Unit V

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Profit and gain from Business of Profession

Introduction:

Among the five heads of Income "Profits and Gain of business or profession" is the most important sources of Tax Collection for the Government. Sec 28 to 44 of the Income Tax Act 1961. Contain provisions relating to computation of profit and gain of business or profession.

Allowable Expenses:

The deduction allowed u/s. 30 to 37 are summarised below:

The Income under the head 'profits and Gains of Business or Profession' shall be computed in accordance with deduction admissable under sec 30 to 37.

1. Rent, rates, taxes repairs and insurance for Buildings Sec 30):

a) Where the premises are occupied by the assessee

i) As a tenant, rent paid for premises. Further if he has undertaken to bear the cost of repairs to the premises, the amount paid on account of such repairs.

ii) otherwise than as a tenant; The amount paid by him on account of current repairs to the premises.

b) Land revenue etc. The amount paid by the assessee on account of land revenue, local rates or municipal taxes.

c) Insurance premium; The amount of premium paid in respect of insurance against risk of damage or destruction of the premises.

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2. Repairs and Insurance of Machinery, Plant and Furniture. Sec. 31.

i) The amount paid on account of current repairs there to.

ii) The amount of premium paid in respect of insurance against risk of damage or destruction in there of.

3. Tea / coffee / Rubber Development Account (33AB)

a) Tea / coffee / Rubber business: The assessee must be engaged in the bussiness of growing and manufacturing tea, coffee, or rubber in India.

b) Deposit with NABARD.: The Assessee must deposit with Nation Bank for agricultural and Rural Development (NABARD) any amount or amounts in an account maintained by the assessee with the bank in accordance with and for the purpose specified in a scheme approved by the Tea Board.

c) Audit of Accounts: The account of the assessee should be duly audited by a Charted Accountant and the report of the auditor is to be filed along with the return of relevant A.Y. in form No: 3AC.

4. Deduction for Shipping Business (Sec. 33AC)

i) A Government Company carrying on shipping business.

ii) An Indian Public Ltd. Company carrying on shipping business.

Expenditure of Scientific research: sec

In respect of expenditure on scientific research the following deduction shall be allowed.

Expenditure on Scientific research.

- Expenditure on research carried by the assessee.
  - Revenue Expenditure incurred by the Assessee
  - Capital expenditure incurred by the Assessee
  - Expenditure on in-house Research and Development.
- Contribution to outsiders.
  - Contribution to an approved scientific research association.
  - Payment to National Laboratory

Revenue expenditure incurred by the assessee: The revenue expenditure incurred by the assessee by carrying on scientific research related to the assessee's business is allowed as business expenditure

Precommencement Period expenses: In the form of salary paid to employees engaged in research and any expenditure incurred on purchase of materials use in scientific research paid or incurred within three years immediately preceding the commencement of business.

Contribution made to outsiders:

a) Payment made to an approved scientific research association: Any payment made to an approved scientific research association which has its object

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undertaking of Scientific research related to unrelated to the business of the assessee.

b) Payment made to an approved university, College etc.

It is institution for the use of scientific research related ~~to~~ or unrelated to the business of the assessee. Any payment to an approved university, college or institution for the use of research for social science or Statistical science is allowed at 100% of actual expenditure related or unrelated to the business of the assessee.

Disallowable Expenses. ~~Deduction~~ Deduction u/s 37(1) from Business Income.

-> Fees to Registrar of Companies for changing an organisation's Articles of Association and Memorandum.

-> Cost incurred by an assessee to gain Possession of a vacant land he/she owns

-> Fees to registrar of Companies to increase an organisation's authorised capital

-> Payments for gaining a property's tenancy rights.

-> Bank guarantee commission payments for securing a loan in order to acquire a fixed asset.

-> Penalities for infringing or violating any law or regulation.

-> Cost incurred for damaging demolishing a building in order to build a hotel on the Same site.

-> Cost incurred for shifting a company's Registered office from it's present location to another.

