oakes Ltd. 303 ITR 357 [MAD.]

When the change of accounting method is bona fide and is recognised in accounting principles, the resultant variation in income cannot be forced to be taxed upon the assessee.

Clause 12: Closing Stock

(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.

1. Here the method employed for valuation of closing stock having regard to the articles or goods dealt in or manufactured by the assessee is to be stated.

2. For ascertainment of the same, reference may be made to the annual financial statements (significant accounting policies) or a management representation may be obtained after duly satisfying himself regarding the method of valuation of closing stock.

3. For Example, it may be stated, wrt method of valuation of closing stock, as under: -3.1 Raw material, at cost or net realizable value whichever is lower3.2 Finished goods at cost or net realizable value whichever is lower4. The term closing stock is to be construed having regard to section 145A and AS-2. Accordingly, closing stock would include raw material, work in progress, spares, loose tools, maintenance supplies, consumables, finished goods etc.5. Section 145A provides for inclusive method of valuation. At the same time AS-2 relating to inventory valuation does not permits inclusive method. Thus all assesseees are to follow AS-2 and make the adjustment here for the purpose of section 145A. Accordingly, there is no need to change the amount of sales, purchases, stock etc in books of accounts. However the adjustments required by section 145A are to be made while computing income for the purpose of return of income.

6. It may be noted that section 145A is tax neutral as long as the assessee makes payment of the duty in accordance with the provisions of section 43B.

7. The Supreme Court held in ALA firm's case (**189 ITR 285**) that when business is discontinued on dissolution, the stock should be valued at market price and the tax auditor may keep the same in mind in suitable cases.

Clause 12A: Conversion of Capital asset into stock in trade 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

The particulars to be stated under new clause 12A should be furnished with respect to the previous year in which capital 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.*

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

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.

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 cost of acquisition and not WDV [in case of depreciable assets]. Even in case of an asset acquired prior to the 1st 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 1st 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).

Under clause (d) the amount at which the asset converted into stock-in-trade should be stated. Such an amount may not be the fair market value 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 such a value. The valuation of stock-in-trade is to be examined with reference to AS-2 – Valuation of Inventories. Non-compliance of AS-2 is to be properly qualified in the main audit report.

However, the date of transfer of conversion is not to be stated.

It is pertinent to mention that the Act and Form 3CD are both silent as to conversion of stock in trade into capital assets, qua taxability and qua reporting. However the said issue has been examined in ITA 6374/ MUM/2004, ACIT v Bright Star Inv P Ltd by Mumbai ITAT.

Clause 13: Amounts not credited to the profit and loss account

(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, 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.

1. The list contained u/s 28 is inclusive and not exhaustive.

2. Amounts not credited to P n L but nevertheless credited to general reserve are to be reported as information is required to be given with reference to the entries in the books of account produced before the tax auditor.

3. The value of any benefit or perquisite derived by a partner or a proprietor whether convertible into money or not, but which has arisen due to the business should be disclosed under this clause. Here the monetary value of free trade trips, gifts, etc received from the companies in capacity as dealers and big traders need be stated. Here the tax auditor may also wish to refer to the latest

CBDT circular wrt pharmaceutical companies and the freebies provided by them to medical practitioners.

4. In order to verify the refunds of excise, sale tax, service tax, customs, VAT, the tax auditor may refer to the relevant returns where such claims have been raised and/or orders of authorities permitting the said claims.

5. The expression admitted as due by the authorities concerned would mean admitted as due within the relevant previous year. However, unilateral claims not admitted by the relevant authorities should not be stated here.

6. Since this clause is exhaustive, particulars of income tax refund need not be stated here.

7. The escalation claims received is based on method of accounting of the assessee. Generally the claims are made in pursuance to a contract, if so permitted. Thus when a claim is made unilaterally or is sub-judice, then they are not to be stated here.

8. Any other item of income would include those receipts which are entered in books of account but are not credited to profit and loss account, and the tax auditor, due to judicial pronouncements, or his professional expertise, is of an opinion that this is to be credited to profit and loss account.

9. While examining all credit items, the tax auditor should give due regard to **AS-9- Revenue Recognition**. 10. The expression Capital receipts may include, Capital Subsidy, Government grants in respect of fixed assets, Profit on sale of fixed assets not passed through profit and loss account, etc. One may refer the following supreme court judgments to understand the fundamental principles distinguishing capital and revenue subsidy, while also referring to AS-12, relating to Accounting for Government Grants: -228 ITR 253 [SC] **Sahney Steel and Press Works Ltd. Vs. Commissioner of Income-tax** 251 ITR 427 [SC] **Commissioner of Income-tax v. Rajaram Maize Products** 306 ITR 392 [SC] **Commissioner of Income-tax v. Ponni Sugars and Chemicals Ltd.**

11. "Capital receipts" for this clause does not cover share capital or item of gift etc. **Clause 14: Depreciation and WDV**

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 case of any addition of an asset, date of put to use, including adjustment 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,

(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.

1. Description/classification should be based on purpose & functions to the assessee & also past assessment history & judicial pronouncements are to be examined. If required seek suitable certificate from technical experts.

2. Determine Rate of depreciation as per Appendix I of Income Tax Rules

3. In case of any dispute between the department & the assessee relating to the ownership, classification, rate of depreciation of the asset, etc the same should be suitably disclosed. The intangible asset should be separately classified and their carrying cost/acquisition cost should be verified.

4. For date on which asset has been put to used, the tax auditor can call for basic records like production, installation details, excise records, power connection, etc. along with management representation. Also due care should be taken for apportionment of deprecation in case of succession, amalgamation & demerger.

a. CENVAT credit on capital goods should be reduced from actual cost. The auditor should verify that the amount of CENVAT credited deducted from cost of capital goods tallies with CENVAT credit account

b. Change in rate of exchange in currency due to fluctuation, incremental liability is to be added/deducted as the case may be (section 43A read with AS-11 amended). Refer **312 ITR 254 (SC) CIT vs. Woodward Governors India Pvt. Ltd.**

c. Capital subsidy & grant is generally received by way of reimbursement and the same, incase is not received in the first year, be deducted in the subsequent year of receipt.

d. The claim of depreciation has now been made mandatory by Finance Act 2001 by over-ruling 243 ITR 056 (SC) CIT Vs. Mahendra Mills Ltd, which laid that depreciation claim is optional.

