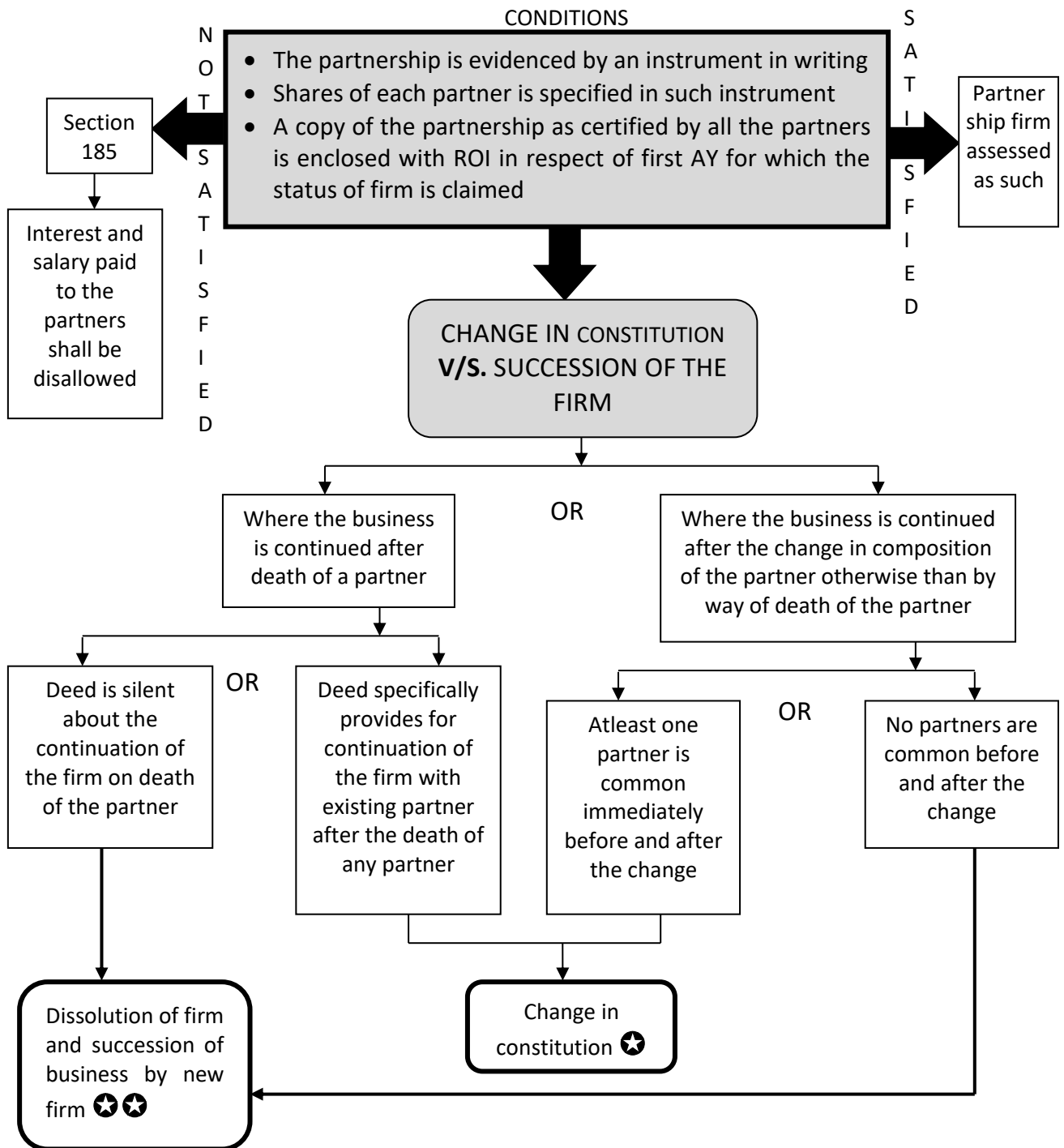


# Assessment of Various Entities

## Partnerships





## 1 LIABILITIES OF PARTNERS:

### ★ Change in constitution: Section 188A:

Every person who was a partner of the firm during the relevant PY and the legal representative of any such person who is deceased shall be jointly and severally liable along with the firm in respect of sum payable by the firm.

