

Ahmedabad Branch of WIRC of ICAI

The background is a light blue gradient. On the left side, there are several white paper airplanes scattered across the frame. On the right side, a single yellow paper airplane is shown in flight, moving towards the right. A white dashed line follows its path, curving upwards and then downwards, suggesting a trajectory or a path.

Changes in tax audit report for AY 2021-22

Ishita Bhaumik

Contents

1 Background

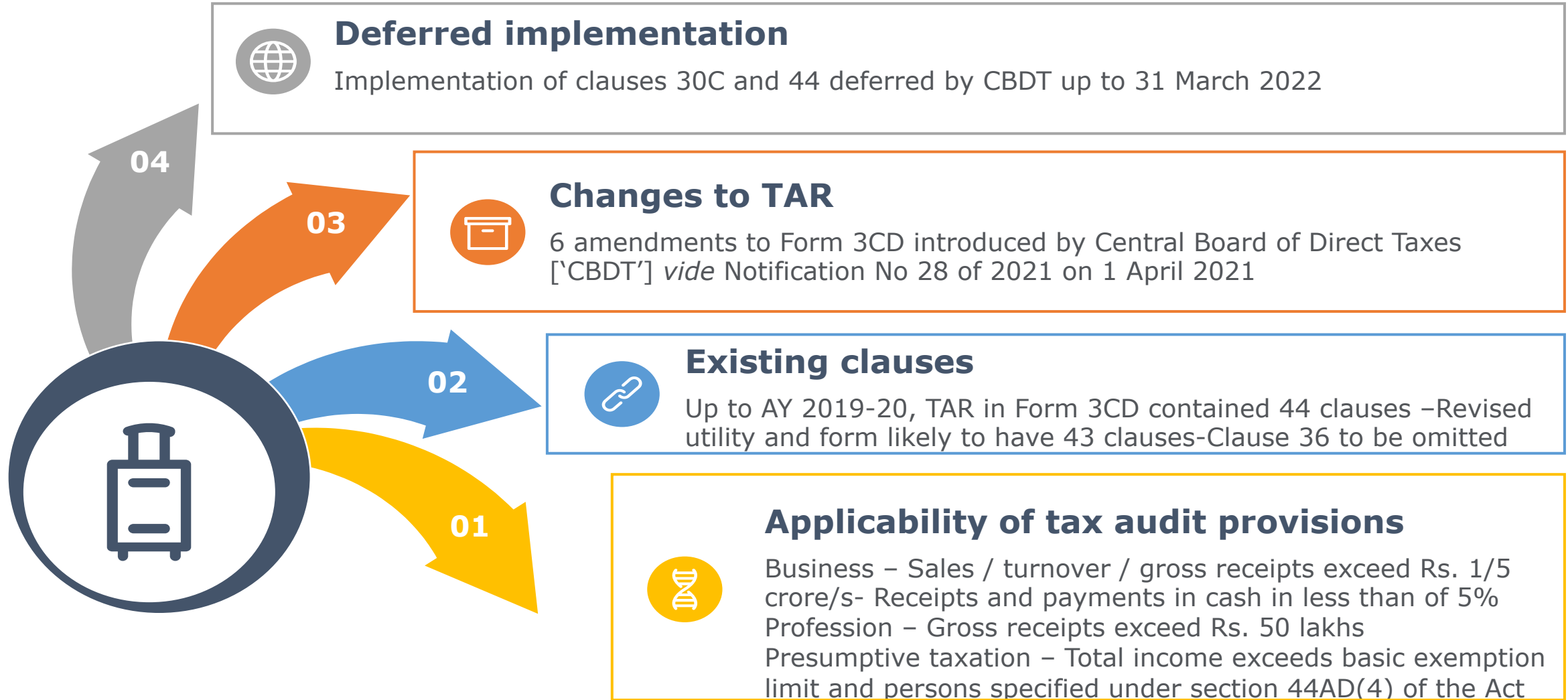
2 Clause-wise analysis of recent changes in tax audit report ['TAR']

3 Non-Applicability of certain clauses for AY 2021-22

4 General issues in tax audit




Background



Clause-wise analysis of recent changes in TAR

Clause No	Particulars
Clause 8A	Whether the assessee has opted for taxation under section 115BA/115BAA/115BAB/ 115BAC/115BAD?
Clause 17	Details on section 43CAor 50C
Clause 18	WDV adjustment for 115BAC/115BAD
Clause 32	Details of brought forward loss or depreciation allowance
Clause 36	Dividend distribution taxes related clause

 Changes to existing clauses

 Clause deleted

Revision in tax audit report allowed to claim the expenses under Section 43B of the Act

Clause-wise analysis of recent changes in TAR

Changes to existing clauses

Clause 8- Whether the assessee has opted for taxation under section 115BA/115BAA/115BAB/115BAC/115BAD?

