Income from House Property

Basic concepts that one should know:

There should be a house property. A house property is one, which is construed to be a habitable house fit for staying in it. Includes the house building and the land appurtenant to the house property like the front yard or the back yard or the kitchen garden etc.
The income should be from letting of the house property.

The property should be let out for residential purposes.

There are three parties in such a transaction. The tenant pays the rent and since it is his expense we shall not discuss his position under this act. The land lord is the person who gets the rent and since it is his income it is his duty to pay taxe**s every time you solve a problem you have to think from the view point of the land lord**.The Govt. is the tax collection authority.

The full income received from the house property is not taxable. Certain expenses as defined under the act are allowed to be deducted from it. E.g. if X a person lets out his house property to y for a monthly of Rs. 2000, then the entire income 24000 [2000*12] is not taxable under the act. Certain expenses are allowed to be deducted from this income and only the net income is taxable.

Income of the house property is considered under section 22 of the act. It means if any other income is derived from the tenant then such income is not taxable under income from house property but it would be taxable under income from business or income from other sources. e.g. if Ramesh a tenant is paying composite rent of Rs. 5000 per month [3000 for house and 2000 for lunch] to land lord Suresh for staying in his house as well for the lunch and dinner provided by the LL to the tenant then only an amount of 3000 would be considered taxable under this section. He balance income of Rs. 2000 per month would be taxable under the head income from business or income from other sources.

There are four types of house properties that are studied under this act.

1. Fully let out house property
2. Fully self occupied house property which also includes a deemed to be let out house property.
3. An entire House Property, which is let out for some time during the previous year and self, occupied for the remaining period of the previous year
4. A house property where some area is let out on rent and the remaining area is self occupied.

Taxability of different under the act is discussed as follows

House type no. 1 -Case of a fully let out house property

Assessment year 2002-03 saw a major change in the computation of income of house property and there is a major difference in the method of computation of the income., hence it is suggested that only latest books of income tax may be referred so that there is no confusion about the applicable provision under ther act
The problem involves there major stage. The first stage is calculating the gross annual value. The second stage is calculating the net annual value and the third stage is to calculate the net income from house property after considering the deductions under section 24 of the act.

COMPUTATION THE GROSS ANNUAL VALUE

Step 1: calculate the reasonable letting value of the house property. The reasonable letting value is the maximum of the following.

1. The municipal valuation
2. The fair rent of the property

E.g. if the municipal valuation is 24000 and the fair rent is 30000 then the reasonable letting value would be Rs 30000 as this the maximum of the two figures
But if the property is subject to standard rent then the reasonable letting value cannot be more than the standard rent .e.g. if the mv is 24000 and the fair rent is 30000 and the standard rent for the property is Rs 25000 then the reasonable letting value of the house cannot be more than 25000.. but take an other example
if the mv is 24000 and the fair rent is 30000 and the standard rent is 32000 then the reasonable letting value is taken as 30000 being the highest of the two figures i.e. fair rent and the municipal valuation.

Particulars	Case 1	Case 2	Case 3	Case4
Municipal valuation	45	60	60	40
Fair rent	50	55	65	Na
Standard rent	Na	52	70	Na
RLV	**50**	**52**	**65**	**40**

From the above table the entire concept will be clear.

In the case 1 the max figure between the MV and FR is 50. This is then compared with the standard rent. Since in this case the standard rent is not applicable the GAV is the maximum of the 2 figures which is the fair rent and so the RLV is 50.

In case 2 the maximum figure between MV and FR is 60. In the same case the standard rent is 52 which is less than the maximum value of 60. In such a case the rule is that the RLV cannot be more than the standard rent and so in case 2 the RLV is 52 which is the standard rent.

In case 3 the maximum figure between the MV and the FR is 65. The SR is 70. In this case the rule says that if the max figure calculated between the MV and FR is less than

the SR then the max figure is the RLV . the rule is that the RLV can be less than the standard rent but not more than the SR. therefore in this case the RLV is 65 and not 70.

