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Tax Flash News

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Classification of US Limited Partnership as firm or company requires examination under India-US tax treaty and applicable US Law

Executive summary

In the case of *Pabrai Investment* Fund,[1] the Mumbai Bench of the Income-tax Appellate Tribunal ('the Tribunal') examined whether a Delaware-based (USA) limited partnership should be treated as 'a firm' or 'a company' for Indian tax purposes, which would determine the applicable due date for filing its tax return and, consequently, its eligibility to carry forward short-term capital losses ('STCL').

Since the taxpayer's permanent account number ('PAN') had been allotted under the status of a firm, the Centralized Processing Centre ('CPC') processed the tax return denying the carry forward of STCL on the ground that the return was filed after the prescribed due date applicable to a firm.

The Tribunal held that *prima facie*, the taxpayer could not be treated as a firm in India as the Income-tax Act, 1961 ('the 1961 Act') refers only to firms registered in accordance with the Indian Partnership Act, 1932 or the Limited Liability Partnership Act, 2008.

[1] *Pabrai Investment Fund IV, L.P. v. ADIT* (ITA No. 637/Mum/2025)

However, the determination of the taxpayer's status additionally required examination of its identity based on its formation and tax treatment in the state of Delaware wherein it was registered and of the relevant provisions of the India-US tax treaty ('the US treaty'). It observed that a US limited partnership would qualify as a company in India only if it is treated as a body corporate or taxed as a separate entity in the USA.

The matter was remanded to the tax officer to determine the taxpayer's status in light of the above observations.

Facts of the case

The taxpayer was a limited partnership ('LP') established and registered in the state of Delaware, USA. It was registered with SEBI as a Foreign Portfolio Investor.

For FY 2017-18, the taxpayer filed its India tax return on 21 September 2018 and claimed carry forward of STCL incurred during the year.

While processing the tax return,[2] the CPC treated the taxpayer as a firm based on its PAN status and accordingly, considered the due date for filing the tax return applicable to a firm, i.e. 31 August 2018.

[2] Section 143(1)

Since the tax return was filed after the due date applicable to a firm, the CPC denied the carry forward of STCL.[3]

The taxpayer challenged the CPC's intimation before the Commissioner of Income-tax (Appeals) ('CIT(A)'), contending that, being a body corporate incorporated outside India (i.e. USA), it ought to have been regarded as a "company" under the 1961 Act. Consequently, the due date applicable to a company, i.e. 30 September 2018,[4] should have been considered. Since the tax return was filed before the prescribed timeline, the taxpayer argued that STCL should be allowed to be carried forward.

The CIT(A), however, upheld the CPC's intimation and aggrieved by the CIT(A)'s order, the taxpayer filed an appeal before the Tribunal.

Relevant provisions

As per the 1961 Act,[5] the terms "firm" and "partnership" have the meaning assigned to them in the Indian Partnership Act, 1932, and include a limited liability partnership ('LLP') as defined in the Limited Liability Partnership Act, 2008.

[3] The 1961 Act permits carry forward of tax losses for the relevant year only where the tax return for that year is filed on or before the statutory due date.
[4] The due date was further extended to 31 October 2018 for the relevant tax year
[5] Section 2(23)

The term “company” is defined to include any body corporate incorporated by or under the laws of a country outside India.[6]

The US treaty defines “person” to include a partnership, company, any other body of persons, and other taxable entity.[7] Further, the term “company” is defined to mean any body corporate or any entity treated as a company or body corporate for tax purposes.[8]

Taxpayer’s contentions

Section 1 of the Indian Partnership Act, 1932 limits the application of the statute to India and therefore cannot govern a partnership firm constituted under the laws of a foreign jurisdiction.

An Indian partnership is not a separate legal entity distinct from its partners, whereas according to the laws of Delaware state, the taxpayer, being an LP, is a separate legal entity and thus, a body corporate incorporated under the laws of a country outside India and consequently, a company.

The Information Technology Act, 2000[9] defines ‘body corporate’ to mean any company and includes a firm, sole proprietorship or other association of individuals engaged in commercial or professional activities.