- Additional sections-115BAC/115BAD added in the clause
- 115BAC and section 115BAD is applicable from AY 2021-22- To incorporate the same, the tax audit report has been changed
- 115BAC-Tax on income of individuals and Hindu undivided family at lower rates without any benefits- ***Refer subsequent slides***
- 115BAD-Tax on income of certain resident co-operative societies @ 22% without any deductions

Clause 17- Details on section 43CA or 50C

- Amendment in Finance Act 2021 was made to increase the safe harbor rules for 43CA and 50C to 20% from 10%
- 43CA-Limit increased for the period from 12th November 2020 to 30th June 2021 in respect of the only primary sale of residential units of value up to Rs. 2 crores
- 50CA-Increasing the safe harbor from 10% to 20% was allowed to buyers of these residential units u/s 56(2)(x) for the same period
- Amended wordings- Whether provisions of second proviso to sub-section (1) of section 43CA or fourth proviso to clause (x) of sub-section (2) of section 56 applicable?

Clause-wise analysis of recent changes in TAR

Changes to existing clauses

Income slab	Option 1: Existing tax rate			Option 2: New tax rate
	Age less than 60 years	Age 60 years or above 60 years but less than 80 years	Age 80 years or above 80 years	
Upto Rs.2,50,000	Nil	Nil	Nil	Nil
Rs. 2,50,001-Rs. 3,00,000	5%	Nil	Nil	5%
Rs. 3,00,001 to Rs. 5,00,000	5%	5%	Nil	5%
Rs. 5,00,001 to Rs. 7,50,000	20%	20%	20%	10%
Rs. 7,50,001 to Rs. 10,00,000	20%	20%	20%	15%
Rs. 10,00,001 to 12,50,000	30%	30%	30%	20%
Rs. 12,50,001 to Rs. 15,00,000	30%	30%	30%	25%
Above 15,00,000	30%	30%	30%	30%

- No change in the rates of surcharge, cess or rebates
- Taxpayer has an Option to choose between option 1 and 2 above-
 - In case of no business income- Option to be exercised annually
 - In case of business income- Option to be exercised and then continued forever. Withdrawal from the Option allowed only once.
- However, while choosing Option 2, the taxpayer cannot claim any exemptions/ deductions. Examples of exemptions/ deductions are Leave travel allowance, House rent allowance, interest on housing loan,, Chapter VI-A deductions (insurance, Medclaim etc. except NPS), no exemptions for any perquisites or other allowance.
- In Option 2, provisions relating to AMT will not be applicable

Clause-wise analysis of recent changes in TAR

Changes to existing clauses

Particulars	Scenario 1- Income of Rs. 8,00,000		Scenario 1- Income of Rs. 12,00,000		Scenario 1- Income of Rs. 15,00,000	
	Existing provisions	New provisions	Existing provisions	New provisions	Existing provisions	New provisions
Income (A)	8,00,000	8,00,000	12,00,000	12,00,000	15,00,000	15,00,000
Deductions						
Standard deduction	50,000	-	50,000	-	50,000	-
Chapter VI-A (insurance. Mediclaim)	1,50,000	-	1,50,000	-	1,50,000	-
Interest on house loan	40,000	-	40,000	-	40,000	-
Total deductions (B)	2,40,000	-	2,40,000	-	2,40,000	-
Net taxable income (A)-(B)	5,60,000	8,00,000	9,60,000	12,00,000	12,60,000	15,00,000
Taxes on the above including cess of 4%	25,480	46,800	1,08,680	1,19,600	1,98,120	1,95,000
Tax savings/ (additional tax)		(21,320)		(10,920)		3,120

