SET~OFF, OR CARRY FORWARD & SET~OFF OF LOSSES

CHAPTER ~ VI

❄ Section 70 : Set- off of loss from one source against income from other source under the same head of income (i.e. Intra-head adjustment)

Loss in respect of any source of income under any head of income can be set-off (S/O) against the income from any other source under the ***same*** head.

Exceptions :

1. Loss from speculation business : Loss from speculation business can be S/O only against the profit from speculation business.

2. Long-term capital loss : Long-term capital loss can be S/O only against the LTCG.

3. Loss from activity of owning and maintaining race horses : Loss from activity of owning and maintaining race horses can be S/O only against profit from activity of owning and maintaining race horses.

4. Loss on account of lotteries, crossword puzzles, races including horse races, card games and other games of any sort or gambling or betting of any form or nature whatsoever : No expenditure or allowance is allowed from winnings from lotteries, crossword puzzles etc. Similarly, no loss on account of lotteries, crossword puzzles etc. is allowed to be set-off at all against any other income under the head IOS, not even against income of another winnings of lotteries, crossword puzzles etc. Again, under the head "IOS" loss from any other activity cannot be S/O from winnings from lotteries, crossword puzzles etc.

Illustration 1 :

X, Y and Z give the following information pertaining to the income under the head "PGBP" :

	X		Y		Z	
	Speculative	**Non-speculative**	**Speculative**	**Non-speculative**	**Speculative**	**Non-speculative**
Business A	1,40,000		1,60,000		1,50,000	
Business B	(-) 50,000		(-) 1,80,000		(-) 60,000	
Business C		2,00,000		4,00,000		2,10,000
Business D		(-) 80,000		(-) 90,000		(-) 2,20,000
Total	90,000	1,20,000	(-) 20,000	3,10,000	90,000	(-) 10,000
			Loss of Rs. 20,000/- can't be S/O against income of Rs. 3,10,000/-. Loss of Rs. 20,000/- shall be C/F.		**Loss of Rs. 10,000/- can be S/O against income of Rs. 90,000/-.**	

Illustration 2 :

A, B, and C give the following information pertaining to the income under the head "CG" :

Capital Asset	A		B		C	
	STCG	LTCG	STCG	LTCG	STCG	LTCG
P	2,50,000		4,60,000		3,12,000	
Q	(-) 90,000		(-) 4,90,000		(-) 80,000	
R		4,00,000		80,000		5,56,000
S		(-) 3,80,000		(-) 15,000		(-) 5,90,000
Total	1,60,000	20,000	(-) 30,000	65,000	2,32,000	(-) 34,000
			Loss of Rs. 30,000/- can be S/O against income of Rs. 65,000/-		**Loss of Rs. 34,000/- can't be S/O against income of Rs. 2,32,000/-. Loss of Rs. 34,000/- shall be C/F.**	

❄ Section 71 : Set-off of loss from one head against income from other head (i.e. Inter-head adjustment)

Loss under any head of income can be S/O against income under the ***other*** heads.

Exception :

1. Loss from speculation business.
2. Loss from activity of owning and maintaining race horses.
3. Loss under the head CG (whether long-term or short-term).
4. Loss under any other head against winnings from lotteries, crossword puzzles etc.
5. Loss under the head PGBP (including unabsorbed depreciation) against income under the head Salaries.

❄ CIT Vs. S. S. Thyagarajan

Loss in respect of exempt income can't be S/O against taxable income under Section 70 & 71.

Illustration 1 :

	Situation I	Situation II
PGBP (Non-speculative)	(-) 3,00,000	4,00,000
LTCG	5,00,000	(-) 2,50,000
Total Income	2,00,000	4,00,000
		Loss of Rs. 2,50,000/- shall be C/F

Illustration 2 :

	Situation I	Situation II
PGBP (Non-speculative)	(-) 3,00,000	4,00,000
STCG	5,00,000	(-) 2,50,000
Total Income	2,00,000	4,00,000
		Loss of Rs. 2,50,000/- shall be C/F.