The taxpayer challenged the CPC’s intimation on the ground that a debatable issue/ claim could not be disallowed by way of *prima facie* adjustment in an intimation issued by the CPC.[10]

To rebut the Revenue's argument that the taxpayer itself had filed the tax return using the form applicable to a firm, the taxpayer contended as follows:

- The taxpayer applied for PAN using the prescribed form for entities incorporated outside India and selected the status of a partnership firm, being an LP in the USA. The Income-tax Department allotted a PAN bearing the fourth character “F”, denoting the status of a firm.
- Owing to the PAN status, the system did not allow the taxpayer to file the tax return form prescribed for a company,[11] and the taxpayer was compelled to file its tax return in the form prescribed for a firm.[12]

[6] Section 2(17)(ii)
[7] Article 3(e)
[8] Article 3(f)

[9] Section 43A
[10] Under section 143(1)(a)
[11] ITR-6
[12] ITR-5

Tribunal’s decision

The Mumbai Bench of the Tribunal held that *prima facie*, the taxpayer cannot be treated as a firm in India as the 1961 Act refers only to firms registered in accordance with the Indian Partnership Act, 1932.

The Tribunal further held that the taxpayer's status as a firm or a company needs to be decided based on the detailed examination of its legal and tax status under the laws of Delaware where it was registered, which in turn, requires examination of the relevant provisions of the US treaty.

Accordingly, the matter was remanded to the tax officer to determine whether the taxpayer qualified as a company or a firm for the purposes of the 1961 Act and, consequently, whether the tax return was filed within the prescribed due date and STCL was eligible to be carried forward.

Key observations of the Tribunal included:

Entity status under the domestic laws

Under the 1961 Act, the terms “partnership”, “firm” and “LLP” derive their meaning from the domestic laws relating to partnership and LLP. Therefore, a corporate entity incorporated outside India could not be considered as a partnership firm for the purposes of the 1961 Act.

However, this proposition alone could not determine the taxpayer’s tax status, as the taxpayer’s identity based on its formation and tax treatment in the USA and its status under the US treaty needs to be examined.

Entity status under the US treaty

A limited partnership established in the USA would be treated as a “company” in India for income-tax purposes, only if it satisfied the condition of being a body corporate or any entity treated as a company/ body corporate for tax purposes.

It would be important to analyse whether the LP is taxed as an entity in the USA or whether its income is taxed in the hands of its partners.

If the LP itself is taxed as an entity, then the taxpayer may qualify as a corporate entity for the income-tax purposes in India. Conversely, if the tax is levied on the partners in respect of their share of income and not on the LP itself, the taxpayer may fail to qualify as a “company” for tax purposes in India.

CPC's action was justified

The CPC had not committed an error in treating the taxpayer as a firm while processing the tax return.

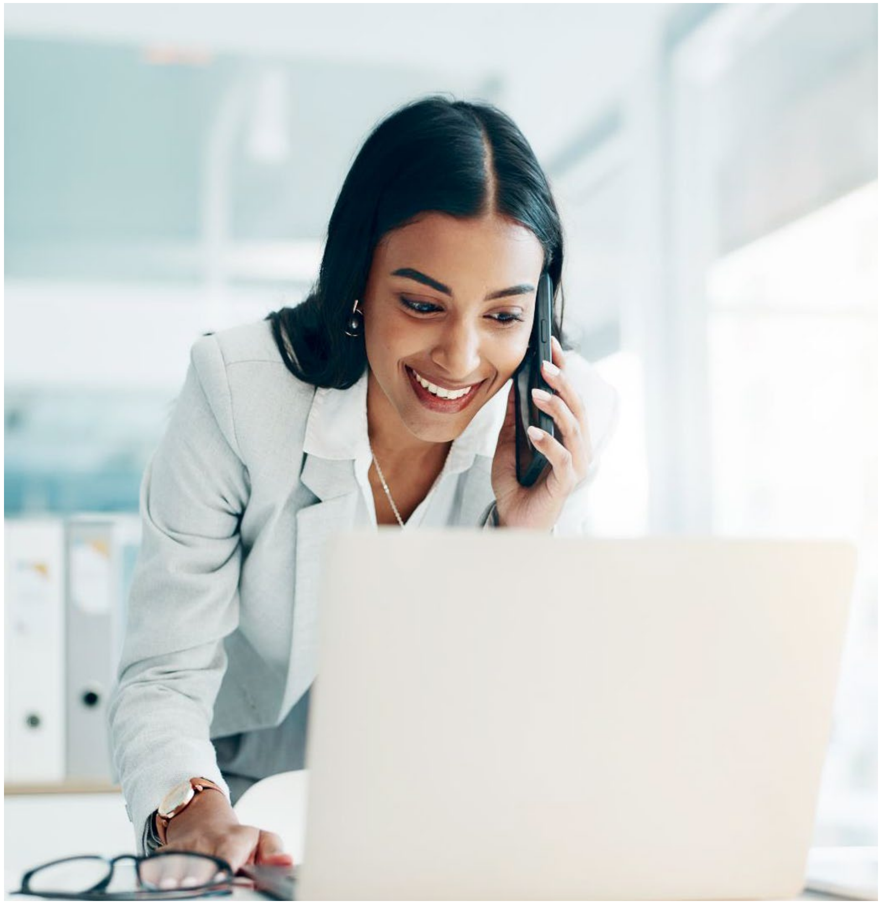
The CPC's role is limited to processing the tax return and making only those adjustments as permitted under the1961 Act.[13] Accordingly, the issue of whether the taxpayer's PAN was issued under the correct status or otherwise fell outside the scope of the CPC processing, which is a system driven mechanism.