5. Assessee need not be the registered owner:

The following decisions highlight the fact that the assessee need not be the registered owner of the asset for claiming depreciation.

Mysore Minerals Ltd Vs CIT 239 ITR 775 (SC)

Dalmia Cement (Bharath) Ltd Vs CIT (2001) 247 ITR 267 (SC)

6. Active User Vs Passive User: It is to be noted that under certain circumstances, depreciation is allowable even if the asset is actually not put to use during the year. Reference in this regard can be made to the following decisions:-

Whittle Anderson Ltd Vs CIT (1971) 79 ITR 613 (Bom)

Capital Bus Service (P) Ltd Vs CIT (1980) 123 ITR 404 (Del)

CIT Vs Refrigerators & Allied Industries 163 ITR 498 (Del)

7. Hotel Building is not a plant **CIT Vs Anand Theatres (2000) 244 ITR (SC)**. However the operation theatre of the hospital is a plant **CIT Vs Dr.B.V.Rao 243 ITR (SC)**. Now it is very clear that building etc., will not constitute as plant

8. Depreciation is admissible for trial run of machinery It was held in the case **ACIT Vs Ashima Syntex Ltd., (251 ITR 133 Guj HC)** that when there is commencement of business by way of production of articles it can be said that the assessee is entitled to depreciation.

9. The Punjab & Haryana High Court held that there is a normal depreciation of value even when a machine or equipment is merely kept in storeroom. Thus actual use of the asset may not be the relevant test in all cases. **CIT Vs Pepsu Road Transport Corpn. [2002] 121 Taxman 232.**

10. The Air Conditioner fitted in the bus forms part of integral part and eligible for higher depreciation available for buses **CIT Vs Delhi Airport Service (2002) 255 ITR 91 (Del)**11. In case the business premises of the assessee, purchased by it are situated in commercial buildings/malls, etc, the tax auditor should ensure that the depreciation claimed by the assessee wrt building does not include the amortization on the cost of land, included in the value of building (since in such cases, the assessee also happens to have a proportionate share in the land, underneath).**Clause 15: Amounts admissible under sections 33AB, 33ABA, 33AC, 35, 35ABB, 35AC, 35CCA, 35CCB, 35D, 35DD, 35DDA, 35E:(a) debited to the profit and loss account (showing the amount debited and deduction allowable under each section separately);(b) not debited to the profit and loss account.**

33 AB	Tea Development Account
33 ABA	Site Restoration
33 AC	Reserves for Shipping Business
35	Expenditure on Scientific Research
35 ABB	Expenditure for obtaining Telecom License
35AC	Expenditure on Eligible Project or Schemes
35CCA	Payments to organizations carrying out rural development programme.
35CCB	Payments to organizations carrying out program of conservation of

	natural resources
35D	Amortisation of certain preliminary expenses.
35DD	Amortisation of expenses in case of amalgamation and demerger
35 DDA	Amortisation of expenditure incurred under voluntary retirement scheme
35 E	Deduction for expenditure on prospecting, etc., for certain minerals

1. Also section 35AD should come within the ambit of this section (as introduced wef 01/04/2010).

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

3. The tax auditor should indicate the amount debited to profit & loss a/c & amount admissible as per applicable provisions.

4. The amount not debited to profit & loss a/c but admissible under any of the section mentioned have to be stated.

5. If the assessee is eligible for deduction under one or more of the above section, the tax auditor has to state deduction allowable under each section separately.

Clause 16: Bonus, commission and employees contributions to welfare dues

(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).

1. If an employer would have given dividend or profit share to his employee then it would not have been allowed as an expense, since it is appropriation of profits. Therefore under this clause the auditor is required to ensure that the assessee is not showing dividend/ share in profits paid as bonus or commission which are otherwise deductible. The reporting under Clause 16(a) is applicable in case of companies and partnership firms. For better understanding of this clause, one may wish to refer to the ratio of the following judicial pronouncements: –

a. Dalal Broacha Stock Broking P. Ltd. v. Addl CIT 010 ITR Trib. 0357 (ITAT Mumbai-Spl Bench)

b. AMD Metplast P. Ltd. v. DCIT 341 ITR 563 (DEL).2. By virtue of omission of first proviso to section 36(1)(ii) w.e.f 01-04- 1989 which Provided that the deduction in respect of bonus paid to an employee employed in a factory or other establishment to which the provisions of the Payment of Bonus Act, 1965 (21 of 1965), apply shall not exceed the amount of bonus

payable under that Act; **presently the bonus paid in excess of amount determined/payable under Payment of Bonus Act is also allowable.**

3. The **amount only is to be quantified.** There is **no need to an expression of opinion as to admissibility** or otherwise of the said payment.

4. Under Clause (b) the tax auditor is to state relevant month, the employee contribution to the said welfare funds, the due date of payment under respective statute and the actual date of payment.

5. The date of **clearing of the cheque** should be taken as **date of payment.**

6. The tax auditor need not report as to whether the professional tax deducted by employer from the salary paid to employee has been paid to the credit of the concerned authorities.

7. However, the amount paid under the Welfare fund may be stated under this clause.

307 ITR 363 [DEL] Shriram Pistons and Rings Ltd. Vs. CIT That the “good work reward” that was given by the assessee to some employees on the recommendation of senior officers of the assessee did not fall in any of the categories of bonus specified under the industrial law. There was nothing to suggest that the good work reward given by the assessee to its employees had any relation to the profits that the assessee may or may not make. The reward had relation to the good work done by the employee during the course of his employment and at the end of the financial year on the recommendation of a senior officer of the assessee, the reward was given to the employee. Consequently, the “good work reward” could not fall within the ambit of section 36(1)(ii) of the Income-tax Act, 1961. The “good work” reward was allowable as business expenditure under section 37(1) of the Act.

