

PROFIT AND GAINS FROM BUSINESS / PROFESSION

SECTION 28-44D

As per section 28, income from any Business / Profession shall be taxable under the head Business / Profession.

Business – Section 2(13)

“Business” includes any Trade, Commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture

Profession – Section 2(36)

“Profession” includes Vocation

INCOMES CHARGEABLE TO TAX UNDER THE HEAD BUSINESS / PROFESSION

SECTION 28

- Income from **speculation business** shall be taxable under head Business / Profession.

Meaning of Speculative Business

Section 43(5)

A Speculative transaction is defined under Section 43(5) to mean a transaction in which a contract for purchase or sale of a commodity including stocks or shares is periodically or ultimately settled otherwise than by actual delivery or transfer of the commodity or scrip.

The following shall not be treated as speculative transaction:

- A contract in respect of Raw material or merchandise entered in the normal course of business to guard against loss due to price fluctuations.
 - A contract in respect of stocks and shares entered into by a dealer or investor to guard against loss through price fluctuations.
 - A contract entered into by a member of forward market or a stock exchange in the course of jobbing or arbitrage to guard against loss in the ordinary case.
- Any payment received by the employer under **Keyman Insurance Policy** shall be considered to be income under the head Business / Profession.
 - Any **benefit or perquisite** in connection with Business / Profession
 - **For Example:** ABC Ltd. has engaged one Advocate with regard to its Legal Proceedings. The Company has provided him facilities of free traveling, boarding/lodging and has incurred Rs. 25,000, it will be considered to be professional receipt of the Advocate.
 - Any payment received **for not pursuing any business activity** shall be taxable under head Business / Profession.
 - **For Example:** If Pepsi Food Ltd. has paid Rs. 100 Crores to Campa Cola for not pursuing business activity, it will be considered to be the income of Campa Cola under the head Business / Profession.

Similarly, if any payment has been given for not sharing any patent right, technical know-how, copy right etc., the amount received is income under the head Business / Profession.

If any payment has been given for closing down any business which is harmful to ozone layer (O₃ Layer), such compensation received shall not be taxable under the head Business / Profession.

- Any **compensation received:**
 - By any person, managing **affairs of an Indian Company**, in connection with the termination of his management or the modification of the terms and conditions.
 - By any person, managing the **affairs in India of any other company**, in connection with the termination of his office or the modification of the terms and conditions.
 - By any person, **holding any agency in India relating to the business of any other person**, in connection with the termination of the agency or the modification of the terms and conditions.
 - By any person, **in connection with the vesting in the Government, or in any corporation owned or controlled by the Government**, of the management of any property or business.
- If any **trade or profession association has income**, such income is exempt from Income Tax under Section 10(23A), but if such associations are **rendering specific services** to their members on payment basis, the income received shall be Taxable.
 - **For Example:** Chambers of Commerce is providing specialized Training in Export Management and is charging Rs. 30,000 from the participants; in this case income is taxable.
- If any person has received any export incentive like **Duty Draw Back or profits on sale of Import Entitlement Licenses**, such export incentives shall be considered to be the income under the head Business / Profession.
 - Duty Draw Back:** If any manufacturer has paid excise duty or custom duty in connection with the goods manufactures by him & subsequently such goods have been exported by him, in such cases excise duty or custom duty is refunded to him as an incentive & it is called Duty Draw Back, i.e., drawing back the duty paid by a person.
 - Import Entitlement Licenses:** Exporters are issued import license in which import is allowed without payment of custom duty & further the exporters are allowed to sell it in the market & any profit received on their sale shall be considered to be income under the head Business / Profession.

9. Any interest, salary, bonus, commission or remuneration, by whatever name called, received by partner of a firm from such firm, and shall be considered to be his income under the head Business / Profession subject to the provisions of Section 40(b)

COMPUTATION OF INCOME UNDER THE HEAD BUSINESS / PROFESSION

SECTION 29

The Income referred to in Section 28 shall be computed in accordance with the provisions contained in Sections 30 to 43D.

EXPENDITURE RELATING TO BUILDING

SECTION 30

OWNED BY ASSESSEE	TAKEN ON RENT
Current repairs. (Earlier years repairs not allowed)	Current repairs.(Earlier years repairs not allowed) if borne by lessee
Municipal Tax or Local tax or Land Revenue subject to provisions of Section 43B	Municipal Tax or Local tax or Land Revenue subject to provisions of Section 43B if borne by lessee
Premium for Insurance of House	Premium for Insurance of House if borne by lessee
	Rent for the Building.

EXPENDITURE RELATING TO PLANT & MACHINERY/FURNITURE & FIXTURES

SECTION 31

OWNED BY ASSESSEE	TAKEN ON RENT
Current repairs. (Earlier years repairs not allowed)	Current repairs.(Earlier years repairs not allowed) if borne by lessee
Municipal Tax or Local tax or Land Revenue subject to provisions of Section 43B	Municipal Tax or Local tax or Land Revenue subject to provisions of Section 43B if borne by lessee
Premium for Insurance of House	Premium for Insurance of House if borne by lessee
	Rent for the Plant & Machinery/Furniture & Fixture

DEPRECIATION

(SECTION 32)

Depreciation under Income Tax Act is allowed on the basis of W.D.V. (SLM is not allowed) and further rates of depreciation are as given below:

S.NO.	PARTICULARS	RATE OF DEPRECIATION
	<u>BUILDINGS</u>	
1	Residential Building (<i>Except Hotel and Boarding Houses</i>)	5%
	Other Buildings (<i>Like Commercial Building</i>)	10%
	Temporary Structure Buildings (<i>Wooden Houses, Mud Houses Etc.</i>)	100%
2	Roads, Wells, Tube wells, Bridges Etc.	10%
3	Furniture & Fittings (<i>Including Electrical Fittings</i>)	10%
4	Plant & Machinery	15%
	<u>MOTOR CARS AND VEHICLES</u>	
5	Motor Cars	15%
	Motor Cars for Tourist Purpose	30%
	Commercial Vehicles	40%
	Aero plane	40%
	Ships	20%
6	Computer Including Computer Software	60%
	<u>BOOKS</u>	
7	Books Being Annual Publication	100%
	Books for Purpose of Library	100%
	Other Books	60%
8	Intangible Assets (<i>Trade Marks, Patent Rights, Technical Know-how, Copy Rights, Licenses, Franchises, or any other Similar Right</i>)	25%

Computation of Depreciation

1. **Purchased and "Put to use" for less than 180 days:** Depreciation shall be allowed at half the normal rate.
 2. **Purchased and "Put to use" for more than 180 days:** Depreciation shall be allowed at full rate.
 3. **Purchased and is not "Put to use" at all:** No depreciation is allowed and if the asset is put to use in the subsequent year full depreciation shall be allowed without calculation of days.
 - **For example:** Mr. X has purchased one asset on 1-4-2007 and has put to use on 31-3-2009 in that case, no depreciation shall be allowed in the P.Y. 07-08, however in the P.Y. 08-09 full depreciation is allowed even it is used for a single day.
 4. **Asset sold During the year:** No depreciation is allowed on such particular asset.
- NOTE:** "Put to use" do not mean actual use rather it means making an asset ready for use.

Block of Asset

Depreciation under Income Tax Act is not allowed on the basis of individual asset rather depreciation is allowed on the basis of block of assets which means a group of similar type of assets having same rate of depreciation.

Depreciation on the basis of block of assets shall be computed in the manner given below:

1. Take opening W.D.V. of the block.
2. **Add purchases** during the same year of that particular block.
3. **Deduct Sale price / Insurance Claim / Scrap Value** of all the assets sold during the year relating to the same block.
4. Depreciation shall be charged on the balance at the end of the year.
 - **For Example:** ABC Ltd. has Plant P₁, P₂, P₃, and P₄ as on 1/4/2007 and the combined W.D.V. is. Rs.70 Lac. The company has purchased Plant P₅ on 1/7/2007 and it was put to use on the same date & it was purchased for Rs. 20lac & the company has sold Plant P₁ on 1/1/2008 for Rs. 15 Lac.

W.D.V. as on 1/4/2007	70 Lac
Add: P ₅	20 Lac
Less: P ₁	(15 Lac)
	<u>75 Lac</u>
Less: Depreciation @ 15%	(11.25 Lac)
Closing W.D.V. as on 31/3/2008	<u>63.75 Lac</u>
5. If any asset was purchased during the year and was put to use for less than 180 days, in that case depreciation shall be allowed at half the normal rate for that particular asset.
 - **For Example:** ABC Ltd. has Plant P₁, P₂, P₃, and P₄ as on 1/4/2007 and the combined W.D.V. is. Rs.70 Lac. The company has purchased Plant P₅ on 1/7/2007 and it was put to use on 1/11/2007 & it was purchased for Rs. 20lac & the company has sold Plant P₁ on 1/1/2008 for Rs. 15 Lac.

W.D.V. as on 1/4/2007	70 Lac
Add: P ₅	20 Lac
Less: P ₁	(15 Lac)
	<u>75 Lac</u>
Less: Depreciation @ 15% on 55 Lac	(8.25 Lac)
Less: Depreciation @ 7.5% on 20 Lac	(1.50 Lac)
Closing W.D.V. as on 31/3/2008	<u>65.25 Lac</u>
6. If any asset was put to use for less than 180 days & the balance left at the end of the year is less than the value of such asset, in that case, depreciation shall be charged at half the normal rate on such balance.
 - **For Example:** ABC Ltd. has Plant P₁, P₂, P₃, and P₄ as on 1/4/2007 and the combined W.D.V. is. Rs.70 Lac. The company has purchased Plant P₅ on 1/7/2007 and it was put to use on 1/11/2007 & it was purchased for Rs. 20lac & the company has sold Plant P₁ on 1/1/2008 for Rs. 80 Lac.

W.D.V. as on 1/4/2007	70 Lac
Add: P ₅	20 Lac
Less: P ₁	(80 Lac)
	<u>10 Lac</u>
Less: Depreciation @ 7.5% on 10 Lac	(75000)
Closing W.D.V. as on 31/3/2008	<u>9.25 Lac</u>
7. If all the asset have been sold but still there is some balance it will be called **Short Term Loss** under **Section 50** & no depreciation is allowed.
 - **For Example:** ABC Ltd. has Plant P₁, P₂, P₃, and P₄ as on 1/4/2007 and the combined W.D.V. is. Rs.70 Lac. The company has sold Plant P₁, P₂, P₃, and P₄ on 1/1/2008 for Rs. 40 Lac.

