

# Clubbing Provisions and Set-off and/ or Carry Forward of Losses

## Lesson 9

### KEY CONCEPTS

■ Clubbing ■ Revocable Transfer ■ Irrevocable Transfer ■ Substantial Interest ■ Set-Off of Losses ■ Carried Forward of Loss

### Learning Objectives

#### To understand:

- What is Clubbing of Income?
- Applicability of Clubbing Provision
- What is Revocable Transfer of Assets?
- What is Irrevocable Transfer of Assets?
- Provisions of set off/carry forward and set off of losses
- Inter-head and Intra-head set-off of losses

### Lesson Outline

- Clubbing of Income
- Transfer of Income without transfer of Assets
- Revocable Transfer of Assets
- Income of Spouse
- Income from Assets transferred to son's wife
- Transfer for immediate or deferred benefit of Son's Wife
- Income to Spouse through a Third Person
- Clubbing of income of Minor Child
- Income from the Converted Property
- Practice Questions
- Set-off and Carry-forward of Losses
- Set-off of Losses
- Carry forward of losses
- Treatment of Carry-forward of losses of certain assesseees
- Practice Questions
- Lesson Round-Up
- Test Yourself
- Lists of Further Readings
- Other References

**REGULATORY FRAMEWORK**

| <b>Sections</b>     | <b>Income Tax Act, 1961</b>  |
|---------------------|--|
| Section 60          | Transfer of Income   |
| Section 61          | Revocable Transfer of Assets   |
| Section 64(1)(ii)   | Income to spouse from a concern in which such individual has substantial interest                  |
| Section 64(1)(iv)   | Income to spouse from the assets transferred   |
| Section 64(1)(vi)   | Income from Assets transferred to Son's Wife   |
| Section 64(1)(viii) | Income for immediate or deferred benefit of son's wife   |
| Section 64(1)(vii)  | Income of spouse through a third person  |
| Section 64(1A)      | Clubbing of Income of Minor Child  |
| Section 64(2)       | Income from the Converted Property   |
| Section 70          | Set-Off of Losses from One Source Against Income from Another Source under the same Head of Income |
| Section 71          | Set-Off of Loss from One Head Against Income from Another Head                                     |
| Section 72          | Loss in Non-Speculation Business   |
| Section 73          | Loss in Speculation Business   |
| Section 73A         | Carry Forward and Set Off of Losses by Specified Business  |
| Section 74          | Set-Off and Carry Forward of Capital Losses  |
| Section 74(A)       | Loss on Maintenance of Race Horses   |
| Section 78          | Carry-forward and set-off of losses in case of change in constitution of firm                      |
| Section 79          | Carry-forward and set-off of losses of change in shareholding of Companies                         |

**CLUBBING OF INCOME**

Generally, a person is taxed in respect of income earned by them only. However, in certain situation, income of other person is included (i.e., clubbed) in the taxable income of the taxpayer and in such a case, he will be liable to pay tax in respect of his income as well as income of other person too. The situation in which income of other person is included in the income of the taxpayer is called as clubbing of income. E.g., Income of minor child is to be clubbed with the income of his/her parent.

Section 60 to 64 of the Income-tax Act, contains various provisions relating to clubbing of income. The special provisions contained in these sections are designed to counteract the various attempts which an individual may make for avoiding or reducing his liability to tax by transferring his assets or income to other person(s) while,

at the same time, retaining certain powers or interest over the property or its income. The clubbing provisions are as under:

| <b>CLUBBING PROVISION'S</b>                                       |  |   |   |
|---|--|---|---|
| <b>Nature of Transaction</b>                                      | <b>Clubbed in the Hands of</b>   | <b>Conditions/Exceptions</b>  | <b>Relevant Reference</b>   |
| <b>Transfer of Income without transfer of Assets (Section 60)</b> | Transferor who transfers the income  | Irrespective of: <ol style="list-style-type: none"> <li>Whether such transfer is revocable or not.</li> <li>The transferor owns the assets.</li> <li>The income has been transferred without transfer of assets.</li> <li>Whether the transfer is effected before or after the commencement of Income Tax Act.</li> </ol>   | <ol style="list-style-type: none"> <li>Income for the purpose of Section 64 includes losses. [<i>P. Doriswamy Chetty</i> (SC)] [also see Expl. (2) to Section 64]</li> <li>Section 60 does not apply if corpus itself is transferred. [<i>Grandhi Narayana Rao</i> 173 ITR 593 (AP)]</li> </ol>   |
| <b>Revocable transfer of Assets (Section 61)</b>                  | Transferor who transfers the Assets<br><br>Assets includes both movable as well as immovable property whether situated in India or outside India | Clubbing not applicable if: <ol style="list-style-type: none"> <li>Trust/transfer irrevocable during the lifetime of beneficiaries/transferee; or</li> <li>Transfer made prior to 1-4-1961 and not revocable for a period of 6 years. Provided the transferor derives no direct or indirect benefit from such income in either case.</li> </ol> Examples of revocable transfers <ol style="list-style-type: none"> <li>If there is an express clause of revocation in the instrument of transfer; or</li> <li>If there is a sale with a condition of re-purchase; or</li> <li>If the transfer is to a trust and if the transfer can be revoked with the consent of two or more beneficiaries; or</li> <li>If the trustees are empowered in sole discretion to revoke the transfer; or</li> </ol> If the transferor has power to change beneficiary or trustees. | Transfer held as revocable <ol style="list-style-type: none"> <li>If there is provision to re-transfer directly or indirectly whole/part of income/asset to transferor;</li> <li>If there is a right to re-assume power, directly or indirectly, the transfer is held revocable and actual exercise is not necessary [<i>S. Raghbir Singh</i> 57 ITR 408 (SC)]</li> <li>Where no absolute right is given to transferee and asset can revert to transferor in prescribed circumstances, transfer is held revocable. [<i>Jyotendrasinhji vs. S.I. Tripathi</i> 201 ITR 611 (SC)]</li> </ol> |