Clause-wise analysis of recent changes in TAR

Changes to existing clauses

As stated, Section 115BAC and 115BAD is applicable from Ay 2021-22 and taxpayer does not get additional depreciation under these sections

Clause 18 and Clause 32

Clause 18-

Adjustment made to the written down value under section 115BAC/115BAD (for assessment year 2021-2022 only) to be reported

Clause 32-

All losses/allowances not allowed under section 115BAA/ 115BAC/115BAD to be reported

Goodwill on intangibles-

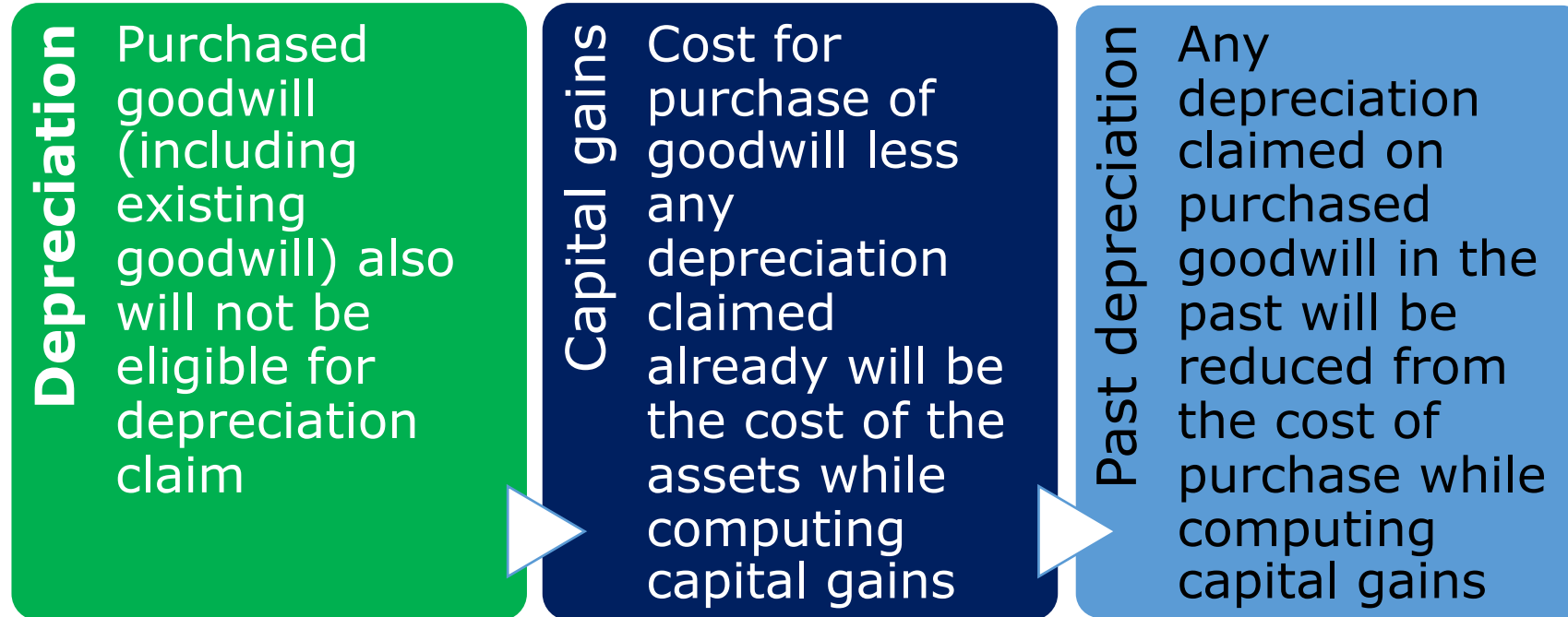
Amendment of section 32 provides refusal of depreciation on goodwill- **Refer next slide**

Such adjustment is to be made to **WDV of Intangible asset due to excluding value of goodwill of a business or profession.**

Hence this is also amended in Clause 18

Clause-wise analysis of recent changes in TAR

Changes to existing clauses

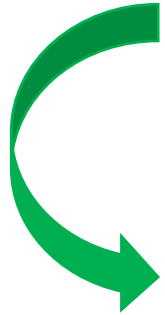


- **Example of purchased goodwill-Goodwill on merger; slump sale; etc**
- **Reversal of the SC caselaw in Smiff Securities Limited [(2012)348 ITR 302 (SC)]**

