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INTERNATIONAL JOURNAL OF LAW MANAGEMENT & HUMANITIES

[ISSN 2581-5369]

Volume 4 | Issue 2

2021

Tax Planning with Respect to Business and Profession

REVA GUPTA[1]

ABSTRACT

Tax planning entails devising and executing different methods to reduce the amount of taxes owed over a given time span. Minimizing a small business's tax liability will free up funds for expenditures, investment, or development. Tax planning may thus serve as a source of working capital. There are a few general tax preparation areas that extend to all types of small businesses. The selection of accounting and inventory-valuation approaches, the scheduling of equipment acquisitions, the distribution of business profits among family members, and the selection of tax-favoured benefit plans and investments are all examples of these fields.

I. INTRODUCTION

If we discuss the definition of tax planning, it is a practise undertaken by a tax payer in order to reduce his or her tax liability by making the best use of all available exemptions, deductions, and other provisions that are permissible and feasible under the income tax act or taxation law. Essentially, it is the examination of a financial situation from a taxation standpoint.

Tax planning ensures that all aspects of the financial plan work together to achieve optimum tax performance. If we look at our Indian taxation law, we can see that it provides a number of choices for taxpayers, including a variety of exemptions and deductions that can help you reduce your total tax liability. The numerous deductions available to tax payers range from Sections 80C to 80U, and any qualifying tax payer may take advantage of them. Other methods for limiting liability exist as well. There are also other provisions of the Income Tax Act of 1961, such as deductions and tax credits, that will help you lower your tax bill. Let us see how the tax planning is done under the head “Business and Profession”.

In general, there are a number of areas where tax planning can be beneficial. There are a few aspects of general tax planning that apply to all small businesses. Some examples of general tax preparation techniques are as follows:

[1] Author is a student at Symbiosis Law School, Noida, India.

II. Application of accounting rules

When the income is being earned by the assessee under the head , it is calculated on the basis of the assessee's accounting form of choice on a regular basis. If the mercantile system of accounting is being adopted by the assessee, then admissible expenses and income which is calculated on accrual basis are eligible for deduction on accrual basis. If he adopts the cash system, then income is calculated on receipt basis, and admissible expenses are allowed to be deducted only when they are on the basis of payment.

Inventory Valuation Methods:

Inventory valuation is important because businesses must reduce the amount they deduct for inventory acquisitions over the course of a year by the amount of inventory remaining at the end of the year.

Equipment Purchases:

Small companies will benefit from this tax cut as well, as it will increase their deductions for business expenses, decrease their taxable income, and reduce their tax liability. Purchases of required equipment up to the limit can be made at the end of the year and are still completely deductible.

Employee Benefits and Investments:

Payroll planning also applies to a range of employee benefits, such as contributions to life, fitness, and retirement programmes, that can provide a company with tax deductions. In addition, many of these insurance programmes are not taxable benefits for employees.

III. Tax planning for various business structures

The first step in tax planning-at least for small business owners and professionals-is to select the right form of organisation for your enterprise. Many aspects of tax planning are specific to certain types of businesses. Some of these are discussed in greater detail further down.

Proprietorships and Partnerships:

Tax planning for proprietorships and partnerships is similar to personal tax planning in several ways. Small business owners file an informational return with the Internal Revenue Service on behalf of their company, and then record any money taken from the entities for personal use on their personal tax return.. Because sole proprietorships and partnerships do not expect to be paid a regular salary, they are not allowed to withhold income taxes for themselves. It's critical that the tax paid in quarterly instalments equals either the total amount owed for the quarter or the total amount owed for the year.90 percent of their previous year's total current tax liability The IRS will charge you interest and a stiff penalty if you don't pay your estimated taxes on time. Making a large lump-sum payment in the fourth quarter does not shield a taxpayer from fines because the IRS calculates the amount owed on a quarterly basis. A large increase in withholding in the fourth quarter, on the other hand, can be advantageous, since tax withheld by an employer is considered to be charged equally over the year, regardless of when it was withheld. For a self-employed person who is behind on their expected tax payments, this could lead to a tax planning plan.