| <b>CLUBBING PROVISION'S</b>  |   |  |  |
|--|---|--|--|
| <b>Nature of Transaction</b>   | <b>Clubbed in the Hands of</b>                  | <b>Conditions/Exceptions</b>   | <b>Relevant Reference</b>  |
| <p><b>Salary, Commission, Fees or remuneration paid to spouse from a concern in which an individual has a substantial interest [Section 64 (1) (ii)]</b></p> | <p>Individual who have substantial interest</p> | <p>Clubbing not applicable if: Spouse possesses technical or professional qualification and remuneration is solely attributable to application of that knowledge/ qualification.</p> <p><b>Substantial Interest:</b> An individual shall be deemed to have a substantial interest in a concern -</p> <p>(i) In a case where the concern is a company, if its shares (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) carrying not less than 20% of the voting power are, at any time during the previous year, owned beneficially by such person or partly by such person and partly by one or more of his relatives;</p> <p>(ii) In any other case, if such person is entitled, or such person and one or more of his relatives are entitled in the aggregate, at any time during the previous year, to not less than 20% of the profits of such concern.</p> <p><b>When both husband and wife have substantial interest</b></p> <p>Where both husband and wife have a substantial interest in the concern and both are in receipt of the remuneration in such concern, the remuneration from such concern is to be included in the total income of the husband or, as the case may be, the wife whose total income excluding the income referred to in that clause, i.e., 64(1)(ii) is greater; and where any such income is once</p> | <ol style="list-style-type: none"> <li>1. The relationship of husband and wife must subsist at the time of accrual of the income. [Philip John Plasket Thomas 49 ITR 97 (SC)].</li> <li>2. Income other than salary, commission, fees or remuneration is not clubbed under this clause.</li> </ol> |

| <b>CLUBBING PROVISION'S</b>  |  |   |  |
|--|--|---|--|
| <b>Nature of Transaction</b>   | <b>Clubbed in the Hands of</b>   | <b>Conditions/Exceptions</b>  | <b>Relevant Reference</b>  |
|  |  | included in the total income of either spouse, any such income arising in any succeeding year shall not be included in the total income of the other spouse unless the Assessing Officer is satisfied, after giving that spouse an opportunity of being heard, that it is necessary so to do.   |  |
| <b>Income from assets transferred directly or indirectly to the spouse without adequate consideration [Section 64(1) (iv)]</b>   | Individual transferring the Asset (subject to the provisions of clause (i) of Section) | Clubbing not applicable if: The assets are transferred; <ol style="list-style-type: none"> <li>1. With an agreement to live apart</li> <li>2. Before marriage</li> <li>3. Income earned when relation does not exist</li> <li>4. By Karta of HUF gifting coparcenary property to his wife. <i>L. Hirday Narain vs ITO 78 ITR 26 (SC)</i></li> <li>5. Property acquired out of pin money. <i>R.B.N.J. Naidu vs. CIT 29 ITR 194 (Nag.)</i></li> </ol> | <ol style="list-style-type: none"> <li>1. Income earned out of Income arising from transferred assets not liable for clubbed. [<i>M.S.S. Rajan 252 ITR 126 (Mad)</i>]</li> <li>2. Cash gifted to spouse and he/ she invests to earn interest. [<i>Mohini Thaper vs. CIT 83 ITR 208 (SC)</i>]</li> <li>3. Capital gain on sale of property which was received without consideration from spouse [<i>Sevential M. Sheth vs. CIT 68 ITR 503 (SC)</i>]</li> <li>4. Transaction must be real. [<i>O.N. Mohindroo 99 ITR 583 (Delhi)</i>]</li> </ol> |
| <b>Income from the assets transferred to son's wife [Section 64(1) (vi)]</b>   | Individual transferring the Asset  | The transfer should be without adequate consideration.  | Cross transfers are also covered [ <i>C.M. Kothari 49 ITR 107 (SC)</i> ]   |
| <p>For the purposes of clauses (iv) and (vi), where the assets transferred directly or indirectly by an individual to his spouse or son's wife (hereafter in this Explanation referred to as "the transferee") are invested by the transferee,—</p> <p>(i) in any business, such investment being not in the nature of contribution of capital as a partner in a firm or, as the case may be, for being admitted to the benefits of partnership in a firm, that part of the income arising out of the business to the transferee in any previous year, which bears the same proportion to the income of the transferee from the business as the value of the assets aforesaid as on the first day of the previous year bears to the total investment in the business by the transferee as on the said day;</p> |  |   |  |