### ★★ Dissolution of firm: Section 189:

All persons who were partners, together with the legal heirs of any deceased partner, during the previous year when dissolution took place, shall be jointly and severally liable in respect of any sum payable by the firm.

## 2 VALUATION OF CLOSING STOCK:

### ★ Change in constitution AND ★★ Dissolution of firm:

ICDS II mentions about valuation of inventory at market/net realizable value, whether or not business is discontinued.

## 3 DISTRIBUTION OF CAPITAL ASSET BY THE FIRM TO ITS PARTNERS:

### ★ Change in constitution AND ★★ Dissolution of firm:

Section 45(4):

- Distribution of capital asset
- By the firm to its partners
- On account of dissolution of the firm or otherwise (the term otherwise shall include change in constitution also)
- Shall be chargeable to capital gains in the hands of firm
- In the PY in which the capital asset is distributed.
- Full value of consideration = Fair market value as on the date of transfer.

## Section 40(b): Interest

**Section 40(b): When interest paid to partners can be disallowed?** Notwithstanding anything to the contrary in section 30 to 38, in the case of any firm assessable as such, the following amount shall not be deducted in computing the income chargeable U/H PGBP.

(i)	any payment of interest to any partner, which is not authorized by, or is not in accordance with, the terms of the partnership deed; or
(ii)	any payment of interest to any partner, which is authorized by, and is in accordance with, the terms of the partnership deed, but which relates to any period falling prior to the date of such partnership deed;
(iii)	any payment of interest to any partner which is authorized by, and is in accordance with, the terms of the partnership deed, and relates to any period falling after the

	date of such partnership deed in so far as such amount exceeds the amount calculated or at the rate of 12% simple interest p.a.;
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**Explanation 1 to Section 40(b): Partner in representative capacity – Interest received in individual capacity – not covered:** Where an individual is a partner in a firm on behalf of any other person (that is, partner in a representative capacity), -

(i)	interest paid by the firm to such individual otherwise than as partner in a representative capacity, shall not be taken into account for the purposes of this clause;
(ii)	interest paid by the firm to such individual as partner in a representative capacity and interest paid by the firm to the person so represented shall be taken into account for the purposes of this clause.

Eg: Mr. Pravin, the karta, is a partner in a representative capacity of ABC & Co. the firm has paid interest at 18% p.a. on the following loan taken by it:

- a. Loan given by Pravin HUF of Rs. 25 lakhs which is authorized by the partnership deed.
- b. Loan given by Mr. Pravin in his individual capacity of Rs. 10 lakhs.

In case of the loan given by Pravin HUF the provision of section 40(b) shall apply and hence Rs. 1,50,000 shall be disallowed.

However, the entire interest paid on loan given by Mr. Pravin shall be allowed as deduction as per explanation 1 to section 40(b).

**Explanation 2 to Section 40(b): Partner in Individual capacity – interest received in representative capacity – not covered:** Where an individual is a partner in a firm otherwise than as partner in a representative capacity, interest paid by the firm to such individual shall not be taken into account for the purposes of this clause, if such interest is received by him on behalf of any other person.

**It is pertinent to note that . . .**

- The conditions laid down u/s 40(b) applies in all cases whether the interest is paid to partners on capital/ current/ loan account.
- Interest paid to a non working partner can be allowed as deduction.
- Compliance with section 40(b) alone is not sufficient for getting deduction in respect of interest paid to partners. Where the loan taken from the partner is not applied towards the business of the firm, the interest expenditure shall not be allowed as deduction in view of conditions laid down u/s 36(1)(iii).
- Similarly if the loan taken from the partner is applied by the firm towards a source which results into an exempt income then the interest expenditure shall be hit by section 14A and disallowed.