Case no 4 is a straight forward case and so the RLV is 40

Step 2:
Compare the figure calculated in step no 1 with the net actual rent . net actual rent for the said step is as follows
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NET ACTUAL RENT = ACTUAL RENT RECD OR RECEIVABLE FROM THE HP – UNREALISED RENT OF THE PREVIOUS YEAR

THE COMPARISON WOULD RESULT IN THE FOLLOWING

Case 1: the net AR is more than the RLV as per step 1.
In this case the AR is more than the RLV then the AR is taken as the GAV.

Case 2:
The net AR is less than the figure calculated as per step 1
In case the AR is less than the figure as per the step 1 then step no 2 is to be ignored.

We extend the above example with the addition of the actual rent amount and find out how is the computation made

Particulars	Case 1	Case 2	Case 3	Case4
Municipal valuation	45	60	60	40
Fair rent	50	55	65	54
Standard rent	Na	52	70	50
Actual rent if the property is let out throughout the year	**60**	**68**	**70**	**0**
Unrealised rent	**nil**	**4**	**6**	**0**
GAV	**60**	**64**	**65**	**50**

In case 1 we find the following
Step 1- RLV is 50.
Step 2 –actual rent – Unrealised rent = 60. Since the amount as per step 2 is more than that as per the step one net annual rent is to be calculated as the GAV

In case 2 the situation is as follows.
Step 1-RLV is 52.
Step no 2: net annual receivable rent is 68-4=64
Since the figure in step no 2 is more than that as per step no 1 the net annual rent is the GAV

In case 3 the situation is as follows
Step –1 RLV is 65
Step no 2- Actual rent is 70 but after reducing the Unrealised rent of 6 the net actual rent becomes 64 which means it falls down below the figure as per step 1. In such a situation when in step 2 the figure falls below step 1 then step 2 is to be ignored and the GAV is Rs 65

The Unrealised rent is reduced from the actual rent only if the following conditions are satisfied.

1. The tenancy is bonafide
2. The defaulting tenant is compelled to vacate the house property and
3. The defaulting tenant is not in possession of any other house property of the landlord
4. The assessing officer is satisfied that the reasonable steps have been taken and the Unrealised rent could not be recovered.
5. the assessee had taken the steps for the recovery of the rent
6. the ITO is satisfied that the same are legitimate and that there are no chance that the rent is recovered

It is important to note that if after deducting the Unrealised rent for the previous years from the actual rent it falls below the figure calculated by step 1 then step no 2 is not applicable.

In other words the step 2 is to be followed only to increase the annual value over step1 and not otherwise.

Step 2 figure can be more than or equal to step no 1 figure. It cannot be less than step 1 figure.

Step no 3: This step is to be followed only if the property under assessment is remaining vacant during the year. It other words the entire rent of the property could not be received because the property was not occupied during the year.

Step no 3 to be followed only if the property is vacant for some period in the year

If the house property is vacant for a period during the previous year then the proportionate amount of the rent received is to be reduced from the gross annual value as per the step no 2.

The figure that remains after deducting the amount for vacancy is known as the adjusted gross annual value.
It is important to note that the deduction for vacancy allowance is to be given on the basis of the actual rent that would not be received due to the vacancy.
Thus allowance for vacancy is as follows:

$$\frac{\text{Actual rent receivable for the entire year * no of months vacant}}{12}$$

We further extend the above example with the addition of the vacancy period and find out how is the computation made.

Particulars	Case 1	Case 2	Case 3	Case4
Municipal valuation	45	60	60	40
Fair rent	50	55	65	54
Standard rent	Na	52	70	50
Actual rent if the property is let out throughout the year	**60**	**68**	**70**	**0**
Unrealised rent	**Nil**	**4**	**6**	**0**
Vacancy period	**2 months**	**Nil**	**3 months**	**4 months**
Adjusted GAV	**50**	**64**	**30**	**50**

We shall discuss the above case by case
In case 1
Step no 1:The RLV is 50 [being the max of MV and FR]
Step no 2: net actual rent is 60-0=60 which is more than figure as per step 1. Therefore the GAV is 60
Step no 3: since the property was vacant for the period of 2 months the vacancy allowance is given as follows
Deduction for vacancy = 60*2/12= 10.
Therefore the adjusted GAV is 60-10=50