Clause 17: Amounts debited to Profit and loss Account

17. (a) Expenditure of Capital Nature

- **Discount on Debenture is Revenue Expenditure Madras Industrial Investment Corporation vs. CIT- 225 ITR 802 (SC)** (Deferred deduction possible)
- Expenses by way of **stamp duty & registration for issue of bonus share** are revenue expense **CIT vs. General Insurance Corp. 286 ITR 232 (SC)**
- Expenses on **issue of shares is capital expense Brooke Bond India Ltd. vs. CIT 225 ITR 795 (SC)**
- **Professional charges towards** services rendered in connection with **amalgamation** were in course of carrying on of assessee's business and thus revenue expense. **Bombay Dying & Manufacturing Co. Ltd. vs. CIT 219 ITR 521 (SC)**

17.(b) Expenditure of Personal Nature

In case of a Company, no partial disallowances for use of vehicles, telephone etc. by the directors can be made. **Sayaji Iron & Engg. Co. vs. CIT 253 ITR 749 (Guj) also 254 ITR 673,**

268 ITR 502, Haryana Oxygen Ltd. vs. CIT 76 ITD 038 (Del), B.S Agricultural Industries India vs. ITO 50 TTJ 295 (Del).

Also Required as statutory auditor to state any personal expenses debited to profit and loss account—section 227 of The Companies Act.

Obtain specific management representation that no personal expenses have been debited to profit and loss account.

17.(c) Advertisement In Publication Of Political Parties

Expenditure on advertisement in souvenirs, brochures etc. published by political parties are specifically disallowed under section 37(2B)

17.(d) Expenditure incurred at Clubs

- Payment to clubs would not include organization such as Rotary, Lions, Jaycees, and Giants etc., they being service organization.
- Payments made through credit card are to be examined so as to ascertain whether any expense incurred could be treated as perquisite in the hands of the person concerned.
- Information may be given separately in respect of entrance fees, subscription & cost of club services.

17.(e) Penalty

- Where a statutory impost is levied, it is to be studied to find whether impost is compensatory or pnal or composite and deduction is to be allowed wholly or partly to the extent the impost is wholly or partly compensated **Swadeshi Cotton Company Ltd. vs. CIT 233 ITR 199 (SC). Also Prakash Cotton Mills Pvt. Ltd. vs. CIT 201 ITR 684 (SC), Malwa Vanaspati & Chemical Co. vs. CIT 225 ITR 383 (SC).**
- Amount paid at option of assessee under law or statutory scheme is not penalty **CIT vs. Mihir Textile Ltd. 205 ITR 163 (SC).**
- Expense incurred in transaction carried out in violation of provisions of FERA (now FEMA) **Maddi Venkta Raman & Co. Ltd. vs. CIT 229 ITR 534 (SC).**
- SEBI Regularisation Scheme providing one-time opportunity to defaulters for regularising default is Incidental to carrying on business. The same is not penalty or akin to penalty. **Kaira Can Co. Ltd. V DCIT 002 ITR [TRIB.] 020 [Mum]**
- **Master Capital Services Ltd. v. DCIT [ITA No. 364/Chandi/2006; A.Y. 2002-03] (26-02-2007)**, it was held that the fines paid by share brokers for violation of BSE/NSE (Stock Exchange) rules (e.g. for trading volume crossing fixed exposure limit, for late submission of margin certificates or for late deliveries of shares due to non-matching of signatures etc.) are not fines paid for infraction of any statute/law and are allowable under section 37(1).

17.(f) Amount inadmissible under section 40(a)

- While quantifying the amount inadmissible under section 40(a)(ia), the tax auditor is to examine the TDS compliance made by assessee through proper returns, challans, records etc. Also the particulars stated here must correspond to Clause 27 also.
- In case of large assessee, TDS compliance may be checked on test check basis also.
- Where TDS has been deposited belatedly it is to be seen that the same is being deposited with interest as stated u/s 201(1A), else the same would amount to non-deposition of TDS wholly and liable for disallowance.
- FBT, income tax, wealth tax, tax on behalf of employee referred under section 10(10CC) are not allowable.
- Also STT is now an eligible deduction upon omission of section 40(a)(ib). However, only state that STT which is in respect of sale and purchase of securities as a dealer and not as an investor.
- **Interest on OD for payment of income tax** is not allowable expense under section 40, **East India Pharmaceutical Works Ltd. vs. CIT 224 ITR 627 (SC)** also **Bharat Commerce & Industries vs. CIT 230 ITR 733 (SC)**.

17.(g) Interest, salary, remuneration, etc inadmissible u/s 40(b) and its calculations

- The tax auditor may refer to the instrument of partnership or AOP to ascertain whether the same authorizes the payment of interest, remuneration, etc to the partners/members.
- Workings may be done keeping in mind new slab rates brought in by Finance Act, 2009 effective 1-4-2010.

17.(h) Payments for expenditure not made through account payee cheque or drafts

- Constructive payments made through banking channels by way of any RTGS, NEFT, E-payment etc. are to be taken as not violative of section 40A(3) as they are in pari materia to the object behind the enactment of the said section.
- The expression expenditure must be understood in its plain meaning to include expenditure for stock in trade & raw material (**Attar Singh Gurmukh Singh vs. ITO 191 ITR 667 (SC)**)
- Amendment by Finance Act 2009 entire payment or aggregate payments, to a single person in a day, if not made through a/c payee cheques or draft, and exceeding Rs. 20000/-, shall be disallowed. For payment for hiring or leasing goods carriages, the limit is made Rs. 35000/-
- Case of Aloo Supply company of Orissa HC now of academic interest as provision changes to aggregate of all payments made in single day.
- If payment have been in contravention of section 40A(3) but are covered by rule 6DD, the particulars of the same should be stated by the tax auditor.
- The certificate relating to compliance with the provisions of section 40A(3) may be obtained from the management through management representation.

17.(k) Liability of Contingent nature

The present value of contingent liability, like warranty expense, if properly ascertained & discounted on accrual basis is allowable **CIT vs. Wipro GE Medical Systems Ltd. 314 ITR 062 (SC).**

17.(l) Deduction inadmissible u/s 14A

The Supreme Court decision in **Rajasthan state warehousing corporation (242 ITR 450)** after which section 14A was brought on books to the effect that in case of indivisible business having tax free and taxable income, no disallowance can be made on proportionate basis and entire expense is allowable. — **Dhanlakshmi Bank Ltd. 12 SOT 625 (Cochin).**

What is the Logic behind enactment of section 14A(2), (3)?

Extracted from Clause 11 of circular no.14/2006 dated 28-12-2006

“In the existing provisions of section 14A, no method of computing the expenditure incurred in relation to income which does not form part of the total income has been provided for. Consequently, there is considerable dispute between the taxpayers and the Department on the method of determining such expenditure.”