Clause-wise analysis of recent changes in TAR

Non-applicability of certain clauses

Reason for
this change

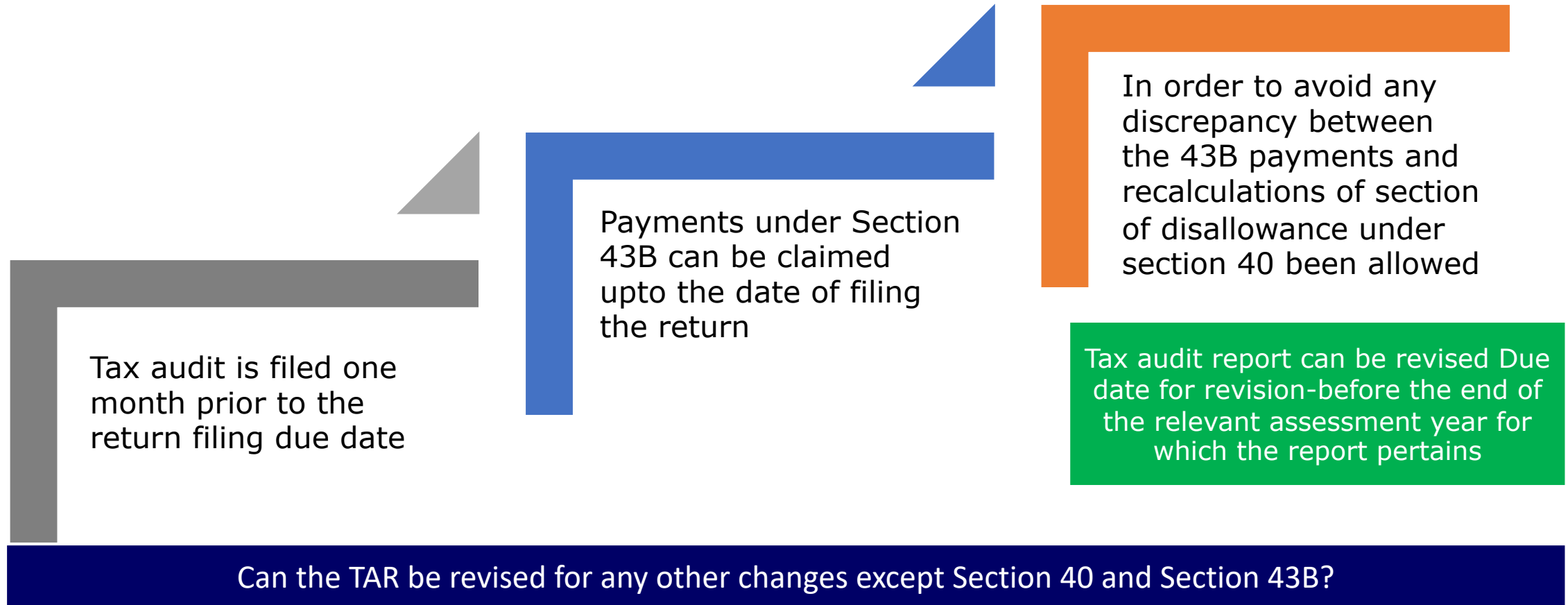


Clause 36 on DDT has been deleted

Finance Act 2020 abolished DDT and made dividends taxable in the hands of the receiver

