

## **Business Income - Basics**

Lahiru Karunaratna

### **What is a Business? (Section 195)**

Business includes;

- A trade, profession, vocation or isolated agreement with a business character. However, short the duration of the agreement. and
- A past, present or prospective business

Trade

Definition of trade is not provided in the act. Hence below needs to be considered.

- Purchase of articles more than required for the person.
- Articles are held for a short period.
- Transactions are repetitive.
- Motive of profit.

Lahiru Karunaratna

## What is a Business Income?

Gains or profit from conducting business during the period (Section 6.1)

### What is included in Business Income? (Section 6.2)

- Service Fees.
- Consideration received in respect of trading stock.
- Gain from realization of capital assets and liabilities.
- Realization of depreciable assets.
- Amount received for restriction of business.
- Gifts received in respect of business.
- Other amounts.

## Computation of Business Income

Generally computation of business income starts from the accounting profit.

### Adjustments to Accounting Profit

Expenses that are not deductible for tax purpose but deducted for accounting

**Add Back**

Expenses that are deductible for tax purpose but not deducted in accounts.

**Deduct**

Income that are taxable but not included in the accounting profit.

**Add Back**

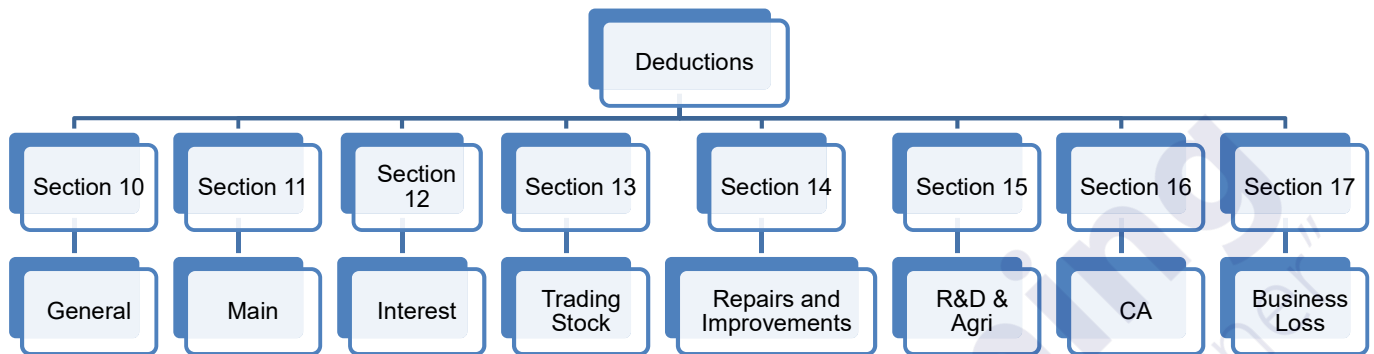
Income that are included in the accounting profit but are not taxable.

**Deduct**

## Exclusions (Section 6.3)

- Exempt amounts and final WHT payments.
- Gains and profits from employment.

## Deductions (Division iv)



## General Deductions (Section 10)

- The followings can not be deducted when calculating a person's income. (Section 10.1.b)
  - Domestic expenses (Section 197).
  - Tax payable under Inland Revenue Act.
  - Interest, penalties and fines payable for breach of law.
  - Expenses incurred for exempt amounts or for final WHT payments.
  - Dividends of a company.
  - Entertainment expenses.
  - Provisions and un-occurred expenses.
  - Taxes and other levies specified by CGIR.
- Where more than one deduction rule applies most specific deduction rule will apply (Section 10.4)

