Assessment of Firm

1. Total income should be computed under four heads of income.

2. After computing the income of the Firm under the head 'Protits and gains of business or profession' ***special deduction*** is allowed on account of *remuneration* ***to working partners and interest paid to the partner.*** However, it is subject to certain limits laid down U/s *40(b)*.

3. ***Essential Conditions of section 184*** which need to be satisfied to be assessed as Firm and to be eligible for deduction of interest, salary etc. to the partners**:**
   - **I. In the first assessment year**
     - a. Partnership is evidenced by an instrument.
     - b. The individual share of the partners are specified in that instrument.
     - c. Certified copy of partnership deed must be filed- in the case of assessment as Firm is first sought.
   - II. **In the subsequent assessment year-** Where change in the constitution of the Firm or change in the the share of the partners had taken place in the previous year, ***the Firm shall furnisha certified copy of the revised instrument of partnership alongwith the return of income.***

4. In case ***Conditions of section 184*** are not satisfied in a *particular assessment year*, although the firm will be assessed as firm, but no deduction by way of payment of interest, salary, bonus, commission or remuneration made to the partner, shall be allowed in computing the income chargeable under the head "profits and gains of business or profession" and such interest, salary, bonus, commission or remuneration shall not be chargeable to income-tax in the hands of the partner. ***Section 184 should not be relevant for LLP.***

5. ***If there is any failure under section 144 (Best Judgment Assessment)***, the Firm shall not be eligible for any deduction on account of any interest to the partners or remuneration to the working partners.

6. Share of profit which a partner receives from the firm ***(after deduction of remuneration and interest allowable)*** shall be fully exempt in the hands of the partner.
   However, ***only that part of the interest and remuneration*** which was allowed as a deduction to the firm ***shall be taxable in the hands of the partners*** in their individual assessment under the head 'profits and gains of business or profession'.

7. Remuneration due to or received by a partner shall be chargeable under the head "profits and gains of business or profession" ***(not under the head "Salaries")***.

Computation of Total Income of the Firm (including LLP)

- The firm (including LLP) will be detemlined as a separate entity.
- Deductions on account of interest and remlmeration to the partners can be claimed but it will be subject to the conditions prescribed by section *40(b)*, which are as under:

a. ***working parmer only:-*** Payment of salary, bonus, commission' or remuneration to a ***working parmer only*** shall be allowed as deduction.

b. ***Any partner:-*** Payment of ***interest to any partner*** *(No matter whether he is working or non-working partner)* will be allowed as deduction only when it is authorised by and is in accordance with partnership deed.

c. **No retrospective effect:-** Payment of remuneration, interest, although authorised by the partnership deed but ***which relates to a period prior to the date of such partnership deed***, shall not be allowed. In other words, salary cannot be claimed as deduction with retrospective date even if the partnership deed provides that it shall be given with retrospective effect.

d. **Interest payable to a partner:-** @12% or as mentioned under partnership deed, whichever is less, shall be allowed.

e. **Payment of remuneration to working partner**:- shall be allowed as a deduction to the extent provided in the partnership deed but subject to maximum of the following limits:

(*a*) on the first ₹3,00,000 of the book profit or in case of a loss	₹1,50,000 or at the rate of 90% of the book profit whichever is more
(*b*) on the balance of the book profit	at the rate of 60%

Computation of Book Profit of the Firm

First Step-Find out the net profit of the Firm as per P/L a/c under the head "profits and gains of business or profession".

Second Step- Add remuneration to all partners (whether working or non-working), if debited to the P/L a/c.

Third Step- The aggregate of Step-l and Step-2 is Book Profit.

- For the purpose of book profit ***only income under the head Business or Profession*** shall be considered.
- Incomes & Expenditures related to Heads “Income from House Property”, “Capital Gains”, “Income from other sources” shall be completely ignored for computation of book profit.
- Brought forward business loss will not be deducted for computatlon of book profit but unabsorbed depreciation brought forward from earlier years will be deducted as unabsorbed depreciation is allowable as cleductionunder section 32(2). However, for allowing unabsorbed depreciation, brought forward business loss shall have to be ***notionally allowed first from the current business income.***
- ***Permissible deductions from gross total income under sections 80C to 80U*** shall be completely ignored for computation of book profit.