Is disallowance u/s 14A to be made even if no exempt income?

Disallowances under section 14A is to be made even in a year in which the assessee has no tax free income. **Cheminvest Ltd. vs. ITO (Delhi ITAT Special Bench unreported till date).** This is in consonance with Rule 8D(2) (iii). Rule 8D is also invited under those cases, where the assessee claims that no expenditure has been incurred by it for the purpose of any income which does not form part of the total income [section 14A(3)].

However a **Contradictory view has been taken by Chennai Bench of ITAT**, in **M/s. Siva Industries & Holdings Ltd. vs. ACIT, ITA. No. 2148/MDS/2010**, Vide order dated 20.05.2011 and has observed that “For the applicability of s. 14A there must be (a) taxable income and (b) tax-free income. If either one is absent, s. 14A has no applicability. If it is assumed that s. 14A would apply even when the assessee does not have tax-free income, the expenditure would get disallowed year after year so long as the assessee held the shares and if he sold them and made a capital gain that would be taxed as well. This is not contemplated by s. 14A. If there is no claim for tax-free income, there cannot be any disallowance u/s 14A.”

Furthermore, recently **Delite Enterprises** case, the Bombay High court have taken a view that in case where there was no exempt income, the disallowance u/s 14A is not warranted.

Whether there is any bar on reopening completed assessments by CIT(A) and ITAT?

ITAT cannot remand back the matter to AO for making disallowance under section 14A- **Top Star Mercantile vs. ACIT (Bombay High Court).** ITAT Delhi Special bench judgement in the case of **Aquarius Travels Pvt. Ltd. (111 ITD 053)** on interpretation of proviso to section 14A, and laying that CIT (A) and ITAT can suo motto or upon a specific ground being raised by any

party in case of a pending appeal, in r/o A/y 2001-02 and earlier years, consider applicability of Section 14A, impliedly overruled

What is the extent and scope of Subsection (2) & (3) of section 14A?

Explained by **ITAT Mumbai Special Bench in the case of ITO vs. Daga Capital Management Private Ltd. (117 ITD 169 Mumbai)**

1. Section 14A(2) & 14A(3) being procedural are retrospective. The intention behind given expression in relation to in section 14A is to encompass not only direct expenses but also indirect expenses which has any relation to exempt income.

2. Section 14A would be applicable where shares are held as stock in trade.3. Expenditure relating to incidental exempt income is also not immune from operation of section 14A(The BHC vide its judgement dated 12-Aug-10 in **Godrej and Boyce Mfg. Co. Ltd. v/s DCIT 328 ITR 081** laid out following principles on interpretation of SECTION 14A and Rule 8D(a) the mandate of section 14A is to prevent claims for deduction of expenditure in relation to income which does not form part of the total income of the assessee ;

(b) section 14A(1) is enacted to ensure that only expenses incurred in respect of earning taxable income are allowed ;

(c) the principle of apportionment of expenses is widened by section 14A to include even the apportionment of expenditure between taxable and nontaxable income of an indivisible business ;

(d) the basic principle of taxation is to tax net income. This principle applies even for the purposes of section 14A and expenses towards non-taxable income must be excluded ;

(e) once a proximate cause for disallowance is established-which is the relationship of the expenditure with income which does not form part of the total income-a disallowance has to be effected.

The SLP filed against the above judgement of the Bombay High Court is pending before the Apex Court S.L.P. (C) No.36516 of 2010 wherein on 10/01/2011, a constitution bench comprising of Three Judges (incl The CJI) have Ordered to Issue notice but refused to grant and ad-interim stay.

Under amended section 14A read with Rule 8D, burden of proof of earning of exempt income/incurrence of expenditure in relation thereto on whom?

It is for the AO to demonstrate that expenditure was incurred by assessee in relation to income not includible in total income. Section 14A(2) (if AO is not satisfied....) (also refer to the Judgement of Delhi High Court in case of Maxopp Investments to bring home the ratio of the expression ‘satisfaction/ recording of reasons by the AO’

Normally the disallowance under section 14A read with rule 8D would be **determined only upon assessment** that is much after tax audit is completed and return filed. Therefore the tax auditor, at the time of tax audit, will have to **verify the amount of inadmissible expenditure determined by the assessee.**

The **primary responsibility** to furnish the detail of expenses incurred in respect of exempt income is on the **assessee.**

The method for computation of disallowance under **Rule 8D is mandatory for the AO only.** Accordingly the assessee may or may not adopt the same.

Interest which is directly attributable to non taxable income and also such interest which is attributable to taxable income must both be deducted out of the total interest paid while arriving at Variable A as referred in Rule 8D(2)

An interesting judgement on the issue whether disallowance u/s 14A is exigible incase the assessee is claiming deduction under chapter VI-A or not, could be referred in case of **Punjab State Co-operative Milk Producers Federation Ltd. v. CIT (No. 1) [2011] 336 ITR 495 (P&H)**, wherein the answer has been given in favour of the revenue.

17.(m) Amount inadmissible under proviso to section 36(1)(iii)

Commitment charges paid in respect of loan taken for establishing new project are in nature of interest and allowable as business expenses **DCIT vs. Gujarat Alkalies and Chemicals Ltd. 295 ITR 085 (SC)**

If the assessee can show that interest free advance to relative or sister concern has been commercial expediency and is for the purpose of business, no disallowance can be made under section 36(1)(iii) **S.A. Builders vs. CIT 288 ITR 001 (SC)**. Also **Dalmia Cement Bharat Ltd. 254 ITR 377 (Del)** stating that no businessman need be compelled to maximize his profit.

Burden of Proof on Whom

Munjal Sales Corporation v. CIT 298 ITR 298 [SC]

Under the Income-tax Act, 1961, after amendment of the Act by the Finance Act, 1992, in order that interest paid on borrowings can be allowed as a deduction in computing the business profits, every assessee, including a firm, has to establish, in the first instance, that it was allowable under section 36(1) (iii);

Clause 17A: Amount of Interest Inadmissible u/s 23 of the MSMED Act, 2009

Detailed discussions are appearing as per ICAI Guidance Note on the same. The Tax auditor is required to obtain a specific management representation from the assessee on this aspect.

Clause 18: Particulars of payments made to persons specified under section 40A(2)(b).

