

Issues in Tax Audit

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What is the objective of Tax Audit ?

Examination or review of accounts of any business or profession carried out by taxpayers

To ensure correctness of implementation and proper compliance of tax provisions envisaged under the Act

Enables the tax authority for verification and assessments

Our Responsibility

To express an opinion on the financial statements based on the audit conducted in accordance with the Standards issued by ICAI

Obtaining sufficient and appropriate audit evidence

To verify the statement of particulars required to be filed under Sec 44AB

Clarification regarding authority attached to the documents Issued by the Institute

Uptill 18th August 2023

- Guidance to members on matters which may arise in the course of their professional work and on which they may desire assistance in resolving issues which may pose difficulty.
- A member should ordinarily follow recommendations in a guidance note relating to an auditing matter except **where he is satisfied that in the circumstances of the case, it may not be necessary to do so.**

WEF 19TH August 2023

- Assist professional accountants in implementing the Engagement Standards and the Standards on Quality Control issued under the authority of the Council.
- A professional accountant who does not consider and apply the guidance included in a relevant Guidance Note should take **reasonable and adequate care in performing the alternate procedures** adopted by him to deal with the objectives and basic principles set out in the Guidance Note. In such situations, a professional accountant **should also document the rationale in performing the alternate procedures**

Guidance Note – Importance

➤ **Virtual Soft Systems Ltd., Supreme Court 404 ITR 409**

*Prior to critically examining the case, it would be appropriate to have an understanding and significance of the Guidance Note issued by the ICAI. **The ICAI is an expert body, created by the Parliament under the Chartered Accountants Act, 1949.** The ICAI's publication on the subject indicates that the Guidance Note on Accounting for Leases was issued by it for the first time in 1988, which was later on revised in 1995. **The Guidance Note reflects the best practices adopted by the accountants throughout the world. The ICAI is a recognized body vested with the authority to recommend accounting standards for ultimate prescription by the Central Government in consultation with the National Advisory Committee of Accounting Standards for the presentation of true and fair financial statements.***

➤ **Punjab Stainless Steel Industries, Punjab and Haryana High court, 364 ITR 144 held as under**

*So as to be more accurate about the word "Turnover", one can refer either to dictionaries or to material, which are published by bodies of Accountants. The Institute of Chartered Accountants of India (hereinafter referred to as the "ICAI") has published some material under the head "Guidance Note on Tax Audit under Section 44AB of the Income Tax Act". **The said material has been published so as to guide the members of the ICAI. In our opinion, when a recognized body of Accountants, after due deliberation and consideration publishes certain materials for its members, one can rely upon the same....'***

Guidance Note – Importance

➤ **J.K. Industries Ltd., Supreme court, 297 ITR 176**

Accounting Standard is a policy statement or document framed by Institute. Accounting Standards establishes rules relating to recognition, measurement and disclosures thereby ensuring that all enterprises that follow them are comparable and that their financial statements are true, fair and transparent.

Accounting Standards are an attempt to overcome some of these deficiencies of Accountancy. Accounting Standards involve codification of fundamental accounting rules, rules which explain and standardize the application of the fundamental rules to a variety of uncertain situations

The object of Accounting Standards is, therefore, to standardize and to narrow down the options. The object of Accounting Standards is to evolve methods by which 'accounting income' is determined.

The object behind the Accounting Standards is to evolve methods by which accounting income is determined, made more transparent and leave less and less room for subjective selection of methods and provide for more attention to the quality of estimates used in arriving at accounting income.

The main object sought to be achieved by Accounting Standards which is now made mandatory is to see that accounting income is adopted as taxable income and not merely as the basis from which taxable income is to be computed

Applicability of Audit

Turnover	Applicability
Turnover > 10 Cr	Assessee is required to get his accounts audited as per section 44AB
1 Cr <= Turnover >= 10 Cr	Not Applicable in case when receipt and payment, <u>by mode other than account payee cheques</u> , during the year does not exceed 5% of total receipt and payment including amount received for sales, turnover or gross receipt during PY and amount paid for expenditure during PY, as the case may be
Turnover <=1 Cr	Will be applicable only if assessee once declared income as per 44AD and wants to declare income less than 8%/6% of turnover and a period of 5 years has not elapsed from when he first opted for 44AD and his income exceeds max. amount not chargeable to tax.

Audit Applicability 44AB VS 44AD - Business

Turnover (44AB/44AD) - Business

Less than 1Cr

44AB is Not Applicable

If after opting for 44AD, assessee declares income as per regular business

Then, for subsequent 5 years

If total Income exceeds maximum amount chargeable to tax

44AB will apply

More than 1Cr

Between 1 Cr to 2 Cr

Option to opt for 44AD- 44AB not applicable

Between 1 Cr to 10 Cr

44AB-Not Applicable, in case when receipt and payment, by mode other account payee cheque, made during the year does not exceed 5% of total receipt and payment including amount received for sales, turnover or gross receipt during PY and amount paid for expenditure during PY, as the case may be

> 10 Cr

44AB will apply

Audit Applicability 44AB VS 44ADA- Profession

Gross Receipts (GR) (44AB/44ADA) - Professionals

Less than 50 lakhs

44ADA - Presumption

But if income declared, lower than 50% **“and”** total Income exceeds maximum amount not chargeable to tax

44AB will apply

More than 50 lakhs

50L <= GR < 75L

44ADA - Applicable

If cash recd during the PY < 5% of the Total Gross Receipts.

44AB Not applicable

GR > 75L

44AB will apply

Issues – Audit applicability

Q – Is tax audit applicable when income is exempt under Section 10 or 11?

A - Section 44AB does not stipulate exemption from tax audit in case of exempt income-

- Trust carrying on business enjoying exemptions under sections 10(21), 10(23A), 10(23B), 10(23BB), 10(23C) or section 11
- Co-operative society carrying on business enjoying deduction under section 80P
- Such institutions shall be governed by Section 44AB if their turnover / gross receipts in business exceeds the prescribed limit

Issues – Tax Audit Applicability

Q - Whether the provisions of tax audit applicable to business under section 11(4A)?

A - There is nothing in the statute to suggest that Tax Audit under section 44AB shall apply to business under section 11(4A) (Incidental Business).

Sections 11 to 13 are independent of the five heads of income. As long as the registration under section 12AA/12AB is in force the income cannot be computed under the five heads of income.

Tax Audit is a specific requirement of the assessee having income under the head "Business and Profession".

