

SET OFF AND CARRY FORWARD OF LOSSES

Question 1

Simran, engaged in various types of activities, gives the following particulars of her income for the year ended 31.3.2007:

	Rs.
(a) Profit of business of consumer and house-hold products	50,000
(b) Loss of business of readymade garments	10,000
(c) Brought forward loss of catering business which was closed in Asst. Year 2006-07	15,000
(d) Short-term loss on sale of securities and shares	15,000
(e) Profit of speculative transactions entered into during the year	12,500
(f) Loss of speculative transactions of Asst. Year 2002-03 not set off till Asst. Year 2006-07	15,000

Compute the total income of Simran for the A.Y. 2007-08. (6 Marks)(May 2007)

The provisions of the Income-tax Act, 1961 relevant for Assessment Year 2010-11 should be taken into consideration while solving the question. Accordingly, the facts given above may be taken as relating to financial year 2009-10. Consequently, it may be taken that catering business was closed in A.Y. 2009-10 and loss of speculation transaction of A.Y. 2005-06 not set off till A.Y. 2009-10 is Rs. 15,000.

Answer

Computation of total income of Simran for the A.Y. 2010-11

Particulars	Rs.	Rs.
Profit of business of consumer and house-hold products	50,000	
Less: Loss of business of readymade garments for the year adjusted under section 70(1)		<u>10,000</u>

Taxation

	40,000	
Less: Brought forward loss of catering business closed in A.Y. 2009-10 set off against business income for the current year as per section 72(1)	<u>15,000</u>	25,000

Profit of speculative transaction	<u>12,500</u>
Total Income	<u>37,500</u>

Notes –

1. Loss of speculative transaction of A.Y. 2005-06 is not allowed to be set off against the profit of speculative transaction of the A.Y.2010-11, since, as per the provisions of section 73(4), such loss can be carried forward for set-off for a maximum period of 4 years only i.e. up to A.Y.2009-10.
2. Short term capital loss of Rs.15,000 on sale of securities and shares has to be carried forward as per section 74 since there is no income under the head Capital Gains for the A.Y.2010-11. The loss is to be carried forward for set off in future years against income chargeable under the head Capital Gains. Such loss can be carried forward for a maximum period of 8 assessment years.

Question 2

State the factors to be borne in mind relating to carry forward and set off of losses in case of change in constitution of firm or succession under section 78. (4 Marks)(May 2007)

Answer

Carry forward and set off of losses in case of change in constitution of firm or succession [Section 78]

- (i) Where there is a change in the constitution of a firm, so much of the loss proportionate to the share of a retired or deceased partner remaining unabsorbed shall not be allowed to be carried forward by the firm. However, unabsorbed depreciation can be carried forward.
- (ii) Where any person carrying on any business or profession has been succeeded in such capacity by another person otherwise than by inheritance, such other person shall not be allowed to carry forward and set off against his income, any loss incurred by the predecessor.
- (iii) Where there is a succession by inheritance, the legal heirs [assessable as body of individuals (BOI)] are entitled to set off the business loss of the predecessor. Such carry forward and set off is possible even if the legal heirs constitute themselves as a partnership firm. In such a case, the firm can carry forward and set off the business loss of the predecessor.

Set off and Carry Forward of Losses

Question 3

Discuss in brief the provisions relating to set off and carry forward of losses in speculation business. (4 Marks)(Nov 2007)

Answer

- (i) The loss of a speculation business of any assessment year is allowed to be set off only against the profits and gains of another speculation business in the same assessment year.
- (ii) The speculation loss not set-off in the same assessment year, is allowed to be carried forward to subsequent years and set-off only against income of any speculation business.
- (iii) The loss in speculation business can be carried forward only for a maximum period of 4 years from the end of the relevant assessment year in respect of which the loss was computed.
- (iv) Loss from the activity of trading in derivatives, however, is not to be treated as speculative loss.
- (v) According to the Explanation to section 73, where any part of the business of a company consists in the purchase and sale of shares of other companies such company shall be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares.

However, this Explanation does not apply to-

- (a) a company whose gross total income consists mainly of income which is chargeable under the heads "Income from house property", "Capital gains" and "Income from other sources"; and
- (b) a company the principal business of which is the business of banking or the granting of loans and advances.

Question 4

M/s. Vivitha & Co., a partnership firm, with four partners A, B, C and D having equal shares, furnishes the following details, summarized from the valid returns of income filed by it :

Assessment year	Item eligible for carry forward and set off
2006-07	Unabsorbed business loss Rs. 1,20,000
2007-08	Unabsorbed business loss Rs. 1,90,000
2007-08	Unabsorbed depreciation Rs. 1,20,000
2007-08	Unabsorbed long-term Capital losses:
	-from shares Rs. 1,10,000
	-from building Rs. 1,90,000

Taxation

C who was a partner during the last three years, retired from the firm with effect from 1.4.2007.

