6 PROFITS OF BUSINESS OR PROFESSION [S. 28 - 43B]

THEORY AND ILLUSTRATIONS

OUTLINE

No.	Topic	Section	Page
1.	**Basis of Charge**	[S. 28]	141
	1.1 Provision		
	1.2 Speculative Business		
2.	**Profits of Business Carried on by Assessee in Previous Year**		142
	2.1 Business		
	2.2 Business Carried on By Assessee		
	2.3 Business Carried on During Previous Year		
	2.4 Profits		
3.	**Computation of Business Income**	[S.29]	145
	3.1 Compuation		
	3.2 Exemption		
4.	**Deductions Expressly Allowed**	[S.30 to 32, 36, 37]	146
5.	**Rent, Repairs, Taxes and Insurance of Building**	[S.30]	146
6.	**Repairs & Insurance of Machinery & Furniture**	[S.31]	147
7.	**Depreciation**	[S.32]	147
	7.1 Provision		
	7.2 Conditions		
	7.3 Computation		
	7.4 Special Cases		
	7.5 Deduction Compulsory, Whether Claimed or Not		
	7.6 Unabsorbed Depreciation		
8.	**Expenditure on Scientific Research**	[S. 35]	153
9.	**Amortisation of Preliminary Expenses**	[S. 35D]	155
10.	**Specific Deductions**	[S. 36]	157
	10.1 Insurance Premium on Stocks		
	10.2 Insurance on Health of Employees		
	10.3 Bonus or Commission to Employees		
	10.4 Interest on Capital Borrowed		

10.5 Discount on Zero Coupon Bond
10.6 Employer's Contribution to RPF/SAF/Pension
10.7 Contribution to Gratuity Fund
10.8 Employee's Contribution to P.F. Paid in Time
10.9 Write Off Allowance for Animals
10.10 Bad Debts Written Off
10.11 Family Planning Expenditure
10.12 Banking Cash Transaction Tax
10.13 Expenses Allowable to Some Specific Assessees

11. General Expenditure [S. 37(1)] 161
11.1 Conditions
11.2 Examples of Expenditure Allowable U/S 37
11.3 Examples of Expenditure Not Allowable U/S 37

12. Expenses Expressly Disallowed [S.37 (2B), 40 & 40A] 162
12.1 Advertisements in Political Souvenir [S. 37(2B)]
12.2 Sums Payable Outside India [S. 40(a)]
12.3 Payments To Residents Without TDS [S. 40 (a) (ia)]
12.4 Securities Transaction Tax [S. 40 (a) (ib)]
12.5 Fringe Benefit Tax [S. 40(a)]
12.6 Royalty on State Government Undertakings [S. 40 (a) (iib)]
12.7 Tax on Business Profits
12.8 Remuneration Paid by Firm to Partners [S.40(b)]
12.9 Interest Paid by Firm to Partners [S.40(b)]
12.10 Payments by AOP/BOI to Members [S.40(ba)]
12.11 Excessive Payments to Relatives [S. 40A(2)]
12.12 Expenses Exceeding ₹ 10,000 Paid in Cash [S. 40A(3)]
12.13 Provision for Gratuity on Retirement [S. 40A(7)]
12.14 Contributions to Non-Statutory Funds [S.40A(9) - (11)]
12.15 Marked to Market Loss [S. 40A(13)]

13. Unpaid Statutory Liability [S. 43B] 166

14. Computing Taxable Income from Accounts 169

15. When Receipts and Payments Account is Given 169
15.1 Scrutiny of Receipts
15.2 Scrutiny of Payments
15.3 Information in Notes
15.4 Compute Net Business Income

16. When Profit and Loss A/c is Given 171
16.1 Additions to Net Profit
16.2 Deductions from Net Profit
16.3 Net Loss vide P & L A/c
16.4 Income & Expenditure Account

17. Worksheet / Rapid Revision 172

18. Illustrations 173

WORKSHEET 4 : COMPUTING INCOME FROM BUSINESS

ASSESSEE :

PREVIOUS YEAR : 1-4-2021 TO 31-3-2022 **ASSESSMENT YEAR : 2022-23**

	Particulars	₹
	INCOME FROM BUSINESS	
1.	**FROM RECEIPTS & PAYMENTS ACCOUNT**	
	1.1 Business Receipts vide R & P A/c	
	1.1.1 Income from Business / Profession	
	1.1.2 Profits chargeable u/s 28 (Compensation; Export benefits; Perks)	
	1.1.3 Remuneration/Interest from firm	
	1.2 Less : Payments vide R & P A/c	
	1.2.1 Business Expenses (Materials, Administration, Selling)	
	1.2.2 Expenses expressly deductible [S.30-32; 35, 35D,36,37]	
	Net Income from Business / Profession	
	1.3 Ignore following receipts -	
	1.3.1 Capital Receipts	
	1.3.2 Exempt income	
	1.3.3 Income under other heads	
	1.4 Ignore following payments -	
	1.4.1 Capital expenditure	
	1.4.2 Personal expenses	
	1.4.3 Expenses related to income under other heads	