Sales/ Turnover/ Gross receipt Includes / Excludes

Items to be included in turnover:

- Sale of scrap
- Sale of by-product
- Sales proceeds of shares, securities, debentures etc. held as stock-in-trade
- Special rebate which is in the nature of commission on sales
- Receipt in kind

Items to be excluded from turnover:

- Ancillary charges - packing, freight, forwarding, interest etc.
- Cash discount allowed in cash memo/sales invoice/ Trade discount / Price adjustments
- VAT and other indirect taxes collected/ collectible
- Sale proceeds of fixed assets/ assets held as investments
- Write back of provisions

Sales / Turnover/ Gross receipt Includes / Excludes

Items to be included in turnover:	Items to be excluded from turnover:
<ul style="list-style-type: none"><input type="checkbox"/> Cash incentives / duty drawback<input type="checkbox"/> Advances received from customers and forfeited<input type="checkbox"/> Exchange differences on export sales<input type="checkbox"/> Liquidated damages<input type="checkbox"/> Interest / rental income – if business income	<ul style="list-style-type: none"><input type="checkbox"/> Dividend on shares except for assessee dealing in shares<input type="checkbox"/> Interest / Rental income unless assessable as business income<input type="checkbox"/> Capital receipts<input type="checkbox"/> Advance forfeited in respect of fixed assets<input type="checkbox"/> Write back of amounts no longer payable to creditors

Calculation of Turnover / Gross Receipts for Shares and Securities

➤ **Speculative Transactions**

The aggregate of both positive and negative differences is to be considered as the turnover on a gross basis

➤ **Derivatives, Futures and Options**

- i. The total of favourable and unfavourable differences shall be taken as turnover
- ii. Premium received on sale of options is also to be included in turnover (in which case the profit if included in premium not be reincluded)
- iii. Any reverse trades entered, the difference thereon, should also form part of the turnover.
- iv. Open position at the end of the FY (i.e., trades which are not squared off during the same FY), **the turnover from the said transaction should be considered in the FY when the transaction has been actually squared off.**

➤ **Delivery based transactions**

Total value of sales is turnover, whether intended or not.

➤ **In case of a clearing & forwarding agent**

Reimbursement of customs duty & other charges collected by an agent not part of turnover.

Calculation of Turnover / Gross Receipts for Partners

Turnover, In Case of Partner of Partnership firm?

- Share of Profit Not includible, Para 5.13(x) of ICAI GN – share of profit exempt U/s.10(2A) so not “gross receipts of business”
- Interest and Remuneration from firm not Includible in gross receipts- (Perizad Zorabian Irani – [2022] 139 taxmann.com 164 (Bombay))

Sale Turnover – Case Laws

➤ **Sanjay Marotrao Modak [2023] 147 taxmann.com 221 (Mumbai - Trib.)**

Where assessee was trading in future and option transactions and Assessing Officer determined turnover from said transactions at Rs. 30.94 crores and levied penalty under section 271B on ground that assessee's turnover was beyond limit prescribed under section 44AB and he failed to submit audit report, since as per ICAI 'Guidance Note on Tax Audit assessee's case did not fall under section 44AB, impugned penalty deserved to be deleted.

➤ **Ghai Construction, 184 Taxman 52, Bom HC**

Tax audit is only in respect of business carried on by the assessee and not in respect of his income from other sources

Turnover- Advance received for services

Q – Advance received for services to be rendered, to be included in gross receipts?

A - ICAI's view Para 5.15 of GN:

Such receipts are liabilities and not a part of gross receipts until services are rendered

However, ITAT (Lucknow) in case of **Gopal Krishan Builders** [2004] 91 ITD 124 upheld a contrary view and held that the scope of the word “gross receipts” is quite wide to include advances also

Issues – Tax Audit report can be Revised

Q - Whether a tax audit report can be revised?

A -

- A Tax Audit Report which has not been approved by Assessee can be revised.
- However, after it has been approved by the Assessee, it should not be revised.
- However, there is no restriction by the utility, as of now, to upload revised JSON File.
- So, we should take due care, so that correct data is uploaded in the first instance itself.

Guidance Note on Tax Audit under Section 44AB issued by the ICAI provides that the audit report under section 44AB should not normally be revised. However, sometimes a member may be required to revise his tax audit report on grounds such as:

- (a) Revision of accounts of a company after its adoption in annual general meeting.
- (b) Change of law e.g., retrospective amendment.
- (c) Change in interpretation, e.g., CBDT Circular, Judgments, etc.

Thus, a tax audit report once filed can be revised on the above-mentioned grounds.

Q. Whether Tax Audit report need to be revised if payment of Expenditures u/s 43B & TDS u/s 40(a) are paid after filing of Tax audit report but before due date of filing Income Tax Return u/s 139(1)?

A. Rule 6G(3) provides that the tax audit report furnished may be revised by accountant and furnish it before the end of the relevant AY for which the report pertains if there is payment after furnishing of report which necessitates recalculation of disallowance u/s 40 or sec. 43B.

2022 GN stated, “However, it is not mandatory to revise tax audit report in the circumstances mentioned in Rule 6G(3). If the tax audit report is revised, while revising the tax audit report, prescriptions in ‘Guidance Note on Revision of the Audit Report’ should be considered.” The 2023 GN omits the above provisions

Therefore, in the circumstances covered by Rule 6G(3), issuing a revised tax audit report is mandatory, and a revised tax audit report is to be issued regardless of prescriptions of the ‘Guidance Note on Revision of the Audit Report.’

Issues – Late Filing of Audit Report

Q - Is there any penalty on late filing of Audit report?

A - As per Section 271B, if any person fails to get his accounts audited or fails to furnish the report of the audit the Assessing Officer may direct such person to pay a penalty of a sum equal to lower of following:

- (a) 0.5% of the total sale, turnover or gross receipts; or
- (b) Rs.1,50,000

However, no penalty shall be imposed if such failure is due to a reasonable cause.

Gemorium ITA No. 514/JP/2014 (ITAT Jaipur) S. 271B: Penalty for delay in furnishing tax audit report should not be imposed if there is no mala fide reason for the delay. Dispute with auditor is a reasonable cause u/s 273B for the delay in furnishing the tax audit report

Issues – What if UDIN not updated within 60 days of Audit Report

Q. Whether Audit report/certificate not to be treated as invalid if UDIN not updated within 60 days.

A. 2022 GN stated, “If the UDIN for any audit report/ certificate is not updated within the 60 days provided for the same, the department will treat such audit report/certificate as invalid submission.”

The 2023 GN omits this sentence. No provision in the Income-tax Act treats audit reports or certificates as invalid on not updating UDIN.

CBDT Circular dated 27.04.2020 makes quoting of UDIN Mandatory.

Issues – Clause 8A : Options for Taxation

Q - Compliance in case the assessee has opted for taxation under section 115BA / 115BAA / 115BAB / 115BAC / 115BAD / 115BAE ?

A - The tax auditor should verify whether the relevant form being 10-IB, 10-IC, 10-ID, 10-IE, 10-IF and 10-IFA furnished under section 115BA, 115BAA, 115BAB, 115BAC, 115BAD and 115BAE (included by revision in form 3CD) respectively for availing new tax regime is already filed by the assessee.

In case, the assessee has not filed the relevant form, written representation from the assessee should be obtained whether he will be availing the new regime or otherwise and based on written representation, the reporting under this clause should be made.

Where reporting is made solely on the basis of assessee's representation, the fact should be stated in paragraph (3) of Form 3CA or paragraph (5) of Form 3CB.

Section 115BAE ?

A – Section inserted by Finance Act, 2023, w.e.f. 1-4-2024

- **S. 115BAE (applicable to Co-operative society) is like S.115BAB (applicable to Domestic Company).**
- Assessee, being a co-operative society resident in India, set-up and registered on or after the 1st day of April, 2023, and has commenced manufacturing or production of an article or thing on or before the 31st day of March, 2024
- IT shall be payable @ 15% in respect of the total income, if certain conditions mentioned in the section is complied with.
- **Form 10-IFA** is to be filed by the assessee for opting to S. 115BAE on or before the due date specified u/s 139(1) for furnishing the **First return of Income.**

Issues – Clause 10 : Nature of business or profession

Q - Whether it is mandatory to disclose the nature of all the businesses carried on by the assessee and any change therein?

