

Assessment of Partnership Firm

Presented by

Manikanta C M

Lecturer in Commerce

JSS College of Arts and Commerce

Gundlupet-571111

Sowmya.K

Lecturer in Commerce

JSS College of Arts and Commerce

Gundlupet-571111

Introduction

Firm is an association of two or more than two persons, who came together to do a business and share profits thereof.

Section 4 of the Partnership Act, 1932 defines Partnership as “relationship between persons who have agreed to share the profits of business carried on by all or any of them acting for all.”

Scheme of Taxation of Firms;

1. The firm is taxed as a separate entity i.e. separate from its partners. No matter whether the firm is registered or not.
2. The definition of firm includes a Limited Liability Partnership and LLP is treated same as firm.
3. The share of partners in the income of the firm is exempted, while computing his individual income or share of partners in the firm is exempted in his hand.
4. Salary, Bonus, Commission or remuneration (by whatever name called) paid /payable to partners is allowed as deduction to the firm and same will be taxable in the hand of partners. These expenses are allowed as deduction subject to certain restriction under the Income Tax Act, 1961.
5. The interest to partners paid by firm is deductible subject to maximum rate of interest @12% pa. The amount is taxable in the hand of partners.
6. The firm is taxed @30.9% or 33.99% (subject to net income of firm is Rs. 1 Crore or exceeds Rs. 1 Crore).

CONDITIONS TO BE FULFILLED BY A FIRM TO BE ASSESSED AS SUCH (PFAS);

Section 184; of the Income Tax Act, 1961 governs the taxation and assessment of Firm. A firm has to satisfy these conditions to be assessed as a firm;

Section 184(1) (i); The Firm should be evidenced by an instrument called “Partnership Deed” and;

1. It should be in writing;
2. It should not be by conduct or oral;
3. The deed may contains following clauses; Name of the Firm, Place of Business, Nature of Business, Date of Commencement of Business, Duration of Partnership(if any), Capital Clause, Profit Sharing Ratio, Remuneration payable to partners, Interest Payable to partners, Arbitration Clause(if any), drawing, power to operate bank account, method of calculation of profit and keeping of books of accounts, management of business, duties of partners, valuation of goodwill , increase of capital of partners, removal or inclusion of partners and some other clauses as agreed among the partners.

CLAIMING DEDUCTION OF REMUNERATION PAID TO PARTNERS;

Section 40(b); claiming deduction of remuneration to partners;

1. Remuneration should be payable to working partners;
2. Remuneration must be authorized by Partnership deed;
3. Remuneration should not pertain to period prior to Partnership Deed and
4. Remuneration should not exceed permissible limited

Maximum Amount as Permitted by Section 40(b); the amount actually deductible is;

1. The remuneration amount permitted by section 40(b) or
2. The amount of remuneration paid or payable to partners as debited to profit and loss account, whichever is lower.

Book Profit	Amount deductible under Section 40(b)
If book profit is negative	Rs. 1,50,000
In case of profit -on first 3 lakhs of book profit -on balance of book profit	Rs. 1,50,000 or 90% of book profit whichever is more 60% of book profit

BOOK PROFIT; – How to calculate;

1. First we have to calculate the net profit or take net profit from profit and loss account;
2. Make adjustments (that is required to convert the net profit of profit and loss account into taxable business income shall be applied) as provided by Sections 28 to 44DB.
3. Add remuneration paid to partners if debited to the profit and loss account.

CLAIMING DEDUCTION OF INTEREST PAID/PAYABLE TO PARTNERS

- The interest to partners will be deductible after complying provisions of Section 184 and 40(b) of the Income Tax Act, 1961.
- Section 40(b); following conditions should be complied;
 1. Payment of interest should be authorized by Partnership Deed;
 2. Payment of interest should pertain to the period after Partnership Deed;
 3. Rate of interest should not exceed @12pa.

CARRY FORWARD AND SET OFF OF LOSS IN CASE OF CHANGE IN THE CONSTITUTION OF FIRM;

Section 78 contains provisions relating to carry forward and set off of loss in case of change in constitution of a partnership firm due to death or retirement of a partner (i.e. when a partner goes out of firm by retirement or death). In such a case, the share of loss attributable to the outgoing partner cannot be carried forward by the firm. Restriction of section 78 is applicable only in case of loss and is not applicable in case of adjustment of unabsorbed depreciation, unabsorbed capital expenditure on scientific research or family planning expenditure.

CALCULATION OF TAX;

1. First find out incomes under various heads;
2. Adjustment of losses of Current as well as earlier years according to provisions of Sections 70 to 78 of the Income Tax Act, 1961. We find Gross Total Income;
3. From Gross Total Income deduct specified deductions under Chapter VIA, we find Net Income;
4. Net Income apply tax @30%
5. Add: Surcharge @10% if Net Income increase Rs. 1.0 Crore;
6. Add: Education cess and Special Education cess;
7. Deduct rebate if any under Sections 86,90,90A and 91;
8. Add: Interest payable if any;
9. Deduct : Advance Tax paid/TDS deducted if any;
10. Balance will be amount of tax to be paid

Thank You