| <b>CLUBBING PROVISION'S</b>  |  |   |  |
|--|--|---|--|
| <b>Nature of Transaction</b>   | <b>Clubbed in the Hands of</b>   | <b>Conditions/Exceptions</b>  | <b>Relevant Reference</b>  |
| <p>(ii) in the nature of contribution of capital as a partner in a firm, that part of the interest receivable by the transferee from the firm in any previous year, which bears the same proportion to the interest receivable by the transferee from the firm as the value of investment aforesaid as on the first day of the previous year bears to the total investment by way of capital contribution as a partner in the firm as on the said day,</p> <p>shall be included in the total income of the individual in that previous year.</p> |  |   |  |
| <b>Transfer of assets by an individual to a person or AOP for the immediate or deferred benefit of his Spouse or Son's wife</b><br><b>[Section 64(1) (vii) &amp; (viii)]</b>   | Individual transferring the Asset  | The transfer should be without adequate consideration   | 1. Transferor need not necessarily have taxable income of his own. [P. Murugesan 245 ITR 301 (Mad)]<br><br>2. Wife means legally wedded wife. [Executors of the will of T.V. Krishna Iyer 38 ITR 144 (Ker)]  |
| <b>Income of a minor child</b><br><b>[Child includes step child, adopted child and minor married daughter]</b><br><b>[Section 64 (1A)]</b>   | 1. If the marriage subsists, in the hands of the parent whose total income is greater; or;<br><br>2. If the marriage does not subsist, in the hands of the person who maintains the minor child; | Clubbing not applicable for: –<br><br>1. Income of a minor child suffering any disability specified u/s. 80U<br><br>2. Income on account of manual work done by the minor child<br><br>3. Income on account of any activity involving application of skills, talent or specialized knowledge and experience | 1. The parent in whose hands the minor's income is clubbed is entitled to an exemption up to Rs. 1,500 per child. [Section 10(32)]<br><br>2. Income once included in the total income of either of parents, it shall continue to be included in the hands of same parent in the subsequent year unless AO is satisfied that it is necessary to do so (after giving that parent opportunity of being heard) |
| <b>Income of HUF from property converted by the individual into HUF property</b><br><b>[Section 64(2)]</b>   | Income is included in the hands of individual & not in the hands of HUF  | Clubbing applicable even if the converted property is subsequently partitioned; income derived by the spouse from such converted property will be taxable in the hands of individual.   | Fiction under this section must be extended to computation of income also. [M.K. Kuppuraj 127 ITR 447 (Mad)]   |

**Practice Questions:****Illustration 1:**

A owns Debentures worth Rs 1,000,000 of ABC Ltd., (annual) interest being Rs. 100,000. On April 1, 2025, he transfers interest income to B, his friend without transferring the ownership of these debentures.

**Solution:** In this particular case during 2025-26, interest of Rs. 100,000 is received by B; it will be taxable in the hands of A as per Section 60.

**Illustration 2:**

Mr. X owns Debentures worth Rs 1,000,000 of ABC Ltd., (annual) interest being Rs. 100,000. On April 1, 2023, he transfers interest income to Mr. Y, his friend without transferring the ownership of these debentures.

**Solution:**

Although during 2025-26, interest of Rs. 100,000 is received by Mr. Y, it is taxable in the hands of Mr. X as per Section 60.

**Illustration 3:**

X has a substantial interest in A Ltd. and Mrs. X is employed by A Ltd. without any technical or professional qualification to justify the remuneration.

**Solution:**

In this case, salary income of Mrs. X shall be taxable in the hands of X.

**Illustration 4:**

Mr. P is employed as Public Relation Officer in a company where Mrs. P holds 21 per cent equity shares. She has been holding the share before marriage with Mr. P., Mr. P gets a salary of Rs. 1,500 per month.

**Solution:**

The whole salary of Rs. 18,000 will be included in the income of Mrs. P provided Mr. P has no technical or professional qualification. It is immaterial that the remuneration so paid is genuine and not excessive and that Mrs. P had substantial interest in the company even before her marriage.

**Illustration 5:**

X transfers 500 debentures of IFCI to his wife without adequate consideration.

**Solution:**

Interest income on these debentures will be included in the income of X.

**Illustration 6 & Solution:**

A transfers certain shares to his wife B. Dividends received on such shares are taxable in the hands of A. B sells the shares and makes some capital gains, such gains are also taxable in A's hands. Now from the dividend money, B purchases some more shares and receives dividends on these new shares, such dividends are not taxable to A. In the same way, if B receives certain bonus shares on the shares transferred by her husband and later on she receives dividend on such bonus shares, the dividend shall not be included in the income of the transferor because the bonus shares were never transferred by her husband.

**Illustration 7:**

Mr. Sharma invests Rs 10 lakh in a fixed deposit (FD) at a bank, in his wife's name. Interest of Rs. 1 lakh arises on this income. Mrs Sharma invests the interest on periodic basis and interest for an amount of Rs. 5,000 arises on the interest deposited by her in bank. Analyze the clubbing provisions and find out the taxability of interest accrued.

**Solution:**

Rs. 1 lakhs in the Now Interest income on FD will be clubbed with his (Mr. Sharma) income. Interest of Rs. 5,000 aroused out of Investment made by Mrs. Sharma will be taxed as her own income.

**Illustration 8:**

Red holds 40% of shares in a Company. Mrs. Red (a CS) is employed in the company as a Company Secretary and is getting salary of Rs. 15,000 per month. Compute total income and tax payable by Red and Mrs. Red assuming other income of Red is Rs. 2,00,000 from a business.

**Solution:**

In the present case, Mrs. Red's salary income will be taxable in her hands only as she is earning the same through her professional qualification.