A - Clause 10 of Form 3CD mandates disclosure of nature of every business or profession carried on by an assessee during the previous year. Information has to be furnished in respect of each business carried on by the assessee.

Any **material change** in the nature of business should be precisely disclosed. The change will include a change from manufacturer to the trader as well as a change in the principal line of business.

Any **addition to or permanent discontinuance** of, a particular line of business may also amount to change requiring reporting. However, **temporary suspension of the business may not amount to change** and therefore need not be reported.

Issues – Clause 11 : Books of accounts

Q - Mr. A is maintaining books of accounts at more than one location. Whether the address of all the locations is to be mentioned in the audit report?

A - Clause 11 of Form 3CD requires a list of books maintained and address at which such books of accounts are kept. If such books of accounts are kept at multiples locations, then the auditor is required to mention the address of all the locations along with the details of books of accounts maintained at each location.

In case of a company assessee, the auditor should verify as to whether **Form AOC-5** has been filed with Registrar of Companies under the Companies Act for maintenance of books of accounts at a place other than the registered office.

The auditor's duties regarding 'books of account maintained' is not limited to merely giving a list of books of account against clause 11(b). He is required to examine the books of account maintained. Based on such examination, he is required to state in Form No. 3CB whether books of account kept are 'proper books of account'.

Q - Mr A has opted for the presumptive scheme under Section 44AD/44ADA in respect of one of his business/profession. Whether auditor is required to mention details of such business in the audit report?

A - In case profit and loss account of the assessee includes any profit declared under the presumptive scheme (Section 44AD, 44ADA, 44AE, 44AF, 44B, 44BB, 44BBA, 44BBB) then it is mandatory to mention the amount of such profit and the section under which the same is declared.

The tax auditor is not required to indicate as to whether the amount of presumptive income has been correctly computed under the relevant section relating to presumptive taxation. The reporting requirement gets satisfied if the amount as per profit and loss account is reported.

Issues – Clause 12 : Profits and gains assessable on presumptive basis

Q - How to ensure that the profit has been computed correctly if the profit & loss account also includes the profit computed on a presumptive basis?

A - If profit and loss account of the assessee also includes the presumptive income, the **common business expenditure** has to be apportioned to arrive at the correct amount of profit credited to profit and loss account and assessable on a presumptive basis.

The tax auditor, in such situation, **should arrive at a fair and reasonable estimate of such expenditure** on basis of evidence in possession of the assessee or by asking the assessee to prepare such estimate which should be checked by him.

It is also **necessary to mention the basis of apportionment of common expenditure.** However, if the tax auditor is not satisfied with the reasonableness of such apportionment, he should indicate such fact under this clause by a suitable note.

Suitable qualification may be provided in the tax audit report in Form 3CB

Issues – Clause 13 : Method of accounting

Q - An assessee has changed the method of accounting from mercantile to cash basis. What disclosure is required in Form 3CD?

A - Clause 13 of Form 3CD requires every assessee to report the method of accounting employed in the previous year. Further, if there was a change in the method of accounting employed in the immediately preceding previous year then same is to be reported.

The assessee is also required to disclose the effect of a change in method of accounting on the profit and loss. If it is not possible to quantify the effect of a change in method of accounting, appropriate disclosure should be made under this clause.

A change in accounting policy will not amount to a change in the method of accounting and hence any change in the accounting policies need not be mentioned under clause 13(b).

Issues – Clause 16 : Amounts not credited to P & L a/c

Q - An assessee has applied for a refund of GST but same wasn't credited in profit & loss account or ITC has been debited to P/L. Whether the disclosure is required in Form 3CD?

A - If a claim for refund of GST has been admitted as due and accepted during the relevant financial year, it shall be reported under Clause 16.

If the claim has been lodged during the previous year **but it has been admitted as due after the relevant previous year**, it need not be reported here.

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

Issues - Clause 17 : Section 43CA / 50C

- ❑ Section 43CA - Special provision for full value of consideration for **transfer of assets other than capital assets** in certain cases: It is applicable where an asset (other than capital asset) being land or building or both has been transferred and the **value of such an asset is less than the value adopted for the purpose of payment of stamp duty**. The value so adopted shall be deemed to be the full value of consideration if such stamp value exceed 110% of Value of Property and the gain arising therefrom is taxable as **business income**.
- ❑ Section 50C - Special provision for full value of consideration in certain cases: It is applicable where a **capital asset being land or building** or both has been transferred and the **value of such an asset is less than the value adopted for the purpose of payment of stamp duty**. The value so adopted shall be deemed to be the full value of consideration if such stamp value exceed 110% of Value of Property and the gain arising therefrom is **taxable as capital gain**.

What should be the manner in which provisions of Section 43CA is to be applied in case of builder adopting Percentage completion method for recognition of revenue?

- According to the cardinal rules of interpretation of tax statute is that a **deeming provision has to be interpreted strictly in terms of the words /language used to create the deeming fiction**. As per the relevant section, it is imperative that there should be **“actual transfer” of land or building or both**.
- Since the builder/developer can **transfer the asset on its existence i.e. on its completion, S. 43CA can't be applied on year to year basis and will be applicable on the final transfer of the asset**.

Issues - Clause 17 : Section 43CA / 50C

Whether leasehold right/development rights/TDR/FSI, etc. would be covered under this clause?

- **Shivdeep Tyagi [2024] 163 taxmann.com 614 (Delhi - Trib.) -**
Section 50C, being a deeming provision, is not applicable in case of transfer of leasehold rights
- **Greenfield Hotels & Estates (P.) Ltd. [2017] 389 ITR 68 (Bom HC) -**
Section 50C of the Act would not be applicable while computing capital gains on transfer of leased hold rights in Land and buildings.
- **Noida Cyber Park (P.) Ltd.(supra) [2021] 186 ITD 593 (Delhi - Trib.) -**
Section 50C of the Act covers only capital asset being land or building or both; it would not cover transfer of leasehold rights in land and building.

Issues - Clause 18 : Depreciation as per the Income-tax Act, 1961

Amendment to Clause 18(ca)

In Clause 18(ca), the following sub-clauses shall be substituted, namely-

(ca) Adjustment made to the written down value-

- (i) under the proviso to sub-section (3) of section 115BAA (for AY 2020-21 only)
- (ii) under the first provision to sub-section (3) of section 115BAC or the proviso to sub-section (3) of 115BAD (for AY 2021-22 only)
- (iii) under the second proviso to sub-section (3) of section 115BAC (for AY 2024-25 only)

Issues - Clause 18 : Depreciation as per the Income-tax Act, 1961

- ❑ **Where a vehicle is registered in the name of a Director, however it is in possession of company. Whether Depreciation is eligible?**

*The Hon'ble Supreme Court in **Mysore Minerals Ltd (239 ITR 775)** held that the terms "own", "ownership" and "owned" are generic and relative terms. The term "owned" as occurring in section 32 (1) of the Act must be assigned a wider meaning. Anyone in possession of property in his own title exercising such dominion over the property as would enable others being excluded therefrom and having the right to use and occupy the property and / or to enjoy its usufruct in his own right would be the owner though a formal deed of title may no have been executed and registered as contemplated by the Transfer of Property Act, the Registration Act, etc.*

Issues - Clause 18 : Depreciation as per the Income-tax Act, 1961

- ❑ Where due to lock out in plant, it did not function for 3 years. Whether Depreciation is available for those 3 years?

