TAX AUDIT AS PAR INDIAN INCOME TAX ACT 1961

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ABSTRACT

Audit means "verification", depending on the purpose they are classified as Energy Audit, Environment Audit, Product Audit, Process Audit, Legal Audit in USA & Tax Audit in Indian Income-Tax Act. Here, person conducting audit should be specialized in that subject. Hence, the word "Audit" is not the domain of Chartered Accountants. Assessing officers of Income-Tax Deptt. who come from different streams conducting audit in scrutiny assessment proceedings are not Chartered Accountants. In conclusion, person specialized in Income-Tax law should issue Certificates/Reports in Income-Tax Act. Practice of law is the Prerogative Power of Advocates in India. Whereas practice of Cost Accounts, Management Accounts & Financial Accounts are not the prerogative powers of respective professional body. Because, penalty has been prescribed U/s 45 of Advocates Act, 1961 for persons illegally practicing the Profession of Law. Under Indian Constitution CAG are the Auditors with wide powers, carrying out meaningful job. Is an audit carried out by a tax collecting agency in order to determine if a taxpayer paid the correct amount of tax? Taxpayers are chosen for audits if they have suspiciously high claims for deductions or credits, or if their reported income is suspiciously low, but an audit may be done simply as part of a random sampling. If the auditor finds a tax deficiency, the taxpayer has to pay back-taxes, as well as interest and penalties.

Tax Audit: Section 44AB, applicability, due date and penalty

Due date of filing Income tax return for assesses who are liable to get their books of accounts audited is 30th September. Since the due date is nearing, let's get some points refreshed on section 44AB.

Who has to get his accounts audited compulsorily:

1.**A Person carrying on business** is required to get his books of account compulsorily audited u/s 44AB If the total sales, turnover or gross receipt in business for the previous year relevant to assessment year exceed or exceeds Rs. 60 Lakh for the Assessment year 2011-12 and 2012-13 (Rs. 1 Crore from the assessment year 2013-14).

2. **A person carrying on profession** is required to get his books of account compulsorily audited u/s 44AB, if his gross receipts in profession for the previous year relevant to the assessment year exceeds 15 lakh for the assessment year 2011-12 and 2012-13 (Rs. 25 lakh from the assessment year 2013-14).

3. **A person covered u/s 44AE, 44BB or 44BBB** is required to get his books of account compulsorily audited u/s 44AB if such person claims that the profits and gains from the business are lower than the profits and gains computed under these sections(irrespective of the turnover)

4. **A person covered u/s 44AD** is required to get his books of account compulsorily audited u/s 44AB if such person claims that the profits and gains from the business are lower than the profits and gains computed in accordance with the provisions of section 44AD(1) and if his income exceeds the maximum amount which is not changeable to tax(i.e basic exemption limit).

Forms and due date: Forms No. 3CA, Form No. 3CD in case of person who carries on business or profession and who is required by or under any law to get his accounts audited and Form No. 3CB and 3CD, in case of a person who carries on business or profession but not being a person referred to above.

Due date for getting the books audit and filing of return in both the above cases is the due date of furnishing return u/s 139(1) i.e 30th September of the relevant assessment year.

Audit under any other law: In case where the accounts are required to be audited by or under any other law (as in the case of companies and cooperative societies), it is sufficient if accounts are audited under such other law before September 30 of the assessment year and the assessee obtains before the said date, audit report as required under such law and also a report of audit from a chartered accountant in the audit forms under Income Tax Act i.e Forms No. 3CA, Form No. 3CD

No penalty u/s 271B if audit report obtained within due date but return filed after due date: After the introduction of new annexure less return forms, the audit report u/s 44AB is not required to be attached with the return. It should not be furnished separately also before or after the due date. However, an assessee should get the audit report before the due date of the furnishing of the return and should fill the relevant columns of return forms on the basis of such report. The assessee should retain the report with himself. It may be furnished at the time of assessment proceedings. No penalty shall be attracted for not furnishing the audit report on or before due date. However, if audit report is not obtained before due date, penalty u/s 271B shall be attracted.

Quantum of Penalty for failure to get accounts audited within due date: If any person fails to get his accounts audited as required under the provisions of section 44AB before the due date u/s 139(1), the AO may impose penalty which may be a sum equal to one-half percent of the total sales, turnover or gross receipts subject to a maximum of Rs. 1.5 Lakh.

Objective of the study

- To understand audit risk and penalty impose on assesses.
- To explain the Section – 44AB and their provisions in relation to tax audit.
- To describe the relationship between tax audit and Chartered Accountants.

Returns Are Selected for an Audit

The IRS uses many different factors when selecting which returns it is going to audit. The majority of tax audits are determined by computers. The IRS has several different computer systems that do various types of analysis on returns that do statistical analysis to score tax returns based on their likelihood of being correct. The IRS also chooses audits based off of other non computer related analysis as well, all methods are described below.

1. **The Discriminate Function System (DIF)**: The IRS has a computer program that is called the Discriminate Function System that gives each tax return a score. This score is called the DIF score. The score is a number that statistically determines the likelihood of the tax return being accurate. The higher the number that is assigned to the tax return, the higher the likelihood of that tax return being audited. The IRS does not share the details of how exactly their system works, but it is believed that there are several hundred variables that are weighed out and it is believed that deductions and exemptions claimed carry the biggest weights.