1. The object behind this section is to ensure that the related parties do not get unreasonably or excessively paid by virtue of being related to the assessee in one way or the other on account of purchases/supplies made or services rendered.
2. List of related party is to be procured from the assessee by way of management representation or last year form 3CD.
3. Only payments made to related parties are covered & not sales/services rendered made to them.
4. The auditor is merely to state particulars of related parties, amount paid to them & their relation. He is not required to quantify whether the payment is reasonable or otherwise
5. Inapplicable to income – goods sold to associates at lower than the market price-section 40A(2) not applicable-123 ITR 592(Mad), 139 ITR 827(MP)
6. Ultimate Burden to prove upon revenue-Circular 6P DT 06-07-1968. However, assessee to discharge onus at first instance.

261 ITR 258 (MUM) Commissioner of Income-tax Vs. Shatrunjay Diamonds

Under Section 40A(2)(b) the Burden of proof is on assessee to prove that price is reasonable.

M.L.B.D. Books International vs. ACIT (ITA 374/2009) order dated 31.03.2009

The fair market value had to be discerned by keeping in mind a similarly circumstanced person.

Clause 19: Amounts deemed to be profits and gains under section 33AB or 33ABA or 33AC.

1. The items are similar to those stated in clause 15 except to the effect that whereas under clause 15, the admissible deduction is to be computed, under this clause, the notional profit attributable to withdrawal of amount from the specified reserve is stated.
2. So far as section 33AC relating to shipping business is concerned, as per amendment by Finance Act 2004, no further deduction shall be available. **Clause 20: Any amount of profit chargeable to tax under section 41 and computation thereof.** 1) Assessee previously claimed deduction of any expenditure, loss or trading liability and during the year any benefit derived by way of remission and cessation (write off) of such trading liability. 2) If assets are sold during the year, consideration of such assets is more than the WDV, amount above WDV up to the extent of Depreciation allowed (Acquisition Cost – WDV) will be treated as business income.
- 3) Assets used as scientific research and subsequently sold out without using in business for some other purpose. Net proceeds of such assets up to the depreciation allowed will be treated as business income.

4) Withdrawal of amount from specified reserve created under 36(1)(vii)

Clause 21: Tax, cess, fees, duty, interest

(i) 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.

Under clause 21 (i)(A), the liability towards sums stated u/s 43B which existed on the first day of the previous year need be stated.

The date of payment under the PF Act shall be the date of clearing.

If amounts are unpaid upto the date of tax audit report and are paid subsequently, the same may be claimed through a separate CA certificate.

[2009] 313 ITR 0161- Commissioner of Income-tax vs. P. M. Electronics Ltd. (Delhi High Court)

Provident fund contributions made before filing return—allowable— income-tax act, 1961, s. 43b.

CIT v. Dharmendra Sharma [2008] 297 ITR 320 (Delhi) CIT v. Vinay Cement Ltd. [2009] 313 ITR (St.) 1

CIT v. Nexus Computer P. Ltd. [2009] 313 ITR 144 (Mad)

Important : – please note that following the decision of the Delhi HC in case of P.M. Electronics, the Delhi ITAT bench in case of ACIT v/s Consulting Engg. Services Pvt. Ltd. ITA No.3823/Delhi /2008 held that even the employees contribution to welfare funds are covered by amendment to section 43B wef 1-4-2004, which is an incorrect appreciation of the law.

Payment made before the grace days allowed under the Provident Fund Act and Rules should also be considered as payment made within the due date under Section 43B(b) of the Income Tax Act, 1961.

M/s Hunsur Plywood Works Ltd Vs CIT (1996) 54 TTJ 260 (Bang.)

CIT Vs Shri Ganapathy Mills Company Ltd. (1999) 243 ITR 879 (Mad.)

Commissioner of Income-tax Vs. Salem Co-operative Spinning Mills Ltd. 258 ITR 360(Mad.)

Hitech (India) Pvt. Ltd. Vs CIT 227 ITR 446. (AP)

Such matters should not arise after the liberalisation in respect of such payments by amendment to section 43B by the Finance Act, 2003 with effect from April 1, 2004. and are merely of academic interest now.

[2009] 118 ITD 535 (HYD.) Assistant Commissioner of Income-tax, Circle 3(4) v. GMR Holdings (P.) Ltd.

Turnover fee to SEBI is covered by to 43B. Adjustment of amount against security deposit by the assessee is not payment

[2009] 118 ITD 401 (MUM.) Air India Ltd. v. Deputy Commissioner of Income-tax,

Foreign travel tax is covered by 43B

[2009] 116 ITD 186 (PUNE) Alfa Laval India Ltd. v. Deputy Commissioner of Income-tax

Based on enquiry report, ESI authorities issued demand notices dated 16-6- 2000 and 29-5-2000 to assessee for liabilities of assessment years 1996-97 and 1997-98. Assessee paid amount on 29-6-2000. Whether since liability in question did not accrue in financial year relevant to assessment year in question, assessee was not entitled to deduct said amount while computing its income for assessment year.

[2008] 306 ITR (A.T.) 0106- Assistant Commissioner of Income-tax vs. Real Image Media Technologies P. Ltd. (Income-tax Appellate Tribunal-Chennai)

Deduction of business expenditure is allowed on actual payment. Assessee is liable to make payment only on received payment and not entitled to claim deduction on account of service tax. Held that section 43 B is not applicable in case of assessee, no addition shall be made.

[2007] 107 ITD 343 (chd.) (SB) Deputy Commissioner of Income-tax Circle 4(1) v. Glaxo Smithkline Consumer Healthcare Ltd.

For claiming deduction under section 43B, in respect of payment of excise duty, it is not necessary that liability to pay duty must be incurred first and only thereafter, payment of such duty is made. Therefore, deduction for tax, excise duty, etc., is allowable under section 43B on payment basis before incurring liability to pay such amounts. However, unexpired Modvat Credit available to an assessee is in nature of a future entitlement which cannot be considered equivalent to actual payment of central excise duty. **Accordingly, unexpired Modvat Credit available to an assessee on last day of previous year would not be eligible for deduction under section 43B.**

[2007] 289 ITR 0154- Shree Pipes vs. Deputy Commissioner of Income-tax (Assessment) (Rajasthan High Court)

Deduction of Business Expenditure is allowed only on actual payment. Interest on arrears of sales tax is a part of sales tax for section 43B. Therefore, interest not deductible unless actually paid

Mewar Motors v. CIT [2003] 260 ITR 218 (Raj)

[2009] 308 ITR 0234- Commissioner of Income-tax vs. Official Liquidator of Essab Computer P. Ltd. (Gujarat High Court)

Circular No. 496, dated September 25, 1987, the Board made it clear that if the sales tax due to the Government was converted into a loan which may be repaid by the assessee subsequently in instalments, the Department shall treat the sales tax dues as actually paid for all purposes.