In Swati Synthetics Case (38 SOT 208) Mumbai Tribunal, it is held that condition of use is relevant only in which asset is purchased, thereafter it forms part of block and is passively used even if the plant is closed. Therefore depreciation is allowable in case of a closed unit too.

Issues - Clause 18 : Depreciation as per the Income-tax Act, 1961

❑ **Computer Software: whether asset?**

Special Bench in case of **Amway India Enterprises 111 ITD 112 (Del)** has laid down 3 tests to be applied to determine whether expenditure is capital or revenue – **test of enduring benefit, ownership test, functional test**

❑ **If new asset are put to use for less than 180 days, Additional Depreciation will be 100% or 50%? Available in full , half in a year and half in subsequent year- fact that said assets were put to use for less than 180 days, does not affect such benefit – Cosmo films 24 taxmann.com 189 (Delhi)**

Issues - Clause 18 : Depreciation as per the Income-tax Act, 1961

- ❑ The Tax Auditor should ensure that the **classification as made by the assessee is in consonance with legal principles.**
- ❑ Since the Tax Auditor is not a technical expert, he must obtain **suitable certificate from concerned experts.**
- ❑ The Tax Auditor must have due regard to the Income Tax Rules, 1962, relevant clarifications from the Department and judicial decisions.
- ❑ If there is a dispute with regard to the classification of an asset in a particular block or the rate of depreciation applied, the tax auditor must give his working with suitable reasons.
- ❑ In the **absence of any specific documentation with regard to the effective date from which the asset is put to use, he could get a representation** letter from the management, in respect of assets acquired.

Clause 21 (a) Amounts debited to the profit and loss

Prior to amendment

Cl. 21 (a) Details of amounts debited to the profit and loss account, being in the nature of :-

- Capital expenditure
- Personal expenditure
- Advertisement expenditure in any souvenir, brochure, pamphlet, etc . published by a political party
- Club entrance fees and subscriptions
- Cost for club services and facilities used
- Penalty or fine for violation of any law for the time being force
- Any other penalty or fine not covered above
- Expenditure incurred for any purpose which is an offence or which is prohibited by law e.g. Bribes, Smuggling expenses etc.

Amount debited to P & L account being in the nature of capital and personal expenditure.

- What if the expenditure are club expenses – whether disallowed u/s. 37
- Expenditure incurred at clubs being entrance fees and subscriptions
- Expenditure incurred at clubs being cost of club services and facilities used

Clause 21 (a) Amounts debited to the profit and loss

Amendment in Clause 21-

In sub-clause (a), in the table, under the column relating to "Nature"

- (i) for the words "Expenditure by way of penalty or fine for violation of any law for the time being force", the words and brackets **"Expenditure for any purpose which is an offence or is prohibited by law or expenditure by way of penalty or fine for violation of any law (enacted in India or Outside India)"** shall be substituted
- (ii) after the row with the words "Expenditure by way of any other penalty or fine not covered above", the row with the words **"Expenditure incurred to compound an offence under any law for the time being in force, in India or outside India"** shall be inserted;
- (iii) for the words "Expenditure incurred for any purpose which is an offence or which is prohibited by law", the words **"Expenditure incurred to provide any benefit or perquisite, in whatever form, to a person, whether or not carrying on a business or exercising a profession, and acceptance of such benefit or perquisite by such person is in violation of any law or rule or regulation or guideline, as the case may be, for the time being in force, governing the conduct of such person"** shall be substituted;

Clause 21 (a) Amounts debited to the profit and loss

The differences are in the reporting requirements in the last three items of clause 21(a)

<u>Prior to amendment</u>		<u>Post amendment</u>	
(vi)	Expenditure by way of penalty or fine for violation of any law for the time being in force	(vi)	<i>Expenditure for any purpose which is an offence or is prohibited by law or expenditure by way of penalty or fine for violation of any law (enacted in India or outside India)</i>
(via)	Expenditure by way of any other penalty or fine not covered above.	(via)	<i>Expenditure by way of any other penalty or fine not covered above.</i>
(vii)	Expenditure incurred for any purpose which is an offence or which is prohibited by law	(vii)	<i>Expenditure incurred to compound an offence under any law for the time being in force, in India or outside India</i>
		(viii)	<i>Expenditure incurred to provide any benefit or perquisite, in whatever form, to a person, whether or not carrying on a business or exercising a profession, and acceptance of such benefit or perquisite by such person is in violation of any law or rule or regulation or guideline, as the case may be, for the time being in force, governing the conduct of such person.</i>

Clause 21 (a) Amounts debited to the profit and loss

Item (vii) - Expenditure incurred to compound an offence under any law for the time being in force, in India or outside India

- ❑ Compounding of an offence is a settlement mechanism, by which, the person is given an option to pay a fee in lieu of penal action or prosecution, thereby avoiding a prolonged litigation. **Cases in which this is permissible are called compoundable offences called compoundable offences.**
- ❑ Examples of such offences may be under various laws. The common laws where compounding is generally done is Income-tax law, Company law, Labour laws, some sections of Indian Penal Code, FEMA, etc.
- ❑ If in the opinion of the assessee, any penalty or fine or part of it is compensatory in nature, the tax auditor should, in addition to reporting in this clause, **report the assessee's stand in para 3 of Form No. 3CA or para 5 of Form No. 3CB, as the case may be.**

Clause 21 (a) Amounts debited to the profit and loss

Item (viii) - Expenditure incurred to provide any benefit or perquisite, in whatever form, to a person, whether or not carrying on a business or exercising a profession, and acceptance of such benefit or perquisite by such person is in violation of any law or rule or regulation or guideline, as the case may be, for the time being in force, governing the conduct of such person

The condition for reporting under this clause is as under:

- (a) There has to be any benefit or perquisite to be given either in cash or in kind, in whatever form. The value of benefit or perquisite should be debited to the profit and loss account/income and expenditure account;
- (b) Such benefit or perquisite is given to a person, whether or not carrying on business or exercising a profession;
- (c) Acceptance of such benefit or perquisite by such person is in violation of any law or rule or regulation or guideline, as the case may be for the time being in force.

Clause 21 (a) Amounts debited to the profit and loss

Item (viii) -

Actions to be taken by the Auditor

- The tax auditor should obtain the list of beneficiaries in respect of whom tax has been deducted at source under section 194R to **form an opinion** as to whether any benefits and perquisites are inadmissible and require reporting under this clause.
- In case the tax auditor is of the opinion that any amount debited to the profit and loss account is to be disallowed as per section 37 and hence, has to be reported under this clause, then, **reporting need not be done under clause 21(b) on amounts inadmissible under section 40(a)(ia) for non-deduction of tax at source.**
- Appropriate disclosure should be made in the audit report in respect of such transactions in the observation in Para 3 of Form No. 3CA or Para 5 of Form No. 3CB, as may be applicable

Issues – Clause 21(a) : Amounts debited to the profit and loss

Whether Entrance Fees (life membership) paid to the club is a dis-allowable expenditure?