2. **The Unreported Income Discriminate Function (UIDIF)**: This is a second computer program that is used by the IRS that looks at different factors than the DIF system. The purpose of this program is to rate the return on its potential to have unreported income. This system scores people based upon expense and income ratio. Mainly what this is trying to determine is if an individual is spending more money than

they make and therefore likely have other income that they are not reporting to the IRS. It does happen sometimes that individuals do have low income years and this triggers an audit for them, but most of the time this can be explained easily to an auditor.

3.The Information Returns Processing System (IRP): This is a third computer system used by the IRS that stores massive amounts of data received from third parties that are required to report taxpayer income, such as employers, banks, brokerage firms, social security administration and other institutions that are required to report information to the IRS on taxpayers. For example, your employer is required to report to the IRS how much they paid their employees throughout the year. The IRS will then run their matching system to make sure the individual taxpayer reported everything that was already provided to the IRS. Using this system the IRS can find individuals that have likely under reported their income and they will follow up with an audit.

4. Incriminating Documents Turned Over to IRS: In rare cases tax returns will be selected to be audited based upon information that was obtained by the IRS in the effort to identify participants in tax avoidance transactions. Sometimes the IRS will get the courts to order information from the promoter to be handed over to the IRS. This information can point out individuals that were involved with the promoter's tax avoidance schemes.

5. Audits of Related Entities: If the IRS audited another tax return and that return involved transactions with other taxpayers such as investors or business partners and that return had a problem and it is likely that other individuals that are related to that entity/individual then it is a possibility that the IRS will then select those related tax returns to audit.

Types of Audits Once Selected

Once the IRS determines that it would like to follow through and get more information about your tax return, they will send a letter stating that your return has been selected for an audit. Below are the 3 different examination methods used by the IRS.

1. ***Correspondence Audit***: This is the most common type of audit and is done by mail. The IRS will normally request specific documentation to support particular items on the tax return.

2. ***Field Audit***: This is when the IRS wants to come to your home, place of business, or your tax professional's office to perform the audit. This is the least common form of audit and is only used if the individual or business being audited earned well over $100K.

3. ***Office Audit***: This is when you are required to go to an IRS office to meet with an IRS auditor. The IRS will determine the time and the particular documents that it would like you to bring for support.

Applicability of Tax Audit: Section 44AB of Income-tax Act provides for compulsory audit of accounts of certain persons carrying on business or profession.

Assessee	**Applicability**
Business	Every assessee, whose total sales or gross receipts in any previous year exceed Rs. 1 Crore, has to get his accounts audited.
Professional	Every assessee, whose gross receipts in any previous year exceed Rs.25 Lakhs, has to get his accounts audited.
Special Cases	Assessee covered u/s 44AD / 44AE / 44BB / 44BBB, if claim that profits from such activities are lower than presumptive income and his income exceed maximum exemption limit.

Tax Audit is the exclusive domain of Chartered Accountants only?

For overcoming this doubts, let's go to history, how this Tax Audit came into existence and how only CAs authorized for it? ICAI Financial, ICAI Cost, ICSI were established in 1949, 1959, 1980 respectively. Finance Act 1984 introduced Tax Audit u/s 44AB under Income Tax Act, 1961 w.e.f Assessment Year 1985-86. At that time, ICAI- Cost was just two years old and ICSI was not even established. At the time out of all professional institute only ICAI- Financial was completely established and had good members' strength therefore non-inclusion of CMAs/CS in

Accountant definition and only authorizing CAs, at that time is justified. But now ICAI- Cost is more than 50 years old with good member strength too, and its members efficiently doing audit of Excise Duty, Service Tax, VAT etc. because of this, now government decided to take their services in income tax too. So thinking that Tax Audit is the exclusive domain of Chartered Accountants only, is completely wrong.

Are CMAs competent enough to handle Tax Audit?

Syllabus, Exam procedure and Passing percentage of both ICAI are same. Perception is that because of their 3 years article ship training CAs has more practical experience to trickle Tax Audit cases. Here the study make it clear, CMA become eligible for practice only after 3 years of post-qualification experience and no one can disagree that having post qualification experience as a professional is far better than having article ship experience as trainee. Assessing officers of Income-Tax Department, who come from different streams conducting audit and scrutinizing assessment proceedings are not CA. They are able to do because of their experience they gain after joining these jobs. CMAs are already conducting taxation audit of Excise Duty, Service Tax VAT etc, then why not Income Tax. We explained above why their name was not included earlier, now that limitation had been over and that why government authorised them in the field of Income tax too.

Conclusion:

Government has shown confidence on CMAs and them worth it. They have required knowledge, skill and efficiently doing taxation audit of Excise Duty, Service Tax VAT etc. Go to any MNC/PSU, one can easily find CMAs doing jobs as Manager – Taxation, Manager – Accounts, Manager – Credit etc. and some are holding top management positions. so doubting their professional efficiency is completely senseless. Give some time, India will see great impact of their service in Income Tax.