-> Sales tax Payments for Purchase and Sale of goods.

General Deduction: Sec. 37.

Conditions of deduction under (Sec. 37)

i) The expenditure should not be of the nature described in section 30 to 36.

ii) It should not be in the nature of capital expenditure.

iii) It is not in the nature of Personal expenses of the assessee.

iv) It should have been incurred in the previous year.

v) It should have been incurred wholly and exclusively for the purpose of the business or Profession of the assessee.

vi) It should not have been incurred for any purpose against the law.

Deemed Business Profit:

1. Recovery of any loss or expenditure or loss in earlier year. Sec. 41. (i)

If any sum allowed as deduction as expenditure or loss in earlier year is recovered in a subsequent year. the amount so recovered shall be treated as deemed profit and shall be assessed to income tax in the year of recovery.

If any loss or expenditure has been allowed as deduction in an earlier year and thereafter if the business has changed hands and subsequently the successor in business has realised any amount in respect of such loss or expenditure.

2. Sale of asset used for scientific research: Sec 41(3)

If a capital asset used for scientific research is sold without having been used for other purposes and the sale proceeds together with the deduction allowed U/S 35 exceeds the amount of capital expenditure incurred on it such surplus or the amount of deduction allowed, whichever is less, is chargeable to tax as business income of the previous year in which the sale took place.

3. Bad debts recovered sec. 41.(4)

If the bad debts allowed as deduction in an earlier year is recovered in a subsequent year, it is taxable as deemed business profit in the year of recovery.

4. Recovery after discontinuance of business or profession. If any business or profession is deemed in any year, and any sum is recovered afterwards it will be deemed to be income of the recipient and charged to tax in the year of recipient.

5. Withdrawn from special reserve (sec. 41(4A)

In any amount is withdrawn from any special reserve created and maintained by a financial corporation. [U/s 36(i)(viii) it will be deemed to be the income of the previous year in which such amount is is withdrawn from the Reserve Account

Compulsory Maintenance Of Basic Accounts:

Accounting methods:

The Income Tax authorities accept the following three methods of accounting for the purpose of assessment of profit and gains.

Cash method. Under this system only such transaction are recorded in which actual receipts and payment of the business occur. Entries in the books are made when money is actually received or actually paid. No account is maintained for outstanding prepaid accrued or unrealised incomes.

Mercantile system: In this system proper records of cash as well as credit transaction is made. Under this system any income which relates to the current year whether it is received or not and any expenditure whether actually paid or not. Is taken into consideration for computing the profits and losses of the business

Maintenance Of Basic of Accounts: U/S 44 AA

1. Specified Profession.

a) Legal b) Medical c) Engineering d) Architectural e) Accountancy f) Technical consultancy g) Interior Decoration h) other notified profession

2. Non Specified Profession Or Business:

Those whose income from such profession or business exceeds Rs 2,50,000 or total sales or turnover or gross receipts exceeds Rs 25,00000 in any of the three years.

Immediately Preceding the Previous Year or in the case of newly set up profession or business income.

2. Business under section 44 AD, 44 AE and or 44B'B or 44 BBB.

Where the assessee claims that the Profits and gains of business of civil construction Sec. 44AD) or Playing, hiring or leasing goods carriage. Sec 44 AE are lower than the deemed profit under these section he has to maintaing the books of accounts of such business.

Audit of Accounts certain Person:

1. Turnover / Gross receipts exceeding Prescribed limit: In 1% obligatory for a person carrying on business to get his accounts audited before the "Specified date" if the total sales, turnover or gross receipt in business for the Previous year exceed Rs 1. crore

2. Business under section 44 AD, 44 AE and 44BB or 44 BBB. Where the assessee. claims that profits and gains of business of civil construction (sec 44 AD) or playing, hiring or leasing goods carriage 44 AE are lower than the deemed proofit under these sections.

3. Assessee claiming deduction under sec. 33AB

Where the assessee claims deduction under "Tea development a/c", "State restoration fund", "Preliminary expenses" or Expenditure or Prospecting etc. for certain minerals. he has to get his accounts audited and furnished by the specified date a a report of the audit in the prescribed form.