**Computation of Total Income and Tax Liability**

| Particulars   | Mr. Red (Rs.) | Mrs. Red (Rs.) |
|---|---------------|----------------|
| Income from Salary  | Nil           | 1,80,000       |
| Income from Business  | 2,00,000      | Nil            |
| Gross Total Income (or Total Income)                        | 2,00,000      | 1,80,000       |
| Tax Liability (as total income does not exceed Rs.2,50,000) | Nil           | Nil            |

**Illustration 9:**

Mr. Amit is beneficially holding 21% equity shares of Essem Minerals Pvt. Ltd. Mrs. Amit is employed as Manager (in accounts department) in Essem Minerals Pvt. Ltd. at a monthly salary of Rs. 84,000. Mrs. Amit is not having any knowledge, experience or qualification in the field of accountancy. Will the remuneration (i.e., salary) received by Mrs. Amit be clubbed with the income of Mr. Amit?

**Solution:**

In this situation, Mr. Amit is having substantial interest in Essem Minerals Pvt. Ltd. and remuneration of Mrs. Amit is not justifiable (i.e., she is employed without any technical or professional knowledge or experience) and, hence, salary received by Mrs. Amit from Essem Minerals Pvt. Ltd. will be clubbed with the income of Mr. Amit and will be taxed in the hands of Mr. Amit.

**Illustration 10:**

Mr. Kapoor gifted Rs. 8,40,000 to his wife. The said amount is invested by his wife in debentures of a company. Will the income from the debenture purchased by Mrs. Kapoor from gifted money be clubbed with the income of Mr. Kapoor?

**Solution:**

Rs. 8,40,000 is transferred to spouse. Fund is transferred via gift (i.e., without adequate consideration) and, hence, the provisions of section 64(1)(iv) will be attracted. The provisions of clubbing will apply even if the form of asset is changed by the transferee-spouse.

In this case asset transferred is money and, subsequently, the form of asset is changed to debentures, hence, income from debentures acquired from money gifted by her husband will be clubbed with the income of her husband. Thus, interest on debenture received by Mrs. Kapoor will be clubbed with the income of Mr. Kapoor.

**Illustration 11:**

Mr. Raj has given a bungalow owned by him on rent. Annual rent of the bungalow is Rs. 84,000. He transferred entire rental income to his friend Mr. Kumar. However, he did not transfer the bungalow.

**Solution:**

In this situation, rent of Rs. 84,000 will be taxed in the hands of Mr. Raj.

**Illustration 12:**

Mr. Soham holds 8,400 debentures of Shyamal Minerals Ltd. He gifted these debentures to his wife. Will the income from debentures be clubbed with the income of Mr. Soham?

**Solution:**

In this situation, the debentures are transferred to spouse. Transfer is via gift (i.e., without any consideration) and, hence, income generated from the transferred asset, i.e., interest on such debentures will be clubbed with the income of Mr. Soham.

**Illustration 13:**

Mr. Raja has two minor children, viz., Master A and Master B. Master A is a child artist and Master B is suffering from diseases specified under section 80U. Income of A and B are as follows:

Income of A from stage shows: Rs. 1,00,000

Income of A from bank interest: Rs. 6,000

Income of B from bank interest: Rs. 1,20,000.

Will the income of minor children be clubbed with the income of their parent (Mrs. Raja is not having any income)?

**Solution:**

As per section 64(1A), income of minor children is clubbed with the income of that parent whose income (excluding minor's income) is higher. In this case, Mrs. Raja is not having any income and, hence, if any income is to be clubbed then it will be clubbed with the income of Mr. Raja.

Income of minor child earned on account of manual work or income from the skill, knowledge, talent, experience, etc., of minor child will not be clubbed with the income of his/her parent. Thus, income of A from stage show will not be clubbed with the income of Mr. Raja but income of A from bank interest of Rs. 6,000 will be clubbed with the income of Mr. Raja.

Income of a minor suffering from disability specified under section 80U will not be clubbed with the income of his/her parent. Hence, any income of B will not be clubbed with the income of Mr. Raja.

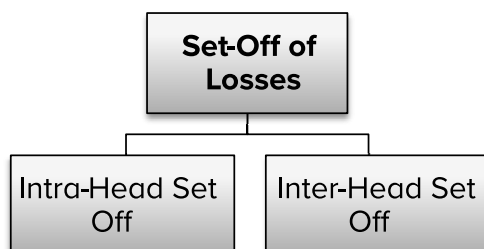
The taxpayer can claim an exemption under section 10(32)). Thus, in respect of interest income of Rs. 6,000 clubbed in the income of Mr. Raja, he will be entitled to claim exemption of Rs. 1,500 under section 10(32)), hence, net income to be clubbed will be Rs. 4,500 (i.e., Rs. 6,000 – Rs. 1,500).

## SET-OFF AND CARRY-FORWARD OF LOSSES

While one endeavors to derive income, the possibility of incurring losses cannot be ruled out. Based on the principles of natural justice, a set-off should be available for loss incurred. The income tax laws in India recognize this and provide for adjustment and utilization of the losses. For this purpose, the Income-tax Act, 1961 contains specific provisions (Sections 70 to 80) for the set-off and carry-forward of losses.

### SET-OFF OF LOSSES

Set off of losses means making adjust in losses which shall be against the profit of the same financial year. If it is not possible to set off the losses against profit in the same year then it will be carry forward to next year. A set off can be of two types which is intra-head set off and an inter-head set off.



- 1. Intra-Head Set Off:** If in any year the taxpayer has incurred loss from any source under a particular head of income, then he is allowed to adjust such loss against income from any other source falling under the same head. The process of adjustment of loss from a source under a particular head of income against income from other source under the same head of income is called intra-head adjustment, e.g. Adjustment of loss from business A against profit from business B.

