CHAPTER 04 House Property

Charging Section [Sec 22]

'Annual value' of any **house property** which is owned by the **assessee** is taxable u/h 'Income from HP. House property shall include **all types of house properties** [i.e. residential houses, shops, godowns, cinema building, workshop building, hotel buildings etc].

Income from Renting of House Property	Taxable u/h 'House Property'.
Income from Sale of House Property	Taxable u/h 'Capital Gains'.

Analysis of Sec 22

I. **Property should consist of any Building or/& Land attached (appurtenant) thereto.**

- Land appurtenant means land connected with the building [Ex: Garden, Garage, Parking, Marriage halls with gardens]
- Letting out of vacant land → Taxable u/h **IFOS** [as No Building]
- Subletting of House Property → Taxable u/h **IFOS** [as No Ownership]

II. **Assessee must be the owner of the rented House Property**

- Registration of the sale deed → Not necessary.[thus, includes also a beneficial owner]
- Ownership includes both free-hold & lease-hold rights.
- Ownership includes deemed ownership (Discussed in Section 27 later).
- Ownership of land on which the building stands is not necessary. [Land may be on lease].
- **House Property with Disputed Title of Ownership**: It will be the decision of Income-tax Department as to who is the owner till the court gives its decision on such property. Generally beneficial owner considered to be actual owner.

III. **Purpose**

- HP may be used for any purpose by the owner (other than for his business/profession).
- Since section 30 of PGBP does not allow deduction of 'notional rent" of the property while computing business income u/h PGBP.

House Property Held as Stock in Trade (SIT)

- ✓ If house property constitutes SIT of a business, rental income from such house property is to be taxed u/h 'Income from House Property'. [Since specific head has been given for income from house property, it cannot be taxed under any other head].
- ✓ **HP held as SIT → Annual value = NIL for 2 years** from the end of FY in which completion certificate is obtained from competent authority, if such property is not LOP during such period. [Sec 23(5)]

Note: Rental Income earned by an assessee engaged in the business of letting out of properties on rent would be taxable as Business Income. [SC ruling in Rayala Corporation (P) Ltd. v. Asstt. CIT (2016) 386 ITR 500] .

Ex: If a Public school has let out a part of its building to a Bank, in this case rent received shall be considered to be income u/h "PGBP" & all the expenses of such house property shall be debited to profit & loss account.

Meaning of Certain Terms: -

- ✓ Fair Rent: - Rent of similar type of buildings in the same locality.
- ✓ Municipal Valuation: - Rental value determined by municipality for the purpose of charging municipal tax (House Tax, Property Tax)
- ✓ Standard Rent: Highest possible rent recovered by owner from tenant as per Rent Control Act.

Steps to Compute "Income from House Property".

A. Gross Annual Value (GAV) {Computed as per Sec 23}	xxx
B. Less: Municipal tax actual paid by the owner {Proviso to Sec 23(1)}	(xxx)
C. Net Annual Value (NAV) [A – B]	Xxx
D. Less: Deduction u/s 24	(xxx)
24(a): Standard deduction (30% of NAV)	(xxx)
24(b): Interest on borrowed Capital	(xxx)

A. Determination of Gross Annual Value [Sec 23]

1. Compare <u>Municipal Value</u> or <u>Fair Rent</u> **Select Whichever is higher**, ↑

   Now Compare <u>this higher figure</u> or <u>Standard Rent</u> **Select Whichever is lower** ↓

   Ans will be **Expected Rent (ER).**

2. Calculate Actual Rent Received (ARR) = Rent Received + Rent receivable - Unrealized Rent.

3. GAV = Higher of ER or ARR ↑

✓ **<u>Unrealized Rent</u>** → House was let out, but rent could not be recovered from tenant.

✓ **<u>Vacancy Loss</u>** → Loss of rent because house property remained vacant during such period.

Computation of GAV for Different Types of House Properties

1. **Self-occupied/unoccupied House Property**

   GAV = Nil for Any 2 Houses [Only for Ind/HUF].

   No deduction of Municipal taxes paid by the owner. Property in India or outside India.

2. **Property Let out for whole year**

   GAV = Higher of **ER** or **ARR**.

