Tax Talk: Know how to set off and carry forward capital losses

Long-term capital loss can be set off only against long-term capital gain

Equity shareholders can set off stock market losses against gains and carry forward any residual losses to subsequent financial years to lower their tax liability. Capital losses incurred from the sale of shares or mutual funds cannot be reported against the head ‘salary income’.

Gains or losses made from stock market investments are categorised as capital gains/losses, business income/loss, and speculative income/loss. Based on these types of transactions, any income from stock market deals may be taxed as capital gains on investment or as profits and gains from a business or profession.

Income is further divided into long-term capital gains (LTCG) and short-term capital gains (STCG). STCG are taxed at 15% regardless of your tax bracket if equity shares listed on a stock exchange are sold within 12 months of purchasing. The buyer may realise a STCG or face a STCL as a result.

Adjusting capital losses and capital gains

The capital loss can be adjusted on LTCG or STCG for the next eight assessment years. Equity share sales that result in any STCL may be offset by equity asset sales that result in either STCG or LTCG. It can be offset by any STCG or LTCG under the head ‘other sources of income’ if the shareholder fails to set off his or her entire capital loss in the same assessment year, as per Section 35AD.

In case of LTCG or LTCL where the holding period is more than 12 months, the LTCG is taxed at 10% without the benefit of indexation in case of sale of listed securities and it exceeds `1,00,000 under Section 112A. Whereas in the case of capital loss, it can be adjusted against LTCG for eight years.

In the case of intra-day trading, where the shares are bought and sold on the same day, the capital gains made are treated as speculative business income and are taxable as per your applicable tax slab rates, and any capital loss made can only be set off against speculative income for four years.

Carry forward losses

To carry forward losses to the following eight assessment years, the taxpayer needs to file his or her ITR on time as per Section 139(1). As per the Income Tax Act, 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).

It is crucial to remember that only LTCG may be offset by LTCL. However, a STCL can be offset by LTCG or STCG, but a loss under the ‘capital gains’ head cannot be offset against income under the head ‘income from other sources’.

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