

Taxation of Future and Options – A Bird's Eye View



INTRODUCTION

Derivative Trading i.e. trading in future and options (F&O) on stocks, currencies, and commodities has become a hot topic amongst investors. Data suggest that during last two years during pandemics the trading in shares & derivative increased substantially.

Derivatives: Derivative are the instrument the value of which derives its value from the underlying assets/securities. Future & Option are two kinds of derivatives available for trading in stock market.

NATURE OF INCOME, CAPITAL GAIN OR BUSINESS INCOME ?

Generally, income derived from sale of shares & securities are considered as capital gain either Long Term Capital Gain (LTCG) or Short Term Capital Gain (STCG). However, gain/loss from F&O are not considered as Capital Gain/loss rather considered as business income and treated accordingly.

SPECULATIVE OR NON-SPECULATIVE

As per Guidance Note Issued by ICAI on Tax Audit U/s 44AB, A speculative transaction means a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips. So, premia facia F&O looks like speculative in nature as generally they are settled otherwise then by actual delivery.

As Section 43(5) of the Income Tax Act states that any transactions that take place during Futures and Options trading through recognized stock exchange are deemed to be non-speculative transactions and accordingly any profits/loss from such trading would be treated in the same manner as profits/loss from any other business.

RED FLAGS FOR SALARIED PERSON

As per Section 115 BAC of the Income Tax Act, Salaried person can switch between new & old tax regime every year at time of filling of Return. However, the person with business income can exercise this option only once & option once exercised shall continue for that year and all subsequent years. So, if salaried person trading in F&O then he should keep this in mind and choose the tax option wisely else in future they will be ends-up paying higher tax.

How to Compute Turnover:

The turnover in case of F&O transaction to be computed as below:

- (i) The total of favourable and unfavourable differences (Profit/Loss) shall be taken as turnover.
- (ii) Premium received on sale of options is also to be included in turnover.
- (iii) In respect of any reverse trades entered, the difference thereon, should also form part of the turnover.

Please note whether the difference is profit or loss it will not make any difference, and all the difference aggregated to compute the turnover.

We can understand with the given example below:

- 1) Bought 1 lot of RIL future having lot size of 500 shares @ Rs.2,000/- and sold at Rs. 2,100/- (Future Transaction).
- 2) Bought 1 Lot of TCS future having lot size 700 share @ Rs. 3200/- and sold at 3,150/- (Future Transaction).
- 3) Bought 1 lot of call option 500 shares of Maruti for Rs. 80 & sold at Rs. 100 (Call Option).
- 4) Sold 1 lot of put Option, lot size 500 share of Tata Motors for Rs 45 and latter on purchased at Rs.50.

In the above example Turnover would be Rs. 1,70,000/- as worked out below:

Script Name	Transaction Type	Lot Size	Purchase Value	Sales Value	Gian / Loss	Turnover
RIL	Future	500	2,000	2,100	50,000	50,000
TCS	Future	700	3,200	3,150	35,000	35,000
Maruti	Option	500	40,000	50,000	10,000	60,000
Tata Motors	Option	500	25,000	22,500	2,500	25,000
Total			70,200	77,750	22,500	1,70,000

CAN WE CLAIM EXPENSES AGAINST F&O INCOME ?

As F&O income is considered as business income so we can claim expenses incurred to earn such income as deduction from F&O (business) Income such as STT, Brokerage, electricity charges, internet expenses, etc. However, onus is on the assess to prove that these expenses are incurred to earn such business income.

CARRY FORWARD & SET-OFF OF THE LOSSES

As F&O income is considered as business income so it can be set-off against other business income, house property Income capital gain and other source income. Any unadjusted loss can be carried forward for eight years. However, in the future, they can only be adjusted from non-speculative income.

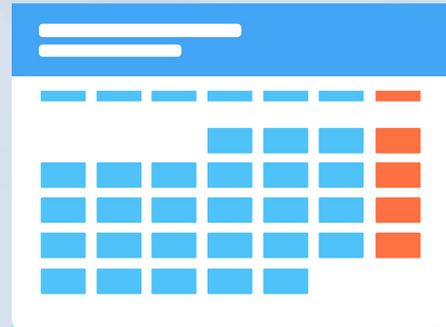
TAX AUDIT REQUIREMENT ?

As F&O transactions are considered as business income so if turnover worked out as described above, exceeds the Tax Audit limit of Rs. 1 crore or 5 crore as specified U/s 44AB of the Income Tax Act Tax Audit needs to be done. Limit of Rs. 5 crores have been further extended to Rs. 10 Crore for FY 2021-22 in case when cash receipt and payment made during the year does not exceed 5% of total receipt or payment, as the case may be. F&O transactions are traded electronically so generally extended limit of 5Cr./10 Cr. applicable for Audit purpose.

44AD APPLICABILITY

Under Section 44AD of presumptive taxation, small taxpayers with less than 2 crores of turnover are not required to maintain books of accounts and their profits are presumed to be 8% or 6% of their turnover. Even though F&O income are considered as business income as per our view 44Ad can't be availed in case of F&O income. As these transactions executed through recognized stock exchange and the stockbroker maintain records of the same & report the details of F&O transaction executed through them to the department, so if assess declare the different income in ITR it will be tracked, and department will issue notice for that. As records of every single transactions are maintained in actuality so we can't opt for 44AD. However other person may have different opinion and even some website suggest to claims 44AD.

COMPLIANCE CALENDER JULY 2021



GST	
GSTR 3B JULY 2021(Turnover in the previous financial year more than Five Crores)	20-08-2021
GSTR 3B JULY 2021 (Others)	22-08-2021
GSTR 1 JULY (Turnover more than Rs. 1.5 Crores)	11-08-2021
Income Tax	
Deposit of TDS	07-08-2021
ESI	
Payment for the month of JULY 2021	15-08-2021
PF	
Payment for the month of JULY 2021	15-08-2021
Return Filing for the month of JULY 2021	25-08-2021