Illustration 3 :

	Situation I	Situation II
PGBP (Speculative) **LTCG**	(-) 3,00,000 5,00,000	4,00,000 (-) 2,50,000
Total Income	5,00,000	4,00,000
	Loss of Rs. 3,00,000/- shall be C/F.	**Loss of Rs. 2,50,000/- shall be C/F.**

Illustration 4 :

	Situation I	Situation II
PGBP (Speculative) **STCG**	(-) 3,00,000 5,00,000	4,00,000 (-) 2,50,000
Total Income	5,00,000	4,00,000
	Loss of Rs. 3,00,000/- shall be C/F.	**Loss of Rs. 2,50,000/- shall be C/F.**

Illustration 5 :

	Situation I	Situation II
PGBP **(Agricultural business)**	(-) 3,00,000	4,00,000
PGBP **(Manufacturing business)**	5,00,000	(-) 2,50,000
Total Income	5,00,000	(-) 2,50,000
	Loss of Rs. 3,00,000/- can't be C/F as per decision of Supreme Court in Harprasad & Co. Pvt. Ltd.	**Loss of Rs. 2,50,000/- shall be C/F.**

❄ Section 71B : C/F & S/O of Loss from House property

Loss under the head "IHP" not fully S/O under Section 71 shall be C/F and S/O against "IHP" only. C/F is allowed for 8 A.Ys. immediately succeeding the A.Y. for which the loss was first computed.

Note : Loss under the head "IHP" can be C/F even if ROI is filed after time prescribed U/S 139 (1).

❄ Section 72 : C/F & S/O of losses of non-speculative business

Losses of non-speculative business not fully S/O under Section 71 shall be C/F and S/O against "PGBP" only. C/F is allowed for 8 A.Ys. immediately succeeding the A.Y. for which the loss was first computed.

Note : Business in relation to which loss is computed need not be continued.

Priority of S/O :

- Current Year's Depreciation
- B/F Business Loss
- B/F Depreciation

Condition for S/O :

"Assessee must be the same" i.e. the assessee who incurred the loss and the assessee who claims the C/F & S/O, must be the same.

Exception to the rule that the assessee must be the same :

1) Loss of business or profession can be C/F by successor, who succeeds business of an individual on his death, for the balance years.

   Note : Unabsorbed depreciation is not covered by Chapter VI but is governed by Section 32 (2). Therefore unabsorbed depreciation of the deceased will not be C/F by the legal heir on inheritance.

2) Section 72A : Unabsorbed losses and unabsorbed depreciation of amalgamating company shall be deemed to be the losses and depreciation of amalgamated company ***of the P.Y. in which amalgamation took place***. Similarly unabsorbed losses and unabsorbed depreciation of a private company/ unlisted public company shall be deemed to be the losses and depreciation of LLP ***of the P.Y. in which conversion of private company/ unlisted public company in LLP took place.***

3) Firm succeeded by a company fulfilling the conditions laid down in section 47 (xiii).

4) Proprietary concern succeeded by a company fulfilling the condition laid down in Section 47 (xiv).

5) Loss of Demerged Company can be C/F by the Resulting Company subject to fulfillment of certain conditions.

Exception to the rule that the loss can be C/F for 8 Assessment Years :

A) Section 41 (5) :

"Loss" of business or profession ***of the P.Y.**** in which business was discontinued can be S/O against the income U/S 41 (1), 41 (3) and 41 (4) arising subsequent to discontinuance of business.

**Section 41 (5) is applicable for the losses of the P.Y. in which business was discontinued and is not applicable for losses B/F in the P.Y. in which business was discontinued.

Section 41 (1) : Recovery of loss or expenditure allowed as deduction & Remission and cessation of the trading liability.

Section 41 (3) : Profit on sale of scientific research asset.

Section 41 (4) : Bad debt recovery.

Illustration 1 : Mr. X discontinued his business on 28-02-1985. The following information is given :

B/F Business Losses of A.Y. 1982-83 to A.Y. 1984-85	Rs. 8,00,000
Business Loss of the A.Y. 1985-86	Rs. 5,00,000

Mr. X recovered bad debts of Rs. 7,00,000/- on 31-3-2011. What will be the tax treatment?

Solution :

Assessment Year : 2011-12

Profit & gains from business or profession :

Bad debt recovery as per section 41 (4)	Rs. 7,00,000
Less : Business Loss of the A.Y. 1985-86 as per Section 41 (5)	Rs. 5,00,000

Profit & gains from business or profession	Rs. 2,00,000
	=========

Illustration 2 : What will be the tax treatment in Illustration 1 above, if Mr. X recovered bad debt of Rs. 4,00,000/- on 31-03-2010 and Rs. 3,00,000/- on 31-03-2011.