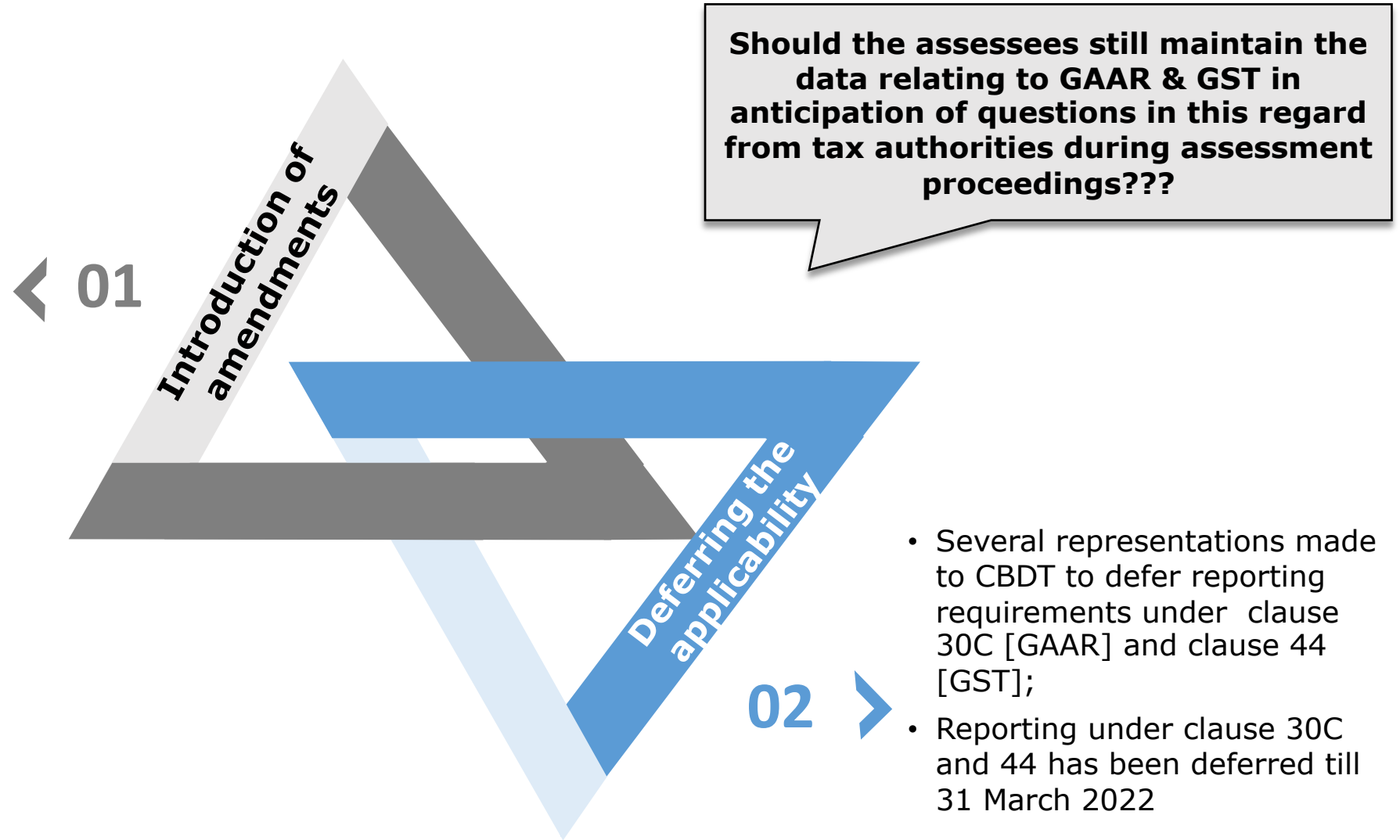
Clause-wise analysis of recent changes in TAR

Revision in tax audit



Non-Applicability of certain clauses for AY 2020-21

- Clause 30C- Details of impermissible avoidance agreement [GAAR]
- Clause 44- GST related date



Non-applicability of certain clauses for AY 2021-22

Clause 30C – Details of impermissible avoidance agreement [GAAR]

- Details of impermissible avoidance agreement as defined under section 96 of the Act to be disclosed; and
- An arrangement shall be presumed to be impermissible, **unless it is proved to the contrary by the assessee**, to have been entered into, or carried out, for the **main purpose of obtaining a tax benefit**.

Details to be furnished

- Nature of impermissible avoidance arrangement; and
- Amount of tax benefit in the previous year arising, in aggregate, to all the parties to the arrangement.

Challenges ahead and duties as tax auditor

- An impermissible avoidance agreement is generally alleged by the tax authorities and defended by the assessee;
- *Suo-moto* reporting on agreements entered into by the assessee may not be a welcome move for the industry;
- Examination of arrangements whose tax benefit is material in nature [above Rs. 3 crores];
- Agreements to be scrutinized in substance and not form;
- Discussion with management to understand the commercial viability of the transaction and reaching a consensus with the assessee that such agreement is an impermissible avoidance agreement; and
- Obtain management representations on debatable issues, if necessary.