W.D.V. as on 1/4/2007	70 Lac
Less: P ₁ , P ₂ , P ₃ , and P ₄	(40 Lac)
	<u>30 Lac</u>
Short Term Loss under Section 50	<u>Rs. 30 Lac</u>

8. If there is **Negative Balance**, it will be **Short Term Gain** under **Section 50** and no depreciation is allowed.
- **For Example:** ABC Ltd. has Plant P₁, P₂, P₃, and P₄ as on 1/4/2007 and the combined W.D.V. is. Rs.70 Lac. The company has sold Plant P₁, P₂, P₃, and P₄ on 1/1/2008 for Rs. 80 Lac.
- | | |
|---|-------------------|
| W.D.V. as on 1/4/2007 | 70 Lac |
| Less: P ₁ , P ₂ , P ₃ , and P ₄ | (80 Lac) |
| | (10 Lac) |
| Short Term Gain under Section 50 | Rs. 10 Lac |

Depreciation in case of Amalgamation / De merger / Conversion of Proprietary Concern Into Company / Conversion of Partnership Firm Into Company. **Section – fifth proviso to section 32**

In case of Amalgamation, De merger etc. depreciation shall be computed as if no such amalgamation etc. has taken place & the depreciation so computed shall be apportioned between the predecessor & successor on the basis of number of days the asset was used by each one of them.

Depreciation in case of Power generating or generating and distributing of units **Section 32(1)(i)**

Power generating units shall have the option to claim depreciation **either on the basis of W.D.V. or on the basis of S.L.M.** & option once exercised has to be followed **consistently** if the assessee has opted for depreciation on the basis of **W.D.V.**, depreciation shall be allowed on the basis of **block of assets**. If the assessee has opted **SLM**, depreciation shall be allowed on the basis of **individual asset** and further at the prescribed rate. However concept of 180 days shall be applicable.

If the assessee has opted for **depreciation on the basis of SLM** & subsequently the asset was sold by the assessee, any loss shall be called **Terminal Depreciation** & shall be debited to P&L Account.

If the asset has been sold at a profit, it will be considered to be income under head Business / Profession & shall be called **Balancing Charge** under **Section 41(2)**, but only to the extent depreciation has been debited & any excess over it shall be considered to be STCG under **Section 50A**.

- **For Example:** ABC Ltd is a power generating unit & the company has purchased one plant on 1.10.2005 for Rs. 10 Lac & rate of depreciation on the basis of SLM is 7.8%, the asset was put to use on 1.11.2005 & subsequently the same asset was sold on 1.05.2005 for Rs. 12 Lac, and accordingly there is a profit of Rs. 317000 [$1200000 - (\text{cost}) 1000000 - (\text{depreciation for PY 05-06}) 39000 - (\text{depreciation for PY 06-07}) 78000$], out of which balancing charge under section 41(2) shall be Rs. 117000 ($39000 + 78000$) and excess over it i.e. Rs. 200000 shall be STCG under section 50A.

Additional Depreciation **Section – 32(1)(ia)**

Additional Depreciation is allowed @ **20%** to all assesses & further it is allowed if all the given conditions are satisfied:

1. It should be **Plant and Machinery** which has been **acquired** and **installed after the 31.03.2005**.
2. Such Plant and Machinery should be used for the purpose of **manufacturing**.
3. It will be allowed only **once in a year**.

Additional Depreciation is **not allowed** in the following cases:

1. **Second Hand** Plant and Machinery.
2. Plant and Machinery used in **office building** or **residential building**.
3. Any **Machinery** or **Plant**, the **whole of the actual cost** of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head Business / Profession of any one previous year.
4. If the **Plant and Machinery** is being put to use for **less than 180 days** than additional depreciation shall be allowed @ **10%**, and the **remaining 10% shall not be allowed** in the subsequent year.

Depreciation in case of Slump Sale

Sale of particular unit or division for lump sum consideration is called **“Slump Sale”**

In case of slump sale if any particular asset has been sold, actual depreciation shall be computed for such asset up to assessment year 87-88 and for the subsequent period notional depreciation shall be computed & total depreciation shall be deducted from the original cost of such asset & the WDV shall be computed in this manner and it will be deducted from the WDV of the block of asset.

- **For example:** ABC Ltd has one block of asset of Plant and Machinery with WDV Rs. 18 Lac on 1.04.2008 and the block contains 25 Plant and Machinery. The company has sold one of its units in slump sale for Rs. 75 Lac & there were 10 Plant and Machinery in that particular unit. Original cost of such Plant and Machinery is Rs. 25 Lac & actual depreciation up to A.Y. 87-88 is Rs. 10 Lac & notional depreciation from A.Y. 88-89 onwards is Rs. 11 Lac, in this case WDV of Rs. 10 Plant and Machinery shall be Rs. 4 Lac (**25 – 10 – 11**)
WDV of Rs. 4 Lac shall be deducted from the WDV of the block of assets. i.e.
 $18 \text{ Lac} - 4 \text{ Lac} = 14 \text{ Lac}$ (WDV of 15 Plant and Machinery)

Basic Conditions for claiming Depreciation

For the purpose of claiming depreciation, the assessee must satisfy the following conditions:

1. The assessee must be the owner of the asset. The ownership may be whole or fractional.
2. The asset must be used for the purpose of carrying on the Business / Profession of the assessee.
3. In the year of acquisition, if the asset is put to use for less than 180 days, then it is eligible for only 50% of the normal depreciation.

4. The asset in respect of which depreciation is claimed should fall within the eligible classification of assets.

Is it Mandatory to claim depreciation?

As per explanation 5 to section 32(1), it is mandatory for every assessee to claim depreciation.

Explanation 5- For the removal of doubts, it is hereby declared that the provisions of this sub section apply whether or not the assessee has claimed the deduction in respect of depreciation in computing his total income.

Depreciation in case of assets not owned by the assessee.

If the business of the assessee is carried on in a building not owned by him but in respect of which the assessee holds a lease right of occupancy and any capital expenditure is incurred by the assessee on the construction, renovation, extension, improvement etc. to the building, the assessee shall be eligible for depreciation in the normal manner and it do not matter that the assessee is not the owner.

TEA/COFFEE/RUBBER DEVELOPMENT ACCOUNT

SECTION 33AB

Deduction is allowed to all the assesses who are engaged in **growing & manufacturing of Tea, Coffee or Rubber** & Deduction is allowed equal to the amount deposit in an account open with NABARD. However maximum deduction allowed shall be 40% of profits before debiting any amount under Section 33AB.

- **For Example:** ABC Ltd. is engaged in growing & manufacturing of tea & profits of the company are Rs. 100 Lac, & the company has deposit Rs. 30 Lac in Tea Development Account, in this case deduction allowed shall be Rs. 30 Lac. If in the above case amount deposited is Rs. 45 Lac, deduction allowed shall be Rs. 40 Lac.

Amount shall be **deposited within 6 months** from the end of the previous year or **before the due date of furnishing of return of income whichever is earlier.**

Deduction is allowed subject to the condition that the accounts of the assessee have been audited by a Chartered Accountant.

The amount so deposited should be utilized subsequently as per the scheme of Tea Board/Coffee Board/Rubber Board of India.

However, **amount cannot be utilized** for any of the purposes given below:

- Expenditure on plant & machinery to be installed in any office premises or residential accommodation or guest house.
- Any Office appliances.(Except Computers)
- Expenditure on any machinery or plant the cost of which has been debited to P&L Account either as depreciation or otherwise.
- Any new machinery or plant to be installed in an industrial undertaking for the purpose of business of construction, manufacture or production of any article or thing specified in the list in the Eleventh Schedule.

If the assessee has already taken deduction and subsequently the amount was utilized for any of the above mentioned purposes, in that case the amount so utilized shall be considered to be the income of the previous year in which the amount has been utilized.

The amount deposited in the special account is allowed to be withdrawn in the circumstances mentioned below:

- Closure of Business
- Dissolution of Business.
- Death of an assessee.
- Partition of HUF
- Liquidation of a Company

If the amount has been withdrawn on the closure of the business or on the dissolution of the firm, it will be considered to be income of the year in which the amount has been withdrawn but in other cases mentioned above, it will not be considered to be income.

SITE RESTORATION FUND

SECTION 33ABA

Deduction is allowed to all the assesses engaged in prospecting income, extraction or production of mineral oils. Deduction is allowed to the extent amount has been deposited with State Bank. However, maximum deduction allowed shall be 20% of the profits before debiting any amount under Section 33ABA. The amount so deposited should be utilized for restoration of the site which is being abandoned.

EXPENDITURE IN CONNECTION WITH SCIENTIFIC RESEARCH

SECTION 35

If any assessee has incurred expenditure in connection with scientific research, such expenditure is allow to be debited to the P&L A/c provided the research is related to the Business / Profession of the assessee and further even capital expenditure can be debited to P&L Account but expenditure on land is not allowed.

If any assessee has given any donation or contribution to any approved scientific research, university, college, Indian Company etc, deduction is allowed equal to 1.25 times of the donation or contribution & further there is no condition that the research should be related to the Business / Profession of the assessee.

Capital expenditure in connection with scientific research is allowed to be debited only to the extent income is available under the head Business / Profession & unadjusted expenditure shall be allowed to be set off & carry forward just like unabsorbed depreciation.

If any assessee has incurred any expenditure before commencement of business in connection with scientific research, but within 3 years before the commencement, such expenditure shall be allowed in the year in which the business has commenced. However, revenue expenditure shall be allowed only to the extent it has been permitted by the prescribed authority.

If any perquisite has been allowed to the employees before commencement of business, it will not be allowed.

IF THE COMPANY IS ENGAGED IN **BIO-TECHNOLOGY, MANUFACTURING OF DRUGS, PHARMACEUTICALS, CHEMICALS, COMPUTER, ELECTRONIC EQUIPMENT, TELECOMMUNICATION EQUIPMENT, OR ANY OTHER PRODUCT NOTIFIED BY THE PRESCRIBED AUTHORITY** IN SUCH CASES DEDUCTION IS ALLOWED EQUAL TO 1.5 TIMES OF THE EXPENDITURE INCURRED, HOWEVER IN CASE OF BUILDING EXPENDITURE SHALL BE ALLOWED EQUAL TO THE AMOUNT INCURRED & EXPENDITURE INCURRED ON LAND SHALL NOT BE ALLOWED. IF EXPENSES HAVE BEEN INCURRED BEFORE COMMENCEMENT OF BUSINESS, EXPENDITURE SHALL BE ALLOWED EQUAL TO THE EXPENDITURE INCURRED.

