

Bombay High Court rules share trading loss of a company to be set off against non speculative income before invoking deeming provisions of section 73 of the Act

Executive Summary

This tax alert summarizes the recent significant ruling of the Bombay High Court (HC) in the case of **Darshan Securities Pvt. Ltd.** (the Taxpayer)¹, on an issue whether loss from share trading can be set off against profits and gains of non speculative business, in a case where after set off of the loss, the gross total income mainly comprises of income from Other Sources.

The Taxpayer, a company, filed return of income disclosing income from service charges, loss from share trading activity (which was set off against income from service charges) and dividend income. The Assessing Officer (AO) held that loss from share trading in the case of a company

being deemed speculative loss² cannot be set off against income from service charges. The first appellate authority reversed the order of AO on an appeal by the Taxpayer. In an appeal by the Revenue, Tribunal upheld the order of the first appellate authority. On an appeal before the HC, held, that for determining whether or not the gross total income mainly consists of amount chargeable under the 'specified heads' of income³, the loss from share trading should be set off

under the normal provisions⁴ of the Act. In the facts of the case, since, post set off, the gross total income mainly comprised of income from Other Sources, the share trading loss is not deemed speculative under section 73 of the Act.

Background

- Section 73 of the Act provides that in the case of a Taxpayer, a company, income from share trading shall be deemed to be speculative business income regardless of the fact that transactions may be delivery based; subject to an exception that the above deeming provision shall not apply to a Taxpayer who is engaged in banking

² As an anti tax avoidance measure section 73 of the Act deems share trading loss as deemed speculative, even when transactions are delivery based

³ Income from House Property, Capital Gains and Income from Other Sources

⁴ As per normal provisions of the Act, delivery based share trading income is not deemed speculative so as to deny set off against loss

¹ ITA No. 2886/ 2009

business, or whose gross total income mainly comprises of income chargeable under specified heads of income. For example, if income of any company comprises of (a) capital gains of INR 50000; (b) income of INR 37000 from normal business and (c) loss from share trading business (delivery based transactions) of INR 10000, then the said loss shall not be deemed speculative because major income consists of income from the specified head viz., Capital Gains

- The Taxpayer had returned income from service charges of INR 2.25 crores and dividend income of INR 4.7 lacs. Apart from the above income, the Taxpayer had loss from share trading of INR 2.23 crores which it had set off against income from service charges. Post set off, the gross total income comprised of dividend of INR 4.7 lacs and INR 3 lacs from business income
- The AO held that loss from share trading is speculative loss since the Taxpayer's income (without set off of loss) mainly consists of income falling under the head business, not being the specified head of income

- Aggrieved by the said order, the Taxpayer filed an appeal before the first appellate authority who allowed the claim of the Taxpayer
- On an appeal to the ITAT by the Revenue, the ITAT upheld the order of the first appellate authority

Tax Authority's contentions

- In determining the components of gross total income for the purpose of deeming fiction under section 73, income under the head profits and gains from business and profession must be ignored
- Alternatively, loss from share trading being speculative business loss, should not be allowed to be set off against income from any source which is a non speculative business

Taxpayer's contentions

- For ascertaining the head wise classification of income, loss from share trading should be adjusted against income from service charges as per normal provisions of the Act
- Since the gross total income (after the set off) mainly consists of income from

Other Sources, the deeming provisions of section 73 does not apply. Hence, loss from share trading cannot be deemed to be speculative business loss

- Thus, the said loss is eligible for set off against income from service charges under normal provisions of the Act without attracting deeming fiction of section 73 of the Act

HC ruling

- Section 73 of the Act restricts set off of loss from speculative business against any income except gains from speculative business. However, loss arising from share trading business of a company is deemed to be speculative subject to the exception when company's gross total income consists of income from specified heads
- As per the provisions of the Act, gross total income is required to be computed before applying the deeming fiction provisions of section 73
- While computing gross total income, the rules of set off as per normal provisions of the Act should be followed i.e. without the consideration of

deeming fiction provided in section 73 of the Act

- After the above process of set off, if the gross total income mainly consists of income from specified heads, the deeming fiction of section 73 shall not apply
- In the facts of the case, as per the above sequence of set off, the gross total income of the Taxpayer mainly consists of income from specified head. Hence, the share trading loss shall be allowed to be set off against normal business profits

Our comments

- This HC ruling reiterates the position in law that deeming fiction of section 73 which considers a non speculative loss in share trading business as deemed to be speculative in certain circumstances, cannot operate without first ascertaining the gross total income. The position taken by the Revenue, that the deeming fiction shall be given effect to in priority to the computation of gross total income as per normal provisions of the Act, has been rightly rejected by the Court on the proper interpretation of the provisions of the Act

- This ruling will help the corporate taxpayers who have incurred non speculative losses in share trading business in claiming set off against profits of non speculative businesses and thereby reduce the income tax liability, when their gross total income, after the aforesaid set off, mainly consists of income chargeable under the heads "Income from House Property", "Capital Gains" or "Income from Other Sources"

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