Demystifying Income from House property

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Income from House Property is one of the 5 heads of income under the Income Tax Act. This article is demystifying the Income from House Property. The article is divided into following parts:

1. Definition
2. Types of House Property
3. Calculation of Income from House Property
4. Deductions from House Property
5. Major Amendments
6. Special Provisions

1. Definition

The Income Tax Act 1961 defines: "The annual value of property consisting of any buildings or lands appurtenant thereto of which the assessee is the owner, other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to income tax, shall be chargeable to income-tax under the head Income from house property".

In common parlance, the rental value received by the assessee during the year, subject to certain deductions, is the annual value and is charged to tax under this head. In all the cases, the assessee should be the owner of the house property. The property can be commercial or residential or mix nature. The property should not be used for the purpose of business.

2. Types of House Property

» Self-Occupied Property

The property used for one's own residential purpose is classified as Self Occupied Property. It may be used by the assessee or his parents or spouse or children.

Till Financial Year 2019 – 2020, only one house was considered and treated as self-occupied. The Assessee could opt the property of his choice as Self Occupied.

From Financial Year 2019 – 2020, the

assessee can avail the benefit of two house properties as self-occupied. This amendment has been made keeping in mind the expanding cities, millennial generations and to boost the demand in reality sector.

» Let Out Property

A house property which is leased / rented – for full or part of the year – is considered as let out property.

» Deemed Let Out Property

Where the assessee has more than 2 self-occupied houses, he can opt for 2 house properties as Self Occupied and the remaining house properties will be considered as "deemed let out". Deemed Let Out property is property, which even though self-occupied, is considered as let out for the purpose of taxation under the Income Tax Act and will be taxed at the sum for which the property might reasonably be expected to let from year to year.

Deductions from the said property will be allowed as they are allowed from let out properties.

3. Calculation of Income from House Property

» Gross Annual Value (GAV)

o For Self Occupied property, Gross Annual Value is zero.

o For Let Out Property, Gross Annual Value is the rent collected from such property.

o For Deemed Let Out Property, Gross Annual Value is the value for which it might reasonably be expected to let from year to year.

» Net Annual Value (GAV)

o From the Gross Annual Value, the amount of Property Tax paid is deducted.

o The deduction of property tax is available when actually paid by the owner - irrespective of the method of accounting employed

o NAV = GAV – Taxes

» Deductions from NAV

o Standard Deduction: 30% of NAV is available as Standard Deduction

o Home Loan Interest paid is available as deduction from NAV

» Income from House Property

= NAV [GAV – Municipal Tax Paid] - Standard Deduction 30% of NAV - Home Loan Interest paid

4. Deductions from House Property

» Standard Deduction

Standard Deduction of flat 30% is

allowed from the NAV [Gross Annual Value less Municipal Tax paid] in computing the Income from the House Property. The standard deduction is provided to cover for the repair expenses and any other expenses relating to the house property during the year. This deduction amount is fixed, irrespective of the actual amount spent during the year.

» Interest paid on Borrowed Funds

Interest can be claimed as deduction up to Rs. 200000 per annum in respect of the interest paid on the borrowed funds for the purpose of acquiring the house property on or after 01.04.99.

The said limit is Rs.30000 instead of Rs. 200000 in the following cases:

- » The loan is taken for repairs/ renewals and not for construction/ acquisition
- » The loan is taken before 01.04.99
- » The loan is taken after 01.04.99 but the construction / acquisition is not completed within 5 years from the end of the financial year in which the loan was availed.

The condition for availing the interest is that the amount borrowed should be for the purpose of acquiring the house property. The borrowed funds should have nexus with the acquisition of the property.

If for instance the Flat A is acquired, thereafter Flat A is mortgaged and funds borrowed then irrespective of the usage of funds borrowed, the interest on such borrowed funds shall not be available for deduction from Income of House Property from Flat A as the borrowed funds have not been used for the purpose of acquisition of House Property of Flat A.

» Pre-Construction Period Interest

- The interest paid on the loan for the period between availing the loan and finishing the construction is called pre-construction period interest
- The said interest can be claimed as deduction only when the construction is completed.
- Pre-construction period interest can be claimed in five equal installments beginning from the financial year preceding the date on which the construction / acquisition is completed.
- Example:

o Mrs. A took a loan in May 2018 for construction of her bunglow. The construction was completed in June 2020 and she received the completion certificate. She leased out the said bunglow in October 2020 for Rs. 1200000. The interest for the said years is as under:

1. May 2018 to March 2020

   Rs. 800000

2. April 2020 to March 2021

   Rs. 55000

- In Income Tax Return of FY 2020-21 pertaining to AY 2021-22:

1. GAV Rs. 1200000
2. Less: Std Deduction Rs. 360000
3. NAV Rs. 840000
4. Less: Interest of current year

   Rs. 55000

5. Less: Pre-construction Interest

   Rs. 160000 (Rs. 800000/5 = 160000)

6. Net Taxable Value Rs. 625000

» The total interest deduction 55000 + 160000 = Rs. 215000 will be restricted to Rs. 200000 if the house is self occupied.

5. Major Amendments

» Union Budget 2019:

Earlier the assessee had an option of declaring any one house as self occupied and others as let out/deemed let out, as the case may be. From FY 2019-20, the assessee is allowed to declare any two houses as self occupied and others as let out/deemed let out, as the case may be.

» Union Budget 2017:

Earlier, the assessee was able to set off the entire loss from the head House Property against other heads of income. From FY 2017-18, such set off of losses has been restricted to Rs. 200000. It is noteworthy that setting limit of set off of losses doesn't impact self occupied house owners as they already have a limit of Rs. 200000 on claiming interest on loans deduction. This amendment affects the rented properties because they can claim the entire interest as deduction but the losses which arise due to such interest deduction can at the maximum be set off to the extent of Rs. 200000.

6. Special Provisions

» Arrears of rent and unrealized rent received subsequently

Any arrears of rent received subsequently shall be taxed in the year in which the rent was received and a deduction of 30% shall be allowed. Such rent will be taxed to the assessee irrespective of whether he is the owner in that financial year or not.

» Co-owners and interest deduction

- If the property is co-owned by two or more owners and the loan is taken jointly, then the interest deduction of each borrower's share will be allowed to him separately as deduction.
- The limit of interest deduction of 30000 or 200000 will be applied separately and thus there will be greater tax savings.
- However, the condition of joint ownership and joint borrowing, both should be satisfied.