Section 41(3)

If any assessee has incurred capital expenditure in connection with scientific research & subsequently the asset was sold by the assessee, in this case amount recovered shall be considered to be the income under the head Business / Profession as per Section 41(3) but only to the extent amount has been debited to the P&L Account & any excess over it shall be taxable under the head Capital Gains.

If any assessee has incurred capital expenditure in connection with scientific research & the amount was debited to the P&L Account but subsequently the amount was transferred to the normal business, in this case it will be entered in the respective block of assets & its WDV shall be taken to be NIL & if such asset has been sold subsequently, in that case sale price shall be deducted from the WDV of the block.

LICENSE FOR TELECOMMUNICATION **SECTION 35ABB**

If any assessee has incurred expenditure for purchase of license for telecommunication, in such cases expenditure shall be allowed in installments, starting with the year in which the payment has been made & ending with the year in which the license has expired.

- **For Example:** Airtel Ltd. has taken license for cellular services on 1/10/2007 & has paid Rs. 25 Lac being the license fee & the license will expire on 31/03/2012, in this case expenditure shall be allowed in the manner given below:

<u>P.Y.</u>	<u>07-08</u>	<u>08-09</u>	<u>09-10</u>	<u>10-11</u>	<u>11-12</u>
<u>Proportion</u>	25/5	25/5	25/5	25/5	25/5

Presume in the above case license is obtained on 01/10/2007 but payment was made on 01/05/2008, in that case:

<u>P.Y.</u>	<u>07-08</u>	<u>08-09</u>	<u>09-10</u>	<u>10-11</u>	<u>11-12</u>
<u>Proportion</u>		25/4	25/4	25/4	25/4

If any assessee has made the payment before commencement of business, in such cases installments shall be allowed from the year in which the business has commenced.

If the payment has been made in installments deduction shall be allowed from the year in which the installment has been paid.

- **For Example:** Airtel Ltd. has taken license for cellular services on P.Y. 07-08 & has paid Rs. 10 Lac in 07-08 & again Rs. 10 Lac in 08-09 & Rs. 5 Lac in 09-10 & the license will expire on 11-12, in this case expenditure shall be allowed in the manner given below:

<u>P.Y.</u>	<u>07-08</u>	<u>08-09</u>	<u>09-10</u>	<u>10-11</u>	<u>11-12</u>
<u>Proportion</u>	10/5	10/5	10/5	10/5	10/5
		10/4	10/4	10/4	10/4
			5/3	5/3	5/3

If any assessee has sold the license subsequently, any loss shall be debited to the P&L Account & if there is any income, it will be taxable under the head Business / Profession but only to the extent amount was debited to the P&L Account & any excess over it shall be taxable under the head Capital Gains.

DONATION / CONTRIBUTION FOR ELIGIBLE PROJECT **SECTION 35AC**

Deduction is allowed to all assessee in case of donation or contribution to the notified institutions which are carrying on eligible project.

“Eligible Project” shall include the projects of social or economic importance. For Example: Drinking Water Project, Contribution of Houses for the Poor Persons etc.

A company assessee has the option to incur the expenditure directly also.

DONATION / CONTRIBUTION FOR RURAL DEVELOPMENT
SECTION 35CCA

Deduction is allowed to all assessee in case of donation or contribution to the notified institutions for the purpose of Rural Development. If there is any contribution to national fund for rural development, such contribution is also allowed. Similarly, contribution to national urban poverty eradication fund shall be allowed.

AMORTIZATION OF CERTAIN PRELIMINARY EXPENSES
SECTION 35D

Expenses incurred before commencement of business shall be allowed to be debited in 5 annual equal installments starting the year in which the business has been commenced & further expenditure is allowed only to the resident assesses and to Indian Companies.

The expenses which are allowed under Section 35D are as given below:

1. Expenditure in connection with project report, feasibility report, engineering services, conducting market survey provided the work has been taken up by the assessee himself or by any organization approved by the board.
2. Expenses incurred in connection with legal agreements relating to the business or profession.
3. Expenses being incorporation fee of the company.
4. Expenses on drafting & printing of memorandum & articles of association.
5. Expenses on issue of share capital & debentures including expenses on drafting and printing of prospectus and also expenses being commission paid to the underwriters.
6. Any other expense prescribed for this purpose.

Expenses incurred before commencement of business is allowed, but maximum to the extent of 5% of the project cost. However, an Indian Company has the option to take 5% of capital employed.

“PROJECT COST” = Total of actual cost of all the fixed assets as on the last day of the year in which the business was commenced.

“CAPITAL EMPLOYED” = Total of issued share capital, debentures and long term borrowings as on the last day of the year in which the business was commenced.

If there is expansion or extension of an existing business, in that case also expenditure shall be allowed in the similar manner.

If there is amalgamation or De merger, in that case remaining installments shall be allowed to the amalgamated company or the resulting company.

EXPENDITURE IN CONNECTION WITH AMALGAMATION / DE MERGER
SECTION 35DD

Expenditure is allowed only to Indian Company and allowed for the expenditure incurred in connection with amalgamation / de merger & expenditure is allowed in 5 annual equal installments.

EXPENDITURE IN CONNECTION WITH VOLUNTARY RETIREMENT
SECTION 35DDA

Deduction shall be allowed to all the assesses with regard to the expenditure incurred in connection with Voluntary Retirement & expenditure shall be allowed in 5 annual equal installments.

[In case of amalgamation / de merger, remaining installments shall be allowed to the amalgamating or the resulting company]

PREMIUM FOR INSURANCE OF STOCKS
SECTION 36(1)(i)

If any assessee has paid premium for the insurance of Raw Material, Finished Goods etc, premium paid is allowed.

PREMIUM FOR INSURANCE OF CATTLE
SECTION 36(1)(ia)

If any Cooperative Society has paid premium for insurance of cattle owned by the members of society, such premium shall be allowed to be debited.

PREMIUM FOR MEDICLAIM POLICY
SECTION 36(1)(ib)

If any assessee has paid premium in connection with Mediciclaim Policy taken in the name of employees, premium shall be allowed to be debited. However payment should be made in cash.

PAYMENT OF BONUS / COMMISSION TO EMPLOYEES

SECTION 36(1)(ii)

Bonus / Commission to the employees is allowed but subject to the provision of Section 43B. Such Bonus / Commission should not have been payable to the employees otherwise as share out of profits.

INTEREST ON LOAN TAKEN FOR BUSINESS / PROFESSION

SECTION 36(1)(iii)

If any assessee has taken a loan for the **purpose of Business / Profession**, in such case interest is **allowed without any restriction**.
[No interest is allowed to the proprietor on his capital]

If the loan has been taken for the purpose of capital asset, interest up to the date of putting the asset to use shall be capitalized & depreciation shall be allowed on capitalized amount & interest for the subsequent period shall be debited to the P&L Account as per Section 43(1).

DISCOUNT ON ZERO COUPON BOND

SECTION 36(1)(iiia)

Discount on Zero Coupon Bond shall be allowed on pro-rata basis taking into consideration life of such bond in months.

“ZERO COUPON BONDS” means such bonds for which no return is allowed till the maturity of such bond.

“DISCOUNT” means difference between the amount received and the amount paid.

- **For Example:** ABC Ltd. has issued Zero Coupon Bond of Rs. 20 Lac and the maturity shall be after 15 years & amount payable on maturity is Rs. 50 Lac, in this case amount of Discount shall be Rs. 2 Lac (**30 Lac / 15 yrs**) and the company shall be allowed Rs. 20 Lac every year under Section 36(1)(iiia).

In the hands of the holder of such bond, additional amount received shall not be considered to be interest income rather there will be capital gains of Rs. 30 Lac.

EMPLOYER'S CONTRIBUTION TO PF / GRATUITY FUND ETC.

SECTION 36(1)(iv)/(v)

Employer's Contribution to RPF, approved Gratuity fund or other similar funds is allowed but subject to the provision of Section 43B.

EMPLOYEE'S CONTRIBUTION TO PF ETC.

SECTION 36(1)(va)

Employee's contribution received by the employer shall be considered to be the income of the employer. However, subsequently the employer shall be allowed to debit the amount to the P&L Account provided the amount has been credited to the PF account latest by the due date.

EXPENDITURE ON PURCHASE OF ANIMALS

SECTION 36(1)(vi)

If any assessee has incurred any expenditure on purchase of animals for the purpose of Business / Profession, the expenditure shall be allowed to be debited at the time of death of animal or when the animal has been discarded.

If the animals are Stock-in-trade, the amount shall be allowed to be debited.

BAD DEBTS / PROVISION FOR BAD DEBTS

SECTION – 36(1)(vii), 36(1)(viia) and 41(4)

If any assessee has incurred any bad debt in **connection with Business / Profession**, such bad debt shall be **allowed to be debited**. If the bad debts debited by an assessee are recovered subsequently, in this case any deficiency shall be allowed as bad debt and any excess shall be considered to be Income under the head Business / Profession under **Section 41(4)**. However, if the bad debt were not allowed, in that case recovery shall not be considered to be income under the head Business / Profession.

- **For Example:** Mr. X has sold goods on credit amounting to Rs. 3,00,000 and has debited Rs. 50,000 as bad debts and subsequently but in final settlement he has received Rs. 2,10,000, in this case

deficiency of Rs. 40,000 shall be allowed as bad debt and if amount received is Rs. 2,60,000, excess of Rs. 10,000 shall be considered to be the income under Section 41(4)

Provision for bad debt is not allowed (provision or reserve even for any other purpose is not allowed), but as a special case provision is allowed as per **Section 36(1)(viiia)** in the cases given below:

- a. In case of **Indian Banks**, provision is allowed maximum up to 7.5% of G.T.I + 10% of average monthly advances of the rural branches of the bank.

- **For Example:** PNB bank has GTI of Rs. 1000 Lac and monthly advances of the rural branches of the bank is Rs. 3000 Lac, in this case maximum provision allowed shall be,

7.5% of 1000 Lac

75 Lac

10% of 3000 Lac

300 Lac

375 Lac

- b. In case of **Foreign Banks, Indian Financial Institutions, State Financial Corporation, State Industrial Investment Corporation** provision shall be allowed maximum up to 5% of G.T.I.