In case 2
Step no 1: The RLV is 52 [being the max of MV and FR but subject to the maximum of SR]
Step no 2: net actual rent is 68-4=64 which is more than figure as per step 1. Therefore the GAV is 64
Step no 3: since the property was not vacant for any period during the previous year step no 3 is not to be followed
Therefore the adjusted GAV is 64

In case 3
Step no 1: The RLV is 65
Step no 2: net actual rent is 70-6=64 which is less than than figure as per step 1. Therefore step no 2 is ignored and the GAV is 65
Step no 3: since the property was vacant for 6 months period during the pervious year vacancy allowance as per step no 3 is as follows
70*6/12=35 is the deduction for vacancy. The adjusted annual value is 65-35=30

In case 4
Step no 1: The RLV is 50
Step no 2: since the actual rent is nil step no 2 is ignored.
Net actual rent is 0 which is less than figure as per step 1. Therefore step no 2 is ignored and the GAV is 50
Step no 3: since the property was vacant for 4 months period during the pervious year vacancy allowance as per step no 3 is as follows
0*4/12= nil. Therefore no deduction for vacancy is given .The adjusted GAV is therefore =50

CALCULATION OF THE NET ANNUAL VALUE

After the calculation of the gross annual value as per step no 1we calculate the net annual value.

The net annual value is calculated as follows
GAV - MUNICIPAL TAXES PAID BY THE LAND LORD IN THE PREVIOUS YEAR = NET ANNUAL VALUE [NAV]

What are municipal taxes?

These are the house taxes that are to be paid in respect of house property. Please note some important things about these taxes.
1. These taxes should be paid by the land lord only. If the same are paid by he tenant then the deduction is not allowed to the landlord.
2. These taxes are allowed on paid basis only. It means that if the same are outstanding then the same are not allowed as deduction. But if these taxes are paid after the end of the year but before the date of filing of return then the same are allowed as deduction. e.g., for the previous year 2001-02 Mr. X the land lord had to pay Rs 2000 as municipal taxes to the govt. but for some reason he could not pay the same till the end of the year, i.e. 31st of march 2001. In such case the deduction will not be allowed to X for the previous year 2000-01. On the other hand if Mr. X files his return on 30th of June 2001 and if Mr. X pays the municipal taxes before 30th of June 2001 for the year ended 31st of march 2001 then even if the year is over the deduction will be given to him.
3. If taxes are paid by the landlord and later on recovered from the tenant the same are not allowed as deduction to the landlord.
4. Municipal taxes are allowed as deduction in the year in which they are paid. It means that even if the taxes for the previous year 2002-03 are paid in advance along with the taxes for the year 2001-02 in the year 2001-02 then in that case the deduction for the year 2001-02 will be available for two years. E.g. if the GAV for a particular house is 50000 and the municipal taxes are paid for the following years together in the previous year 2001-02
Previous year 2001-02 Rs: 4000
Previous year 2002-03 Rs: 5000 then the net annual value is 50000-9000 which is 41000 and in the year 2002-03 no deduction would be allowed.

5. These taxes are also known as water cess, or education cess or sewage tax etc., All mean the same thing and that is municipal taxes.

DEDUCTIONS UNDER SECTION 24

With the amendment in the act for the assessment year 2002-03 there are major changes in the deductions allowed under the above section. Previously a number of expenses were allowed as allow deduction under section 24. This has all changed and only 2 deductions are now allowed under this section.

1. STANDARD DEDUCTION

This deduction is notional in nature and is allowed for all House Properties which are let out during the previous year.

Quantum of deduction: 30% of the Net annual value.

This is a flat deduction and should be given even if the assessee has not incurred any expenditure in regard to the House Property.

2. INTEREST ON BORROWED CAPITAL

If any loan is taken on the purpose of Repairs Renovation Reconstruction Extension or Purchase of a house property then any interest paid on the amount borrowed is allowed as deduction.

The following points have to be considered for the purpose of this deduction

1 THE LOAN AMOUNT SHOULD BE USED FOR THE HOUSE

It means that the amount of the loan should be used for the purpose of the house. If the loan is not used for the house then the interest paid on such a loan is not allowed for the deduction. E.g. if a borrows Rs 100000 for the purpose of repairs for the House Property and instead for this he purchases a car from the amount then interest paid on such a loan will not be allowed.