   No Question of vacancy since property was occupied for whole year.

3. **Let out Property vacant for a part of year.**

   ER shall be calculated for whole year. While computing ARR, rent for the period for which the house was vacant shall be excluded.

   If ARR > ER, GAV = ARR

   If ARR < ER due to vacancy, GAV = ARR

   If ARR < ER due to other reason, GAV = ER OR ER – Loss due to vacancy

4. **Let out for part & self-occupied for part of year (Time wise) (Let-out for even 1 day).**

   ER shall be calculated for the whole year.

   ARR shall be computed for let out period.

   GAV = Higher of (i) ER (for whole year) or (ii) ARR (for let out part). Full M.tax allowed.

5. **More than 2 SOP / Deemed Let out property.**

   If Assessee is having more than 2 houses & he is using all of them for himself, he has the option to choose any 2 houses as SOP & other houses will be deemed to be let out.

   GAV of DLOP → ER, bec. there is no rent since both HPs are SOP. Intt allowed unlimited.

   GAV of SOP = Nil.

6. **Single House – One portion is let out & another portion is self- occupied (Area Wise).**

For SOP → GAV = Nil; No deduction of Municipal taxes paid.

For LOP → ER shall be computed on proportionate basis. Actual rent always for LOP.

There is no requirement to regard the property as a single property.

B. Municipal Taxes {Proviso to Sec. 23(1)}

✓ Municipal taxes are to be deducted from GAV if both the following condition satisfied:

(a) Municipal taxes have been borne by the owner &

(b) they have been **actually paid** during PY.

Points to Remember:

✓ Municipal Taxes are allowed as deduction in PY of payment even if they relate to past years.

✓ Municipal Taxes levied by foreign local auth. → Deductible if such taxes are paid by owner.

✓ Refund of Municipal Tax Paid → Not taxable.

✓ If Municipal taxes are borne by tenant, rent received/receivable should not be increased to calculate rent since it is the duty of occupier of HP (i.e. tenant) to pay the municipal taxes.

✓ If municipal taxes are given on % age basis then it should be calculated on municipal value.

Also known as: - House Tax, Property Tax, Local Tax etc.

✓ Municipal tax includes water tax, sewerage tax, Fire tax etc.

C. Net Annual Value [NAV]

✓ NAV = GAV - Municipal Taxes paid & borne by the owner.

✓ NAV can be -ve if municipal taxes actually paid exceed GAV.

D. Deductions U/S 24 { From NAV to calculate Income from HP }

(a) **Standard Deduction [Sec 24(a)]**

- Standard deduction = 30% of NAV shall be allowed from NAV.
- This is a flat deduction & is allowed irrespective of the actual expenditure incurred.
- No other expenses shall be allowed for example Repair & Maintenance, Parking Charges, Insurance Charges, Paint, Lift Charges etc.
- If NAV is -ve then no standard deduction.
- SOP → Standard Deduction = Nil (as NAV itself is Nil).

(b) **Interest on Borrowed Capital [Sec 24(b)]**

1. **Current year Interest**

Deduction	Interest = Amount of Loan × ROI p.a. (Without any limit)
From When	Interest relating to the PY of completion of construction can be fully claimed in that PY **(irrespective of the date of completion)**.
Purpose	Loan can be taken for Acquisition, construction, repair, renovation, reconstruction of HP.
Accrual/ Due	Deduction u/s 24(b)for interest is available on accrual basis. Thus, Interest accrued but not paid during PY can claim as deduction.

2. **Pre-construction period Interest**

Meaning	Pre-construction Period means period during which loan was taken but the construction of HP was/could not be started.
Deduction	Pre-commencement Interest is allowed as deduction **in 5 successive PYs** starting from PY of completion of construction. **[1/5th of Total Interest]**
Pre-Construction Period	Start: From Date of Borrowing & End: (a) 31st March immediately prior to date of completion of construction (b) Date of payment of Loan (Whichever is earlier).
Note: Interest will be aggregated from the date of borrowing till the end of the PY prior to the PY in which the house is completed and not till the date of completion of construction.	

Computation of Prior Period Interest

Step 1: Identify the Date of Borrowing of Loan.

Step 2: Identify the Date of Completion/Acquisition.