If any assessee was allowed provision for bad debt under Section 36(1)(viiia), bad debt shall be first debited to the provision for bad debts and only after that balance amount shall be allowed to the P&L Account.

- **For Example:** If a particular Bank has provision for Bad debts Rs. 20 Lac and actual Bad debts are Rs. 21 Lac, in this case only Rs. 1 Lac can be debited to P&L Account as Bad debt.

EXPENDITURE ON PROMOTION OF FAMILY PLANNING NORMS

SECTION 36(1)(ix)

Expenditure is **allowed only to the company assessee** who is promoting family planning among its employees & further revenue expenditure is allowed to be debited in the same year.

Capital expenditure is allowed in 5 annual installments. Expenditure is **allowed to be debited only to the extent income is available under the Business / Profession** & unadjusted expenditure shall be allowed to be set-off and carried forward just like unabsorbed depreciation.

If any capital asset has been purchased for the purpose of promotion of family planning norms among the employees and subsequently the asset was sold, the **sale proceeds shall be considered to be the income under the head Business / Profession** as per Section 41(3) but maximum to the extent of the amount debited to the P&L Account. If the business is not in existence at that time, even then it will be considered to be income under the head Business / Profession.

If subsequently there is **amalgamation or de merger**, the above provisions shall apply in case of resulting company as they would have applied to the amalgamating company or the parent company.

BANKING CASH TRANSACTION TAX (BCTT)

SECTION 36(1)(xiii)

If any assessee has paid BCTT, it will be allowed to be debited to the P&L Account. BCTT is not payable in case of withdrawal from savings bank A/c.

If the amount has been withdrawn from any other account, BCTT is payable @ 0.1% of the amount withdrawn & further in case of individual & HUF, amount withdrawn should exceed Rs. 50,000 on a single day and in case of any other person, it should exceed Rs. 10 Lac.

Similarly, if any person has received payment on the maturity of a term deposit, BCTT shall be payable.

[BCTT HAS BEEN ABOLISHED W.E.F. A.Y. 2010-11]

COMMODITIES TRANSACTION TAX

SECTION 36(1)(xv)

If any assessee has paid CTT in connection with Sale/Purchase of various commodities, it will be allowed to be debited to the P&L Account.

GENERAL EXPENDITURE

SECTION 37(1)

If any expenditure is neither allowed nor disallowed specifically, such expenditure is allowed under Section 37(1), provided it is revenue in nature & is related to the Business / Profession of the assessee.

The expenses which may be allowed under Section 37(1) are as given below:-

1. Expenditure being payment of salary to employees.
2. Expenditure in connection with advertisement (like diaries, calendars etc.) but if the assessee has incurred capital expenditure, depreciation shall be allowed

- **For Example:** ABC Ltd has incurred Rs. 20,000 on Sign Board, in this case depreciation shall be allowed.
3. Expenditure incurred in connection with traveling relating to Business / Profession of the assessee including expenditure incurred on stay in hotels etc.
 4. Expenditure incurred in connection with opening economy
 5. Expenditure incurred on the occasion of Diwali provided the expense is not personal nature or religious nature i.e. it should be in the nature of Business / Profession.
 6. Security Deposit under Own Your Telephone Scheme (OYT) or Tatkal Telephone Scheme or Telex Connection shall be allowed to be debited.
 7. Expenditure being loss due to embezzlement of funds by the employees.
 8. Expenditure due to theft.
 9. Expenditure in connection with legal proceedings.
 10. Any other expenditure relating to the Business / Profession & is revenue in nature.
- If the assessee has incurred any illegal expense, it will not be allowed. ANY FINE OR PENALTY IS NOT ALLOWED.

ADVERTISEMENT IN NEWSPAPER ETC. OF A POLITICAL PARTY

SECTION 37(2B)

If any assessee has incurred any expenditure in connection with advertisement in newspaper of a political party is disallowed.

ASSETS IN MIX USE

SECTION 38

If any assessee has any asset in the use of Business / Profession & also in personal use, in such cases, expenses shall be allowed only to the extent the asset is in the use of Business / Profession.

PAYMENT OF INCOME TAX OR WEALTH TAX ETC.

SECTION 40(a)

If any assessee has paid Income tax, Wealth Tax, FBT, Additional Income tax(CDT), it will not be allowed to be debited to the P&L Account, but if any person has paid Sales Tax, Excise Duty, Custom Duty, Service Tax etc. it will be allowed to be debited to the P&L Account but subject to the provisions of Section 43B

If any person has taken any loan for payment of Income Tax etc, interest is not allowed but if loan has been take for the payment of sales tax etc, interest is allowed.

If any person has paid interest for late payment of Income Tax etc, interest is not allowed but if any person has paid interest for late payment of sales tax etc., interest is allowed.

If there is any income tax refund or wealth tax refund etc., it will not be considered to be income of the assessee. If there is sales tax refund et., it will be considered to be income under head Business / Profession.

If there is interest on refund of income tax etc., it will be income under the head Other Sources, but if the interest is on the refund of sales tax etc., it is income under the head Business / Profession.

If any assessee has incurred expenditure in connection with filing of return of income the expense is allowed. Similarly, if salary has been paid to an employee who is looking after income tax matters, salary is allowed. Similarly if there is any expenditure in connection with audit, it is allowed.

Payment of Income Tax by the employer on behalf of employee in connection with Non-monetary perquisite

If the employer has paid Income Tax on behalf of the employee in connection with Non-monetary perquisite, such Income tax shall not be considered to be Income of the employee under Section 10(10CC) and the employer shall not be allowed to debit the amount to the P&L Account.

If the employer has paid Income Tax on behalf of the employee in general(i.e. not for Non-monetary perquisite), such Income tax is shall be considered to be the income in the hands of the employee under Section 17(2)(iv) & employer shall be allowed to debit the amount to the P&L Account as salary to the employees under Section 37(1).

PAYMENTS OUTSIDE INDIA WITHOUT DEDUCTING TAX AT SOURCE

SECTION 40(a)(i)

If any assessee has made payment of interest, technical fees etc. outside India or to any NR or any foreign company in India without deducting tax at source, in such cases expenditure is disallowed.

If the assessee has deducted the tax at source & payment was made till the last day of the relevant previous year or it was paid in the subsequent year but within the time allowed under Section 200, in such cases expenditure shall be allowed otherwise expenditure shall be allowed in the year in which the payment has been made.

- **For Example:** ABC Ltd has paid interest outside India on 10/01/2008 after deducting tax at source but payment was made by the company to the Government on 07/04/2008, in this case, interest is allowed but if the tax was paid to the Government on 08/04/2008, expenditure shall be allowed in the Previous Year 08-09. Similarly, if in the above case payment was made and tax has been deducted on 31/03/2008 & tax was paid to the Government on 31/05/2008, interest is allowed in Previous Year 07-08.

PAYMENTS IN INDIA TO ANY RESIDENT WITHOUT DEDUCTING TAX AT SOURCE

SECTION 40(a)(ia)

FOR A.Y. 08-09: Similar provisions as per Section 40(a)(i)

FOR A.Y. 09-10: If any assessee has made payment in India to any resident person and tax has been deducted at source up to the end of February of the relevant Previous year, in such cases amount of TDS shall be paid to the Government up to 31 march of such P.Y.. If the TDS is deducted during month of march, tax should be deposited up to the last date of filing of return of income.

PAYMENT OF SALARY OUTSIDE INDIA WITHOUT TDS

SECTION 40(a)(iii)

If any assessee has paid salary outside India or salary has been paid in India to any NR and the assessee has neither deducted tax at source nor the tax has been paid to government, in such cases salary is disallowed. But if either the TDS has been deducted or TDS has been paid to the Government, in such cases salary is allowed to be debited.

PAYMENT OF SALARY AND INTEREST TO THE PARTNER.

SECTION 40(b)

Salary and Interest to the partner is allowed but only to the extent given below:-

1. Interest is allowed but maximum @ 12% p.a. simple interest.
2. Salary, Bonus, Commission etc. is allowed, but only to the working partners & maximum salary allowed shall be as given below:-
 - a. If the partnership firm has specified profession under section 44AA, maximum salary allowed shall be as given below:-

BOOK PROFITS

SALARY ALLOWED AS PERCENTAGE OF BOOK PROFITS

Up to 3 Lac
Balance amount

90% or Rs. 1,50,000 whichever is higher
60%

“Book Profits” means profit & gains of the Business / Profession but before debiting any salary to the partners. If the firm is paying salary less than from the salary calculated by above formula, in that case lesser salary shall be allowed.

- b. If any partner ship firm has business or non-specified profession, in that case maximum salary allowed shall be as given below:-

BOOK PROFITS

SALARY ALLOWED AS PERCENTAGE OF BOOK PROFITS

Up to 3,00,000
Balance amount

90% or Rs. 1,50,000 whichever is higher
60%

SALARY AND INTEREST IS ALLOWED ONLY IF IT IS PERMITTED AS PER THE PARTNERSHIP DEED.

PAYMENTS TO RELATIVES / RELATED PARTY

SECTION 40A(2)

If any person has made payment whether revenue or capital and such payment has been made to any relative / related person and it is unreasonable / excessive, in such cases it is disallowed to the extent the payment is unreasonable / excessive.

The term “**Relative**” shall include:

1. In case of individual, any relative of individual.
2. If the assessee is company, firm etc. it will include their directors, partners etc. & also their relatives.
3. If the assessee has made payment to any person who has substantial interest in the business of the assessee or the assessee has substantial interest in the business of such person.
4. If the payment is being made to any company or firm etc. holding 20% of equity shares, in that case it will include the directors or partners etc. also and also their relative and if the person having substantial interest is a director or partner etc. in some company or firm etc., it will include such company or firm etc. and their other directors ad partners etc. and also their relatives.

PAYMENT IN EXCESS OF RS. 20,000
SECTION 40A (3) RULE 6DD

If any assessee has incurred **Revenue Expenditure** (i.e. these provisions are not applicable in case of capital expenditure) & payment with regard to such expenditure has been made in a sum exceeding Rs. 20,000 & such payment was made otherwise than through account payee cheque or account payee bank overdraft, in such cases entire expenditure is disallowed & further amount shall be disallowed only if the **individual expenditure** as well as **individual payment** is exceeding Rs. 20,000.