C Corporations:

Corporate tax preparation differs significantly from that of sole proprietorships. This is due to the fact that profits gained by C companies are accumulated rather than the individual owners or shareholders, to the company. A company is a legal entity that exists for the purpose and Under the statute, it is a separate, taxable entity, and various corporate tax rates apply depending on its size. The total sum of money earned as a result of your efforts. Personal service businesses, such as medical and legal practises, pay a 35 percent of premium. Corporations can be subject to a variety of special taxes in addition to the general corporate tax. Corporations must file an annual corporate tax return on a calendar-year basis or a fiscal-year basis

S Corporations:

Instead of paying dividends, Sub-Chapter S corporations avoid double taxation by handing on their income (or losses) to shareholders directly. Experts say that for tax purposes, starting a new business as a S corporation rather than a C corporation is often preferable. It is normal for a company to lose money for the first year or more after it is established. Individual owners, on the other hand, often sell assets and cash out investments to collect the funds needed to start a business. S corporate shareholders/employees are only required to pay FICA taxes on salary income; they are not required to pay FICA taxes on dividends or profits held in the corporation. It's worth noting, however, that the IRS can question unreasonably low salaries.

IV. Tax planning strategies to support salaried people in lowering their taxes

Salaried people of our country are mostly unaware of the tax planning process, which is why they rush to spend at the end of the tax planning season in order to reduce their tax liability. As a result, their tax burden increases, and they end up paying more taxes than they should.

Make the most of your Section 80C deduction:

Section 80C allows for a maximum reduction of 1 lakh and salaried residents with a gross income of two lakh fifty thousand or more are eligible to use the entire one lakh cap. Individuals who invest more than one lakh in Section 80C in specific areas fail to realise that the benefits are minimal.

Beyond Section 80C deductions, there are other ways to reduce the tax liability.

If your income exceeds two lakh fifty thousand a year and the Section 80C deductions aren't enough to reduce your overall tax liability, consider the following:

- Home loan: Under Section 24, interest rates of up to one lakh fifty thousand per year are eligible for a reduction.
- Medical insurance: This qualifies for a deduction of up to one lakh fifty thousand per year under section 80D.
- Donations: Donations to specific funds/institutions are eligible for tax benefits under Section 80G.

Assert tax benefits on house rent charged:

If HRA (House Rent Allowance) is not included in the wage framework, salaried persons can deduct rent paid for residential accommodation as an asset. This reduction is available under Section 80GG and is the smallest of the following amounts.

- Surplus of housing fee charged above 10% of total wages
- 25% of total earnings
- or two thousand a month.

Reorganize your salary:

Reorganizing your salary and adding such apparatus will help you reduce your tax burden in the long run..

Choose a blended mortgage loan:

To maximise tax benefits, a salaried person may take out a shared joint home loan with his or her parent, spouse, or sibling. All owners will be able to claim tax breaks based on the percentage of the loan they own in this manner.

V. TAX PLANNING STRATEGIES OF VARIOUS TYPES

Tax planning strategies aim to reduce a person's or a company's overall tax liability for the year while still achieving personal or business financial objectives. Comprehensive analysis and meticulous record keeping are necessary components of all forms of effective planning strategies in order to achieve these objectives. The most critical tax preparation approach is to investigate all facets of income taxes, focusing on those that are relevant to an individual's financial situation

General Principles Governing Deductions

Section 28 describes a variety of income that is subject to taxation. Section 29 allows deductions and allowances under sections 30 to 43D to be taken into account when calculating earnings from profession and business.

Before looking at the types and amounts it's better to remember the following rules that control admissibility:

1. It is the assessee's duty to demonstrate that a specific deduction is allowable in his case.

2. One must remember that, the allowances set out in sections 30 to 37 are cumulative and not alternative.

3. To be eligible for a deduction, the expense must have occurred in the previous year. The system of accounting commonly used by the assessee must be examined in order to determine if the expenditure applies to the applicable prior year or not.

4. To be eligible for a deduction, the assessee must have carried on the business for which the expenditures were incurred during the previous year.