Special Provision for computing income of estimated Business:

Sec. 44 AD: Computation of income on estimated basis in the case of tax payers engaged in the business of retail trade or any other business or civil construction is applicable only if the following conditions are satisfied:

1. The tax payer may be an individual, HUF, AOP, BOI, Firm, company, Co-operative society or any other Person (Resident or non resident)
2. The Assessee is engaged in the business does not exceed Rs or supply of labour for civil construction work.
3. Gross receipt from the above business does not exceed Rs two crores
4. The estimated income is 8% of the gross receipts paid or payable. or higher income declared by the assessee.
5. Comprehensive income: 8% If as calculated above is comprehensive income and no deduction U/S 30 to 38 is allowed except salary and interest on capital in the case of a firm.
6. The income is aggregated with any other income of the assessee. The brought forward business loss and other losses shall be deducted as per the rules of set off and carried forward. Tax on income is computed and rebate under Se. 88, 88B and 88C shall be allowed.

7. Provision regarding books of Accounts and Audits of Accounts under Sec. 44 AA and 44 AB are not required. However if the assesse declares a lower income than stated above. the tax payer has to maintain books of accounts u/s 44 AA and get the books audited u/s 44 AB.

Compution of Business Income:
Problem. 1.

From the following, compute the taxable income under the head income from business, Profit before adjusting the following items. Rs. 5,50,000

Administration expenses.	10000
Trade expenses	5000
House hold expenses	3000
Discount allowed	4000
Income Tax	400
Provision for bad debts.	2000
Bad debts.	3000
Donation to P.M National relief fund	4000
Legal fee.	200

Solution

Computation of Business Income.

Particular	Rs	Rs.
Net Profit.		5,50000
(-) Admissiable expenses: Administration expenses.	10,000	
Trade expenses	5000	
Discount allowed	4000	
Baddebts	3000	
Legal fee	200	22200
Business Income.		5,27800

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Problem 2.

Mr. Ravi Submits the following Particulars of his business from which you calculate the income from business. Net profit as per P/L a/c. (after charging the following) Rs 1,25,000

a) Sales tax Rs 20000 and Income Tax. 55000
b) Bad debts Provisions Rs 3000.
c) Commission to procure business order Rs 8000.
d) interest on Capital Rs 38000.
e) Depreciation Rs 4,000. (but as per income Tax rules Rs 2000 only.

Solution:

Computation of Business Income

Particulars	Rs	Rs
Net Profit.		1,25,000
Add Inadmissable expenses:		
Income Tax.	55000	
Bad debts Provision	3000	
Interest on Capital.	38000	
Depreciation.	4000	1,00000
		225000
Less. Expenses allowed.		
Depreciation		2000
Business Income.		2,23,000

Problem 3.

The profit and loss a/c of a firm shows a profit of Rs 50000 after debit of following sums.

Income Tax paid.	30000
Travelling expenses	20000
Penalty & fees	40000
Sales Tax	30000

~~Computation of Business Income:~~

Particulars	Rs	Rs.
Net Profit.		50,000
Add. Inadmissable expenses.		
Income Tax Paid.	30000	
Penalty & fees.	40000	70000
Business Income.		1,20,000

Problem 4:

Following is the P&L AC of Aswin kumar for the year ending 31st Marc 2025. You are required to ascertain his income from business for the year ended on that date.

Particulars	Rs	Particulars	Rs.
Salaries	7800	Gross Profit.	35672
Sundry expenses	1200	Discount	751
Reserve for bad debts	3000	Commission	1205
Insurance	450	Sundry Receipts	52
Advertising	2500	Profit on sale of	
Income Tax	2375	Import Licence.	20000.
Loss on Sale of Car	1200		
Interest on capital	1000		
Interest on Bank Loan	1550		
Charity	150		
Taxation Reserve	3000		
L.I.C. (self)	550		
Loss of a Part of building by fire	1500		
Amount Paid to a university for Social research	10,000		
Depreciation.			
on Building	1000		
on Furniture.	200		

Difference in Trial balance.	105	
Net profit	30100.	
	57680	57680

Additional data:

1). Motor car was used equally for business purposes and the Proprietors private purposes.

