

# 15

## C H A P T E R

# TAX AUDIT

### Introduction

**15.1** Besides shareholders, the audited financial statements have different users viz., creditors, potential investors, lenders, tax authorities, etc. The information revealed by the financial statements may not be as per the specific requirements of these users. The tax authorities need this information to charge taxes and allow deductions. It is in this context that the concept of tax audit developed. *Tax audit* can be defined as *"an examination of financial records to assess correctness of calculation of taxable profit, to ensure compliance with provisions of the Income-tax Act (hereinafter referred to as the Act) and also ensure fulfilment of conditions for claiming deductions under the Income-tax Act."*

### Scope of auditor's role under the Income-tax Act, 1961

**15.2** The auditor's role under the Income-tax Act can be broadly summarised under three heads :

- Conducting the tax audit under section 44AB.
- Certifying information in prescribed form for claiming various deductions under the Income-tax Act.
- Conducting selective audit under section 142(2A).

#### **15.2-1 Compulsory tax audit under section 44AB—**

■ **PERSON FOR WHOM COMPULSORY** - According to section 44AB, tax audit is compulsory for a person carrying on any business or profession if—

- (a) in case of *business*, whose total *sales turnover* or *gross receipts* exceed Rs. 1 crore in the previous year;
- (b) in case of *a profession*, if the gross professional receipts in the previous year exceed Rs. 25 lakhs; and
- (c) in case of an assessee (covered under section 44AD, 44AE, 44AF, 44BB or 44BBB) who claims that the profits and gains computed in accordance with sub-section (1) of section 44AD or sub-section (2) of section 44AE or

sub-section (1) of section 44AAF, as the case may be (irrespective of his turnover).

■ **FILING OF TAX AUDIT REPORT ALONG WITH THE RETURN OF INCOME** - The assessee, who is required to get his accounts audited under section 44AB, must obtain a report of audit as required under this section before the specified date and must e-file the Tax Audit report alongwith the Income-tax refund.

■ **QUALIFICATION FOR APPOINTMENT OF A TAX AUDITOR** - According to the provisions of section 44AB, the tax audit report should be given by an accountant. An "accountant" for the purposes of section 44AB will mean a chartered accountant within the meaning of the Chartered Accountants Act, 1949 and includes a person who is eligible to be appointed as an auditor of a limited company under section 226(2). As per the proviso to section 44AB, in case of assessee (for example, a cooperative society) whose accounts are allowed to be audited under any other law by a person other than a chartered accountant, the tax audit may also be conducted by the statutory auditor who may not be a chartered accountant. Further, a chartered accountant in practice who renders tax consultancy on a professional fee basis (not as an employee) can also conduct tax audit.

■ **DISQUALIFICATIONS OF A TAX AUDITOR**

(a) An employee of the assessee or of a concern under the same management<sup>1</sup>.

(b) A chartered accountant who has written the books of the assessee<sup>2</sup>.

(c) Internal auditor if appointed after December, 2008.

■ **APPOINTMENT OF TAX AUDITOR** - The tax auditor may be appointed by the management of entity or any person duly authorised by it for making such an appointment. Similarly, a partner of a firm, a proprietor or any other authorised person can appoint the tax auditor in case of partnership firms or proprietary concerns.

■ **CEILING ON THE NUMBER OF AUDITS** - The following points should be noted with regards to ceiling on the number of audits—

(a) A chartered accountant cannot accept more than 60 (sixty) tax audit assignments in a financial year.

(b) In case of a firm of chartered accountants, the specified number of sixty tax audit assignments is to be counted for every partner of the firm.

The audit report shall be submitted in the following Forms—

TABLE 15.1  
AUDIT FORMS

	Audit report	Statement of particulars
● In case of a person who carries on business or profession and who is required by or under any law to get his accounts audited	Form No. 3CA	Form No. 3CD

1. Reported in Code of Conduct, ICAI, New Delhi 8th edn., 1988.

2. Guidance Note on *Tax Audit under section 44AB of the Income-tax Act*, ICAI, 3rd edn., 1998, paragraph 8.11.

Audit report	Statement of particulars
<ul style="list-style-type: none"> <li>• In case of a person who carries on business or profession but not being a person referred to above</li> </ul>	
Form No. 3CB	Form No. 3CD

### Certifying information in prescribed form for claiming various deductions under the Income-tax Act

**15.2-2** The Income-tax Act provides for various exemptions on and deductions from the taxable income of the assessee.

For claiming some of these, the assessee has to furnish along with the return of income, a report by an 'accountant' in the prescribed form certifying that the deduction has been correctly claimed besides fulfilling other conditions. Examples of some such deductions allowed for assessment year 2006-07 are given below :

(i) *Deduction under section 33AB*

It is allowed to an assessee carrying on the business of growing and manufacturing tea, coffee or rubber plantation in India provided, besides fulfilling other conditions, the accounts of the taxpayer should be audited by a chartered accountant and the report of the auditor in prescribed form<sup>3</sup> duly signed and verified is filed along with the return of relevant assessment year.

(ii) *Amortisation of preliminary expenses under section 35D*

Deduction for certain preliminary expenses is allowed to an Indian company or a resident non-corporate assessee for setting up a new industrial unit or expanding an industrial undertaking. The amortisation will be admissible if, besides fulfilling other conditions, the accounts of the assessee for the relevant year in which the qualifying expenditure is incurred have been audited by a chartered accountant. The audit report should be furnished in prescribed form<sup>4</sup> along with the return of income for the first year in which deduction is claimed.

(iii) *Amortisation of expenditure on prospecting, etc. for development of certain minerals under section 35E*

- Section 35E provides for the amortisation of expenditure incurred on any operation relating to prospecting for minerals/group of associated minerals or on the development of their mine. These should be specified in the Seventh Schedule.
- Deduction is allowed only to Indian companies.
- Deduction is permitted if the books of account of the relevant year have been audited. In such a case audit report in prescribed form<sup>4</sup> should be submitted along with return of income for the first year in which deduction is claimed.

3. Form No. 3AC.

4. Form No. 3B.



- (iv) *Deduction in respect of profits and gains from industrial undertaking engaged in infrastructure development, etc. under section 80-IA*

Deduction under section 80-IA is available only to residential undertakings engaged in provision of infrastructure facility, telecommunication services, industrial parks and power generation, transmission and distribution. This deduction is admissible only if the audit report duly signed and verified by a chartered accountant is furnished along with the return of income in prescribed form (Form No. 10CCB).

### Selective tax audit

**15.2-3** Under section 142(2A) to 142(2D) selective tax audit can be conducted. The important points to be noted with regard to this are as follows:

- (i) Section 142(2A) empowers the Assessing Officer to direct the assessee to get his accounts audited by an 'accountant' nominated by the Chief Commissioner/Commissioner of Income-tax. This direction can be given by the Assessing Officer if he is of the opinion that it is necessary to get the accounts audited in view of the nature or the complexity of the accounts of the assessee or in the interest of revenue.
- (ii) The form of the audit report has been prescribed under section 142(A) in Rule 14A of the Income-tax Rules, 1962.
- (iii) The selective audit can be ordered even if the assessee has got his accounts audited under any other law including section 44AB of the Income-tax Act, 1961.
- (iv) The audit fees and expenses incidental to audit shall be determined by the Chief Commissioner or Commissioner and paid by the assessee. In case the assessee defaults in such payment, it would be recoverable as arrears of tax.