GAAR

GAAR test

An arrangement aligns with one of the below pillars

creates rights, or obligations, which are not ordinarily created between persons dealing at arm's length
(no guidance given)

results, directly or indirectly, in the misuse, or abuse, of the provisions of this Act;
(no guidance given)

lacks commercial substance or is deemed to lack commercial substance under section 97, in whole or in part;
(further guidance given)

is entered into, or carried out, by means, or in a manner, which are not ordinarily employed for bona fide purposes
(no guidance given)

The main purpose of the arrangement is obtaining tax benefit

- The entire principle of GAAR tests has been developed on the foundation that the taxpayer has entered into an arrangement and that arrangement's main purpose is to obtain a tax benefit;
- The companies has entered into these transaction under post-GAAR regime, therefore the said transaction can be evaluated by the tax authorities, if any of the aforementioned criteria is fulfilled;
- The pillars hold the GAAR principles together in evaluating whether a transaction is an **impermissible avoidance arrangement;**
- Assesseees are required to demonstrate that the setting-up of an entity / transaction is entered because of the genuine need of the business. Accordingly, establishment of commercial expediency is necessary to pass the test of GAAR.

GAAR

How to evaluate its impact???

Understand commercial and other non-tax considerations of an arrangement or transaction

Identify main commercial purpose of arrangement or transaction

GAAR provisions

- Cannot be literally interpreted or applied
- Can be evaluated “in spirit” based on substance of an arrangement or transaction
- Can apply at a transaction level as well as at an entity level
- Apply to domestic as well as cross border arrangements

Evaluate alternate ways of undertaking same arrangement or transaction

Avoid 1:1 linkage between steps or parts of the arrangement or transaction

Back up analysis and conclusion with appropriate documentation and evidences

GAAR

Clarifications issued by CBDT

Interplay with SAAR

- The provisions of **GAAR and SAAR, can co-exist**, and will apply, as may be necessary, in the facts and circumstances of the case.

Interplay with tax treaty

- On the issue of interplay between GAAR and DTAs, that have an LOB clause in the DTA, the CBDT have given an **unclear clarification**, by stating that the LOB clause in a DTA may not be sufficient to address all tax avoidance strategies and the same are required to be tackled through domestic anti-avoidance rules. If a case of avoidance is sufficiently addressed by the LOB in the DTA, there shall not be an occasion to invoke GAAR; and
- If the **jurisdiction of an FII** is finalised based on non-tax commercial considerations and the main purpose of the arrangement is not to obtain a tax benefit, then GAAR will not apply.

Actions taken by taxpayers

- GAAR will not interplay with the **right of a tax payer to select** or choose the method of implementing a transaction; and
- GAAR will not be invoked merely on the ground that the **entity is located in a tax efficient jurisdiction**.

GAAR

Clarifications issued by CBDT

Judicious implementation

- GAAR will not apply to an arrangement that is held to be a “permissible arrangement” by the Authority for Advance Rulings in India;
- If the IRA and the GAAR Approving Panel have held an arrangement to be permissible in one year, and facts and circumstances remain the same, per the principle of consistency, GAAR will not be invoked for that arrangement in a subsequent year;
- GAAR will not apply to an arrangement sanctioned by the Court where the Court has explicitly and adequately considered the tax implications of the arrangement; and
- Clarified that (i) adequate safeguards are in place to ensure that GAAR is invoked only in deserving cases, and (ii) for invocation of GAAR, the case will first need to be approved by a Principal Commissioner of Income-tax or the Commissioner of Income-tax, and second by the GAAR Approving Panel which is to be headed by a High Court judge.

GAAR – as deterrent

- The period of time for which an arrangement exists is only a relevant factor and not a sufficient factor, to determine whether an arrangement lacks commercial substance;
- GAAR is an anti-avoidance provision with deterrent consequences and corresponding tax adjustments across different taxpayers could militate against deterrence; and
- Tax benefit limit of Rs. 3 crores cannot be read in respect of a single taxpayer and impact on all parties to the arrangement is to be considered.