Step3: Identify Last Date of FY immediately preceding the date of Completion / Acquisition.

Step 4: Prior Period = Period calculated from Step 1 to Step 3

Step 5: Prior Period Interest =Amt of Loan × Rate of Interest × Prior Period as per Step 4.

Step 6: Allowable Prior Period Interest = $Prior\ Period\ Interest\ as\ per\ Step\ 5/5\ Years$

Points to Remember:

(a) Loan may be taken for purchasing the land even if construction is done out of the own funds.

(b) Interest on unpaid interest (penal interest) is not deductible.

(c) Interest on fresh loan taken to repay original loan is allowed as a deduction. {>1 Loan allowed}

(d) Amount paid as brokerage/commission/processing fees for arrangement of loan → NOT Allowed as deduction.

(e) If loan is taken from o/s India, Interest is deductible if TDS deducted and agent in India.

(f) Where a buyer enters into an arrangement with a seller to pay the sale price in installments along with interest due, the seller becomes the lender in relation to unpaid purchase price & buyer becomes the borrower. In such case, unpaid purchase price can be treated as capital borrowed for acquiring property & interest paid can be allowed as deduction.

(g) Loan may be taken from Bank, FI, Friend, Family etc

Limit on Deductions of Interest for Self-occupied Properties

Loan is taken for ↓	Maximum Interest Allowed
Repair or Renovation of House property on/after 1.4.1999	Actual Interest payable **(Maximum of Rs. 30,000)**
Acquisition or Construction of House Property **on/after 1.4.1999** & such acquisition or construction is completed within **5 years** from the end of the PY in which capital was borrowed.	Actual interest payable **(Maximum of Rs. 2,00,000)**

Note: Above-mentioned Limits are applicable combinedly for 2 SOP & not for each SOP.

Note: *No such limit is applicable in case of Let-out property or Deemed Let out property.*

Unrealised Rent & Arrears of Rent Received Subsequently [Sec 25A]

Unrealized Rent	Arrears of Rent
✓ Rent which could not be realized from the tenant. (Bad Debt) ✓ If such amount is realized subsequently, it gets taxed in the **PY of Receipt under HP**. ✓ However, deduction shall be allowed @ 30% of such unrealized rent. ✓ **Taxable @ 70%** of received amount.	✓ If assessee has increased the rent payable by the tenant retrospectively & there is a dispute over such increase; & later on the assessee receives the increased rent as arrears, it is called arrears of rent. ✓ It is taxable in the **PY of Receipt**. ✓ Deduction of 30% is allowed from such arrears. ✓ **Taxable @ 70%** of received amount.

Note: It does not matter whether the Assessee is owner of such house property in PY of receipt. Any expenditure incurred for recovery of such rent shall be ignored.

Unrealised rent is deductible from gross rent to arrive at the net amt. of rent R/R

- ✓ the tenancy is bonafide;
- ✓ the defaulting tenant has vacated, or steps have been taken to compel him to vacate the property;
- ✓ the defaulting tenant is not in occupation of any other property of the assessee;
- ✓ the assessee has taken all reasonable steps for the recovery of the unpaid rent

Note: - Generally, we reduce URR from ARR but ITR permitted to reduce URR from GAV.

Composite Rent

✓ Meaning: Owner of a property may sometimes receive rent in respect of building as well as

(i) Other assets [Ex: Furniture, AC, Plant and Machinery] or

(ii) for different services provided in the building [Ex: Lifts; Security; Power backup; generator].

✓ **Tax Treatment**

Two lettings are separable (Agreement)	Two lettings are not separable
✓ **Rent from HP** → Taxable u/h HP. ✓ **Rent from Use of other services** → Taxable u/h **PGBP or IFOS**.	✓ **Taxable u/h PGBP or IFOS**. ✓ **Ex for PGBP:** Hotel business/paying guest accommodation or warehousing or auditorium

Note: All the expenses for other facilities → Deducted while computing its income u/h PGBP or IFOS.

Income from House Property Situated Outside India

1.	**ROR in India (Note)**	**Taxable**, whether or not such income is brought into India.
2.	**RNOR/NR in India**	**Taxable only if it is received in India.**

Note: Foreign currency should be converted into Indian Rs. in TTBR on the last day of P.Y.