#### Restrictions to be kept in mind while making intra-head adjustment of loss

|    |  |
|----|--|
| 1. | Loss from speculative business cannot be set off against any income other than income from speculative business. However, non-speculative business loss can be set off against income from speculative business. |
| 2. | Long-term capital loss cannot be set off against any income other than income from long-term capital gain. However, short-term capital loss can be set off against long-term or short-term capital gain.         |
| 3. | No loss can be set off against income from winnings from lotteries, crossword puzzles, race including horse race, card game, and any other game of any sort or from gambling or betting of any form or nature.   |
| 4. | Loss from the business of owning and maintaining race horses cannot be set off against any income other than income from the business of owning and maintaining race horses.                                     |

|    |  |
|----|--|
| 5. | Loss from business specified under section 35AD cannot be set off against any other income except income from specified business (section 35AD is applicable in respect of certain specified businesses like setting up a cold chain facility, setting up and operating warehousing facility for storage of agricultural produce, developing and building a housing projects, etc.). |
|----|--|

2. **Inter-Head Set Off:** After making intra-head adjustment (if any) the next step is to make inter-head adjustment. If in any year, the taxpayer has incurred loss under one head of income and is having income under other head of income, then he can adjust the loss from one head against income from other head, E.g., Loss under the head of house property to be adjusted against salary income.

#### Restrictions to be kept in mind while making inter-head adjustment of loss

|    |   |
|----|---|
| 1. | Loss from speculative business cannot be set off against any other income. However, non-speculative business loss can be set off against income from speculative business.  |
| 2. | Loss under head "Capital gains" cannot be set off against income under other heads of income.   |
| 3. | No loss can be set off against income from winnings from lotteries, crossword puzzles, race including horse race, card game, and any other game of any sort or from gambling or betting of any form or nature.  |
| 4. | Loss from the business of owning and maintaining race horses cannot be set off against any other income.  |
| 5. | Loss from business specified under section 35AD cannot be set off against any other income (section 35AD is applicable in respect of certain specified businesses like setting up a cold chain facility, setting up and operating warehousing facility for storage of agricultural produce, developing and building housing projects, etc.) |
| 6. | Loss from business and profession cannot be set off against income chargeable to tax under the head "Salaries".   |
| 7. | Loss under the head "house property" shall be allowed to be set-off against any other head of income only to the extent of Rs. 2,00,000 for any assessment year.  |
| 8. | Unabsorbed loss shall be allowed to be carried forward for set-off in subsequent years as per the existing provisions of section 71B.   |

#### CARRY-FORWARD OF LOSSES

Many times it may happen that after making intra-head and inter-head adjustments, still the loss remains unadjusted. Such unadjusted loss can be carried forward to next year for adjustment against subsequent year(s) income. Separate provisions have been framed under the Income-tax Law for carry forward of loss under different heads of income. Losses can be set-off against the income of following years provided that they have been suffered by assessee and determined in pursuance of a return filed by the assessee. Further, carry forward of losses (other than loss from house property and unabsorbed depreciation) is permissible if the return of income for the year, in which loss is incurred, is filed in time. The late filing of return should not impact the status of carry forward of loss of previous years.

| Loss under the Head   | Loss carried forward and Set-Off   | Loss can be carried forward only if the return of income/loss of the year in which loss is incurred is furnished on or before the due date of furnishing the return, as prescribed under section 139(1). | Loss can be carried forward upto |
|---|--|--|----------------------------------|
| <b>Loss from Non-Speculation Business</b>                           | If loss of any business/profession (other than speculative business) cannot be fully adjusted in the year in which it is incurred, then the unadjusted loss can be carried forward for making adjustment in the next year. In the subsequent year(s) such loss can be adjusted only against income charged to tax under the head "Profits and gains of business or profession"   | Applicable   | Eight Years                      |
| <b>Loss from Speculation Business</b>                               | If loss of any speculative business cannot be fully adjusted in the year in which it is incurred, then the unadjusted loss can be carried forward for making adjustment in the next year. In the subsequent year(s) such loss can be adjusted only against income from speculative business (may be same or any other speculative business).   | Applicable   | Four Years                       |
| <b>Loss from business specified under section 35AD</b>              | Loss from business specified under section 35AD cannot be set off against any other income except income from specified business (section 35AD is applicable in respect of certain specified businesses like setting up a cold chain facility, setting up and operating warehousing facility for storage of agricultural produce, developing and building a housing projects, etc.). Such loss can be carried forward for adjustment against income from specified business for any number of years. | Applicable   | Infinite Period                  |
| <b>Loss from the business of owning and maintaining race horses</b> | Loss from the business of owning and maintaining race horses cannot be set off against any income other than income from the business of owning and maintaining race horses.   | Applicable   | Four Years                       |
| <b>Loss under the head 'Income from House Property'.</b>            | If loss under the head "Income from house property" cannot be fully adjusted in the year in which such loss is incurred, then unadjusted loss can be carried forward to next year. In the subsequent years(s) such loss can be adjusted only against income chargeable to tax under the head "Income from house property".   | Not Applicable   | Eight Years                      |