Sales tax liability converted as loan under deferred payment scheme– disallowance under section 43b by assessing officer while processing return under section 143(1)(a)–cbdt circular that sales tax liability converted into loan may be allowed as deduction in year in which conversion permitted by government order–additional tax cannot be levied–income-tax act, 1961, ss. 43b, 143(1)(a), (1a)–cbdt circular no. 674 dated 29-12-1993.*

Whether the conversion of interest due into term loan can be considered as payment u/s 43B?

Madras High Court in Kalpana Lamp and Components Ltd., (2002) ITR 491 (MAD) can not be allowed as payment. It is also not part with the sales tax loan allowed by the state Government. Also refer to **Explanation 3C**.–For the removal of doubts, it is hereby declared that a deduction of any sum, being interest payable under clause (d) of this section, 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 borrowing shall not be deemed to have been actually paid.

Clause 22: Treatment of MODVAT claim and Prior Period Income/ Expenditure

(a) Amount of modified 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 modified 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.

1. It requires factual reporting of CENVAT credit & is to be read along with clause 12(b) of form 3CD. The auditor should check relevant statutory records i.e. RG 23 (both parts), Account Current & records maintained under CENVAT Credit Rules.
2. Since CENVAT credit availed & utilized are to be reported, it is advisable to report the opening & closing balance of CENVAT also to avoid any misleading conclusion and inferences. The treatment of CENVAT Credit in profit & loss and outstanding CENVAT credit in account has to be reported. (this may be referred through section 145A)
3. Separate disclosures may be reported for CENVAT credit on capital goods and other than capital goods.
4. In sub-clause (b), the particulars of prior period income or expense as debited or credited to profit & loss a/c are to be stated.
5. This clause becomes inapplicable in case of an assessee following cash system of accounting as per point no. 11(a). Where however the method of accounting is accrual & accounts are audited under any other Act, then reference may be made to disclosures/ Notes to accounts attached with financial statements.
6. The AS (IT)-II relating to prior period items & extra-ordinary items has been notified by government under section 145.

280 ITR (A.T.) 0194 (DEL.) Deputy Commissioner of Income-tax Vs. Indag Rubber Ltd.

That in a case where any liability or receipt had accrued but was not quantified, the assessment is to be made on the basis of the date of accrual in a case where the mercantile system of accounting is applicable. The accrual of liability or income is not postponed for want of quantification. In such cases, if at the time of assessment or appellate proceedings, the quantified amount becomes known, the same should be made part of the relevant assessment. The assessee was disputing the liability itself and not merely the quantum thereof. The doctrine of hindsight cannot affect the date of accrual of liability or, as the case may be, income. Thus, the doctrine of hindsight had no application.

243 ITR 35 (Mad) CIT Vs Anna Transport Corporation Ltd

When an assessee is following the mercantile system of account, it cannot possibly make a provision in its accounts, unless the liability had accrued. When the assessee is not in a position to determine the existence of liability, let alone the quantification thereof, the assessee cannot be penalised for not making a provision in the earlier years.

Clause 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].

1. Where any amount is borrowed on a hundi from a person, or any amount due thereon is repaid to any person, otherwise than through an account payee cheque drawn on a bank, the amount so borrowed or repaid shall be deemed to be the income of the person borrowing or repaying the amount aforesaid in the P.Y. in which the amount was borrowed or repaid, as the case may be. However, in case the amount borrowed under this section has been deemed as income of the borrower, then the borrower shall not be liable to be assessed again in respect of such amount under this section on repayment of such amount.

2. It is advised to get a copy of complete list of hundi loans obtained by a mode other than account payee cheque and verify the same with books of account. Where it is not able to get all the relevant details, proper reporting should be there.

Clause 24 Particulars of each loan and deposit accepted/repaid in an amounting exceeding limits as per section 269SS/269T

Difference between Loan and Deposit

In A. M. Shamsudeen v. Union of India [2000] 244 ITR 266 (Mad), that in a loan, it is the duty of the debtor to seek the creditor and repay the money to him, while in the case of deposit, it is generally the duty of the depositor to go to the depositor to make a demand for repayment.

Baidya Nath Plastic Industries (P.) Ltd. v. K.L. Anand, ITO [1998] 230 ITR 522 (Delhi)

There is a distinction between a loan and a deposit. In the case of a loan, it is the duty of the debtor to seek the creditor and repay the money to him or to repay the money according to the agreement. But in the case of a deposit, it is generally the duty of the depositor to go to the banker or the person with whom the money is deposited, and make a demand for the repayment of the same.

Loans and deposits by means of transfer entries otherwise than by an account payee cheque/draft have to be reported under this clause.

Transfer Entry and their scope

CIT Vs Noida Toll Bridge Co. Ltd 262 ITR 260 (Del)

Where the transaction was by an account payee cheque and the transaction was made by the assessee through ILFS, by journal entry in the books of account of the assessee by crediting the account of ILFS, held no violation u/s 269SS

[2001] 78 ITD378 (Jp.) Assistant Commissioner of Income-tax v. Jag Vijay Auto Finance (P.) Ltd.

Where deposits were accepted by assessee-company through transfer vouchers from depositors who had bank accounts in same bank in which assessee-company had its accounts – and the amounts in question were credited in company's bank account through proper banking channel, Held that there was no violation of provisions of section 269SS in any manner.

[2004] 3 SOT 811 (Ahd.) Assistant Commissioner of Income-tax v. Gujarat Ambuja Proteins Ltd.

Where there was no actual receipt of money by assessee-company and amounts were credited by journal entries on account of payments made by its sister concern for and on behalf of assessee-company, held that the AO was not justified in holding that assessee had taken those deposits in violation of section 269SS. Thus, penalty under section 271 D was rightly deleted.