The summarized results of the firm for the assessment year 2008-09 are as under:

	Rs.
Income from house property	70,000
Income from business:	
Speculation	2,20,000
Non-speculation	(-) 50,000
Capital gains	
Short-term (from sale of shares)	40,000
Long-term (from sale of building)	2,10,000
Income from other sources	60,000

Briefly discuss, how the items brought forward from earlier years can be set off in the hands of the firm for the assessment year 2008-09, in the manner most beneficial to the assessee. Also show the items to be carried forward. Computation of total income is not required.

(9 Marks)(May 2008)

The provisions of the Income-tax Act, 1961 relevant for Assessment Year 2010-11 should be taken into consideration while solving the question. Accordingly, the facts given above may be taken as relating to financial year 2009-10. Therefore, unabsorbed loss of A.Y. 2006-07 may be taken as relating to A.Y. 2008-09 and unabsorbed loss of A.Y. 2007-08 may be taken as relating to A.Y. 2009-10. Further, it may be taken that C retired on 1.4.2009.

Answer

According to section 78(1), where there is a change in the constitution of the firm, the loss relatable to outgoing partner (whether by way of retirement or death) has to be excluded for the purposes of carry forward. However, this provision does not apply in the case of unabsorbed depreciation.

Accordingly, M/s. Vivitha & Co. is entitled to carry forward the losses to the extent detailed herebelow:

Item	Loss (Rs.)	Relatable to C (Rs.)	Balance eligible for carry forward (Rs.)
Business loss of A.Y.2008-09	1,20,000	30,000	90,000
Business loss of A.Y.2009-10	1,90,000	47,500	1,42,500
Long term capital loss of A.Y.2009-10	3,00,000	75,000	2,25,000

Set off and Carry Forward of Losses

Set off of items in the hands of M/s. Vivitha & Co. for the A.Y. 2010-11

Particulars	Amount (Rs.)	Amount (Rs.)
1. Income from house property		
Current year as given	70,000	
Less: Brought forward depreciation (See Note 1)	<u>70,000</u>	NIL
2. Profits and gains of business or profession		
Current year speculation	2,20,000	
Less: Current year Non-speculation loss set off (See Note 2)	<u>50,000</u>	
	1,70,000	
Less: Brought forward business losses of earlier year (2008-09 Rs. 90,000 and 2009-10 Rs. 80,000) (See Note 3)	<u>1,70,000</u>	NIL
3. Capital gain		
Short term (from sale of shares)		40,000
Long-term (from sale of building)	2,10,000	
Less: Brought forward LTC loss of A.Y. 2009-10 (See Note 4)	<u>2,10,000</u>	NIL
4. Income from other sources		
Current year before set off	60,000	
Less: Brought forward depreciation (See Note 1)	<u>50,000</u>	10,000
Losses to be carried forward to A.Y. 2011-12		
Business loss (Rs. 1,42,500 - Rs. 80,000)		62,500
Long term capital loss (Rs. 2,25,000 – Rs. 2,10,000)		15,000
Both these losses relate to A.Y. 2009-10.		

Taxation

Notes:

- (1) Unabsorbed depreciation can be set off against income from any head. Hence, it will be advantageous to set off unabsorbed depreciation against income from house property and income from other sources.
- (2) In the current year, non-speculation business loss can be set off against speculation business income.
- (3) Brought forward non-speculation business loss can also be set off against speculation business income of current year.
- (4) According to section 74, brought forward long term capital losses shall be set off only against long-term capital gains of current year.
- (5) The set-off and carry forward of losses should be most beneficial to the assessee. If the students set off brought forward depreciation against current year's business income first, then the quantum of brought forward business loss which can set off against current year's business income will be lower. This will not be beneficial to the assessee.

Question 5

Mr. P, a resident individual, furnishes the following particulars of his income and other details for the previous year 2007-08:

	Rs.
(i) Income from salary	18,000
(ii) Net annual value of house property	70,000
(iii) Income from business	80,000
(iv) Income from speculative business	12,000
(v) Long term capital gain on sale of land	15,800
(vi) Loss on maintenance of race horse	9,000
(vii) Loss on gambling	8,000

Depreciation allowable under the Income-tax Act comes to Rs.8,000 for which no treatment is given above.