This was particularly so considering that the status of "firm" was never disputed by the taxpayer, nor was any attempt made before the Revenue to have the same corrected.

Our comments

This is an important ruling as it provides guidance on the characterisation of foreign limited partnerships as a firm or a company for Indian tax purposes, emphasising that such determination requires an examination of their legal and fiscal characteristics under the laws of their home jurisdiction and the applicable tax treaty.

Further, the ruling reiterates that the role of CPC in processing the tax returns is confined to making adjustments expressly permitted under the 1961 Act, and question involving a determination of the taxpayer's tax status falls outside the scope of such processing.



[13] Section 143(1)(a)

KPMG in India addresses:

Ahmedabad
Commerce House V, 9th Floor, 902, Near Vodafone House, Corporate Road, Prahlad Nagar, Ahmedabad – 380 051.
Tel: +91 79 4040 2200

Bengaluru
Embassy Golf Links Business Park, Pebble Beach, 13/02, 'B' Block, 1st & 2nd Floor, Off Intermediate Ring Road, Bengaluru – 560 071
Tel: +91 80 6833 5000

Chandigarh
Elante Offices, Unit No. A505, 5th Floor, Plot No.178-178A, Industrial Area Phase-1, Chandigarh – 160 002.
Tel: +91 172 664 4000

Chennai
KRM Towers, Ground, 1st, 2nd, & 3rd Floor, No. 1, Harrington Road, Chetpet, Chennai – 600 031.
Tel: +91 44 3914 5000

Gurugram
Building No.10, 8th Floor, DLF Cyber City, Phase II, Gurugram, Haryana – 122 002.
Tel: +91 124 307 4000

Hyderabad
Salarpuria Knowledge City, Orwell 6th Floor, Unit-3, Survey No 83/1, Plot No 2, Raidurg, Hyderabad – 500 081.Tel: +91 40 6111 6000

Jaipur
Signature Towers, Office No. 402, Fourth Floor, S Plot No. DC-II, Lal Kothi District Shopping Center, Tonk Road, Jaipur – 302 001
Tel: +91 141 – 672 1000

Kochi
Syama Business Centre, 49/179, 3rd Floor, NH 47, Bypass Road, Vytilla, Kochi – 682 019.
Tel: +91 484 302 5600

Kolkata
Unit No. 604, 6th Floor, Tower – 1, Godrej Waterside, Sector – V, Salt Lake, Kolkata – 700 091.
Tel: +91 33 4403 4000

Mumbai
Lodha Excelus, Apollo Mills Compound, 2nd Floor, N M Joshi Marg, Lower Parel, Mumbai- 400 011.
Tel: +91 22 3989 6000

Noida
Unit No. 501, 5th Floor, Advant Navis Business Park, Tower-A, Plot# 7, Sector 142, Expressway Noida, Gautam Budh Nagar, Noida – 201 305.
Tel: +91 0120 386 8000

Pune
9th floor, Business Plaza, Westin Hotel Campus, 36/3-B, Koregaon Park Annex, Mundhwa Road, Ghorpadi, Pune – 411 001.
Tel: +91 20 6747 7000

Vadodara
Ocean Building, 303, 3rd Floor, Beside Center Square Mall, Opp. Vadodara Central Mall, Dr. Vikram Sarabhai Marg, Vadodara – 390 023.
Tel: +91 265 619 4200

Vijayawada
PR heights, 4th Floor, NH 16 Service Rd, opp. Manipal Hospital Road, Tadepalle, Andhra Pradesh – 522 501.
Tel: +91 0864 536 2000

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