CARRY FORWARD AND SET OFF OF LOSSES UNDER ANY HEAD OF INCOME

- The losses and unabsorbed depreciation of the firm can be carried forward ***by the firm only***.
- **In case of change in constitution of firm**:- Where a change has occurred in the constitution of a firm, due to retirement of a partner or death of a partner, the firm shall not be entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner as exceeds his share of profits, if any, in the firm in respect of the previous year.

In other words, treatmem in case of change in constitution of firm will be as follows:

Step 1: Find out the ***share of profit of the retiring/deceased partner*** in the year in which there is a change in the constitution due to such retirement/death.

Step 2: Find out the ***share of loss of the retiring/deceased partner in the brought forward loss of the firm.***

Step 3: Set off the share in the brought forward losses of the retiring/deceased partner from his share of the profit of the current year.

This set off of share of brought forward loss will be allowed to the extent of share of profit of such partner.

The balance loss, if any, will not be allowed to be carried forward either to such partner or to the firm. On the other hand, ***if in the current year also the share of the partner is a loss, then share of the brought forward loss alongwith the share of loss of current year will not be allowed to be set off and carried forward***.

- Where any person carrying on any business or profession has been succeeded in such capacity by another person otherwise than by inheritance, no person other than the person incurring the loss shall be entitled to have it carried forward and set off against his income.

COMPUTATION OF TOTAL INCOME OF FIRM

DETERMINATION OF RESIDENTIAL STATUS

CLASSIFICATION OF INCOMES UNDER FOUR HEADS

HOUSE PROPERTY | BUSINESS & OROFESSION | CAPITAL GAINS | OTHER SOURCES

AGGREGATE OF INCOMES

APPLICATION OF CLUBBING PROVISIONS

MAKE ADJUSTMENT ON ACCOUNT OF BROUGHT FORWARD OF LOSSES, UNABSORBED DEPRECIATION ETC.

GROSS TOTAL INCOME

DEDUCTIONS FROM GROSS TOTAL INCOME

TAXABLE TOTAL INCOME

RATE OF TAX FOR FIRMS INCLUDING L.L.P. FOR THE A. Y. 2013-14

On Total Income (exculsive of S.T.C.G. COVERED U/s 111A & L.T.C.G.)	30%+2% education cess+SHEC @ 1%
On L.T.C.G.	20%+2% education cess+SHEC @ 1%
On S.T.C.G. on sale of shares as per Section 111A	15%+2% education cess+SHEC @ 1%

Alternate Minimum Tax (AMT) on all persons other than companies (Sections 115JC to 115JF- Chapter XIIBA)

Where the ***regular income-tax payable*** for a previous year by a person (other than a company) is less -than **alternate minimum tax payable** for such previous year, the ***adjusted total income*** shall be deemed to be the total income of such person and he shall be liable to pay income-tax on such total income *at the rate of 18.5%*.

***Step* 1** -Find out the regular income-tax liability ignoring the provisions of sections 115JC to 115JF.

***Step* 2 -**Find out adjusted total income, **Adiusted total income** is net income or total income of as increased by ,
a. amount claimed as deduction undersections 80H to 80RRB (except section 80P), and
b. amount claimed as deduction under section 10AA,

If the assessee is an individual. HUF, AOP, BOI or an artificial juridical person and the adjusted total income is Rs. 20 lakh (or less), ***then the provisions of alternate minimum tax are not applicable,***

Step 3-Find out 19.055% (i.e., 18.5%+ EC+SHEC) of adjusted total income computed under ***Step 2***,

***Step* 4** -If amount computed under ***Step* 1** is equal to or more than amount determined under ***Step* 3**, then the provisions of alternate minimum tax will not be applicable, If, however, amoullt computed under ***Step* 3** is more than the regular tax liability determined under ***Step* 1**, then
a, adjusted total income determined under *Step* 2 will be deemed as total income for such previous year; and
b, 19.055% of adjusted total income will be deemed as tax liability for such previous year.

Step* 5** -The excess of the amount computed under ***Step* 3** over the amount computed under ***Step* 1** will be available ***as credit for alternate minimum tax. It can be carried forward and can be set off against regular tax liability of the next year or subsequent year (but not beyond the ***10th*** assessment year). ***No interest is payable on such credit.***

Tax credit shall be allowed to be set off for an assessment year in which the regular income-tax exceeds the alternate minimum tax to the extent of the excess of the regular income-tax over the alternate minimum tax.

***Step* 6** If provisions of alternate minimum tax are applicable, the assessee will have to obtain a report in Form No. 29C from a chartered accountant.