Tax Wire

Update on Section 44AD & Section 44ADA of Income Tax Act, 1961

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Update on Section 44ADA of Income Tax Act, 1961.

Dear Readers,

This communication is to apprise you of some amendment that has happened to Income Tax act relating to professional starting FY 2016-17. The amendment will apply to taxpayers engaged in specified profession like:

1) Legal 2) Medical 3) Engineering or architectural 4) Accountancy 5) Technical consultancy 6) Interior decoration 7) Any other profession as notified by tax board in future

The new provision requires that professionals having a gross professional receipts of Rs.50 lakhs and below will have to pay tax under presumptive basis by estimating their income to be 50% of their gross receipts. An example for this is as under:

Computation of income under Presumptive Taxation Scheme for Professionals	
Example: If the Gross receipts of the profession for the FY 2016-17 is Rs. 20,00,000.	
Mode of computation:	
Profit at 50% of Rs. 20,00,000	Rs. 10,00,000
Tax there on (Normal Slab rates)	**Rs. 128,750**

Audit of the accounts

In order to avoid the above situation, it is required that such professionals maintain books of accounts and get such books audited by a Chartered Accountant. Some of the basic steps for getting the accounts audited are:

a) Maintenance of books of account like, Cash Book, Bank Book, General Ledger, vouchers, bills and other necessary documents.

b) Should not made cash payments more than Rs. 20,000

c) Should not accept loans/advances exceeding Rs. 20,000 in cash.

d) Should not repay loans/advances exceeding Rs. 20,000 in cash.

e) Maintain invoices towards professional receipts or such documents to support the professional receipts

If the above are maintained, the books of accounts can be audited and the actual profit even when it is less than 50% can be declared as income for the purpose of taxation.

Consistency in approach

Another important change that has happened is that, once a professional adopts to compute income at 50% of receipts for a year, such professional has to adopt the same scheme for next 5 years, or else such benefit of presumptive taxation cannot be claimed for 5 years subsequent years. Once an option to get the accounts audited is chosen, such professional looses the option to pay tax on income at 50% for next 5 years.

Hence it is advisable to adopt a proper strategy in FY 2016-17 based on state of affairs of the tax payer.

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Update on Section 44AD of Income Tax Act, 1961.

This communication is in order to appraise you of a change that has been carried out regarding computing income and tax of Partnership Firms, which are not liable for getting their account audited mandatorily. These changes are applicable for FY 2016-17 and onwards.

1. Computation of Income and Tax

Prior to FY 2016-17		From FY 2016-17 onwards	
Example: If the turnover/sales of the firm for the FY 2015-16 is Rs. 50,00,000.		**Example:** If the turnover/sales of the firm for the FY 2016-17 onwards is Rs. 50,00,000.	
Mode of computation:		**Mode of computation:**	
Profit at 8% of Rs. 50,00,000	Rs. 4,00,000	Profit at 8% of Rs. 50,00,000	Rs. 4,00,000
Less: a) Remuneration allowable	Rs. 3,30,000	Less: a) Remuneration allowable	-
b) Interest on Capital, say	Rs. 60,000	b) Interest on Capital, say	-
Net profit of the firm	Rs. 10,000	Net profit of the firm	Rs. 4,00,000
Tax there on (30% + 3% cess)	**Rs. 3,090**	Tax there on (30% + 3% cess)	**Rs. 1,23,600**
Before the amendment in Finance Act, 2016, the tax payer being the Partnership firm ***was allowed to claim separate deduction*** from the net income for ***remuneration and interest*** paid to its partners. Hence tax liability was less.		After the amendment in Finance Act, 2016, the tax payer being the Partnership firm ***is not allowed to claim separate deduction*** from the net income for ***remuneration and interest*** paid to its partners. Hence tax liability will increase.	

Since no remuneration is allowable as a deduction while computing the Firm's income, remuneration will not be taxable in the hands of the Partners.

2. Audit of the accounts

In order to avoid the above situation, it is required that such Firms maintain books of accounts and get such books audited by a Chartered Accountant. Some of the basic steps for getting the accounts audited are:

f) Maintenance of books of account like, Cash Book, Bank Book, Purchase Register, Sales Register, General Ledger, vouchers, bills and other necessary documents.

g) Should not made cash payments more than Rs. 20,000

h) Should not accept loans/advances exceeding Rs. 20,000 in cash.

i) Should not repay loans/advances exceeding Rs. 20,000 in cash.

j) TDS has to be deducted wherever necessary.

k) Maintain invoices towards sales and necessary supporting documents towards sales

If the above are maintained, the books of accounts can be audited and the actual profit after deducting remuneration and interest on capital can be declared as income of the Firm.

3. Consistency in approach

Another important change that has happened is that, once a Firm adopts to compute income at 8% of turnover for a year, such Firm has to adopt the same scheme for next 5 years, or else such benefit of presumptive taxation cannot be claimed for 5 years subsequent years. Once an option to get the accounts audited is chosen, such Firm looses the option to pay tax on income at 8% for next 5 years.

Hence it is advisable to adopt a proper strategy in FY 2016-17 based on state of affairs of the tax payer.

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