Note: Municipal Taxes Paid o/s India – Deductible.

Treatment of Income From Co-Owned Property [Sec 26]

Co-owned HP is Self-occupied	Co-owned HP is Let out
For Each Co-owner: ✓ **Annual Value** → **NIL** ✓ Deduction of **Rs. 30,000/2 Lacs** u/s 24(b) **separately** for each co-owner.	✓ Income from such HP shall be computed as if property is owned by **one owner** & then Income so computed shall be **apportioned** amongst each co-owner **as per their share.**

Note: If Shares of co-owners are not definite → Income from HP is taxed as income of AOP (Co-owners).

Deemed Ownership [Sec 27]

1. Transfer to a spouse: If an Individual transfer any HP to his/her spouse for Inadequate/Without consideration, such transferor is deemed to be the owner of the transferred House property.

   Exception: If a property is transferred in connection with an agreement to live apart.

   Ex: Mr. X has two house property each having income of Rs. 10 lacs and Mr. X has gifted one house property to Mrs. X, in this case income from such house property shall be taxable in the hands of Mr. X but if Mr. X has sold the house property to Mrs. X and has taken full payment, income from house property shall be taxable in the hands of Mrs. X.

   Note: Where an individual gives cash to his/her spouse or minor child & such transferee acquires HP from such cash, transferor shall not be treated as deemed owner. It will attract clubbing provisions.

2. Transfer to Minor Child: If an Individual transfer any house property to minor child for Without/ inadequate consideration, transferor is deemed to be the owner of transferred house property. **Exception:** Where a property is transferred to a minor married daughter.

3. Holder of an Impartible estate: Holder of an Impartible estate (Impartible estate is a property which is not legally divisible) shall be deemed to be owner of all properties in the estate.

   Ex: A Property could not be divided at the time of partition since it was occupied by the temple. Mr. X being the eldest son is the owner of the property as per the family convention. Property is given to Mr. X because the property could not be divided amongst the younger brother. Mr X in this case if not the beneficial owner of the property. He holds the property as a trustee on behalf oh his younger brothers since all the members of the family have right to enjoy the benefits of the property. Mr. X is deemed as owner of the property.

4. Member of a Co-operative Society, etc: Member of a co-operative society, company or other AOPs to whom a building or part thereof is allotted or leased under a House Building Scheme of a society/company/association, shall be deemed to be owner of that building or part thereof allotted to him although the co-operative society/company/association is the legal owner of that building.

5. Person in possession of a property: A person who is allowed to take possession of any building or part thereof in part performance of a contract of the nature shall be deemed owner of that house property. This would cover cases where

(a) Possession of property has been handed over to the buyer,

(b) Sale consideration has been paid or promised to be paid to the seller by the buyer,

(c) Sale deed has not been executed in favour of the buyer. Buyer would be deemed to be the owner of the property although it is not registered in his name.

6. Person to whom a property is leased out for not less than 12 years.

Lessee is deemed to be as the owner even though the lessor is the legal owner of the HP.

Losses under House Property

<u>Intra Head Adjustment (Sec 70)</u>: - Losses of one house can be set-off against income of another house during the same year

<u>Inter Head Adjustment (Sec 71)</u>: - Losses under the head HP can be set off against any other head income for that particular year except casual income. (Max set-off would be upto 2,00,000).

<u>Carry forward of House Property loss (Sec 71B)</u>: - Unadjusted HP losses can be c/f maximum 8 years and in future years, such losses can be set-off only against HP income.

✓ **Letting out of Building which is supplementary to the business:**

Income from letting out any HP for any purpose is taxable u/h PGBP provided such letting is supplementary to the business / profession of the assessee. All expense in relation to such house property are allowed to be debited to the P& L a/c prepared u/h PGBP.

Ex. Rent received by a school from letting out its auditorium for conducting coaching classes, rental income from letting out of houses by a company to its employees, etc.

<u>Which deduction not to allowed u/s 115BAC U/h HP ?</u>

- Interest in respect of Self Occupied Property – section 24(b)
- Set off of loss under the head income from HP against other heads.