GAAR

Clarifications issued by CBDT

Grandfathering benefits

- The grandfathering of investment provisions that relate to “transfer of investments” will be available to investments made before 1 April 2017 in respect of instruments that are **compulsorily convertible** from one form to another, at terms that are finalised at the time of issue of the such instruments;
- Grandfathering benefits would also be available in respect of shares acquired pursuant to a **share split or consolidation or bonus issue**, provided original shares were held before 1 April 2017; and
- Grandfathering benefits will not be available in respect of **lease contracts and loan arrangements**.

Others

- Clarified that (i) levy of penalty depends on the facts and circumstances of the case and is not automatic, and (ii) that no blanket exemption for a period for 5 years from the penalty provisions is available under the law.

Non-Applicability of certain clauses for AY 2021-22

Clause 44 – GST related details

- Break-up of expenditure w.r.t vendors from whom the services have been availed in terms of registered, unregistered, etc.; and
- Intention of the Government is to use data analytics to track tax evaders.

Details to be furnished

- Total amount of expenditure incurred during the year;
- Expenditure in respect of entities registered under GST; and
 - ✓ Relating to goods or services exempt from GST
 - ✓ Relating to entities falling under composition scheme;
 - ✓ Relating to other registered entities; and
 - ✓ Total payment to registered entities.
- Expenditure relating to entities not registered under GST.

Duties as tax auditor

- Onerous task for the assessee and tax auditor to classify each vendor into various categories; and
- No clarity on classification as on a cut-off date vs status of vendor throughout the year.

General issues in tax audit

Who needs to file TAR ?

- ✓ Persons in business and profession
- ✓ Having total sales, turnover or gross receipts more than Rs.1 crore in any previous year/ 5 cores with cash payments/ receipts less than 5%
- ✓ Professional income for more than Rs.50 lacs

Does a foreign company needs to file TAR in India?

- ✓ The section does not specify any exclusion for foreign companies
- ✓ Companies having PGBP are required to file TAR
- ✓ However, companies having India sourced income from royalties, FTS, etc. may not file TAR placing reliance on the decision of the Calcutta Tribunal in case Voest which states that “ROI filed without TAR in case of foreign companies is not invalid as long as income is not chargeable to tax in India” thereby indirectly meaning that, if foreign company earns India sourced business income, it is liable to file TAR

Penalty for not filing TAR

- ✓ Penalty for non-filing of TAR is Rs.1.5 lacs or 0.5% of the Turnover whichever is less
- ✓ None linked to the period of delay for filing of TAR- changes suggested?
- ✓ For the foreign companies if a PE is determined during the course of proceedings can a penalty be imposed on the foreign company for non-filing of TAR?

General issues in tax audit

Additional comments on specific clauses

- ✓ Specific comments by tax auditors may be given in the Form 3CA / 3CB subject to the space constraint; and
- ✓ It is advisable to make reference to the TAR signed by auditor where detailed comments can be provided and the same may be uploaded as 'other report' on the portal.
- ✓ However, important qualifications/ observations should be made in the Form only and not general comments is not advised to be provided in this report as well

TAR in case of joint auditors

- ✓ Joint auditors may mutually agree and decide which one of them will upload the report;
- ✓ However, all auditors are required to sign the hard copy of TAR; and
- ✓ In case the joint auditors are in disagreement, each one of them should express his / her opinion and upload the same on the portal.

Date of TAR vs date of furnishing TAR

- ✓ Date of TAR means the date on which TAR is physically signed by the tax auditor; and
- ✓ Date of furnishing the TAR means the date on which the report is uploaded on portal by the tax auditor.

General issues in tax audit

Clause 8 – Relevant clause of tax audit

- Rendering of professional services by corporates do not make them professionals [*Example - software development by engineers*]; and
- The relevant clause of tax audit would be (a) [Business] and not (b) [Profession].

Clause 11 – Books of account

Stock records in case of retail business

- Concept of materiality to be considered; and
- Professional judgement to be applied to ascertain whether absence of such records would affect reporting requirement [*Example – Retail business at electronic store vs groceries*].

Clause 11b – Maintenance of books of account

- Companies Act: maintenance of books of accounts
- Accounts maintained in cloud/ ERP package
- Is it required to have the server in India where the books are maintained?
- Assessee for whom tax authorities determine an existence of PE

General issues in tax audit

Clause 12 – Presumptive income

- Profits and gains assessable on presumptive basis, credited to profit and loss account, needs to be reported and not the *net* amount taxed under respective sections of the Act; and
- *Example – Two lines of business – consolidated profit and loss account - income of one business offered to tax on presumptive basis.*

Clause 15 : Conversion of capital asset into stock in trade

Conversion of capital asset into stock in trade is covered
Conversion of stock in trade into capital asset?
Does it need to be reported here?