Solution :

Assessment Year : 2010-11

Profit & gains from business or profession :

Bad debt recovery as per section 41 (4)	Rs. 4,00,000
Less : Business Loss of the A.Y. 1985-86 as per Section 41 (5)	Rs. 4,00,000

Profit & gains from business or profession	Nil
	=========

Assessment Year : 2011-12

Profit & gains from business or profession :

Bad debt recovery as per section 41 (4)	Rs. 3,00,000
Less : Business Loss of the A.Y. 1985-86 as per Section 41 (5)	Rs. 1,00,000

Profit & gains from business or profession	Rs. 2,00,000
	=========

B) Proviso to Section 72 (1) :

Where business is discontinued due to flood, cyclone, earthquake, riots etc. and re-established before the expiry of 3 years from the end of the P.Y. in which business discontinued, then loss of such business ***including the B/F loss*** can be S/O against business income (and not the income from speculation business) in the A.Y. relevant to the year in which business is re-established and the balance in 7 succeeding A.Y.

Note : Depreciation is not covered by Section 41 (5) and Proviso to Section 72 (1).

Illustration 1 : Mr. X discontinued his business on 31-01-2009 because of floods. The following information is given :

B/F Business Losses of A.Y. 2003-04 to A.Y. 2008-09	Rs. 6,00,000
Business Loss of the A.Y. 2009-10	Rs. 5,00,000

The business is re-established on 01-01-2012. How will you deal with the above losses ?

Answer : Business loss of Rs. 11,00,000/- can be C/F to A.Y. 2012-13 and S/O against PGBP only. The loss to the extent not S/O shall be C/F upto A.Y. 2019-20.

Illustration 2 : Suppose in example 1, the business is re-established on 01-01-2013, will your answer be different ?

Answer : Proviso to Section 72 (1) is not applicable since the business is re-established after 3 years from the end of the P.Y. in which business discontinued. Losses shall be C/F as under :

Loss of A.Y.	C/F permissible u/s 72 upto A.Y.	Whether loss can be C/F in A.Y. 2013-14 ?
2009-10	2017-18	Yes
2008-09	2016-17	Yes
2007-08	2015-16	Yes
2006-07	2014-15	Yes
2005-06	2013-14	Yes
2004-05	***2012-13***	***No***
2003-04	***2011-12***	***No***

Notes :

1. **CIT Vs. J. H. Gotla (Supreme Court) :**

   B/F ***business*** losses of an individual can be S/O against the ***PGBP*** of spouse/minor clubbed U/S 64.

   Note :

   Once income of minor is clubbed, Section 70, 71 etc. apply to parent regarding S/O, or C/F & S/O.

	Situation I	**Situation II**	**Situation III**
Mr. X	Rs. 2,00,000/- (B/F Business Loss)	Rs. (-) 80,000/- (PGBP of current P.Y.)	Rs. 1,00,000/- (B/F Business Loss)
Minor child / wife of Mr. X (Income is to be clubbed)	Rs. 4,00,000/- (PGBP of current P.Y.)	Rs. 2,00,000/- (IOS of current P.Y.)	Rs. 1,50,000/- (IHP)
Total Income of Mr. X	Rs. 2,00,000/-	Rs. 1,20,000/-	Rs. 1,50,000/-
			Business Loss of Rs. 1,00,000/- shall be C/F by Mr. X

	Situation IV	**Situation V**	**Situation VI**
Mr. X	Rs. (-) 1,00,000/- (PGBP of current P.Y.)	Rs. 1,00,000/- (PGBP of current P.Y.)	Rs. 1,00,000/- (B/F Business Loss)
Minor child / wife of Mr. X (Income is to be clubbed)	Rs. (-) 1,50,000/- (PGBP of current P.Y.)	Rs. (-) 70,000/- (PGBP of current P.Y.)	Rs. 2,00,000/- (CG)
Total Income of Mr. X	Rs. (-) 2,50,000/-	Rs. 30,000/-	Rs. 2,00,000/-
	Business Loss of Rs. 2,50,000/- shall be C/F by Mr. X		**Business Loss of Rs. 1,00,000/- shall be C/F by Mr. X**

2. **Harprasad & Co. Pvt. Ltd. (Supreme Court) :** Loss from a non-taxable source can't be C/F.