[w.e.f. A.Y. 09-10, aggregate payments during a particular day to a particular person shall be taken into account.]

- **Examples:** 1. ABC Ltd. has incurred an expenditure of Rs. 15000 on 01/10/07 & payment is given in cash to Mr. X & on the same day the company has incurred one more expenditure of Rs. 18000 & payment was given to Mr. X in cash, in this case, entire expenditure is allowed. *[For A.Y. 09-10 disallowed]*
- 2. One assessee has incurred Rs. 35000 & payments were made in two installments of Rs. 17500 each & the payment was made in cash & the payments were made on the same day, amount disallowed in A.Y. 08-09 shall be NIL *[Amount disallowed in A.Y. 09-10 shall be Rs. 35000.]*
- 3. ABC Ltd. has incurred an expenditure of Rs. 40000 out of which 27000 paid in cash & Rs. 13000 by account payee cheque, in this case amount disallowed shall be Rs. 27000 in A.Y. 08-09. *[Same in A.Y. 09-10]*
- 4. Mr. X has incurred one expenditure of Rs. 150000 & payment was given in cash in 10 installments of Rs. 15000 each & payment were made in a single day, in this case expenditure disallowed in A.Y. 08-09 shall be NIL *[Amount disallowed in A.Y. 09-10 shall be Rs. 150000]*
- 5. ABC Ltd. has purchased one plant for Rs. 100000 and the payment was made in cash, in this case **nothing is disallowed** because Section 40A(3) is not applicable in case of **Capital Expenditure**.

If any assessee has claimed expenditure on due basis & after filing the return of income the payment was made in cash, in such cases, it will be considered to be income of the assessee of the year in which the payment is given in cash.

- **For Example:** ABC Ltd. has incurred one expenditure of Rs. 30,000 on 01/10/07 & the company has claimed the expenditure on due basis, but subsequently payment was made in cash by the company on 01/01/09, in this case it will be considered to be income of the assessee for A.Y. 09-10

The above provisions are also applicable in case of Stock-in-trade.

As per **Rule 6DD** payment in cash or by bearer cheque or by crossed cheque shall be allowed in following cases:

- If the payment is being made to the **Government's financing Institutions (like LIC, UTI etc.) or the Government Banks** etc.
- If the payment is being made for purchasing
 - i) **Agricultural produce or forest produces.**
 - ii) **Products of dairy farming, poultry farming, fisheries etc.** & further the payment should be made to the **producer or cultivator.**
 - iii) **Products of cottage industries** & goods have been produce without the aid of power.
 - iv) **Products of Horticulture or Apiculture.**
- If the payment is being made in a **village / town & there is no bank in that village or town on the date of making the payment** & further payment is being made to a **person who has Business / Profession** at that place or the **person ordinarily resides** at that place.
- If the payment is being made on a day when the **banks are closed due to strike or otherwise.**
- If the payment is being made to **Central / State Government**, which as per rules has to be in legal tender.
- Payments of **terminal benefits like gratuity, retrenchment compensation etc. to low paid employees (Drawing less than Rs. 7,500 annually)** or the families.
- Where the payment is **made by any person to his agent who is required to make payment in cash for goods and services on behalf of such person.**
- Where the payment is made **by an assessee by way of salary to his employee after deducting the Income-Tax** from salary in accordance with the provisions of Section 192 of the Act, and when such employee –
 - i) Is temporarily posted for a continuous period of fifteen days or more in a place other than his normal place of duty or on a ship
 - ii) Does not maintain any account in any bank at such place or ship.

PROVISION FOR GRATUITY
SECTION 40A(7)

In general provision or reserve is not allowed . However, provision for Gratuity is allowed provided the amount has become due for payment.

- **For Example:** Mr. X is retired from ABC Ltd on 28/03/2008 and gratuity of Rs. 3 Lac has become due for payment. The employee has not completed formalities till 31/03/2008 and the company has created a provision for Gratuity, such provision is allowed.

CONTRIBUTION TO VARIOUS FUNDS

SECTION 40A(9)

Employer's Contribution to RPF, SPF, Approved Superannuation Fund, Approved Gratuity fund or any other fund required under any other Act shall be allowed.

Employer's Contribution to URPF, Unapproved Superannuation Fund, Unapproved Gratuity fund etc. shall not be allowed.

For Example: Employer's Contribution to Staff welfare Fund or other similar fund is not allowed.

DEEMED INCOME

SECTION 41(1)

If any assessee has debited any expenditure and subsequently such expenditure was recovered by him, amount so recovered shall be considered to be his income under the head Business / Profession under Section 41(1)

BALANCING CHARGE

SECTION 41(2)

In case of power generating unit if any asset has been sold or destroyed etc. and depreciation was claimed on SLM basis, any amount received on sale etc. shall be considered to be income under the head Business / Profession and shall be called Balancing Charge but only to the extent depreciation was debited to the P&L Account & any excess over it shall be taxable under the head Capital Gains.

SALE OF CAPITAL ASSET – SCIENTIFIC RESEARCH

SECTION 41(3)

If any assessee has incurred capital expenditure in connection with scientific research & subsequently the asset was sold by the assessee, in this case amount recovered shall be considered to be the income under the head Business / Profession as per Section 41(3) but only to the extent amount has been debited to the P&L Account & any excess over it shall be taxable under the head Capital Gains.

RECOVERY OF BAD DEBTS

SECTION 41(4)

If any amount was allowed as bad debt and subsequently it was recovered in the subsequent years, in such cases the amount so recovered shall be considered to be income under the head Business / Profession of the year in which the amount has been recovered.

[In general a person may have income under the head Business / Profession only if such person has Business / Profession but if the assessee has income under Section 41(1), 41(2), 41(3) or 41(4), such income is taxable under the head Business / Profession even if the assessee has closed down his Business / Profession.]

LOSSES OF DISCONTINUED BUSINESS / PROFESSION

SECTION 41(5)

If any assessee has closed down his Business / Profession and there is losses relating to such Business / Profession, the losses shall be allowed to be carried forward even after expiry of the period of 8 years but such losses can be set off only from income under Section 41(1), 41(3) and 41(4).

(The above provisions shall not be applicable in case of Speculation Business)

CERTAIN EXPENDITURE ALLOWED ONLY ON ACTUAL PAYMENT BASIS

SECTION 43B

Write a short note on method of accounting as per Section 145

As per **Section 145** every assessee has the option to maintain the books of accounts either on the basis of mercantile system of accounting or on the cash basis.

If the books are maintained on the basis of mercantile basis of accounting, all the expenses are allowed on due basis and all incomes are taxable on accrual basis. If the books are maintained on cash basis, all expenditures are allowed on actual payment basis & all incomes are taxable on actual receipt basis.

Any system of accounting once adopted has to be followed consistently & it can be changed with the permission of assessing officer. If any assessee has violated the provisions of **Section 145**, in such cases assessing officer may complete assessment in the manner given under **Section 144**.

Section 43B

If any assessee is maintaining books of accounts on the basis of mercantile system of accounting, all expenditures are allowed on due basis, however expenses listed below shall be allowed only on actual payment basis: -

- b) Sales tax, Custom Duty, Excise Duty, Service Tax, Municipal tax or License Fee Etc.
- c) Employer's Contribution to RPF, approved superannuation fund, statutory provident fund, approved gratuity fund or any other approved fund for employee's welfare.
- d) Bonus or Commission to the employees.
- e) Leave salary to the employees.
- f) Interest on loan taken from Public Financial Institutions, State Financial Corporations, State Industrial Investment Corporation.
- g) Interest on loan or advance from Banks.

The expenses listed above shall be allowed only on actual payment basis. However payment can be made till the last date of filing of return of income, otherwise expenditure shall be allowed in the year in which the payment has been made.

- **For Example:** ABC Ltd. has incurred excise duty of Rs. 25 Lac during the P.Y. 07-08 & entire amount was debited to the P&L account & Net Profit is Rs. 11 Lac. The company has paid excise duty of Rs. 12 Lac on 29/09/2008 & balance on 10/05/2009. Determine the amount allowed to be debited in different years.

<u>Solution:</u>	<u>P.Y. 07-08</u>	<u>P.Y. 08-09</u>	<u>P.Y. 09-10</u>
Excise Duty Allowed	12 Lac	Nil	13 Lac
Excise Duty Disallowed	13 Lac	Nil	Nil

Expenditure listed under **Section 43B** shall be allowed only if the assessee has made the actual payment, further proof of having made the payment should be enclosed.

If any assessee has not paid interest on a particular loan and such interest has been converted into fresh loan, in such cases, it will not be considered to be payment of interest & deduction shall not allowed, but whenever, such converted loan has been repaid, deduction shall be allowed in that year.

[Some of the state government have a scheme to permit the assessee to retain the amount of sales tax etc. for some period, in such cases, deduction shall be allowed on due basis.]

ACTUAL COST **SECTION 43(1)**

In case of depreciable assets, depreciation shall be allowed on the actual cost which means total of expenditure incurred up to the date of putting the asset to use.

If the assessee has incurred expenditure in connection with transportation of the capital asset, expenditure on loading and unloading, transit insurance, payments given to the experts for installation of such asset, interest on loan taken for purchase of such asset (but only for the period between purchase of asset and put to use of such asset) etc., it shall be capitalized.

If the assessee has received any subsidy from the Government or similar agency, it will be deducted while computing actual cost.

- **For Example:** ABC Ltd has purchased a P&M and the Government has given subsidy of Rs. 10 Lac because it is a non polluting P&M, in that case, actual cost of the P&M shall be reduced by Rs. 10 Lac.

If any assessee has any building in his personal use and subsequently the building was transferred to the Business / Profession of the assessee, in such cases building shall be considered to be in Business / Profession of the assessee from the date of its purchase and depreciation shall be computed accordingly, but depreciation shall be allowed only for the current year.