|  |  |                |                 |
|--|--|----------------|-----------------|
| <b>Loss under the head Capital Loss</b>  | If loss under the head “Capital gains” incurred during a year cannot be adjusted in the same year, then unadjusted capital loss can be carried forward to next year. In the subsequent year(s), such loss can be adjusted only against income chargeable to tax under the head “Capital gains”, however, long-term capital loss can be adjusted only against long-term capital gains. Short-term capital loss can be adjusted against long-term capital gains as well as short-term capital gains.   | Applicable     | Eight Years     |
| <b>Unabsorbed depreciation, unabsorbed capital expenditure on scientific research and unabsorbed</b> | Depreciation is first deducted from the income chargeable to tax under the head “Profits and gains of business or profession”. If such depreciation could not be fully adjusted against such income chargeable to tax in that previous year, the unabsorbed portion shall be added to the amount of depreciation for the following year and shall be deemed to be the part of depreciation for that year(similar treatment would be given to other allowances as mentioned above). However, in the case of set off, following order of priority is to be followed: | Not Applicable | Infinite Period |
| <b>capital expenditure on promoting family planning amongst the employees</b>                        | <ol style="list-style-type: none"> <li>1) First adjustments are to be made for current scientific research expenditure, family planning expenditure and current depreciation.</li> <li>2) Second adjustment is to be made for brought forward business loss.</li> <li>3) Third adjustments are to be made for unabsorbed depreciation, unabsorbed capital expenditure on scientific research or on family planning.</li> </ol>   |                |                 |

### TREATMENT OF CARRY-FORWARD OF LOSSES OF CERTAIN ASSESSEES

#### (1) Carry forward of loss in case of change in the constitution of business

Generally, the person incurring the loss is only entitled to carry forward the loss to be adjusted in subsequent year(s). However, in certain cases of reconstitution of the business like amalgamation, demerger, conversion of proprietary firm into company or conversion of partnership firm into company, etc., the reconstituted entity is entitled to carry forward the unadjusted loss of predecessor entity (provided that conditions specified in this regard are satisfied).

#### (2) Carry-forward and set-off of losses in case of succession of business or profession

When a business or profession is succeeded by another person, the brought forward losses by the predecessor can be set-off against the income earned by the predecessor before the succession. The successor is not entitled to carry forward the losses sustained by the predecessor and set them off against the income earned by him. However, there is exception. If the succession is by inheritance, the heir-at-law is entitled to carry-forward and set-off the losses sustained by the predecessor provided the business in question continues to be carried on by the successor.

**(3) Carry-forward and set-off of losses in case of change in constitution of firm or on succession [Section 78]**

Section 78 contains provisions relating to carry forward and set off of loss in case of change in constitution of a partnership firm due to death or retirement of a partner (i.e. when a partner goes out of firm by retirement or death). In such a case, the share of loss attributable to the outgoing partner cannot be carried forward by the firm. Restriction of section 78 is applicable only in case of loss and is not applicable in case of adjustment of unabsorbed depreciation, unabsorbed capital expenditure on scientific research or family planning expenditure.

**(4) Special provisions relating to carry forward and set-off of losses in case of change in shareholding of certain companies [Section 79]**

Section 79 of the Income-tax Act, 1961 provides for carry forward and set-off of losses where a change in shareholding has taken place in a previous year in case of following companies

- (i) In case of a company, being a company in which the public are not substantially interested but not being an eligible start-up as referred to in section 80-IAC, no loss incurred in any year prior to the previous year in which change in shareholding has taken place shall be carried forward and set off against the income of the previous year, unless on the last day of the previous year, the shares of the company carrying not less than 51% of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than 51% of the voting power on the last day of the year or years in which the loss was incurred.
- (ii) In case of a company, being a company in which the public are not substantially interested and an eligible start-up as referred to in section 80-IAC, the loss incurred in any year prior to the previous year in which change in shareholding has taken place, shall be allowed to be carried forward and set off only if all the shareholders of the company who held shares carrying voting power on the last day of the previous year in which the loss was incurred, continue to hold shares on the last of the current year. Further, the loss should have been incurred during the period of 10 years beginning from the year in which the company is incorporated.

However, to facilitate ease of doing business in case of an eligible start-up, the Finance (No.2) Act, 2019 has amended section 79 to provide that loss incurred, by the closely held eligible start-up, shall be allowed to be carried forward and set off against the income of the previous year on satisfaction of either of the two conditions specified above, i.e., continuity of 51% shareholding or continuity of 100% of original shareholders. [w.e.f. Assessment Year 2020-21]

However, the provisions of section 79 shall not apply in following cases. In other words, there shall be no restriction on carry forward and set-off of losses if :

- a) the change in shareholding takes place consequent upon the death of a shareholder or on account of transfer of shares by way of gift to any relative of the shareholder making such gift.
- b) the assessee is a subsidiary of a foreign company and the foreign holding company is amalgamated or merged with another foreign company subject to condition that 51% shareholders of the amalgamating or demerged foreign company continue to be the shareholders of the amalgamated or the resulting foreign company.
- c) the change in shareholding take place in the previous year pursuant to approved resolution plan under the Insolvency and Bankruptcy Code, 2016 after affording a reasonable opportunity of being heard to the jurisdictional Principal CIT or CIT.

- d) A company, and its subsidiary and the subsidiary of such subsidiary, where:
  - i. National Company Law Tribunal (NCLT), on a petition moved by the Central Govt., has suspended the board of directors of such company and has appointed new directors.
  - ii. Change in shareholding has taken place in a previous year pursuant to a resolution plan approved by the NCLT.
- e) Change in the shareholding has taken place during the previous year on account of relocation referred to in the Explanation to clauses (viiac) and (viiad) of section 47.
- f) the ultimate holding company of such erstwhile PSU, immediately after completion of the strategic disinvestment, continues to hold, directly or through its subsidiary or subsidiaries, at least 51% of the voting power of such PSU in aggregate.