2) Bank loan is taken for business purposes.

3) The amount of depreciation allowable according to income Tax Rules. in respect of Building and furniture was rs. 800 and rs. 150 respectively.

4) Included in the advertising expenses is a sum of rs 1000 expended on a special advertising campaign undertaken during the year. in respect of a product of a company placed recently in the market.

5) Salaries include rs 3000 being the amount drawn by Aswin Kumar during the year against profits.

Solution:

Computation Of Business Income Of Ashwin kumar. for the Pr. Year. 2024-25.

Particulars.	rs	Rs.
Net Profit		30100
Add: Inadmissable expenses:		
Reserve For bad debts.	3000	
Income Tax	2375	
Loss on sale of car.	1200	
Interest on capital	1800	
Charity	150	
Taxation Reserve	3000	
L.I.C (self)	550	
Loss of a Part of building by fire (being capital loss)	1500	
Difference in Trial balance.	105	

Depreciation chaged: on Building	1000	
On furniture	1200	
Salary drawn by owner	3000	
Amount ~~drawn~~ Paid to ~~by~~ University	10,000	27080
		57,180
(-) Allowance Depreciation.		
On Building	800	
On furniture.	150	
Amount Paid to university for Social & Statistical research @ 100% of 10,000.	10000	10950
Business Income		46230

Problem 5.

From the following Profit & Loss A/c of a Manufacturer Calculate income under the head "Profits and Gains of Business or Profession" for the year ending 31st March 2025.

Particulars	Rs	Particulars	Rs.
Salaries to employees	95000	Gross Profit.	3,80000
Advertisement expenses	24000	Interest on Securities	14000
General expenses	16000	Income from House Property	25000
Entertainment expenses.	22000		
Bad debts	1500	Bad debts recovered (allowed earlier)	12000.
Drawings by proprietor	24000		
Sales tax (due and paid on 1.7.2025	6000		
Interest on Proprietor Capital	2500		
Repairs.	21000		
Legal expenses.	5000		
Depreciation	15000		
Bonus	6000		
Bonus to proprietor	4000		

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Car Purchased.	72000		
Expenses on car during the year	12000		
Donation	2000		
Provision for bad debts	6000		
Net Profit.	90000		
	4,31,000		4,31,000

From the examination of books of accounts, the following other information are available.

a) Advertisement expenses were spent on insertion in newspapers.
b) Rs 3000 was spent on Purchase of land and is included in legal expenses.
c) Half of the repair expenses were on let-out building.
d) Depreciation allowable on all assets including car is Rs. 14,400.
e) Bonus was paid to employees on 30.6.25 and due date of filling of returns is 31.7.2025.

Solution:

Computation of Business Income of Manufacturer. for the Previous year 2024-25

Particulars	Rs	Rs.
Net Profit		
Add: Inadmissable deduction / Expenses		
Advertisement expenses exceeding Rs 10,000 Paid in cash (disallowed upto 100%)	24,000	
Drawings by Proprietor	24,000	
Interest on Capital	7000	
Depreciation	15000	
Bonus to proprietor	4000	
Cost of car being capital expenditure	72000	
Provision for bad debts	6000	

Legal expenses incurred on Purchase		
Of Land being capital expenditure.	3000	
Repairs expenses on let-out building (1/2 x 2500)	1250	
Donation	2000	1,58,250
		2,48,250
Less: Allowable depreciation	14,400	
Less: Income to be shown under other heads:		
Interest on securities	14000	
Income from House Property	25000	53,400
Business Income		1,94,850

Computation of Income from Profession.

Problem: 6. [Legal Profession].

