

## **UNIT -2**

### **MAKE OR BUY DECISIONS**

When a business concern requires a product or any part or component of the product for its existing unit, it has to decide whether it should make the product or buy it from other manufacturers. Various tax considerations with respect to these decisions are:

1. If the organization has surplus capacity and even decide to buy a product it may require to sell surplus plant and machinery. In such a case it may be liable to capital gains tax.
2. If anew undertaking is established to make the product which fulfils the conditions of section 80-IB/80-IC of the Act, a deduction is allowed to such undertakings.
3. If the product is a capital asset, its cost will not be allowed as a deduction in computing the income in both cases. But in both cases, the organization can claim depreciation.

### **OWN OR LEASE DECISIONS**

Leasing is an arrangement that provides a person with the use and control over an asset, for a price payable periodically, without having title of ownership. Here the decision with respect to own the asset by paying the cash in full or leasing the product by paying periodical installments. It is an important consideration in tax planning. The assessee should follow such a method for obtaining an asset which reduces his tax liability and profits after tax are greater. For this purpose some people suggest that own funds should not be used in purchase of an asset because interest on owned fund is not deductible in computing total income, whereas interest on borrowed funds is deductible. We can invest the own fund outside the business and the interest earned will offset the interest payment of outside loan. This situation can best understand through the following illustration.

### **III. REPAIR OR REPLACE DECISIONS**

Repair of an asset is revenue expenditure whereas replacement is capital expenditure as per tax point view. If the factors other than tax were not predominant, they can select repairs as a part of tax planning. Following points should be kept in mind to reduce the tax liability while taking a decision to repair or replace an asset:

1. There are some conditions to carry-forward and set-off of business losses. Hence, if in the relevant previous year less income is expected, it will be better to slow down the pace of repair and renewal of a part of asset in such a manner that it is spread over a number of years. On the other hand, if the income is increased, the repair work can be increased.
2. As far as possible a part of the asset should be replaced and not the entire asset. In case of replacement of a part of asset, the cost of replacement is allowed as a deduction in computing the income for tax purpose

### **SHUT DOWN OR CONTINUE DECISIONS**

When a business suffers loss continuously, whatever reasons of loss may be, the management has to decide whether the business should shut down or continue. While taking this decision, the impact of Income tax provisions should not be over looked. Various tax planning considerations are:

1. If the business is discontinued, the business losses and unabsorbed depreciation still can be carry forwarded and set off against profits and gains of business or profession. (in the case of unabsorbed depreciation – set off against income under any head)
2. The benefit of deductions under section 33AB (Tea Development Account/ Coffee Development Account/ Rubber Development Account) and 115VT (Reserve for shipping business) may be withdrawn and liable to tax for the year in which business is discontinued.
3. If the business is discontinued and the assets used for scientific research and family planning are sold, the selling price to the extent of deduction claimed shall be deemed as the profits of the previous year in which such assets are sold.
4. If a person is running more than one business the loss making business should not be discontinued but operated in a minimal way so that the losses and expenses like retrenchment compensation, interest on borrowed funds, bad debts etc. adjusted with profit making units.