- **For Example:** Mr. X purchased one building on 01/11/2005 for Rs. 10 Lac and subsequently the building was transferred to the business of the assessee on 01/12/2007, in this case WDV and depreciation shall be computed in the manner given below:

Actual Cost	10 Lac
Depreciation for P.Y. 05-06	(50000)
@ 5%(< 180 days)	
Depreciation for P.Y. 06-07	(95000)
@ 10% of (10 Lac – 50000)	
Depreciation for P.Y. 07-08	(85500)
@ 10%(950000-95000)	
	7,69,500

The above provision is applicable only in case of building (i.e. in case of other capital assets, the actual cost of the assessee shall be taken into consideration)

- **For Example:** Mr. X purchased one motor car on 01/11/2005 for Rs. 10 Lac and subsequently the building was transferred to the business of the assessee on 01/12/2007, in this case WDV and depreciation shall be computed in the manner given below:

Actual Cost	10 Lac
Depreciation for P.Y. 07-08	(150000)
@ 15%	<u>8,50,000</u>

[15% because asset purchased in one year and put to use in subsequent year]

If any assessee has purchased any capital asset for the purpose of Business / Profession and has paid excise duty or sales tax etc. but he has taken VAT credit for such excise duty or sales tax etc., in such cases while computing actual cost, such sales tax or excise duty etc. shall be deducted.

If any manufacturer has purchased capital goods and has paid sales tax or excise duty etc., in such cases VAT credit shall be allowed on such capital goods because otherwise cost of the capital goods and also the amount of sales tax etc. shall be distributed in the cost price of the product manufactured by the manufacturer and accordingly there will be two anomalies i.e. taxing the same product twice, thrice and cascading effect hence VAT credit is allowed.

If VAT credit has been allowed for capital goods, it will be deducted while computing actual cost.

BOOKS OF ACCOUNTS

SECTION 44AA RULE 6F

In case of Specified Profession

Any person having specified profession has to maintain any books of accounts which may help the assessing officer in computing his income but if the gross receipt has exceeded Rs. 1,50,000 during all the 3 years immediately preceding the relevant P.Y., in such cases assessee should maintain prescribed books of accounts.

“Prescribed Books of Accounts” shall include Cash Book, Journal, Ledger, Bills Received, Copies of Bills issued etc.

If any person is required to maintain prescribed books of accounts, such person must retain such books of accounts for a period of at least 6 years from the end of the relevant A.Y.

“Specified profession” shall include:

1. Medical Profession
2. Architectural Profession
3. Legal Profession
4. Profession of Accountancy
5. Interior Decoration
6. Technical Consultancy
7. Authorized representative
8. Film artist.

If any person has started specified profession during the year, he must maintain prescribed books of accounts if the gross receipts are likely to exceed Rs. 1,50,000

In case of Business or Non-Specified Profession

If any assessee has Business or Non-Specified Profession, in such cases no books of accounts are required. However, if the gross receipt is exceeding Rs. 10 Lac or the income is exceeding Rs. 1,20,000 in any of the 3 years immediately preceding the relevant P.Y., in such cases the assessee should maintain any books of accounts which may help the assessing officer in computing his income. *(Prescribed Books are required only if the Books are required to be Audited)*

If the Business or the Non-Specified Profession has been setup during the year, in that case assessee should maintain any books of accounts if the Gross Receipt is likely to exceed Rs. 10 Lac or the income is likely to exceed Rs. 1,20,000.

If income of any person is to be computed on presumptive basis under Section 44AD, 44AE and 44AF and such person has rejected presumptive income, in that case, such person should maintain any books of accounts which may help the assessing officer in computing his income.

If any assessee has violated the provisions of Section 44AA, penalties may be imposed amounting to Rs. 10,000.

COMPULSORY AUDIT

OR

TAX AUDIT

SECTION 44AB

If any person is engaged in a business and his turnover during the year has exceeded Rs. 40 Lac, in such cases such person must get his accounts audited in that particular year.

If any person is engaged in specified or non-specified profession and his gross receipt during the year has exceeded Rs. 10 Lac, in such cases, such person must get his accounts audited in that particular year.

If income of any person is to be computed on presumptive basis under Section 44AD, 44AE and 44AF but such person has rejected the presumptive income, in such cases such person shall be required to get his accounts audited.

Any *Kachha Arahtia* shall be considered to be carrying Non-Specified profession and *Pucca Arahtia* shall be considered to be carrying on business.

If any person is required to get his accounts audited, such person must submit the audit report maximum up to the last date of filing of return of income.

If any assessee has violated the provision of Section 44AB, in that case penalties shall be imposed equal to 0.5% of the turnover but subject to a maximum of Rs. 1 Lac.

PRESUMPTIVE INCOME IN CASE OF PERSONS ENGAGED IN CIVIL CONSTRUCTION

SECTION 44AD

If any person is engaged in the business of civil construction or in the business of supply of labor for civil construction & his turnover during the year is not exceeding Rs. 40 Lac, in that case his income under the head Business / Profession shall be 8% of the Gross Receipt and no other expenditure shall be allowed under Section 28-44D and such person shall be exempt from maintaining the books of account.

If the assessee is a partnership firm, in that case salary and interest to the partners is allowed as per Section 40(b).

The assessee has the option to reject the presumptive income but in that case the assessee has to maintain books of accounts and also he should get the books of accounts audited. If the assessee has unadjusted losses, such loss shall be allowed to be set off, but if the assessee has unabsorbed depreciation, it will not be allowed to be set off. The assessee has the option to declare a higher income "Civil Construction" means construction of roads, Dams, bridges, sea port, airport etc.

Deduction under Section 80C-80U shall be allowed.

PRESUMPTIVE INCOME IN CASE OF PERSONS ENGAGED IN THE BUSINESS OF PLYING, HIRING OR LEASING GOODS CARRIAGES

SECTION 44AE

If any person is engaged in the business of plying, hiring or leasing goods carriages and such person do not have more than 10 goods carriages in his name at any time during the year, in such cases his income shall be presumed to be:

FOR HEAVY GOODS VEHICLES: Rs. 3500 p.m.

FOR LIGHT OR MEDIUM GOODS VEHICLES Rs. 3150 p.m.

And while computing Income under the head Business / Profession, no further expenditure shall be allowed under Section 28-44D

If the assessee is a partnership firm, in that case salary and interest to the partners is allowed as per Section 40(b).

The assessee has the option to reject the presumptive income but in that case the assessee has to maintain books of accounts and also he should get the books of accounts audited. If the assessee has unadjusted losses, such loss shall be allowed to be set off, but if the assessee has unabsorbed depreciation, it will not be allowed to be set off. The assessee has the option to declare a higher income

Deduction under Section 80C-80U shall be allowed.

PRESUMPTIVE INCOME IN CASE OF PERSONS ENGAGED IN RETAIL TRADE

SECTION 44AF

If any assessee in the business of retail trade and turnover is not exceeding Rs. 40 Lac, in such cases income shall be presumed to be 5% of the Gross Receipt.

While computing Income under the head Business / Profession, no further expenditure shall be allowed under Section 28-44D

If the assessee is a partnership firm, in that case salary and interest to the partners is allowed as per Section 40(b).

The assessee has the option to reject the presumptive income but in that case the assessee has to maintain books of accounts and also he should get the books of accounts audited. If the assessee has unadjusted losses, such loss shall be allowed to be set off, but if the assessee has unabsorbed depreciation, it will not be allowed to be set off. The assessee has the option to declare a higher income

Deduction under Section 80C-80U shall be allowed.

PRESUMPTIVE INCOME IN CASE OF NON-RESIDENTS ENGAGED IN SHIPPING BUSINESS

SECTION 44B

If any NR is engaged in shipping business, income shall be presumed to be 7.5% of the following amounts:-

1. Amount received in India in connection with loading of goods etc. outside India.
2. Income received / receivable in connection with loading of goods etc. in India.

PRESUMPTIVE INCOME IN CASE OF NON-RESIDENTS ENGAGED IN AIRCRAFT BUSINESS

SECTION 44BBA

If any NR is engaged in shipping business, income shall be presumed to be 5% of the following amounts:-

1. Amount received in India in connection with loading of goods etc. outside India.
2. Income received / receivable in connection with loading of goods etc. in India.

REBATE UNDER SECTION 88E

If any assessee is holding **equity shares or equity oriented mutual fund as Stock-in-trade & has paid STT**, in such cases rebate shall be allowed under Section 88E, which will be equal to the amount of STT or the amount of Income Tax computed at average rate whichever is less & further assessee shall not be allowed to debit the amount of STT to the P&L Account.

[w.e.f. A.Y. 09-10, rebate under Section 88E shall not be allowed and further STT shall be allowed to be debited as per Section 36(I)(xv)]

- **For Example:** Mr. X has income under the head Business / Profession Rs. 20 Lac after debited STT of Rs. 2 Lac. Income under the head Business / Profession includes income of Rs. 7 Lac from sale of Equity Shares on which STT has been paid & the shares were held as Stock-in-trade. Compute his Tax Liability for the A.Y. 08-09 and 09-10.

<u>A.Y. 08-09</u>	
Net Profit	20 Lac
+ STT	<u>2 Lac</u>
	<u>22 Lac</u>
Tax	609000
(-) Rebate u/s 88E	<u>193773</u>
	<u>415227</u>
+ Surcharge	41522.7
+ Edu. Cess	<u>13702.49</u>
	<u>470452.19</u>
Rounded Off	
U/s 288B	4,70,450

<u>A.Y. 09-10</u>	
Net Profit	20 Lac
Tax	5,72,170
(including surcharge and Edu. Cess)	

Calculation of Rebate u/s 88E
 $\frac{6,09,000}{22 \text{ Lac}} \times 7 \text{ Lac} = 193773$

OR

STT Paid = 2,00,000
Whichever Is less

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For PCC/IPCC

SUMMARY OF THE 7TH CHAPTER INCOME FROM BUSINESS & PROFESSION

- 1) **Section 145:** Profits and gains of Business or Profession shall be computed either on cash basis or mercantile basis of accounting.
- 2) Speculation Business income should to be computed separately as loss from such business cannot be set off against any other business income.
- 3) Revenue loss or expenditure incidental to business is excludable in the computation even though there is no specification provision. For example expenditure on stationery is deductible even though there is no specific section for this.
- 4) All the assets use for business can be classified as under:

Tangible: (a) Land – it is not eligible for depreciation.
(b) Building, machinery, plant and furniture are eligible for depreciation.