- Tax Auditor to only report payment of Entrance fees and not to report on its allowability.
- Even if the expenses brings enduring benefit, if the benefit is on revenue field, i.e. to carry on the business more efficiently and effectively, it is revenue expenses.

Empire Jute co. 124 ITR 1 SC

Engineers India Ltd.(1999) 239 ITR 237 Delhi

Otis Elevator Co. (I) Ltd (1992) 195 ITR 682 Mum

Gujarat State Export Corp. Ltd. (1994) 209 ITR 649 Guj

Issues – Clause 21(b) : Amounts inadmissible u/s 40(a) / (ia)

Q - Whether capital expenditure shall be reduced from the actual cost of a capital asset if tax was not deducted from such expenditure?

A - As per section 40(a)(ia), 30% of an expense is disallowed if tax is not deducted or after deduction not paid to the government. Whether this provision shall be **applicable only in case of revenue expenditure or in respect of capital expenditure** as well has been a matter of dispute between taxpayer and revenue. The revenue always argues to reduce the actual cost of a fixed asset if the tax has not been deducted for an expense which is capitalized as per provisions of section 43(1).

Plasmac Machine Mfg. Co. Ltd. 201 ITR 650 (Bom.) and Sumilon Industries Ltd. [2010] 3 taxmann.com 187 (Ahmedabad-ITAT), it was held that disallowance under this section can be made **only from an expense which is claimed in Profit and Loss Account**. Since in the case of capital expenditure no deduction is claimed under the P/L account, there should not be any disallowance under section 40(a)(ia) in respect of such payment.

Issues – Clause 21(b) : Amounts inadmissible u/s 40(a)

Q - Whether TDS amount will be allowed if assessee has not deducted TDS and obtained a CA Certificate in Form No.26A?

A –ICAI GN 2023 provides that where assessee has not deducted TDS and obtained a CA Certificate in Form No.26A to the effect that deductee/payee has declared the payment in his ITR and paid tax on the total income, including such payment and relies on the same **so that non-deduction of TDS does not attract disallowance**, tax auditor should verify the certificate in Form 26A and how it has been reflected in the statement of TDS filed vide Form 24Q / Form 26Q / Form 27Q.

Allowability in hands of Partners

- ❑ Supreme Court in **Ramlak Kothari** had held that **expenditure incurred by the partner for earning income from partnership firm is an allowable expenditure.**

- ❑ The Bangalore Tribunal in **Suresh Sreeram**, has ruled that that **Interest on funds borrowed for investment as capital in a partnership firm are deductible expenditure.** In absence of earning any interest income on capital from the firm is no bar to claim the interest paid on borrowings for the purpose of contributing capital to the firm by the assessee as deductible expenditure. In such an event there would be loss under the head “PGBP” sub- head “interest, salary from the partnership firm” and the assessee is entitled to set off the said loss against other income under the same head “PGBP”.

Allowability in hands of Partners

❑ S. Meyyappan (1969) 73 ITR 20 , Madras High Court

s Section 37(1) of the Income-tax Act, 1961 [Corresponding to section 10(2)(xv) of the Indian Income-tax Act, 1922] – Business expenditure – Allowability of – **Assessee, having half share in a firm, engaged one employee to look after his interest, and assist him in work he was expected to execute under terms of partnership – Assessee claimed allowance of payments made to said employee from his share of profit from firm – Whether since expenditure had been incurred by assessee for purpose of earning his half share of profits in firm, Tribunal was justified in allowing same while computing assessee share income from firm.**

Issues - Clause 22: Micro, Small & Medium Enterprises

Prior to amendment, clause 22 required **reporting of amount of interest inadmissible** under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006.

Amendment to clause 22

In clause 22, after the figures “2006”, the words and figures “ or any other amount not allowable under clause (h) of section 43B of the Income-tax Act, 1961” shall be inserted;’

Thus, under the amended clause 22 of Form No. 3CD, the reporting requirement has two limbs –

- (1) the amount of interest inadmissible under section 23 of the MSMED Act, 2006;
- (2) **any other amount not allowable under clause (h) of section 43B of the Income-tax Act, 1961.**

Issues - Clause 22: Micro, Small & Medium Enterprises

(I) Reporting requirements under the first limb of clause 22

If the buyer has not provided interest and/or if there is any dispute pending before MSE facilitation center, then, **present status can be obtained from the auditee.**

Also, in case of an auditee being a company, reference may be made to MSME-1 form furnished on MCA portal.

(II) Reporting requirements under second limb of clause 22

The second limb of clause 22 requires reporting of **any other amount not allowable** under clause (h) of section 43B of the Income-tax Act, 1961

Issues - Clause 22: Micro, Small & Medium Enterprises

Amendments in section 43B of the Income-tax Act, 1961

Cl. (h) has been inserted in section 43B w.e.f. 1-4-2024 (applicable from A.Y. 2024-25).

“43B. Notwithstanding anything contained in any other provision of this Act, a deduction otherwise allowable under this Act in respect of-

Following clause (h) shall be inserted after clause (g) of section 43B by the Finance Act, 2023, w.e.f. 1-4-2024:

(h) any sum payable by the assessee to a micro or small enterprise beyond the time limit specified in section 15 of the Micro, Small and Medium Enterprises Development Act, 2006 (27 of 2006),

shall be allowed (irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him) only in computing the income referred to in section 28 of that previous year in which such sum is actually paid by him:

Issues - Clause 22: Micro, Small & Medium Enterprises

Proviso to Sec 43B

Provided that nothing contained in this section [except the provisions of clause(h)] shall apply in relation to any sum which is actually paid by the assessee on or before the due date applicable in his case for furnishing the return of income under sub-section (1) of section 139 in respect of the previous year in which the liability to pay such sum was incurred as aforesaid and the evidence of such payment is furnished by the assessee along with such return.

Explanation 4 to section 43B-

(e) "micro enterprise" shall have the meaning assigned to it in clause (h) of section 2 of the Micro, Small and Medium Enterprises Development Act, 2006 (27 of 2006);

(g) "small enterprise" shall have the meaning assigned to it in clause (m) of section 2 of the Micro, Small and Medium Enterprises Development Act, 2006 (27 of 2006).

Issues - Clause 22: Micro, Small & Medium Enterprises

Composite Criteria : Investment in Plant & Machinery/ Equipment and Annual Turnover

Classification	Particulars	Micro	Small	Medium
Manufacturing enterprises and Enterprises rendering services	Investment in Plant and Machinery or Equipment, And	<= 1 cr	<= 10 cr	<= 50 cr
	Annual Turnover	<=5 cr	<=50 cr	<=250 cr

Issues - Clause 22: Micro, Small & Medium Enterprises

The following is the checklist for the tax auditor while reporting on section 43B(h)-

- (i) The tax auditor should take note of the following –
 - (a) The second limb of cl. 22 of 3CD has become applicable from A.Y.2024-25.
 - (b) Cl.(h) of S.43B is attracted when any sum payable by the assessee to a micro enterprise or small enterprise is paid beyond the time limit specified in S.15 of the MSMED Act, 2006.
 - (c) The provisions of section 43B(h) are applicable only in respect of sum payable by the assessee to a micro or a small enterprise and not to a medium enterprise.
 - (d) S.43B(h) is applicable only in respect of **'a deduction otherwise allowable under this Act'**.
 - (e) The proviso to section 43B which provides relaxation (from applicability of Section 43B) for payment made in respect of "any sum payable referred to in clauses (a) to (g) of section 43B on or before the due date of filing of income-tax return is not available for the newly inserted clause (h) of section 43B, where payment has to be made within the time limit specified in terms of section 15 of MSMED Act 2006,

"Section 15 of MSMED Act - Liability of buyer to make payment

Where any **supplier** supplies any goods or renders any services to any **buyer**, the buyer shall make payment therefor on or before the date agreed upon between him and the supplier in writing or, where there is no agreement in this behalf, before the **appointed day**:

Provided that in no case the period agreed upon between the supplier and the buyer in writing shall exceed forty-five days from the day of acceptance or the day of deemed acceptance.