	1.4.4 Appropriations such as Tax, Drawings, donations	
	1.4.5 Expenses expressly disallowed (S.37, 40, 40A, 43B)	
2.	**FROM PROFIT & LOSS ACCOUNT**	
	2.1 Net Profit vide P & L A/c	
	2.2 Add : Unrelated items debited to P & L A/c	
	2.2.1 Expenses related to earlier or future period	
	2.2.2 Capital expenditure (fixed assets)	
	2.2.3 Capital Losses	
	2.2.4 Personal expenses	
	2.2.5 Expenses related to income under other head	
	2.2.6 Appropriation from profits (reserves, drawings, income-tax)	
	2.3 Add : Expenses separately allowable	
	2.3.1 Depreciation debited to P & L A/c	
	2.4 Add : Expenses expressly disallowable [S. 37(2), 40, 40A, 43B]	
	2.4.1 Payments without T.D.S., WT	
	2.4.2 Securities Transaction Tax	
	2.4.3 Fringe Benefits Tax	
	2.4.4 Tax on Profits	
	2.4.5 Excess Remuneration or Interest, Paid by Firm to Partner	
	2.4.6 Excessive Payments to Specified Persons (Relatives etc.)	
	2.4.7 100% Expenses Exceeding ₹ 10,000 paid in cash	
	2.4.8 Provision for Gratuity on retirement	
	2.4.9 Employer's Contribution to Non-Statutory Funds	
	2.4.10 Tax, bonus, interest, contributions paid late	
	2.5 Add: Items taxable; not shown in P & L A/c	
	2.5.1 Income from Business / Profession	
	2.5.2 Profits chargeable u/s 28 (Compensation; Export benefits ; Perks)	
	2.5.3 Remuneration / Interest from firm	
	2.6 Less : Unrelated items credited to P & L A/c	
	2.6.1 Business income for earlier or future years	
	2.6.2 Capital Receipt (loan, personal gifts, income-tax refund)	
	2.6.3 Exempt Income (agriculture income, casual income.)	
	2.6.4 Income from other heads (from Salary, House-Property etc.)	
	2.7 Less : Deductions separately allowable	
	2.7.1 Depreciation (as allowable)	
	2.8 Less : Deductions expressly allowable	
	2.8.1 Expenditure on Family Planning (only by a Co.)	
	Net Income from Business / Profession	

18. ILLUSTRATIONS

Illustration 14 :

From the following Profit and Loss Account of X for the year ending 31st March, 2022 compute his business income :

Particulars	₹	Particulars	₹
To Office Salaries	15,000	By Gross Profits	[illegible]
To General expenses	8,500	By Interest on Bank Deposits	[illegible]
To Interest on Capital of X	3,000	By Interest on Company Deposits	[illegible]
To Bad debts reserve	5,000	By Refund of Income tax for A.Y 2018-19	[illegible]
To Depreciation	15,000		
To Advertisement	9,000		
To Fire Insurance premium	1,200		
To Donation	5,000		
To Advance Income Tax	4,000		
To GST paid	5,000		
To Income-tax for 2020-21	3,000		
To Net Profit	69,000		1,42,700
	1,42,700		

Following additional information is given :

(1) Allowable depreciation was ₹ 10,000.

(2) General expenses include furniture purchased worth ₹ 2,500.

(3) Office salaries include salaries paid to Mrs. X ₹ 3,000. Mrs X, B.Com. writes the accounts of the business.

(4) Advertisement includes ₹ 2,500 for the advertisement in souvenir of a political party.

(SYBAF, Mar. 18, adapted)

Solution :

COMPUTATION OF BUSINESS INCOME OF MR. X **ASSESSMENT YEAR : 2022-23**

PREVIOUS YEAR : 2021-22

Particulars	₹	₹
(A) Net Profit as per Profit and Loss A/c		69,000
(B) Add :		
(1) Purchase of furniture (Capital expenditure)	2,500	
(2) Interest on Capital of proprietor	3,000	
(3) Bad debts reserve - (not actual expenditure)	5,000	
(4) Depreciation - allowed separately	15,000	
(5) Donation	5,000	
(6) Advance Income tax (personal expenditure)	4,000	
(7) Income tax for last assessment (personal expenditure)	3,000	
(8) Advertisement (WN 2)	2,500	40,000
		1,09,000
(C) Less :		
(1) Interest on bank deposits (Taxable under other sources)	4,100	
(2) Interest on Company Deposits (Taxable under other sources)	7,600	
		10,000
(3) Depreciation Separately Allowed	1,000	22,700
(4) Income-tax refund (not considered as income)		86,300
(D) Net Income from Business (A + B - C)		

Working Note :

(1) As salary paid to Mrs. X is reasonable, it is allowed as a business expenditure.

(2) Advertisement in souvenir of a political party is not allowable deduction, u/s. 37(2B).

Illustration 15 :

Mr. X owns a soap factory at Pune. Following is the Profit and Loss Account prepared by him for the accounting year 2021-22.