[1996] 56 TTJ 580 (AHD) BOMBAY CONDUCTORS & ELECTRICALS LTD. v. DEPUTY COMMISSIONER OF INCOME-TAX

Assessee had purchased goods from its holding company and while it paid part purchase price by account-payee cheque, for rest of purchase price it made adjustment in its books of account by transferring equivalent amount from 'goods purchase account' to 'Sarafi account' standing in holding company's name. Held that, such adjustment could not be held to be 'deposit' or 'loan' within meaning of section 269SS and penalty u/s 271 B was not exigible.

[2004] 3 SOT 162 (Ahd.) Premier Art Silk Processors (P.) Ltd. v. Deputy Commissioner of Income-tax

Where the assessee had made repayments to several depositors in cash due to low creditworthiness and credibility of company which was not favourable to creditors. On account of such situation creditors were insisting upon payments being made in cash only and they were not accepting cheque or draft. Held that such repayment of loan or deposit in cash with a view to meet urgent business necessities and such payments made under bona fide belief is a valid excuse and constitutes a reasonable cause within meaning of section 273B and in such a case no penalty is leviable.

RTGS, NEFT, High Value, A/c Transfer, etc. are constructive payments made through bank accounts and are to be viewed liberally in view of the object behind enactment of section 269SS/269T. Also finds support from the ICAI guidance note.

Interest free loans are also loans.

For violation of Sec 269SS and Sec 269T, Sec 271 D and 271 E provides penalty, respectively, for an amount equivalent to loan accepted or repaid. However, if there is a reasonable cause then penalty may not be levied.

Clause 25 Brought forward losses and change in shareholding of Companies

(a) Details of brought forward loss or depreciation allowance, in the following manner, to the extent available:

Sl No.	Assessment	Nature of Loss/	Amount	Amount	Remarks
	Year (s)	Allowance	as	Assessed	
			Returned	Give ref to relevant orders	

(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 Sec 79;

1. The amount to be tabulated is required to be quantified as per return and assessment/appellate orders.
2. The format is for standardization & can be amended to incorporate relevant information.
3. Separate statements in prescribed format can be prepared if more than one type of loss/allowances is carried forward for same assessment year.
4. In the remark column information about the pending assessment or appellate proceedings or delay in filing loss returns (section 139(3)) may be given.
5. In case where the assessments are in various stages of litigation, details may be given unto the stage till which orders have been passed and the factual position relating to pending litigation may be given by way of remark.
6. In case of corporate assessee, where CARO is applicable, details of pendency before various may be cross verified.
7. Clause (b) relates to carry forward & set off of losses in case of companies and is not applicable to companies in which public is substantially interested.
8. Section 79 is non obstante chapter VI and dilution of shareholding from 51 % will not effect the provisions of section 32(2) relating to set off & carry forward of unabsorbed depreciation and **CIT vs. Concord Industries Ltd. 119 ITR 458 (Mad).**
9. 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 year.
10. The above comparison of the shareholding can be done by referring to the register of members.

11. Section 79 is inapplicable in case of change in voting power takes place either due inheritance or on account transfer of shares by way of gift to any relative of the shareholder.

Clause 26: Section-wise details of deductions, if any, admissible under Chapter VI-A.

The deduction available under chapter VIA may be categorized as follows

A. Deduction in respect of certain payments.

B. Deduction in respect of certain incomes

C. Other Deductions

1) Only those deductions are required to be stated for which either the expense of the income is recorded in books of accounts. In case, LIC is paid outside the books of accounts, the same is not to be stated. 2) The deduction available to the assessee is subject to his GTI, which the tax auditor may not be aware. In such cases the tax auditor should put a note that the deduction is subject to determination of GTI of the assessee.

3) If the deduction computed by assessee and the tax auditor are different due to judicial pronouncement or interpretation, the fact is to be stated

4) In case of deduction in respect of payments/incomes, the tax auditor should ascertain whether there is corresponding expenditure/income covered by the relevant section recorded in the books audited by him.

Clause 27. Compliance with TDS

(a) Whether the assessee has complied with the provisions of Chapter XVII-B regarding deduction of tax at source and regarding the payment thereof to the credit of the Central Government. [Yes/No]

(b) If the provisions of Chapter XVI I-B have not been complied with, please give the following details, namely:

(i) Tax Deductible and not deducted at all

(ii) Shortfall on account of lesser deduction than required to be deducted

(iii) Tax deducted late

(iv) Tax deducted but not paid to the credit of the Central Government (Please give the details of cases covered in (i) to (iv) above)

1. The new clause 27 is different from the earlier clause. In the earlier clause the requirement was with reference to the tax deducted at source but not paid to the credit of the Central

Government in accordance with the provisions of chapter XVIII-B. The new clause requires reporting on the compliance with the provisions of chapter XVIII-B regarding deduction of tax at source and payment thereof to the credit of the Central Government. Thus, the scope of reporting under the new clause is much wider. This reporting requirement is to be read with the specific non-compliances stated under clause (b).2. Since the old as well amended section relates to chapter XVII-B, details of any non compliance relating to TCS (covered by chapter XVII-BB) are not to be stated.

3. This clause may be read with clause 17(f) and corresponds to 40(a) (ia)

4. In case where the assessee submits that tax is not required to be deducted on any payment the tax auditor may exercise his judgement in light of applicable law/judicial pronouncement and in case of difference of opinion both the view points should be stated. Whereas the primary reporting responsibility relating to compliance with provisions of chapter XVII-B, the primary responsibility to prepare the information in such manner so that tax auditor can verify the compliance is on the assessee

5. In case of large organization it is in their interest to get separate and independent audit conducted in respect to TDS.

Clause 28: Quantitative details of principle items in case of trading and manufacturing concerns

1. Quantitative details are to be given only of principal of goods. What would constitute principal item would depend upon facts of each case however items which constitute more than 10% in value of the aggregate purchase consumption or turnover may be classified as principal items.

2. Petty items need not be stated. In case of non corporate assessee the tax auditor should management representation certified documents for principal items of raw materials, finished goods and by-products:

3. Certificate from the assessee certifying the balance of the opening stock, purchases, sales and closing stock.

4. Certificate to the extent of shortage/excess/damage and the reasons thereof.

5. In the case of an assessee engaged in the manufacture of goods where the input of raw materials and the output of finished goods are recorded in different units of measurement, unless an alternative method is available for conversion of the end product into the same unit of measure, the yield and shortage cannot be ascertained. In some cases where the end product is standard item and can be converted back and related to the input of the raw material in the same unit of measurement, the same should be done to ascertain the shortage, yield etc. In case it is not possible, the fact should be so stated under this clause.**Clause 29: 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) total tax paid thereon;

(c) dates of payment with amounts.