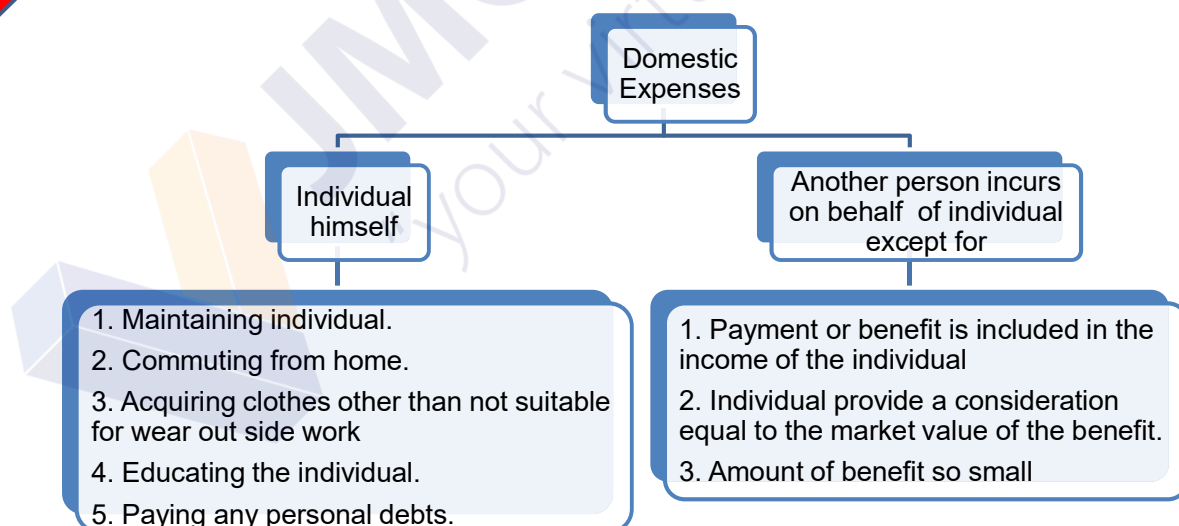
## General Deductions (Section 10)

- Taxes that are treated as disallowable expenses are as follows.
  - Income Tax.
  - Economic Service Charge (ESC).
  - VAT on Financial Services.
  - Crop Insurance Levy.
  - Super Gains Tax.
  - Bar and Taverns Levy.
  - Casino Industry Levy.
  - Mobile Telephone Operator Levy.
  - Satellite Location Levy.
  - Dedicated Sports Channel Levy.
  - Mansion Tax.

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## Domestic Expenses (Section 197)



Any interest on borrowings for any of the above is also considered as domestic expenditure

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## Main Deduction (Section 11)

- When calculating the income from business or investment, expenses that incurred in production of income and incurred during the year of assessment can be deducted (Section 11.1).
- Capital nature expenses are not allowed under above (Section 11.2).

## Allowance for Trading Stock (Section 13)

- Allowance for trading stock = Opening stock + expenses incurred during the year of assessment – Closing stock (Section 13.2).
- Opening value of the stock should be the closing balance of the previous year of assessment (Section 13.3).
- Closing value of the stock should be lower of;
  - Cost of trading stock as of the end of the year or,
  - Market as of the end of the year (Section 13.4).

## Capital Allowances and Balancing Allowances (Section 16)

### What is a depreciable asset?

An asset used in production of income from a business and likely to lose the value due to wear and tear and obsolescence (Section 195).

### What is depreciation basis?

Similar to written down value.

## Capital Allowances and Balancing Allowances (Section 16)

### Types of depreciable assets (Fourth Schedule)

Asset Class	Description	Number of years
1	Computers and data handling equipment	5
2	Buses, mini buses and similar heavy vehicles and plant and machinery used in manufacturing	5
3	Other vehicles, machinery and furniture	5
4	Buildings and structures	20
5	Intangible assets excluding goodwill	Actual useful life or 20

## **Capital Allowances and Balancing Allowances (Section 16)**

**No capital allowance shall be granted in respect of road vehicles other than;**

- Commercial Vehicle.
- Buses and mini Buses.
- Goods vehicles.
- Heavy general purpose or specialized truck or trailer.

**What is a commercial vehicle?**

- Road vehicles designed to carry more than half a ton or 13 passenger.
- Vehicles used in transportation or vehicle rental business.

## **Capital Allowances and Balancing Allowances (Section 16)**

**What is balancing allowance?**

If an asset is sold at an amount lesser than the written down value of the asset, that difference will be known as the balancing allowance. This will be allowed to be deducted from the business income.