General issues in tax audit

Clause 14 – Method of valuation of closing stock

Different methods for different businesses in case of non-corporates

- Different methods of valuation of closing stock for different businesses permissible in case of non-corporates [*Example – cash system for one line of business and accrual system for another*]; and
- Specific comments on such valuation of closing stock may be separately uploaded along with TAR.

Deduction under section 43B of the Act w.r.t excise duty on closing stock

- Deduction of excise duty is allowed only when the excise duty is paid on finished stock cleared / dispatched; and
- Excise duty paid in excess of amount payable cannot be claimed as deduction (Advance payment).

General issues in tax audit

Clause 21 & 26 – Disallowance of provision towards gratuity

Disallowance and allowance of provision towards un-approved gratuity fund

- Provision created for contribution towards un-approved gratuity fund disallowed under section 40A(7) of the Act; and
- Various approaches followed for claiming deduction on payment of gratuity:

Particulars	Approach 1	Approach 2	Approach 3
Provision created during the year	100	100	100
Reversal of provision out of current year provision	20	20	20
Payment / reversal of provision out of opening balance	10	10	10
Disallowance under section 40A(7) of the Act	70	80	100
Allowance under section 43B of the Act	-	10	-
Allowance under section 37 of the Act	-	-	30
Net disallowance in the current year	70	70	70

General issues in tax audit

Clause 21a – Amount debited to P/L account

- Capital in nature
- Personal expenditure
- Club entrance fees and subscription

Clause 21a : penalties

Expenditure by way of penalty or fine for violation of any law – Interest for late payment of GST vis a vis interest paid u/s 201

Expenditure by way of any other penalty or fine not covered above Expenditure incurred to set right pollution control violation

Expenditure incurred for any purpose which is an offence- e.g Hiring of lawyers to fight a case against prohibition introduced by a State Govt

General issues in tax audit

Clause 26 – Disallowance under section 43B of the Act

Whether performance incentive is covered by the provisions of section 43B of the Act?

- Bonus as per section 36(1)(ii) of the Act covers only that bonus which is related to the profit that a company makes;
- Performance incentive may not be covered under section 36(1)(ii) of the Act; and
- Courts have upheld this view; However, conservative position would be to disallow the same under section 43B of the Act.

Clause 16 & 27(b) – Prior period items

How are prior period items classified?

- Expenditure relating to earlier year, which has crystallized during the year is not treated as prior period item; and
- *Example – Dispute in wages for March 2017 settled and accounted during FY 2017-18.*

Prior period items in Ind-AS regime

- With introduction of Ind-AS, impact of prior period items is reinstated rather than routing it through profit & loss account; and
- Disclosure under clause 16 necessary when prior period incomes are not credited to profit & loss account by virtue of Ind-AS.

General issues in tax audit

Clause 32(b) – Impact on brought forward losses due to change in shareholding

- Assessee not allowed to carry forward and set-off losses if shareholding pattern changes by 51% or more as per section 79 of the Act; and
- Contradictory rulings available with respect to carry forward and set-off of losses in case of change in shareholding within the group; and
- Karnataka HC has ruled the matter in favour of assessee in CIT vs Amco Power Systems Ltd (2015) 379 ITR 375.

Clause 18 – Depreciation on low-value assets

- Many assessees have policy in place to write off assets costing less than a specified value [say Rs. 5 thousand] to profit and loss account; and
- However, assets are required to be capitalized from Re. 1 for tax purposes and corresponding depreciation may be claimed on the same.

THANK YOU!

The image features the words 'THANK YOU!' in a highly stylized, hand-painted font. Each letter is a different color: 'T' is pink, 'H' is green, 'A' is blue, 'N' is red, 'K' is yellow, 'Y' is red, 'O' is pink, and 'U' is green. The letters have a rough, textured appearance with visible brushstrokes and frayed edges. The text is surrounded by a multitude of small, colorful dots in shades of pink, blue, yellow, and green, resembling confetti or paint splatters. The entire graphic is set against a plain white background.