

## Overview of Tax Audit and Auditor's Responsibilities



*In recent years, significant changes have been made in Form No. 3CD. Insertion of new clauses in recent years such as clause 17 related to transfer of land, building or both, changes in clause 21(b) in respect of amounts inadmissible under section 40(a), clause 33 which requires section-wise details of deductions admissible under Chapter III, clause 34 related to tax deduction at sources has significantly enhanced reporting responsibilities of assessee and tax auditor in respect of information submitted in Form No. 3CD. Further, introduction of Income Computation and Disclosure Standards (ICDS) and applicability of Ind AS to certain class of assessee requires more comprehensive disclosures in financial statements and Form No. 3CD. By virtue of provision of section 44AB of Income-tax Act, 1961, tax auditor has responsibility to ensure factual accuracy of information furnished in Form No. 3CD as tax authorities rely on information provided in Form No. 3CD while computing taxable income of the assessee.*



**CA. Girish Arora and  
CA. Rajit Arora**

The authors are members of the Institute. They can be reached at [girisharorafca@yahoo.com](mailto:girisharorafca@yahoo.com)

Section 44AB of Income-tax Act, 1961 (hereinafter referred to 'Act') makes it obligatory for a person carrying on business to get his accounts audited by an accountant, and to furnish by the 'specified date', the report in the prescribed form of such audit, if the total sales, turnover or gross receipts in business in the relevant previous year exceed or

exceeds ₹ 1 Crore. For a professional, the provisions of tax audit become applicable, if his gross receipts in profession exceeds ₹ 50 lakhs in the relevant previous year. The scope of section 44AB also provides that audit under the section would be required in case of a person carrying on

- (i) business of the nature referred to in sections 44AE, 44BB and 44BBB, where he claims his income to be lower than the deemed presumptive income under the respective section.
- (ii) business of the nature referred to in section 44AD, if the provisions of section 44AD(4) are applicable in his case and his income exceeds the basic exemption limit.
- (iii) profession of the nature referred to in section 44ADA, where he claims his income to be lower than the deemed presumptive income under that section and his income exceeds the basic exemption limit.

In case of an assessee with higher turnover/gross receipts of upto ₹ 2 crore, opting for presumptive taxation under section 44AD, tax audit is not required.

The compulsory tax audit is intended to ensure proper maintenance of books of account and other records, in order to reflect the taxable income of the tax payer and to facilitate the administration of tax laws by a proper presentation of the accounts before the tax authorities. This also saves the time of the Assessing Officers considerably in carrying out the assessment.

Section 44AB read with *Explanation* below sub-section (2) of section 288 stipulates that only Chartered Accountants should perform the tax audit. This section does not stipulate that only the statutory auditor appointed under the Companies

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Act or other similar Statute should perform the tax audit. As such, tax audit can be conducted either by the statutory auditor or by any other chartered accountant in full time practice.

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

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

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

*\*\* (increased to Rs. Fifty Lakhs w.e.f. A.Y. 2017-18)*

In view of above, responsibilities have been cast under the Act upon Chartered Accountants to perform the tax audit because of their effective practical training, professional skills, knowledge and expertise to perform the required audit procedures.

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

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

# Tax Audit

Sub-rule (2) of Rule 6G further provides that the particulars which are required to be furnished under section 44AB shall be in Form No. 3CD. The requirements of Form No. 3CA or Form No. 3CB, as applicable relating to particulars in Form No. 3CD is that the auditor should report that these particulars in Form No.3CD are “true and correct”. Therefore, the tax auditor has responsibility to ensure factual accuracy of the information reported in Form No. 3CD.

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

- (a) He can rely upon the judicial pronouncements while taking any particular view about inclusion or exclusion of any items in the particulars to be furnished under any of the clauses specified in Form No.3CD.
- (b) If there is a conflict of judicial opinion on any particular issue, he may refer to the view which has been followed while giving the particulars under any specified clause.
- (c) The Guidance Notes and SAs issued by the Institute from time to time should be followed. While furnishing the particulars in Form No.3CD, it would be advisable for the tax auditor to consider the following:
  - (a) If a particular item of income/expenditure is covered in more than one of the specified clauses in the statement of particulars, care should be taken to make a suitable cross reference to such items at the appropriate places.
  - (b) If there is any difference in the opinion of the tax auditor and that of the assessee in respect of any information furnished in Form No. 3CD and the annexure thereto, the tax auditor should state both the view points and also the relevant information in order to enable the tax authority to take a decision in the matter.
  - (c) If any particular clause in Form No.3CD and the annexure thereto is not applicable, he should state that the same is not applicable.
- (d) In computing the allowance or disallowance, he should keep in view the law applicable in the relevant year, even though the form of audit report may not have been amended to bring it in conformity with the amended law.
- (e) In case the prescribed particulars are given in part or piecemeal to the tax auditor or relevant form is incomplete and the assessee does not give the information against all or any of the clauses, the auditor should not withhold the entire audit report. In such a case, he can qualify his report on matters in respect of which information is not furnished to him. In the absence of relevant information, the tax auditor would have no option but to state in his report that the relevant information has not been furnished by the assessee.
- (f) The information in Form No. 3CD should be based on the books of accounts, records, documents, information and explanations made available to the tax auditor for his examination.
- (h) If the tax auditor is not able to perform required audit procedures to check accuracy of information furnished in Form No. 3CD due to non-availability of information or required documentation in the possession of the assessee, he should clearly mention the same in the report.
- (i) In case of certain clauses, the tax auditor relies on management representation to support completeness of information furnished in Form No. 3CD. The tax auditor should bring this fact in his audit report.
- (k) In case of changes in applicable laws which may have impact on information furnished in Form No. 3CD such as introduction of GST effective from 1 July 2017, however, necessary changes in Form 3CD have not been made to incorporate all regulatory changes, the tax auditor may consider appropriate disclosure in his report.
- (l) If there are disputes with the tax authorities related to particular information furnished in Form No. 3CD of earlier years which may

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impact opening balances disclosed in the current year Form No. 3CD, the tax auditor should bring this fact in his report.

(m) The Tax Auditor should also ensure the eligibility of the expenditure/payment for deduction and compliance of the conditions prescribed in the sub-section including approval from the relevant/prescribed authority, notification issued by the Central Government. Tax auditor should also refer Rule 6 of Income-tax Rules, 1962.

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the extent of checking and to ensure adequate documentation in support of the information being certified.

The audit report given under section 44AB is to assist the income-tax department to assess the correct income of the assessee. The Assessing Officer or any other authority who is authorised to call for evidence or documents, can call upon the tax auditor who has audited the accounts to give any evidence or produce documents.

In order that the tax auditor may be in a position to explain any question which may arise later on, it is necessary that he should keep detailed notes about the evidence on which he has relied upon while conducting the audit and also maintain all his working papers. For this purpose attention is also invited to SA 230 - Audit Documentation, which provides that the tax auditor should document matters which are important in providing evidence that the audit was carried out in accordance with the basic principles. Such working papers should include his notes on the following, amongst other matters:

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

The liability of the tax auditor in respect of tax audit will be the same as in any other audit assignment. In case the assessee is found guilty of having concealed the particulars of his income it would not *ipso facto* mean that the tax auditor is also responsible. However, tax auditor should ensure factual accuracy of information provided by assessee in Form No. 3CD, performance of required audit procedures to check the same and appropriate documentation in support of his audit report. ■