1. Dividend means dividend as defined under section 2(22) excluding deemed dividend under section 2(22)(e).
2. The amount of dividend declared, paid or distributed whether out of current profits or accumulated profits shall be subject to dividend distribution tax @ 15% plus education cess and secondary Higher Education Cess
3. The auditor is not to see the determination of the distributed profits but is to state the amount of profits which he may refer from minutes books.
4. Under clause (b) the tax payable on distributed profit is to be determined and reduced in case any dividend is received by a domestic company from its subsidiary which has paid DDT and recipient company is not a subsidiary company of any other company (section 11 50(1A))
5. Under clause (c) the particulars of the DDT deposited are to be stated that is date of payment and amount of DDT deposited.

Clause 30: Whether any cost audit was carried out? if yes, enclose a copy of the report of such audit [see section 139(9)].

1. The tax auditor has to state if cost audit was carried out and if the answer is in affirmative, he has to attach the copy of the same.
2. The tax auditor is not required to make detailed study of the cost audit report however he has to take note of any material observation having relevance to tax audit.
3. Where the cost audit has been ordered but is not completed by the time of tax audit report, the fact relating to same is to be stated.
4. Information is required to be given only in respect of such cost audit whose time period corresponds to the previous year under tax audit.
5. Even though cost audit report is required to be filed along with income tax return (section 139(9)(e)) which failure would render the return as defective, the annexure less return forms bars any document to be accompanied with the return. Under these circumstances it is advisable that the cost audit report may be furnished before the AO by way of letter.

Clause 31: Whether any audit was conducted under the Central Excise Act, 1944, if yes, enclose a copy of the report of such audit.

1. The tax auditor has to state if any audit was conducted under the Central Excise Act, 1944 and if the answer is in affirmative, he has to attach the copy of the same.

2. The tax auditor is not required to make detailed study of such audit report however he has to take note of any material observation having relevance to tax audit.
3. Where the audit has been ordered under central excise but is not completed by the time of tax audit report, the fact relating to same is to be stated.
4. Information is required to be given only in respect of such excise audit whose time period corresponds to the previous year under tax audit.

Clause 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.

1. The ratios are to be given for assessee engaged in manufacturing or trading activities and not to professionals.
2. Computation of various components based upon which ratios have been worked out is required to be stated under this clause
3. There should be consistency between the numerator and denominator while calculating the ratios
4. The ratios have to be given for the business as a whole and not product wise
5. While calculating the ratios, the tax auditor should assign meaning to terms used in the above ratios having regard to GAAP
6. The net profit to be shown is NPBT
7. In case of partnership firm the NP ratio has to be calculated after charging interest and remuneration to partners.
8. The stock turnover ratio is to be computed while taking only finished goods.

ANNEXURE -I

PART A

Clauses 1 to 6 – These are just the same as of part A of form 3CD and have already been deliberated upon in earlier part of the discussion paper.

PART B

Nature of Business

The nature of business or profession must be same as in form 3CD [refer cl. 8(a)]. The code must correspond to the relevant code as per the list. In case the code is not specific one, the residual code pertaining to the main activity may be stated.

1. Paid-up share capital/ Capital of Partner/Proprietor The Paid up capital as per the balance sheet is to be stated in case of Corporates.

There is no need to state the Authorised Capital.

In case of non corporates, the expression may be construed to mean capital contribution made by the sole proprietor or the partner as the case may be.

2. Share Application Money/ Current account of Partner/ Proprietor This clause is applicable only for corporates. The amount received as share application must be stated hereunder.

3. Reserves and Surplus/ Profit and Loss Account

Means portion of earnings appropriated by the management for General or for specific purpose other than provisions for depreciation or diminution in the value of asset or for known liability

The Tax Auditor may also refer to part III of Schedule VI of The Companies Act, in this regard too.

Incase of non corporate assesseees, besides the reserves, un-appropriated balances of the profit and loss account of the partner/proprietor should also be disclosed.

4 & 5. SECURED LOANS & UNSECURED LOANS

There is no requirement to give individual bifurcation of each secured/ unsecured loan.

Only the aggregate quantum of the same is to be disclosed.

Secured Loans are those, which are secured wholly or partially against an asset. Whereas, an unsecured loan is a one, which is not a secured loan.

The details of assets/guarantees given for secured loans need not be stated.

7. Total of Balance Sheet

Incase of corporate assessee's and those whose accounts are required to be audited under any other act, requiring the audit report in form 3CA, the tax auditor must ensure that the total of the balance sheet annexed with his tax audit report must be stated here.

Incase of Audit report in Form 3CB, the total of balance sheet, on which the tax auditor is giving his opinion, is to be stated.

9. Gross profit

The gross profit computed for working out the GP ratio as per cl 32[a] of form 3CD must be stated here.

10 & 11. Commission received & Commission paid

The Gross amount of commission received and gross commission paid must be stated here. The intention of the legislature seems to be verification of the amount claimed/compliance with provisions of section 194H of the Act.

12 & 13. Interest received & Interest paid

The Gross amount of interest received and gross interest paid must be stated here. The intention of the legislature seems to be verification of the amount claimed/compliance with provisions of section 194A of the Act. Where the assessee has received and paid interest to a same party, during the year, instead of net interest gross amount is to be stated.

14. Depreciation as per books of account

The amount of depreciation debited in the books of accounts is to be stated. The Tax auditor is not required to comment here as to whether the same has been correctly or aptly determined.

15. Net Profit (or loss) before tax as per Profit and Loss Account

The net profit computed for working out the NP ratio as per cl 32[b] of form 3CD must be stated here.

16. Taxes on income paid/provided for in the books

The requirement relates to stating the income tax provided for in the books of accounts, which, incase of corporate assessees, should match with the provision for taxation in profit and loss account.

Incase, no provision of taxation has been provided for in the books of the assessee, the tax auditor should state the amount of tax [es] paid as per books of account which are subject to his audit.

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 proprietor or partner.

SI. 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