Issues - Clause 22: Micro, Small & Medium Enterprises

Definition in the MSMED Act, 2006

<u>Section of the MSMED Act, 2006</u>	<u>Term</u>	<u>Definition</u>
2(d)	Buyer	Whoever buys any goods or receives any services from a supplier for consideration
2(n)	Supplier	A micro or small enterprise, which has filed a memorandum with the authority referred to in sub-section (1) of section 8, and includes,-
		(i) the National Small Industries Corporation, being a company, registered under the Companies Act, 1956
		(ii) the Small Industries Development Corporation of a State or a Union territory, by whatever name called, being a company registered under the Companies Act, 1956;
		<u>(iii) any company, co-operative society, trust or a body, by whatever name called, registered or constituted under any law for the time being in force and engaged in selling goods produced by micro or small enterprises and rendering services which are provided by such enterprises;</u>

Issues - Clause 22: Micro, Small & Medium Enterprises

Definition in the MSMED Act, 2006

<u>Section of the MSMED Act, 2006</u>	<u>Term</u>	<u>Definition</u>
2(b)	Appointed Day	Appointed day' means the day following immediately after the expiry of the period of fifteen days from the day of acceptance or the day of deemed acceptance of any goods or any services by a buyer from a supplier.
		Explanation For the purposes of this clause -
		(i) "the day of acceptance" means-
		(a) the day of the actual delivery of goods or the rendering of services; or
		(b) where any objection is made in writing by the buyer regarding acceptance of goods or services within fifteen days from the day of the delivery of goods or the rendering of services, the day on which such objection is removed by the supplier.
		(ii) "the day of deemed acceptance" means, where no objection is made in writing by the buyer regarding acceptance of goods or services within fifteen days from the day of the delivery of goods or the rendering of services, the day of the actual delivery of goods or the rendering of services.

Issues - Clause 22: Micro, Small & Medium Enterprises

Points to be considered by Tax auditor

- (a) Whether the enterprise is registered under the MSMED Act, 2006, since registration of MSME is a pre-requisite for attracting the provision of section 43B(h) of the IT Act.
- (b) If an entity is registered at any time during the current previous year, then, such registration will be applicable prospectively. Accordingly, any transactions carried out before the date of registration will not attract disallowance under section 43B(h).
- (c) If registration of the supplier is cancelled at any time during the previous year, then, it will be effective prospectively. Therefore, payment made for any purchases or services received before the date of cancellation shall be covered under section 43B(h).
- (d) Traders are allowed to be registered with MSME only for a limited purpose of Priority Sector Lending and not for any other benefit. **Accordingly, if the supplier to the auditee is a retail or wholesale trader, the provisions of section 43B(h) of the Income-tax Act, 1961 would not be attracted**

Issues - Clause 22: Micro, Small & Medium Enterprises

(e) For the purpose of disallowance under section 43B(h) of the Income-tax Act, 1961, the tax auditor should consider only the amount remaining outstanding as on 31st March of the financial year for the supply of goods or services.

Unpaid interest payable under section 16 of MSMED Act, 2006 need not again be considered for disallowance under section 43B(h) of the Income-tax Act, 1961, since, as per section 23 of the MSMED Act, 2006, the entire interest payable under section 16 of the said Act is inadmissible as deduction while computing income under section 28 of the Income-tax Act, 1961.

Issues - Clause 22: Micro, Small & Medium Enterprises

S.15 of the MSMED Act, 2006 requires the buyer to make payment to the supplier of the goods or services on or before date agreed upon (subject to max 45 days from the day of acceptance or deemed acceptance) or where there is no agreement in this behalf, before the Appointed Day.

(A) Where the agreement is in writing

The amount remaining outstanding as on 31st March of the FY but payment whereof has duly been made in the Next FY but within the time limit (agreed period or 45 days, whichever is earlier) will not attract disallowance us 43B(h).

(B) Where there is no agreement in writing

The amount remaining outstanding as on 31st March of the FY but payment whereof has duly been made in the next FY but within the time limit of 15 days will not attract disallowance us 43B(h).

Issues - Clause 22: Micro, Small & Medium Enterprises

Some examples for Applicability of S. 43B(h) in different cases

(A) Where the agreement is in writing

Sr No.	Day of acceptance or deemed acceptance	Agreed upon payment date in writing	Due Date of payment as per S.15 of MSMED Act	Actual Date of Payment	Status in terms of S. 43B(h)		
					AY 24-25	AY 25-26	AY 2026-27
1	20-03-2024	19-04-2024	19-04-2024	19-04-2024	Allowed	-	-
2	20-03-2024	19-04-2024	19-04-2024	10-05-2024	Disallowed	Allowed	-
3	20-03-2024	19-04-2024	19-04-2024	10-06-2025	Disallowed	-	Allowed
4	20-03-2024	20-06-2024	04-05-2024	02-05-2024	Allowed	-	-
5	20-03-2024	20-06-2024	04-05-2024	08-05-2024	Disallowed	Allowed	-

Issues - Clause 22: Micro, Small & Medium Enterprises

Some examples for Applicability of S. 43B(h) in different cases

(B) Where there is no agreement in writing

Sr No.	Day of acceptance or deemed acceptance	Agreed upon payment date in writing	Appointed Day	Due Date of payment as per S.15 of MSMED Act	Actual Date of Payment	Status in terms of S. 43B(h)	
						AY 24-25	AY 25-26
1	20-03-2024	NA	05-04-2024	04-04-2024	29-03-2024	Allowed	-
2	20-03-2024	NA	05-04-2024	04-04-2024	04-04-2024	Allowed	-
3	20-03-2024	NA	05-04-2024	04-04-2024	10-04-2024	Disallowed	Allowed

Issues - Clause 23 : Payment to specified person

Q - Whether Auditor has to quantify whether the payment to a related person is unreasonable or excessive under Clause 23?

A - No, Auditor is not required to quantify whether the payment is unreasonable or excessive. Only the Assessing Officer can make the disallowance if in his opinion the expenditure is unreasonable.

Excess payments of GST lying in Electronic Cash Ledger

❑ Whether can be claimed as deductible u/s 43B?

Amount deposited in the ECL although not adjusted against the Tax Liability and lying as a Balance as at 31.03.2023.

❑ Whether it can be claimed as deduction u/s. 43B?

Whether the assessee is entitled to claim deduction under Section 43B of the Income Tax Act, 1961 in respect of the excise duty paid in advance in the Personal Ledger Account, The above Issue arose during the excise regime. **Hon'ble SC in case of M/s. Modipon Ltd, [2018] 400 ITR 1 (SC)**

Issues - Clause 27(b) : Prior Period Items

Q - If the statutory auditor does not consider an item as a prior period expense, whereas tax auditor feels that such item should be considered as a prior period, should that expense be disclosed in Clause 27(b) of Form 3CD?