2 IT IS ALLOWABLE ON PAID AS WELL AS IF IT IS OUTSTANDING

The deduction is allowed for interest paid as well as interest outstanding which is not paid.

3.INTEREST PAID OUT OF INDIA WITHOUT DEDUCTING TAX AT SOURCE WOULD NOT BE ALLOWED

If interest is paid to the lender who is situated out of India and tax is not deducted at source or not deposited with the govt. then the same is not allowed as deduction. However if the necessary tax on the interest remitted outside India were deposited by the landlord with the tax department then the same would be allowed as deduction.

4.PENAL INTEREST CHARGED BY THE LENDER FOR DEFAULT IN PAYMENT OF INTEREST IS NOT ALLOWED AS DEDUCTION

If the landlord fails to pay the interest in time and because of which the money lender charges penal interest on the same then only normal interest is to be considered for deduction and Penal interest paid for default in the interest is not allowed as deduction.

5.COMMISSION PAID FOR ARRANGING A LOAN IS NOT ALLOWED AS DEDUCTION

In case any commission is paid for the broker for arranging the loan then the same is NOT allowed as deduction

6.LOAN TAKEN FOR PAYING THE PREVIOUS LOAN IS ALSO ELIGIBLE FOR DEDUCTION

Income tax circular no 28 dated 20th of August 1969 states that If another loan is taken for repaying the existing loan then the interest paid on the second loan is allowed as deduction also.

7.MONEY CAN BE BORROWED FROM ANY PERSON INSTITUTION OR BANK.

It is not important from where the loan is borrowed and it may be private person , a financial institution or any bank or cooperative credit society.

CEILING LIMIT ON DEDUCTION ALLOWED FOR INTEREST ON BORROWED LOAN

FOR A LET OUT PROPERTY:

There is no ceiling on fixed for interest paid on a loan borrowed for a property which is let out on rent. Any amount paid is allowed as deduction

FOR A SELF OCCUPIED PROPERTY:

Ceiling is fixed on the amount of interest paid on a loan borrowed for a property which is self occupied for the Landlord for self residential purposes. The limits are as follows

Particulars	**If the loan is borrowed prior to 1st April 1999**	**If the loan is borrowed on or after 1st of April 1999**	**If part of the loan is borrowed before 1st of April 1999 and part of the loan is borrowed after 1st of April 1999**
Maximum Amount of deduction	**Rs 30000** The limit is for current year interest as well as pre construction interest** in other words total interest should not exceed this limit	**Rs.150000** The limit is for current year interest as well as pre construction interest** in other words total interest should not exceed this limit	30000 is the limit for the loan taken before 1st April 99 and 150000 limit for the loan taken after 1st of April 99
Purpose of loan	For repairs renovation or purchase or construction and reconstruction	For construction or purchase **only**	Depends on the purpose and the date of loan taken
Limit of	Not specified	Purchase or	Depends on the purpose

completion of construction or purchase		construction should be before April 2003	and the date of loan taken

** pre construction interest ** is discussed later

House type –2. INCOME OF ONE SELF OCCUPIED PROPERTY

What is a self occupied property?

A self occupied property or S-O-P is one which the landlord or the owner of the house uses for his own private residential purposes. The Govt. of India allows one house for every body free and no tax is calculated on such a house.

How is the income computed for such a Self occupied property?

For a Self occupied property the GAV is calculated as follows.

GROSS ANNUAL VALUE OF SUCH AS HOUSE IS CONSIDERED AS NIL

MUNICIPAL TAXES ARE NOT ALLOWED AS DEDUCTION FROM THE GAV

NAV IS ALSO TAKEN AS NIL.

What are the deductions allowed under section 24?

