GUIDELINES FOR PERSONS CARRYING BUSINESS / PROFESSION

Profits and gains from business or profession

Business includes any trade, commerce, manufacture or any adventure or concern in the nature of trade, commerce of manufacturing. Under this chapter, any income from the exercise of any profession will also be taxed.

Let us understand the expenses which are allowable in computing the taxable business / professional income.

Rent, rates, taxes, land revenue, municipal taxes, repairs and insurance premium paid or payable for business premises or insuring them against damage will be allowed as a deduction in determining business or professional profits.

Repairs and Insurance of palnt, machinery and furniture Any expenditure incurred by way of repairs and insurance of machinery, plant and furniture used for the purpose of business or profession will be allowed as expense.

Depreciation is allowed as a deduction on fixed assets used for the purpose of business on the value as per income tax records. The following are the conditions for claiming depreciation as a deduction:-

- The concerned assets must be owned either wholly or partly by the assesee.
- The assets must be used for the assesee business or profession
- The asset must be used for the for the assesee's business or profession in the relevant previous year in respect of which depreciation is claimed.

Under the Income Tax Act depreciation is allowed on the return down value of the asset as per the income tax records

Expenses Expressly Disallowed

Certain expenses will not be allowed as a deduction in obtaining the amount of taxable income. The following expenses have been expressly disallowed:-

1. Any interest, royalty or fees paid for technical services chargeable to tax under the Income Tax Act which is payable outside India will not be allowed as a deduction if tax has not been paid on those amounts or deducted at source in accordance with the provisions of the Income Tax Act. If however at a later date, tax on such amounts is paid or deducted at source such amounts will be allowed as deduction in the year in which the tax has been paid or deducted.

2. Income Tax payable or paid will not be allowed as a expenditure in computing the amount of taxable income

3. Wealth tax payable or paid on the wealth of the assessee will not be allowed as a deduction.

4. Salaries payable outside India on which tax has to be deducted but on which tax has not actually been deducted will not be allowed as a deduction. However such salaries will be allowed as a deduction in the year in which the tax has been paid in respect of the salary.

5. Payments of provident fund or other funds established for the benefits of the employees of the assesee will not be allowed as a deduction unless the provident fund is recognised or is a statutory provident fund or the other fund for welfare of the employees is recognised under any law for the time being in force. Such payment will not be allowed as a deduction if tax has not been deducted in the year in which such payments have been made. However these payments will be allowed as a deduction in the year in which tax has been paid.

6. Any expenditure incurred by way of advertisement expenses for giving an advertisement in any publication of a political party will not be allowed as a deduction.

7. Any expenditure resulting in any payment to any specified person will be disallowed to the extent it is excessive or unreasonable, having regard to the market value of the goods or services and the benefit to the business or profession. The specified persons stated above include the relatives of the assesee or persons who have substantial interest in the assesses's business or profession.

8. Payments exceeding Rs20,000 other than by way of crossed cheque or demand draft. Where in respect of any expenditure, payment exceeding Rs20,000 is made otherwise than by way of crossed bank cheque or draft, 20per cent of this expenditure will be disallowed and only the balance 80 per cent will be allowed as a deduction. This provision has been inserted with a view to encourage cheque payments. However, Rule 6D provides that in the following cases, no disallowance will be made even if the payment exceeds Rs20,000 and is made otherwise than by way of crossed cheque or crossed bank draft:-

- Payments made to bank or financial institutions
- Payments made through the banking system i.e. by letters of credit or mail or telegraphic transfer or through book adjustment in an account in the bank with any other account in that or any other bank or through bills of exchange payable only to a bank.
- Payments by way of book adjustment against payee's liabilities to the assessee for goods supplied or services rendered.
- Payments for purchase of agriculture or forestry products or produce of animal husbandry, dairy or poultry farming, or fish or fish product or product of horticulture or sericulture provided the payment is made to the cultivator, grower or producer of such articles and not to a trader or dealer in such products.
- Payments to the producer for purchase of products manufactured or produced in a cottage industry without the aid of power.
- Payment to a person ordinarily residing or carrying on business in a village, which does not have any branch of a bank.
- Payment of gratuity, retrenchment, compensation or other similar terminal benefits to an employee whose salary income does not exceed Rs7,500 in the year of retirement.