**(5) No set-off of loss against undisclosed income discovered during search**

The Finance Act, 2022 has inserted a new section 79A to the Income-tax Act to restrict set off of losses consequent to search, requisition and survey. It has been provided that in case the total income of any previous year of an assessee includes any undisclosed income detected as a result of: (a) Search initiated under section 132; or (b) A requisition made under section 132A; or (c) A survey conducted under section 133A other than under section 133A(2A). Then, no set-off of any loss, whether brought forward or otherwise, or unabsorbed depreciation, shall be allowed against such undisclosed income while computing the total income of the assessee for such previous year.

**PRACTICE QUESTIONS**

1. If income from a particular source is exempt from tax, then loss from such source cannot be set off against any other income which is chargeable to tax.
  - (a) True
  - (b) False

Answer: (a) True
2. The process of adjustment of loss from a source under a particular head of income against income from other source under the same head of income is called \_\_\_\_\_.
  - (a) Inter-head adjustment
  - (b) Intra-head adjustment
  - (c) Carry forward of loss
  - (d) Clubbing of income

Answer: (b) Intra-head adjustment
3. While making intra-head adjustment of loss, short-term capital loss cannot be set off against long-term capital gain.
  - (a) True
  - (b) False

Answer: (b) False
4. While making intra-head adjustment, loss from the business of owning and maintaining race horses can be set off against
  - (a) Income from winnings from lotteries

- (b) Income from crossword puzzles \_\_\_\_\_ only.
- (c) Income from business of owning and maintaining race horses
- (d) Income from card game

Answer: (c) Income from business of owning and maintaining race horses

5. While making inter-head adjustment of loss, loss from business and profession cannot be set off against income chargeable to tax under the head "Salaries".
- (a) True
  - (b) False

Answer: (a) True

6. Loss under the head "Profits and gains of business or profession" can be carried forward even if the return of income/loss of the year in which loss is incurred is not furnished on or before the due date of furnishing the return, as prescribed under section 139(1).
- (a) True
  - (b) False

Answer: (b) False

7. If loss under the head "Income from house property" cannot be fully adjusted in the year in which such loss is incurred, then unadjusted loss can be carried forward for \_\_\_\_\_ years immediately succeeding the year in which the loss is
- (a) 2
  - (b) 5
  - (c) 8
  - (d) 10

Answer: (c) 8

8. In case of a Company, being a company in which public are not substantially interested but not being an eligible start-up as referred to in section 80-IAC, if the person beneficially holding \_\_\_\_\_ of the voting power as on the last day (i.e. 31st March) of the year in which the loss was incurred and on the last day (i.e. 31st March) of the year in which the company wants to set off the brought forward loss are different, then the company cannot set off such brought forward loss.
- (a) 20%
  - (b) 25%
  - (c) 50%
  - (d) 51%

Answer: (d) 51%

#### LESSON ROUND-UP

- Sections 60 to 64 of the Income-tax Act provide that in computing the total income of an individual for the purposes of assessment, there shall be included all the items of income specified in these sections.

- **Transfer of Income (Section 60):** Where a person transfers to any other person income (whether revocable or not) from an asset without transferring that asset, the income shall be included in the total income of the transferor. "Transfer" includes any settlement, trust, covenant, agreement or arrangement.
- **Revocable Transfer:** Where a person transfers any asset to any other person with a right to revoke the transfer, all income accruing to the transferee from the asset shall be included in the total income of the transferor. The income under revocable transfer of asset shall be included in the income of transferor even when only a part of income from transferred asset has been applied for the transferor.
- **Irrevocable Transfer:** In case of an irrevocable transfer of assets for a specified period, the income from such assets shall not be included in the income of transferor.
- **Income to spouse from a concern in which such individual has substantial interest [Section 64(1)(ii)]:** All such income as arises directly or indirectly, to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual has a substantial interest, shall be included in the income of the individual.
- **Income to spouse from the assets transferred [Section 64(1)(iv)]:** Where any individual transfers directly or indirectly any asset (other than a house property) to the spouse, the income from such asset shall be included in the income of the transferor.
- **Income to Son's Wife [Section 64(1)(vi)]:** Where any individual transfers, directly or indirectly, any asset to his/her son's wife without adequate consideration, the income from such asset shall be included in the income of the transferor.
- **Transfer for Immediate or Deferred Benefit of Son's Wife [Section 64(1)(viii)]:** Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly after June 1, 1973, otherwise than for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is for the immediate or deferred benefit of his son's wife be included in computing the total income of such individual.
- **Income to spouse through a third person [Section 64(1)(vii)]:** Where a person transfers some assets directly or indirectly to a person or association of persons (trustee or body of trustees or juristic person) without adequate consideration for the immediate or deferred benefit of his or her spouse, all such income as arises directly or indirectly from assets transferred shall be included in the income of the transferor.
- **Clubbing of Income of Minor Child [Section 64(1A)]:** All income which arises or accrues to the minor child (not being a minor child suffering from any disability of the nature specified in Section 80U) shall be clubbed in the income of his parent. However, any income which is derived by the minor from manual work or from any activity involving application of his skill, talent or specialised knowledge and experience will not be included in the income of his parent.
- In case the income of an individual includes any income of his minor child in terms of this section [i.e. section 64(1A)], such individual shall be entitled to exemption of the amount of such income or Rs. 1,500 whichever is less.
- **Income from the Converted Property [Section 64(2)]:** Where an individual, being a member of Hindu Undivided Family, transfers his self-acquired property after 31st December, 1969 to the family for the common benefit of the family, or throwing it into the common stock of the family, or transfers it directly or indirectly to the family otherwise than for adequate consideration, such property is known as converted property.