A - In case of any conflict in the opinion of the statutory auditor and tax auditor, the opinion of tax auditor shall prevail and the information thereof shall be reported in Form 3CD.

Issues – Clause 29 : Section 56(2)(viib)

Q – Whether any consideration for issue of shares which exceeds the fair market value of the shares as referred to in section 56(2)(viib) received by a start-up to be reported in clause 29?

A - Reporting obligation under Clause 29 is triggered if unquoted shares are issued at a premium by a closely held company. In such case, the excess of the premium over the fair market value of the shares shall be taxable as income from other sources in the hands of the company.

The DPIIT recognised start-ups are exempted from applicability of Section 56(2)(viib) subject to satisfaction of various conditions prescribed under the notification issued by the DPIIT.

Therefore, **Clause 29 shall apply only to closely held companies except DPIIT recognised start-ups which satisfy the condition for exemption.**
(Not applicable from AY 25-26, Finance Bill 2024)

Issues – Clause 29A : Section 56(2)(ix)

Q – Mr A, a sole proprietor, agreed to transfer his personal property to Mr X and received some non-refundable advance against such deal. The sale could not materialize as Mr X could not pay the whole amount and the advance money was forfeited by Mr A. What are the disclosure requirements?

A - Section 56(2)(ix) of the Income-tax Act, provides for taxability of any sum received as an advance in course of negotiations for the transfer of capital asset and such sum was forfeited due to non-transfer of such capital asset.

Clause 29A to Form 3CD requires auditor to report any advance received from the buyer but forfeited due to non-materialization of a deal to sale of the capital asset.

The auditor is not required to report any such forfeited amount if it is in respect of a personal capital asset or stock-in-trade.

Issues – Clause 29A : Section 56(2)(ix)

A - Any advances received and **forfeited towards the sale of stock-in-trade** would be taxable under section 28(i), and would not be required to be reported since the amount would be credited to profit & loss account.

The requirement of reporting arises only on forfeiture of advance. If an advance has been received and has been outstanding for a considerable time, **there is no requirement to report such amount unless and until it is forfeited by an act of the assessee.**

Issues - Clause 31 : Section 269SS & 269ST

- ❑ Company B purchased goods from Company A worth Rs. 3,00,000 on credit basis
Company A has dues payable to Company C
Company B has dues receivable from Company C
On the basis of internal arrangement between the 3 companies, Company A receives payment from Company B by set-off of inter-company balances
- ❑ **Section 269ST restricts receipts otherwise than through specified modes. Whether settlement of debt by book entry are also restricted?**
- ❑ **How should such transactions be reported in Form 3CD?**
- ❑ **A similar provision regarding loans and deposits exists in section 269SS and section 269T**

Issues - Clause 31 : Section 269SS & 269ST

❑ Unfavorable ruling -

Triumph International Finance (I) Ltd. 345 ITR 270 (Bom. HC) *where loan/deposit has been repaid by merely debiting account through journal entries, it must be held that assessee has contravened provisions of section 269T*

❑ Favourable rulings -

Worldwide Township Projects Ltd. (367 ITR 433) (Del. HC) *Object of section 269SS is to prevent transaction in currency, it is not intended to affect cases where a debt or a liability arises on account of book entries*

Ajitnath Hi-Tech Builders (P.) Ltd. (92 taxmann.com 228 (Bom. HC) - SLP dismissed by SC *There was reasonable cause to receive loan through journal entries. Non-compliance of section 269SS would certainly be a reasonable cause under section 273B for non imposition of penalty under section 271D*

Issues - Clause 31 : Section 269SS & 269ST

Q - Whether advance received from a person for sale of goods shall also be disclosed under Clause 31?

A - Loans or deposits are generally squared off by repayment of the sum to the lender. While as in the case of advance for the sale of goods, the party's ledger is squared off by the delivery of goods or services.

Thus, advance received against the agreement of sale of goods could not be deemed as loan or deposit. Accordingly, details of advances shall not be reported in Clause 31. Further, the ICAI, in the guidance note, has clarified that **Advance received against the agreement of sale of goods is not a loan or deposit.**

Issues - Clause 31 : Section 269SS & 269ST

- Q – Mr. A, received cash gifts in following manner – -**
- Rs. 2,50,000 each from his father and brother on a single day**
 - Rs. 1,80,000 each from his 10 friends on occasion of his marriage**

Section 269ST Apply?

A - Section 269ST, inter alia, states that –

“No person shall receive an amount of two lakh rupees or more

(a) in aggregate from a person in a day; or

(b) in respect of a single transaction; or

(c) in respect of transactions relating to one event or occasion from a person, otherwise than by an account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account:”

Issues - Clause 31 : Section 269SS & 269ST

Gift from father and brother – Rs. 2,50,000 each

- Any sum received from relatives shall not be taxable u/s 56(2)(x)
- Section 269ST provides that no amount shall be received in excess of Rs. 2 lakhs from a person on a single day otherwise than specified mode
- Hence, cash gift from father and brother, though exempt u/s 56(2)(x), shall be liable for penalty u/s 271DA

Gift from friends – Rs. 1,80,000 each

- Any sum received on occasion of marriage shall not be taxable u/s 56(2)(x)
- Section 269ST provides that no amount shall be received in excess of Rs. 2 lakhs on an occasion from a person otherwise than specified mode
- Since cash gift from each friend is less than Rs.1,80,000 though on a single occasion, should not be liable for penalty u/s 271DA

Issues – Clause 35 : Raw Material/Finished Goods/By-product

Q- Due to complexity of the business, assessee do not have quantitative information of stock. The software is not accepting any comment and it is accepting only numeric value. What should be reported ?

A - Write nil in online form 3CD

Report why quantitative details is not provided in the following two places:

- In paper form 3CD &
- Notes to accounts

The Following Statement Should Be Written In Paper Form 3CD as well as Notes:
"Due To Nature & Complexity of Business of Assessee, It Is Not Possible To Provide Quantitative Details"

Issues - Clause 36A : Deemed Dividends u/s 2(22)(e)

If assessee has received an amount in the nature of dividend referred to in Section 2(22)(e) of the Act, following details to be disclosed:

- Amount received
- Date of receipt

Applicability

- ❖ Advance or Loan by Company to Shareholder ($\geq 10\%$ of Voting Power)
- ❖ Advance or Loan by company to concern where share holder has substantial interest (20%)
- ❖ Payment on behalf or for individual benefit of the shareholder

The above advances and payments are considered as Deemed Dividend “to the extent of accumulated profits”.