**What is assessable charge?**

If an asset is sold at an amount more than the written down value of the asset, that difference will be known as the assessable charge. This will be added to the business income.

# Capital Allowances and Balancing Allowances (Section 16)

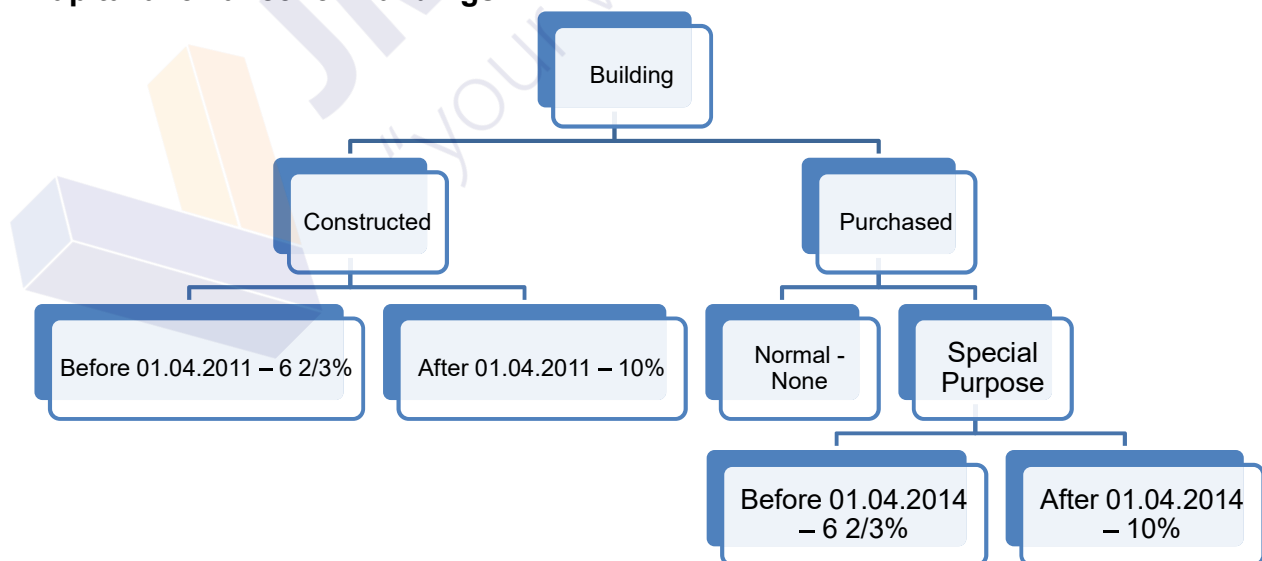
How the capital allowance is granted for the assets acquired prior to 01.04.2018?

For assets acquired prior to 01.04.2018 capital allowances are granted based on the **Inland Revenue Act No. 10 of 2006**.

- Motor vehicles not used for travelling 20%.
- Machinery 33 1/3%.
- Office furniture 20%.
- Computer Hardware 25%.
- Computer Software Locally Built 100%.
- Computer Software others 25%.

# Capital Allowances and Balancing Allowances (Section 16)

## Capital allowance for Buildings





# Capital Allowances and Balancing Allowances (Section 16)

## What are special purpose buildings?

- Unit from a condominium property.
- Previously used as an industrial building.
- Previously used as a hotel building.

## Knowledge Test 01

Given below are the assets owned by AD Enterprises as of 31.03.2020. Compute the amount of capital allowance can be deducted from business income for the year of assessment 2019/20 and balancing allowance or assessable charge if any.

Asset	Year of Purchase / Constructed	Amount Rs.	Remarks
Building constructed	2017/18	5,000,000	
Motor Car	2018/19	2,500,000	Used by the CEO
Mini Bus	2018/19	3,000,000	Used for transport office staff
Machine 1	2017/18	1,500,000	
Accounting software	2017/18	250,000	Off shelf purchased foreign software
Building purchased	2017/18	3,500,000	Used as a branch office in Kandy
Machine 2	2017/18	1,000,000	This was sold during the year for Rs. 200,000