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Tax Alert - Maintenance of books of accounts under the Income Tax Act, 1961

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Direct Tax

MAINTENANCE OF BOOKS OF ACCOUNTS UNDER THE INCOME TAX ACT, 1961

Section 44AA of the Income Tax Act, 1961 ("the Act") provides for maintenance of accounts by certain persons carrying on profession or business. Section 44AA reads as under:

"(1) Every person carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or any other profession as is notified by the Board in the Official Gazette shall keep and maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of this Act.

(2) Every person carrying on business or profession [not being a profession referred to in sub-section (1)] shall,—

(i) if his income from business or profession exceeds one lakh twenty thousand rupees or his total sales, turnover or gross receipts, as the case may be, in business or profession exceed or exceeds ten lakh rupees in any one of the three years immediately preceding the previous year; or

(ii) where the business or profession is newly set up in any previous year, if his income from business or profession is likely to exceed one lakh twenty thousand rupees or his total sales, turnover or gross receipts, as the case may be, in business or profession are or is likely to exceed ten lakh rupees, during such previous year; or

(iii) where the profits and gains from the business are deemed to be the profits and gains of the assessee under section 44AEor section 44BB or section 44BBB, as the case may be, and the assessee has claimed his income to be lower than the profits or gains so deemed to be the profits and gains of his business, as the case may be, during such previous year; or

(iv) where the provisions of sub-section (4) of section 44AD are applicable in his case and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year,

keep and maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of this Act.

Provided that in the case of a person being an individual or a Hindu undivided family, the provisions of clause (i) and clause (ii) shall have effect, as if for the words "one lakh twenty thousand rupees", the words "two lakh fifty thousand rupees" had been substituted:

Provided further that in the case of a person being an individual or a Hindu undivided family, the provisions of clause (i) and clause (ii) shall have effect, as if for the words "ten lakh rupees", the words "twenty-five lakh rupees" had been substituted.

(3) The Board may, having regard to the nature of the business or profession carried on by any class of persons, prescribe, by rules, the books of account and other documents (including inventories, wherever necessary) to be kept and maintained under sub-section (1) or sub-section (2), the particulars to be contained therein and the form and the manner in which and the place at which they shall be kept and maintained.

(4) Without prejudice to the provisions of sub-section (3), the Board may prescribe, by rules, the period for which the books of account and other documents to be kept and maintained under sub-section (1) or sub-section (2) shall be retained."

Therefore, sub-section (1) of section 44AA provides that books of account are to be maintained by assessees carrying on a specified profession while sub-section (2) of section 44AA is meant for other assessees, not covered by sub-section (1) i.e. assesses carrying on business or non-specified professions.

Rule 6F of the Income-tax Rules, 1962 prescribes books of accounts and other documents to be kept and maintained under section 44AA(3) by person carrying on certain professions.Sub-rule (1) of Rule 6F provides for the category of professionals (here-in-after referred to as "specified professionals") for whom the said Rule has been prescribed. Sub-rule (2) and (3) specifies the books of account and other documents which are required to be maintained by the specified professionals while sub-rule (4) specifies the place such books must be kept.

Rule 6F(5) provides that the books of account and other documents specified in sub-rule (2) and sub-rule (3) shall be kept and maintained for a period of six years from the end of the relevant assessment year. However, where the assessment in relation to any assessment year has been reopened under section 147 of the Act within the period specified in section 149 of the Act, all the books of account and other documents which were kept and maintained at the time of reopening of the assessment shall continue to be so kept and maintained till the assessment so reopened has been completed.

Therefore, Rule 6F of the Income Tax Rules, 1962 clearly lays down the books of accounts to be kept, place and time period for which they are to be maintained by specified professionals, covered under Section 44AA of the Act. However, no such rules have been prescribed for assessees carrying on business or non-specified profession, to whom sub-section (2) of Section 44AA of the Act is applicable. This fact has also been observed and noted by various courts while dealing with penalty imposed on the assessees under Section 271A for failure to maintain books of accounts as required under Section 44AA of the Act. Some of such cases are:

- K.V. Ramachandranv.DCIT, Circle 1(1), Kannur[2013] 32 taxmann.com 200 (Cochin - Trib.)
- Mehta Parveshvs Income-Tax Officer(1998) 60 TTJ (Del) 278
- Sujan Singh vs Assessing Officer(2007) 110 TTJ (Asr) 818
- ITO v. Dinesh Paper Mart (1999) 70 ITD 274 (Nag)

Therefore,in absence of express rules prescribed for assessees covered under Section 44AA(2), assesseesthereunder are required to keep and maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Act.

So the issue that arises for consideration is as to what would constitute proper 'maintenance of accounts' to the satisfaction of the Assessing Officer and for what time span such books of accounts should be maintained by thoseassessees who do not fall within the ambit of Rule 6F.

Section 2(12A) of the Act defines "books or books of account" to include ledgers, day-books, cash books, account-books and other books, whether kept in the written form or as print-outs of data stored in a floppy, disc, tape or any other form of electro-magnetic data storage device.

Section 139(9) of the Act while dealing with defective returns prescribes that where regular books of account are maintained,the return of income should be accompanied by manufacturing account, trading account, profit and loss account or, as the case may be, income and expenditure account or any other similar account and balance sheet, and in the case of a proprietary business or profession, the personal account of the proprietor; in the case of a firm, association of persons or body of individuals, personal accounts of the partners or members; and in the case of a partner or member of a firm, association of persons or body of individuals, also his personal account in the firm, association of persons or body of individuals.

Section 145 of the Act provides that income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" shallbe computed in accordance with either cash or mercantile system of accounting regularly employedby the assesse, and that where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting has not been regularly followed by the assessee, or income has not been computed in accordance with the standards notified thereunder, the Assessing Officer may make an assessment in the manner provided in section 144 i.e. an ex-parte assessment.

Thus, although the Act does not prescribe the manner in which the books of accounts should be maintained byassessees covered under Section 44AA(2) of the Act, it is required of the assessees to maintain accounts in the normal course of businessconsistently applying the prescribed method of accounting soto escape the rigors of best judgement assessment under Section 144 or levy of penalty under Section 271A for failure to maintain books of accounts as required under Section 44AA of the Act. It is however, subject to the satisfaction of the Assessing Officer or the revenue/ appellate authoritiesto judge the sufficiency and correctness of the books so maintained.

Apropos the time span for which such books should be maintained, Section 44AA(2) requires assessees to maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of this Act. Besides regular assessment, the income of an assessee for a previous year can be subjected to reassessment under Section 147 of the Act.

Section 149 of the Act provides for the following time limits within which the assessments can be reopened for assessment under Section 147 of the Act –

a) if four years have elapsed from the end of the relevant assessment year, unless the case falls under clause (b) or clause (c);
b) if four years, but not more than six years, have elapsed from the end of the relevant assessment year unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to one lakh rupees or more for that year;
c) if four years, but not more than sixteen years, have elapsed from the end of the relevant assessment year unless the income in relation to any asset (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment.

Therefore, in view of the above time limits an assessee is required to maintain books of accounts and such other documents so as to enable the Assessing Officer to complete his assessment, for at least six years from the end of the relevant assessment yeari.e. for seven financial years if he is not assessable with respect to any income from any asset (including financial interest in any entity) located outside India.

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