Kumar a lawyer by profession keeps his cash book as per cash system of accounting. The following is the summary of his cash book for the year ended 31.3.2025.

Particulars	Rs	Particulars	Rs.
To Balance	5000	By Rent of Chamber	2400
To Fees	35000	By car expenses	3600
To Remuneration as examiner.	3000	By Household expenses	12000
To Interest on bank deposit	2500	By Local taxes for the house	1200
To Rent from House property	8000	By Repairs of the house	4000
To Dividend	1600	By LIC Premium for self	4600
		By cost of Books for Profession	4000
		By Medical treatment of self	5000
		By Balance	18100
	55100		55100

Additional Information.

(a) 1/3 of the house is used by Kumar for his own residence

b) Kumar is insured for Rs 40,000

c) Kumar has to get medical treatment for an eye ailment caused by intensive study of law books.

d) ½ of the car expenses relate to personal use of the car by Kumar,

Depreciation computed at the prescribed rate on the written down value of the car is Rs 2000.

Compute his income from Profession.

Solution:

Computation of Income from Profession of Mr. Kumar. for the Assessment year 2025-26.

Particulars	Rs	Rs.
Professional receipts:		
Fees	35000	
Remuneration as examiner.	3000	
		38000
Less: Expenses in connection with Profession		
Rent of Chamber	2400	
½ of the expenses of Car	1800	
Cost of Depreciation books for Profession $4,000 \times \frac{40}{100}$	1600	
Depreciation of the car $(2000 \times \frac{1}{2})$	1000	6,800
Income From Profession		31,200

Problem 7:

Medical Profession:

The following is the receipts and payment accounts of a medical practitioner for the year ending 31. 2025.

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Receipts	Rs	Payments	Rs
Balance b/d	1,10,000	Clinic rent	15000
Visiting fees	65,000	Staff Salaries	80000
Consultation fees	65000	Rent and taxes	5000
Sales of medicines	25,000	Electricity and water	4000
Operation theatre rent	15,000	Purchase of medical books	4000
Interest and dividends.	20,000	Purchase of surgical equip.	30,000
		Motor car expenses	15000
		Medical association membership fees	5000
		Audit fees	20,000
		Staff welfare expns	2,000
		Diwali expenses	1,000
		Entertainment expenses	6,000
		Medical Purchased	30000
		Balance C/F	83000.
	3,00,000		3,00,000

Addition information:

1. A cash payment of Rs 5000 was given to him by a Patient in appreciation of his medical service but was not accounted for in the books of accounts.

2. One third of Motor Car expenses relate to his Personal use. Depreciation on motor car allowable under the Income Tax Act was Rs 6000 for Personal use.

3) Audit fees include Income Tax appeal expenses Rs 15000.

4) Depreciation Computed at the prescribed rate on Surgical equipment is Rs 10,000

5) Interest and dividend include : a) Interest on Bank deposit 4000 b) Dividend from U.T.I 4000. c) Interest on National Deposit scheme 5000. d) Divident from Indian Companies 7000.

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6) His taxable Income from House Property (was Rs 5,00,000)

Compute his net income from Profession for A.Y 2025-2[6]

Solution:

Computation of Income from Profession of Medical Practioner for the A.Y 2025-26.

Particulars	Rs	Rs.
Income From Profession:		
Visiting fees.	65000	
Consultation fees	65000	
Sale of Medicines	25000	
Operation Theatre rent	15000	
Cash receipt from a patient	5000	1,75000
Less: Expenses in connection with Profession:		
Clinic rent	15000	
Staff Salaries	80000	
Rent and Taxes	5000	
Electricity and water	4000	
Depreciation on medical Books ($4000 \times \frac{40}{100}$)	1600	
Medical association membership fees	5000	
Audit fees	20000	
Staff welfare expenses	2000	
Diwali expenses	1000	
Entertainment expenses	8000	
Depreciation on Surgical equipment	10000	
Motor car expenses ($15000 \times \frac{2}{3}$)	10000.	1,95600
Income from Profession.		(-) 20600