Section 40(b): Remuneration

**Section 40(b): When remuneration paid to partners can be disallowed:** Notwithstanding anything to the contrary in section 30 to 38, in the case of any firm assessable as such, the following amount shall not be deducted in computing the income chargeable U/H PGBP:

(i)	any payment of salary, bonus, commission or remuneration, by whatever name called, to any partner who is not a working partner; or	
(ii)	any payment of remuneration to any partner who is a working partner which is not authorized by, or is not in accordance with, the terms of the partnership deed; or	
(iii)	any payment of remuneration to any partner who is a working partner which is authorized by, and is in accordance with, the terms of the partnership deed, but which relates to any period falling prior to the date of such partnership deed or	
(iv)	any payment of remuneration to an partner who is a working partner, which is authorized by, and is in accordance with, the terms of the partnership deed and relates to any period falling after the date of such partnership deed in so far as the amount of such payment to all the partners during the previous year exceeds the aggregate amount computed as hereunder:—	
	(a) on the first Rs. 3,00,000 of the book profit or in case of a loss	Rs. 1,50,000 or at the rate of 90% of the book-profit, whichever is <b>higher</b> ;
	(b) on the balance of the book-profit	At the rate of 60%.

**Explanation 3 to section 40(b): Meaning of book profit:** “Book-profit” means the net profit, as shown in the profit and loss account for the relevant previous year, computed in the manner laid down in Chapter IV-D as increased by the aggregate amount of the remuneration paid or payable to all the partners of the firm if such amount has been deducted while computing the net profit.

**Explanation 4 to section 40(b): Meaning of working partner:** “Working partner” means an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner.

**It is pertinent to note that . . .**

- Remuneration only to working partner is allowed as deduction.
- Any form of remuneration paid to partner in whichever capacity (individual or representative) shall be covered within the ambit of section 40(b).

## Association of Persons (AOPs) & Body of Individuals (BOIs)

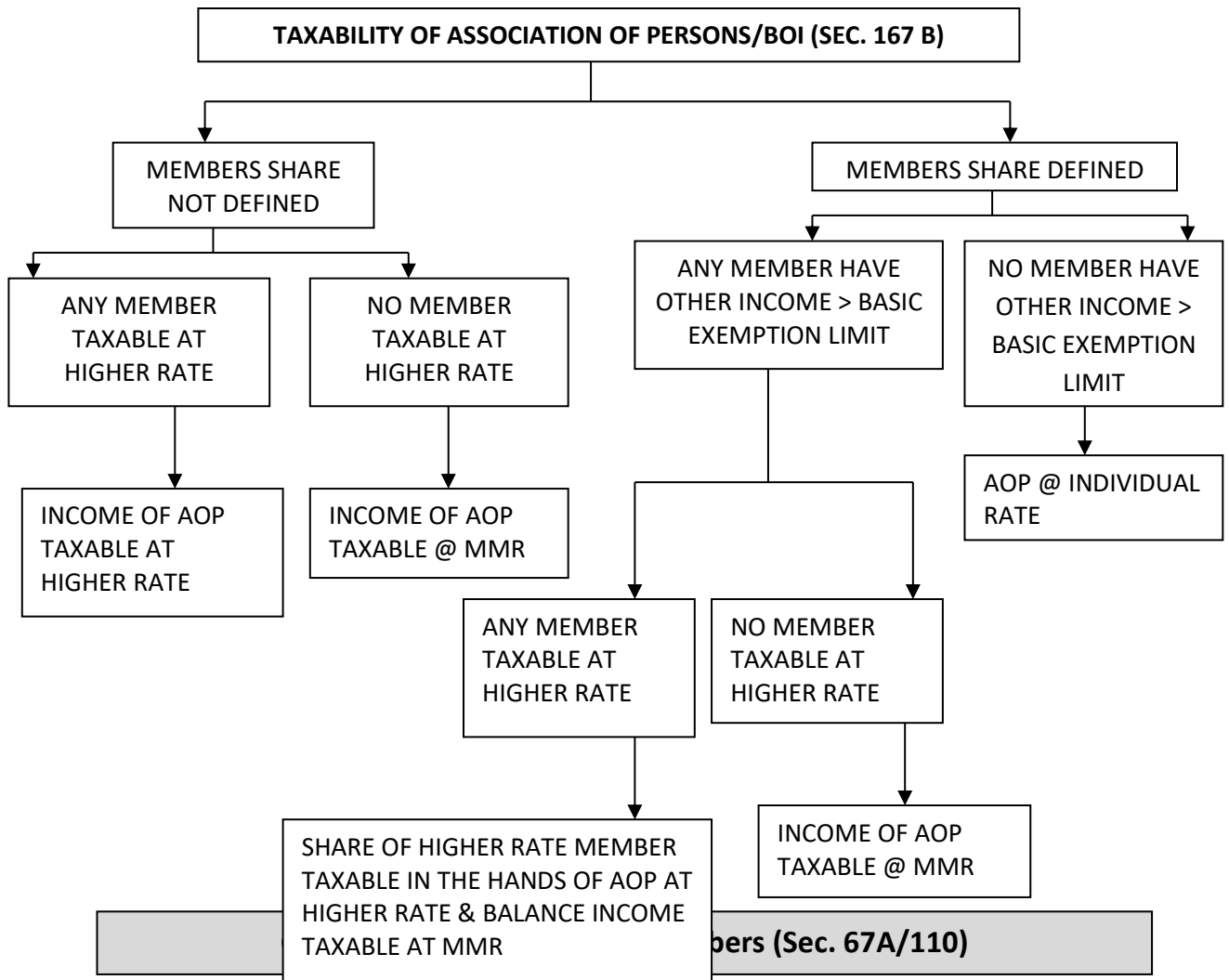
Basis	AOP	BOI
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<b>Creation</b>	Created <b>Voluntarily</b>	Created by <b>operation of law</b>
<b>Members</b>	AOP may consist Individual or Non individual	BOI consist individual only
<b>Condition</b>	AOP means two or more persons joining together for a common purpose to earn income, & <b>without</b> an intention to form a partnership	The business run by a widow on her behalf or on behalf of her children would be assessed as BOI
<b>Examples</b>	Co-Heirs, Co-Legatees or Co-Donees joining together for common purpose/action shall be chargeable as AOP.	Co-Executors, Co-Trustees are assessable as BOI