The other details of unabsorbed depreciation and brought forward losses are:

	Rs.
(i) Unabsorbed depreciation	9,000
(ii) Loss from speculative business	16,000
(iii) Short term capital loss	7,800
(iv) Unrealised rent	17,000

Set off and Carry Forward of Losses

Compute the gross total income of Mr. P, for the Assessment year 2008-09, and the amount of loss that can or cannot be carried forward. (6 Marks)(Nov 2008)

The provisions of the Income-tax Act, 1961 relevant for Assessment Year 2010-11 should be taken into consideration while solving the question. Accordingly, the facts given above may be taken as relating to financial year 2009-10.

Answer

Computation of Gross Total Income of Mr. P for the A.Y. 2010-11.

	Rs.	Rs.
(i) Income from salary		18,000
(ii) Income from House Property		
Net annual value	70,000	
Less : Deduction under section 24 (30% of Rs.70,000)	21,000	49,000
(iii) Income from business and profession		
(a) Income from business	80,000	
Less : Current year depreciation	8,000	
	72,000	
Less : Unabsorbed depreciation	9,000	63,000
(b) Income from speculative business	12,000	
Less : Brought forward loss from speculative business	12,000	Nil
(Balance loss of Rs.4,000 (i.e. Rs.16,000 – Rs.12,000) can be carried forward to the next year)		
(iv) Income from capital gain		
Long term capital gain on sale of land	15,800	
Less : Brought forward short term capital loss	7,800	8,000
Gross total income		1,38,000

Amount of loss to be carried forward to the next year

Particulars	Rs.
Loss from speculative business (to be carried forward as per section 73)	4,000
Loss on maintenance of race horses (to be carried forward as per section 74A)	9,000

Taxation

Notes:

- (i) Loss on gambling can neither be set-off nor be carried forward.
- (ii) As per Section 74A(3), the loss incurred on maintenance of race horses cannot be set-off against income from any other source other than the activity of owning and maintaining race horses. Such loss can be carried forward for a maximum period of 4 assessment years.
- (iii) Only speculative business loss can set off against income from speculative business of the current year and the balance loss can be carried forward to A.Y. 2011-12. It may be noted that speculative business loss can be carried forward for a maximum of four years as per section 73(4).

Question 6

Ms. Geeta, a resident individual, provides the following details of her income / losses for the year ended 31.3.2009:

- (i) Salary received as a partner from a partnership firm Rs. 7,50,000.
- (ii) Loss on sale of shares listed in BSE Rs. 3,00,000. Shares were held for 15 months and STT paid on sale.
- (iii) Long-term capital gain on sale of land Rs. 5,00,000.
- (iv) Rs. 51,000 received in cash from friends in party.
- (v) Rs. 55,000, received towards dividend on listed equity shares of domestic companies.
- (vi) Brought forward business loss of assessment year 2007-08 Rs. 12,50,000.

The return for assessment year 2007-08 was filed in time.

Compute gross total income of Ms. Geeta for the assessment year 2009 -10 and ascertain the amount of loss that can be carried forward. (8 Marks)(June 2009)

The provisions of the Income-tax Act, 1961 relevant for Assessment Year 2010-11 should be taken into consideration while solving the question. Accordingly, the facts given above may be taken as relating to financial year 2009-10. Brought forward business loss relates to A.Y. 2008-09 for which the return of income was filed in time.

Answer

Computation of Gross Total Income of Ms. Geeta for the Assessment Year 2010-11

Particulars	Rs.
Profits and gains of business and profession	
Salary received as a partner from a partnership firm is taxable under the head "Profits and gains of business and profession"	7,50,000

Set off and Carry Forward of Losses

Less: brought forward business loss of assessment year 2008-09 to be set-off against business income	7,50,000
	<u>Nil</u>
Capital Gains	
Long term capital gain on sale of land – (See Note 2)	5,00,000
Income from other sources	
Cash gift received from friends - since the value of cash gift exceeds Rs.50,000, the entire sum is taxable	51,000
Dividend received from a domestic company is exempt under section 10(34)	<u>Nil</u>
	<u>51,000</u>
Gross Total Income	<u>5,51,000</u>

Notes –

1. Balance brought forward business loss of assessment year 2008-09 of Rs.5,00,000 has to be carried forward to the next year.
2. Long-term capital loss on sale of shares cannot be set-off against long-term capital gain on sale of land since loss from an exempt source cannot be set-off against profit from a taxable source. Since long-term capital gain on sale of listed shares on which STT is paid is exempt under section 10(38), loss on sale of listed shares is a loss from an exempt source. So, it cannot be set-off against long-term capital gain on sale of land, which is a profit from a taxable source.

Taxation

NOTE

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