Particulars	₹	Particulars	₹
To GST (incurred during year)	2,000	By Gross Profit	75,000
To Advertising	5,000	By House Property Income	5,000
To Bonus	8,000		
To Commission	2,000		
To Depreciation	6,000		
To Donation to National Defence Fund	1,000		

To Embezzlement by an employee	2,000		
To General expenses	5,000		
To Salary to staff	10,000		
To Office expenses	5,000		
To Discount to retailers	3,000		
To Sundry expenses	5,000		
To Net Profit	26,000		
	80,000		80,000

Compute his business income for the assessment year 2022-23. Further particulars -

(1) GST paid during the year was ₹ 400. Total bonus paid during the year was ₹ 8,000 debited in the books and ₹ 11,000 provided for in preceding year but paid in the current year.

(2) Office expenses include ₹ 1,050 paid as bribe.

(3) General expenses include ₹ 1,000 being the municipal taxes in respect of house property.

Solution:

COMPUTATION OF BUSINESS INCOME OF MR. X ***(SYBAF, Mar. 18, adapted)***

PREVIOUS YEAR : 2021-22 **ASSESSMENT YEAR : 2022-23**

Particulars		₹	₹
(A)	**Net Profit as per Profit and Loss A/c**		26,000
(B)	**Add :** Expenses disallowed		
	(1) Municipal taxes (allowed as a deduction from House property)	1,000	
	(2) Donation to National Defence Fund	1,000	
	(3) GST (subject to s. 43B)	2,000	
	(4) Bribe [disallowed u/s 37(1) - Explanation]	1,050	5,050
			31,050
(C)	**Less :**		
	(1) Chargeable under Income from house property	5,000	
	(2) Bonus for preceding year, paid (allowed vide S. 43B)	11,000	
	(3) GST paid (allowed vide S. 43B)	400	16,400
(D)	**Business Income (A + B - C)**		14,650

Working Notes :

(1) Embezzlement (theft) by an employee is a business loss hence, allowed as a deduction.

(2) Bribe is an illegal expenditure hence, not allowed as a deduction.

(3) In absence of information, depreciation debited to P & L A/c is assumed to be the depreciation allowable under the Income Tax Act.

(4) Income from house property will be computed separately.

(5) Bonus is allowed as a deduction on payment basis (even if for previous year) U/S 43 B.

Illustration 16 :

Mr. Roshan is a proprietor of a business. Following was the Profit and Loss Account of his business for the year ended 31st March, 2022. You are required to compute his income from business for the Assessment year 2022-23.

Particulars	₹	Particulars	₹
To Opening stock	2,34,000	By Sales	12,40,000
To Purchase	10,00,000	By Closing stock	2,05,000
To Office Salaries	57,000	By Income tax refund	15,000
To Proprietor's Salaries	30,000	By Dividend from UTI	20,000
To Bad debts	25,000	By Dividend from Bajaj Ltd.	25,000
To Advertisement	10,500	By Interest on PPF	15,000
To Fire Insurance Premium	4,500		
To Conveyance Expenses	6,000		
To Interest on proprietor's capital	25,000		
To Medical Expenses	20,000		
To General Expenses	35,000		
To Wealth tax paid	5,000		
To Residential telephone expenses	14,000		

To GST penalty	4,000		
To Depreciation	30,000		
To Net Profit	20,000		
	15,20,000		15,20,000

Additional Informations :

(1) The residential telephone is used half the time for office work.

(2) Purchases include ₹ 80,000 paid for cash purchases, exceeding the limits prescribed Under Section 40A (3) of the Income Tax Act, 1961.

(3) General expenses include advance Income tax of ₹ 10,000 paid during the year and ₹ 500 for purchase of Lottery tickets.

(4) Depreciation allowable as per Income Tax Rules ₹ 25,000. ***(T.Y.B.Com., Mar. 2000, adapted)***

Solution :

MR. ROSHAN **LEGAL STATUS : R & OR**

STATUS : INDIVIDUAL **ASSESSMENT YEAR : 2022-23**

PREVIOUS YEAR : 2021-22

Particulars		₹	₹
(A)	**Net Profit as per P & L A/c**		20,000
(B)	**Add : Expenses Disallowed**		
	Proprietor's Salaries (appropriation)	30,000	
	Interest on Proprietor's Capital (appropriation)	25,000	
	Medical Expenses (personal)	20,000	
	Wealth-tax paid [S. 40(a)(3)]	5,000	
	Residential Telephone Expenses (1/2)	7,000	
	GST Penalty	4,000	
	Depreciation (as per books)	30,000	
	Cash Purchases (100% of ₹ 80,000) [U/S 40A(3)]	80,000	
	Income-tax [S. 40(a)(2)]	10,000	
	Lottery Tickets	500	2,11,500
			2,31,500
(C)	**Less : Considered Separately / Not Taxable**		
	Income-tax Refund (Capital receipt)	15,000	
	Dividend from UTI (IFOS)	20,000	
	Dividend from Bajaj Ltd. (IFOS)	25,000	
	Interest on PPF (Exempt u/s 10)	5,000	
	Lottery Prize (IFOS)	10,000	
	Depreciation (allowable)	25,000	1,00,000
(D)	**Income From Business**		1,31,500