Only one deduction is given under this section which is interest of loan borrowed for purpose of construction or purchase of a house property. except of interest and the same is given subject to the following conditions

Amount of deduction for interest on loan for a Self occupied property
Actual interest for the year or Rs. 150000 which ever is less**

** Rs 30000 in case of the loan taken before 1st of April 99.
This is the maximum amount that could be allowed for the assessment year 2002-03

Income from a self occupied property is calculated as follows

Gross annual value	Nil
less Municipal taxes paid	Not allowed
net annual value	Nil
Less deduction under section 24	
Interest on capital Actual interest or Rs. 150000 [or 30000 in case of loan before apr99] which ever less	as applicable
net income from House Property	As applicable

INCOME FROM S-O-P CAN BE ZERO, OR NEGATIVE BUT IT CANNOT BE POSITIVE

House Type 2A-INCOME OF A DEEMED TO BE LET OUT PROPERTY

What is a deemed to be let-out property?[D-L-O-P]
A Deemed to be Let Out Property is one which is S-O-P but which is subject to income tax. This is done when an assessee has more than one house and he is using them for his self-residential purposes. According to the income tax act the assessee can have one house for the purpose of his residence

If the assessee has more than 1 house property and he is using these houses for his self residential purposes then one house is allowed to be considered as a self occupied property and Govt. of India does not tax this house. But the second house is taxable under the act because the tax authorities want to recover tax from people who can afford to have more than one house for self-residence.
In such a case the government gives an option to the assessee to select the house of his choice as a Self occupied property and then the remaining houses are considered taxable on the basis of notional rent or the reasonable letting value of these houses. There is no difference in the taxability process of this house and the let out property with only one exception.

ALLOWANCES FOR VACANCY AND UNREALISED RENT ARE NOT PERMITTED AS DEDUCTION FOR A DEEMED TO BE LET OUT PROPERTY.

Income from a Deemed to be Let Out Property is calculated as follows

Gross annual value	Max of fair rent and MV but subject to SR
less Municipal taxes paid	As given
net annual value	As arrived
Less deduction under section 24	
Standard deduction	30% of the NAV as above
Interest	As given
net income from House Property	Balancing figure

House Type-3 INCOME OF A HOUSE PROPERTY THAT IS PARTLY LET OUT FOR SOME PERIOD AND SELF OCCUPIED FOR THE REMAINING PERIOD OF THE YEAR

This is a special type of house in which the house is let out for rent for some part of the year and for some period the house is self occupied. E.g. the house was used for 3 months as SOP and the balance 9 months is let out on rental purposes.

WHENEVER A HOUSE PROPERTY IS LET OUT FOR SOME PART OF THE YEAR AND SELF OCCUPIED FOR THE REMAINING PART THEN THE INCOME IS CALCULATED AS IF THE HOUSE IS LET OUT FOR THE ENTIRE YEAR

Please follow the following steps

Step no 1: calculate the GAV for the full house for the full year
step no 2: deduct the municipal taxes for the full house for the full year/
The balance is known as the Net annual value
Step no 4 the balance is known as he adjusted annual value
give all the deductions under section 24 which are to be allowed
the most important points are
The income of such a house cannot be negative. It means it can be positive or it can be zero but never negative

special deduction for interest paid in the preconstruction period.
The Income tax provides a special deduction for interest paid on a loan taken for the purpose of constructing a house property. This is a special deduction and has been clarified by a special circular. This interest is called as interest in the pre construction period . E.g. X takes a loan of Rs 500000 for constructing a house which is to be let on hire on 1st Jan 98.In this case the interest of the loan will start from the date on which the loan is taken and at that time the house property because is under construction will not have any income. Let us say the house is completed in the month of December 2000. So during such time the assessee has paid the interest on the loan but there is no income on the house property. So the act provides for allowing this deduction after the property starts getting income. In order to claim the payment the following step are to be followed

1. Find out the date of completion of the house property and the year in which it is completed. Go backwards to the first 31st march. Mark that particular 31st of march. E.g. If the house is completed on the 26 of November 2000 then the immediate preceding 31st march is 31st march 200.
2. Find out the date on which the loan was taken.
3. The pre construction period will be the date from which the loan was taken to the preceding 31st march as calculated in step no 1.
4. Calculate the interest for the period as per step 3.
5. Divide the total interest in five equal parts.
6. This is the addition deduction that will be given for pre construction interest in addition to the interest for the year.

Important point

The year in which the house is completed should always come in the post construction period.