3. **Where losses sustained are not S/O against the profits of the immediately succeeding year(s), then these losses can't be S/O against the profits at a later date :**

   Illustration 1 :

   Mr. X provides the following information regarding his "PGBP" of various assessment years :

A.Y. 2009-10	**A.Y. 2010-11**	**A.Y. 2011-12**
Rs. (-) 80,000	Rs. 1,60,000 (Before S/O of B/F Loss of Rs. 80,000)	Rs. 3,00,000 (Before S/O of B/F Loss of Rs. 80,000)

   Mr. X did not set-off the B/F business loss of A.Y. 2009-10 in A.Y. 2010-11 and filed his ROI showing business income of Rs. 1,60,000 for the A.Y. 2010-11. Now Mr. X wants to S/O the loss of Rs. 80,000 in A.Y. 2011-12. Can he do so?

   Answer :

   The loss of Rs. 80,000 can't be C/F & S/O in A.Y. 2011-12 since it was not S/O in A.Y. 2010-11.

Illustration 2 :

Mr. X provides the following information regarding his "PGBP" of various assessment years :

A.Y. 2009-10	A.Y. 2010-11	A.Y. 2011-12
Rs. (-) 2,00,000	Rs. 1,60,000 (Before S/O of B/F Loss of Rs. 2,00,000)	Rs. 3,50,000 (Before S/O of B/F Loss of Rs. 2,00,000)

Mr. X did not set-off the B/F business loss of A.Y. 2009-10 in A.Y. 2010-11 and filed his ROI showing business income of Rs. 1,60,000 for the A.Y. 2010-11. Now Mr. X wants to S/O the loss of Rs. 2,00,000 in A.Y. 2011-12. Can he do so?

Answer :

Mr. X can C/F & S/O only Rs. 40,000 in A.Y. 2011-12. The remaining loss of Rs. 1,60,000 can't be C/F & S/O in A.Y. 2011-12 since it was not S/O against the income of Rs. 1,60,000 in A.Y. 2010-11.

4. **Western State Trading Co. (Pvt.) Ltd. Vs. CIT (Supreme Court)** :

Where shares are held by an assessee as stock-in-trade, dividend on such shares would form part of business income and consequently, he will be entitled to claim S/O of business loss B/F from earlier years against dividend of the current year. However, for taxation purpose such dividend will be taxable under the head "IOS".

❄ Section 73 : Losses of Speculation Business

Section 43 (5) : Speculative transaction :

"Speculative transaction" means a transaction in which a contract for the purchase or sale of any commodity (including shares and stocks) is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips.

Explanation 2 to Section 28 :

Where the ***speculative transactions*** carried on by an assessee are of such a nature as to constitute a business, such business (i.e. "Speculation business") shall be deemed to be distinct and separate from any other business.

Section 73 :

- Loss can be C/F for 4 A.Ys. immediately succeeding the A.Y. for which the loss was first computed.
- C/F loss of a speculation business ------> S/O possible only against profit and gains of another speculation business.
- Business need not be continued but assessee must be the same.

❄ Section 74 : Losses under the head CG

- Loss can be C/F for 8 A.Ys. immediately succeeding the A.Y. for which the loss was first computed.
- C/F Long-term capital loss ------> Can be S/O only against LTCG.
- C/F Short-term capital loss ------> Can be S/O against STCG as well as LTCG.

Illustration 1 : During the P.Y. 2010-11, X Ltd. has generated STCG of Rs. 80,000. It has B/F Short-term capital loss : Rs. 10,000 and B/F Long-term capital loss : Rs. 15,000. In this case, while B/F Short-term capital loss of Rs. 10,000 can be S/O against STCG of Rs. 80,000, the B/F Long-term capital loss of Rs. 15,000 cannot be S/O against STCG of Rs. 80,000.

Illustration 2 : During the P.Y. 2010-11, X Ltd. has generated LTCG of Rs. 1,16,000. It has B/F Short-term capital loss : Rs. 8,000 and B/F Long-term capital loss : Rs. 40,000. In this case, B/F Short-term capital loss of Rs. 8,000 as well as B/F Long-term capital loss of Rs. 40,000 can be S/O against LTCG of Rs. 1,16,000.

❄ Section 74A : Losses from activity of owning and maintaining of race horses

- Can be C/F for 4 A.Ys. immediately succeeding the A.Y. for which the loss was first computed.
- C/F Loss ------> Can be S/O only against income from the activity of owning and maintaining race horses.
- Business of owning and maintaining race horses must be continued.