Intangible: Know-how, patents, copyrights, trademarks, licenses, franchises are eligible for depreciation.
- 5) Revenue expenses incurred in relation to the assets mentioned in point 4) should be considered for deduction u/s. 30, 31 and 37(1). Capital expenditure not qualifying under these provisions may be capitalized and depreciation u/s. 32 can be claimed if eligible.
- 6) Only in the case of undertakings engaged in the business of generation or generation and distribution of power, there is an option to avail depreciation on straight-line method. This option is for only those assets, which have been purchased after 31/3/98. In all other cases depreciation is deductible only on written down value method. The option has to be exercised in the beginning and shall apply to all the subsequent assessment years.
- 7) If depreciation has been charged as per SLM basis as mentioned in 6) above and then block of asset has been sold:
 - (a) For the value less than the value of block then we get terminal depreciation, which can be debited, to PL account.
 - (b) For the value more than the value of block then up to the amount of depreciation debited to the day is treated as PGBP income and balance if any is treated as STCG.
- 8) Interest on loan borrowed for acquiring on asset used in the business has to be treated as under:
 - a) Before the commencement of production/Business has to be capitalized.
 - b) Interest relating to the period after the asset is first put to use shall never form part of the cost of the asset. As per Sec. 43(1) it shall be allowed as revenue expenditure.
- 9) Unabsorbed depreciation is treated as part of current year depreciation and therefore, can be set off against income under other heads of income as well (except income of salary and casual incomes). It can be carried forward indefinitely even if the business is discontinued.
- 10) As per section 50 there shall be always STCG on sale of a depreciable asset.
- 11) In case of asset being destroyed and insurance company gives a similar asset to assessee then the value of such asset destroyed shall not be reduced from the block as per the SC case of **CIT vs Kasturi and Sons Ltd..**
- 12) The deduction of scientific research expenditure u/s. 35 shall be as follows:

	Particulars	Deduction permissible.
1	Expenditure incurred for own business: - U/s. 35(2AB) – special activities such as pharmaceuticals, bio-technology, computers etc. - U/s. 35 – Other cases	Weighted deduction of 150% Deduction of 100%
2	Contribution to Government's, approved university's, college or institution's laboratory	Weighted deduction of 125%

- 13) Generally, revenue expenditure is deductible in the year when expenditure has been incurred and capital expenditure is capitalized. The concept of deferred revenue expenditure is not prevalent in Indian income tax structure. However, such principle is made applicable under the following sections:

A) Section 35D – Amortization of preliminary expenditure – write it off over 5 years. Qualifying amount shall be follows:

 - a. For non-corporate assessee it cannot exceed 5% of cost of project
 - b. For a Company it cannot exceed 5% of cost of project OR 5% capital employed which ever is higher.

B) Section 35DD – Expenses incurred for amalgamation and demerger – write off over 5 years.

C) Section 35DDA – Voluntary Retirement Service compensation – write off over 5 years.

D) Section 37(1) – Discount/ premium on redeemable preference shares or bonds or debentures can be spread over the life of the instrument – **Madras Industrial Investment Corporation Ltd..**

14) The bad debts written off during preceding previous years and which are recovered during the previous year then recovery is fully taxable in the year of recovery provided it is recovered by the same assessee who has incurred such bad debt as was decided by **SC in the case of P.K.Kaimal**.

15) Expenditure on advertisement in souvenir, brochure, pamphlet etc. published by a political party is not allowed as deduction. However a deduction for the same or/and similar expenditure is allowed as deduction under section 80GGB and 80 GGC.

16) Expenses not deductible are as follows:

1. **Sec. 40(a)** – Any payment outside India on which no TDS has been done or has been paid.
2. **Sec. 40A(2)** – Excessive and unreasonable expenditure where a relative and substantial interest holding is involved.
3. **Sec. 40A(3)** – Expenditure paid in excess of Rs.20000 otherwise than by account payee cheque or bank draft subject to rule 6DD.
4. **Sec. 40A(7)** – Provision for gratuity.
5. **Sec. 40A(9)** – Contribution to unapproved funds.
6. **Sec. 43B** – Certain expenses not paid within the stipulated time limit. This applies irrespective of method of accounting.

17) Where the partnership deed stipulates terms of interest and salary to partners, the amount authorized by the deed or the limit prescribed by Sec. 40(b), whichever is lower, shall be allowed as deduction. This limit is as follows:

BOOK PROFITS OF PROFESSIONAL FIRMS	BOOK PROFITS OF OTHER FIRMS	REMUNERATION AS % OF BOOK PROFITS
On first Rs.300000 or in case of Loss	On first Rs.300000 or in case of Loss	Rs.150000 or 90% of book profits which ever is higher
On Balance	On Balance	60%

18) U/s. 44AA the assessee needs to maintain books of account in the following cases:

- a) Notified professions – Gross receipts exceed Rs. 1.5 lakhs.
- b) Other professions/business– Income exceeds Rs. 12 lakhs or turnover exceeds Rs. 10 lakhs.

19) U/s.44AB Audit is mandatory if

(a) Profession gross receipts exceed Rs. 10 lakhs.

(b) Presumptive cases covered by 44AD; 44AE & 44AF. 44BB and 44BBB, where the income is less than prescribed limit.

20) Presumptive business income provisions are as follows:

Provision	Sec. 44AD	Sec. 44AE	Sec. 44AF
Nature & Eligibility	Civil construction business having Turnover $\leq$ 40 lakhs.	Transport business-having no. of vehicles $\leq$ 10	Retail Traders having Turnover $\leq$ 40 lakhs.
Deemed Income	8% or more of turnover.	Heavy vehicle – Rs. 3,500 or more. Others Rs. 3,150 or more (p.m. or part of the month)	5% or more of Turnover.

Computation of income from Business (For the assessment Year 2010-11)

Profit (+) and loss (-) as per Profit and loss account		XX
ADD:- Expenses claimed (debited in the P.&L. A/C) but not allowed under the income tax Act. :-		
1) All provisions and reserves (reserve for bad debts / Depreciation / Income tax etc.) [except creation of reserve by financial corporations u/s 36]	X	
2) All taxes (i.e., Income tax, Advance income tax, Wealth tax etc.) [except Sales tax, Excise duty & local tax of premises used for business.]	X	
3) Rent paid to self	X	
4) All capital expenses except on scientific research	X	
5) All capital losses	X	
6) All charities and donations	X	
7) All expenses relating to other heads of income (e.g., Taxes on house property etc.)	X	
8) Cultivation expenses	X	
9) Any interest on capital unless the amount is borrowed	X	
10) All personal expenses (Drawing etc.)	X	
11) Any depreciation if wrongly debited	X	
12) Gifts and presents (Non-advertisement)	X	
13) Any type of fine or penalty	X	
14) Any payment to a partner (In case of firms only by way of salary, interest, bonus, commission or remuneration excess over prescribed limits)	X	
15) Any salary or interest payable outside India unless tax is deducted at source (TDS) or is paid according to the law	X	
16) Past losses (i.e., loss of the past years)	X	
17) Any other expenditure which is not incurred according to the provisions of law,	X	
18) Salary paid to self or any other member of family for casual help	X	
19) Personal life insurance premiums	X	
20) Any amount invested in savings such as NSS, NSC, PPF etc.	X	
21) Speculation loss	X	
22) Bad Debt still recoverable	X	
23) Legal expenses on criminal case; or a personal case of employee	X	
24) Legal expenses on acquiring an asset	X	
25) Legal expenses on curing title of asset	X	
26) Loss by theft from residence	X	
27) Expenses on illegal business	X	
28) Employer's contribution to unrecognized provident fund	X	
29) Difference in trial balance	X	
30) Difference due to under crediting of stock	X	
31) Cost of Patent rights being capital expenditure	X	
32) Cost of Technical know-how being capital expenditure	X	
33) Preliminary expenses being capital expenses.	X	
Total of these items is added in the profit or is adjusted out of the loss	X	XX
LESS: - Any expenditure which is allowable under the Act, but has not been debited to P. & L. A/c:		
1) Actual bad debts (not charged in P & L A/c)		
2) Depreciation (-do-)	X	
3) Any other expenditure incurred according to provision of law	X	
4) Difference due to under debiting of stock	X	
LESS: - Any income which is either exempt or not taxable under this head:	X	(XX)
a) Incomes exempted from tax:		
1) Post office saving bank interest		
2) Agricultural receipts	X	
3) Gifts from relatives	X	
4) Income-tax refund	X	
5) Bad debt recovered-disallowed earlier	X	
6) Life Insurance Maturity Amount	X	
7) Any capital receipt	X	
8) Withdrawal from PPF	X	(XX)
b) Incomes taxable under other heads: -		
1) Part-time salary	X	
2) Interest on Securities	X	
3) Rent from House property Let	X	
4) Capital gains	X	
5) Dividend, Bank Interest, winnings from Lotteries, race course etc.	X	(XX)
Add: Income from any other business (legal or illegal) to get income taxable under the head Profits & Gains of Business or Profession.		XX
Taxable income from business.		XX

Computation of Professional Income: -

The above-mentioned method is not suitable to compute professional income because professional persons usually do not prepare profit and loss account. They prepare Income and Expenditure Account of Receipts and Payment Account. To compute the professional income, it is easier to take professional receipts of them previous year and deduct out of these the professional expenses incurred during that year. The following illustration can help a person to compute the personal income of an assessee.