### Expenditure not deductible for AOP/BOI (Section 40(ba))

<b>Nature of Expenditure disallowed</b>	<p>(a) Interest, Salary, Bonus, Commission, Remuneration paid by an AOP/BOI to its Members is <b>not allowed</b> as deduction in computation of Income of the AOP/BOI.</p> <p>(b) If the AOP/BOI receives as well as pays interest to its members during the Previous Year, then the <b>excess</b> interest <b>paid</b> over and above the interest received shall be <b>disallowed</b>.</p>
<b>Exception</b>	<p>The above condition does not apply in the following situations—</p> <p>(a) Where an Individual is a Member on behalf of or for the benefit of any other person (Karta of HUF, Director of Company), and interest is paid by AOP to the individual otherwise than as Member in a representative capacity.</p> <p>(b) Where an Individual is a Member in his individual capacity &amp; interest is received by such individual from AOP on behalf of or for the benefit of any other person (Karta of HUF, Director of Company).</p> <p>However, provisions of Section 40A(2) may apply in such a case.</p>

# Assessment of AOP/BOI's Income (Section 167B)



(1) **If AOP taxed at MMR or Higher rate:** Share Income from the AOP/BOI shall not be included in the Total Income of the Member. Therefore, the member shall be assessable only in respect of their other income.

(2) **If AOP taxed at rate applicable for Individuals:**

**Step I: Computation of Apportionable Share of Income of AOP/BOI**

Particulars	Amount (Rs.)
Total Income of AOP/BOI	xxx
<i>Less:</i> Interest, Salary, Commission or Remuneration paid to Member	(xxx)
<b>Balance apportionable among the members of AOP/BOI (in their agreed Ratio)</b>	<b>xxxx</b>

### Step II: Computation of income of Member of AOP/BOI

Particulars	Amount (Rs.)
Apportionable Share of Income of a Member as computed above	xxxx
Add: Interest, Salary, Commission or Remuneration received from AOP/BOI by the member	xxx
<b>TOTAL</b>	xxxx
Less : Interest Paid/incurred on Loan taken for investment in AOP/BOI	(xxx)
<b>Income of member from AOP/BOI</b>	<b>xxxx</b>

**Note:** Where the Total Income of an AOP/BOI consists of Income under various heads of income, the income of member shall also be apportioned under the respective heads.