❄ Section 80 : Return of loss should be filed on or before the due date of furnishing of return as prescribed under Section 139 (1)

If an assessee fails to file his return of loss on or before the due date of furnishing of return as prescribed under Section 139 (1) then the following losses (***of the assessment year for which the return is not submitted in time***) can't be C/F :

1. Loss of a speculative or non-speculative business (not being unabsorbed depreciation);
2. Short-term and long-term capital loss; and
3. Loss (not being unabsorbed depreciation) from the activity of owning and maintaining race horses.

It may be noted that right to S/O and C/F loss of past years is not affected even if the return of the current P.Y. is filed after the due date. Moreover, S/O of losses of the current P.Y. against the current previous year's income is permissible even if the return of income is filed after the due date.

❄ Section 73A : S/O or C/F & S/O of losses by specified business. [Inserted by the Finance (No. 2) Act, 2009, w.e.f. A.Y. 2010-11]

- ❖ Any loss, computed in respect of any specified business referred to in Section 35AD shall not be set-off ***except against profits and gains, if any, of any other specified business***.

- ❖ Where for any assessment year any loss computed in respect of the specified business referred to in Section 35AD has not been wholly set-off in the current year, so much of the loss as is not so set-off or the whole loss where the assessee has no income from any other specified business shall be carried forward to the following assessment year.

- ❖ Loss can be C/F for 8 A.Ys. immediately succeeding the A.Y. for which the loss was first computed.

- ❖ B/F loss in the subsequent A.Y. can be set off against the profits and gains, if any, of any specified business carried on by him assessable for that assessment year.

SET-OFF, OR CARRY FORWARD & SET-OFF OF LOSSES

PRACTICAL PROBLEMS

Question No. 1 :

X, an individual, submits the following information relevant for the assessment year 2011-12 :

	Profit Rs.	Loss Rs.
Salary income (computed)	42,000	
Income from house property :		
House A	15,000	
House B		17,000
House C		21,000
Profits and gains of business or profession :		
Business A	8,000	
Business B		18,000
Business C (speculative)	11,000	
Business D (speculative)		23,000
Capital gains :		
Short-term capital gains	6,000	
Short-term capital loss		28,000
Long-term capital gains on sale of building	12,500	
Income from other sources :		
Income from card games	8,000	
Loss from card games		7,010
Loss on maintenance of race horses		6,000
Interest on securities	4,000	

Determine the net income of X for the assessment year 2011-12.

SET-OFF, OR CARRY FORWARD & SET-OFF OF LOSSES

SOLUTION

Answer to question No. 1 :

Computation of Net Income

Name of assessee : Mr. X
Previous Year : 2010-11
Assessment Year : 2011-12

	Rs.	Rs.
A. Income from salaries :	(+) 42,000	
Less : Loss under the head Income from house property	(-) 23,000	19,000
B. Income from house property :		Nil
C. Profits & Gains of business or profession :		Nil
D. Capital Gains :		Nil
E. Income from other sources :		
Income from card games		
(losses can't be S/O against this income as per Section 70 & 71)		8,000
Interest on securities	(+) 4,000	
Less : Loss under the head PGBP (non-speculative business)	(-) 10,000	
Loss under the head PGBP (non-speculative business) to be C/F to the next assessment year	(-) 6,000	
Gross total income		27,000
Less : Deductions u/s 80C to 80U		Nil
Net Income		27,000

Note :

Intra-head adjustment :

	Rs.		Rs.
Income from house property :			
House A	(+) 15,000		
House B	(-) 17,000		
House C	(-) 21,000		
Loss under the head income from house property			(-) 23,000
Profits & Gains of business or profession :			
Non-speculative :			
Business A	(+) 8,000		
Business B	(-) 18,000	(-) 10,000	
Speculative :			
Business C	(+) 11,000		
Business D	(-) 23,000	Nil	
To be C/F to the next assessment year	(-) 12,000		
Loss under the head PGBP (non-speculative business)			(-) 10,000

Capital gains :			
Short-term capital gains	(+) 6,000		
Short-term capital loss	(-) 28,000	(-) 22,000	
Long-term capital gain	(+) 12,500	(+) 12,500	
To be C/F to the next assessment year		(-) 9,500	
Capital gains			Nil
Income from other sources :			
Income from card games	(+) 8,000		
Loss from card games	(-) 7,010	(+) 8,000	
Loss from card games (this loss can't be S/O against any income u/s 70 & 71. C/F is also not permitted)	(-) 7,010	Nil	
Interest on securities	(+) 4,000	(+) 4,000	
Loss on maintenance of race horses (to be C/F to the next A.Y)	(-) 6,000	Nil	
Income from other sources			12,000