Computation of income from Profession

(For the assessment Year 2010-11)

I. In case of Doctor or Medical Practitioner

<u>Professional Receipts</u>		
1) Consolation fees	X	
2) Operation fees	X	
3) Visiting fees	X	
4) Sale of medicines	X	
5) Gift from patients (<i>because these are received as token of gratitude for professional services rendered</i>)	X	
6) Value of any perquisite received by such person	X	
7) Examiner's fees	X	
8) Nursing home receipts	X	
9) Any other professional receipt	X	XXX
<u>Less: Professional Expenses:</u>		
1) Dispensary Expenses (i.e., rent, light, water charges, salary to staff, telephone expenses etc.)	X	
2) Opening stock plus Cost of medicines less closing stock	X	
3) Depreciation on Surgical Equipment and X-ray Machines, etc., (at prescribed rates)	X	
4) Cost of books for professional purposes	X	
5) Motor car expenses: depreciation relating to professional work	X	
6) Expenditure incurred to increase professional knowledge	X	
7) Nursing home expenses	X	
8) Any other expenditure incurred during the year	X	(XXX)
<u>Professional Income</u>		<u>XXX</u>

II. In case of Chartered Accountant: -

<u>Professional Receipts</u>		
1) Audit fees	X	
2) Income from accountancy work	X	
3) Institute fees	X	
4) Examiner's fees	X	
5) Gifts from clients, if any	X	
6) Consultancy Services	X	
7) Fees for taxation work	X	
8) Any other receipt	X	XX
<u>Less: Professional Expenditure</u>		
1) Office expenses	X	
2) Institute expenses	X	
3) Cost of books	X	
4) Motor car expenses relating to professional work	X	
5) Membership fees	X	
6) Depreciation on office equipment, car or scooter etc.	X	
7) Any other expenditure incurred to increase professional knowledge	X	

8) Stipend to trainees	X	
9) Subscriptions	X	
10) Dep. on office furniture	X	<u>(XX)</u>
<u>Professional Income</u>		<u>XXX</u>
III. Income of a Lawyer or an Advocate: -		
<u>Professional Receipts</u>		
1) Practicing fees	X	
2) Legal fees	X	
3) Special commission	X	
4) Presents from clients	X	
5) Examiner's fees	X	
6) Any other receipt	X	XX
<u>Less: Professional Expenses</u>		
1) Office expenses	X	
2) Salary of staff, if any	X	
3) Cost of books for professional purposes	X	
4) Depreciation of office equipment	X	
5) Expenditure incurred to increase professional knowledge	X	
6) Subscription	X	
7) Purchase of stamp paper and court fee	X	
8) Travelling expenses	X	<u>(XX)</u>
<u>Professional Gain</u>		<u>XXX</u>

PROFITS AND GAINS FROM BUSINESS OR PROFESSION

- 1) Anticipated hedging loss under a contract to purchase raw material.
- 2) Non-recovery of a bill due to negligence of an employee.
- 3) Initial expenditure incurred on installation of fluorescent tube lights.
- 4) Non-recovery of advance allowed to 100% subsidiary company engaged in the business of financing subsidiary companies.
- 5) Consultation fees paid to tax advisor.
- 6) Lump sum payment made to acquire a licence regarding technical information to reduce the production cost.
- 7) Payment made to catering agency for providing food/beverages to employees, working in overtime @ Rs 75 per employee for 20 days.
- 8) Subsidy received from the government to compensate the loss suffered in exports under government sponsored scheme, has been directly credited to Capital Reserve A/c. The assessee claims it as exempt.
- 9) Compensation paid to an employee under voluntary retirement scheme which does not conform to the guide lines under Sec. 10(10C).
- 10) Commission accrued during the year but not credited in books as it has been held back due to breach of certain conditions, which may create liability to pay damages.
- 11) Rent of quarters, located near factory, let out to the employees of the factory, was treated as income from house property.
- 12) Fees of Rs 30,000 were paid by the company to a lawyer to defend the company in a court case. Lawyer is the brother of the director of the company. The fees have been paid by a bearer cheque and it is found excessive to the extent of Rs 20,000.
- 13) Employees contribution to the recognised provident fund, Rs 60,000 has been charged to the profit and loss account but only Rs 25,000 was credited to their accounts on due date and the balance was credited to their account on the due date fixed for furnishing return of income for the relevant previous year.
- 14) Bonus/commission to employees was paid: (a) during the previous year; or (b) after the previous year but on or before the due date of return of income for that year, or (c) after the due date the return of income for that previous year.
- 15) Salary has been paid to a resident employee outside India and non-resident employee in India but no tax has been paid thereon or deducted therefrom.
- 16) Advertisement expenses incurred outside India in foreign currency. RBI permission has not been obtained.
- 17) Municipal taxes and land revenue in respect of staff quarters were paid after due date of furnishing return of income for the relevant previous year.
- 18) Foreign tour expenses of the managing director for 10 days. However, 2 days were devoted to personal work.
- 19) Advertisement in a journal published by political party.
- 20) 600 VIP brief cases, costing Rs.1,500 each, presented to customers.
- 21) Voluntary payment of gratuity paid an account of commercial expediency to an employee who died on business tour.
- 22) Traveling expenses to explore the feasibility of new line of business.
- 23) Annual payments in installments over a period of 10 years to seek assistance in technical know-how for improving quality of product.
- 24) Expenses incurred for registration of trademarks.
- 25) Employees were issued shares at par to protect business interest. Difference of market price and par value was charged as revenue expenditure.
- 26) Expenditure incurred on neon-sign board for the business premises.
- 27) Theft of stock-in-trade assuming (a) it is insured (b) it was uninsured
- 28) Expenditure incurred for new telephone connection.
- 29) Purchase of sanitary and pipeline for factory
- 30) Legal charges incurred for framing the scheme of amalgamation of C company with the assessee company.
- 31) Compensation paid to cancel the purchase order of a machine due to abnormal rise in its price. The assessee claims it as trading loss, or capital loss.
- 32) Confiscation of goods, imported without a valid import licence. The assessee was also fined by custom authorities. The assessee claims deduction for both of them under general deductions Sec. 37(1).
- 33) The assessee claims the set-off unabsorbed depreciation of a discontinued business against the profits of another business.

Solution:

- 1) Anticipated hedging loss under a forward contract is not allowed to be deducted.
- 2) Loss caused due to negligence of employee is allowed to be deducted.
- 3) Initial expenditure on installation of fluorescent tube lights is a capital expenditure, not deductible [Sec. 37(1)].
- 4) As the business of 100% subsidiary is to finance subsidiary company, loss on account of non-recovery of such advances relates carrying on business. Such loss is an allowable deduction.
- 5) Consultation fee paid to tax-advisor is allowed under Sec. 37(1).
- 6) Payment made to acquire licence regarding technical information is a capital expenditure. Depreciation is allowed under Sec. 32 on such cost.
- 7) Payment made to catering agency to provide food/beverages to employees is allowed under Sec. 37(1). However, the employer becomes liable to pay Fringe Benefit Tax.
- 8) Subsidy granted by government against loss suffered by exporters under government-sponsored scheme, is a trading receipt. Recovery of loss is taxable under Sec. 41(1).
- 9) Compensation paid under voluntary retirement scheme is allowed to be deducted in five equal annual instalments [Sec. 35DDA]. Scheme of voluntary retirement need not be in accordance with the guidelines of Sec. 10(10C).
- 10) Commission accrued during the year is taxable under mercantile system. Liability to pay damages for breach of certain conditions is a contingent liability. No deduction can be allowed for such provision.
- 11) Rent from quarters, let out to employees, is a business income provided the letting is subservient and incidental to the main business.
- 12) Payment made by a company to the brother of the director of the company, is covered under Sec. 40A(2). Therefore, excessive fees of Rs 20,000 have to be disallowed. Provisions of Sec. 40A(3) apply to the balance payment since it has been made by bearer cheque. Accordingly, the balance of Rs.20,000 shall have to be disallowed in computing taxable business profits, w.e.f. A.Y.2008-09.
- 13) Deduction is allowed for employees' contribution credited to their account on the due date under provident fund rules. No deduction is allowed for such contribution credited to their account thereafter. Employees' contribution, deducted from their salaries, is first treated as business income. If the same has not been credited to their account, the same has to be treated business income first.
- 14) Bonus/commission paid to the employees during the previous year or paid after the previous year but before the due date fixed for furnishing return of income for the previous year is allowed to be deducted in the same previous year in which the liability to pay such bonus/commission arose. Any bonus/commission, paid to employees after such due date, is allowed to be deducted in the previous year in which the date of payment falls.
- 15) Salary paid to any person outside India (resident or non-resident) or salary paid to a non-resident in India is not allowed to be deducted if tax has not been paid thereon nor deducted therefrom [Sec. 40(a)(iii)]. Thus, no deduction is allowed in the instant case. It is operative from the assessment year 2004-2005.
- 16) Advertisement expenditure incurred in India or outside India is allowed to be deduction under Sec. 37(1) provided it is not of capital nature and it is incurred wholly and exclusively for the purposes of business. Permission of RBI is not relevant.
- 17) Deduction of municipal taxes and land revenue in respect of staff quarters, will be deducted in the previous year in which the date of payment falls (Sec. 43B).
- 18) Proportionate foreign tour expenses of the director relating to personal work are not to be allowed; such expenditure has not been incurred wholly and exclusively for the purposes of business. However, air fare (both ways) will be fully allowed.
- 19) No deduction can be allowed for advertisement in the journals published by a political party [Sec. 37(2B)].
- 20) Presentation of VIP bags to customers is allowed as expenditure on advertisement under Sec. 37(1). There is no ceiling limit for gift articles.
- 21) Voluntary payment of gratuity on account of commercial expediency is allowable deduction under Sec. 37(1).
- 22) Travelling expenditure for exploring new line of business is a capital expenditure. It is not allowed under Sec. 37(1). It may be capitalised for the purposes of Sec. 35D.
- 23) Annual instalment paid for technical know-how is a revenue expenditure. It is allowed under Sec. 37(1).
- 24) Expenses incurred for registration of trademark is a revenue expenditure. It is, therefore, allowed under Sec. 37(1).
- 25) Waiver of premium while issuing shares to employees, is not a trading transaction. It is not deductible.
- 26) Expenditure incurred on neon-sign board is a capital expenditure. It is not allowed in computing business income [(Sec. 37(1))]. However, depreciation can be claimed on it @ 15%.
- 27) Loss of stock-in-trade due to theft is allowed under Sec. 29 as incidental to business. However, if it is insured insurance compensation will be a trading receipt.
- 28) Expenditure on new telephone lines is allowed under Sec. 37(1). It is a revenue expenditure incurred for the purposes of business.
- 29) Purchase of sanitary pipe-line is a capital expenditure, not allowable under Sec. 37(1). However, depreciation is allowed under Sec. 32 @ 15%.
- 30) Amalgamation expenses are allowed to be deducted in computing taxable profits under Sec. 35DD in five equal annual instalments.
- 31) Compensation paid to cancel the purchase order of a machine, is a capital expenditure. It avoids futile investment in machine. It cannot be deducted under Sec. 37(1). As there is no "transfer" of a capital asset, compensation paid cannot be claimed as a capital loss also.
- 32) Explanation to Sec. 37(1) does not allow any illegal expense in computing taxable profit of business. Therefore, fine imposed for illegal import cannot be allowed [Explanation to Sec. 37(1)]. However, loss by way of the confiscation of goods can be allowed as incidental to business under Sec. 29.
- 33) Unabsorbed depreciation of a discontinued business now can be set-off against the profits of any other business and thereafter against the income of any other head. It is operative from the assessment year 2001-2002.