Important provision

No person can take or accept from any other person any loan or deposit in excess of Rs20,000 in cash or by bearer cheque. Such loans or deposits in excess of Rs20,000 must be by way of an account payee cheque or an account payee bank draft.

Similarly no company or co-operative society or firm shall repay a deposit in excess of Rs20,000 in cash or by bearer cheque.

Contravention of the above provision may lead to penalty of upto the amount of such loan taken or repaid in cash or by bearer cheque.

Deduction only on payment basis

Under Section 43B, certain expenses will be allowed as a deduction only if they are paid on or before the due date of filing the return of income. These include:-

- Any sum payable by way of any tax, duty, cess, or fee under any law.
- Any sum payable by way of bonus or commission to employee, provided such bonus or commission is not by way of distribution of dividend so profits.
- Any interest on borrowings from public financial institutions as per terms and conditions of the borrowings.
- Any interest on term loans taken from scheduled banks.
- Any sum payable to employees in lieu of any leave at the credit of employee (leave encashment)

However in respect of the above expenses, if payment is made at a later date, then deduction will be allowed in the year of payment.

Maintenance of books of accounts and other records by certain persons Under Section 44AA, certain records and books of accounts have to be maintained by the assessee. A person carrying on the profession in legal, medical, engineering, architecture, accountancy or technical consultancy or interior decoration or authorised representative or film artist or company secretary is required to keep and maintain books of accounts and other documents as specified under:-

- Cash Book i.e. records of all cash receipts and payment maintained from day to day basis and giving the cash balance at the end of each day.
- A journal if the accounts are maintain according to the mercantile system of accounting.
- A ledger
- Carbon copy of machine numbered or serially numbered bills and receipts over Rs25 wherever such bills or receipts are issued.
- Original bills wherever issued to the person and receipts in respect of expenditure incurred by the person or where the bills or receipts are not issued and the expenditure exceeds Rs50, such payment voucher must be prepared and signed by the person authorising the same.

The books of accounts and other relevant documents are required to be kept and maintained at a principal place of business. These documents must be preserved for a period of eight years from the end of relevant assessment year. However cashbook and ledger are required to be preserved on for a period of 15 years.

Any person carrying on profession other than above mentioned professions is required to maintain books of accounts and documents only if his annual income from the profession or business exceeds Rs120,000 or the gross receipts and turnover from the business or profession exceeds Rs one million in any one of the three years immediately preceding the previous year. If the income or the turnover is below the prescribed limits then only reasonable records need be maintained so as to determine his income.

Failure to keep, maintain and retain such records or documents invite penalty of Rs2,000 minimum or a maximum of Rs100,000.

Audit of accounts of certain persons Under Section 44AB, it is obligatory for a person to get his accounts audited before the specified date by a chartered accountant if the total sales turnover or gross receipts from the business for the accounting year exceeds Rs four million. A person carrying on profession also has to get his accounts audited if his gross receipt from the profession in that accounting year exceeds Rs one million. Specified date in this connection means the 31st of October of the relevant assessment year in case of a non corporate assesee and 30th of November in case of a corporate assesee.

Hints for Tax Planning

1. Since depreciation for the whole year is allowed only if the asset is purchased prior to October of the relevant previous year, depreciable assets must be purchased in the first half of the year. Otherwise only 50 per cent of the depreciation will be allowed as deduction.

2. Expenses falling u/s 43 B such as taxes, duties, cess payable to the government, interest on borrowings from financial institutions, etc taxes which are allowed as a deduction only on payment basis must be paid on or before the prescribed time for making payment.

3. Since only 80 per cent of the total expenditure paid otherwise than by account payee cheque or bank draft is allowed as a deduction, cash payments in excess of Rs20,000 must be avoided.