- **Set Off & Carry Forward of losses:** Sometimes the assessee incurs a loss from a source of income and unless such loss is set-off against any income, the net result of the assessee's activities during the particular accounting year cannot be ascertained and consequently the tax payable would also be incapable of determination. For this purpose, the Income-tax Act contains specific provisions for the set-off and carry-forward of losses.
- **Carry-Forward and Set-Off of Losses:** If it is not possible to set-off the losses during the same assessment year in which these occurred, so much of the loss as has not been so set-off out of the following losses, can be carried forward to the following assessment year and so on to be set-off against the income of those years provided the losses have been determined in pursuance of a return filed by the assessee and it is the same assessee who sustained the loss.

### TEST YOURSELF

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.)*

#### Multiple Choice Questions "MCQs"

1. Income of a minor child from a Fixed Deposit with a bank, made out of income earned from scholarship, is to be?
  - a) Assessed in the hands of the minor child
  - b) Clubbed with the income of the parent whose total income before such clubbing is higher
  - c) Exempted from tax
  - d) Clubbed with father's income

Answer: (b)

2. Carried forward losses of normal business can be set-off against other income in subsequent assessment year except:
  - a) Income from speculation business
  - b) Income under the head house property
  - c) Income under the head other sources
  - d) Income under the head salaries

Answer: (d)

3. Transfer of income without transfer of asset would be taxable in the hands of:
  - a) Transferor only
  - b) Transferee only
  - c) Either transferor or transferee
  - d) Both transferor and transferee

Answer: (a)

4. The maximum period for which losses from speculative business can be carried forward is:
  - a) 4 years
  - b) 8 years

- c) Indefinitely
- d) None of the above

Answer: (a)

5. Income of Minor Child, includible in the income of his/her parents income, deductible to the extent of such income does not exceeds for each minor child:
- a) Rs. 500
  - b) Rs. 1000
  - c) Rs. 1500
  - d) Rs. 2000

Answer: (c)

6. Unabsorbed depreciation which could not be set off in the assessment year in which it arose, can be carried forward for:
- a) 8 Years
  - b) Indefinite Period
  - c) 4 Years
  - d) 12 Years

Answer: (b)

7. Loss from the activity of owning and maintaining race horses can be set off against \_\_\_\_\_ of the same assessment year.
- a) Speculation profits
  - b) Specified business profits
  - c) Any business profits
  - d) Income from owning and maintaining race horses

Answer: (d)

8. Loss from specified business under Section 35 AD can be carried forward for :
- a) 8 Years
  - b) Infinite Period
  - c) 4 Years
  - d) 12 Years

Answer: (b)

9. If the loss from business is Rs. 20,000 and income under the head salary is Rs. 2,40,000 then total income of assessee is:
- a) Rs. 2,40,000
  - b) Rs. 2,20,000
  - c) Rs. 2,40,000 and carry forward loss of Rs. 20,000
  - d) Rs. 2,40,000 and no carry forward loss

Answer: (c)

**Practical Questions:**

1. Mr. Sharma gifted his wife Rs 5,00,000. The wife invests this amount in a FD and starts earning an interest on the same. Will this interest income be taxable in the hands of Mr. Sharma? Give reasoning to support the answer.
2. Mr Chandra Babu holds 25% equity shares of Heritage Minerals Pvt. Ltd. His wife – Smt Bhuvaneshwari is employed as Manager (*in Sales department*) in the same company, at a monthly salary of Rs. 90,000. Bhuvaneshwari is not having any knowledge, experience or qualification in the field of Sales. Will the remuneration (*i.e.*, salary) received by Bhuvaneshwari be clubbed with the income of Mr. Babu? If yes, give reasoning to support the answer.
3. Mr. Suresh (transferor) gifts Rs. 1 crore to his wife Swapna (transferee). The said amount is invested by his wife in a house property. Will the rental income (if any) from the house property purchased by Swapna Suresh from gifted money be clubbed with the income of Mr. Suresh. Give reasoning to support the answer.
4. Mr. Pawan Kalyan has given a bungalow owned by him on rent. Annual rent of the bungalow is Rs. 10,00,000. He transferred entire rental income to his friend Mr. Trivikram. However, he did not transfer the bungalow. In whose hand the rental income of Rs. 10,00,000 will be taxed. Give reasoning to support the answer.

**LIST OF FURTHER READINGS**

- **Direct Taxes Law and Practice**  
**Author :** Dr. Vinod K. Singhania & Dr. Kapil Singhania  
**Publisher :** Taxmann
- **Direct Taxes Ready Reckoner with Tax Planning**  
**Author :** Dr. Girish Ahuja & Dr. Ravi Gupta  
**Publisher :** Wolters Kluwer

**OTHER REFERENCES (INCLUDING WEBSITES AND VIDEO LINKS)**

- **Income Tax Act, 1961:** <https://www.incometaxindia.gov.in/Pages/acts/income-tax-act.aspx>
- **Income Tax Rules, 1962:** <https://www.incometaxindia.gov.in/Pages/rules/income-tax-rules-1962.aspx>
- **Circulars:** <https://www.incometaxindia.gov.in/Pages/communications/circulars.aspx>
- **Notifications:** <https://www.incometaxindia.gov.in/Pages/communications/notifications.aspx>