### Step III: Taxability of Share income from AOP/BOI:

- A. Include the **Share Income** from the AOP/BOI in the hands of the Members, & Total Income shall be computed accordingly.
- B. Compute the **Tax Payable** on the above Total Income.
- C. Compute **average rate of tax** = Tax on total income(Step B)/Total Income (Step A)
- D. **Tax Rebate** for Share Income of AOP = Share Income of AOP x Avg rate of Tax (Step C) **(Section 110)**
- E. **Tax Payable** by the Member = Step B **Less** Step D

## Co-operative Societies

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- (i) **General provisions:** The expression “co-operative society” means a society registered under the Cooperative Societies Act, 1912 or under any other law for the time being in force in any State for the registration of co-operative societies [Section 2(19)]. For purposes of taxation, it is treated as a separate assessable entity. The profits of any business of insurance carried on by a co-operative society are to be computed in accordance with the rules set out in the First Schedule to the Act. Apart from this, the computation of income in the case of a co-operative society should also be made in the same way under each head of income as in the case of any other assessee. Entrance fees received by a co-operative society from its members is taxable as its income from business irrespective of the nature of the business carried on by the society as was held in *Co-operative Central Bank vs. C.I.T. (1965) 57 ITR 579*.

A member of a co-operative society to whom a building or a part thereof is allotted or leased under a house building scheme of the society must be deemed to be the owner of that building or part thereof under section 27(iii). Accordingly, the co-operative society is not liable to

pay tax in respect of the income from the house property even though it may be the real owner according to official records and the tenant may have taken the building on lease. But where the tenant is not a member of the society or where the house is allotted to him otherwise than under a house building scheme of the society, the society will be liable to tax in respect of the income of the house property.

**(ii) Exemptions:** Section 80P provides certain exemptions to co-operative societies. However, the exemption is not available to co-operative banks, other than primary agricultural credit societies and primary co-operative agricultural and rural development banks. Students may refer to the detailed discussion of this provision in Chapter 11 “Deductions from Gross Total Income”. It may also be noted that the provisions of section 194A which require deduction of income-tax at source from interest other than interest on securities, credited or paid, do not apply to such income credited or paid—

- (i) by a co-operative society (other than a co-operative bank) to a member thereof or to any other co-operative society;
- (ii) in respect of deposits with a primary agricultural credit society or a primary credit society or a co-operative land mortgage bank or a co-operative land development bank;
- (iii) in respect of deposits (other than time deposits) with a co-operative society, other than a co-operative society or bank engaged in carrying on the business of banking.

**(iii) Option to exercise concessional rates of tax under section 115BAD:** Section 115BAA has been inserted by the Taxation Laws (Amendment) Act, 2019 to provide an option to

an existing domestic company to pay tax at concessional rate of 22%, if it does not claim incentive/exemption and deduction as provided in said section.

**I. Option to pay tax at concessional rate:** On similar lines, section 115BAD also provide an option to resident co-operative society to pay **tax @22% plus surcharge @10% plus Health and education cess @4% (effective tax rate is 25.168%)** on the total income subject to the conditions mentioned in point (II) below.

**II. Conditions to be satisfied for availing concessional rate of tax:** The following are the conditions for availing concessional rate of tax:

S. No.	Particulars												
(1)	<p><b>Certain deductions/exemptions not allowable:</b> Section 115BAD(2) provides that while computing total income, the following deductions/exemptions would not be allowed, if a co-operative society opts for concessional rate of tax under section 115BAD(1):</p> <table border="1" data-bbox="436 836 1292 1750"> <thead> <tr> <th data-bbox="436 836 676 884">Section</th> <th data-bbox="676 836 1292 884">Exemption/Deduction</th> </tr> </thead> <tbody> <tr> <td data-bbox="436 884 676 935">10AA</td> <td data-bbox="676 884 1292 935">Tax holiday for units established in SEZ</td> </tr> <tr> <td data-bbox="436 935 676 985">32(1)(iia)</td> <td data-bbox="676 935 1292 985">Additional depreciation</td> </tr> <tr> <td data-bbox="436 985 676 1116">33AB</td> <td data-bbox="676 985 1292 1116">Deduction for deposit into Tea development account, coffee development account and rubber development account</td> </tr> <tr> <td data-bbox="436 1116 676 1166">33ABA</td> <td data-bbox="676 1116 1292 1166">Site Restoration Account</td> </tr> <tr> <td data-bbox="436 1166 676 1750">35(1)(ii),(iia),(iii) or 35(2AA)</td> <td data-bbox="676 1166 1292 1750">           Deduction in respect of contribution to           <ul style="list-style-type: none"> <li>- notified approved research association/ university/college/other institutions for scientific research [Section 35(1)(ii)]</li> <li>- approved Indian company for scientific research [Section 35(1)(iia)]</li> <li>- notified approved research association/ university/college/other institutions for research in social science or statistical research [Section 35(1)(iii)]</li> <li>- An approved National laboratory/university/ IIT/ specified person for scientific research undertaken under an approved programme [Section 35(2AA)]</li> </ul> </td> </tr> </tbody> </table>	Section	Exemption/Deduction	10AA	Tax holiday for units established in SEZ	32(1)(iia)	Additional depreciation	33AB	Deduction for deposit into Tea development account, coffee development account and rubber development account	33ABA	Site Restoration Account	35(1)(ii),(iia),(iii) or 35(2AA)	Deduction in respect of contribution to <ul style="list-style-type: none"> <li>- notified approved research association/ university/college/other institutions for scientific research [Section 35(1)(ii)]</li> <li>- approved Indian company for scientific research [Section 35(1)(iia)]</li> <li>- notified approved research association/ university/college/other institutions for research in social science or statistical research [Section 35(1)(iii)]</li> <li>- An approved National laboratory/university/ IIT/ specified person for scientific research undertaken under an approved programme [Section 35(2AA)]</li> </ul>
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	35AD	Investment linked tax incentives for specified businesses
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	35CCC	Deduction in respect of expenditure incurred on notified agricultural project
	80C to 80U	Deductions under Chapter VI-A (other than under section 80JJAA).
(2)	<b>Certain losses not allowed to be set-off:</b> While computing total income, set-off of any loss carried forward or depreciation from any earlier assessment year, if such loss or depreciation is attributable to any of the deductions referred to in (1) above, would not be allowed.	
(3)	<b>Depreciation or additional depreciation:</b> Depreciation u/s 32 is to be determined in the prescribed manner. Depreciation in respect of any block of assets entitled to more than 40%, would be restricted to 40% on the written down value of such block of assets. Additional depreciation u/s 32(1)(ia), however, cannot be claimed.	
<b><u>Additional point:</u></b> In case of a co-operative society opting for section 115BAD, total income should be computed without set-off of any loss brought forward or depreciation from any earlier assessment year, where such loss or depreciation is attributable to any of the deductions listed in (1) above [Such loss and depreciation would be deemed to have been already given effect to and no further deduction for such loss or depreciation shall be allowed for any subsequent year]		

- III. **Deduction under section 80LA(1A) allowable:** In case of a person, having a Unit in the International Financial Services Centre, as referred to in section 80LA(1A), which has exercised option under this section, the deduction under the said section shall be available to such Unit subject to fulfilment of the conditions contained in that section.
- IV. **Time limit for exercise of option:** The concessional rate would be applicable only if option is exercised in the prescribed manner on or before the due date of filing return of income specified under section 139(1) for any previous year relevant to the assessment year commencing on or after A.Y. 2021-22. Once such option is exercised, it would apply to subsequent assessment years and cannot be subsequently withdrawn for the same or any other previous year.
- V. **AMT liability not attracted:** Co-operative societies exercising option u/s 115BAD are not liable to alternate minimum tax u/s 115JC.