

TAX FLASH NEWS

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Rental loss from a hotel unit in US and share of loss in US LLCs are treated as 'income from other sources', eligible for set-off against salary income in India

Recently, the Delhi Bench of Income-tax Appellate Tribunal (the Tribunal) in the case of Rohit Kapur¹ (the taxpayer) held that the rental loss from a hotel unit in the US and share of loss in the US Limited Liability Companies (LLCs) are in the nature of 'income from other sources' and not business losses. The taxpayer never intended to run a hotel unit and had not been engaged in running the hotel unit on his own. Thus, the hotel unit cannot be considered to be a business undertaking of the taxpayer. Further the taxpayer by virtue of being the whole-time employee director in an oil exploration company, could not have made the capital outlay in the foreign LLCs for the purpose of business. It was only for the purpose of an investment.

Thus, the Tribunal held that both the losses were in the nature of 'income from other sources' and therefore, the taxpayer was eligible to set-off such losses with the salary income in India.

Facts of the case

The taxpayer is the whole-time managing director of an oil exploration company. During the Assessment Year (AY) 2016-17, apart from salary from the whole-time directorship, the taxpayer had also earned income from other sources within India and he has also disclosed income from sources outside India in the nature of rental income (loss) and income from transactions in financial securities.

The taxpayer is the owner of one unit of hotel in US on which he incurred loss and claimed the said loss under the head 'income from other sources' and sought to set-off the loss against the salary income of the same year. The taxpayer also claimed share of loss from two LLCs in the US as income from other sources.

However, the Assessing Officer (AO) considered the loss from the unit held in hotel and share of loss from the LLCs as business loss. The AO observed that the

taxpayer was doing business as partner in the LLCs and, therefore, the resultant income or loss was to be booked under the head 'business income' and not income from other sources.

Tribunal's decision

Treatment of loss arises from hotel unit located in US

The Supreme Court in the case of Sultan Brothers Pvt Ltd.² dealt with an issue of whether a particular income was covered under the head 'income from business or profession' or 'income from other sources'. In that case, the taxpayer had constructed a building fully furnished and had let out the same to another person for the use as a hotel. The taxpayer never carried on the business of the hotel in the premises let out and there was nothing to show that it intended to carry on the hotel business itself. The building, the furniture and plants, etc. were all let out for running the hotel and were inseparable from each other. In view of these facts, the Supreme Court held that the income was to be assessed as 'income from other sources'.

In the present case, the taxpayer was not intending to run a unit in hotel himself but rather he had purchased the unit while he was employed with a company in US. The taxpayer had not been engaged in running the hotel unit on his own. Thus, the hotel unit cannot be considered to be a business undertaking of the taxpayer.

The Supreme Court in the case of Radha Soami Satsang³ held that the tax department cannot disturb and alter issues which have already been settled in previous years if there is no change in the facts and circumstances. Accordingly, loss arose from the unit in hotel was treated as income from other sources.

¹ Rohit Kapur v. ACIT - [ITA No. 9016/Del/2019, AY- 2016-17] - Taxsutra.com

² Sultan Brothers Pvt Ltd. v. CIT [1964] 51 ITR 353 (SC)

³ Radha Soami Satsang v. CIT [1992] 193 ITR 32 (SC)

Treatment of share of loss arises from LLCs situated in the U.S.

The taxpayer by virtue of being the whole-time employee director in an oil exploration company, could not have made the capital outlay in the two LLCs for the purpose of business. Apparently, this was only for the purpose of an investment. The lower authorities have failed to appreciate that in the case of outlays of this nature, it is important to determine as to whether the investment was in the realm of business or not. In the preceding AYs, the investment of this nature has consistently not been treated as business. Therefore, on the ground of consistency, the impugned loss should have been treated as loss under other sources.

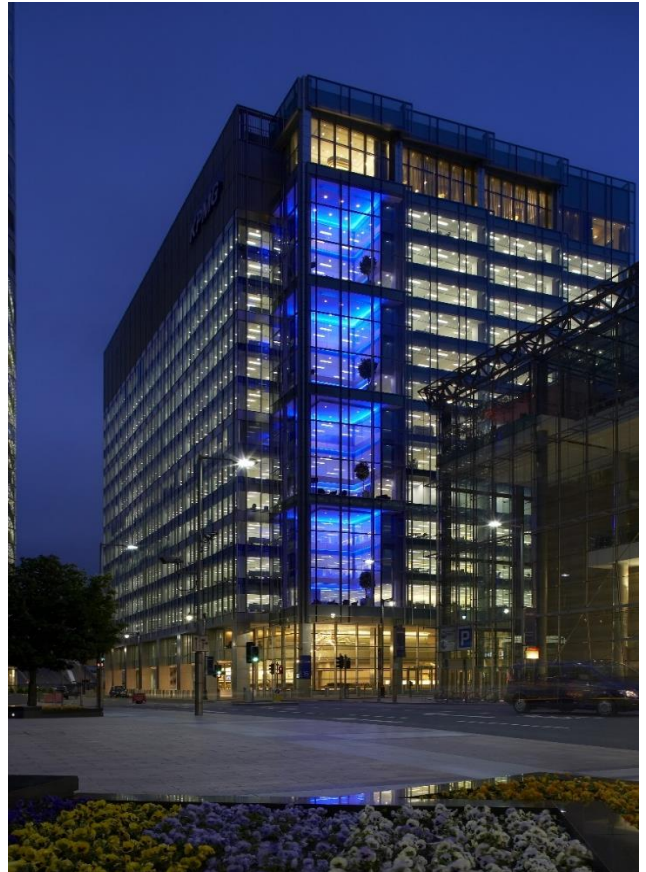
There is no foundation for the AO to treat the above losses as business losses. Accordingly, set-off of losses was allowed to the taxpayer.

Our comments

The characterisation of income/losses under the head 'business income' or 'income from other sources' has been a subject matter of debate before Courts/Tribunal.

The Jaipur Tribunal in the case of Vikram Golecha⁴ held that since primary intention of taxpayer was to exploit property as a commercial centre and services rendered by the taxpayer to occupants were result of activities carried on continuously in an organised manner with a set purpose and with a view to earn profits, service charges were treated as 'business income'.

In the present case, the Tribunal observed that rental loss from a hotel unit and share of loss in foreign LLCs are to be assessed under the head 'income from other sources' and not as 'business income'. Therefore, the taxpayer was allowed to set-off such losses with the salary income in India.



⁴ Vikram Golecha v. DCIT [2010] 123 ITD 438 (Jaipur)

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