Issues - Clause 36A : Deemed Dividends u/s 2(22)(e)

Who is to be taxed - Registered share holder or beneficial share holder

- ❑ The **Supreme Court of India** in case of **Gopal and Sons HUF [2017] 77 taxmann.com 71** held that although, HUF is a Beneficial Shareholder but cannot be a Registered shareholder. The Share Certificates are issued in the name of Karta. The Loans/advances received by HUF and Shareholder is a member of HUF and he has a substantial Interest. **Therefore, it shall constitute Deemed Dividend in the hands of HUF as per Explanation 3 to Section 2(22)(e).**
- ❑ **National Travel Service (Supreme Court) 2068-2071 of 2021** - The argument that as the shares are issued in the name of the Karta, the HUF is not the “registered shareholder” and so section 2(22)(e) will not apply to loans paid to the HUF is not correct because in the annual returns filed with the ROC, the HUF is shown as the registered and beneficial shareholder. In any case, the HUF is the beneficial shareholder. **Even if it is assumed that the Karta is the registered shareholder and not the HUF, as per Explanation 3 to s. 2(22), any payment to a concern (i.e. the HUF) in which the shareholder (i.e. the Karta) has a substantial interest is also covered.**

Issues - Clause 36A : Deemed Dividends u/s 2(22)(e)

Sec. 2(22)(e) is not applicable in case of commercial transactions

- ❑ Trade advances, which are in the nature of commercial transactions would not fall within the ambit of the word 'advance' in section 2(22)(e) of the Act. CBDT Circular No. 19/2017 dated 12 June 2017

Money lending business

- ❑ **Mohan Bhagwatprasad Agrawal - [2020] 115 taxmann.com 69 (Gujarat)**
Companies were having money lending as substantial part of their business, no addition could be made by way of deemed dividend in income of assessee -

Amount received for providing corporate guarantee, not deemed dividend

- ❑ **Accel Limited - [2020] 118 taxmann.com 103 (Madras)** *an advance made by its subsidiary company, in the course of the business, for providing corporate guarantee, not constitute as deemed dividend .*

Issues - Clause 36A : Deemed Dividends u/s 2(22)(e)

There must be a payment by the company by way of advance or loan

❑ **Exotica Housing & Infrastructure Company Pvt. Ltd. (ITAT Delhi)**

Advances given for purely temporary financial accommodation for business purposes does not attract the deeming fiction.

❑ **Veena Goyal - [2020] 119 taxmann.com 362 (Jaipur - Trib.)**

In absence of any payment by way of advance or loan by company to shareholder holding not less than ten per cent of voting power in company, provisions of section 2(22)(e) could not have been invoked

Issues - Clause 36A : Deemed Dividends u/s 2(22)(e)

Shareholding in lender company and substantial interest in borrower company to be checked at the time of advancement of loan

❑ **Jignesh P. Shah (Bombay High Court)**

2(22)(e) has to be construed strictly. If assessee is not a shareholder of lending co, section 2(22)(e) does not apply even if funds are ultimately paid by company in which assessee is a shareholder

❑ **Gurdeep Singh – [2020] 117 taxmann.com 451 (Chandigarh – Trib.)**

Where AO made addition to assessee's income by invoking provisions of section 2(22)(e) on the ground that assessee was holding more than 10% shareholding, in view of the fact that as per annual return filed before ROC, assessee had already transferred its shareholding in borrower company to lender company before advancement of loan out of surplus funds, impugned addition was to be deleted.

Issues - Clause 40 : Applicability of Ratios

- Only applicable to Manufacturing and Trading concerns
- Not applicable to Professionals, Service providers, etc.
- Ratios to be given in value terms and for the business as a whole
- Ratios may not make any sense in case of multiple activities

Issues – Clause 41 : Demand/Refund in Previous Year

Q - A demand was raised with respect to Custom duties and the same was adjusted against the refund due. So no amount was paid to the department. As an auditor, do we need to disclose the same in form 3CD?

A - Yes, an auditor is required to report the details of demand raised or refund issued to the assessee during the previous year irrespective of the fact that it was adjusted against any pending demand or refund.

The details are to be shown under **Clause 41 of Form 3CD.**

Issues – Clause 44 : Break-up of expenditure under GST

Sr No.	Total amount of Expenditure incurred during the year	Expenditure in respect of entities registered under GST				Expenditure relating to entities not registered under GST
		Relating to goods or services exempt from GST	Relating to entities falling under Composition scheme	Relating to Other Registered entities	Total Payment to Registered Entities	
1	2	3	4	5	6	7

Issues – Clause 44 : Break-up of expenditure under GST

The following are **certain transaction** on which **additional analysis** have been provided herewith –

➤ **Stock transfers, Cross Charge or Credit distributed through ISD**

- i. These amounts cannot be included in amount to be reported in Column (5) – expenditure relating to registered entities as tax audit is carried out of based on PAN and not GSTIN wise.
- ii. The same should be excluded from purchase register or GSTR-3B ITC register.
- iii. This should not be consider as expenditure incurred under this clause.

➤ **Cost of material consumed mentioned in financials**

- i. Many of taxpayers mention cost of material consumed instead of showing purchases in the financials.
- ii. One has to calculate actual purchase amount considering opening stock and closing stock calculation to calculate expenditure w.r.t purchases.

Issues – Clause 44 : Break-up of expenditure under GST

- **Expenditures on which ITC not claimed as per GST Law or by the taxpayers**
 - i. It may possible that assessee purchased materials from registered entities, however no ITC claimed.
 - ii. In this cases also reporting under this clause is required. Further, one can take stand to mention suitable observation stating that “since No ITC claimed by the assessee, hence no reporting made under this clause.”

- **Details of Expenditure relating to goods/services falling under composition scheme**
 - i. In most of the cases assessee did not maintain records of purchases from composite dealers.
 - ii. In this situation suitable observation should be incorporated stating that Assessee did not maintain records of purchases from composite dealers, hence such details are not provided in column (4) of clause 44.

Issues – Clause 44 : Break-up of expenditure under GST

➤ **Import of Goods on which IGST is paid**

- i. The same can be included in amount to be reported in Column (7) – expenditure relating to un-registered entities.
- ii. Further, suitable observation should be incorporated stating that amounts reported in clause 44 (7) includes Import of Goods on which Assessee paid IGST.

➤ **Import of Services on which recipient is required to pay GST under RCM**

- i. The same can be included in amount to be reported in Column (7) – expenditure relating to un-registered entities.
- ii. Further, suitable observation should be incorporated stating that amounts reported in clause 44 includes Import of services on which Assessee paid GST under RCM.

Issues – Clause 44 : Break-up of expenditure under GST

Q. Whether the above information is to be given in respect of each and every head of expenditure or only the total expenditure is to be given.

A. The guidance may be taken from the heading of the table which starts with the words “Breakup of total expenditure” and hence the total expenditure including purchases as per the above format may be given. It appears that head-wise / nature wise expenditure details are not envisaged in this clause.

Note : Depreciation under section 32, deduction for bad debts u/s 36(1)(vii) etc. which are accounting expenses in the nature of non-cash charges on the Profit and Loss account should not be reported under this clause in any of the Columns from 3 to 7.

Issues – Clause 44 : Break-up of expenditure under GST

Q. What if after purchasing goods/availing services from Registered supplier, the Registration of Supplier got cancelled.

A. It is important to differentiate the 'current status' of a supplier's registration from their status as it was at the time of supply.

Events occurring after the balance sheet date that alter the data relating to the year under audit do not alter the nature of the expenditure, that it is from registered suppliers.

Issues – Clause 44 : Break-up of expenditure under GST

Q. What if the assessee is not in a position to give the details as required in clause 44

- A. An appropriate disclosure/disclaimer may be made by the auditor in Form 3CA/3CB. Where the assessee has provided reason for not being able to provide details, the same may be reported, if found appropriate.



Questions

**THANK YOU
CA PIYUSH .S. CHHAJED**