5. Only expenditures incurred for the benefit of the assessee's own business are allowable as deductions in calculating taxable income.

6. Even if the expenditure was for the benefit of someone else, it would be allowed as a deduction if it was primarily for the benefit of the assessee's own business.

VI. Expenses which are allowed as deductions

- Rates, Rent, Taxes, Insurance, and Repairs [Section 30]
- Factory, equipment, and furniture, insurance and repairs [Section 31]
- Allowance for investment in a Notified Backward Area in Bihar, Andhra Pradesh, West Bengal, or Telangana [Section 32AD]
- Depreciation [Section 32]
- Fund for Site Restoration [Section 33ABA]

- Development Account for Rubber, Coffee, and Tea [Section 33AB]
- Expenses for acquiring the right to use spectrum for telecommunications services [Section 35ABA]
- Expenses for obtaining a telecommunications services licence [Section 35ABB]
- Deduction for Expenditure on a Specified Business [Section 35 AD]
- Payments to organisations and institutions for implementing rural development programmes [Section 35CCA]
- Payments to organisations and institutions for implementing rural development programmes [Section 35CCA]
- Agricultural Extension Project Expenditure [Section 35CCC]
- Expenditure on project for Skill Development [Section 35CCD]
- Amortisation of Expenditure under Voluntary Retirement Scheme [Section 35DDA]

List of Expenses Allowable as a Deduction from Business Income Under Section 37(1):

A few examples of expenses that are allowable under section 37(1) are given below –

1. Expenses associated with litigation in order to defend a trade or company.
2. Expenditure incurred in the interest of assessee's company for the preservation or security of the asset, or for saving such asset from loss, dissipation, or wastage.
3. Expenses incurred in order to protect or retain an established title of a business asset via litigation.
4. An assessee pays a company a royalty for using its logo.
5. Fees paid for consulting services related to software maintenance.

Deduction of Business Losses

The income tax act, 1961 provides for the losses which are deductible under the business and profession, Some of them are –

1. Stock-in-trade loss as a result of enemy action or other related circumstances.
2. Stock-in-trade loss as a result of a natural disaster.
3. Loss incurred as a result of the assessee's failure to accept delivery of goods.
4. Depreciation of funds held in a foreign country for stock-in-trade purchases.
5. Loss of security deposit for the purpose of stock-in-trade acquisition.

Section 35 AD

Section 35AD of the Income Tax Act provides that the deduction is available for any capital expenditure incurred solely and exclusively for the purpose of carrying on a specified business. Notably, the section 35AD deduction does not apply to expenses incurred for the purchase of property, goodwill or financial instrument.

VII. CONCLUSION

Tax preparation, as opposed to tax compliance or reporting, is a forward-looking practise that reflects on past events. For professional advice in this complex field, corporations usually hire certified public accountants or tax attorneys. Essentially, corporate tax planning refers to techniques for lowering taxes. Tax preparation and management is a dangerous and difficult task. Dealing with taxes in an efficient and reliable manner is a top priority. There is a clear need for excellent corporate tax planning that will help to ensure a smooth flow. One of the most important aspects of corporate tax planning is deciding which nations, states, and cities have the authority to tax business activities. Since each sovereign government has its own set of taxation laws, jurisdictional arbitrage will result in tax cost differences. Identifying the best period to recognise an item of income or cost is a common source of corporate tax planning opportunities. Due to the time value of money, deferring income recognition to a future period or accelerating cost deductions to the current period results in positive cash flows and savings. Exploiting the gaps in rules for book accounting and tax accounting in a strategic way may help establish timing differences that result in tax benefits. India's corporate tax rate is comparable to that of other countries around the world. The corporate tax rate in India is determined by the company's location. If the company is headquartered in India, the tax rate is 30 percent. The tax rate for a foreign corporation, on the other hand, is determined by a number of other factors and considerations. Tax is paid on global income for Indian-domiciled firms, while tax is charged on income earned within Indian territory for foreign-domiciled companies. Benefit from capital assets in India, interest received, income from the selling of the company's equity shares, royalties, dividends earned, and so on are all taxable for foreign companies.

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